



# PEARL GROUP STAFF PENSION SCHEME

(formerly the HHG Staff Pension Scheme)

The Trustee's report  
to members  
for the year ended  
31 December 2005



# Changes to the Scheme

The following changes to the board of directors took place during 2005:

<b>Tom Cross Brown</b>	<b>appointed 17 August 2005</b>
<b>James Darkins</b>	<b>resigned 13 April 2005</b>
<b>Malcolm Jones</b>	<b>resigned 13 April 2005</b>
<b>Robin Holland-Martin</b>	<b>resigned 21 November 2005</b>

During 2005, following the de-merger of Henderson and the Pearl Group of Companies, a transfer-out of Henderson and Towry Law members took place. As a result the Scheme now has members in only four sections: the Pearl Final Salary section, the London Life Final Salary section, the NPI Final Salary section and the Money Purchase section.

As part of the transaction the principal employer was changed to Pearl Assurance Group Holdings Ltd, and then, following a further Company re-structure, the Trustee secured a second change of principal employer to Pearl Group Limited.

## **Escrow payments**

As part of the de-merger agreement an amount of money was paid across to a third party for the benefit of the Scheme - to be released to the Scheme if certain conditions were met. Known as an 'Escrow' account it was intended to be used to enhance the funding of the Scheme, if necessary.

Following the de-merger, the Trustee re-assessed the Scheme's investment strategy and decided that a revised asset allocation was appropriate. Taking account of this revised investment strategy, the Scheme Actuary calculated that there was a deficit in the Scheme, which triggered payments from the Escrow account. Consequently, payments from the Escrow account of £9.7m per year have commenced and will continue until the Escrow account is exhausted, or 2009 if earlier. The Company has also agreed to make these annual payments for the calendar years 2010 to 2014 inclusive.

## Introducing the new annual summary funding statement

A key part of the Government's new pensions legislation is that defined benefit pension schemes, such as our Final Salary sections, must provide their members and all beneficiaries with a summary funding statement, which has to be issued within a reasonable period following each actuarial valuation or actuarial report.

The summary funding statements must be issued annually, with the first one to be provided no later than 21 September 2006, even if an actuarial valuation has not yet been completed.

**Your first statement is included in this report - see page 10.**

# The financial development of the Scheme

## Income and expenditure for 2005

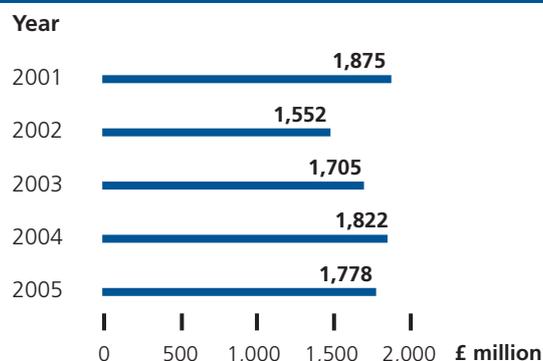
Value of Fund at 1 January 2005: £1,822,265,000

	Final Salary £'000	Money Purchase £'000	Total £'000
<b>Income for the year</b>			
Contributions	16,241	371	16,612
Investment income	49,124	-	49,124
<b>TOTAL</b>	<b>65,365</b>	<b>371</b>	<b>65,736</b>
<b>Expenditure for the year</b>			
Benefits payable	64,477	287	64,764
Payments to, and on behalf of, leavers*	226,691	19,399	246,090
State Scheme premium payments	5	85	90
Administrative expenses	1,360	-	1,360
Investment management expenses	444	-	444
<b>TOTAL</b>	<b>292,977</b>	<b>19,771</b>	<b>312,748</b>
Income less expenditure	(227,612)	(19,400)	(247,012)
Change in market value of investments	197,904	4,450	202,354
Net (decrease)/increase	(29,708)	(14,950)	(44,658)

Value of Fund at 31 December 2005: £1,777,607,000

\*This amount is mainly due to the transfer of assets to the Henderson Group Pension Scheme.

The chart below shows how the value of the Fund has changed over the last five years



In 2005 the value of the Fund decreased by £44 million. At the end of the financial year to 31 December 2005, the assets of the Fund were valued at £1,778 million. Part of the decrease was as a result of the transfer-out of the Scheme of Henderson Group members following the de-merger.

