

New Airways Pension Scheme

**Report on the actuarial
valuation as at 31 March 2009**

30 June 2010

TOWERS WATSON 

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Throughout this document:

- "Scheme" refers to the New Airways Pension Scheme
- "Trustees" refers to the Management Trustees of the New Airways Pension Scheme
- "Company" refers to the Principal Employer, British Airways Plc, and other participating companies.

Further definitions and terms in italics are explained in the glossary (Appendix F).

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Section 1: Summary of main conclusions

Introduction

- 1.1 This is my report on the *actuarial valuation* of the New Airways Pension Scheme as at 31 March 2009. The report is addressed to the Trustees, who should forward a copy to the Company.
- 1.2 The main purposes of the *actuarial valuation* are to review the financial position of the Scheme relative to its *statutory and subsidiary funding objectives*, as required under Clause 13 of the Consolidated Trust Deed and Part 3 of the Pensions Act 2004, to determine the appropriate level of future contributions, and to examine the extent to which the Scheme's resources would have been adequate to secure accrued benefits if it had discontinued at the valuation date.
- 1.3 This report has been prepared in accordance with the guidance note GN9 version 8.1 "Funding Defined Benefits – Presentation of Actuarial Advice" adopted by the Board for Actuarial Standards and current at the date of signing.
- 1.4 This report also complies with the "Technical Actuarial Standard R: Reporting Actuarial Information", published by the Board for Actuarial Standards and effective from 1 April 2010. I make this statement on the basis that no decisions are intended to be made on the basis of this report or the enclosed certification of the *technical provisions* (as distinct from the advice and other information provided by me earlier in the valuation process). As such, most of the requirements of this standard are not relevant.
- 1.5 This valuation is based on the *Statement of Funding Principles* agreed by the Trustees and Company dated 30 June 2010. The principal conclusions of the valuation are summarised below.

Ongoing funding position

- 1.6 Past service:

On the assumptions adopted by the Trustees and agreed with the Company, the Scheme had a shortfall relative to its *statutory funding objective* of £2,682 million at the valuation date. This means that the assets of £6,096 million covered 69% of the Scheme's *technical provisions*.

- 1.7 Post valuation events:

A range of approximate updates of the Scheme's funding position to reflect changes since the valuation date was considered. These showed that on a consistent approach the funding position was estimated to have improved at most dates, but for the purposes of setting the recovery plan the Trustees determined to base this on a broadly unchanged funding shortfall as at 31 March 2010.

- 1.8 Recovery plan:

The Company and the Trustees have agreed that the Company will pay additional contributions as set out below to eliminate the shortfall at the valuation date:

- £11,506,250 per month from April 2009 to June 2010 inclusive;
- £13,481,250 during July 2010;
- £12,000,000 per month from August 2010 to March 2011 inclusive;
- in each of the next 15 years from April 2011 the amounts set out in the following table as twelve equal monthly payments:

Year ending 31 March	Deficit contributions (£m)														
	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026
	164	177	191	205	221	238	257	277	298	321	346	355	364	373	383

In addition, the Trustees and the Company have agreed a package of additional security and other measures aimed at improving the funding position and members' benefit security over time, which are documented in a separate legal agreement.

If the assumptions set out in the *Statement of Funding Principles* and *recovery plan* are borne out in practice, the shortfall will be removed within 17 years of the valuation date.

1.9 Future service:

The Company is in the course of implementing various changes to the Scheme's benefits, further details of which are set out in Appendix A of this report. On the assumption that these changes are implemented with effect from 1 October 2010, the Trustees and the Company have agreed that participating employers will contribute at the following rates:

	Percentage of Pay for Contribution Purposes			
	1 July 2010 – 30 September 2010		From 1 October 2010	
	Plan 60	Plan 65	Plan 60	Plan 65
General Staff	19.1%	18.1%	16.5%	15.3%
Air Cabin Crew	21.7%	20.7%	15.0%	14.7%
Pilots and Officers	25.9%	23.9%	19.7%	18.6%

Assuming member contributions are increased by 1.5% of pensionable pay from 1 October 2011, future employer contributions will reduce by a corresponding percentage from that date.

In addition to the rates outlined above, the employers will contribute an amount equal to the normal contributions that would otherwise be payable by those members who participate in the Scheme's salary sacrifice arrangement.

1.10 Expenses:

Administrative and other non-investment expenses (except *Pension Protection Fund* levies) are met from the Scheme's assets and an allowance of 0.8% pensionable pay has been included in the employer future service contribution rates above to cover these costs. *Pension Protection Fund* levies are payable by the Company.

1.11 The Pensions Act 2004 requires the Trustees and the Company to agree a revised *schedule of contributions* following my signing this report. The Trustees will also need to submit a *recovery plan* to the *Pensions Regulator*.

Discontinuance position

- 1.12 If the Scheme had been discontinued and wound up at the valuation date, there would not have been sufficient assets to secure the accrued benefits through the purchase of annuity policies with an insurer. My estimate of the solvency of the Scheme at the valuation date is 46%, before taking any account of the benefit of the additional security available to the Trustees. The approach I have followed in making this estimate is set out in Section 4 of this report.

Reporting to members

- 1.13 The Trustees are required to disclose to members, in a *summary funding statement*, certain outcomes of this *actuarial valuation* within a reasonable period.

Next actuarial valuation

- 1.14 The financial position of the Scheme and the level of Company contributions to be paid will be reviewed at the next *actuarial valuation*, which is expected to be carried out as at 31 March 2012. However, in the intervening years the Trustees will obtain annual *actuarial reports* on developments affecting the Scheme's assets and *technical provisions*. Following this valuation, an *actuarial report* as at 31 March 2010 will need to be provided by 31 March 2011.

James C Wintle
Fellow of the Institute of Actuaries

30 June 2010

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The limitations of the investigation

Third parties

I have written this report for the Trustees and the Company, as required under Clause 13 of the Consolidated Trust Deed dated 1 April 2008. I have prepared it to satisfy both the requirements of the Deed and the statutory requirements of section 224 of the Pensions Act 2004. It has not been prepared for any other purpose. As such, it should not be used or relied upon by any other person for any other purpose, including, without limitation, by individual members of the Scheme for individual investment or other financial decisions, and those persons should take their own professional advice on such investment or financial decisions. Neither I nor Towers Watson Limited accepts any responsibility for any consequences arising from a third party relying on this report.

Except with the prior written consent of Towers Watson Limited, the recipient may not reproduce, distribute or communicate (in whole or in part) this report to any other person other than to meet any statutory requirements.

Data supplied

The Trustees bear the primary responsibility for the accuracy of the information provided, but will, in turn, have relied on others for the maintenance of accurate data, including the Company who must provide and update certain membership information. Even so, it is the Trustees' responsibility to ensure the adequacy of these arrangements. I have taken reasonable steps to satisfy myself that the data provided is of adequate quality for the purposes of the investigation, including carrying out basic tests to detect obvious inconsistencies. These checks have given me no reason to doubt the correctness of the information supplied. It is not possible, however, for me to confirm that the detailed information provided, including that in respect of individual members and the asset details, is correct.

This report has been based on data available to me as at the effective date of the *actuarial valuation* and takes no account of developments after that date except where explicitly stated otherwise.

Assumptions

The choice of assumptions, as set out in the Scheme's *Statement of Funding Principles* dated 30 June 2010, is the responsibility of the Trustees, in agreement with the Company, after taking my advice. They are only assumptions; they are not predictions and there is no guarantee that they will be borne out in practice. In fact I would expect the Scheme's experience from time to time to be better or worse than that assumed. The Trustees and the Company must be aware that there are uncertainties and risks involved in any course of action they choose based on results derived from these assumptions.

The structure of the asset model, used to determine the spread of likely future outcomes for the Scheme's finances, is based on an analysis of historical investment returns, although subjective judgement was incorporated to complement the information provided by historical returns. The model is designed to illustrate the future range of returns stemming from different asset classes and their inter-relationship and the consequent uncertainty in the future financial development of the Scheme. It should be noted that no economic model could be expected to capture future uncertainty perfectly or to be precise about the risk of extreme events. In particular, it should be noted that the timeframe in establishing the asset model and the assumptions used in this investigation are intentionally long term, and are not meant to be reflective of the possible, or even likely, course of the investment markets in the short term.

