

**ISLE OF MAN LOCAL
GOVERNMENT PENSION
SCHEME**

**ANNUAL REPORT
AND
ACCOUNTS**

31 MARCH 2003

Being a public service pension scheme as defined by the Pension Schemes Act 1993, the Isle of Man Local Government Pension Scheme is statutorily exempt from the overriding provisions relating to the issue and content of a pension scheme's annual report; nevertheless, every effort has been made to ensure that this Report meets the major requirements imposed on other schemes, allowing for the differences between statutory schemes and those operating under trust. Furthermore, the financial statements have been prepared in accordance with the guidelines set out in the Statement of Recommended Practice, "Financial Reports of Pension Schemes", as far as is practicable.

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ISLE OF MAN LOCAL GOVERNMENT PENSION SCHEME

ANNUAL REPORT AND ACCOUNTS

FOR THE YEAR ENDED
31 MARCH 2003

Administering Authority

Mayor, Aldermen and Burgesses of the Borough of Douglas

Town Clerk and Chief Executive

Mr D R King, LL.B. F.I.Mgt.

Borough Treasurer

Mr G M Bolt, C.P.F.A

Auditors

KPMG Audit LLC
Heritage Court
41 Athol Street
Douglas
Isle of Man. IM99 1HN

Scheme Administrator

Capita Hartshead
257 Ecclesall Road
Sheffield. S11 8NX

Bankers

Isle of Man Bank
Athol Street
Douglas
Isle of Man IM99 1AN

Investment Manager

Merrill Lynch Investment Managers
Belgravia House
34/44 Circular Road
Douglas
Isle of Man. IM1 1QW

Consulting Actuary

Hymans Robertson.
221 West George Street
Glasgow. G2 2ND

Custodian of Securities

RBSI Custody Bank Limited

REPORT BY THE MAYOR, ALDERMEN AND BURGESSES OF THE BOROUGH OF DOUGLAS

INTRODUCTION

The Isle of Man Local Government Pension Scheme (“the Scheme”) is a statutory public service pension scheme (as defined by the Pension Schemes Act 1993) under the Isle of Man Local Government Pension Scheme 1996 (“the 1996 Scheme”) which provides retirement and dependants’ benefits for employees of Local Government employers and Admitted Bodies on the Isle of Man.

The Scheme is contracted-out of the State Earnings Related Pension Scheme (“SERPS”) and is exempt approved for the purposes of the Income Tax (Retirement Benefit Schemes) Act 1978 and Part I of the Income Tax Act 1989 (Acts of Tynwald). Full tax relief is granted on members and the employers’ contributions paid to the Scheme and on all investment income.

MANAGEMENT

The Administering Authority’s Responsibilities

The Mayor, Aldermen and Burgesses of the Borough of Douglas (“the Borough”) are the administering authority for the Isle of Man Local Government Pension Scheme. They are responsible for obtaining audited financial statements for each financial year which give a true and fair view of the financial transactions of the Scheme and the disposition of its assets and liabilities at the year end. In preparing the financial statements the Borough have:

- selected suitable accounting policies and then applied them consistently;
- made judgments and estimates that are reasonable and prudent; and
- followed applicable accounting standards, in particular the Statement of Recommended Practice, “Financial Reports of Pension Schemes”, subject to any material departures described in the financial statements.

The Borough are responsible for keeping proper accounting records which disclose, with reasonable accuracy at any time, the financial position of the Scheme.

The Borough are also responsible for keeping records of contributions received in respect of active members of the Scheme and for procuring that contributions are made to the Scheme in accordance with the recommendations of the Consulting Actuary.

In addition, the Borough are responsible for safeguarding the assets of the Scheme and hence for taking reasonable steps for the prevention and detection of error, fraud and other irregularities.

REPORT BY THE MAYOR, ALDERMEN AND BURGESSES OF THE BOROUGH OF DOUGLAS – continued

MANAGEMENT (continued)

General

Responsibility for managing the Scheme's investments has been delegated to Merrill Lynch Investment Managers ("Merrill Lynch").

The Borough have a contractual arrangement with Capita Hartshead, a trading division of Capita Business Services Limited, to undertake the day to day administration of the Scheme.