An actuarial valuation took place during 2004, based on the position of the Scheme at 31 December 2003. This showed a satisfactory financial position, although an increased contribution was recommended for 2005.

**The contribution rates for 2005 were:**

27% of pensionable salary for Final Salary section members

13.8% of pensionable salary for pure Money Purchase section members

20.8% of pensionable salaries for hybrid members

## Membership

	Final Salary	Money Purchase	Total
<b>TOTAL MEMBERSHIP</b>			
<b>1 January 2005</b>	<b>25,453</b>	<b>3,408</b>	<b>28,861</b>
<b>Members in service</b>			
<b>1 January 2005</b>	<b>977</b>	<b>1,586</b>	<b>2,563</b>
<b>Members in service</b>			
<b>31 December 2005</b>	<b>551</b>	<b>558</b>	<b>1,109</b>
<b>Pensioners</b>			
<b>1 January 2005</b>	<b>8,966</b>	<b>45</b>	<b>9,011</b>
<b>Pensioners</b>			
<b>31 December 2005</b>	<b>8,839</b>	<b>51</b>	<b>8,890</b>
<b>Preserved pensions</b>			
<b>1 January 2005</b>	<b>15,510</b>	<b>1,777</b>	<b>17,287</b>
<b>Preserved pensions</b>			
<b>31 December 2005</b>	<b>13,915</b>	<b>1,500</b>	<b>15,415</b>
<b>TOTAL MEMBERSHIP</b>			
<b>31 December 2005</b>	<b>23,305</b>	<b>2,109</b>	<b>25,414</b>

# Managing our investments

## Money Purchase section

Members of the Money Purchase section can choose to invest in five Henderson Funds as well as the Fidelity Global Equity Fund, the Legal & General Global Equity Fund and the Standard Life Managed Fund, which replaced the Deutsche Balanced Fund in January 2005. If a member does not make an investment choice, their credits are invested in the 'default'

fund, which is the Henderson Mixed Managed Fund. Members may also choose to invest AVCs in the Henderson Global Technology and the Henderson Industries of the Future funds.

The performance of all the funds over the year ended 31 December 2005 is shown below.

Fund	Value 31.12.2005 £000	Value 31.12.2004 £000	One year performance %	Benchmark %
Henderson Global Equity (Active)	5,145	7,248	20.40	22.90
Henderson Global Equity (Passive)	0	4,610	N/A	N/A
Henderson Mixed Managed	15,128	19,884	18.80	21.50
Henderson Global Bond	301	665	4.40	4.10
Henderson Index Linked Bond	156	310	8.60	9.70
Henderson Cash	229	476	4.40	4.80
Henderson Industries of the Future	75	74	18.61	23.06
Henderson Global Technology	41	40	20.50	N/A
Deutsche Balanced	0	1,120	N/A	N/A
Fidelity Global Equity	1,687	2,081	24.40	23.40
Standard Life Managed	404	9	23.97	22.30
Legal & General Global Equity (Passive)	1,548	0	23.80	23.80

## Final Salary section

Our investment manager for the Final Salary section is Henderson Global Investors.

The estimated return achieved by the Scheme for 2005 was 19.7% against the estimated benchmark return of 20.7%. Over the three years to 31 December 2005 the Scheme returned 15.7% per annum against the estimated benchmark return of 16.1%.

Henderson has taken action to address this underperformance by making changes to the people managing the investments and the structure of the team. The Trustee has monitored these changes to see if the actions taken are satisfactory. In addition, some of the overseas investments are to move to an 'enhanced index'. An 'enhanced index' fund aims to track an index, but also attempts to boost returns by taking advantage of market timing, specific stock selections, and other factors. The Trustee will continue to monitor the performance closely in the future and consider if the changes made are adequate.



# The Markets

The following is a summary of Henderson's analysis of market movements in 2005.

## Equities

2005 was another good year for equity investors. Markets rallied as global economic growth stayed strong and the corporate earnings outlook improved. High levels of merger and acquisition activity across the major markets also helped.

The UK equity market recorded its best showing in six years with the FTSE All Share Index gaining 22%. The FTSE Mid 250 Index finished 2005 at an all-time high, posting a gain of 30.2% overall.

