Armed Forces Pension Scheme

(Incorporating the Armed Forces Compensation Scheme)

Annual Accounts 2014-15

HC 33

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Annual Accounts 2014-15

(For the year ended 31 March 2015)

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History and Statutory Background

The Armed Forces Pension Scheme 2005 (AFPS 05)

The Armed Forces (Pension & Compensation) Act 2004 is the primary legislation covering the Armed Forces Pension Scheme 2005 (AFPS 05) and the Early Departure Payment (EDP) Scheme.
From 6 April 2005, the AFPS 05 was introduced for all new members of the Armed Forces. The AFPS 05 is an unfunded, defined benefit, salary-related, contracted out, occupational pension scheme. The Scheme is designed to meet the special requirements of Service life. Pensions are paid immediately if an individual serves to age 55. Those who have at least two years service who leave before age 55 will have their pensions preserved until age 65. The Scheme also includes an EDP for those who leave before age 55 providing they have at least 18 years service and are at least 40 years of age. The EDP Scheme pays a tax-free lump sum and income of between 50% and 75% of preserved pension between the date of the individual's departure from the Armed Forces and age 55. The income rises to 75% of preserved pension at age 55 and is index linked. At age 65 the EDP stops and the preserved pension and preserved pension lump sum are paid. Pensions may be payable to the spouse, civil partner, partner or to eligible children. Death-in-service lump sums are payable subject to nomination.

From 31 March 2015 AFPS 05 was closed to new members; approximately 5,000 members remained in the Scheme with Transitional Protection but some 75,000 members were transferred to the new AFPS 15. Those transferring have had their AFPS 05 accrued pensions protected.

The Armed Forces Compensation Scheme (AFCS)

The Armed Forces (Pension & Compensation) Act 2004 is the primary legislation covering the Armed Forces Compensation Scheme (AFCS). The AFCS was introduced on 6 April 2005, replacing two separate compensation arrangements under the Armed Forces Pension Scheme 1975 and the War Pension Scheme. The AFCS covers injury, illness and death that are caused by service on or after 6 April 2005. The AFCS is a tariff-based compensation scheme, which has been designed to be simple to understand and to produce consistent and equitable decisions, using an evidence-based approach.

The Armed Forces Pension Scheme 1975 (AFPS 75)

The AFPS 75 was the primary Scheme for Armed Forces personnel prior to 2005. The Scheme rules are set out in "Prerogative Instruments" that derive their authority from Her Majesty The Queen and are not subject to approval, annulment or amendment by Parliament. The current prerogative instruments are the Naval and Marine (AFPS 75 and Attributable Benefits Scheme) Order 2010, the Army Pensions (AFPS 75 and Attributable Benefits Scheme) Warrant 2010 and the Air Force (AFPS 75 and Attributable Benefits Scheme) Order 2010. The AFPS 75 regulations are set out in Schedule 1 to the prerogative instruments.

The AFPS 75 is an unfunded, defined benefit, salary-related, contracted-out occupational pension scheme. It provides immediate pension benefits to many of those who leave without completing a full career but who have completed at least 16 years reckonable service for Officers and 22 years reckonable service for Other Ranks. The full career pension can be earned relatively early, at age 55, and invaliding and death benefits are available in the event of illness, injury or death at different rates depending upon whether or not these are caused by service. From 6 April 2005, unless already in payment at that date, these benefits are not provided for service related illness, injury or death but are provided by the Armed Forces Attributable Benefits Scheme (AFABS) where the cause is service prior to that date and the AFCS where the cause is service after that date. For those who leave without entitlement to immediate pension but who have completed at least two years reckonable service a preserved pension is payable at the age of 60 for service before 6 April 2006 and age 65 for service from that date.

The AFPS 75 was closed to new members from 6 April 2005. Members of the AFPS 75 were given the opportunity to transfer to the AFPS 05 from this date.

From 31 March 2015 some 96,000 AFPS 75 members were transferred to the new AFPS 15; with approximately 10,000 members remaining in the scheme with Transitional Protection. Those members transferring to the new AFPS 15 had their AFPS 75 accrued pensions protected.

The Armed Forces Attributable Benefits Scheme

The current Scheme Rules are set out in Schedule 2 to the following prerogative instruments; the Naval and Marine (AFPS 75 and Attributable Benefits Scheme) Order 2010, the Army Pensions (AFPS 75 and Attributable Benefits Scheme) Warrant 2010 and the Air Force (AFPS 75 and Attributable Benefits Scheme) Order 2010.

The Scheme provides invaliding benefits to those discharged from the Services on medical grounds in respect of injuries caused by service on or before 5 April 2005, who have been awarded a benefit under the War Pensions Scheme and whose degree of disablement due to the disabling condition is 20% or more.

Reserve Forces Pension Schemes

There are two non contributory Reserve Forces occupational Pension Schemes for members of the Reserve Armed Forces: Full Time Reserve Services Pension Scheme (FTRSPS 97) and the Reserve Forces Pension Scheme (RFPS 05).

FTRSPS 97 is the Scheme applicable to those who gave Full Time Reserve Service as a member of the Reserve Forces before 6 April 2005. It was closed to new entrants and those starting new commitments from 6 April 2005.

With the exception of those personnel within 10 years of their normal pension age on April 2012, all members of FTRSPS97 were automatically transferred to AFPS 15 on 1 April 2015.

RFPS 05 is the Scheme applicable to those starting or renewing a Full Time Reserve Service (FTRS) commitment, including those on Additional Duties Commitment terms on or after 6 April 2005. Personnel mobilised under parts 4, 5 or 6 of the Reserve Forces Act 1996, (or corresponding provisions of the Reserve Forces Act 1980) from that date may choose to become members of RFPS 05. Members of FTRSPS 97 were given an opportunity to transfer to RFPS 05 from this date.

RFPS 05 was closed from 31 March 2015 and replaced by AFPS 15. With the exception of those personnel within 10 years of their normal pension age on April 2012, all members were automatically transferred to AFPS 15 on 1 April 2015.

Non Regular Permanent Staff Pension Scheme

The Non Regular Permanent Staff Pension Scheme (NRPSPS), which covers non regular personnel in support of the Territorial Army, is a non contributory pension scheme available to all members of the Non Regular Permanent Staff (NRPS). The NRPSPS closed to new entrants effective 31 August 2011 with any new appointments being FTRS appointments covered under the RFPS 05.

With the exception of those personnel within 10 years of their normal pension age on April 2012, all members of NRPSPS were automatically transferred to AFPS 15 on 1 April 2015.

Gurkha Pension Scheme

The Gurkha Pension Scheme (GPS) was established by Royal Warrant in 1949. It provides pensions for former members of the Brigade of Gurkhas, who have completed 15 years or more service, at rates based on those of the Indian Army.

In March 2007, the Government announced the outcome of a Review of Gurkha Terms and Conditions of Service. It was announced that serving Gurkhas, and those who left service on or after 1 July 1997, would be given the right to transfer to one of the two Armed Forces Pension Schemes for members of the Regular Armed Forces, from October 2007, under the following conditions:

- Gurkhas recruited after 1 December 2006 will join the AFPS 05.
- Gurkhas serving on 1 October 2007 who joined on or after 6 April 2005 but before 6 April 2006 (the 2006 intake) were offered the option to transfer from the GPS to AFPS 05.
- Gurkhas serving on 1 October 2007 who were serving before 6 April 2005 were offered the option to transfer from GPS to AFPS 75 or AFPS 05.
- Gurkhas who retired between 1 July 1997 and 5 April 2006 were offered the option to transfer to AFPS 75 or remain in the GPS. Those who retired from 6 April 2006 but before 1 October 2007 were offered the option to transfer to AFPS 75 or AFPS 05 or remain in the GPS.
- Gurkhas transferring from GPS to AFPS are given actuarial value for any service before 1 July 1997, but service given on or after 1 July 1997 is transferred on a year-for-year basis.
- From 1 April 2015 all members were transferred to AFPS 15, unless they qualified for Transitional Protection.

Minor Pension Schemes

In addition to the above Schemes, the AFPS also manages a number of Minor Pension Schemes covering Locally Employed Military Personnel in places such as Malta, Gibraltar, Singapore, Hong Kong, Seychelles, Sri Lanka, India/Pakistan (Hong Kong Singapore Royal Artillery).

With the exception of Gibraltar these schemes are now closed to new members.

The Armed Forces Pension Scheme 2015 (AFPS 15)

A new Armed Forces Pension Scheme was introduced on 1 April 2015 (AFPS 15). All serving Service personnel who were members of an Armed Forces Pension Scheme were automatically transferred to the new Scheme, unless they qualified for Transitional Protection.

The government offered Transitional Protection for those who were within 10 years of their respective Scheme's Normal Pension Age (NPA) on 1 April 2012. AFPS 75, AFPS 05 and FTRS 97 (Full Commitment) have a NPA of 55. RFPS, FTRS 97 (on Limited or Home Commitment) and NRPS have a NPA of 60.

This means members of AFPS 75, AFPS 05 or FTRS 97 (FC) who were aged 45 or over on 1 April 2012, stayed on their current pension scheme and their benefits were unaffected. Members of the RFPS (including those on Additional Duties Commitment), FTRS 97 (on LC or HC) or NRPS who were aged 50 or over on 1 April 2012, remained in their current pension scheme and their benefits were unaffected.

This Transitional Protection was a government decision for all public service schemes, for those personnel who were nearest to their NPA and who, therefore, had less time to adjust their financial plans in response to the changes to their pension scheme. Approximately 15,000 members benefited from Transitional Protection.

Key features of the new Scheme include:

- The EDP will normally be paid as a monthly income and one-off lump sum. However, in light of views expressed by Service personnel during consultation, the new Scheme will also offer the choice to forego the lump sum and convert it into additional monthly income. This additional option is not currently available to members of any current Armed Forces Pension Scheme.
- A NPA of 60 and a Deferred Pension Age linked to the State Pension Age.
- The option to convert pension income into a tax-free lump sum at a transfer rate of £12 lump sum for £1 per annum pension income (up to HM Revenue and Customs limits).

Further information is available at: **www.gov.uk/pensions-and-compensation-for-veterans**

The Scheme rules are set out in the Armed Forces Pension Regulations Statutory Instrument Order 2014, the Armed Forces Early Departure Payments Scheme Regulations Statutory Instrument 2014 and the Armed Forces (Transitional Provisions) Pensions Regulations Statutory Instrument 2015.

The reforms implemented in April 2015 may affect the behaviour of members, which has been reflected in the valuation completed by the Government Actuary's Department, see Report of the Actuary, page 13, paragraph 13. No other allowance has been made for AFPS 15 within these accounts.

AFPS Added Pension

Members have an option to make periodical contributions to purchase Added Pension:

- increase the benefits payable to them when they draw their pension, this is known as Added Pension (member), or;
- increase the benefits payable to them when they draw their pension and increase the benefits payable to their dependants after they die, this is known as Added Pension (member and dependants).

These Additional Voluntary Contributions and their associated liabilities are recognised in these Accounts.

Freestanding Additional Voluntary Contributions (FSAVC)

Active members may contribute to a FSAVC. The contribution is passed to the relevant institution and is a private arrangement between the member and the institution, and as such these transactions are not recognised in these Accounts.

Stakeholder Pensions

The Stakeholder pension is a private pension that was introduced by the Government to help people save for their retirement. Scottish Widows has been designated as the preferred provider of Stakeholder pensions to the Armed Forces. The contribution is passed to the relevant institution and is a private arrangement between the member and the institution, and as such these transactions are not recognised in these Accounts.

Management of the Schemes

The AFPS and AFCS are managed and operated by Defence Business Services (DBS), a business unit within the Ministry of Defence (MOD). The costs of administering the Schemes are borne by the MOD and are reflected in the Department's Annual Report and Accounts.

The MOD has a contract with Serco Ltd to provide management services to DBS. The Chief Executive Officer (CEO) and a number of the Executive appointments are made through Serco Ltd.