ADMINISTRATION

Changes to the Regulations Affecting the Scheme

The Isle of Man Local Government Superannuation Scheme Regulations 2003 were enacted on 20 February 2003. They apply to individuals who were contributing members of the IoMLGPS on 1 April 2003 or who have since joined the Scheme. The Scheme is based on the regulations that applied to England and Wales with effect from 1 April 1998, and some provisions are effective from that date.

The Scheme Rules and Benefits are set out later, and the full details are shown in the Guide provided to all members.

Pensions Increase

Pensions in payment and preserved benefits are subject to annual review under the Pensions (Increase) Act 1974 (an Act of Tynwald). The Pensions Increase (Review) Order 2003 required an increase of 1.7% (2002: 1.7%) (reduced proportionately for pensions in payment for less than 12 months) to be awarded from 7 April 2003 (8 April 2002). This corresponds to the increase applied to State retirement pensions and pensions paid by other public service pension schemes on the Island, being the rise in the UK's Retail Prices Index during the 12 months ended 30 September 2002 (30 September 2001).

REPORT BY THE MAYOR, ALDERMEN AND BURGESSES OF THE BOROUGH OF DOUGLAS – continued

ADMINISTRATION (continued)

Myners' Review

A major issue affecting all occupational pension schemes is the review undertaken by Mr Paul Myners, the details of which are contained within a document titled "Institutional Investment in the UK: A review" and which has been endorsed by the UK Government and accepted as best practice by the Pensions Committee. As part of this review, 10 principles have been established as being key in terms of how Trustees manage pension schemes. These principles relate to the following matters:

- Effective decision making
- Setting clear objectives for the Fund
- Focusing on strategic asset allocation investment decisions
- Receiving expert advice
- Having explicit mandates for investment management contracts
- Taking an active approach relative to corporate governance
- Establishing appropriate benchmarks for investment returns
- Measuring investment performance
- Ensuring transparency relative to investment objectives, asset allocation, investment related fees
- Regular reporting to Scheme members

These principles are being reviewed by the Pensions Committee and where appropriate actions taken to improve the management of the Scheme.

REPORT BY THE MAYOR, ALDERMEN AND BURGESSES OF THE BOROUGH OF DOUGLAS – continued

MEMBERSHIP AND BENEFICIARIES

	2003	2002
	No.	No.
Active Membership At 1 April 2002	371	374
Backdated members	2	-
<i>Add:</i>		
Entrants - new starters	59	43
	<u>432</u>	<u>417</u>
<i>Less:</i>		
Exits - options pending	-	(2)
- new retirement pensions	(8)	(13)
- deaths in service	(1)	(2)
- preserved benefits	(19)	(17)
- refunds of contributions/transfers	(12)	(12)
	<u>(40)</u>	<u>(46)</u>
At 31 March 2003	<u>392</u>	<u>371</u>