Section 2: Background to the valuation

Purposes of the valuation

2.1 The main purposes of the *actuarial valuation* are to:

- review the financial position of the Scheme relative to its *statutory and subsidiary funding objectives* as required under Clause 13 of the Consolidated Trust Deed and Rules and by section 224 of the Pensions Act 2004, and to determine the level of future Company contributions required; and
- examine the extent to which the Scheme's resources would have been adequate to secure accrued benefits if it had discontinued at the valuation date.

Previous valuation and the contributions paid since then

2.2 The previous *actuarial valuation* of the Scheme was carried out by Greg Alexander as at 31 March 2006. The main results were:

- a past service shortfall on an ongoing basis of £1,723 million which meant that the Scheme's assets of £5,846 million were expected to cover 77.2% of the benefits earned for service to 31 March 2006 (after allowing for the cap on future pensionable earnings increases);
- the Trustees and the Company agreed that the Company would pay the following additional contributions over the period from 1 April 2006 to 31 March 2016 to eliminate the shortfall as at 31 March 2006:
 - £240 million on 9 February 2007,
 - £560 million by 2 April 2007, and
 - £10.547 million per month from 1 April 2007 for nine years, increasing each April in line with Pension Increase (Review) Orders.
- The Company also agreed a series of "cash sweeps" whereby it would pay further sums of up to £50 million in each of the financial years ending 31 March 2007, 2008 and 2009. These sums would be paid if the Free Cash reported in BA's consolidated preliminary results exceeded specified levels (Free Cash was defined as cash and cash equivalents and other current interest bearing deposits as reported in BA's consolidated financial statements, excluding any cash or deposits which were, or were to be, hypothecated or pledged or otherwise subject to a security charge or lien).
- In addition, the Company arranged a guarantee of £150 million to be paid to the Scheme, in full or in part, in certain circumstances including BA's insolvency. The guarantee had an expiry date of 31 March 2010 but included provisions for renewal depending on the financial position of the Scheme as at 31 March 2009. The amount of the guarantee would reduce by any amounts paid under the cash sweep agreement.
- The Trustees and the Company also agreed that participating employers would pay contributions at the following rates to cover the cost of benefit accrual from 1 April 2006. These rates allowed for changes to benefits and member contributions from 1 April 2007:

	Employer future service contributions		
	From 1 April 2006 to 31 March 2007	From 1 April 2007	
	(multiples of member contributions)	Plan 60 (% pay)	Plan 65 (% pay)
General Staff	5.2 x	19.1%	18.1%
Air Cabin Crew	5.8 x	21.7%	20.7%
Pilots and Officers	7.0 x	25.9%	23.9%

- It was agreed that administrative and non-investment expenses would be met by including a multiple of 0.1 in the contribution multiples above (up to 31 March 2007) and an allowance of 0.8% pay in the rates payable from 1 April 2007. The Company agreed to pay any levies required by the *Pension Protection Fund*.

2.3 Employer contributions have been paid at the rates outlined above since 1 April 2006. Under the cash sweep arrangement a payment of £50 million was made in the year ending 31 March 2008 and the £150 million guarantee was consequently reduced to £100 million. This guarantee has now been relinquished. The employers have also paid amounts equal to the normal contributions that would otherwise have been payable by those members who participate in the Scheme's salary sacrifice arrangement.

Legislative changes and other material developments

2.4 Since 31 March 2006, there have been a number of legislative changes introduced by the Finance Act 2004 and Pensions Act 2008. Details of these changes are provided in Appendix C. The majority of these changes will either have already been allowed for at the last valuation or have had no impact on the valuation calculations.

Scheme benefits valued

2.5 I have valued the Scheme's benefits as set out in the Consolidated Trust Deed and Rules dated 1 April 2008. A summary of the main benefits applying to employed members is shown in Appendix A. These reflect changes that were made with effect from 1 April 2007. The treatment of discretionary benefits, including discretionary increases in benefit, is described in the *Statement of Funding Principles* dated 30 June 2010 which is reproduced in Appendix D. There have been no discretionary increases to pensions granted in the last five years.

2.6 The Company is in the process of making various changes to future benefit accrual. These changes are summarised in Appendix A and the employers' contribution rates for funding future service have been assessed taking these changes into account. The changes do not affect the benefits valued in order to determine the funding position at 31 March 2009.

2.7 There is still legislative uncertainty about whether the Scheme will need to adjust benefits to counter the effect of unequal GMPs. In this valuation no allowance has been made for the cost implications of such a requirement.

2.8 There are some pensions payable to former members of Dan Air and Davies & Newman which are provided by external insurance contracts. Assets and liabilities in respect of these contracts have been excluded from the technical provisions, subsidiary funding objective, and solvency results shown in this report.

Membership data

- 2.9 In order to carry out the present valuation, I have obtained detailed information regarding the membership of the Scheme from the administrators. A summary of the data supplied is shown in Appendix B. In addition, I have made allowance in the calculation of the *technical provisions* for the effects of a restructuring exercise which took place after the valuation date.
- 2.10 I have taken reasonable steps to satisfy myself that the data provided is of adequate quality for the purpose of the valuation. There was some detailed data which was not complete and so I have made appropriate assumptions but this will not have had a material impact on the valuation.

Pension increases

- 2.11 In the intervaluation period most elements of pension have continued to be increased, either in payment or in deferment, in accordance with the Pension Increase (Review) Orders subject to a maximum of 5% in any one year. The actual rates of increase were as follows:

Date of increase	Increase
9 April 2007	3.6%
7 April 2008	3.9%
6 April 2009	5.0%

This valuation also took into account the 0% increase that was due for April 2010.

- 2.12 In all cases pensions have been increased in accordance with the relevant rules including those pensions in payment as if under the Rules of British Caledonian and Dan Air Schemes which are paid by the Scheme.

Assets and financial transactions

- 2.13 I have been provided with audited accounts for the period since the previous valuation. The market value of the Scheme's assets, including £0.9 million in respect of external AVCs, was £6,096 million at the valuation date. A summary of the main classes of the Scheme's assets and the main financial transactions in the intervaluation period is shown in Appendix B.
- 2.14 The corresponding market value of assets at the previous valuation date was £5,846 million.

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Section 3: The funding position and future contribution requirements

- 3.1 This part of the *actuarial valuation* reviews the financial position of the Scheme relative to its *statutory and subsidiary funding objectives*. From this assessment we determine the level of Company contributions required to meet the *funding objectives*.
- 3.2 There are normally three stages to the assessment of the financial position of the Scheme relative to its *statutory funding objective*:
- first, we compare the Scheme's assets with the value of the benefits earned in respect of service up to the valuation date (the *technical provisions*);
 - if this reveals a shortfall, a *recovery plan* to remove this shortfall with additional Company contributions over a suitable period is required;
 - finally, we calculate the cost of the continuing accrual of benefits for employed members after the valuation date, so that the funding plan remains on track.

Funding objectives

- 3.3 Having considered the support available for the Scheme from the Company, including additional security that would be available in the event of the Company's insolvency, the Trustees and the Company have agreed the *funding objectives* for the Scheme, and the method and assumptions for calculating the Scheme's *technical provisions*. These are set out in the *Statement of Funding Principles* dated 30 June 2010, which is included as Appendix D.
- 3.4 The Scheme's *statutory funding objective* is to have sufficient and appropriate assets to cover its *technical provisions* (ie the amount that the Trustees have determined should be set aside to meet the Scheme's liabilities).
- 3.5 In addition to the *statutory funding objective*, the Trustees have a *subsidiary funding objective* which is to be able to provide benefits in accordance with the Scheme Rules with a very high level of security on a self-sufficiency basis without reliance on further support from the Company. For this purpose the Trustees will calculate the value of the liabilities allowing only for investment returns from risk-free assets such as gilts, and will include suitable loadings to cover risks and expenses. The Trustees will have regard to the Scheme's anticipated progress towards meeting this subsidiary objective when deciding on funding matters and the Company acknowledges that over time the calculation of *technical provisions* will converge towards the liabilities determined in accordance with this subsidiary objective.
- 3.6 The funding objectives have not changed since the last valuation.

