

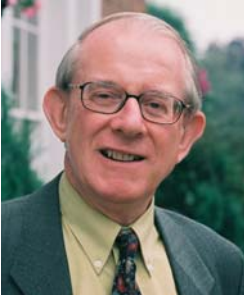
Special

newsbrief

September 2006

An update on developments and a summary of the financial health of the British Steel Pension Scheme

Chairman's Introduction



The past year has been a particularly challenging time for pension schemes and their trustees. There have been wide-ranging changes in pensions and tax law, introduced mainly in April 2006 against a background of extremely testing conditions for schemes including

volatile investment markets, lower anticipated investment returns, increasing life expectancy and the burden from the new regulatory environment. The legislative changes have a significant effect on the way pension schemes will operate in the years ahead and are already placing greater demands on trustees' time.

A new Pensions Regulator has been given the power to intervene in scheme matters. Trustees and the scheme sponsor will take on more responsibility for setting funding arrangements. New member nominated trustee requirements are to be introduced and trustees will be subject to a new code of practice on the levels of knowledge and understanding they must have to be able to act as a trustee.

One particular new feature to the regular updates on the Scheme's progress that you receive from the Trustee is that we must now provide members with a summary funding statement every year showing the scheme's financial health. The first statement is enclosed and, as required by law, reflects the position as at 31 March 2005. This was when the last formal three-yearly valuation was carried out by the Scheme Actuary but as the Trustees review the funding position informally each year, I have therefore included some more up-to-date figures in the statement. The annual pensions Newsbrief will be issued later in the year, as normal, and from next year it is intended that it will include the summary funding statement.

With all the change and activity going on, I am taking this opportunity to update you on Scheme developments generally and particularly what is being done by the interested parties to the Scheme to protect the security of the Scheme and improve its affordability and sustainability going forward. It should be noted that benefit changes are

in respect of service accrued on or after April 2006 and do not affect pensions earned before April 2006. Therefore benefits for existing pensioners and beneficiaries at 1 April 2006 are unaffected by the changes.

All the changes have involved a considerable amount of work for Scheme Officers at the Pensions Office in Glasgow. They have had to ensure that computerised administration systems and procedures were amended to reflect the new legislation and other changes. I am pleased to report that the work was completed successfully to time, thus ensuring continuity of service to Scheme members. Additionally, following the completion of the 2005 Actuarial Valuation, a review of our longer term investment strategy is being undertaken to ensure we have the right mix of assets to meet our liabilities. The Scheme Officers and the new Chief Investment Officer, Hugh Smart, at our Investment Office in London are currently extremely busy reviewing the investment strategy with the Scheme Actuary.

I thank my trustee colleagues on the Management and Investment Committees and all of those involved in the administration of the Scheme and Fund for their dedication and commitment to our pension arrangements. Our history of prudent and careful management of the Scheme continues to provide a strong foundation in our approach to Scheme matters.

Finally, I had planned to retire as Trustee Chairman this year on completion of the Actuarial Valuation. However with the amount of ongoing work and unfinished business I have agreed with the Company to remain as Chairman until completion of the February 2007 Trustee Meeting at which point I will be succeeded by Allan Johnston, who has been providing succession cover in recent years. In keeping with past tradition, I am happy to remain as a trustee for a further year to completion of the February 2008 Trustee Meeting in support of the new Trustee Chairman.

A handwritten signature in black ink, appearing to read 'Bob Avis'. The signature is stylized and cursive.

Bob Avis
Trustee Chairman



Introduction

In recent years there has been significant funding pressure on final salary pension schemes and a number of factors have contributed to increased costs and risks in operating this type of pension arrangement. The national trend to move away from final salary scheme membership for new entrants is continuing and there have been examples recently of this being extended to future pension accrual for existing members. The BSPS is in better shape than most schemes in the UK but it is not immune to current influences. Additionally the size of the Scheme when compared to the value of our sponsoring company, Corus, means that funding is extremely sensitive to changes in asset and liability values and therefore needs to be managed very prudently.

Changes to BSPS Pensions Package for Future Service

Employees

During 2005, a comprehensive consultation process took place between Corus and the National Trade Union Steel Co-ordinating Committee to consider the longer term challenges facing the Scheme and to improve the affordability and sustainability of the Scheme going forward.

This resulted in agreement to revise the benefit package for future service and increase members' contributions from 5% to 6% of pensionable earnings from 1 April 2006. From this date, Corus recommended cash contributions to the Main Section at the rate of 10% of pensionable earnings with a commitment that future Employer contributions would not be less than the members' ordinary contribution rate. The 10% rate is

supported by only a limited amount of actuarial surplus, with the balance retained within the Fund to give security against future volatility in Scheme funding.