REPORT BY THE MAYOR, ALDERMEN AND BURGESSES OF THE BOROUGH OF DOUGLAS – continued

MEMBERSHIP AND BENEFICIARIES - continued

Active Membership as at 31 March 2003

	Active	Deferred	Pensioners	2003 Total	2002 Total
Andreas Commissioners	0	0	0	0	0
Arbory Commissioners	0	0	0	0	0
Ballaugh Commissioners	0	0	0	0	0
Braddan Parish Commissioners	3	0	0	3	0
Vicars & Wardens of Braddan Church	1	1	0	2	2
Bride Commissioners	1	0	0	1	0
Castletown Commissioners	12	1	4	17	16
Castletown & Malew Elderly Persons Housing Board	0	0	0	0	0
Cooil Roi Housing Authority	0	0	0	0	0
Crossroads Caring for Carers	4	0	0	4	4
Borough of Douglas	208	61	106	375	360
German Commissioners	0	0	0	0	0
Jurby Commissioners	0	0	0	0	0
Kirk Michael Commissioners	1	0	0	1	0
Laxey Commissioners	0	0	0	0	0
Leonard Cheshire Foundation	4	3	0	7	5
Lezayre Commissioners	0	0	0	0	0
Lonan Commissioners	0	0	0	0	0
Malew Parish Commissioners	3	2	1	6	4
Manx Blind Welfare	0	1	0	1	1
Manx Foundation for Physically Disabled	1	1	0	2	2
Marashen Crescent Housing Committee	3	1	0	4	5
Marown Commissioners	0	0	0	0	1
Manx Churches Adoption & Welfare Society	3	2	0	5	6
Maughold Commissioners	0	0	0	0	0
Northern Local Authorities Swimming Pool Board	6	1	1	8	7
Northern Parishes Refuse Collection Board	0	0	0	0	0
Onchan District Commissioners	44	15	13	72	67
Patrick Commissioners	0	0	0	0	0
Peel & Western District Housing Committee	0	1	0	1	1
Peel Town Commissioners	17	5	2	24	24
Port Erin Commissioners	14	6	1	21	21
Port St Mary Commissioners	10	6	3	19	18
Ramsey Town Commissioners	37	13	13	63	58
Ramsey & Northern District Housing Committee	7	1	0	8	8
Rushen Commissioners	0	0	0	0	0
Santon Commissioners	0	0	0	0	0
Southern Civic Amenity Site Board	3	0	0	3	0
Southern Local Authorities Swimming Pool Board	7	3	3	13	13
The Vicars & Wardens of St Peters Church Onchan	1	0	0	1	1
Department of Tourism & Leisure – Villa Marina	2	0	0	2	1
Western Swimming Pool Board	0	0	0	0	0
Total	392	124	147	663	625

REPORT BY THE MAYOR, ALDERMEN AND BURGESSES OF THE BOROUGH OF DOUGLAS – continued

ACTUARIAL VALUATION

The 1996 Scheme requires an actuarial valuation of the Scheme to be carried out every three years. The purpose of a valuation is to review the funding position and determine an appropriate level of employers' contributions.

In accordance with the 1996 Scheme, a valuation of the Scheme was made as at 31 March 2001 which showed that it continued to be in deficit.

The Actuarial Statement is reproduced on pages 15 to 16 of the Annual Report.

REGISTRATION UNDER THE DATA PROTECTION ACT 1986 (An Act of Tynwald)

The data provided by members on their starter's forms is processed using computers. The use of the data is registered under the Data Protection Act 1986 for the purposes of pensions administration by the Borough and of personnel/employee administration by the employers.

D W CHRISTIAN, JP
Chairman
Policy and Resources Committee
Borough of Douglas

11 August 2003

G M BOLT, CPFA
Borough Treasurer
Borough of Douglas

11 August 2003

INVESTMENTS

INVESTMENT LIMITS

The Isle of Man Local Government Superannuation Scheme Regulations 2003 require the Borough to immediately invest any monies not needed to make payments from the Scheme. In doing so, it prescribes the limits on the type and extent of investments which the Borough may pursue.

Although they may vary the types of investment adopted the Scheme's investment policy must be formulated with a view to:

- the advisability of investing Scheme money in a wide variety of investments; and
- the suitability of particular types of investments.

However, of the total value of the Scheme's investments no more than the percentages shown below can be invested in the form of investment described:

- **1%** - a single sub-underwriting contract, i.e. a contract with a person who is underwriting a share issue to acquire the shares from him if that's what he requires, but with the total value of all sub-underwriting contracts not exceeding 15%;
- **2%** - as a limited partner in any single partnership (but not exceeding more than a total of 5% in such partnerships);
- **10%** - loans made to other than the Government of the Isle of Man, or Her Majesty's Government;
 - total investments in unlisted securities, i.e. securities not quoted on a recognised stock exchange;
 - total deposits with any single bank, or similar institution except the National Savings Bank; and
 - any single holding unless the investment is made by an external investment manager in a unit trust scheme;
- **35%** - all investments in unit trust schemes;
 - all investments in open-ended investment companies where the collective investment schemes constituted by the companies are managed by any one body;
 - all investments in unit trust schemes and open-ended investment companies where the unit trust schemes and the collective investment schemes constituted by those companies are managed by any one body;
 - the total value of all insurance contracts; and
 - all securities (shares, stocks, debentures, etc) which the Borough transfer or agree to transfer under stock lending arrangements.

INVESTMENTS - continued

INVESTMENT STRATEGY AND MANAGEMENT

The investment strategy developed by the Borough aims to maximise the return of the Scheme by diversifying its investments throughout world markets. It is applied by their investment manager, Merrill Lynch, which has full discretion in the management of the portfolio subject to complying with the statutory limits and the ranges of asset distribution defined by the Borough.