Method and assumptions for calculating technical provisions

- 3.7 The funding method is to determine the discounted capital value of the prospective benefits arising from service completed before the valuation date, including allowance for prospective salary increases for employed members at the valuation date. This is the same method that was used for the last valuation.
- 3.8 The assumptions for calculating the *technical provisions* are set out in the *Statement of Funding Principles* dated 30 June 2010 in Appendix D. The table below summarises the key financial assumptions adopted as at 31 March 2009, with the corresponding assumptions at the previous valuation shown alongside.

	2009 assumptions		2006 assumptions	
	Nominal % pa	Real % pa	Nominal % pa	Real % pa
Price inflation (RPI)*	3.5	-	2.7	-
Discount rate	6.1	2.5	5.2	2.4
Salary increases				
- first 2 years	0.0	(3.5)	3.2	0.5
- 2 to 5 years	In line with RPI	0.0	3.2	0.5
- 5 to 10 years	In line with RPI	0.0	3.7	1.0
- after 10 years	In line with RPI	0.0	4.2	1.5
Pension revaluation in deferment				
- for current deferred pensioners	3.4	(0.1)	2.7	0.0
- for future deferred pensioners	3.5	0.0	2.7	0.0
Pension increases in payment				
- LPI 5% for current pensioners & dependants	3.3	(0.2)	2.7	0.0
- LPI 5% for other members	3.4	(0.1)	2.7	0.0
- LPI with a floor of 3% and a cap of 5% per annum	3.7	0.2	3.0	0.3
- LPI 3% on post-1988 GMPs	2.7	(0.8)	2.4	(0.3)

* At 31 March 2009 this assumption was term-dependent. The rate shown above is the single equivalent assumption at the valuation date allowing for the appropriately weighted average duration of the liabilities.

- 3.9 The key changes to the financial assumptions since the last valuation date are:
- an increase of 0.1% per annum in the real *discount rate* (ie in excess of the assumed rate of inflation);
 - reductions in the real pension increase assumptions (ie relative to inflation), to reflect the particular pattern of future anticipated inflation at the valuation date;
 - an assumption that general salary increases (ignoring the increases from promotion and service increments) would be zero for two years from the valuation date and thereafter equal to increases in price inflation.

3.10 The key changes to the demographic assumptions since the last valuation date are:

- the assumptions for current rates of mortality have been updated to reflect the results of the latest analysis of the Scheme's mortality experience;
- the allowance for future improvements in rates of mortality has been strengthened by applying a minimum improvement rate of 1.25% per annum to the medium cohort improvement factors;
- a reduction in the assumed proportion of pension commuted at retirement for cash from 25% to 20%;
- an increase in the assumed promotional rate of salary increase for active members on GSS and engineering grades.

3.11 Investment management costs are assumed to be met out of future investment income, and so the valuation discount rate is net of such costs.

3.12 As Scheme Actuary I am required to certify that the *technical provisions* were calculated in accordance with section 222 of the Pensions Act 2004. My certificate for this purpose is included at Appendix E.

3.13 It should be noted that the *technical provisions* are not an estimate of the cost of securing the benefits if the Scheme were to wind up.

Past service – comparing assets with technical provisions

3.14 A comparison of the Scheme's *technical provisions* in respect of service up to 31 March 2009 with the market value of the Scheme's assets is as follows:

Valuation statement as at 31 March 2009	£m
Amount required to provide for the Scheme's past service liabilities of:	
Employed members, in respect of service up to 31 March 2009	4,461
Deferred pensioners	1,147
Pensioners and other dependants	2,994
AVCs and other money purchase benefits	176
Total value of accrued benefits (<i>technical provisions</i>)	8,778
Market value of assets	6,096
Past service surplus (shortfall) (assets less <i>technical provisions</i>)	(2,682)
Funding level (assets / <i>technical provisions</i>)	69.4%

3.15 I confirm that, for the purpose of this comparison, the basis for valuing the Scheme's assets is compatible with the basis for valuing its liabilities.

3.16 The figures above compare with a shortfall of £1,723 million, corresponding to a funding level of 77.2%, revealed at the 31 March 2006 *actuarial valuation*.

3.17 The main factors contributing to this deterioration in the funding position are shown below.

Reconciliation from 1 April 2006 to 31 March 2009	£m
Shortfall at 31 March 2006	(1,723)
Interest on the deficit	(283)
Losses on investments relative to 2006 discount rate	(2,168)
Contributions in excess of cost of accruing benefits	1,343
Impact of section 75 payment	43
Pension increases higher than 2.7% per annum assumed at 2006 valuation	(176)
Change in financial assumptions	488
Change in mortality assumptions	(253)
Change in other assumptions	(74)
Other experience items and miscellaneous	121
Shortfall at 31 March 2009	(2,682)

Note: The analysis has been completed in nominal terms. If the analysis were to be completed using an alternative approach or in a different order, the allocation across each of the items above would differ although the losses on investment would still be the most substantial item.

3.18 The corresponding funding level on the subsidiary funding objective is 49.9% as at 31 March 2009.

3.19 It is advisable to monitor the Scheme's finances on a regular basis because movements in the market value of assets can make the funding position volatile. The Trustees are required by law to obtain annual *actuarial reports* on developments affecting the Scheme's assets and *technical provisions* in years when a formal *actuarial valuation* is not carried out. Following this valuation, an *actuarial report* as at 31 March 2010 will be provided by 31 March 2011.

Post valuation events

3.20 A range of approximate updates of the Scheme's funding position to reflect changes since the valuation date was considered. These showed that on a consistent approach the funding position was estimated to have improved at most dates, but for the purposes of setting the recovery plan the Trustees determined to base this on a broadly unchanged funding shortfall as at 31 March 2010.

Recovery plan

3.21 As there was a shortfall relative to the *technical provisions* at the valuation date, the Trustees and the Company must agree a *recovery plan*. This specifies how and by when the *statutory funding objective* is expected to be met.

3.22 The Trustees and the Company have agreed that additional contributions aimed at meeting the funding shortfall will be paid to the Scheme by the Company as follows:

- £11,506,250 per month from April 2009 to June 2010 inclusive;
- £13,481,250 during July 2010;
- £12,000,000 per month from August 2010 to March 2011 inclusive;

- in each of the next 15 years from April 2011 the amounts set out in the following table as twelve equal monthly payments:

Year ending 31 March	Deficit contributions (£m)														
	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026
	164	177	191	205	221	238	257	277	298	321	346	355	364	373	383

- 3.23 The balance of the funding shortfall at 31 March 2010 is expected to be met by an allowance for investment returns at 2.0% pa in excess of inflation from 1 April 2010 over the recovery period (ie 0.3% per annum ahead of the discount rate used for the approximate update of the funding position at 31 March 2010). On this basis, the technical provisions shortfall is expected to be eliminated by 31 March 2026. The recovery period is sensitive to the assumed level of allowance for investment returns from 1 April 2010 and so if for instance this had been 1.7% pa in excess of inflation then the funding shortfall would have been eliminated by 31 March 2029.
- 3.24 In addition, the Trustees and BA have agreed a package of additional security and other measures aimed at improving the funding position and members' benefit security over time, which are documented in a separate legal agreement.

Future service contribution rates

- 3.25 The annual employer contribution rates required over the year, in addition to members' normal contributions, to cover the accrual of benefits for future service are set out in the following table.

	Employer future service contribution rates (% pay for Contribution Purposes)	
	Plan 60	Plan 65
General Staff	16.5%	15.3%
Air Cabin Crew	15.0%	14.7%
Pilots and Officers	19.7%	18.6%

These rates will take effect from 1 October 2010, assuming that changes to members' benefits (as set out in Appendix A) are implemented from that date. In addition, assuming members' contributions are increased by 1.5% of pensionable pay from 1 October 2011, the employers' rates above will then reduce by a corresponding percentage. In addition to the rates outlined above, the employers will contribute an amount equal to the normal contributions that would otherwise be payable by those members who participate in the Scheme's salary sacrifice arrangement. These rates exclude any allowance for Additional Voluntary Contributions paid by members.