Benefit changes have been made to reflect new legislation and a new pensions tax framework which are generally beneficial to Scheme members. Additionally, the main benefit changes agreed were in respect of early retirement terms for future service (no future service accrual for added years at 60 and less generous early retirement reduction factors) and capping at 4% per annum on the indexation of future service pensions. The resultant total headline rate of the future service package (without surplus support) was reduced by 3.5% of pensionable earnings to 18%. During the consultation process the parties agreed to set up a joint working group to look at possible options for new entrants.

All employees who are members of the Scheme were notified of the detail of the changes and pensions roadshows were conducted by Scheme Officers at all major sites, as part of a comprehensive communication exercise.

Separate from this consultation process, the Company closed the Supplementary Section for Senior Managers of the Scheme to new entrants and stopped bonuses being pensionable for external appointments to Group Senior Manager posts. Bonuses are not pensionable for Executive Directors but continue to be pensionable for other Scheme members, capped at 30% for pension purposes in any Scheme year.

Pensions in Payment

The changes do not affect pensions earned before April 2006. Therefore benefits for existing pensioners and beneficiaries at 1 April 2006 are unaffected by the changes.

Deferred Pensioners

Benefits for existing deferred pensioners at 1 April 2006 are generally unaffected by the changes, except in the following respects:

Higher tax-free retirement lump sums are now available under the new tax regime but, if there is an increase in the lump sum taken, the balance of pension to be paid will be lower.

Previously, on the death of a deferred pensioner, a child allowance could be paid up to age 25 where the child was financially dependent on the deceased member and remained in full time education. Under the new tax regime, new child allowances must cease on reaching age 23 unless dependency is on account of disability



Trustee Actions to address Costs and Risks

In the light of the increased funding pressures the Trustees have taken various actions during 2005/2006 to address costs and risks.

The practice of accepting individual transfer values in respect of pension entitlement from former employers and other external arrangements was stopped. The terms for granting service credits in the Scheme in lieu of transfer payments were based on actuarial assumptions and if these proved to be wide of the mark for an individual then there could be a strain on the Scheme from pay, investment, early retirement or life expectancy experience.

The terms of the in-house additional voluntary contribution arrangements were amended leading up to the closure of that arrangement to new contributors in April 2006.

The Inland Revenue recognise that the payment of small pensions can add a disproportionate cost to the administration of pension schemes and therefore allowed for pensions under £260 a year to be paid instead as a one-off lump sum. Over 6,300 members and beneficiaries accepted this option, mainly deferred pensioners. The criteria have changed under the new tax regime and the position is being assessed for any further opportunities to offer this type of option to members with small pensions.

The Trustee is continuing its audit checks to ensure that pensions are being paid to the correct people. Where there is clear evidence of fraud, cases are pursued rigorously and referred to the Scheme's solicitor for criminal or civil court action where necessary. The Trustees intend to supplement the current process by participating in the 2006/07 National Fraud Initiative (NFI), which is conducted by The Audit Commission. The data on the Scheme's records will be checked against registered deaths on the Department for Work and Pensions' database to identify pensions being paid despite a pensioner's death. Deferred pensioner records will also be checked for unreported deaths. The Data Protection Act 1998 requires the Trustee to inform Scheme pensioners and deferred pensioners that the NFI meets the requirements of data protection laws. The Audit Commission will process the data for this purpose only, complying with data protection principles.



Investment Strategy

Following completion of the 2005 Actuarial Valuation, the Actuary carried out a detailed study of the Scheme's assets and liabilities. This study projected assets and liabilities over a number of years using a range of investment scenarios and analysed the risks involved. The analysis helps the Trustee formulate its longer term investment strategy to meet the key objective of security of members' benefits. The Scheme's future investment strategy is currently being considered and will be subject to consultation with Corus, as the sponsoring employer, in the months ahead. The Scheme Actuary has also recommended that the Trustee considers carefully the strength of the sponsor covenant in determining investment strategy, particularly given the maturity of the Scheme and the size of liabilities when compared to the market value of Corus. Under the new regulatory environment, this is best achieved through an independent third-party assessment and the Trustee has commenced this process.

Investment Policy

Now and again members make representation to the Trustees on investment matters. Scheme membership is a broad body of people with many views and opinions on a whole range of matters including green issues, smoking, animal rights, armaments and political stances. It would be impossible for the Trustee to make investments that meet all these views while at the same time complying with the obligation to maximise financial returns. The basic principle upon which the Trustee acts is to make sound and proper investments on the grounds that they secure the funds needed to meet the pension obligations to the Scheme's members. The summary statement of investment principles is included in the Scheme's Annual Report and Accounts.