The CEO of DBS has been designated by the Departmental Accounting Officer (Jon Thompson) to be the Scheme Administrator for both the AFPS and AFCS. The DBS Head of Resources has been designated by the Departmental Accounting Officer to be the Senior Finance Officer for both the AFPS and AFCS. In administering the AFPS and AFCS on behalf of the MOD, DBS aims to ensure that all pension and compensation payments due to entitled pensioners and members of the Armed Forces are made in a timely and accurate fashion.

The DBS Executive Committee meets regularly and is responsible for managing DBS within agreed financial limits. It has primary authority for day to day management of DBS. The Executive Committee consists of:

DBS Executive Committee (EC)

EC Members Composition - Serco

Rod McCurdy (from 05/05/2014)	Chief Executive Officer
Mike Stone (until 05/05/2014)	Chief Executive Officer
Simon Freeman (from 15/05/2014)	Chief Operating Officer
Rod McCurdy (until 05/05/2014)	Chief Operating Officer
Vince Groome	Chief Information Officer
Helen Hall (from 22/09/2014)	Chief People Officer
Russell Sowden (until 21/09/2014)	Chief People Officer
Andy Tyler-Smith (from 17/11/2014)	Operations Director
Giles Wood (from 08/05/2014 until 31/08/2014)	Operations Director
Simon Freeman (until 15/05/2014)	Operations Director
Andrew Thompson (from 01/09/2014)	Service Development Director
Stuart Cotton (until 01/11/2014)	Development Director
Nicola Smith (from 01/05/2014)	Transformation Director
Chris O'Connor (until 01/05/2014)	Transformation Director

EC Members Composition – MOD Personnel

Georgina Benzies	Head of Resources
Jon Parkin	Head of Veterans UK
Andy Dowds	Head of Finance
Commodore Ian Bisson	Head of Military Personnel
Andrew Stafford	Head of Civilian Personnel
Caroline Rumming	Head of National Security Vetting
AVM Ross Paterson (until 30/06/2014)	Service Personnel Veterans CE

Changes during the year

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

Armed Forces Pension Schemes

The Pensions increase rate was 2.7% (2.2% in 2013-14) with effect from 7 April 2014 (8 April 2013).

Changes in Accounting Standards

There are no changes in International Accounting Standards that have an impact on the AFPS or the AFCS.

Membership Statistics

The HM Treasury standard format for membership disclosure has been expanded due to the complexity of the Armed Forces Pension Schemes. The membership data below has moved away from an "individual" being synonymous with a "member". Members of the AFPS 75 Scheme who leave the Armed Forces before they can claim an Immediate Pension receive a pension at age 60 (for service before 6 April 2006) and an additional pension at age 65 (for service post this date). For example, a Deferred Member on attaining age 60, becomes a Pensioner but also remains as a Deferred Member until the age of 65. To reflect this, and to be able to show the movements within each category, the membership table shows Deferred Benefits instead of Deferred Members and Benefits in payment instead of Pensioners in payment.

There are three groups, defined as follows:

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

Active members

	Active members brought forward from 31 March 2014	171,968
	Adjustment (see Membership Statistics note 6)	28
	Total active members at 1 April 2014	**171,996**
Add:	New entrants in year	14,931
	Transfers in	19
Less:	Deaths in service	(72)
	Left active service with under two years service and no benefits	(2,912)
	Left active service with deferred benefits	(11,461)
	Left active service and received benefits	(6,903)
	Active members at 31 March 2015	**165,598**

Deferred and unclaimed benefits

	Deferred benefits brought forward from 31 March 2014	459,903
	Adjustments (see Membership Statistics note 6)	1,119
		461,022
	Being:	
	Deferred benefits	447,362
	Benefits due but unclaimed	13,660
	Total deferred and unclaimed benefits at 1 April 2014	**461,022**
Add:	Benefits not immediately payable	14,828
	New benefit on divorce	369
Less:	Transfers out	(1,819)
	Benefits taken up	(4,815)
	Benefits elapsed (see Membership Statistics note 5)	(1,565)
		468,020
	Being:	
	Deferred benefits	451,697
	Benefits due but unclaimed	16,323
	Total deferred and unclaimed benefits at 31 March 2015 (430,283 members)	**468,020**
	(see Membership Statistics note 4)	

Benefits in payment

	Benefits brought forward from 31 March 2014	
	- Members	345,000
	- Dependants	73,112
	Total	418,112
	Adjustments due to data received post 31 March 2014	
	- Members	(156)
	- Dependants	33
	Total benefits at 1 April 2014	**417,989**
Add:	Benefits that became payable in the year	
	- Members	11,662
	- Dependants	3,943
Less:	Benefits that have ceased in the year	
	- Members	(6,679)
	- Dependants	(3,952)
		422,963
	Being:	
	- Members	349,827
	- Dependants	73,136
	Total benefits in payment at 31 March 2015	**422,963**

Membership Statistics Notes

1. Individuals may be a member of more than one Scheme.
2. A member may be entitled to more than one benefit under a Scheme (see above).
3. Where a member is divorced and the ex-spouse is entitled to a proportion of the benefit, the deferred figures show both benefits when notified to AFPS post March 2006. Benefits in payment show both benefits.
4. Comparison of movements between tables cannot be made due to the use of members in one table and benefits in the other tables, as explained above.
5. Where a member has not claimed benefits by the age of 72, the member is out of time to claim. This is an assumption for membership reporting purposes only.
6. The active and deferred members brought forward from 31 March 2014 have been restated to account for better information obtained from the membership database. The database used to manage active and deferred members is a dynamic system that allows records to be updated retrospectively. It is therefore accepted that the opening balance will not reconcile to the previous years closing balance, hence the adjustment line present in the membership table.
7. The Government Actuary's Department (GAD) valuation includes a number of members with estimated benefits. This is due to one or more of the elements required to determine the benefit being missing from the database.
8. The Minor Pension Schemes' membership data as at 31 March 2015, equating to 218 active members, 34 deferred members and 2,374 benefits in payment are excluded from the above table.

National Fraud Initiative (NFI)

On a biennial basis, the AFPS takes part in the NFI, which commenced in 1998 and is co-ordinated by the Audit Commission. This initiative allows the Scheme to submit approved data to the Audit Commission who match it against other data sources to ensure the payments are still being made to the individual originally entitled to the pension. This exercise was in addition to the Scheme's normal procedure of regularly confirming entitlement with individual pensioners. The table below provides an update of the position for the exercises conducted since 2002 and lists the outstanding amounts which are still being actively pursued. The NFI 2012 exercise was still live in 2014-15 resulting in additional cases identified from that reported in the 2013-14 AFPS Annual Accounts.

			Prior Years		2014-15		
NFI Exercise	**Total Cases**	**Total Identified £000**	**Recovered £000**	**Written-off £000**	**Recovered £000**	**Written-off £000**	**Outstanding at 31/03/2015 £000**
NFI 2002	252	1,071	764	275	2	1	29
NFI 2004	257	426	355	66	1	0	4
NFI 2006	297	789	701	82	1	0	5
NFI 2008	175	959	871	30	11	0	47
NFI 2010	126	695	611	6	18	0	60
NFI 2012	160	768	447	0	283	0	38
NFI 2014*	153						

* Although the number of cases has been identified for this exercise, no action has yet commenced on calculating/pursuing these overpayments.

Disclosure of information to auditors

So far as I am aware, there is no relevant audit information of which the Scheme's auditor is unaware. I have taken all steps that I ought to have taken to make myself aware of any relevant audit information and to establish that the Scheme's auditor is aware of that information.

Events After the Reporting Period

A new Armed Forces Pension Scheme 2015 (AFPS 15) was introduced on 1 April 2015. Further details on this can be found in the Report of the Managers, page 4.

As announced on 8 November 2014, from 1 April 2015 all survivors' pensions awarded to spouses and civil partners in the Scheme will be for life. Those already in receipt of a survivor's pension will be entitled to keep their pension for life if they decide to remarry, cohabit or form a civil partnership after this date. Applications for ceased pensions to be restored will no longer be subject to a means test. The additional cost of this change in policy is estimated at around £0.1Bn. £30M of this relates to the expected increase in ceased pensions being restored, which has been reflected in these Accounts as a past service cost. The remainder has been reflected in these Accounts as a change in actuarial assumptions.

Managers, Advisers and Employers

Managers

Accounting Officer:
Jon Thompson
Permanent Under-Secretary of State for Defence
Ministry of Defence
Whitehall
London SW1A 2HB

Director General of Finance:
Louise Tulett
Ministry of Defence
Whitehall
London SW1A 2HB

AFPS & AFCS Scheme Administrator:
Rod McCurdy
Chief Executive Officer
Defence Business Services
Abbey Wood North
Bristol BS34 8JH

Pension Policy:
Air Commodore Garry Tunnicliffe
Head of Remuneration
Ministry of Defence
Whitehall
London SW1A 2HB

Advisers

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

Bankers:
Government Banking Service
Southern House
Wellesley Grove
Croydon CR9 1WW

Legal Advisers:
MOD Central Legal Services
Ministry of Defence
Whitehall
London SW1A 2HB

Medical Advisers:
Medical Services Team
Defence Business Services
Tomlinson House, Norcross
Thornton-Cleveleys FY5 3WP

Auditor:
Comptroller and Auditor General
National Audit Office
157 – 197 Buckingham Palace Road
Victoria
London SW1W 9SP

Employer

Ministry of Defence

Further information

Any enquiries should be addressed to:

	AFPS	AFCS
Post:	Veterans UK Mail Point 480, Kentigern House 65 Brown Street Glasgow, G2 8EX	Veterans UK Tomlinson House, Norcross Thornton-Cleveleys FY5 3WP
Email:	DBS-PensionsHelp@dbspv.mod.uk	veterans-uk@mod.uk
Phone:	0800 085 3600	0808 1914 218

Jon Thompson
Accounting Officer for the Armed Forces Pension Scheme
and Armed Forces Compensation Scheme **1 July 2015**

Report of the Actuary for the Armed Forces Pension Scheme for Accounts for the Year Ended 31 March 2015

Introduction

1. This statement has been prepared by the Government Actuary's Department at the request of the Ministry of Defence ('MoD'). It summarises the pensions disclosures required for the 2014-15 Annual Accounts of the Armed Forces Pension Scheme ('the scheme', or 'AFPS').

2. The AFPS is a final salary defined benefit scheme, the rules of which are set out in the Army Pensions (Armed Forces Pension Scheme 1975 and Attributable Benefits Scheme) Warrant 2010 (and Naval and Marine, and Royal Air Force equivalents), and the Armed Forces Pension Scheme Order 2005 (SI 2005/438), and subsequent amendments. The scheme is wholly unfunded. I am not aware of any informal practices operated within the scheme which lead to a constructive obligation (under IAS 19 constructive obligations should be included in the measurement of the actuarial liability). The liabilities disclosed in this statement also include an allowance for the benefits accrued by personnel who are in the Reserve Forces Pension Scheme (RFPS), the Full-Time Reserve Service Pension Scheme (FTRS), the Non-Regular Permanent Staff Pension Scheme (NRPS) and the Gurkha Pension Scheme (GPS); benefits payable from the Early Departure Payments (EDP) arrangement; and benefits payable from the other minor overseas schemes that are included in the AFPS accounts.

3. The statement is based on an assessment of the liabilities as at 31 March 2012, with an approximate updating to 31 March 2015 to reflect known changes.