European equity markets posted healthy gains in 2005 with the FTSE Europe ex UK Index returning 24.1%. The performance of the US equity market was markedly disappointing, advancing only 4.9%. Domestically, US equities were held back by a combination of record highs in the oil price over the summer months, the impact of hurricanes on the Gulf Coast and the potential impact of interest rate hikes on consumer demand and corporate profitability.

Japanese equities capped a memorable year which saw the Topix Index return 41%, with growing evidence that the economy was emerging at last from a prolonged era of deflation triggering a wave of buying from international investors. Asian equity markets also made significant progress, with the FTSE Pacific ex Japan Index gaining 35.6%.

## Bonds

The JP Morgan Global Government Bond index rose by 4.53%. This compared poorly to the UK bond returns, where the long gilt index rose by 11% and index-linked by 9.6%. Corporate bonds outperformed slightly. US Treasury yields started the period at 4.22%, and ended it at 4.40%.

Fixed interest Gilts fared well over the review period, the FTA Government All Stocks index returned 7.93% in total return terms.

Index-linked gilts also performed strongly, returning 8.97%. Key drivers included the belief that higher oil prices and resilient economic growth would feed into inflation.

## Currency

In currencies, the dollar strengthened on the rising interest rate differential and faltering European growth into the first half of 2005. Sterling was largely flat, though it succumbed slightly to increasing expectations of a rate cut which finally came in August. The euro weakened, although the currency is expected to strengthen as the interest rate differential between Europe and the US could well narrow. In July, China revalued the renminbi by 2.1% against the dollar.

## Outlook

We anticipate weaker growth in US consumer spending, but a sustained domestic-led revival in Japan and a modest, short-lived pick up in domestic spending in Europe.

Financial markets are expecting modest interest rate increases in the US and EU in 2006 and no change in the UK, which could lead to another dull year for bonds.

We expect equity markets to make progress in 2006, although they may struggle to match the returns produced in 2005.



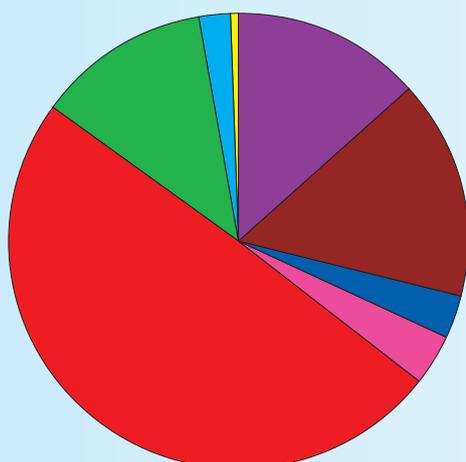
## Fund performance for 12 months to 31.12.05

	Pearl%	Benchmark%	Relative%
UK Equities	19.2	22.0	-2.8
International Equities	25.4	28.2	-2.8
Fixed Income	8.0	8.4	-0.4
Property	21.2	18.5	2.6
<b>TOTAL</b>	<b>19.7</b>	<b>20.7</b>	<b>-1.0</b>

## The top ten holdings

The ten largest holdings held by the Fund at 31 December 2005 were:

Holding	Market Value £ million	% of Portfolio
UK Treasury 2% index-linked 26/01/35	357.4	20.5%
UK Treasury 2.5% index-linked 16/04/20	307.7	17.7%
UK Treasury 4.125% index-linked 22/07/30	111.9	6.4%
UK Treasury 2.5% index-linked 17/07/24	89.6	5.1%
BP	15.0	0.9%
UK Treasury 4.75% 07/09/15	14.8	0.9%
Vodafone Group	12.9	0.7%
HSBC	12.4	0.7%
Royal Dutch Shell	10.9	0.6%
UK Treasury Stock 4.75% 07/06/10	10.9	0.6%



## Asset distribution

● UK Equities	13.4%
● International Equities	15.6%
● Gilts	3.1%
● Corporate Bonds	3.5%
● Index-linked	49.6%
● Property	12.2%
● Cash	2.2%
● Other assets	0.4%

# Fund changes for Money Purchase section

The Trustee has agreed with Henderson Global Investors to make changes during 2006 to the Money Purchase funds that Henderson manage. The choice of funds will be broadly similar to that currently available and the table below sets out more information about the investment objectives and benchmarks of each fund.