Fluctuations in Pensionable Pay

Significant increases in pensionable pay near retirement put a strain on the funding requirements of the Scheme and have a disproportionate impact on past service liabilities when compared to Members' contribution records. Unchecked these could undermine the security of benefits for other members. As a broad rule of thumb, every £1 added to pensionable pay in the run up to retirement has the potential to increase past service liabilities by £10.

The Rules of the Scheme provide that if the Company concludes that earnings paid to a Member include emoluments which are subject to abnormally wide fluctuation, then in determining that member's earnings under the Scheme, the fluctuating emoluments must be averaged over 3 years. The Rule, which was introduced a number of years ago as a condition for tax approval of the Scheme, protects the Scheme against disproportionate increases in pension liabilities and undue financial strain. Basic pay and shift allowances are not normally regarded as fluctuating emoluments and, generally, the two main fluctuating elements are bonus and overtime payments. It is very important that the Company applies controls on such elements of pensionable pay, as final pensionable earnings under the Scheme are based generally on the highest year in the last 5 years prior to termination of membership.

Bonuses to Group Senior Managers are subject to abnormally wide fluctuations and are averaged over 3 years for pension purposes. The combination of overtime and bonus payments can fluctuate significantly for other Members year on year and these cases are also subject to 3 year averaging. Scheme Officers check all cases of retirement and leaving and where there has been at least a 10% movement in gross earnings year-on-year, the general pattern of pay progression is reviewed. Where there have been unusual pay patterns or volatility a breakdown of pay components is obtained from the relevant Pay Office and each case is assessed individually for the application of the 3 year averaging rule.

Pension Protection Fund

The Pension Protection Fund (PPF) was introduced by the Government on 6 April 2005 to provide a safety net for members of defined benefit schemes whose employer becomes insolvent and whose scheme is in deficit with insufficient assets to buy-out the level of benefits for which PPF cover provides.

Funds to pay for the benefits guaranteed by the PPF are raised through compulsory levies on all schemes that are eligible for support. For 2006/7 the levy will be made up of two parts: 20% of the PPF comes from a scheme based levy and 80% from a levy based on the risk posed by a scheme to the PPF. The PPF running costs are funded through an additional administration levy based on scheme membership. The total levy payable by our Scheme for 2006/2007 is forecast to be around £1.4 million.

In many cases the benefits paid by the PPF will be limited. For individuals who have reached the Scheme's normal pension age prior to the scheme being assessed for PPF eligibility or, irrespective of age, are either in receipt of dependants' pension or incapacity pension, the PPF will pay a starting level of cover of 100% of the pension in payment. Normal pension age under the Scheme is usually age 65 unless an earlier age has been specified in a member's contract of employment. However, for members who have not yet reached normal pension age and who have not retired on the grounds of incapacity, benefits are restricted to the lower of 90% of their accrued benefits and the compensation cap (*£26,050 per annum adjusted downwards according to the age at which PPF benefit comes into payment*).

The PPF cover does not provide pension increases on pre-April 1997 accrual of pension.

To ensure consistency between the benefits that an individual would receive if their scheme fell into the PPF and if their scheme winds up outside of the PPF, the Government has amended the statutory priority order, that is who has first call on the Scheme's funds on any winding-up.

The previous statutory order of priorities gave priority to pensions in payment. However, this priority order can produce arbitrary results. Members who have not

yet retired may receive little or no pension where there are insufficient assets (*even if they are near to retirement and have been members of the scheme for many years*). The new priority order was introduced from 6 April 2005 and is designed to ensure that available assets are used mainly to provide the level of benefits that would be payable from the PPF for all members.

Operating as a closed fund, Scheme benefits would continue to be paid in full as and when they fall due until such time as there were insufficient assets to meet the PPF liabilities, at which time the Scheme would be assessed for membership of the PPF.

The Scheme Actuary has certified the funding level as at 31 March 2005 on a PPF basis as comfortably above the minimum funding level.

It is interesting to note that a forthcoming European Court judgment could potentially lead to pressure on the UK government to improve the benefits provided by the PPF so that all members' final salary benefits are covered in full. This outcome would have significant cost implications for PPF levies.

Further information is available on the PPF website at www.pensionprotectionfund.org.uk. Or you can write to the Pension Protection Fund at **Knollys House, 17 Addiscombe Road, Croydon, Surrey CR0 6SR.**



Civil Partnerships

The Civil Partnership Act 2004 came into force on 5 December 2005 and introduced the opportunity for same-sex couples to gain legal recognition of their relationship. Civil partners now have rights and responsibilities that affect insurance and pension provision, state benefits, tax, ownership of property and family responsibilities. This is overriding legislation and therefore from now on where a Scheme member forms a civil partnership and the partner survives the member, the Scheme will pay the surviving partner this new pension entitlement as required by law.

