IN FOCUS

SELEX Pension Scheme

A newsletter for members of the SELEX Pension Scheme

Issue 9. September 2009

In this issue

In this issue of IN FOCUS we provide you with:

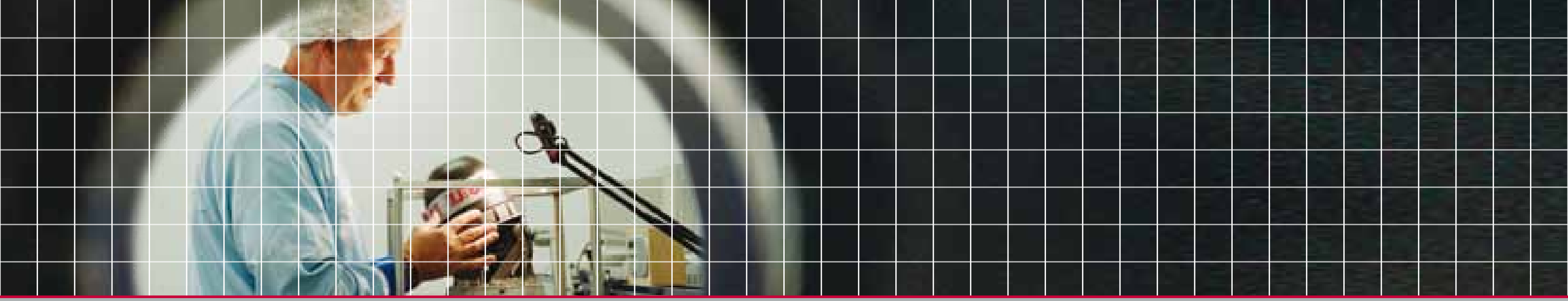
- Key dates for the new voluntary savings options;
- A summary of the changes which have been made to the Scheme limits following the completion of the actuarial valuation;
- Details of the new process for purchasing pension from your Additional Voluntary Contributions, Selected Benefits Scheme account and Retirement Account;
- A summary of the Trustee Report and Accounts for 2008/09;
- A summary funding statement providing information about the Scheme's funding position.

News

Actuarial Valuation

The Trustee and Company have finalised the actuarial valuation, including the benefit and contribution changes associated with it. Members currently participating in the Scheme will have received Valuation Bulletin 4 from the Company setting out the agreed changes. The relevant documentation, including the recovery plan which sets out how the funding shortfall is to be met, was submitted to the Pensions Regulator in July 2009 and the Regulator has accepted the plan.

This newsletter sets out further details on the dates for the changes to the voluntary savings options and the changes which have been made to Scheme limits. We also provide information on the new process for purchasing pension from your Additional Voluntary Contributions (AVCs), Selected Benefits Scheme (SBS) account (2000 Section only) and Retirement Account (100+ Section only).



Changes to voluntary savings

Key dates

In order to give members time to decide how they wish to make voluntary savings in the future, the changes to the voluntary savings options are being phased in from 1 September 2009 and then from 1 December 2009 as set out below.

Changes implemented from 1 September 2009:

- The limit on AVC contributions (including core benefit contributions) increased to 100% of earnings.
- The limit on SBS death in service contributions (including core benefit contributions and other voluntary contributions) increased to 100% of earnings.
- The limit on SBS retirement benefit contributions (including core benefit contributions) remains at 15% of earnings, subject to the Earnings Cap.
- Members can take the whole of their AVC and SBS voluntary savings as tax free cash, up to a maximum of £50,000. This is subject to the overall HM Revenue & Customs (HMRC) limit of 25% of the value of all your SELEX pension benefits. If you have a voluntary savings fund in excess of £200,000, then you are able to take 25% of that larger sum as tax free cash.
- 100+ Section members can take the whole of their Retirement Account as tax free cash, subject to the overall 25% HMRC limit.
- It is no longer possible to use voluntary savings or your Retirement Account to purchase pension within the main fund. Please see the article on page 3 regarding the new process.
- Voluntary savings ceased to be included in the calculation of the 2/3rds maximum pension Scheme limit. Please see article on page 3 regarding the changes to Scheme limits.

