LEONARDO
ELECTRONICS PENSION SCHEME

PENSIONS CONSULTATIVE COMMITTEE (PCC)
REPORT TO MEMBERS FOLLOWING THE MEETING ON 31 OCTOBER 2017

A meeting of the PCC took place in London on 31 October 2017.

The PCC has been set up to discuss, co-ordinate, advise and represent the views of the members of the Leonardo Electronics Pension Scheme. There are currently eleven representatives on the Committee and their contact details are attached to this Report.

The meeting was attended by:-

Tony Kingsbury	Capability Green	Chairman
Jim Cull	Edinburgh	
James Fordyce	Edinburgh	
Martin Johnson	Basildon	
Scott McMillan	Basildon	
Stephen Park	Edinburgh	
Phil Slade	Capability Green	
Ken Thompson	Pensioner Representative	
Scott Wallace	Edinburgh	
Paul Wilton	Southampton	
Colin Wylie	Edinburgh	
Andrew Letton	HR – Leonardo MW Ltd	
Lucy Astbury	HR – Leonardo MW Ltd	
Mike Nixon	Head of Pensions	
Rachael Skuse	Pensions Manager	
Helen Pass	Pensions Management Team	

The meeting was held to receive feedback from the Trustee meetings on 10 October 2017 and 17 October 2017.

Annual Report and Accounts

The 2017 Report & Accounts have been completed and signed (available at www.leonardoelectronicspensions.co.uk). The Auditors (RSM) gave unqualified opinions on the financial statements and statement on contributions.

Employer Covenant

Every six months, the Trustee's covenant adviser, Ernst & Young, provides a review of the financial strength of Leonardo MW Ltd and Leonardo SpA. At 30 June 2017, the financial position was assessed as remaining strong, taking into account the Scheme's funding position.

Quarterly Funding Update to 30 June 2017

The quarterly funding update showed that the Scheme had an estimated surplus of £169 million at 30 June 2017. The surplus had increased over the quarter, primarily due to higher than assumed returns on the Scheme assets (excluding the liability hedge).

The cost of new benefit accrual has reduced slightly between 31 March 2017 and 30 June 2017. However, the cost remains significantly higher than the contributions being paid to the Scheme. Whilst some surplus is allocated to support future service costs, the total cost of accrual is 19% p.a. ahead of the rate agreed at the 2014 valuation (which means that the cost of providing pensions is significantly higher than the cost set at the last valuation, and the surplus is being used at a faster rate than was anticipated).

This is an estimated funding position and the calculations are being updated as part of the 2017 valuation calculations, as a full member data update has been carried out.

Actuarial Valuation as at 5 April 2017

The three-yearly actuarial valuation of the Scheme is being carried out with an effective date of 5 April 2017. This process involves looking at the past service funding position of the Scheme (how the value of the Scheme's assets compare to the value of the Scheme's liabilities accrued up to 5 April 2017) and looking at the cost of earning future pension within the Scheme. The preliminary results from the valuation calculations have been presented to the Trustee by the Actuary and they have discussed the valuation assumptions and areas where changes may be appropriate.

The next steps are for the valuation results to be discussed between the Company and the Trustee and the final figures will not be known until the Trustee and Company have agreed the assumptions to be used.

Investment Performance

- The market value of the total assets of the Scheme at 30 June 2017 was £910 million.
- Investment performance of the return-seeking assets over the quarter had been 1% which was 0.2% ahead of the objective. In the longer term the assets were ahead of the return-seeking objective over 12 months, 3 years and 5 years.
- The total investment strategy (both the return-seeking and the matching assets) returned 1.3% ahead of the benchmark (which looks at the change in the Scheme's liabilities). The total fund return is now ahead of benchmark over 12 months and 5 years, and remains slightly behind over 3 years (due primarily to falls in interest rates, and underperformance of the investment fund in some previous quarters).

Allocation of Assets

At 31 March 2017 the Trustee held 71.6% of the Scheme's assets "on-risk" and 28.4% "off-risk". On-risk assets are those seeking to generate an investment return (e.g. equities, commodities, high yield bonds). Off-risk assets are those seeking to manage risk and match Scheme liabilities (e.g.: Government gilts, cash).

Strategic Business Plan

In line with best practice governance, the Trustee is developing a medium-long term strategic business plan. This will set a long term vision for the Scheme, particularly in relation to areas such as funding targets and risk management.