No action needs to be taken by you as your Henderson account and future credits will be switched automatically to the corresponding replacement fund at no additional cost.

The Trustee expects that the changes to the managed and equity funds will address the recent under performance of these funds. The aim of the new funds is to provide more consistent performance and to match or perform a little above the relevant indices.

**Choosing the right fund to invest in is extremely important and should be considered carefully given your individual circumstances.**

You may wish to take independent financial advice. If you wish to change your choice of fund you are entitled to a free switch once a year and three times a year once you reach age 55. (Further switches can be made at a charge of £25 per switch. Please see the Scheme booklet for details.)

If you wish to change your investments a Switching Investment Options Form can be obtained from the Scheme Administrators at the address on the back page. Please note that the Scheme Administrators are not allowed by law to give specific financial advice.



Current Fund	Aim and Benchmark	Annual mgmt fund charge	Replacement Fund	Aim and Benchmark	Annual mgmt fund charge
Henderson Mixed Managed Fund	Aim is to provide growth over a medium to long period, investing in a mix of bonds and equities. Benchmark is Russell Mellon Pooled Median and Discretionary ex Property.	0.25%	Henderson Enhanced Balanced Fund	Aim is as current fund, but all equities will be managed on an 'enhanced index' basis. This approach aims to outperform the relevant FTSE index in each region through investing in most of the companies in the index and exploiting anomalies in those markets to add value. Composite benchmark: 37.5% UK equity, 37% overseas equity, 25% bonds.	0.25%
Henderson Global Equity (Active) Fund	Aim is to provide good growth over a medium to long period, investing in equities. Benchmark is 70% FTSE All Share, 30% Russell Mellon Discretionary Overseas Equity Median.	0.375%	Henderson Global (50/50) Enhanced Equity Fund	As current fund, but all equities will be managed on an 'enhanced index' basis. This approach aims to outperform the relevant FTSE index in each region through investing in most of the companies in the index and exploiting anomalies in those markets to add value. Composite benchmark: 50% UK equity, 50% overseas equity.	0.25%
Henderson Global Bond Fund	Aim is to provide a more stable alternative to equity investment. Benchmark is Citigroup World Government Bond Index.	0.15%	Henderson Global Bond Fund	Aim and benchmark mirror current fund.	0.15%
Henderson Index Linked Bond Fund	Aim is to protect pension buying power as much as possible. Benchmark is FTA Government Index-Linked (over 5 years).	0.25%	Henderson Index Linked Bond Fund	Aim and benchmark mirror current fund.	0.25%
Henderson Cash Fund	Aim is to avoid risk of falls in the fund. Benchmark is seven day LIBOR.	0.15%	Henderson Enhanced Sterling Liquidity Fund	Targets a higher return than current fund without compromising security or liquidity over the longer term. Benchmark is three month LIBID.	0.15%

The following is a summary of all the funds available for your normal pension and Additional Voluntary Contributions (AVCs). Further information can be found in the Scheme booklet.

Fund name	Investment risk	Inflation risk	Pension conversion risk	Offers protection against	Aim of the fund
Henderson Global (50/50) Enhanced Equity Fund	Medium to high	Low	High	Inflation	Good growth
Fidelity Global Equity Fund	Medium to high	Low	High	Inflation	Good growth
Legal and General Equity Index Fund	Medium to high	Low	High	Inflation	Good growth
Henderson Enhanced Balanced Fund	Medium	Low	High	Inflation	Steady growth
Standard Life Managed Fund	Medium	Low	High	Inflation	Steady growth
Henderson Global Bond Fund	Medium	Medium	Medium	Investment risk and inflation (partially)	Steady growth
Henderson Index Linked Bond Fund	Medium	Low	Low to medium	Pension conversion risk (partially)	Maintain pension buying power
Henderson Enhanced Sterling Liquidity Fund	Low	High	High	Investment risk	Steady performance

The following funds can only be used for AVCs.

Fund name	Investment risk	Inflation risk	Pension conversion risk	Offers protection against	Aim of the fund
Henderson Industries of the Future Fund	High	Low	High	Inflation	Good growth
Henderson Global Technology Fund	High	Low	High	Inflation	Good growth

## Pensions administration has been outsourced

The administration of the Pearl Group Staff Pension Scheme has now been outsourced to a third party provider, First Actuarial plc.