Changes to be implemented from 1 December 2009:

- The payment of ABCs into the 100+ Retirement Account will cease. Members paying ABCs are being contacted in advance and given the opportunity to switch future contributions into AVC payments.
- No new contributors will be accepted into SBS for retirement benefits. Members of the 2000 Section are being contacted in advance and given one last opportunity to join SBS for the purposes of retirement benefits. Members must be contributing a regular monthly SBS retirement benefit contribution in order to be classed as an existing contributor for the purposes of retirement benefits. One-off lump sum contributions or contributions to SBS for death in service cover will not count as regular monthly SBS retirement benefit contributions.
- 2000 Section members who wish to make voluntary contributions will need to choose between contributing to AVCs and contributing to SBS for retirement benefits. Members of the 2000 Section currently contributing to both SBS and AVCs will be contacted in advance in order to choose between the two retirement savings options. Members will be able to continue making SBS death in service contributions even if they switch their retirement savings from SBS to AVCs.

The Scheme booklets and voluntary savings guides are being updated and will be available on the Scheme website shortly.

Voluntary savings in the Scheme

Additional Voluntary Contributions (AVCs) – **all Sections**
Selected Benefits Scheme (SBS) – **2000 Section only**
Additional Basic Contributions (ABCs) – **100+ Section only**

Scheme limits on benefits

The rules of the Scheme have always contained limits on the amount of pension you may take from the Scheme due to historic tax regulations. Broadly, these limits allow you to take a pension of up to two-thirds of your final salary.

Up until September 2009, benefits payable to you by the Scheme and by BAE Systems, including benefits bought with voluntary contributions (AVCs, SBS and ABCs) to the Scheme and to BAE Systems were all included within the two-thirds limits. This included all transfers-in to a BAE Systems pensions arrangement.

As a result of the changes which were made to the SELEX Pension Scheme following the actuarial valuation, there has been a relaxation of a number of these limits which will reduce the likelihood of members reaching them.

With effect from 1 September 2009, benefits resulting from the following payments will no longer be taken into account by the SELEX Pension Scheme when applying the limits calculation:

- SBS contributions to either SELEX or BAE Systems;
- AVC contributions to either SELEX or BAE Systems;
- Retirement Accounts with either SELEX or BAE Systems;
- Transfers-in to a BAE Systems pension arrangement which are fixed pension amounts which SELEX has no liability to "top up" via an earnings link.

Any other transfers-in to a BAE Systems pension arrangement, for example transfers-in which were used to purchase a service credit which the SELEX Scheme may have a liability to "top-up" through the continuing earnings link, will be included in the Scheme limits calculation.

Annuity purchase

With effect from 1 September 2009, it is no longer possible to use SBS accounts, AVCs or Retirement Accounts ("Voluntary Savings") to purchase additional pension within the main fund. It is not anticipated that this will be a change for the vast majority of our membership as a significant proportion currently take their Voluntary Savings as tax free cash.

A new process has been adopted with Standard Life to provide retirement quotes to members who do wish to take their Voluntary Savings as a pension income (an annuity). If you select this option, when you come to retirement your final figures will be calculated by Standard Life and the proceeds of your Voluntary Savings will be used to set up your annuities.

You are under no obligation to accept the quotation provided by Standard Life and are able to take your Voluntary Savings fund to another insurance provider of your choice to purchase a pension (known as the open market option). If you wish to speak to an independent financial adviser (IFA) about your options for purchasing a pension on the open market, Aon can provide you with details of their independent annuity advice service. Please note that there will be commission payable should you select this option which will be reflected in any annuity quotation provided. Alternatively, contact details for IFAs in your area can be found at www.unbiased.co.uk or through the IFA consumer helpdesk on 0800 085 3250.