- 3.26 These rates include an allowance of 0.8% of pensionable pay for administration and non-investment expenses. *Pension Protection Fund* levies are payable by the Company.
- 3.27 The Company contribution rates have been calculated as the rates required over a 12 month period in addition to the member contributions payable, to meet the cost of the benefits expected to be earned over that year based on the new benefit structure that will take effect from 1 October 2010. On this basis, these rates will be sufficient, if the assumptions are borne out in practice, to cover the accrual of benefits in the future provided the age, sex and salary profile of the employed membership as at the valuation date remains stable.

- 3.28 In practice, however, because the Scheme is closed to new entrants, the average age of the employed membership is expected to rise in due course. When this happens, the contribution rates required to cover accruing benefits are expected to rise (as there is a shorter period over which investment returns can be earned on the contributions). For example the rates of Company contributions for this purpose are expected to increase by, on average, 0.8% of employed members' pensionable earnings by 31 March 2012.

Section 4: The position of the Scheme on discontinuance

- 4.1 This section of the report considers what would happen to the Scheme on discontinuance. This would occur, for example, if the Company were to terminate its liability to contribute or ceased to exist.
- 4.2 If the Scheme were discontinued, employed members would become deferred pensioners with no entitlement to future service benefits. The Scheme would then have liabilities comprising:
- the pensions payable to pensioners and deferred pensioners (and contingent pensions payable to their dependants);
 - future increases in the deferred pensions;
 - future increases to pensions whilst in payment; and
 - future expenses.
- 4.3 On discontinuance, the Trustees could seek to meet the Scheme's liabilities either by buying out the liabilities with an insurance company or by continuing to run the Scheme as a closed fund. The appropriate approach would depend mainly on the financial position of the Company, the level of the Scheme's assets, whether the Scheme would be eligible for entry to the *Pension Protection Fund* (PPF), and whether a buy out of the liabilities would be possible in practice. In paragraphs 4.6 to 4.11 below, I consider a number of possible eventualities.
- 4.4 If the Scheme had wound up at 31 March 2009, legislation would impose a debt on the Company (the "employer debt") equal to my estimate of the full cost of securing all accrued benefits with an insurance company, allowing for expenses, less the value of the Scheme's assets.
- 4.5 The amount of any such employer debt that would actually be paid would depend on the Company's ability to pay what could be a substantial sum of money. The outcome for the Scheme would then depend significantly on whether the Company remained solvent or not, as follows.

Discontinuance when the Company is solvent

- 4.6 If the Company paid the employer debt in full, all of the Scheme's benefits would in theory be met if the Trustees then bought out the Scheme's liabilities immediately with an insurance company. Alternatively, the Trustees might continue to run the Scheme as a closed fund, particularly if there were practical restrictions on buying out the Scheme's liabilities with an insurance company.
- 4.7 If the Trustees decided to run the Scheme as a closed fund without winding up, the ability to provide members' accrued benefits in full from the assets of the Scheme would depend on future experience, in particular the future investment returns achieved and the longevity of the members.

- 4.8 A decision to run the Scheme as a closed fund might well lead the Trustees to change the Scheme's investment strategy. For example, the Trustees might reduce the equity content of the investment policy, choosing instead further exposure to financial instruments that more closely match the liabilities such as index-linked and fixed-interest bonds.

Discontinuance when the Company is insolvent

- 4.9 If the Company had been, or had become, insolvent, any such employer debt may have a low or nil rate of recovery. The existence of additional forms of security as noted in paragraph 3.24 should increase the probability of obtaining at least partial recovery, but for the purpose of this report I have taken no credit for this unless otherwise indicated.
- 4.10 The Scheme would be assessed for possible entry to the PPF. If the assets were insufficient to secure PPF levels of compensation in full, the Scheme would be likely to enter the PPF.
- 4.11 If the full PPF compensation was covered, the Scheme would be required to wind up and the Trustees could not choose to run it as a closed fund instead. If in practice the Trustees were unable to buy out the benefits, the Scheme would be called a 'closed scheme' under the legislation, and would operate as if it were in wind-up, cutting back benefits where necessary to comply with the *statutory priority order*.

Pension Protection Fund

- 4.12 The Government introduced the PPF in April 2005 to ensure that members of private sector occupational defined benefit schemes receive compensation (the "PPF compensation") if the scheme sponsor becomes insolvent. The level of compensation provided would not normally be at the full level promised by the Scheme.
- 4.13 In brief, the levels of PPF compensation are as follows:
- for non-pensioner members younger than normal pension age: a deferred pension equal to 90% of the pension built up to date, subject to a maximum amount and payable from normal pension date;
 - for non-pensioner members over normal pension age: the full deferred pension;
 - for pensioners younger than normal pension age who retired in normal health: 90% of the pension in payment subject to a maximum amount which varies by age;
 - for other pensioners and dependants: the pension in payment;
 - deferred pensions will be increased in line with Retail Price Inflation (capped at 5% per annum for pensions that accrued prior to 6 April 2009 and at 2.5% per annum for pensions accruing after that date) between the assessment date and normal pension age;
 - pensions built up before 6 April 1997 will receive no increases in payment. Pensions built up on or after that date will increase in line with Retail Price Inflation (capped at 2.5% a year);
 - survivor benefits (up to 50% of members' benefits) are provided if they were provided under the Scheme Rules.

- 4.14 The Trustees are required by Section 179 of the Pensions Act 2004 to submit routinely an assessment of the Scheme's discontinuance position, based on assumptions specified by the PPF Board and accrued benefit entitlements similar in form to the PPF compensation. The results of the Section 179 valuation for the Scheme as at 31 March 2009 reveal that the Scheme's assets covered approximately 64% of this measure.
- 4.15 As the level of cover for PPF compensation was less than 100% at the valuation date, the Scheme would have been expected, on discontinuance with an insolvent employer at that date, to enter the PPF, as described in paragraph 4.10. This would mean that the members would be expected to receive 100% of the PPF compensation but no other benefits.

Estimate of the solvency of the Scheme

- 4.16 I am required by law to provide the Trustees with an estimate of the solvency of the Scheme. Normally this means an estimate of the level of cover of accrued benefits if the Trustees were to secure (or buy out) the Scheme's liabilities with an insurance company, on the premise that no further contributions would be available from the Company.
- 4.17 I have based my estimate of the solvency of the Scheme on indicative costs of buying out pension liabilities with insurance companies at the valuation date. In particular, I have:

- projected the future cashflows arising from benefits accrued at the valuation date, as if the Scheme discontinued at that date;
- discounted each future year's cashflow to the valuation date, assuming returns in line with gilt yields of appropriate duration for each cashflow, but allowing for further margins for different categories of member as set out in the table below:

Category	Solvency discount rate
Pensioners	Gilts +0.3% pa
Non-pensioners	Gilts -0.4% pa

- determined future increases to accrued benefits by reference to break-even inflation (the difference between fixed interest gilt yields and index-linked gilt yields in each future year);
 - assumed all other relevant assumptions are as set out in the *Statement of Funding Principles* in Appendix D, except that no allowance is made for the impact of members commuting pension for cash at retirement;
 - made allowance for around £200 million (1.5% of the Scheme's solvency liabilities) of the Scheme's assets to be set aside to cover the expenses of winding up.
- 4.18 My estimate of the solvency of the Scheme at 31 March 2009 is that the assets of the Scheme would have met 46% of the cost of buying annuities to meet the accrued benefits at that date. The coverage for particular benefits depends on where they fall in the *statutory priority order*, as listed below:
- category 1 – benefits relating to certain pension annuities secured by the Scheme before 6 April 1997;

- category 2 – the cost to the Scheme of securing the liabilities for pensions and other accrued benefits that would be payable by the PPF (if the Scheme were eligible for entry to the PPF);
 - category 3 – benefits in respect of defined benefit AVCs not already covered above (money purchase liabilities are excluded from the priority order and should therefore normally be secured in full); and
 - category 4 – all other pensions and benefits provided by the Scheme, including pension increases (where these exceed those under the PPF).
- 4.19 I estimate that all of the benefits in category 1, approximately 74% of the benefits in category 2, and none of the benefits in categories 3 and 4 would have been covered on this basis. If the Scheme was accepted into the PPF, members would be expected to receive 100% PPF compensation but no other benefits.
- 4.20 This figure is only an estimate of the position at the valuation date and should not be relied upon to indicate the position on a future winding up. It is based on indicative market rates for buying out the liabilities of average schemes at the valuation date. However, various factors, including the size of the Scheme, changes in market interest rates and in the supply and demand for annuities, mean that the actual position at any particular point in time (including the valuation date) can be established only by completing a buy out. Furthermore, given the size of the Scheme a buy-out of all the liabilities could have been difficult to achieve at the valuation date.
- 4.21 The corresponding level of cover at the previous valuation was approximately 52%. The reduction in the estimated buy out cover is due mainly to the investment return achieved on the scheme's assets falling below the rate that was assumed. It also reflects a reduction in gilt yields, which form the basis of the solvency estimate at both valuation dates. In addition, there have been various changes in the methodology for assessing solvency at the two valuation dates, some of which have increased the solvency liabilities while others have reduced them.
- 4.22 The solvency position of the Scheme is expected to improve from the valuation date if both the assumptions are borne out in practice and Company contributions are paid as set out in Section 3 above. On this basis, at the *actuarial valuation* due at 31 March 2012, I estimate that coverage will have improved to 100% of the benefits in category 1 and 82% of category 2 benefits. None of the benefits in categories 3 or 4 would be met.