INVESTMENT PERFORMANCE

Portfolio	-15.9%
Benchmark	-14.8%
Value of Portfolio as at 31 March 2002	£12,311,526
Value of Portfolio as at 31 March 2003	£11,380,867

Benchmark

The benchmark is used as a reference point to compare the performance of the portfolio. It allows the overall performance of the Fund Manager to be compared with the overall performance of the various indices. Any divergence between the benchmark and the Scheme's return is due to the preferences of the Fund manager.

INVESTMENT MANAGER'S REPORT

Summary

The Portfolio fell, by 15.9% over the year compared with a benchmark fall of 14.8% mainly due to the Fund's overseas exposure which was relatively weak during what was a highly volatile year.

The Fixed Interest holdings outperformed their benchmark, rising by 13.6% compared with a rise of 13.1%. A weak start to the year was followed by stronger performance the second half as equity markets fell heavily.

UK equities underperformed their benchmark by 0.7% during the year. Performance was hindered by the Fund's exposure to a number of blue chip quality companies which fell out of favour.

Financial Background

The year to the end of March 2003 proved to be extremely volatile, with the early part of the period seeing markets fall heavily due to concerns over corporate governance, particularly in the US, where Enron and WorldCom shocked the investment community. The summer of 2002 saw these concerns amplified, as investors became concerned about the slow pickup in global economic activity.

INVESTMENTS - continued

Financial Background (continued)

Following these sharp falls experienced, the final quarter of 2002 started with a flourish, as investors perceived that those falls had left certain areas of the market showing good value for the long-term. A particular focus driving the rally was the US earnings season, where companies met low expectations.

However, the conflict in the Middle East dominated the first quarter of 2003, with prices tumbling and bouncing in response to the latest 'embedded' news reports. Shares fell as worries about the impending conflict and corporate governance issues in Europe dominated headlines. Falls were especially sharp in Europe, in particular the UK market was down more than 16.5% at one stage.

UK Equities

The UK portion of the Fund declined 30.6% over the period slightly underperforming the FTSE All Share which fell 29.8%. On a relative basis, the more defensive sectors outperformed with utilities, consumer staples and non-cyclical services all falling less than the index. The sharpest falls were seen in the high beta sectors such as technology and general industrials, the former suffering from a collapse in demand and over extended valuations, whilst the latter was hit by a series of company specific incidents and pension concerns.

The weakness seen in equity markets during the year was used to introduce a number of high quality companies that fell as markets declined. The volatility seen in equity markets was also used to advantage, by buying and selling various shares making short term gains.

Overseas Equities

Unfortunately the overseas performance has hindered the overall performance of the Fund during the year. Due to the size of the Pension Fund, the most cost efficient way to gain exposure to the overseas market is through collective vehicles. Accordingly, a range of unit and investment trusts, both internal and external are used. The central reason for the underperformance of the overseas exposure has been due to a widening of the discount to the underlying asset value of a number of investment trusts held. This normally occurs during periods of high volatility. If however you look at the underlying holdings within the Fund they have performed relatively well over the period. Accordingly, these holdings will be retained until market volatility begins to reduce.

INVESTMENTS - continued

Fixed Interest Securities

Global bond markets continued to show strong performance as investors' appetite for a safe haven was fueled by the sharp falls in equity markets, fears of deflation and the situation in Iraq. Corporate spreads followed the equity markets until Quarter 1 2003 when there was a sharp tightening seen despite the equity sell off driven in part by the renewed focus on deleveraging corporate balance sheets.

A number of corporate bonds were introduced into the portfolio during the period due to a change in the strategic asset allocation. The higher quality end of this asset class have performed particularly well, as investors have sought higher yields than in UK government securities but with a greater deal of certainty than the more speculative end of the market. This has helped the overall performance of the Pension Scheme due to the restriction of only investing in high quality corporate bonds.

Property

Towards the end of the year property was introduced into the benchmark. An opportunity to purchase property at bid price arose and the Fund invested at the end of November. Over the first quarter of 2003 the property units had a return of 1.6% compared with the CAPS Pooled Property return of 1.7%.