Report and Accounts

Each year the Trustee is required to publish a report and audited accounts for the Scheme. The summary below is based on the accounts for the year to 5 April 2009. The audit work has been completed by our independent auditors Ernst & Young LLP. The Trustee is due to sign the accounts shortly and the figures are not expected to change in any material respect before signature.

If you would like to see a copy of the full annual Report and Accounts, a copy will be placed on the Scheme's website, www.selexpensions.co.uk

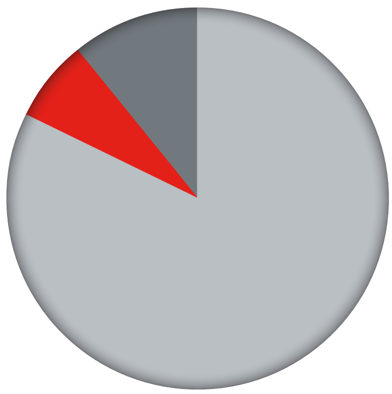
Scheme assets

The assets of the Scheme have grown since the inception of the Scheme to £162 million. Further information is set out below:

	Assets of the Scheme at 5 April 2008	£111m
+	**Income** (Company contributions, member contributions and other income)	£38m
-	**Outgoings** (Pensions, lump sums, death in service insurance and administration expenses)	£3m
+	**Net return on investments** (Market value of investments after allowing for expenses) made up of: • An increase in the derivatives value, including swaps, of £28 million; • A decrease in other asset values, including TIGS, DC funds and investment expenses of -£14 million; and • Investment income of £2 million	£16m
=	**Assets of the Scheme at 5 April 2009**	**£162m**

Membership numbers

The majority of our members are current employees who are paying contributions and building up benefits. This chart shows that out of a total of 4,883 members, 82% are employed (active) members.



Membership as at 5 April 2009

- Employed (active) members 4,022
- Pensioners 343
- Deferred Pensioners 518

Investing the assets of the Scheme

The Trustee has continued to work with the Scheme's investment manager, PSigma Investments Limited, to develop and refine the Scheme's investment strategy. The year to 5 April 2009 was an extremely difficult time for investors. There have been significant falls in asset values and extreme volatility across many markets.

Our overall investment strategy enabled us to generate positive returns during the Scheme Year. Our swaps portfolio has provided protection for the Scheme during this period, preventing further losses and producing a significant mark to market valuation increase over the period.

As a result of the difficult market conditions, the TIGS investments underperformed our objectives over the year and there has been a fall in the value of our TIGS investment portfolio. The Trustee monitors the performance of our investment managers regularly and we receive detailed investment reports which show how each of our investments has performed and whether our managers have met our benchmarks.

The Trustee's investment strategy is set out in the Statement of Investment Principles, a copy of which is available on request from the Pension Administrator, Aon.

Swaps arrangements

In order to protect the Scheme against changes in long term interest rates and inflation, the Trustee entered into a portfolio of swap contracts. Swap contracts are agreements between the Trustee and the bank under which the Trustee will either pay or receive money depending on the movements in inflation and long term interest rates. The Trustee regularly considers whether the swaps need refining in order to ensure the Scheme's liabilities remain suitably matched. There has been a lot of activity in relation to the Scheme's swap portfolio during the year. The swaps were refined in June 2008, October 2008, January 2009, February 2009 and March 2009. These refinements were made in order to allow for new pension accrual, to take account of the low interest rates and to release funds from the swaps which were partly re-invested in a new equity derivative product within TIGS.

By entering into the swap contracts, the Trustee has ensured that:

- when inflation rises and the deficit of the Scheme increases, the value of the Scheme's assets will also increase; and
- when long term interest rates fall and the deficit of the Scheme increases, the value of the Scheme's assets will also increase.

