

benefits & YOU

The Northrop Grumman UK Pension Scheme

February 2007

INSIDE

- Membership1**
- Pension Scheme Update2**
- Movement of the Fund3**
- Investment Section4**
- Bringing Pensions into the 21st Century5**
- Trusteeship of the Fund5**
- Useful Addresses6**

Introduction

The Trustees of the NG UKPS welcome you to the newsletter for members of the Scheme. This newsletter is designed to bring you up to date with what has been happening in relation to the Scheme in the recent past. As you will be aware, it has been a very busy period in the UK pensions world, with significant new legislation introduced — including Government initiatives to improve the security of your pension benefits. This newsletter provides highlights from the last Trustees’ formal report and accounts, which covers the year to 31 December 2005. We also provide useful links and addresses for your information. If you have any suggestions for future issues, please write to us at the contact address shown on the back.

Membership

Active members at 1 January 2005	318
< Add	
Members joining during the year	22
> Less	
Leavers taking a refund	(10)
Leavers with a deferred pension	(29)
Retirements	(7)
Deaths	(1)
Active members at 31 December 2005	293
Pensioners at 31 December 2005	173
Deferred members at 31 December 2005	272
Total Membership at 31 December 2005	738

Prepared especially for participants of the Northrop Grumman UK Pension Scheme

Pension Scheme Update

Implementation of “A-Day” Changes

You will have received earlier notification of Scheme changes which were introduced as a consequence of Pensions Act 2004 and Finance Act 2004.

As a reminder, from 6 April 2006, the following changes have been made to the Scheme:

- Members can now take tax-free cash at retirement of up to 25% of the value of their benefits. Subject to this overall limit, members who started paying AVCs before 7 April 1987 can take 25% of the value of their AVCs as cash instead of pension.
- Members are now able to make contributions to any number of retirement savings arrangements, including Stakeholder plans and personal pension arrangements, subject to the overall limits of the Lifetime and Annual Allowances. You can also invest in the Northrop Grumman Stakeholder Plan by payroll deduction. For the tax year 6 April 2006 – 5 April 2007, the Annual Allowance is set at £215,000.

- Members can build up benefits on a tax-advantaged basis up to the Lifetime Allowance starting at £1.5 million on 6 April 2006. The Lifetime Allowance applies to an individual's total retirement savings from all registered arrangements. Benefits over the Lifetime Allowance will be subject to a 25% recovery charge (in addition to income tax).
- A Scheme earnings cap has been introduced. This currently mirrors the earnings cap applied by the HM Revenue & Customs before 6 April 2006 and will initially be set at £108,600. The current intention is that it will be increased on an annual basis in line with inflation, although this is subject to review in the future.
- The increases applied to benefits in payment from the DB Section of the Fund will, in respect of benefits earned from 6 April 2006, be equal to the increase in the Retail Prices Index (RPI) to a maximum of 2.5%.
- The earliest age at which you can retire will move to age 55 beginning in April 2010.

The new rules will apply to all tax-approved retirement benefits – including benefits earned up to 6 April 2006 – in place of the previous rules.

Extra Security for Pension Scheme

There have been a number of legislative changes, with the broad purpose of improving the security of members' pensions.

If the Plan were to start to wind up, the participating companies would be required to pay enough into the Plan to enable members' benefits to be completely secured with an insurance company.

It may be, however, that the participating companies would not be able to pay this full amount. If the companies were to become insolvent, the Pension Protection Fund (PPF) might be able to take over the Plan and pay compensation to members, although this compensation is likely to be less than the benefits provided for under the Scheme rules.

The PPF was introduced by the Government to protect the benefits of members of certain pension schemes on the insolvency of the sponsoring employer.

Summary Funding Statement

All members of the Scheme should have received a copy of the Trustees' Summary Funding Statement. This statement sets out the most recent measure of the Scheme's solvency in the circumstances where either the Scheme continued with Company support or where the Trustees had to discontinue the Scheme because the Company was no longer able to support the Scheme.

This statement is updated and circulated each year. In particular, the next statement will have details of the results of the formal actuarial valuation as at 31 December 2005. This formal valuation is performed on a three-yearly basis, the value of assets to the value of the benefits due to be paid out now and in the future. The results are currently being finalised and will be made available during the second quarter of 2007.

If you have any questions about the Summary Funding Statement, or if you did not receive your copy, please contact your HR manager in the first instance.

Age Discrimination

From 1 October 2006, new age discrimination legislation came into force that means employers cannot discriminate against employees, prospective employees and trainees because of their age. The legislation relating to pensions came into force from 1 December 2006, and could impact the benefits provided by pension schemes.

The Trustees and the Company have reviewed the Scheme's rules, policies, practices and procedures to identify any issues that need to be addressed. Only one benefit change was required at this stage, which is to allow death in service lump sum benefits to continue for any members working beyond their normal retirement age.