Membership data

4. Tables A to C summarise the principal membership data as at 31 March 2012 used to prepare this statement.

Table A – Active members

31 March 2012		31 March 2015
Number (thousands)	Total Pensionable Pay † (£ million pa)	Total Pensionable Pay * (£ million pa)
191	6,080	5,509

† Including increases applying in April of year
* Excluding increases applying in April of year and estimated based on data as at 28 February 2015

Table B – Deferred members

31 March 2012		31 March 2015
Number (thousands)	Total deferred pension † (£ million pa)	Number (thousands) *
399	963	429

† Including increases applying in April of year
* Estimated based upon data as at 28 February 2015

Table C – Pensions in payment

31 March 2012		31 March 2015
Number (thousands)	Total pension † (£ million pa)	Total pension * (£ million pa)
380	3,348	3,747

† Including increases applying in April of year
* Excluding increases applying in April of year and estimated based on data as at 28 February 2015

Methodology

5. The present value of the liabilities has been determined using the Projected Unit Credit Method (PUCM), with allowance for expected future pay increases in respect of active members, and the principal assumptions applying to the 2014-15 Annual Accounts. The contribution rate for accruing costs in the year ended 31 March 2015 was determined using the PUCM and the principal assumptions applying to the 2013-14 Annual Accounts.

6. This statement takes into account the benefits normally provided under the scheme, including age retirement benefits, ill-health retirement benefits and benefits applicable following the death of the member. It does not include premature retirement and redundancy benefits in respect of current active members, although the assessment of liabilities includes pensions already in payment in respect of such cases. It does not include the cost of additional death benefits or injury benefits provided through the Armed Forces Compensation Scheme (in excess of ill-health benefits).

7. The liabilities disclosed in this statement include the benefits accrued by personnel who are in the Gurkha Pension Scheme (GPS), together with an approximate allowance in respect of past service costs for current GPS members resulting from the Gurkha Offer to Transfer.

8. The liabilities disclosed in this statement include the benefits accrued by personnel who are in the minor overseas schemes covered by the AFPS accounts.

Principal financial assumptions

9. The principal financial assumptions adopted to prepare this statement are shown in Table D.

Table D – Principal financial assumptions

Assumption	31 March 2015	31 March 2014
Rate of return (discount rate)	3.55%	4.35%
Rate of earnings increases	4.20%	4.50%
Rate of future pension increases	2.20%	2.50%
Rate of return in excess of:		
Pension increases (CPI)	1.30%	1.80%
Earnings increases	-0.65%	-0.15%
Expected return on assets:	n/a	n/a

10. The pension increase assumption as at 31 March 2015 is based on the Consumer Price Index (CPI) expectation of inflation.

Demographic assumptions

11. The demographic assumptions adopted to prepare this statement were derived from the specific experience of the scheme membership.

12. The 'S1NXA' standard tables prepared by the Continuous Mortality Investigation (part of the Actuarial Profession) are used but with adjustments derived from scheme experience. A multiplier is applied to the mortality rates of 88% for Officers and 118% for Other Ranks. Mortality improvements are in accordance with those incorporated in the 2012-based principal population projections for the United Kingdom.

13. Reforms to the AFPS due to be implemented in April 2015, together with the introduction of the MoD's New Employment Model, may affect the behaviour of members, for example the pattern of withdrawal or retirement from active service. An allowance for these changes and their potential impact on member behaviour was included in the assumptions adopted for the actuarial valuation of the AFPS arrangements as at 31 March 2012 (completed on 24 February 2015). The assumptions used to calculate the accounting liabilities as at 31 March 2015 are aligned with those used for the actuarial valuation. This is a change from the approach used to assess the accounting liabilities as at 31 March 2014 when, given the uncertainty surrounding the scheme changes and their potential impact on member behaviour, the MoD decided to make no allowance for the reforms.

14. The contribution rate used to determine the accruing cost in 2014-15 was based on the demographic and financial assumptions applicable at the start of the year: that is, those adopted for the 2013-14 Annual Accounts.

Liabilities

15. Table E summarises the assessed value as at 31 March 2015 of benefits accrued under the scheme prior to 31 March 2015 based on the data, methodology and assumptions described in paragraphs 4 to 14. The corresponding figures for the previous four year ends are also included in the table.

Table E – Statement of Financial Position

£ billion

	31 March 2015	31 March 2014	31 March 2013	31 March 2012	31 March 2011
Total market value of assets	nil	Nil	Nil	Nil	Nil
Value of liabilities	(154.4)	(129.5)	(118.0)	(105.6)	(100.6)
Surplus/(Deficit)	(154.4)	(129.5)	(118.0)	(105.6)	(100.6)
of which recoverable by employers	n/a	n/a	n/a	n/a	n/a

Pension cost

16. The cost of benefits accruing in the year ended 31 March 2015 (the Current Service Cost) is based on a standard contribution rate of 56.9% of Officer pensionable salaries, and 44.8% of Other Ranks pensionable salaries. The AFPS is non-contributory for members.

17. Table F shows the Current Service Cost, which is met fully by the employer. The corresponding figures for 2013-14 are also included in the table.

Table F – Contribution rate

Percentage of pensionable pay	1 April 2014 to 31 March 2015	1 April 2013 to 31 March 2014
Officers	56.9%	51.8%
Other Ranks	44.8%	39.8%

18. For the avoidance of doubt the employers' share of the standard contribution rate determined for the purposes of the Annual Accounts is not the same as the actual rate of contributions payable by employers, 41.6% for Officers and 28.2% for Other Ranks over the period 2014-15, which was determined based on the methodology and the financial and demographic assumptions adopted for the financing of the scheme in the actuarial valuation as at 31 March 2005. (Note this excludes the cost of the Armed Forces Compensation Scheme.) The most significant difference between the actuarial assessments for Annual Accounts and for scheme funding purposes is the discount rate net of pension increases, which was 1.80% pa for the 2014-15 Current Service Cost compared with 3.5% a year for the existing scheme funding rate derived from the 2005 valuation. (Note that the contribution rate payable by employers has changed from 1 April 2015 as a result of the outcome of the actuarial valuation of the scheme as at 31 March 2012. The discount rate adopted for that assessment was 3% a year.) A higher discount rate for scheme funding purposes results in a lower assessed cost of benefit accrual. The discount rate for scheme funding is set by HM Treasury, and is expected to stay the same for a period so as to provide a stable budgeting mechanism for pension accrual within government. The discount rate for Annual Accounts is set each year by HM Treasury to reflect the requirements of IAS19.

19. The estimated pensionable payroll for the financial year 2014-15 was £5.5 billion (derived from the contributions payable by employers over the year). The scheme accounts assess the accruing cost of pensions in 2014-15 (at 56.9% of Officer pensionable salaries and 44.8% of Other Ranks pensionable salaries) to be £2.7 billion. There is also a small past service cost for the year 2014-15 which is related to changes in the treatment of AFPS75 widow(er)s' pensions on cohabitation/remarriage.

Sensitivity analysis

20. The results of any actuarial calculation are inherently uncertain because of the assumptions which must be made. In recognition of this uncertainty I have been asked to indicate the approximate effects on the actuarial liability as at 31 March 2015 of changes to the significant actuarial assumptions.

21. Changes to IAS19 published on 16 June 2011 introduced enhanced disclosure requirements for defined benefits pension schemes, including the AFPS. In particular, we understand these include a requirement to disclose a sensitivity analysis for each 'significant' actuarial assumption.

22. The principal financial assumptions are the future increases in pensionable salary due to general inflation (earnings increases), pension increases (both in payment and deferment), and the rate of interest (or discount rate) used to calculate the value of the benefits and contributions. A key demographic assumption is pensioner mortality.

23. As a result of the scheme reform and the MoD's New Employment Model, there is significant uncertainty associated with timings of member exits (withdrawals and retirements) in future. Relatively few members of the AFPS remain in service until their normal pension age. However, a significant proportion retire with immediate benefits in the form of an Immediate Pension (IP) or Early Departure Payments (EDP), often from around age 40. The numbers of members reaching their IP or EDP qualification points could potentially have an impact on the scheme liabilities and so we have included an indication of the approximate effect (on the total past service liability) of a 5% increase in the number of new entrants reaching IP/EDP point compared to the main liability calculations.

24. Table G shows the indicative effects on the total liability as at 31 March 2015 of changes to these assumptions (rounded to the nearest ½%).

Table G: Sensitivity to significant assumptions

Change in assumption		Approximate effect on total liability	
Financial assumptions			
(i) discount rate*	+½% a year	- 10%	- £14.9 billion
(ii) earnings increases*	+½% a year	+ 1%	+ £1.4 billion
(iii) pension increases*	+½% a year	+ 9%	+ £13.5 billion
Demographic assumptions			
(iv) additional one year increase to life expectancy at retirement*		+ 2%	+ £3.5 billion
(vi) a 5% increase in the proportion of new entrants who reach IP/EDP point		+ 0%	+ £0.4 billion

* Opposite changes in the assumptions will produce approximately equal and opposite changes in the liability.

Alan Dorn
Government Actuary's Department
1 May 2015

Statement of Accounting Officer's Responsibilities

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

The combined financial statements must give a true and fair view of the state of affairs of the combined schemes at the year end and of the net resource outturn and cashflows for the year then ended. The financial statements are required to provide disclosure of any material expenditure or income that has not been applied to the purposes intended by Parliament or material transactions that have not conformed to the authorities that govern them. In addition, the financial statements must be prepared so as to ensure that the contributions payable to the Scheme during the year have been paid in accordance with the Scheme rules and the recommendations of the Actuary.

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

- Observe the accounts direction issued by HM Treasury including the relevant accounting and disclosure requirements, and apply suitable accounting policies on a consistent basis;
- Make judgements and estimates on a reasonable basis;
- State whether applicable accounting standards, as set out in the FReM have been followed, and disclose and explain any material departures in the financial statements; and
- Prepare the financial statements on a going concern basis.

HM Treasury has appointed the Permanent Head of the Department as Accounting Officer for the Armed Forces Pension Scheme. The responsibilities of an Accounting Officer, including responsibility for the propriety and regularity of the public finances for which the Accounting Officer is answerable, for keeping proper records and for safeguarding the assets of the Pension Scheme are set out in the Accounting Officers' Memorandum issued by HM Treasury and published in Annex 1 of the FReM.

The Governance Statement

Scope of Responsibilities

1. As the Accounting Officer for the Armed Forces Pension Scheme (AFPS) and the Armed Forces Compensation Scheme (AFCS), collectively “the Schemes”, I have responsibility for maintaining a sound system of governance that supports the achievement of the Schemes’ policies, aims and objectives, whilst safeguarding the public funds and departmental assets for which I am personally responsible, in accordance with the responsibilities assigned to me in Managing Public Money. Where necessary I, or officials on my behalf, engage with Treasury officials on funding and policy issues pertaining to these Schemes.

2. In discharging this responsibility, I am responsible for putting in place proper arrangements for the governance of the Schemes’ affairs which facilitate the effective discharge of their statutory functions and which include arrangements for the management of risk.

3. The Schemes have adopted the Corporate Governance Code for Central Government as far as is practicable in the context of a pension scheme. The Executive Committee have operated in accordance with the recognised precepts of good corporate governance: leadership, effectiveness, accountability and sustainability.

The Purpose of the Governance Framework

4. The governance framework comprises the systems and processes, and culture and values, by which the Schemes are administered and controlled. It also includes the activities by which they account to Parliament.

5. The system of internal control is a significant part of the governance framework and is designed to manage risk to a reasonable level. It cannot eliminate all risk of failure to achieve policies, aims and objectives and therefore can 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 Schemes’ 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.