Linking our assets to our liabilities has enabled us to be more certain about the size of our deficit. The swap contracts increased in value by £32 million over the Scheme Year. As mentioned above, cash was released from the swaps during the year and reinvested in other products. These gains will broadly offset an increase in the value of the Scheme's liabilities due to the net effect of increases in inflation expectations and changes in long term interest rates.

TIGS performance

The majority of the assets of the Scheme continue to be invested in the Total Investment Governance Solution (TIGS) provided by PSigma Investments Limited. TIGS is a managed service designed to deliver performance in excess of a client specific target through exposure to diversified investment arrangements. PSigma Investments Limited invests and manages the Scheme's assets on the Trustee Directors' behalf.

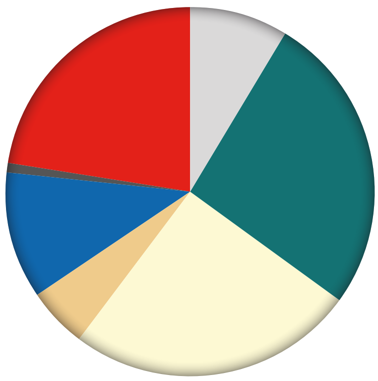
The service reduces the risks and costs of decision delay and provides access to a broad range of asset allocation and increased investment specialisation, such as commodities, high yield bonds, leveraged loans and other alternative asset classes as well as currency hedging. As well as the delegated responsibility for dynamic asset allocation, PSigma Investments Limited are also responsible for selecting and replacing fund managers.

The investment objective for TIGS is a return of LIBOR + 3% per annum, after the deduction of fees, over rolling three year periods. Over the year, TIGS has returned -13.52% against an objective of 7.66%. Since inception the TIGS fund has returned -1.45% against an objective of 8.37% per annum.

The TIGS investment has therefore fallen short of the Trustee's targets. The underperformance of the TIGS fund should be considered in the context of the investment environment. Although the Scheme underperformed its objective, it outperformed all major asset classes with the exception of UK gilts and global bonds.

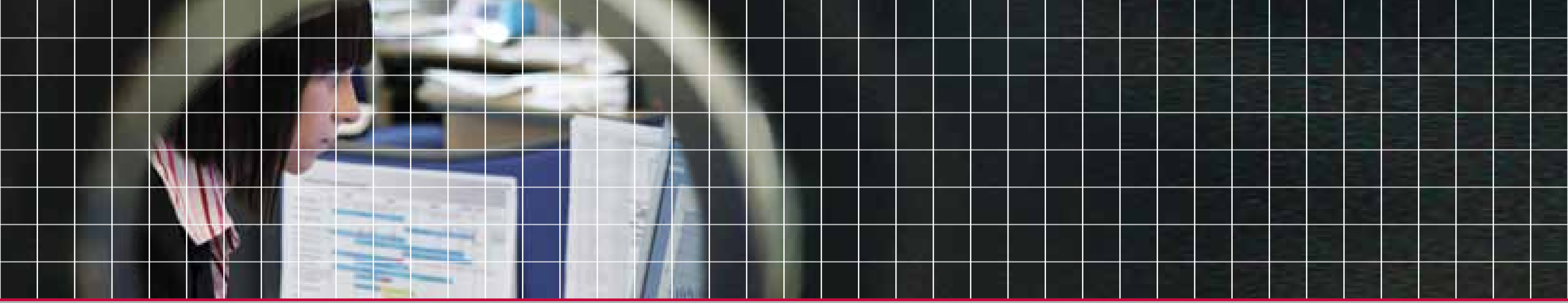
TIGS investment portfolio

The allocation of assets varies each month but our assets in TIGS were invested as follows as at 5 April 2009:



TIGS Assets as at April 2009

- UK equities 8.8%
- Overseas equities 26.2%
- Alternative asset classes (including hedge fund of funds) 25.5%
- Property 5.2%
- Cash 11.2%
- Currency hedge 0.8%
- Global bonds 22.3%



Summary Funding Statement

The Pensions Act 2004 introduced a requirement that the Trustee informs you on an annual basis about the funding of the Scheme. Set out below are details of the Scheme's funding position as at 5 April 2008 (the date of the most recent formal funding valuation of the Scheme). In addition, we have included information confirming the approximate funding position of the Scheme, based on an interim funding update as at 5 April 2009.