Administration

Scheme administrator

As communicated to members in the August 2017 InFocus newsletter, the administration of the pension Scheme will move from Aon Hewitt to PS Administration Limited (known as PSAL) with effect from 1 February 2018. Contact details for PSAL will be communicated to members in the near future.

In the meantime please continue to contact Aon Hewitt in the usual way.

If you are planning to retire in 2018 please do use the Aon Hewitt online modeller to obtain details of your pension benefits before the end of this year. Due to the work around the transfer to PSAL, the pension modelling tool will cease to be available during January 2018. A new PSAL online modeller will be under development during 2018, with a target for launch to members in late 2018.

Group Life Assurance policy

The Scheme's Group Life Assurance provider has been changed from Aviva to Zurich, who offered more competitive pricing and a good overall service rating.

Annual Benefit Statements

Annual Benefit Statements for active members of the Scheme will be issued in November 2017.

Holiday Pay – Overtime earnings adjustment

An error has been discovered in relation to a small number of members in the February 2017 Company payroll. During that month, the Company made a payment to some employees for holiday pay related to overtime earnings. This is a non-pensionable payment, however due to an error by the payroll provider, this was processed as pensionable for some members, in error. As this relates to a previous tax year, the Company does not propose to 'rectify' the error made in February 2017, but going forward this payment will be treated as non-pensionable for all members of the Scheme.

<u>£50,000 concession on voluntary savings as cash</u>

The PCC have raised the £50k concession on voluntary savings as cash with the Company. It was asked why the £50k maximum was in place and whether the Company would consider increasing it. The below is a summary of the background and the Company's position.

The concession allows members to take up to £50k of their voluntary savings as part of their Pension Commencement Lump Sum (PCLS - sometimes known as tax free cash) subject to the HMRC rule that a PCLS cannot exceed 25% of the total pension pot.

In general the tax rules allow members to take a PCLS of 25% of their defined benefit pot, and 25% of their voluntary savings pot. The remaining 75% of the voluntary savings pot would then need to be used to purchase an annuity (a pension income through an insurance company), or take all or part of the funds as an UFPLS (sometimes known as a taxed cash lump sum).

In the past, many members did not wish to use their remaining voluntary savings pot to purchase an annuity (due to perceived poor annuity rates). Therefore, as a concession, the Company and the Trustee changed the Rules of the Scheme to allow Voluntary Savings of up to £50k to be used towards the overall PCLS.

However, through the concession members are also able to retain a higher level of defined benefit pension (as less cash is taken out of the core Scheme benefits) and this has a financial impact on the Scheme:

- The valuation basis assumes that members will take PCLS from their Core Scheme benefits (which reduces the amount of defined benefit pension the member receives from the Scheme). Accordingly a proportion of the surplus is used up if members instead fund their PCLS from their voluntary savings (and therefore remain entitled to receive a higher unreduced level of defined benefit pension from the Scheme); and

- Risk is retained in the Scheme for the higher pension in relation to investment return and longevity risk (how long the pension is payable for in retirement).

There are also now a wider range of flexible retirement options available for the remaining voluntary savings, rather than only having the ability to purchase an annuity with an insurance company.

For these reasons the Company would not wish to increase the level of the £50,000 concession.

PCC representatives

Ken Thompson (Pensioner Representative) has tendered his resignation from the PCC. We thank Ken for the support he has provided in his PCC role. The PCC have elected to appoint Martin Johnson as the Pensioner Representative on the PCC, as Martin has recently retired from the business. Martin will also continue in his role as a Trustee of the Scheme.

There is a vacancy for an active member PCC representative in Basildon and a selection process will be undertaken shortly.

Joint DC investment committee meeting

A joint DC investment committee meeting of the Leonardo UK pension schemes was held on 19 September 2017. The Leonardo Electronics Pension Scheme benefits which are invested in the common DC strategy are the Additional Voluntary Contributions and the 100+ Retirement Accounts.

Investment performance

The majority of the P-Solve 'blend funds' (which make up the default fund in the DC investment strategy) had out-performed their long term targets since the inception of the funds.

Administration

The pension administration of the FuturePlanner pension arrangement will move from Aon Hewitt to PSAL on 1 December 2017.

Date of the Next Meeting

The next meeting of the PCC is scheduled for 16 January 2018.

Contact Details

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