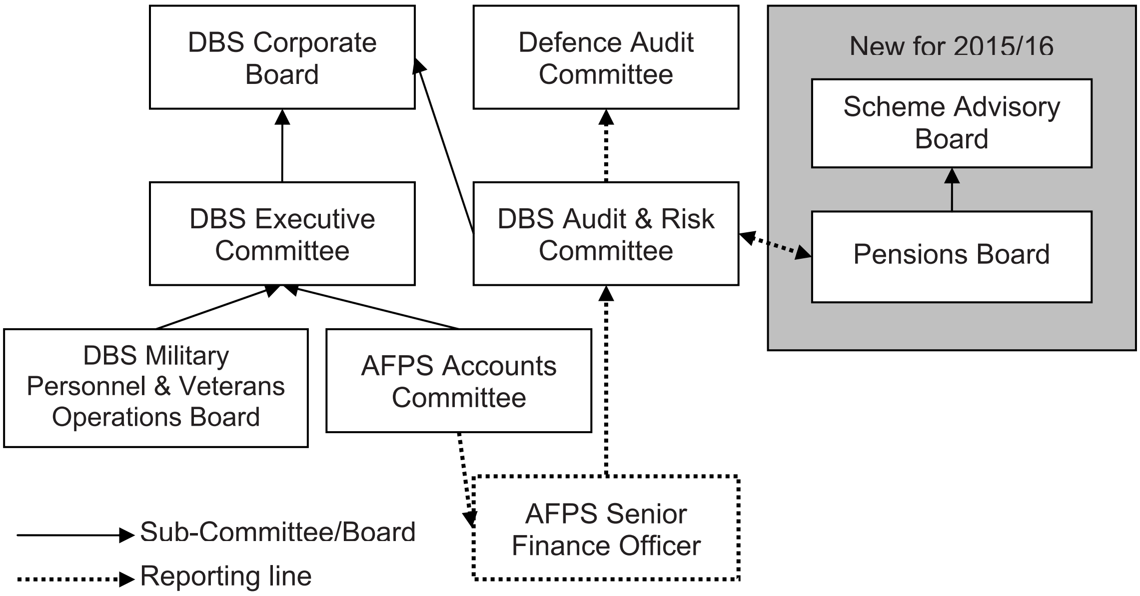
6. The governance framework has been in place for the Schemes for the year ended 31 March 2015.

The Schemes’ Governance Framework

7. Following the merger of the Service Personnel and Veterans Agency (SPVA) with Defence Business Services (DBS) on 1 April 2014, I delegated responsibility for day to day administration of the Schemes to the Chief Executive Officer (CEO) of the DBS and I delegated the role of Senior Finance Officer (SFO) for the Schemes to DBS Head of Resources. The Ministry of Defence (MOD) has a contract with Serco Ltd to provide management services to DBS. The CEO and a number of the Executive appointments are made through Serco Ltd and these appointments are detailed in paragraph 10 overleaf. In January 2015 DIA gave substantial assurance that the DBS governance framework effectively supported delivery of the Schemes following the merger of DBS and SPVA.

8. Administration of the Schemes is delivered through a combination of MOD civilian personnel and contractors and CSC Computer Sciences Ltd (CSC), via a commercial partnering agreement which came into effect on 11 November 2012. The arrangement for joint working with CSC is governed by commercial agreements and is managed by DBS Military Personnel & Veterans Operations Board (MP&V OB).

Boards and Committees



9. The **DBS Corporate Board** comprises of a Non-Executive Chair, two other Non-Executive Directors (NEDs), the DBS CEO, two DBS Executive Heads and the Head of MOD Corporate Services Transformation Team. The Board oversees the conduct of business in DBS, supports and supervises the DBS executive management, leads on compliance with all applicable Government/Defence policies and governs and oversees the transformation programmes and service delivery issues. No specific review of Board performance was undertaken in 2014/15.

Corporate Board Members Composition	**Meetings Attended**
Non-Executive Chair: Keith Archer-Jones	6 of 6
Executive Members:	
Rod McCurdy, Chief Executive Officer	6 of 6
Simon Freeman, Chief Operating Officer	6 of 6
Georgina Benzies, Head of Resources	5 of 6
Richard Vincent, Head of MOD Corporate Services Transformation Team	6 of 6
Non-Executive Directors:	
Chris Wright	5 of 6
Paul Smith	5 of 6

10. The **DBS Executive Committee (EC)** is chaired by the CEO and comprises the Executive Heads of Department and the Schemes' SFO. The EC is responsible for managing DBS within Corporate Board agreed financial limits, primary authority for day to day management of DBS save for those matters reserved to the Corporate Board. The EC meets once/twice a month and convened 20 times between April 2014 and March 2015. No specific review of Committee performance was undertaken in 2014/15.

EC Members Composition – Serco	**Meetings Attended**
Chief Executive Officer: Rod McCurdy, (Chair), from 05/05/2014 Mike Stone (Chair), until 05/05/2014	 15 of 17 3 of 3
Executives:	
Simon Freeman, Chief Operating Officer, from 15/05/2014 Rod McCurdy,Chief Operating Officer, until 05/05/2014	15 of 17 2 of 3
Vince Groome, Chief Information Officer	19 of 20
Helen Hall, Chief People Officer, from 22/09/2014 Russell Sowden, Chief People Officer, until 21/09/2014	8 of 8 12 of 12
Andy Tyler-Smith, Operations Director, from 17/11/2014 Giles Wood, Operations Director, from 08/05/2014, until 31/08/2014 Simon Freeman, Operations Director, until 15/05/2014	0 of 4 4 of 8 2 of 3
Andrew Thompson, Service Development Director, from 01/09/2014	6 of 9
Stuart Cotton, Development Director, until 01/11/2014	6 of 15
Nicola Smith, Transformation Director, from 01/05/2014 Chris O’Connor, Transformation Director, until 01/05/2014	13 of 17 1 of 3
EC Members Composition - MOD Personnel **Executives:**	
Georgina Benzies, Head of Resources	17 of 20
Jon Parkin, Head of Veterans UK	17 of 20
Andy Dowds, Head of Finance	16 of 20
Commodore Ian Bisson, Head of Military Personnel	16 of 20
Andrew Stafford, Head of Civilian Personnel	19 of 20
Caroline Rumming, Head of National Security Vetting	16 of 20
Air Vice-Marshal Ross Paterson, Service Personnel Veterans CE, until 30/06/2014	3 of 7

11. The **DBS Military Personnel & Veterans Operations Board (MP&V OB)**, a sub-committee of the EC, manages the commercial agreements with CSC. The Service Delivery Management Team within DBS actively monitor the performance of CSC against over 700 Measures of Performance (MOPs). Any failure to meet MOPs, and actions to ensure future compliance, are discussed at the monthly Service Delivery Working Group attended by representatives from both DBS and CSC, and reported to the MP&V OB. The Board is also responsible for reviewing unit level risks on a monthly basis, with the most critical escalated to the EC where the impacts are assessed and appropriate mitigating action taken.

12. The **AFPS Accounts Committee**, a sub-committee of the EC, undertakes a detailed review of financial performance of the Schemes on a monthly basis. Membership of the AFPS Accounts Committee includes three EC members: Head of Resources (as Schemes’ SFO), Head of Veterans UK and Head of Finance. Escalations and a monthly summary report from the AFPS Accounts Committee are submitted to the EC for review, decision and endorsement.

13. The **DBS Audit & Risk Committee (ARC),** a sub-committee of the DBS Corporate Board, comprises of one Non-Executive Chair and one MOD Executive, and is attended by members of the EC. The ARC supports the CEO in discharging his responsibilities for Risk Control and Governance by reviewing the comprehensiveness, reliability and integrity of DBS's Risk and Assurance framework, agreeing priority risk areas for Defence Internal Audit (DIA) annual programme, reviewing the outcome of work by DIA and NAO and following progress on completion of actions. The ARC reviewed the 2014/15 AFPS Accounts prior to final review by the Defence Audit Committee. The Committee met five times between April 2014 and March 2015. An additional NED has been recruited from May 2015.

ARC Members Composition	Meetings Attended
Non-Executive Chair: Paul Smith	5 of 5
MOD Executive: Richard Vincent Head of MOD Corporate Services Transformation Team	5 of 5

14. The **Defence Audit Committee (DAC)** is responsible for making a recommendation to the Accounting Officer for approval of the AFPS Accounts prior to publication. The DAC gains assurance on the reliability of the financial and reporting disclosures from the DBS ARC review. The DAC comprises of a Non-Executive Chair and three other NEDs. The DAC is also attended by the Permanent Secretary for Defence or the MOD Director General Finance, the Head of DIA and a representative from the National Audit Office

15. The **Scheme Advisory Board** and **Pensions Board**. As recommended by the Independent Public Service Pensions Commission, the Secretary of State for Defence, who acts as the Armed Forces Pension Scheme Manager, agreed the structure and composition of the Scheme Advisory Board and a Pensions Board in July 2014. The Boards have been in place from 1 April 2015.

16. The Government introduced a framework for the governance and administration of public service pension schemes under the Public Service Pensions Act 2013, which also provides an extended regulatory oversight by The Pension Regulator. The appointed boards will be responsible for assisting the Scheme Manager with compliance of the Scheme rules and legislation relating to the governance and administration of the Scheme; including any requirements imposed by the Pension Regulator.

Financial Management

17. The Schemes' financial management arrangements conform to the requirements of HM Treasury as laid out in "Managing Public Money". The DBS Head of Resources is the SFO for the Schemes and is a key member of the EC. The Schemes' financial management reports provide the level of detail for effective oversight and are reviewed by the AFPS Accounts Committee on a monthly basis. CSC provides an operations dashboard of pension volumes/values which is reviewed by the Military Personnel & Veterans Operation Board on a monthly basis. Performance against Key Performance Indicators is reviewed by the DBS Corporate Board. Management's confidence in the financial/management information and reporting is supported through the work of these Committees/Boards and is reviewed by DIA as part of a rolling three year audit programme of the Schemes.

18. The Pensions Finance Team, with input from the Government Actuary's Department and challenge from HM Treasury and the Office of Budget Responsibility, refined future forecasts to take into account new and emerging trends, central assumptions and anticipated changes in behaviour as a result of perceived and actual changes to the Schemes. The Pensions Finance Team falls under the responsibility of DBS Head of Resources but worked closely with DBS Veterans UK throughout the financial year to ensure emerging issues were factored into in-year forecasts. Pensions Finance and Veterans UK also liaised with other major UK Public Pension Schemes throughout the year to identify best practice on a number of ongoing initiatives.

Risk Assessment

19. Risk assessment processes within DBS are in place throughout the year. Risks are identified and recorded on the business unit risk registers and are reviewed on a monthly basis by the MP&V OB. The most critical are escalated to the EC where the impacts are assessed and appropriate mitigating action taken. The ARC has oversight of all risks raised within DBS. Any risks not capable of being managed at Committee level would be escalated to the Chief of Defence People (CDP) and/or Director General Finance, and ultimately to me for action. No risks were escalated by DBS in 2014/15.

The Risk and Control Framework

20. A framework of internal controls within the Schemes' day-to-day operations (including authorisations, reconciliations and separation of duties) control the risks of fraud or error; the framework is documented to current best practice standards and is incorporated within the process guides provided for staff. This framework is maintained, updated and reviewed on an annual basis by the DBS Process Controls Management Team.

21. Risk owners and managers are identified as part of the risk management process. Formal risk management training is provided to project and operational teams. Risk management information and guidance is available to all on the MOD intranet.

22. Oversight of the Schemes' rules and policies and advice on their application is provided by the Chief of Defence People's Service Personnel Policy branch.

23. During this period the EC has continued to ensure that the seven key fundamental principles have been used to underpin the way that risks are managed within DBS:

- Nested Risks and Associated Action Plans;
  A nested approach to risk management in accordance with the DBS Risk Governance structure, ensuring risks are owned from the business (Assistant Head) level through to DBS Senior Management level, with each level taking responsibility for mitigation actions within their scope of responsibility.

- Clear Links to Governance Approach;
  Risks are managed throughout the DBS Governance structure ensuring that responsibilities and escalation routes are clearly identified within a formalised structure. This also includes Shared (MOD/Commercial Partner) risk. Risks are standing agenda items at a variety of DBS Governance forums, including the DBS Corporate Board, EC, ARC, Senior Leadership Team as well as within the Functional Governance areas of Operations, Transformation, People and Technology. The Minutes of the Boards record Actions, Decisions and Escalations and are used as a vehicle to provide feedback to the Risk Owner/Manager and to update the Risk Register.

