

7 PENSION SCHEMES

Group entities operate pension arrangements in order to provide pension benefits to retired employees. Benefits granted have been developed to reflect local practice and may be provided through defined benefit or defined contribution schemes.

The main defined benefit plans are in the UK and Australia:

UK: The majority of pensions for UK employees are funded through the industry-wide scheme, the Electricity Supply Pension Scheme (ESPS), which is a defined benefit scheme with assets invested in separate trustee administered funds. The ESPS is divided into sections, and the International Power Group of the ESPS was opened to members on 1 April 2002 and employees' past service rights were transferred into the Group later that year.

The majority of employees taken on in First Hydro, as part of the acquisition of the EME portfolio, are members of another section of the ESPS, the First Hydro Group.

The liabilities and costs shown in the disclosures for the UK schemes are based on the most recent actuarial valuations at 31 March 2004. The results of these valuations have been updated to 31 December 2006 by independent qualified actuaries to take account of the requirements of IAS 19.

AUSTRALIA: Employees at Hazelwood and Loy Yang B participate in a standard Australian superannuation fund called Equipsuper. This plan provides benefits primarily for employees in the electricity, gas and water industry, and was developed from the scheme sponsored by the State Electricity Commission of Victoria. Employees at Synergen participate in the Electricity Industry Superannuation Scheme.

The liabilities and costs shown in the disclosures for the Australian schemes are based on the most recent actuarial valuations at 31 December 2006.

The liabilities and costs for IAS 19 were determined using the projected unit credit method. The Group has decided to recognise gains and losses through the income statement over the expected working lifetime of active employees to the extent that gains or losses are in excess of the 'corridor' (10% of the greater of the defined benefit obligation and the plan assets).

The charge for 2006 in respect of defined contribution plans was £4 million (2005: £3 million).

The Group used the following assumptions to calculate the scheme liabilities under IAS 19:

Financial assumptions	31 December 2006		31 December 2005		31 December 2004	
	UK %	Australia %	UK %	Australia %	UK %	Australia %
Discount rate	5.1	4.9	4.7	4.6	5.3	4.5
Rate of increase in salaries	4.6	4.3	4.4	4.0	4.4	4.0
Inflation rate	3.1	3.0	2.9	3.0	2.9	3.0
Increase to deferred benefits during deferment	3.1	n/a	2.9	n/a	3.0	n/a
Increases to pensions payments	3.1	n/a	2.9	n/a	2.9	n/a

7 PENSION SCHEMES continued

The amounts charged to profit from operations, recorded in the income statement, in relation to the defined benefit pension plans for the year ended 31 December 2006 were as follows:

	Year ended 31 December 2006 £m	Year ended 31 December 2005 £m
Current service cost	11	9
Expected return on schemes' assets	(13)	(11)
Interest on schemes' liabilities	10	9
Curtailement cost	2	–
Total operating charge	10	7

The assets in the schemes and expected rates of return (weighted averages) were:

	31 December 2006		31 December 2005		31 December 2004	
	UK %	Australia %	UK %	Australia %	UK %	Australia %
Long-term rate of return expected:						
Equities	7.5	7.8	7.1	7.5	7.5	7.3
Bonds	4.7	4.6	4.4	5.0	4.9	4.8
Other	6.2	5.9	6.0	5.9	6.0	5.5
Total long-term rate of return expected	7.1	6.7	6.6	6.7	7.0	6.5

The expected rates of return reflect the Group's best estimate of the investment returns that will be earned on each asset class. These returns are based on advice provided by independent qualified actuaries.

	31 December 2006			31 December 2005			31 December 2004		
	UK £m	Australia £m	Total £m	UK £m	Australia £m	Total £m	UK £m	Australia £m	Total £m
Assets in schemes:									
Equities	108	55	163	84	52	136	66	44	110
Bonds	17	15	32	14	17	31	11	16	27
Other	10	21	31	16	15	31	12	10	22
Total market value of assets	135	91	226	114	84	198	89	70	159

Other assets principally comprise property and cash.

The reconciliation of the schemes' (deficits)/surpluses to the balance sheet amount is:

	31 December 2006			31 December 2005			31 December 2004		
	UK £m	Australia £m	Total £m	UK £m	Australia £m	Total £m	UK £m	Australia £m	Total £m
Total market value of assets	135	91	226	114	84	198	89	70	159
Present value of scheme liabilities	(158)	(83)	(241)	(151)	(79)	(230)	(114)	(70)	(184)
(Deficit)/surplus in the scheme	(23)	8	(15)	(37)	5	(32)	(25)	–	(25)
Unrecognised actuarial (gains)/losses	–	(10)	(10)	12	(7)	5	–	(4)	(4)
Unrecognised asset due to limit in IAS 19 para 58(b)	–	–	–	–	–	–	–	–	–
Pension liability before deferred tax	(23)	(2)	(25)	(25)	(2)	(27)	(25)	(4)	(29)

Movements in fair value of assets:

	Year ended 31 December 2006 £m	Year ended 31 December 2005 £m
At 1 January	198	159
Expected return on assets	13	11
Actuarial gains	9	16
Employer contributions	12	9
Scheme participants' contributions	3	3
Benefits paid	(3)	(2)
Expenses, taxes and premiums paid	(1)	(1)
Exchange differences	(5)	3
At 31 December	226	198

Movements in defined benefit obligations:

	Year ended 31 December 2006 £m	Year ended 31 December 2005 £m
At 1 January	230	184
Service cost	11	9
Interest cost	10	9
Actuarial (gains)/losses	(6)	25
Scheme participants' contributions	3	3
Benefits paid	(3)	(2)
Expenses, taxes and premiums paid	(1)	(1)
Settlements and curtailments	2	–
Exchange differences	(5)	3
At 31 December	241	230

History of asset experience gains and losses

The transition date for conversion to IFRS for International Power was 1 January 2004 and therefore the following historical data has been presented from that date. This will be built up into a rolling five-year record over the next two years.

	Year ended 31 December 2006	Year ended 31 December 2005	Year ended 31 December 2004
Difference between the actual and expected return on schemes' assets:			
Amount (£m)	9	16	9
Percentage of schemes' assets	4%	8%	6%
Experience (losses)/gains on schemes' liabilities*:			
Amount (£m)	(2)	11	7
Percentage of the present value of schemes' liabilities	1%	5%	4%

*Does not include the effect of changes in assumptions.

Contributions in 2007

The Group expects to make contributions of approximately £8 million to its defined benefit pension arrangements in 2007.