Relationship between the technical provisions and the buy out liabilities

- 4.23 If the *statutory funding objective* had been exactly met on 31 March 2009 (ie there had been no shortfall), I estimate that the solvency of the Scheme would have been approximately 66%. If the subsidiary funding objective had been exactly met on 31 March 2009, I estimate that the solvency of the Scheme would have been approximately 92%

Section 5: Sensitivity of the results

- 5.1 The assumptions used to determine the Scheme's funding and discontinuance positions each represent only one possible scenario of future events. To the extent that the actual experience turns out to be different from the assumptions the financial position of the Scheme will be affected.
- 5.2 The results of the valuation are especially sensitive to the assumptions made regarding investment returns and longevity.

Sensitivity to investment conditions

- 5.3 The assumed future investment returns are unlikely to be precisely borne out. The possible variation in outcomes is considerable, particularly given the substantial proportion of the assets expected to be invested in 'return-seeking' assets (eg equities) the value of which may not move in line with the value of the liabilities. The Trustees and the Company should therefore be aware of the sensitivity of the results to future investment conditions.
- 5.4 If future investment returns over the long term are lower than assumed, then other things being equal the cost of providing the benefits will be higher than calculated in this valuation, which means that unless contributions are adjusted to reflect the experience, the funding position of the Scheme will fall short of the expected position.
- 5.5 To illustrate this we have considered the following examples:
- if yields on fixed and index-linked bonds at the valuation date had been lower by 0.50% per annum, with a corresponding impact on the value of the Scheme's bond assets and the discount rate, but without any change in other asset values; or
 - if the value of the return-seeking investments, such as equities fell by 20%, assuming no movement in the value of the other assets held, nor any change in the discount rate used to determine the technical provisions;

	Actual funding level at 31 March 2009	Funding level assuming 0.5% pa fall in bond yields	Funding level assuming 20% fall in equity values
Technical provisions	69%	67%	62%
Estimated solvency	46%	41%	41%

	Employer contribution rates to cover post October 2010 benefits		Impact of a 0.5% reduction in bond yields on employer contribution rates	
	% Pay for contribution purposes			
	Plan 60	Plan 65	Plan 60	Plan 65
General Staff	16.5%	15.3%	17.9%	16.7%
Air Cabin Crew	15.0%	14.7%	16.6%	16.3%
Pilots and Officers	19.7%	18.6%	21.7%	20.2%

- 5.6 'Catastrophic' investment conditions which would produce significantly worse funding positions than those shown in the above table are also possible.

Sensitivity to mortality experience

- 5.7 The future financial position of the Scheme is also particularly susceptible to future variations in the mortality experience of its pensioners relative to the assumptions adopted for the valuation. For example, the current valuation assumes that mortality rates improve year on year by at least 1.25%. If, in fact, mortality rates improved year on year by at least 2.0% and this was reflected in the 31 March 2009 valuation assumptions, this would add approximately 1.1 years to the life expectancies of pensioners currently aged 65 and approximately 2.6 years to the life expectancies of pensioners aged 65 in 20 years' time. This would result in around a 3% reduction in the Scheme's funding level relative to the technical provisions at the valuation date.
- 5.8 If mortality rates were assumed to improve by at least 2.0% year on year, the contribution rates payable from 1 October 2010 would increase by approximately 1.0% pay for contribution purposes.

Appendix A: Summary of Scheme benefits

The Scheme is a registered pension scheme under the Finance Act 2004 and is contracted out of the State Second Pension. The following is a summary of the benefits valued to determine the *technical provisions* at the valuation date. It does not reflect the proposed benefit and contribution changes from 1 October 2010. These are summarised at the end of this Appendix.

The main provisions of the Scheme are summarised as follows.

Definitions

Normal Retirement Age (NRA)	As defined in the Rules
Pensionable pay	Remuneration designated by the Employer as pay for these purposes, and capped in line with the Index of Retail Prices.
Retiring pay	The average of members' pensionable pay for contribution purposes during the best two years of the last five years of pensionable service. Pensionable pay for contribution purposes is pensionable pay in excess of 1½ times the Lower Earnings Limit. For members under Part 2 of the Rules, pensionable pay for contribution purposes is 85% of pensionable pay or pensionable pay less 1½ times the Lower Earnings Limit if greater.
Pensionable service	Service in respect of which contributions have been paid to the Scheme.

Benefits

Retirement at NRA	General Staff – a pension of 1/56 th of Retiring Pay for each year of pensionable service before 1 April 2007.
	Pilots and Air Cabin Crew – a pension of 1/52 nd of Retiring Pay for each year of pensionable service before 1 April 2007.
	A pension of 1/60 th of Retiring Pay for each year of Pensionable Service on or after 1 April 2007.
Retirement on ill health	An immediate pension calculated as for retirement at NRA but including one-half of potential future pension service as pensionable service.
Lump sum on retirement	On retirement, part of the pension may be exchanged for a lump sum.
Death after retirement	A spouse's pension of two-thirds of member's pension (accrued while Higher Rate contributions were made) which would have been in payment at the date of death assuming no pension was commuted at retirement. Children's allowances are also payable.

Benefits

Death in service	<p>A lump sum of three times pensionable pay is payable.</p> <p>A dependant's pension equal to two-thirds of the pension which the member would have received at NRA had he not died in service, and including one-half of future potential service for a Higher Rate contributor.</p>
Leaving service	<p>A deferred pension is payable from NRA based on Retiring Pay at date of leaving and past pensionable service. Deferred pensions are revalued up to date of retirement in line with Statutory Revaluation Orders.</p>
Pension increases in payment	<p>Pensions in excess of any Guaranteed Minimum Pension (GMP) are increased in line with the Pension Increases (Review) Orders, subject to a maximum of 5% in any one year.</p> <p>GMPs arising from service after 5 April 1988 are increased in line with RPI, subject to a maximum of 3% in any one year.</p>

Members' contributions

	% of Pay for Contribution Purposes	
	Plan 60	Plan 65
All members (Higher Rate)	8.50	5.25
All members (Lower Rate)*	7.00	3.75

In addition, members may elect to pay Additional Voluntary Contributions (AVCs) on the Trustees' published AVC terms.

* The Lower Rate is payable if spouses' benefits are excluded.

Members who participate in the Scheme's salary sacrifice arrangement pay nil member contributions. Instead the employers contribute to the Scheme an amount equal to the normal contributions that would otherwise be payable by these members.

Members of the BAMPS Section of the Rules are provided with money purchase benefits and lump sum death benefits whilst in service of three times' pensionable pay.