- Independent Quality Assurance;
  A dedicated Risk Management Team providing oversight and implementation of the Risk Management Strategy throughout DBS. Providing assurance and guidance to individual risk owners, and ensuring a risk management culture is embedded throughout DBS.

- Managing Risk Volumes;
  The implementation of a nested risk structure ensuring that for each governance group handling risks, the number of risks remains manageable.

- Risk Appetite & Thresholds;
  Definition of a risk appetite statement that is also expressed as a series of boundaries in time, cost and performance, with tolerance levels allowable for risk at differing levels of the organisation.

- Risk Aggregation;
  Pillars being responsible for escalating risks which exceed their tolerances, and the DBS Risk Manager responsible for aggregating common risks from two or more pillars which collectively exceed the tolerance.

- Management of Strategic Risks;
  Strategic risks are identified at any time at any level of the business, and then managed at the EC.

Fraud

24. DBS has a fraud focal point offering advice and guidance on fraud related matters, additionally all staff have direct access to the Defence Irregularity Cell to escalate any suspicions of irregularity. Potential AFPS fraudulent claims are reported to the MOD Fraud Incident and Irregularity Reporting Unit for investigation by the MOD Police or Royal Military Police. DBS continues to utilise the National Fraud Initiative (NFI) to identify potential AFPS fraudulent claims and a small internal team is resourced to investigate any potential fraudulent AFCS claims. The Report of the Managers on pages 2 to 10 contains details of the results of the NFI exercises since 2002.

25. Since 2012/13 DBS has canvassed 76,000 pensioners to confirm their continuing entitlement to pension under the Scheme rules. The exercise was completed during 2013/14 and resulted in the suspension of 782 pensions due to unreported deaths or other unreported changes in circumstances affecting pensioner's entitlement. Recovery of overpayments is being pursued on a case by case basis as each case is investigated. To date there are 520 pensions still suspended with an annual saving valued at £1.8M per year. No overpayments relating to fraud were written off in 2014/15.

Information Assurance

26. Data is managed in accordance with the principles of HM Government's Information Assurance Maturity Model (IAMM). The CEO is the Senior Information Risk Owner (SIRO) for DBS, with Information Asset Owners (IAOs) supporting the SIRO. Information Assurance (IA) training remains a mandatory requirement, with specific modules for dedicated IA roles - General Users, IAOs and NEDs.

27. Following the work undertaken last year to identify the gaps within IAMM (Levels 1-3), work has continued to review the evidence and to provide increased evidence to support the gaps. Significant efforts have been made during this year to embed the IA governance structure, IA risk management and upward reporting through the IAOs, SIRO and to the MOD Chief Information Officer (CIO). Building on the identification of the information assets within DBS, work is now underway to develop and issue Memorandum of Understandings (MOUs) to those third parties and Delivery Partners responsible for handling DBS information assets and to implement a programme of assurance activity to ensure ongoing protection of the information. The implementation of the IAO Steering Group last year has provided another layer within the IA governance structure, meeting on a quarterly basis to review IA risks and allow upward reporting to the DBS CIO and SIRO.

28. As a result of the SPVA merger with DBS, work continues to identify areas for improvement within IA across DBS and how IAMM is progressed as a joined up organisation. Work has already progressed to integrate the completion of the Privacy Impact Assessments and the implementation of the MOUs.

29. There have been no data losses reported during the year in relation to the Schemes.

Business Continuity

30. AFPS/AFCS output from DBS Norcross and Glasgow, and the development and implementation of future Compensation and Pensions System (CAPS) pensions and allowances solutions at DBS Gosport, is governed by Business Continuity (BC) measures outlined in the DBS Business Continuity Management Programme Strategy, which is currently under development. Business Impact Analysis (BIA) for key business areas have been completed which indicate that individual Business Continuity Plans (BCP) are required.

31. The Disaster Recovery (DR) Plan for CAPS was updated to version 2.0 on 8 October 2014. It is subject to periodic review, in parallel with the ongoing CAPS transformation.

32. The Business Process Outsourcing Service Delivery BCP was base-lined at version 8.0 on 16 February 2015. This plan covers the Joint Personnel Administration Centre Enquiry Centre and back-office pension activity.

33. During the year sufficient BC testing was undertaken and there were no significant BC incidents affecting pensions delivery.

Review of Effectiveness

34. As Accounting Officer, I have responsibility for reviewing the effectiveness of the governance framework. My review is informed by the work of the MOD internal auditors DIA, the executive managers within the DBS who have responsibility for the development and maintenance of the internal control framework, the ARC who are responsible for risk control and governance, the DAC who are responsible for reviewing and endorsing the year end accounts and comments made by the external auditors in their management letter and other reports.

35. As planned CAPS was upgraded in October 2014 (a project known as PENS003). As part of this upgrade the hardware on which the system runs was replaced and relocated to a new MOD approved Data Centre. Disaster Recovery procedures were also updated. This upgrade provides additional functionality and improves the security and efficiency of Scheme administration.

Internal Audit

36. The Head of DIA or one of his senior managers attends meetings of the ARC and provides expert advice on audit issues.

37. The AFPS assurance programme was developed by DIA with the support of PricewaterhouseCoopers and commenced in 2013/14. The programme is intended to form the basis of a rolling year on year programme of assurance, undertaken by DIA. The programme has been reviewed and progress reports regularly taken by the ARC throughout 2014/15.

38. DIA has reported their overall Annual Audit Opinion for the AFPS as one of Substantial Assurance. This opinion is based on the audit programme undertaken, advisory work performed, attendance at key meetings, engagement with line management and other developments within DBS where they are known to be relevant.

39. During 2014/15 it was found that the AFPS had successfully integrated into the DBS processes covering risk management, internal control and governance. As a result the AFPS had been supported in year by the DBS Governance framework.

40. DIA reported that the overall governance arrangements and that of day-to-day management control remained effective. However, their specific audit work in year identified some weaknesses within the oversight and assurance mechanisms. Primarily these were an over reliance on contractor self reporting, accompanied by weaknesses in some internal checking arrangements. I will ensure that these weaknesses are addressed.

Significant Governance Issues

41. It was reported last year that there had been some differences in the interpretation of the Scheme rules allowing aggregation of service between the AFPS 05 and AFPS 75 Schemes, which occurred between April 2005 and January 2012, resulting in some personnel receiving incorrect Early Departure Payments (EDP) and forecasts based on incorrect aggregation of periods of service. HM Treasury approval was obtained in 2014/15 to write-off the incorrect EDPs paid during this period. Details of the write-off volumes and values are disclosed in Losses and Special Payments note, note 18 to the Scheme Statements. Correct interpretation of the rules was applied from January 2012 until 17 December 2013, when the rules were changed to allow aggregation. HM Treasury approval was obtained in 2014/15 to pay compensation to those members who were prevented from aggregating

their service when discharged from January 2012 until 17 December 2013. The compensation payments made to 31 March 2015, amounting to £4.1M, were borne by the MOD and as such are not reflected in these Accounts.

42. I am pleased to report that there have been no significant governance issues arising during 2014/15.

Future Improvements

43. AFPS will be automatically issuing annual Benefit Information Statements to all members on a rolling programme commencing August 2015. The Schemes are engaging with the 'Tell Us Once' initiative; this will give DBS early notification of deaths which in turn will reduce overpayments of pension and compensation. Work is underway to enhance digital communications with the Schemes' paying agent which will allow confidential/sensitive information to be exchanged securely in real time.

44. Further enhancements to online calculators are planned to meet changing demands and in recognition of significant increase in online usage. A quality improvement schedule for CAPS is also planned. These upgrades will improve functionality and efficiency of Scheme administration.

45. In addition, where a Pension Sharing Order exists, further analysis will be undertaken of the full active population to determine any effect on Annual Allowance limits.

Summary

46. As a result of these reviews I have concluded that the Schemes have operated in line with the Corporate Governance Code for Central Government, and the governance, risk management and internal control framework is well established and working effectively although with some minor weaknesses. These will continue to be addressed over the coming year.

Jon Thompson
Accounting Officer for the Armed Forces Pension Scheme **1 July 2015**
and Armed Forces Compensation Scheme

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

I certify that I have audited the financial statements of the Armed Forces Pension Scheme for the year ended 31 March 2015 under the Government Resources and Accounts Act 2000. The financial statements comprise: the Combined Statements of Comprehensive Net Expenditure, Financial Position, Cash Flows, Changes in Taxpayers' Equity; and the related notes. I have also audited the Statement of Parliamentary Supply and related notes. These financial statements have been prepared under the accounting policies set out within them.

Respective responsibilities of the Accounting Officer and auditor

As explained more fully in the Statement of Accounting Officer's Responsibilities, the Accounting Officer is responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. My responsibility is to audit, certify and report on the financial statements in accordance with the Government Resources and Accounts Act 2000. I conducted my audit in accordance with International Standards on Auditing (UK and Ireland). Those standards require me and my staff to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Scheme's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Accounting Officer; and the overall presentation of the financial statements. In addition I read all the financial and non-financial information in the Report of the Managers, Report of the Actuary and the Governance Statement to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by me in the course of performing the audit. If I become aware of any apparent material misstatements or inconsistencies I consider the implications for my certificate.

I am required to obtain evidence sufficient to give reasonable assurance that the Statement of Parliamentary Supply properly presents the outturn against Parliamentary control totals and that those totals have not been exceeded. The voted Parliamentary control totals are Annually Managed Expenditure (Resource), Non-Budget (Resource) and Net Cash Requirement. I am also required to obtain evidence sufficient to give reasonable assurance that the expenditure and income recorded in the financial statements have been applied to the purposes intended by Parliament and the financial transactions recorded in the financial statements conform to the authorities which govern them.

Opinion on regularity

In my opinion, in all material respects:

- the Statement of Parliamentary Supply properly presents the outturn against voted Parliamentary control totals for the year ended 31 March 2015 and shows that those totals have not been exceeded; and
- the expenditure and income recorded in the financial statements have been applied to the purposes intended by Parliament and the financial transactions recorded in the financial statements conform to the authorities which govern them.

Opinion on financial statements

In my opinion:

- the financial statements give a true and fair view of the state of the Scheme's affairs as at 31 March 2015 and of its net operating cost for the year then ended; and
- the financial statements have been properly prepared in accordance with the Government Resources and Accounts Act 2000 and HM Treasury directions issued thereunder.

Opinion on other matters

In my opinion:

- the information given in the Report of the Managers and the Report of the Actuary for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which I report by exception

I have nothing to report in respect of the following matters which I report to you if, in my opinion:

- adequate accounting records have not been kept or returns adequate for my audit have not been received from branches not visited by my staff or
- the financial statements are not in agreement with the accounting records and returns; or
- I have not received all of the information and explanations I require for my audit; or
- the Governance Statement does not reflect compliance with HM Treasury's guidance.

Report

I have no observations to make on these financial statements.

Sir Amyas C E Morse 7 July 2015
Comptroller and Auditor General

National Audit Office
157-197 Buckingham Palace Road
Victoria
London
SW1W 9SP

Statement of Parliamentary Supply

Summary of Resource Outturn 2014-15

£000								2014-15	2013-14
		Estimate			Outturn				Outturn
	Note	Voted	Non-Voted	Total	Voted	Non-Voted	Total	Voted outturn compared with Estimate: saving/ (excess)	Total
Annually Managed Expenditure - Resource	SOPS2	6,749,204	-	6,749,204	6,446,395	-	6,446,395	302,809	5,454,602
Total Budget		6,749,204	-	6,749,204	6,446,395	-	6,446,395	302,809	5,454,602
Non-Budget -Resource		-	-	-	-	-	-	-	-
Total		**6,749,204**	**-**	**6,749,204**	**6,446,395**	**-**	**6,446,395**	**302,809**	**5,454,602**

Net Cash Requirement 2014-15

£000		**2014-15**		**2014-15**	**2013-14**
	Note	Estimate	Outturn	Outturn compared with Estimate savings/ (excess)	Outturn
	SOPS3	**2,534,144**	**2,532,948**	**1,196**	**2,375,970**

Administration Costs 2014-15

2014-15 Estimate	**2014-15** Outturn	**2013-14** Outturn
-	-	-

Figures in the areas outlined in bold are voted totals or other totals subject to Parliamentary control

Notes to the Statement of Parliamentary Supply

SOPS1. Statement of accounting policies

The Statement of Parliamentary Supply and supporting notes have been prepared in accordance with the 2014-15 Government Financial Reporting Manual (FReM) issued by HM Treasury. The Statement of Parliamentary Supply accounting policies contained in the FReM are consistent with the requirements set out in the 2014-15 Consolidated Budgeting Guidance and Supply Estimates Guidance Manual.