Movement of the Fund

Fund at 1 January 2005	£37,689,123
Income	£3,667,944
Expenditure	£1,970,842
Excess of Income over Expenditure	£1,697,102
Investment Returns	£6,692,553
Fund at 31 December 2005	£46,078,778

The estimated value of Scheme assets as at 31 December 2006 is £58.3 million. This includes a special Company payment into the Scheme following the departure of two participating employers during the last 12 months. More details will be available once the 2006 accounts have been audited.

Reminder

Expression of Wish Forms

One of the benefits provided to you under the Scheme is a lump sum payment, made to one or more beneficiaries, if you die in active service. Under current legislation, there is usually no liability for inheritance tax on this benefit, provided that the beneficiary of the lump sum is selected at the Trustees' discretion. When exercising their discretion on this decision, the Trustees will consider your wishes as indicated on your Expression of Wish form, although they cannot be legally bound by your wishes. **It is important that you keep this form up to date.** If there are any changes in your circumstances, you should provide an updated Expression of Wish form. Forms can be obtained at any time from the Human Resources Department.

Civil Partnerships

The Civil Partnership Act became effective from 5 December 2005. This legislation allowed same-sex couples to register their relationship. Registered Civil Partnerships can end only on death of a partner or formal dissolution. If you have a civil partner, that person is now entitled to the same benefits from the Scheme as those to which a spouse would be entitled. If the registered civil partnership comes to an end, the ex-civil partner is treated in the same way for pension-sharing purposes as an ex-spouse would be. Please ensure that you notify the Human Resources Department if you have a civil partner and that you update your Expression of Wish form.

Investment Section

In the first half of 2004, there were a number of changes made to the investment arrangements of the Scheme. Firstly, the investment strategy was altered, and a fixed split of 80% equities and 20% bonds was adopted. This was a change from the previous strategy, which was based on a flexible asset split between equities, bonds and cash. Secondly, the investment managers were changed: JPMorgan, Invesco and Legal & General were all terminated, with their assets being transferred to Capital International and PIMCO, who began managing them in line with the new investment strategy. Capital were appointed to manage the UK and Overseas equities, and PIMCO were appointed to manage the Bond assets. These two managers were chosen following advice from the

Scheme's consultant, who positively rated their investment capabilities, and due to the preferential fee schedule which was offered to the Scheme as a result of our wider corporate relationship with these two managers.

The table below shows the performance of the Scheme's investment managers from inception of the performance measurement for the revised investment arrangements on 31 March 2004 and for the 12 months of 2006:

The Trustees meet with the managers at least once a year to review performance. Although disappointed with the recent performance, the Trustees believe the managers have the ability to outperform in the future, but will continue to closely monitor performance.

Investment Performance

Asset Class	Managers	Quarter		Since Inception	
		Fund (%)	Benchmark (%)	Fund (% p.a.)	Benchmark* (% p.a.)
UK Equities***	Capital	15.9	16.6	15.4	18.4
Overseas Equities	Capital	4.2	5.2	10.3	12.2
Bonds	PIMCO	-0.2	0.7	4.4	5.0
Total Scheme**		6.3	7.3	10.6	12.6

Source: Respective Investment Managers and Mellon Analytical Solutions. Gross of Fees.

* Benchmark is a standard against which performance is measured.

** Total Scheme and benchmark figures calculated by Mercer Investment Consulting.

*** Includes the returns of the UK equity allocation within the global equity mandate.

Bringing Pensions into the 21st Century

For some time now, it has been accepted that the pension system in the UK has needed a major overhaul. So the Government published a Pensions Bill on 29 November 2006, intended to implement the proposals for state pension reform detailed in its White Paper "Security in Retirement: Towards a New Pension System", which aimed at strengthening pension provision in the UK.

The Bill follows a three-year investigation by Lord Turner. The main aim of the change was to increase personal savings and reduce the growing dependence of pensioners on means-testing.

The proposals are:

(i) State Pension

Fundamental changes will be made to improve the state scheme and ensure its long-term affordability:

- The state pension age will rise gradually: from 65 to 66 by 2026; to 67 between 2034 and 2036; and to 68 between 2044 and 2046.
- The basic state pension will be uprated in line with average earnings, rather than inflation. At the moment, state pensions are increased in line with inflation, not earnings, and this has meant that the income gap between pensioners and the working population has increased. This change will come into effect from a future date to be determined, but expected to be between 2012 and 2015.

- The eligibility rules for basic state pension will be amended to make it easier for people who take breaks from employment, or who have responsibilities as carers, to accrue their full entitlement.