Proposed benefit / contribution changes from 1 October 2010

The proposed changes to members' benefits and contributions from 1 October 2010 are as follows:

Members will have a choice of accrual and contribution rates as set out in the following tables, with the contribution rate changes being phased in as shown:

From 1 October 2010 to 30 September 2011:

Accrual rate	% Pay for contribution purposes		
	Option 55*	Plan 60	Plan 65
1/75	16.0%	7.0%	3.75%
1/67	18.25%	9.25%	6.0%
1/60	20.5%	11.5%	8.25%

From 1 October 2011:

Accrual rate	% Pay for contribution purposes		
	Option 55*	Plan 60	Plan 65
1/75	17.5%	8.5%	5.25%
1/67	19.75%	10.75%	7.5%
1/60	22.0%	13.0%	9.75%

* Members who opt to retire at 55 with unreduced benefits

Members will still be able to elect not to accrue spouse's benefits, with a consequent reduction of 1.5% in the contribution rates they are required to pay.

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Appendix B: The information supplied

The information supplied to us for the purposes of the valuation is summarised below; the corresponding 2006 figures are shown for comparative purposes.

Members in service (FSS only)*	31 March 2009		31 March 2006	
	Number	Annual Pay £m pa	Number	Annual Pay £m pa
Males				
General Staff	9,954	325.7	12,585	374.2
Air Cabin Crew	3,288	84.6	3,520	79.4
Pilots and Officers	2,356	193.4	2,496	167.5
Total Males	15,598	603.7	18,601	621.1
Females				
General Staff	5,045	149.4	6,587	173.8
Air Cabin Crew	7,242	186.6	8,127	184.5
Pilots and Officers	149	10.5	154	8.6
Total Females	12,436	346.5	14,868	366.9
Total Members in Service	28,034	950.2	33,469	988.0

Deferred pensioners	31 March 2009		31 March 2006	
	Number	Deferred pension revalued to valuation date £000s pa	Number	Deferred pension revalued to valuation date £000s pa
Total deferred pensioners	22,172	79.1	20,474	58.7

Pensioners	31 March 2009		31 March 2006	
	Number	Annual Pension £m pa	Number	Annual Pension £m pa
In own right	15,690	157.0	13,219	120.6
Widow(er)s	2,437	16.1	1,993	11.4
Dependants/ Children	318	0.6	232	0.4
Total Pensioners	18,445	173.7	15,444	132.4

Notes:

1. In addition, there were combined entitlements for BAMPS members of £5.7 million (2006: £3.8 million).
2. This summary does not reflect changes in the membership as a result of a restructuring exercise which took place after the valuation date.

3. The *technical provisions* shown in this report reflect the impact of a restructuring exercise which took place after the valuation date, and which resulted in a £22 million reduction in liability.

Assets and financial transactions

According to the audited accounts supplied as at 31 March 2009, the market value of the Scheme's assets was £6,096 million. This includes external Additional Voluntary Contributions (AVCs) which amounted to £0.9 million.

The assets, excluding external AVCs, were invested as follows:

	Market value as at 31 March 2009		Market value as at 31 March 2006	
	£m	%	£m	%
Quoted overseas equities	2469.1	40.5	1967.8	33.7
Quoted UK equities	970.2	15.9	1993.0	34.1
Private equities	217.5	3.6	67.3	1.2
Fixed interest securities	895.3	14.7	543.8	9.3
Index linked securities	764.4	12.5	564.7	9.6
Property	471.9	7.7	398.4	6.8
Other investments	194.0	3.2	34.9	0.6
Cash and net current assets	113.1	1.9	274.8	4.7
Total	6095.5	100.0	5844.7	100.0

The table below summarises the Scheme's key financial transactions over the 3 years to 31 March 2009:

Consolidated Revenue Account for the period 1 April 2006 to 31 March 2009

	£m	£m
Fund at 31 March 2006		5,846.0
Income		
Contributions from employer – normal	899.0	
– additional	33.3	
– special deficit contributions	850.0	
– other	55.4	
Contributions from members – normal	104.8	
– AVCs	43.1	
Income from investments	589.7	
Transfer values received from other funds	2.7	
Funded pensions receivable	14.3	
Total income		2,592.3
Expenditure		
Benefits paid – pensions	459.9	
– commutation lump sums	128.2	
Lump sum death benefits	8.8	
Transfer values paid to other funds	52.0	
Administrative expenses	18.0	
Investment management charges	14.1	
Total expenditure		681.0
Change in market value of investments		(1,660.9)
Fund at 31 March 2009		6,096.4

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Appendix C: Legislative changes since 31 March 2006

Since the previous valuation, various Acts of Parliament have been enacted which potentially impact members' benefits. The majority of these changes will either have already been allowed for in the previous valuation or have no impact on the valuation calculations.

Finance Act 2004

In essence this Act and associated Regulations were intended to simplify the entire taxation framework for UK pensions. From 6 April 2006 the former Inland Revenue maximum limits on benefits payable from approved pension schemes were replaced by a system of tax "allowances" by the new HMRC. More specifically:

- members can receive any amount of benefit from a registered occupational pension scheme. However, if the benefits provided have a value higher than a specified amount (the 'Lifetime Allowance', £1.75 million for 2009/10) then the excess value over the Lifetime Allowance is subject to additional tax;
- the value of benefits for the purpose of comparing with the Lifetime Allowance is calculated as 20 times the pension provided plus the face value of the cash sum provided. Benefits provided from money purchase arrangements are based upon the fund value;
- cash sums at retirement are restricted to 25% of the value of the member's benefits;
- if the assessed value of benefit accrual in, and contributions to tax-advantaged pension arrangements for an individual, exceed an Annual Allowance of £245,000 a year for 2009/10, the excess is subject to a special tax charge;
- dependants' pensions are not tested against the Lifetime Allowance, but lump sums provided to dependants are tested against the member's unused allowance;
- the technical details of benefits that can be provided as 'authorised benefits' from a tax-advantaged pension arrangement were specified;
- the statutory surplus test was abolished;
- the minimum age at which members may retire early has increased from age 50 to age 55 from 6 April 2010 except in certain protected situations.

Transitional arrangements were introduced for cases where the new requirements would adversely impact a member's benefits compared to pre-6 April 2006 limits.

Pensions Act 2008

Under this Pensions Act, the cap on the statutory revaluation of deferred benefits was reduced from 5% per annum compound to 2.5% per annum compound in respect of benefits accruing after 5 April 2009. A similar change was introduced by the Pensions Act 2004 in relation to the statutory increases to pensions in payment for benefits accruing after 5 April 2005.

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Appendix D: Statement of Funding Principles

This statement has been prepared by the Trustees of the New Airways Pension Scheme (“the Scheme”) to satisfy the requirements of Section 223 of the Pensions Act 2004, after obtaining the advice of the Actuary, James C Wintle. The Trustees have discussed and agreed it with the Principal Employer, British Airways Plc (“BA”).

Statutory funding objective

The statutory funding objective is that the Scheme should have sufficient and appropriate assets to cover its technical provisions, and this statement sets out the Trustees’ policy for securing that this objective is met.

Subsidiary funding objective

In addition to the statutory funding objective, the Trustees have a subsidiary funding objective, which is to be able to provide benefits in accordance with the Scheme Rules with a very high level of security on a self-sufficiency basis without reliance on further support from BA. For this purpose the Trustees will calculate the value of the liabilities allowing only for investment returns from risk-free assets such as gilts and will include suitable loadings to cover risks and expenses. The Trustees will have regard to the Scheme’s anticipated progress towards meeting this subsidiary objective when deciding on funding matters and BA acknowledges that over time the calculation of technical provisions will converge towards the liabilities determined in accordance with this subsidiary objective.

Technical provisions

Method

The Trustees and BA have agreed that the technical provisions for the Scheme at any given date are to be calculated as the capital value of the prospective benefits arising from service completed before that date, including allowance for prospective salary increases for those members in active service at that date. This method of calculating technical provisions is known as the projected unit method.

Assumptions

The Trustees and BA have further agreed that:

- the discount rate used to calculate the capital value of future cashflows will be a prudent estimate of future investment returns on the assets of the Scheme, allowing for expected changes in the investment policy over time;
- this estimate of future investment returns, together with the remaining financial assumptions, will take into account information available in respect of the relevant investment markets at the effective date of the actuarial valuation. In particular, the assumed level of retail price inflation (RPI) will have regard to break-even inflation derived from the difference between the full index-linked and nominal gilt curves at the valuation date;

- demographic assumptions will have regard to an analysis of the experience of the Scheme membership as well as relevant statistics applicable to similar pension schemes, and the Trustees' and BA's views about how these may change in future.