SOPS1.1 Accounting convention

The Statement of Parliamentary Supply and related notes are presented consistently with HM Treasury budget control and Supply Estimates. The aggregates across government are measured using National Accounts, prepared in accordance with the internationally agreed framework 'European System of Accounts' (ESA95). ESA95 is in turn consistent with the System of National Accounts (SNA93), which is prepared under the auspices of the United Nations.

The budgeting system and the consequential presentation of Supply Estimates and the Statement of Parliamentary Supply and related notes, have different objectives to IFRS-based accounts. The system supports the achievement of macro-economic stability by ensuring that public expenditure is controlled, with relevant Parliamentary authority, in support of the Government's fiscal framework. The system provides incentives to departments to manage spending well so as to provide high quality public services that offer value for money to the taxpayer.

The Government’s objectives for fiscal policy are set out in the Charter for Budget Responsibility. These are to:

- ensure sustainable public finances that support confidence in the economy, promote intergenerational fairness, and ensure the effectiveness of wider government policy; and

- support and improve the effectiveness of monetary policy in stabilising economic fluctuations.

SOPS1.2 Comparison with IFRS-based accounts

Many transactions are treated in the same way in National Accounts and IFRS-based accounts, but there are a number of differences as detailed below. A reconciliation of the Scheme’s outturn as recorded in the SoPS compared to the IFRS-based SoCNE is provided in SoPS note 3.

SOPS1.3 Provisions - Administration and Programme expenditure

Provisions recognised in IFRS-based accounts are not recognised as expenditure for national accounts purposes until the actual payment of cash (or accrual liability) is recognised. To meet the requirements of both resource accounting and national accounts, additional data entries are made in the Statement of Parliamentary Supply across Annually Managed Expenditure (AME) and Departmental Expenditure Limit (DEL) control totals, which do not affect the Statement of Comprehensive Net Expenditure. As the Administration control total is a sub-category of DEL, Administration and Programme expenditure reported in the Statement of Parliamentary Supply will differ from that reported in the IFRS-based accounts.

SOPS2. Analysis of net resource outturn by section

£000	2014-15									2013-14
	Outturn							Estimate		Outturn
	Administration			Programme						
	Gross	Income	Net	Gross	Income	Net	Total	Net Total	Net total compared to Estimate	Total
Spending in Departmental Expenditure Limit										
Voted:	-	-	-	-	-	-	-	-	-	-
Non Voted:	-	-	-	-	-	-	-	-	-	-
Annually Managed Expenditure										
Voted:										
A: Retired pay, pensions and other payments to ex-service personnel	-	-	-	8,312,390	1,865,995	6,446,395	6,446,395	6,749,204	302,809	5,454,602
Non Voted:	-	-	-	-	-	-	-	-	-	-
Total	-	-	-	8,312,390	1,865,995	6,446,395	6,446,395	6,749,204	302,809	5,454,602

SOPS3. Reconciliation of Net Resource Outturn to Net Cash Requirement

	Note	Estimate	Outturn	Net Total outturn compared with Estimate: savings/ (excess)
		£000	£000	£000
Net Resource Outturn	SOPS2	6,749,204	6,446,395	302,809
Accruals adjustments:				
Non cash items		(8,612,412)	(8,312,390)	(300,022)
Changes in working capital other than cash		(15,271)	(60,526)	45,255
Use of provision:				
Pension		4,322,736	4,386,599	(63,863)
Compensation Scheme		89,887	72,870	17,017
Net cash requirement		**2,534,144**	**2,532,948**	**1,196**

Combined Statement of Comprehensive Net Expenditure

for the year to 31 March 2015

	Note	2014-15 £000	2013-14 £000
Principal Arrangements – Armed Forces Pension Scheme			
Income			
Contributions receivable	3	(1,865,164)	(1,945,433)
Transfers In	4	(831)	(935)
Expenditure			
Current Service cost	5	2,662,588	2,454,782
Past Service cost	5	30,000	-
Enhancements	6	805	703
Transfers In	7	831	935
Pension financing cost	8	5,597,036	4,803,003
Net Expenditure		**6,425,265**	**5,313,055**
Armed Forces Compensation Scheme			
Movement in provision for AFCS	15	(30,331)	98,359
Compensation financing cost	15	51,461	43,188
Net Expenditure		**21,130**	**141,547**
Combined Net Expenditure	SOPS2	**6,446,395**	**5,454,602**
Other Comprehensive Net Expenditure			
Pension re-measurements:			
Actuarial loss – Armed Forces Pension Scheme	12.8	20,995,339	8,394,944
Actuarial loss – Armed Forces Compensation Scheme	15	203,611	118,659
Total Comprehensive Net Expenditure for the year ended 31 March 2015		**27,645,345**	**13,968,205**

The Notes on pages 34 to 46 form part of these accounts.

Combined Statement of Financial Position

as at 31 March 2015

		2014-15	2013-14
Principal arrangements – Armed Forces Pension Scheme	Note	£000	£000
Current assets:			
Receivables	9	159,826	164,542
Cash and cash equivalents	10	1,196	46,192
Total current assets		161,022	210,734
Current liabilities:			
Payables	11	(527,299)	(516,201)
Total current liabilities		(527,299)	(516,201)
Net current liabilities, excluding pension liability		**(366,277)**	**(305,467)**
Pension liability	12.5	(154,400,000)	(129,500,000)
Net liabilities, including pension liabilities		**(154,766,277)**	**(129,805,467)**
Armed Forces Compensation Scheme			
Receivables	13	284	256
Payables (within 12 months)	14	(2,270)	(2,526)
Provisions for liabilities and charges	15	(1,402,623)	(1,250,752)
Net liabilities		**(1,404,609)**	**(1,253,022)**
Combined Schemes – Total net liabilities		**(156,170,886)**	**(131,058,489)**
Taxpayers' equity:			
General fund		(156,170,886)	(131,058,489)
		(156,170,886)	**(131,058,489)**

Jon Thompson
Accounting Officer for the Armed Forces Pension Scheme
and Armed Forces Compensation Scheme **1 July 2015**

The Notes on pages 34 to 46 form part of these accounts.

Combined Statement of Changes in Taxpayers' Equity

for the year ended 31 March 2015

	Note	2014-15 £000	2013-14 £000
Balance at 1 April		**(131,058,489)**	**(119,466,254)**
Net Parliamentary Funding – drawn down		2,487,952	2,372,580
Net Parliamentary Funding – deemed		46,192	49,582
Supply payable adjustment	10	(1,196)	(46,192)
Excess Vote – Prior Year		-	-
CFERs payable to the Consolidated Fund		-	-
Contingencies Fund Advance		116,000	50,000
Repayment to the Contingencies Fund		(116,000)	(50,000)
Combined Net Expenditure for the Year	SOPS2	(6,446,395)	(5,454,602)
Actuarial (loss) – Armed Forces Pension Scheme	12.8	(20,995,339)	(8,394,944)
Actuarial (loss) – Armed Forces Compensation Scheme	15	(203,611)	(118,659)
Net change in Taxpayers' Equity		**(25,112,397)**	**(11,592,235)**
Balance at 31 March		**(156,170,886)**	**(131,058,489)**

The Notes on pages 34 to 46 form part of these accounts.

Combined Statement of Cash Flows

for the year ended 31 March 2015

	Note	2014-15 £000	2013-14 £000
Cash flows from operating activities			
Combined net expenditure for the year	SOPS2	(6,446,395)	(5,454,602)
Adjustments for non-cash transactions:			
Decrease / (Increase) in receivables – principal arrangements	9	4,716	6,780
Increase in receivables - AFCS	13	(28)	(161)
Increase / (Decrease) in payables – principal arrangements	11	56,094	(83,778)
(Decrease) / Increase in payables – AFCS	14	(256)	(168)
Increase in pension provision	12.5	8,289,624	7,257,785
Increase in pension provision – enhancements and transfers in	12.5	1,636	1,638
Use of provisions – pension liability	12.6	(4,291,258)	(4,089,291)
Use of provisions – refunds and transfers	12.7	(95,341)	(65,076)
Increase in provisions – compensation Scheme	15	21,130	141,547
Use of provisions – compensation Scheme	15	(72,870)	(90,644)
Net cash outflow from operating activities		**(2,532,948)**	**(2,375,970)**
Cash flows from financing activities			
From the Consolidated Fund (Supply): current year		2,487,952	2,372,580
From the Contingencies Fund		116,000	50,000
Repayment to the Contingencies Fund		(116,000)	(50,000)
Net Financing		**2,487,952**	**2,372,580**
Net Decrease in cash and cash equivalents in the period before adjustment for receipts and payments to the Consolidated Fund		**(44,996)**	**(3,390)**
Receipts due to the Consolidated Fund which are outside the scope of the Scheme's activities		-	-
Payments of amounts due to the Consolidated Fund		-	-
Net Decrease in cash and cash equivalents in the period after adjustment for receipts and payments to the Consolidated Fund	10	**(44,996)**	**(3,390)**
Cash and cash equivalents at the beginning of the period	10	**46,192**	**49,582**
Cash and cash equivalents at the end of the period	10	**1,196**	**46,192**

The Notes on pages 34 to 46 form part of these accounts.

Notes to the Scheme Statements

1. Basis of Preparation of the Scheme Financial Statements

The financial statements of the combined Scheme have been prepared in accordance with the relevant provisions of the 2014-15 Government Financial Reporting Manual (FReM) issued by HM Treasury. The accounting policies contained in the FReM apply International Financial Reporting Standards (IFRS) as adapted or interpreted for the public sector. IAS 19 Employee Benefits and IAS 26 Accounting and Reporting by Retirement Benefit Plans are of particular relevance to these statements.

In addition to the primary statements prepared under IFRS, the FReM also requires the Scheme to prepare an additional statement – a Statement of Parliamentary Supply. This statement and its supporting notes, shows Outturn against Estimate in terms of the net resource requirement and the net cash requirement.

1.1 The Armed Forces Pension Scheme (AFPS) is a contracted-out, unfunded, defined benefit pay-as-you-go occupational pension scheme operated by the Ministry of Defence (MOD) on behalf of members of the Armed Forces who satisfy the membership criteria.

1.2 The employer's charge to the pension Scheme is met by payment of a Superannuation Contribution Adjusted for Past Experience (SCAPE), calculated as a percentage of military pay based on rank. The SCAPE contribution made by the MOD partially funds the payments made by the AFPS in year.

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

1.4 The administrative expenses (staff, office facilities, etc.) associated with the operation of the Scheme are borne by MOD and are reported in the Department's Statement of Comprehensive Net Expenditure (SoCNE).

1.5 The financial statements of the Scheme summarise the transactions of the AFPS incorporating the Armed Forces Compensation Scheme (AFCS). The Statement of Financial Position shows the unfunded net liabilities of the Schemes; the SoCNE shows, amongst other things, factors contributing to the change in the net liabilities analysed between the pension cost, enhancements and transfers in, and the financing cost on the Schemes' liabilities. Further information about the actuarial position of the Scheme is dealt with in the Report of the Actuary, and the Scheme financial statements should be read in conjunction with that Report.