When the valuation was carried out on 5 April 2008, the Actuary valued the Scheme on two different bases:

- **Ongoing basis**
  This is the amount of money needed to pay pensions as they fall due. The Actuary valued the Scheme as underfunded by £54.3 million on an ongoing basis. The assets were £109.3 million at 5 April 2008 and the Scheme had liabilities of £163.6 million.

Underfunded

- **Buy out/discontinuance basis**
  This is the amount of money needed to buy an insurance policy to pay your benefits. This would only be relevant if it was decided to wind up the Scheme. The Actuary valued the Scheme as 93% funded on a buy out basis, which is equivalent to a £7.8 million increase in the deficit since the last formal solvency valuation.

Underfunded

Where has this deficit come from?

The deficit at 5th April 2008 has increased compared with previous results due to a number of factors. Firstly, the returns on the Scheme's assets have been lower than expected. In addition, the Trustee has updated the assumptions used to value the liabilities and in particular has updated the assumption used for longevity. This reflects the fact that the length of time members are expected to live for is still increasing. This has increased the value placed on the liabilities.

What is the Trustee doing to eliminate the deficit?

As a result of the 5 April 2008 valuation, the Trustee and the Company agreed that the participating employers will pay additional contributions each year (in addition to the cost of funding future benefits) to eliminate the shortfall over a ten year period starting from 1 July 2009. The additional contributions will be paid quarterly in advance starting at £6.71 million in the first year and increasing each year up to £10.33 million in the final year.

What would be the funding position of the Scheme at the current date?

The Scheme Actuary provides the Trustee with regular updates of the funding position of the Scheme. The approximate update as at 5 April 2009 showed that the ongoing Scheme deficit was around £76.5 million. This increase in the deficit occurred largely because the Scheme's investments in TIGS have underperformed relative to the benchmark over the year.

The next detailed calculation of the Scheme's funding position will occur as part of the formal actuarial valuation as at 5 April 2011. The Trustee is monitoring the funding of the Scheme on a quarterly basis and will take action at an earlier date if necessary.

We anticipate that you will have questions about the funding of the Scheme. We hope the following information will answer your questions.

How is my pension funded?
Active members and the participating employers pay contributions to the Scheme based upon members' pensionable salaries. The Scheme holds the money in a common fund from which it pays members' pensions when they retire.

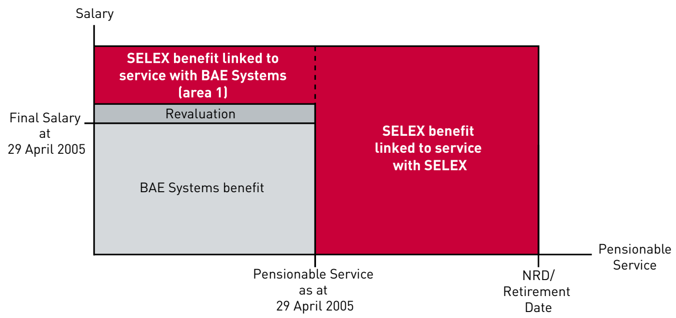
If you pay voluntary contributions to the Selected Benefits Scheme then these contributions are also held in this common fund. Other AVCs and your Retirement Account (100+ Section) are held separately with Standard Life.

How is the amount of money the Scheme needs worked out?
The Trustee obtains regular valuations of the benefits earned by members. Using this information and recommendations from the Scheme Actuary, the Trustee and the Company must agree on the future contributions that must be paid to ensure there is sufficient money in the Scheme to pay the benefits.