Taken together, the assumptions adopted at a particular date will be prudent and consistent with the Trustees' desired level of confidence that assets equal to the technical provisions will prove adequate to meet benefits already accrued as they fall due without the need for further contributions.

Discretionary Benefits

There are a number of areas where the benefits payable are subject to some exercise of discretion on the part of the Trustees and/or BA, the principal details of which are set out below:

- At BA's request, and upon payment to the Scheme of any contributions advised by the Actuary to be necessary, the Trustees shall increase or alter any benefit or provide additional benefits under the Scheme. The Trustees and BA have agreed that such discretionary benefits will not be taken into account in the calculation of technical provisions, but that the capital value of any such benefits granted would be paid in full by BA at the time the discretion is exercised.
- Aside from these general provisions there is no requirement for either the Trustees or BA to consider granting discretionary increases to pensions in deferment or in the course of payment, which receive guaranteed levels of increases as specified in the Rules of the Scheme. Consequently for the purposes of calculating the technical provisions, no allowance for discretionary pension increases is made.
- There are a number of options that enable Members to convert the benefits from one form into another subject to the Trustees' consent, such as on early retirement, crystallisation (late retirement), ill-health retirement, or the commutation of pension into cash at retirement. Following completion of formal valuations it is anticipated that the terms for most of these options will be reviewed and updated to be cost neutral on the technical provisions basis, and so the Trustees and BA have agreed that no allowance for the exercise of these options will be made in the determination of technical provisions. However, it is anticipated that the terms applying for cash commutation will continue to differ from those on the technical provisions basis, and so the Trustees and BA have agreed to make allowance for the commutation of some pension into cash in the calculation of technical provisions.

Actuarial investigation as at 31 March 2009

The Trustees (having taken the advice of the Actuary) and BA have agreed assumptions for the determination of technical provisions as at 31 March 2009, following the principles described above. These assumptions are as follows.

Key financial assumptions as at 31 March 2009

	Nominal % per annum	Real % per annum
Discount rate:	6.1	2.5
Price inflation (RPI):	3.5*	-
Salary increases (in addition to promotional scale):		
- first 2 years	0.0	n/a
- after first 2 years	in line with RPI	0.0
Pension revaluation in deferment		
- for current deferred pensioners	3.4	(0.1)
- for future deferred pensioners	3.5	0.0
Pension increases in payment		
- LPI 5%, for pensioners, dependants and crystallised members	3.3	(0.2)
- LPI 5% for all other members	3.4	(0.1)
- LPI with a floor of 3% and a cap of 5% per annum	3.7	0.2
- LPI 3% on post-1988 GMPs in payment	2.7	(0.8)

* this is the single equivalent figure for this term-dependent assumption

Statistical assumptions as at 31 March 2009

The post-retirement mortality assumptions are based on the standard tables issued by the CMI which reflect the experience of self-administered pension schemes ("SAPS tables"). These tables were then calibrated, based on the results of a Generalised Linear Model (GLM) mortality analysis, to reflect the demographic profile of the Scheme (by reference to age, gender, category of membership, occupation category, pension amount and postcode). They incorporate medium cohort improvement factors to 2009. The assumptions are summarised in the table below.

Group	Base table** for non-pensioners	Base table** for current pensioners
Male members with pensions*:		
< £21,800	86% of S1PML	87% of S1PML
> £21,800	95% of S1PMA_L	96% of S1PMA_L
Female members	88% of S1PFA	98% of S1PFA
Male dependants	105% of S1PMA	117% of S1PMA
Female dependants	86% of S1DFL	87% of S1DFL

* at the valuation date

** standard SAPS table notation

For prospective ill-health retirements from active status, the multipliers above are uplifted by 84%.

In addition, allowance was made for future improvements in rates of mortality from calendar year 2009 by reducing the rates of mortality from the base tables described above according to the medium cohort improvement factors issued by the CMI, subject to a minimum annual rate of improvement of 1.25%.

Details (including sample rates) of the remaining demographic assumptions are shown in the appendix to this statement.

Expenses

Investment management costs are assumed to be met out of future investment income. The valuation discount rate is therefore net of such costs.

Administrative and other non-investment expenses (except Pension Protection Fund levies) are met in full by the Scheme and so the expected amount of such expenses (0.8% of pensionable pay) has been added to the contributions required from the Participating Employers. In addition to the contributions arising from this calculation, BA has also agreed to pay in full any Pension Protection Fund levies in respect of the Scheme.

Eliminating a shortfall

The Trustees and BA have agreed that any funding shortfalls identified at an actuarial valuation should be eliminated as quickly as the employers can reasonably afford by the payment of additional contributions over the recovery period. In determining the recovery period at any particular valuation the Trustees will take into account relevant factors such as:

- the provisions of the Trust Deed & Rules;
- the size of the funding shortfall and the degree of prudence in the technical provisions;
- any estimated change in the financial position of the Scheme for part or all of the period between the valuation date and when the recovery plan is agreed, and in order, inter alia, to facilitate the development of the recovery plan the Trustees have also determined the real discount rate at 31 March 2010 to be 1.7% per annum;
- the risk that the Scheme's financial position may deteriorate against the statutory and subsidiary funding objectives;
- the projected financial position of BA, including its free assets and projected cashflow, and the risk of significant deterioration in this position;
- any contingent assets or letters of credit provided by BA (to the extent that these are not already being used to support the level of technical provisions).

Frequency of actuarial investigations

In the normal course of events the Trustees will request subsequent valuations three years after the preceding one. The Actuary will provide an estimate of the up-to-date financial positions of the Scheme as at each anniversary of the formal funding valuation.

The Trustees may call for a formal funding valuation at any date if they are of the opinion that events have made it unsafe to rely on the results of the previous valuation for funding purposes. In reaching such a view, the Trustees will consider the advice of the Actuary and consult with BA.

Arrangements for other parties to make payments to the Scheme

There are no arrangements for a person other than the Participating Employers or a Member of the Scheme to contribute to the funds held by the Scheme.

Paying funding surpluses to the employer

The Rules do not include provisions for the Trustees to make payments to any of the Participating Employers out of funds held for the purposes of the Scheme unless there exists a surplus following a winding up of the Scheme.

Cash equivalent transfer value calculations

The Trustees will ask the Actuary to advise them at each valuation of the extent to which assets are sufficient to provide cash equivalent transfer values for all non pensioners without adversely affecting the security of the benefits of other members and beneficiaries. The Trustees' current policy is not to reduce cash equivalent transfer values paid to members. This policy is reviewed from time to time in the light of the Scheme's financial position, and the amount and volume of cash equivalent payments made from the Scheme. The policy will also be reviewed whenever the basis of calculation of cash equivalent payments changes.

Dates of review of this statement

This statement will be reviewed, and if necessary revised, by the Trustees (subject to agreement from BA) either

- within 15 months after the effective date of each actuarial valuation; or
- within a reasonable period after any occasion on which the Regulator has used its powers to modify future accrual of the Scheme, directed as to the manner in which technical provisions are to be calculated or the period over which failure to meet the statutory funding objective is to be remedied, or imposed a schedule of contributions.

The Trustees may also elect to review, and if necessary revise (subject to agreement from BA), the statement at other times.

Date of preparation of Statement of Funding Principles: 30 June 2010

Signed on behalf of the Trustees of the Scheme

Signature:

Print name:

Position:

Signed on behalf of the employers

Signature:

Print name:

Position:

Appendix – Statistical assumptions

In-service decrements and promotional salary increases

For each separate category of active member, various assumptions are made about the rates of decrement from active membership on account of withdrawal (resignation), death or ill-health retirement at each age. In addition, age-related increases to unabated pensionable pay arising from promotion and service increments are assumed. Sample rates for the separate categories of active members are shown in the tables below.

Post-retirement mortality

The post-retirement mortality assumptions are described in the Statement itself.

Pre-retirement mortality for deferred pensioners

Consistent with post-retirement mortality assumptions

Spouses' and dependants' pensions

For current pensioner members, each member's current marital status is assumed to remain unchanged. For all other members, the proportion of members whose death prior to retirement is assumed to give rise to a spouse's or other dependant's pension varies by age but is around 90% for men and 80% for women at ages close to retirement. After retirement, these proportions are assumed to reduce in accordance with assumed rates of spouse's / dependant's mortality.