The current employees of Staff Pensions have transferred to First Actuarial and moved to a new office close to the Pearl Centre.

The award of the contract followed a rigorous selection process by the Trustee. The move took place during August and the new contact details can be found on page 12.

You will continue to receive the same administration service, since the current team have all transferred to First Actuarial, bringing their knowledge and experience of the Scheme with them.

To find out more about First Actuarial, you can visit their website at: [www.firstactuarial.co.uk](http://www.firstactuarial.co.uk)

## Pension increases

The Pearl Group Staff Pension Scheme operates a system of guaranteed pension increases. In accordance with the Scheme Rules, pensions in payment were increased by 3.2% on 1 April 2005 (2.5% on 1 April 2004). Deferred pensions were increased in line with the relevant Scheme Rules.

## Auditors' report

The Trustee can confirm that PricewaterhouseCoopers, the Fund's independent auditors, have confirmed that, in their view, the financial statements show a true and fair view of the financial transactions of the Scheme for the year ended 31 December 2005.

# Summary Funding Statement

## Final Salary sections only

### The last ongoing funding valuation

The most recent funding valuation of the pension Scheme showed that on 31 December 2003 the funding position (excluding Money Purchase section and AVC assets and liabilities) was as follows:

Assets	£1,663 million
Amount needed to provide benefits	£1,654 million
Excess	£9 million
Funding level	101%

There is no change in the rate of active members' contributions. If the Scheme had started winding up it is estimated that the assets available would have been sufficient to secure, on average, approximately 75% of benefits for members of the Final Salary sections. Inclusion of this information does not imply that Pearl Group Limited is thinking of winding up the Scheme.

There has not been any payment to Pearl Group Limited out of Scheme funds in the previous 12 months.

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

### Change in funding position

Using the same methodology as was used for the 31 December 2003 valuation of the Scheme, the Scheme Actuary has estimated that the funding level of the Scheme at 31 December 2005 was approximately 103%. The estimated funding level has improved since the 2003 valuation, mainly due to the better than expected investment returns on the Scheme's assets more than offsetting the increase in the value of the Scheme's benefits. At the next formal valuation the Actuary will review the funding position in more detail and it is likely that increasing life expectancy will be allowed for, which would reduce the funding level.

The next formal valuation of the Scheme is due to take place with an effective date no later than 31 December 2006. This will be the first valuation of the Scheme which will fall within the scope of the new Scheme specific funding requirements introduced by the Pensions Act 2004.

### How the Scheme operates

#### How is my pension paid for?

Pearl Group Limited pays contributions to the Scheme so that the Scheme can pay pensions and other benefits to Scheme members as they fall due.

The money to pay for the Final Salary benefits is held in a common fund. It is not held in separate funds for each individual.

#### How is the amount the Scheme needs worked out?

The Trustee obtains regular valuations of the benefits earned by members. Using this information, the Trustee comes to an agreement with Pearl Group Limited on future contributions.

### The importance of Pearl Group Limited's support

The Trustee's objective is to have enough money in the Scheme to pay pensions now and in the future. However, success of the plan relies on Pearl Group Limited continuing to support the Scheme because:

- Pearl Group Limited will be paying the future expenses of running the Scheme on an annual basis;
- the funding level can fluctuate, and when there is a funding shortfall, Pearl Group Limited will usually need to put in more money;
- if the target funding level should turn out not to be enough, Pearl Group Limited will need to put in more money.

### What would happen if the Scheme started to wind up?

If the Scheme winds up, you might not get the full amount of pension you have built up even if the Scheme is fully funded under our plan. However, whilst the Scheme remains ongoing, even though funding may temporarily be below target, benefits will continue to be paid in full.

If the Scheme were to start to wind up, Pearl Group Limited is required to pay enough into the Scheme to enable the members' benefits to be completely secured with an insurance company. It may be, however, that Pearl Group Limited would not be able to pay this full amount. If Pearl Group Limited became insolvent, the Pension Protection Fund might be able to take over the Scheme and pay compensation to members.