1.6 The Scheme Statements summarise the transactions of not only the AFPS but also the Reserve Forces Pension Scheme (RFPS), Gurkha Pension Scheme (GPS), Non-Regular Permanent Staff (NRPS) Pension Scheme, Full-Time Reserve Service (FTRS) Pension Scheme, several minor pension schemes and the AFCS. These are administered and managed in a similar way to the AFPS. From 1 April 15 the Armed Forces Pension Scheme 2015 (AFPS 15) was introduced – there are no provisions for this new Scheme within these Accounts.

1.7 Members have no choice over the allocation of benefits between the lump sum and the annual pension. However, there are two forms of commutation for existing pensioners – resettlement commutation and life commutation, where the pensioner has the option to abate their pension in return for a lump sum. Members of the AFPS 05 also have the option to reverse-commute their lump sum. Benefit payments are accounted for on an accruals basis. However, from the 1 April 15, the introduction of AFPS 15 will mean that members will not automatically receive a lump sum, but will be given the choice to convert pension income into a tax-free lump sum.

1.8 The Report of the Actuary, shown on pages 11 to 15, which takes account of future obligations, has been prepared by the Government Actuary's Department and should be read in conjunction with the Scheme Statements. The Report of the Actuary has been prepared using the projected unit credit method.

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

1.10 In order that the defined benefit obligations recognised in the financial statements do not differ materially from those that would be determined at the reporting date by a formal actuarial valuation, the FReM requires that “the period between formal actuarial valuations shall be four years, with approximate assessments in intervening years”. Approximate actuarial assessments in intervening years between formal valuations using updated membership data (referred to as 'roll forward data') are accepted as providing suitably robust figures for financial reporting purposes.

2. Statement of accounting policies

The accounting policies contained in the FReM follow IFRS to the extent that they are meaningful and appropriate in the public sector context.

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

2.1 Accounting convention

These accounts have been prepared under the historical cost convention.

2.1.1 Contributions receivable

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

2.1.1.2 Additional Voluntary Contributions (AVCs) are accounted for on an accruals basis. Contributions deducted from employees’ salaries are in respect of ‘in-Scheme’ enhancements. Neither Free-Standing Additional Voluntary Contributions (FSAVCs) nor payments to providers of stakeholder pensions are brought into account in this statement. The associated increase in the Scheme liability is recognised as expenditure.

2.1.2 Transfers in

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

2.1.3 Other income

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

2.1.4 Current service cost

The current service cost is the increase in the present value of the Scheme liabilities arising from current members’ service in the current period and is recognised in the Statement of Comprehensive Net Expenditure. The cost is based on a discount rate of 1.8% real (i.e. 4.35% including inflation).

2.1.5 Past service costs

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

2.1.6 Pension financing cost

The financing cost is the increase during the period in the present value of the Scheme liabilities because the benefits are one period closer to settlement and is recognised in the Statement of Comprehensive Net Expenditure. The financing cost is based on the discount rate of 1.8% real (i.e. 4. 35% including inflation).

2.1.7 Other expenditure

Other payments are accounted for on an accruals basis.

2.1.8 Scheme liability

2.1.8.1 Provision is made for liabilities to pay pensions and other benefits in the future. The Scheme liability is measured on an actuarial basis using the projected unit credit method and as at 31 March 2014 was discounted at 1.8% real (i.e. 4.35% including inflation).The discount rate changed on 31 March 2015 to 1.3% real (i.e. 3.55% including inflation) and the Scheme liability was discounted at this rate. Further details of the financial assumptions used are set out at Note 12 to these accounts and in the Report of the Actuary on pages 11 to 15.

2.1.8.2 Full actuarial valuations by a professionally qualified actuary are typically obtained at intervals not exceeding four years (see note 1.10). The actuary reviews the most recent actuarial valuation at the Statement of Financial Position date and updates it to reflect current conditions.

2.1.9 Pension benefits payable

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

2.1.10 Pension payments to those retiring at their normal retirement age

A retiring member has no choice over the allocation of benefits awarded between the value of the lump sum and the annual pension. The transaction is accounted for as a decrease in the Scheme liability on an accruals basis. However, from the 1 April 15, the introduction of AFPS 15 will mean that members will not automatically receive a lump sum, but will be given the choice to convert pension income into a tax-free lump sum.

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

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

2.1.12 Lump sums payable on death in service

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

2.1.13 Actuarial gains and losses

Actuarial gains and losses arising from any new valuation and from updating the latest actuarial valuation to reflect conditions at the Statement of Financial Position date are recognised in the Statement of Comprehensive Net Expenditure for the year.

2.1.14 Armed Forces Compensation Scheme

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

2.1.15 Cash and cash equivalents

Cash and cash equivalents comprise cash in hand and current balances with banks and similar institutions, which are readily convertible to cash and are subject to insignificant risk of changes in value and have an original maturity of three months or less. For the purpose of the consolidated cash flow statement, cash and cash equivalents are stated net of bank overdrafts. Where relevant, bank overdrafts are included within payables on the Combined Statement of Financial Position, and separately disclosed within note 10.

Statement of Comprehensive Net Expenditure – Armed Forces Pension Scheme

3. Pension contributions receivable

	2014-15	2013-14
	£000	£000
Employers	1,864,359	1,944,730
Employees:		
Purchase of added years	805	703
	1,865,164	**1,945,433**

£3,000M contributions are expected to be payable to the Scheme in 2015-16.

4. Pensions transfers-in (see also Note 7)

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

	2014-15	2013-14
	£000	£000
Individual transfers in from other Schemes	831	935
	831	**935**

5. Service Cost

	2014-15	2013-14
	£000	£000
Current service cost (see Note 12.5)	2,662,588	2,454,782
Past service cost (see Note 12.5)	30,000	-
	2,692,588	**2,454,782**

6. Enhancements (see also Report of the Managers and Note 12.5)

	2014-15	2013-14
	£000	£000
Employees purchase of added years	805	703
	805	**703**

7. Transfers in – additional liability

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

	2014-15	2013-14
	£000	£000
Individual transfers in from other schemes	831	935
	831	**935**

8. Pension financing cost (see also Note 12.5)

	2014-15	2013-14
	£000	£000
Net interest on defined benefit liability	5,597,036	4,803,003
	5,597,036	**4,803,003**

Statement of Financial Position – Armed Forces Pension Scheme

9. Receivables

9.1 Analysis by type

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

	2014-15	2013-14
	£000	£000
Amounts falling due within one year:		
Overpaid pensions	4,548	5,019
Bereavement Scholarship Scheme	213	203
Ministry of Defence – SCAPE & AVC receipts and Transfers In	152,880	157,571
	157,641	**162,793**
Amounts falling due after more than one year:		
Overpaid pensions	2,185	1,749
	159,826	**164,542**

9.2 Analysis by organisation

	Amounts falling due within one year		Amounts falling due after more than one year	
	2014-15	2013-14	2014-15	2013-14
	£000	£000	£000	£000
Balances with other central government bodies:				
Ministry of Defence	152,880	157,571	-	-
Devolved Administrations (AFBSS)	213	203	-	-
Balances with bodies external to government	4,548	5,019	2,185	1,749
Total receivables	**157,641**	**162,793**	**2,185**	**1,749**

10. Cash and cash equivalents

	2014-15	2013-14
	£000	£000
Balance at 1 April	46,192	49,582
Net change in cash balances	(44,996)	(3,390)
Balance at 31 March	**1,196**	**46,192**
The following balances at 31 March were held at:		
Government Banking Services	1,196	46,192
Balance at 31 March	**1,196**	**46,192**

11. Payables

11.1 Analysis by type

	2014-15	2013-14
	£000	£000
Amounts falling due within one year:		
Pensions	408,559	368,718
HM Revenue & Customs	59,199	52,846
Third party organisations	841	810
Ministry of Defence	57,424	47,532
Bereavement Scholarship Scheme	80	103
	526,103	470,009
Amounts issued from the Consolidated Fund for supply but not spent at year end	1,196	46,192
	527,299	**516,201**

11.2 Analysis by organisation

	Amounts falling due within one year	
	2014-15	**2013-14**
	£000	£000
Balances with other central government bodies:		
HM Revenue & Customs	59,199	52,846
Consolidated Fund	1,196	46,192
Ministry of Defence	57,424	47,532
Department for Business, Innovation & Skills	80	103
Balances with bodies external to government	409,400	369,528
Total payables	**527,299**	**516,201**

12. Pension Liability

12.1 Assumptions underpinning the pension liability

The Armed Forces Pension Scheme is an unfunded defined benefit scheme. The Government Actuary's Department carried out an assessment of the Scheme liabilities as at 31 March 2015.The Report of the Actuary on pages 11 to 15 sets out the scope, methodology and results of the work the Actuary has carried out.

The Scheme managers together with the Actuary and the Auditor have signed a Memorandum of Understanding that identifies, as far as practicable, the range of information that the Scheme managers should make available to the Actuary in order to meet the expected requirements of the Scheme Auditor. This information includes, but is not limited to, details of:

- Scheme membership, including age and gender profiles, active membership, deferred pensioners and pensioners;

- benefit structure, including details of any discretionary benefits and any proposals to amend the Scheme;

- income and expenditure, including details of expected bulk transfers into or out of the Scheme; and,

- following consultation with the Actuary, the key assumptions that should be used to value the Scheme liabilities, ensuring that the assumptions are mutually compatible and reflect a best estimate of future experience.

The key assumptions used by the Actuary were:

	At 31 March 2015	At 31 March 2014	At 31 March 2013	At 31 March 2012	At 31 March 2011
Rate of increase in salaries	4.2%	4.5%	3.95%	4.25%	4.9%
Inflation assumption	2.2%	2.5%	1.7%	2.0%	2.65%
Discount rate net of pension increases	1.3%	1.8%	2.35%	2.8%	2.9%
Mortality rate at age 60					
- Current Pensioners					
• Officers Men	29.6	29.3	29.2	29.0	29.2
• Officers Women	32.1	31.8	32.6	32.4	32.5
• Other Ranks Men	26.9	27.4	27.1	27.0	27.1
• Other Ranks Women	29.4	29.9	30.5	30.4	30.4
- Future Pensioners (from active status) *					
• Officers Men	31.9	31.6	31.7	31.5	31.1
• Officers Women	34.4	34.1	35.2	35.0	34.6
• Other Ranks Men	29.1	29.7	29.5	29.4	29.0
• Other Ranks Women	31.6	32.2	33.0	32.9	32.5

* Life expectancies for active members have been calculated based on members aged 40 as at 31 March 2015.

These key assumptions are inherently uncertain, since it is impossible to predict with any accuracy future changes in the rate of salary increases, inflation, longevity or the return on corporate bonds. The Actuary uses professional expertise in arriving at a view of the most appropriate rates to use in the annual valuation of the Scheme liabilities. However, the Scheme managers acknowledge that the valuation reported in these Accounts is not certain, since a change in any one of these assumptions will either increase or reduce the liability. For example, on its own, even a small rise in the assumed rate of inflation will result in an increase in the pension liability.

The assumption that has the biggest impact on the amount of the reported liability is the discount rate net of price inflation. As set out in the FReM, and as required by IAS 19, the discount rate net of price inflation is based on yields on high quality corporate bonds. The rates are set out in the above table. Any decrease in the discount rate net of price inflation leads to a significant increase in the reported liability.

In accordance with IAS 19 the Scheme Managers are required to undertake a sensitivity analysis for each significant actuarial assumption as of the end of the reporting period, showing how the defined benefit obligation would have been affected by changes in the relevant actuarial assumption that were reasonably possible at that date. This analysis, including details of the methods and assumptions used in preparing the sensitivity analyses, the limitations of these methods, and the reasons for any changes in methods and assumptions used in preparing the sensitivity analyses, are included in the analysis of the pension liability below.