Age difference between members and dependants

Non-pensioner male members are assumed to be 2.5 years older than their spouses. Non-pensioner female members are assumed to be 1.5 years younger than their spouses. Actual spouses' data is used for pensioner members.

Allowance for option of members to commute pension for cash at retirement

Members are assumed to commute 20% of their pension for cash at retirement on current terms.

In service decrements and promotional salary increases: Flight crew

Age	Sample rates of decrement per 1,000 members at each age					Assumed percentage increase in pay to the next year of age	
	Withdrawal		Death		Ill-health Retirement	Past service	Future service
	Men & Women	Men	Women	Men & Women	Men & Women		
25	10	0.3	0.2		0.0	0.0	0.0
30	10	0.4	0.2		0.5	3.7	3.8
35	10	0.4	0.3		1.2	3.4	3.4
40	10	0.6	0.5		2.5	2.9	3.0
45	10	0.9	0.8		5.0	2.2	2.3
50	-	1.5	1.2		5.0	0.9	1.1
55	-	2.4	1.9		5.0	0.5	0.6
60	-	3.8	3.1		-	0.0	0.0

Note that all co-pilots are assumed to attain command before leaving the Scheme.

In service decrements and promotional salary increases: Cabin crew

Age	Sample rates of decrement per 1,000 members at each age						Assumed percentage increase in pay to the next year of age
	Withdrawal		Death		Ill-health Retirement		
	Men	Women	Men	Women	Men & Women	Men & Women	
25	50	56	0.3	0.2	1.0	0.0	
30	35	50	0.4	0.2	1.0	2.5	
35	20	38	0.4	0.3	1.0	1.6	
40	10	27	0.6	0.5	1.0	1.6	
45	-	16	0.9	0.8	1.5	1.2	
50	-	5	1.5	1.2	2.7	1.2	
55	-	-	2.4	1.9	5.8	0.7	
60	-	-	3.8	3.1	9.5	0.4	

In service decrements and promotional salary increases: Ground staff (GSS and Engineering)

Age	Sample rates of decrement per 1,000 members at each age					Assumed percentage increase in pay to the next year of age	
	Withdrawal		Death		Ill-health Retirement		
	Men	Women	Men	Women	Men & Women	Men & Women	
25	70	126	0.3	0.2	1.0	5.2	
30	56	99	0.4	0.2	1.0	3.6	
35	45	77	0.4	0.3	1.0	2.8	
40	36	54	0.6	0.5	1.0	1.5	
45	30	36	0.9	0.8	1.5	1.2	
50	11	18	1.5	1.2	2.7	0.9	
55	-	-	2.4	1.9	5.8	0.9	
60	-	-	3.8	3.1	9.5	0.7	

In service decrements and promotional salary increases: Ground staff (Other)

Age	Sample rates of decrement per 1,000 members at each age					Assumed percentage increase in pay to the next year of age Men & Women
	Withdrawal		Death		Ill-health Retirement	
	Men	Women	Men	Women	Men & Women	
25	153	126	0.3	0.2	1.0	5.2
30	111	99	0.4	0.2	1.0	3.6
35	80	77	0.4	0.3	1.0	2.8
40	59	54	0.6	0.5	1.0	1.5
45	44	36	0.9	0.8	1.5	1.2
50	14	18	1.5	1.2	2.7	0.9
55	-	-	2.4	1.9	5.8	0.9
60	-	-	3.8	3.1	9.5	0.7

Appendix E: Statutory certificate

Actuarial certification for the purposes of regulation 7(4)(a) of the Occupational Pension Schemes (Scheme Funding) Regulations 2005

Name of scheme: **New Airways Pension Scheme**

Calculation of technical provisions

I certify that, in my opinion, the calculation of the Scheme's technical provisions as at 31 March 2009 is made in accordance with regulations under section 222 of the Pensions Act 2004. The calculation uses a method and assumptions determined by the Trustees of the Scheme and set out in the Statement of Funding Principles dated 30 June 2010.

James C Wintle
Fellow of the Institute of Actuaries

30 June 2010

Towers Watson Limited
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London Road
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Authorised and regulated by the Financial Services Authority

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Appendix F: Glossary

This glossary describes briefly the terminology of the new regime for funding defined benefit pension schemes as introduced by the Pensions Act 2004. Defined terms are in *italics*.

Actuarial report: this is a financial check carried out by the Scheme Actuary in-between *actuarial valuations* to estimate the level of coverage of the *technical provisions*. This financial check is carried out using more approximate methods than for an *actuarial valuation*. The estimates are based upon the assumptions set out in the *Statement of Funding Principles*.

Actuarial valuation: this is a financial check carried out by the Scheme Actuary that assesses whether the assets are sufficient to meet the *funding target*. It also determines the contributions required to meet the target, both in respect of benefits built up to date for all members and the benefits that are building up to employed members. The calculations are based upon a number of assumptions.

Discount rate: this is the investment return expected to be achieved on the scheme's assets in the future. The lower the investment return assumed the more cautious the assumption.

Employer covenant: this is the ability and willingness of the sponsoring employer to support a scheme; under the new funding regime trustees are required to take this into consideration in making funding decisions.

Funding target/objective: this is a policy to achieve, by the end of a specified period, the minimum amount of assets expected to be sufficient to pay benefits built up to date as they fall due over the lifetime of the scheme. It is usually based on a scenario that requires assumptions to be made about the future.

Pension Protection Fund (PPF): established by the Pensions Act 2004, this provides compensation to members of an occupational scheme in the event that the scheme is wound up with insufficient assets and the employer has become insolvent.

Recovery plan: this will be drawn up where an *actuarial valuation* discloses that the assets held are less than the *technical provisions*. It is a formal agreement between trustees and the employer that sets out the steps to be taken with the aim to ensure there are sufficient assets to cover the *technical provisions* at the end of an agreed period.

Schedule of Contributions: this is a document that sets out the agreed contributions payable into a scheme by members and the employers and the dates by which such contributions are to be paid. It includes, but is not limited to, contributions agreed under a *recovery plan*.

Statement of Funding Principles: trustees are responsible for preparing and maintaining this document (with the agreement of the employer and after taking the advice of the actuary). It sets out the trustee's policy for ensuring that the *statutory funding objective* is met and, in particular, the method for determining the assumptions for calculating the *technical provisions*.

Statement of Investment Principles: trustees are responsible for preparing and maintaining this document. It sets out the policy for investing the scheme's assets.

Statutory funding objective: every pension scheme is subject to the *statutory funding objective*, which is to have sufficient and appropriate assets to cover its *technical provisions*. Trustees may establish other funding objectives in addition to the *statutory funding objective*.

Statutory Priority Order: this sets out the order in which the assets of a scheme should be applied in securing the benefits of different members in the event of a *wind-up*. In broad terms it requires that, after allowing for expenses, a scheme first secures benefits that are in line with the compensation that would be provided by the *Pension Protection Fund* with any remaining assets then being used to secure any other benefits.

Subsidiary funding objective: in addition to the *statutory funding objective* to which all pension schemes are subject, trustees may wish to adopt other funding objectives. Such objectives are subordinate to the *statutory funding objective* from a regulatory perspective.

Summary funding statement: Trustees must issue a statement to members following each *actuarial valuation* and each *actuarial report* to disclose the scheme's funding position and certain other information.

Technical provisions: this is the amount of assets required to make provision for the accrued liabilities of the scheme. Over the lifetime of the scheme, this amount is expected to be sufficient to pay all of the benefits built up to date as they fall due, based upon the method and assumptions set out in the *Statement of Funding Principles*.

The Pensions Regulator: the statutory body established with the aim of ensuring the security of members' benefits and reduce the claims for compensation from the *Pension Protection Fund*. As part of this role it monitors the funding plans of all occupational defined benefit schemes and has wide-ranging powers to ensure these are adequate.

Wind-up: a particular method of discharging a scheme's liability to pay benefits. It typically arises where the employer no longer provides financial support to the scheme (for example if it becomes insolvent) and would usually involve using the scheme's assets to buy a policy with an insurance company that pays as much of the scheme's benefits as possible in accordance with the *statutory priority order*.