Further information and guidance is available on the Pension Protection Fund's website at [www.pensionprotectionfund.org.uk](http://www.pensionprotectionfund.org.uk). Or you can write to the Pension Protection Fund at Knollys House, 17 Addiscombe Road, Croydon, Surrey CR0 6SR.

### Why does the funding plan not call for full solvency at all times?

The full solvency position assumes that benefits will be secured by buying insurance policies. Insurers are obliged to take a very cautious view of the future and need to make a profit. The cost of securing pensions in this way also incorporates the future expenses involved in administration. By contrast, our funding plan assumes that Pearl Group Limited will continue in business and support the plan.

### What does the Scheme invest in?

The Trustee's policy is to invest in a broad range of assets in approximately the following proportions:

Bonds (including index-linked bonds)	58 %
Company shares	30 %
Property	12 %

During the year the Trustee switched further investments from equities to index-linked bonds. In the light of changed market conditions, the Trustee is actively reviewing its investment strategy.

### Where can I get more information?

If you have any other questions, or would like any more information, please contact the Scheme Administrators (contact details on page 12). A list of more detailed documents which provide further information is attached. If you want us to send you any of these documents please let us know. Please help us to keep in touch with you by telling us if you change address.

### Additional documents available on request

*The Statement of Investment Principles*, which explains how the Trustee invests the money paid into the Scheme.

*The Schedule of Contributions*, which shows how much money is being paid into the Scheme.

*The Annual Report and Accounts of the Pearl Group Staff Pension Scheme*, which shows the Scheme's income and expenditure in the year up to 31 December 2005.

The full report on the *Actuarial Valuation* following the Actuary's examination of the Scheme's financial situation as at 31 December 2003.

*An Annual Benefit Statement*. If you are an active member of the Scheme (and have not received a benefit statement in the previous 12 months) you can ask for a statement that provides an illustration of your likely pension.



## The Trustee and Advisers

The Pearl Group Staff Pension Scheme is managed by a Trustee company called P.A.T. (Pensions) Limited. There are six directors of P.A.T. of whom three are elected by active members. Member nominated directors are elected every six years and the next round of elections is due no later than December 2007.

### Trustee

P.A.T. (Pensions) Limited

### Trustee Directors

K Jones, FIA, MBA (Chairman)

T Cross Brown, MA, MBA

G S Felston, FCII, MBA

J Marshall-Robb, Chartered FCIPD

M J Mauchline, FCII

H Nawaz-Khan, FIA

Deferred Member

External Company appointment

Governance Director, Life Services (Member Nominated Director)

Director of Human Resources, Life Services

Pensioner Member (Member Nominated Director)

Deferred Member (Member Nominated Director)

### Secretary

L A Williams, MBA, APMI (until 31.03.06)

C L Wilson (appointed 01.04.06)

Head of Pensions, Henderson Group PLC

First Actuarial plc

### Assistant Secretary

A J Yates APMI

First Actuarial plc

(formerly Staff Pensions Technical Manager)

### Sponsoring Employer

Pearl Group Limited (formerly HHG PLC)

The Pearl Centre, Lynch Wood, Peterborough PE2 6FY

### Actuary

A F M Watson FFA (until 30.06.06); N Wearing FIA (appointed 01.07.06)

Watson Wyatt LLP

### Joint Legal Advisers

Pearl Group Services

Richards Butler

### Investment Advisers

Hewitt Bacon & Woodrow

### Investment Managers

Henderson Global Investors

For Money Purchase section only:

Fidelity Investments

Deutsche Asset Management

(until January 2005)

Standard Life

Legal and General (from May 2005)

### Auditors

Ernst & Young LLP

(until 6 September 2005)

PricewaterhouseCoopers LLP

(from 29 September 2005)

### Custodians

BNP Paribas Securities Services

### Bankers

HSBC Bank PLC

### Your contacts

If members have any queries concerning their benefits, they should contact the Scheme Administrators at:

First Actuarial plc,  
Pearl Group Staff Pension Scheme,  
38 Tyndall Court,  
Commerce Road,  
Lynch Wood,  
Peterborough PE2 6LR

Telephone: 08708 795100  
Fax: 08708 795200  
Email: [pearl@firstactuarial.co.uk](mailto:pearl@firstactuarial.co.uk)