Outlook

The global economic recovery is expected to consolidate in 2003 with early cyclical characteristics as investment picks up and consumer spending slows. The US will continue to be the key driver for a world-wide aggregate demand whereas the focus in Europe will be on the European Central Bank as it adjusts interest rates to stave off any further economic deterioration. The outlook for Japan still hinges on the lack of structural reform as each short recovery is followed by a deeper recession.

In terms of the relative attractions of asset classes, the equity markets are still trading above long term multiples. The onus, therefore, is for the recovery in corporate earnings to continue in order to shore up the recent rallies. The oil price is also a major swing factor as the war premium dissipates and production in Iraq restarts – historically any significant fall has benefited the markets. In general, recent major corporate disappointments have been avoided, but the favoured sectors are still those that offer defensive growth (healthcare and utilities).

INVESTMENTS - continued

CUSTODIAL ARRANGEMENTS

The Borough of Douglas has appointed RBSI Custody Bank Limited, Isle of Man Branch, (part of the RBS Group and not an Associate of Merrill Lynch) as its custodian.

The reasonable costs of transferring assets of the portfolio to the custodian (or where applicable, its sub-custodians) are normally borne by the portfolio.

A nominee company, normally Nutraco Nominees Limited, a UK-based associate of the custodian, is registered as the holder of the portfolio's UK securities (other than UK bearer securities which are held in safe custody and securities relating to In-House Schemes and Connected Investment Trusts). Securities relating to investments of the portfolio's In-House Schemes and Connected Investment Trusts are normally registered in the name of Bath Street Nominees Limited, a Jersey-based associate of the custodian. Any securities registered in the name of a nominee company are pooled with those of other clients of the custodian. The custodian cannot pool such securities with its own property except when settling transactions.

Where the Scheme investments are held collectively in a pool, its entitlements may not be identifiable by separate certificates or other physical documents of title and, should the custodian default, any shortfall in investments belonging to the Scheme and other customers of the custodian may be shared pro-rata among all customers whose investments are so held.

Non-UK securities are normally held by sub-custodians appointed by or on behalf of the custodian in separate accounts designated "RBSI Custody Bank Limited – Client Account". This arrangement also applies for securities held in Euroclear.

INVESTMENT ACCOUNTING AND BANKING ARRANGEMENTS

The Borough of Douglas has authorised monies to be held on the Scheme's behalf on the following basis:

- In investment and income accounts with the custodian in the Borough's or the Scheme's name. The Borough has authorised Merrill Lynch to give the custodian instructions regarding such accounts on the Scheme's behalf.
- In Merrill Lynch Investment Managers (IOM) Designated Client Bank Accounts (as defined in the Financial Supervision Commission (Clients' Money) Regulatory Code 1993 (the "Code") with those institutions being Recognised Banks (as defined by the Code) which meet the minimum short-term credit rating of A1/P1 and which may include the custodian or any of its associates. Such monies are pooled with those of other clients but such designated client bank accounts do not hold monies beneficially owned by Merrill Lynch.

INVESTMENTS - continued

INVESTMENT ACCOUNTING AND BANKING ARRANGEMENTS (continued)

Monies held awaiting delayed settlement are held by the custodian in a pooled settlement account.

Interest is paid on the investment and income accounts, and balances on the income accounts are dealt with on the basis set out below;

Interest period: Quarterly on all accounts

Interest Rate: A commercial rate appropriate to the balances standing to the credit of the above accounts. The custodian benefits from the provision of banking services for clients.

Accounts are maintained in the currency of account and in such other currencies as may be required from time to time.

REMUNERATION BASIS OF THE INVESTMENT MANAGER

Ordinary Portfolio

Merrill Lynch's remuneration for managing and administering the portfolio is calculated and paid in arrears on its market value (including uninvested cash) as shown in its valuations and paid in arrears. Investments of the portfolio in In-House Funds and Connected Investment Trusts are disregarded for the purposes of calculating the fees.

Merrill Lynch's fees in respect of managing the portfolio are at the following annual rates:

Market Value	Rate per annum
On the first £5,000,000	0.75%
Thereafter	0.50%

They include those of the custodian and are settled by transfers from the portfolio on the due dates and no interest is charged if such transfers are effected after the due date.