Annual Summary Funding Statement Explaining the Financial Health of the Scheme

On the basis of the Ongoing Funding Valuation

The past service funding level at the valuation on 31 March 2002 was 111%.

The latest actuarial valuation of the Scheme showed that on 31 March 2005:

The Scheme's assets were valued at:

£8,096 million

*The value of the Scheme's past
service liabilities was:*

£7,682 million

*This means that there was an
actuarial surplus of:*

£ 414 million

*And past service funding level was
therefore:*

105%

The decrease was attributable to a number of factors but mainly

- the abatement to employers Main Section contributions
- further allowance made for members to live longer
- membership changes and additional voluntary contribution take-up
- freezing of the LEL deduction from pay for a further 3 years
- one-off cost in stopping the further accrual of added years at 60

These factors were offset in part by a reduction in the assumed future rate of pay growth.

The Company recommenced contributions at the rate of 10% of pensionable earnings in respect of members of the Main Section, with effect from 1 April 2006 and continued to pay at the rate of 12.3% of pensionable earnings for members of the Acquisition Section. Members' contributions were increased from 5% to 6% of pensionable earnings from 1 April 2006.

A very broad estimate of the updated position of the Scheme was made on 31 March 2006 using the same actuarial assumptions as in 2005 and allowing only for investment experience. This showed that the funding level had improved to about 110%, reflecting strong investment performance. Had it been a formal valuation, the assumptions would have been reviewed in the light of market conditions. Given the very strong investment returns, it is very likely that the assumed future investment returns would have been cut back, thus reducing the funding level. The value of the Scheme's assets at 31 March 2006 had risen to £9,218 million but investment markets have fallen back since then and the current funding position is estimated to be close to the 2005 outcome.

The Trustees will continue to monitor the financial position of the Scheme on a regular basis and the next formal valuation is scheduled for 31 March 2008.

On the basis of the Scheme Winding Up

The Trustees are required by law to provide information on the Scheme's solvency position:

If Corus were to become insolvent and in the unlikely event of buying annuities through insurance companies, the Scheme's assets at the valuation date on 31 March 2005 would have been sufficient to provide only 93% of the Scheme's total liabilities. The estimated amount required to buy-out benefits in full would be about £8,730 million. The more likely scenario is that the Scheme would be run as a closed scheme thereby avoiding the additional buy-out costs charged by insurance companies. On this basis the Scheme was broadly in balance.

If Corus decided, as a going concern, to discontinue the Scheme then it would have to make good the buy-out deficit.

Points to note:

- The money to pay for members' pensions is held by the Trustees in a common fund. It is not held in separate funds for each individual.

- There has not been any payment to Corus out of Scheme funds in the last 12 months nor at any other time in the past.

Further Information

Enquiries:

If you have a question about the Scheme generally or on the information provided in this statement please contact the Pensions Office.

The following primary Scheme documents are available on request:

Annual Report & Accounts for year ended 31 March 2006

Full Report on the Actuarial Valuation of the Scheme as at 31 March 2005



Change of address:

It is very important if you change your address that you confirm your new details to the Pensions Office as soon as possible, otherwise it may not be possible to keep you up-to-date with Scheme developments.

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Contacting the Pensions Office

When you contact the Pensions Office, please quote your Membership Number as this will help us to answer your enquiry as promptly and efficiently as possible.



In writing

British Steel Pension Scheme

6th Floor, Sentinel, 105 Waterloo Street

Glasgow G2 7BW

If you live in the UK, you can write to the Pensions Office using our Freepost facility, so there is no need for a stamp.

Your envelope should state the following:

British Steel Pension Scheme

Freepost RLXS-ZXKT-AUER

6th Floor, Sentinel, 105 Waterloo Street

Glasgow G2 7BW

Pensioners living outside the UK can write to the Pensions Office at:

British Steel Pension Scheme

6th Floor, Sentinel, 105 Waterloo Street

Glasgow G2 7BW, Scotland,

United Kingdom



By telephone

The Pensions Office aims to make it as easy as possible for you to contact it.

All UK calls to the Pensions Office will be charged at local rates:

If your surname begins

A - K, please call 0845 274 0900.

If your surname begins

L - Z, please call 0845 274 0901.

Dialling from outside the UK:

If your surname begins A - K, please call +44 141 274 2222.

If your surname begins L - Z, please call +44 141 274 2266.

Standard office hours are 8.45 am to 4.45 pm Monday to Friday. If you telephone outside these times or during statutory holidays, you will normally hear a recorded message giving details of when we can be contacted. You also have the option of leaving a message, which we will reply to as soon as possible.



By fax

You can fax your enquiry to us on **0141 248 5299**



By email

You can send an email to us at:

pension.enquiries@corusgroup.com



Website

Our website provides general information about the Scheme. The website address is: **www.bspensions.com**