(ii) Pension Savings Accounts

As many as nine million people are estimated not to be saving enough for retirement, and consequently it has become an accepted fact that more needs to be done to encourage people to make additional savings for their old age. The Government's response to this is to propose the establishment of a semi-compulsory system of pension saving in the form of new, low-cost pension savings accounts:

- All companies will automatically have to enrol workers in the scheme at the age of 22 unless they have a more generous scheme such as the NG UKPS, which already enrolls workers automatically.
- Companies will have to make a compulsory 3% contribution of salary to the scheme, with employees paying 5% (on earnings between £5,000 pa and £33,000 pa).
- The money will be invested on behalf of employees in a variety of savings vehicles, such as investments in stocks, bonds, and property.
- To minimize charges, personal accounts will be delivered via a central clearing house, which will outsource the investment and administration.

The intention is that most of these reforms will not be introduced for some years, and much of the detail is still to be worked out. No doubt there will be plenty of related news items appearing in the media over the coming months, and the Trustees will keep members informed.

Trusteeship of the Fund

Fund Trustees

To safeguard the benefits earned by members of the Scheme, the Scheme's assets are held under a Trust and are invested separately from the Company's assets.

The current Scheme Trustees are:

- Stephen Hanson – NGC International Inc. – Corporate Director of Human Resources, Europe-Asia (UK-based)
- Lucy Shippey – Northrop Grumman Sperry Marine – Human Resources Manager (UK-based)
- Dennis Wootan – Corporate Director Benefits Analytic Services & International Programs (US-based)
- Bill Allis – Park Air Systems Limited – Technical Director (UK-based)

Trustees' Advisers

The Trustees have appointed the following professional advisers to assist them in day-to-day operation of the Scheme:

- Pension & Investment Consultants and Administrators — Mercer Human Resource Consulting Limited

- Scheme Actuary — Paul Gouling, FIA, employed by Watson Wyatt Limited
- Investment Managers — Capital International Limited and PIMCO
- Legal Adviser — CMS Cameron McKenna*
- Auditor — Chantrey Vellacott DFK**

* Following a Trustee review, it was agreed that to ensure independent advice and avoid potential conflict of interest, the previous legal advisers, Eversheds, were replaced.

** Following a Trustee review, the previous Scheme auditors, Deloitte & Touche, were replaced in December 2006.

Fund Governance

The Pensions Regulator takes an active role in promoting the good governance of pension schemes. This includes the issue of guidance and codes of practice in areas such as trustee training, reporting, scheme funding and risk management.

The Trustees take their responsibilities seriously, and undertake training from their advisers on a regular basis.

The Trustees have also considered the risks that the Fund is exposed to, and have compiled a list of the risks, in conjunction with the Company. Having recognised the risks that the Scheme is exposed to, the Trustees have also put in place controls to mitigate these risks.

Useful Addresses

The Pensions Advisory Service (TPAS)

The Pensions Advisory Service (TPAS) is available to assist members

and beneficiaries of the Fund in connection with any pensions query they may have, or difficulties which they have failed to resolve with the Trustee or administrators of the Fund. TPAS can be contacted through any Citizens Advice Bureau or at 11 Belgrave Road, London, SW1V 1RB. www.pensionsadvisoryservice.org.uk.

Pensions Ombudsman

If TPAS is unable to resolve any disputes between members or beneficiaries and the Trustees or administrators of the Fund, the member or beneficiary may refer the matter to the Pensions Ombudsman. The Pensions Ombudsman may investigate and determine any complaint or dispute of fact or law in relation to pension schemes. The complaint may be made by or on behalf of a member or beneficiary of the Fund. The Pensions Ombudsman may be contacted at First Floor, 11 Belgrave Road, London, SW1V 1RB. www.pensions-ombudsman.org.uk.

The Pension Tracing Service

A pension tracing service is carried out by the Department for Work and Pensions. The service has access to a database of over 20,000 occupational pension schemes and can help individuals to find details about old pensions; for example, with previous employers. If at any time you lost contact with the Trustees of the Fund, this service can help you to trace them. The service can be contacted at Pension Tracing Service, The Pension Service, Tyneview Park, Whitley Road, Newcastle upon Tyne NE98 1BA www.thepensionsservice.gov.uk

The Pensions Regulator

From 6 April 2005, the statutory body that regulates occupational pensions is The Pensions Regulator (TPR). The objectives of TPR are to protect the benefits of members of work-based occupational schemes and encourage high standards and good practice in running pension schemes. TPR has broad powers to collect data to help in their risk assessments, investigate schemes and issue directions and orders to ensure necessary actions are taken by scheme managers. TPR will not resolve disputes from scheme members. TPR's address is Napier House, Trafalgar Place, Brighton BN1 4DW. www.thepensionsregulator.gov.uk.

Contact Information

If you would like further information about your own benefits or have any questions about the Scheme, please contact any of the Trustees directly or through Mercer Human Resource Consulting Limited at the address below:

**The Trustees of The Northrop Grumman UK Pension Scheme
c/o Mercer Human Resource Consulting Limited**

**5 Bedford Park
Croydon
CR0 2AQ**

This newsletter is a summary of the formal Trustees' Report and Accounts for the year to 31 December 2005, which can also be obtained by writing to the Trustees.