Property Fund

Charges are 1% of the underlying net asset value per annum and 5.75% when units are purchased. A 5.75% charge was however waived on the purchase of the initial property units.

Care and Maintenance Portfolio

On the whole value of the Care and Maintenance Portfolio – Rate per annum 0.30%.

INVESTMENTS - continued

Charges Within In-House Funds and Connected Investment Trusts and Commissions

Initial (and in some cases conversion) charges are waived for investments made for the Isle of Man Local Government Pension Scheme. The price of each share or unit of certain In-House Funds and Connected Investment Trusts normally includes on both subscriptions and redemptions a 'rounding' of a maximum of one currency unit which is retained by the relevant manager or the relevant In-House Fund and Connected Investment Trusts.

Where the annual management and administration fees of the relevant In-House Fund and Connected Investment Trusts exceed the fee rates listed in the table below, Merrill Lynch procures that the portfolio receives a retrocession of the annual management and administration fees to the fee rates as set out in the table below.

	Management Fees % per annum	Transaction Commissions	Custodian/ Trustee Fees % per annum
Schemes of Mercury Offshore			
Sterling Trust	0.65	Nil	Approx 0.17
Mercury International Bond Fund	1.00	Nil	0.1

ACTUARIAL STATEMENT

Actuarial Statement for the purpose of Local Government Pension Scheme 1996 (Statutory Document No. 396/96)

As required by regulations, an actuarial valuation of the Scheme's assets and liabilities was carried out as at 31 March 2001.

Security of Prospective Rights

In my opinion, the resources of the Scheme are likely in the normal course of events to meet the liabilities of the Scheme, as required by the Regulations. In giving this opinion I have assumed that the following amounts will be paid to the Scheme:

Contributions paid by the members in accordance with the Local Government Pension Scheme 1996 (Statutory Document No. 396/96).

Contributions, for the three years commencing 1 April 2002, paid by the employers are as specified in our certificate dated September 2002 contained in our report on the valuation of the Scheme as at 31 March 2001.

Summary of Methods and Assumptions Used

Full details of the method and assumptions are described in our valuation report dated September 2002.

My opinion on the security of the prospective rights is based on the projected unit valuation method. This assesses the cost of benefits accruing to existing members during the year following the valuation, allowing for future salary increases. The resulting contribution rate is adjusted to allow for any difference in the value of accrued liabilities (allowing for future salary increases) and the assessed value of assets.

Like the previous (1998) valuation, a "market related" valuation method has been used. The market related method derives the financial assumptions by considering various averaged yields in the twelve month period leading up to the valuation date and values the assets of the Scheme based on the average market value in this same period. Using average yields and market values builds in an element of smoothing and stability for the future.

The key financial assumptions adopted for this valuation are as follows:

Financial Assumptions	Nominal at March 2001 % p.a	Real at March 2001 % p.a
Investment Return		
Equities	6.25-6.75%	3.45-3.95%
Bonds	5.25-5.75%	2.45-2.95%
75% Equities/25% Bonds	6.00-6.50%	3.20-3.70%
Pay Increases	4.30%	1.50%
Price Inflation/Pension Increases	2.80%	-

ACTUARIAL STATEMENT - continued

For liabilities which will accrue in respect of service after the valuation date we have adopted a discount rate which is initially the expected return from the existing assets at current market conditions but which in the longer term reverts to our longer term assumptions.

The 2001 valuation revealed that the Scheme's assets, which at 31 March 2001 were valued at £12.82 million, were sufficient to meet approximately 64% of the liabilities accrued up to that date. Assets were valued at their market value smoothed over the 12 months to the valuation date.

Copies of this report are available on request from the Isle of Man Local Government Pension Scheme. The next valuation of the Scheme will be carried out as at 31 March 2004.

Bryan Chalmers
Fellow of the Faculty of Actuaries
September 2002

Hymans Robertson
221 West George Street
Glasgow G2 2ND

REPORT OF THE INDEPENDENT AUDITORS, KPMG AUDIT LLC, TO THE MAYOR, ALDERMEN AND BURGESSES OF THE BOROUGH OF DOUGLAS

We have audited the financial statements on pages 20 to 28.