Analysis of the pension liability

	At 31 March 2015 £Bn	At 31 March 2014 £Bn	At 31 March 2013 £Bn	At 31 March 2012 £Bn	At 31 March 2011 £Bn
Pensions in Payment	92.3	74.0	69.2	62.6	58.3
Deferred Pensions	25.0	22.1	17.2	14.4	13.8
Active Members (Past Service)	37.1	33.4	31.6	28.6	28.5
Total	**154.4**	**129.5**	**118.0**	**105.6**	**100.6**

12.2 Pension Scheme liabilities accrue over employees' periods of service and are discharged over the period of retirement and, where applicable, the period for which a spouse or eligible partner survives the pensioner. In valuing the Scheme liability, the Actuary must estimate the impact of several inherently uncertain variables into the future. The variables include not only the key financial assumptions noted in the table above, but also assumptions about the changes that will occur in the future in the mortality rate, the age of retirement and the age from which a pension becomes payable.

12.3 The value of the liability on the Statement of Financial Position may be significantly affected by even small changes in assumptions. For example, if at a subsequent valuation, it is considered appropriate to increase or decrease the assumed rate of inflation, or increases in salaries, the value of the pension liability will increase or decrease. The managers of the Scheme accept that, as a consequence, the valuation provided by the Actuary is inherently uncertain. The increase or decrease in future liability charged or credited for the year resulting from changes in assumptions is disclosed in notes 12.8 and 12.9. The notes also disclose 'experience' gains or losses for the year, showing the amounts charged or credited for the year because events have not coincided with assumptions made for the last valuation.

12.4 Sensitivity Analysis of Actuarial Assumptions

A sensitivity analysis for each significant actuarial assumption as at the end of the reporting period is detailed below.

The principal financial assumptions are the discount rate, general earnings increases and pension increases (currently based on CPI). A key demographic assumption is pensioner mortality.

As a result of the Scheme reform and the MOD's New Employment Model, there is significant uncertainty associated with timings of member exits (withdrawals and retirements) in future. Relatively few members of the AFPS remain in service until their normal pension age. However, a significant proportion retire with immediate benefits in the form of an Immediate Pension (IP) or Early Departure Payment (EDP), often from around age 40. The numbers of members reaching their IP or EDP qualification points could potentially have a significant impact on the Scheme liabilities and so we have included an indication of the approximate effect (on the total past service liability) of a 5% increase in the number of new entrants reaching IP/EDP point compared to the main liability calculations.

The table below shows indicative effects on the total liability as at 31 March 2015 of changes to these assumptions.

Change in assumption		Approximate effect on total liability	
Financial assumptions			
(i) discount rate*	+½% a year	-10%	-£14.9 billion
(ii) earnings increases*	+½% a year	+1%	+£1.4 billion
(iii) pension increases*	+½% a year	+9%	+£13.5 billion
Demographic assumptions			
(iv) additional one year increase to life expectancy at retirement*		+2%	+£3.5 billion
(vi) a 5% increase in the proportion of new entrants who reach IP/EDP point		+0%	+£0.4 billion

* Opposite changes in the assumptions will produce approximately equal and opposite changes in the liability.

12.5 Analysis of movements in the Scheme liability

	2014-15	2013-14
	£000	£000
Scheme liability as at 1 April	**(129,500,000)**	**(118,000,000)**
Current service cost (Note 5)	(2,662,588)	(2,454,782)
Past service cost (Note 5)	(30,000)	-
Pension financing cost (Note 8)	(5,597,036)	(4,803,003)
Enhancements (Note 6)	(805)	(703)
Pension transfers in (Note 4)	(831)	(935)
	(8,291,260)	(7,259,423)
Benefits payable (Note 12.6)	4,291,258	4,089,291
Pension payments to and on account of leavers (Note 12.7)	95,341	65,076
	4,386,599	4,154,367
Actuarial (loss) / gain (Note 12.8)	(20,995,339)	(8,394,944)
Scheme liability at 31 March	**(154,400,000)**	**(129,500,000)**

12.6 Analysis of benefits paid

	2014-15	2013-14
	£000	£000
Pensions to retired employees and dependants (net of recoveries or overpayments)	3,808,262	3,513,007
Commutations and lump sum benefits on retirement	482,996	576,284
Total benefits paid	**4,291,258**	**4,089,291**

12.7 Analysis of payments to and on account of leavers

	2014-15	2013-14
	£000	£000
Individual transfers to other Schemes	95,341	65,076
Total payments to and on account of leavers	**95,341**	**65,076**

12.8 Analysis of actuarial (loss) / gain

	2014-15	2013-14
	£000	£000
Experience (losses) / gains arising on Scheme liabilities	(7,795,339)	3,005,056
Changes in assumptions underlying the present value of Scheme liabilities	(13,200,000)	(11,400,000)
Total actuarial (loss) / gain	**(20,995,339)**	**(8,394,944)**

12.9 History of experience losses / (gains)

	2014-15	2013-14	2012-13	2011-12	2010-11
Experience losses / (gains) on Scheme liabilities: (£000)	7,795,339	(3,005,056)	42,737	746,322	(1,505,444)
Percentage of the present value of the Scheme liabilities	5.05%	(2.32%)	0.04%	0.71%	(1.50%)
Losses / (gains) arising due to changes in actuarial assumptions: (£000)	13,200,000	11,400,000	9,200,000	300,000	(9,000,000)
Percentage of the present value of the Scheme liabilities	8.55%	8.80%	7.80%	0.28%	(8.95%)
Total amount recognised in Combined Statement of Comprehensive Net Expenditure: (£000)	20,995,339	8,394,944	9,242,737	1,046,322	(10,505,444)
Percentage of the present value of the Scheme liabilities	13.60%	6.48%	7.83%	0.99%	(10.44%)
Total cumulative actuarial loss/(gain): (£000)	73,925,255	52,929,916	44,534,972	35,292,235	34,245,913

Statement of Financial Position – Armed Forces Compensation Scheme

13. Receivables

	2014-15	2013-14
	£000	£000
Amounts falling due within one year:		
Overpaid compensation	284	256
	284	**256**

14. Payables

	2014-15	2013-14
	£000	£000
Amounts falling due within one year:		
Compensation	2,270	2,526
	2,270	**2,526**

15. Provision for liabilities and charges

Armed Forces Compensation Scheme

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

The Scheme is required to provide for the injuries to military personnel that have occurred whilst in service. The provision reflects claims that have been made based on injuries that have occurred, including those incidents occurred but not yet claimed. Military personnel have up to 7 years to make a claim under the AFCS.

Assumptions underpinning the provision for AFCS liability

As for previous years, the actuarial assumptions used in assessing liabilities for GIPs are consistent with those used for resource accounting in respect of the AFPS.

Assumptions fall into two categories, financial and demographic. The main financial assumptions adopted as prescribed by HM Treasury are set out below.

% per annum	31 March 2015	31 March 2014
Gross discount rate	3.55%	4.35%
CPI inflation	2.20%	2.50%
GIP increases	2.20%	2.50%
Discount rate net of CPI	1.30%	1.80%
Discount rate net of GIP increases	1.30%	1.80%

The key demographic assumption is in respect of mortality. The mortality assumptions adopted follow a consistent approach to the AFPS mortality assumptions for resource accounting as at 31 March 2015. The levels of future mortality improvement have been assumed in accordance with the improvements incorporated in the published 2012-based principal population projections for the United Kingdom (prepared by Office of National Statistics).

The projections have been adjusted for Scheme-specific effects. Details of rank were not available, and for the purposes of determining the mortality assumption to be used it has been assumed that all the GIPs relate to other ranks rather than officers. Mortality for members and their spouses and children is assumed to be consistent with the relevant AFPS assumption for other ranks.

Where members have been awarded a GIP but have not yet been discharged the liability has been estimated on the assumption that they are discharged on the accounting date.

For incidents incurred but not yet claimed the GIP and Lump Sum liability is estimated using the assumption that the amount to be awarded will be consistent with historical awards and rejections based on a comparable level of injury being sustained.

	2014-15	2013-14
AFCS Provision	£000	£000
Balance at 1 April	**(1,250,752)**	**(1,081,190)**
Use of provision in year	72,870	90,644
Interest on Scheme Liabilities	(51,461)	(43,188)
Revaluation at year end	30,331	(98,359)
Actuarial loss	(203,611)	(118,659)
Balance at 31 March	**(1,402,623)**	**(1,250,752)**
Breakdown of Balance at 31 March:		
Incidents incurred but not yet claimed – Lump Sums and Guaranteed Income Payments	(162,823)	(196,852)
Guaranteed Income Payments – "In Payment"	(977,800)	(738,600)
Guaranteed Income Payments – "Underlying Entitlement"	(262,000)	(315,300)
	(1,402,623)	**(1,250,752)**

16. Financial Instruments

As the cash requirements of the Scheme are met through the Estimates process, financial instruments play a more limited role in creating and managing risk than would apply to a non-public sector Scheme of a similar size. There are no material financial instruments in relation to the Scheme.

17. Contingent Liabilities

The Scheme has the following unquantifiable liability in accordance with IAS 37:
There is ongoing legal action regarding compulsions of service relating to allegations of bullying under the AFCS. The outcome of this case cannot yet be predicted, however, if it goes against existing Scheme rules then this may lead to a change in policy, which may or may not be applied retrospectively. At present the potential number of cases that this would affect, and their financial value, is unknown.

18. Losses

During the year, losses arose in 2,722 cases (2013-14: 3,217 cases). The total loss was £226,501.34 (2013-14: £643,485.33). The losses all relate to the write-off of pension overpayments. None relate to fraud cases.

During the period of April 2005 to January 2012 differences occurred in the interpretation of the Scheme rules allowing aggregation of service between the AFPS 05 and AFPS 75 Schemes, resulting in some personnel receiving incorrect Early Departure Payments (EDP) and forecasts based on incorrect aggregation of periods of service. HM Treasury approval was obtained in 2014/15 to write-off the incorrect EDPs paid during this period, amounting to £1,352,695.84 in respect of 63 different members.

19. Related-party transactions

The Schemes fall within the ambit of the MOD, which is regarded as a related party. During the year, the Schemes received employers' contributions (SCAPE) and employees' contributions from MOD in respect of active members of the AFPS. These contributions totalled £1.86Bn (see Note 3). None of the managers of the Schemes, key managerial staff or other related parties has undertaken any material transactions with the Schemes during the year.

Certain key managerial staff and members of the Executive Committee are members of the Scheme. The benefits they are entitled to are not different to other members of the Scheme.

20. IFRSs in issue but not yet effective

There are no IFRSs that have been issued but are not yet effective that impact on the Armed Forces Pension Scheme or Armed Forces Compensation Scheme.

21. Adjusting events after the reporting period

21.1 As detailed in the Report of the Managers page 4, a new Armed Forces Pension Scheme was introduced on 1 April 2015 (AFPS 15). The reforms implemented in April 2015 may affect the behaviour of members, which has been reflected in the valuation completed by the GAD, see Report of the Actuary, page 13, paragraph 13.

21.2 From 1 April 2015 all pensions awarded to Armed Forces spouses and civil partners under AFPS 75 will be for life. Those already in receipt of a survivor's pension who have not remarried or formed a new relationship will be entitled to keep their pension for life with no loss of pension benefits if they later decide to re-marry, cohabit or form a civil partnership.

Those who have already surrendered their pension on remarriage, cohabitation or formed a civil partnership will be able to apply to have their pension restored for life if the new relationship ends.

Additionally those who had been refused restoration of their pension at the end of a second or subsequent relationship because of the 'betterment rule', as long as they remained eligible on 1 April 2015 and apply for restoration of their pension, it will be restored from that point forward without the test being applied.

This change will act to increase the future liabilities of the Scheme and has been calculated by GAD at £30M. This has been treated as a past service cost and has been recognised in the 2014-15 financial statements.

Date of authorisation for issue

The Accounts have been authorised for issue by the Accounting Officer on the same date as the C&AG's Audit Certificate.