Which funding basis is used?
The ongoing funding basis is used to assess the amount needed to ensure the Scheme is adequately funded and to determine how much needs to be paid into the Scheme by participating employers and members. It assumes that SELEX will continue in business and support the Scheme.

The buy out basis is not used as it assumes that benefits will be secured by buying insurance policies. Insurers need to make a profit and therefore charge more to insure pensions than it costs the Scheme to provide benefits. This basis would be relevant if the Scheme wound up and the benefits needed to be insured.

How are my SELEX benefits linked with my BAE Systems benefits?
Members who joined the Scheme on 29 April 2005 have SELEX benefits which are linked to their BAE Systems benefits. The following diagram shows how these benefits are structured:



The SELEX Pension Scheme will pay the benefits shaded red. The BAE Systems pension schemes will pay the benefits shaded grey.

You will see that the SELEX Pension Scheme will pay some benefits which are linked to your service in the BAE Systems scheme (marked as area 1 on the diagram). The amount of area 1 will depend on how much pensionable salaries of SELEX employees grow compared to inflation.

This link between BAE Systems and SELEX accounts for some of the underfunding that currently exists on the funding basis.

What would happen if the Scheme started to wind up?

We are legally required to tell you what would happen if the Scheme were to wind up. This does not mean that there is any intention to wind up the Scheme in the foreseeable future.

If the Scheme was to start to wind up, SELEX is required to pay enough into the Scheme to enable the members' benefits to be insured with an insurance company. If SELEX is not able to pay the deficit (if any), the Pension Protection Fund (PPF) might be able to take over the Scheme and pay some compensation to members.

The PPF's main function is to provide compensation to members of eligible defined benefit (final salary) pension schemes, when there is a qualifying insolvency event in relation to the employer, and where there are insufficient assets in the pension scheme to cover the Pension Protection Fund level of compensation.

Other information

The law requires the Trustee to inform you that no payments have been made from the Scheme to any participating employers in the last 12 months.

If you are thinking of leaving the Scheme for any reason, you should consult a professional adviser, such as an independent financial adviser, before taking any action.

If you require any further information about the Scheme then please contact the Pension Administrator, Aon, using the details below.

Remember, if you move house, please keep the Pension Administrator informed so you can continue to receive up to date information.

Pensions quiz answers

Set out below are the answers to the pensions quiz featured in the last edition of IN FOCUS.

1. How often does the Scheme Actuary undertake an actuarial valuation to assess the Scheme's assets and liabilities? **(B) Every 3 years**

2. As part of the valuation, the Scheme Actuary must make an assumption regarding the life expectancy of the membership. What is the life expectancy assumption (i.e. how many years a person will live for after age 65) used for a male member aged 65? **(A) 21 years**

3. The valuation requires various assumptions to be set in order to anticipate how much money needs to be paid into the Scheme to meet all the benefits. Who sets the assumptions? **(C) The Trustee and the Company by agreement**

4. How many members (active, deferred and pensioner) were there in the Scheme at the date of the valuation (5 April 2008)? **(A) 4,777**

5. What is the average time it takes to become a qualified Actuary? **(B) 6 years**

6. How many years' experience of advising pension schemes does our current Scheme Actuary, Danny Vassiliades, now have? **(C) 19 years**

Contact details

Telephone: 0117 945 3544
Email: selex.pensions@aonconsulting.co.uk
Pensions Website: www.selexpensions.co.uk

Address: SELEX Pension Scheme, Aon Consulting Limited, 25 Marsh Street, Bristol BS1 4AQ

Disclaimer

The content of this newsletter is given for the purpose of providing you with information about the Scheme only and has no legal effect. The rules of the Scheme govern how the Trustee must act and if the rules of the Scheme are inconsistent with the information given in this newsletter, the rules will prevail. Copies of the rules are available from the Pension Administrator, Aon.