This report is made solely to the administering authority, as a body, in accordance with the Superannuation Act 1984. Our audit work and our work on contributions has been undertaken so that we might state to the administering authority those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the administering authority as a body, for our audit work, our work on contributions, for this report, or for the opinions we have formed.

Respective responsibilities of the Borough and Auditors

As described on page 2 the administering authority are responsible for obtaining audited accounts which comply with applicable Isle of Man law and United Kingdom Accounting Standards. They are also responsible for making available, commonly in the form of a report, certain other information about the Scheme which complies with applicable Isle of Man law. Further, as described on page 2, they are responsible for procuring that contributions are made to the Scheme in accordance with the Scheme rules and the recommendation of the actuary. Our responsibilities as independent auditors are established in the Isle of Man by statute, the Auditing Practices Board and by our profession's ethical guidance.

We report to you our opinion as to whether the accounts give a true and fair view and contain the information specified in the Superannuation Act 1984. We also report to you our opinion as to whether the contributions have been paid in accordance with the Scheme rules and the recommendation of the actuary and if we have not received all the information and explanations we require for our audit.

We read the report and other information accompanying the accounts and consider whether it is consistent with those accounts. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the accounts.

Basis of opinion

We conducted our audit in accordance with Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by or on behalf of the administering authority in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Scheme's circumstances, consistently applied and adequately disclosed.

The work that we carried out also included examination on a test basis, of evidence relevant to the amounts of contributions paid to the Scheme and the timing of those payments.

REPORT OF THE INDEPENDENT AUDITORS, KPMG AUDIT LLC, TO THE MAYOR, ALDERMEN AND BURGESSES OF THE BOROUGH OF DOUGLAS - continued

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In our opinion, the financial statements give a true and fair view of the financial transactions of the Scheme during the year ended 31 March 2003 and of the disposition at that date of its assets and liabilities (other than liabilities to pay pensions and benefits after the end of the Scheme year) and contain the information specified in the Superannuation Act 1984.

In our opinion, the contributions payable to the Scheme during the year ended 31 March 2003 have been paid in accordance with the Scheme rules and the recommendation of the actuary.

**KPMG Audit LLC
Chartered Accountants and Registered Auditor
Douglas
Isle of Man**

28th November 2003

FOREWORD TO THE FINANCIAL STATEMENTS

The financial statements have been prepared on a market value basis. The net income from all transfer values received has increased by £295,331. Contributions have increased by £165,488. This has resulted in an overall increase in income in respect of members of £460,819. Retirement benefits and other payments made to or in respect of members during the year have increased by £92,673.

In overall terms the net additions from dealings with members during the year amount to £1,075,197 (2002: £707,050).

The net assets of the Scheme at 31 March 2003 have decreased by £1.03 million (2002: increased by £0.6 million) to £11.62 million (2002: £12.65 million).

Financial Statements for the year ended 31 March 2003

	Notes	2003 £	2002 £
FUND ACCOUNT			
Contributions and Benefits			
Contributions receivable	3	1,710,850	1,545,362
Transfer values received	4	431,033	135,702
		<u>2,141,883</u>	<u>1,681,064</u>
Benefits payable	5	(814,192)	(820,658)
Leavers	6	(126,441)	(78,443)
Administration expenses	7	(126,053)	(74,913)
		<u>(1,066,686)</u>	<u>(974,014)</u>
Net additions from dealings with members		<u>1,075,197</u>	<u>707,050</u>
Returns on investments			
Investment income	8	349,041	324,709
Change in market value of investments	9	(2,387,418)	(368,807)
Investment management expenditure	10	(64,029)	(65,350)
Net loss on investments		<u>(2,102,406)</u>	<u>(109,448)</u>
Net (decrease)/increase in the Scheme during the year		<u>(1,027,209)</u>	<u>597,602</u>
Net assets of the Scheme			
At 1 April 2002		<u>12,646,429</u>	<u>12,048,827</u>
At 31 March 2003		<u>11,619,220</u>	<u>12,646,429</u>

The notes on pages 22 to 28 form part of these Financial Statements.

Financial Statements for the year ended 31 March 2003 - continued

	Notes	2003 £	2002 £
NET ASSETS STATEMENT			
Investments	9	11,428,221	12,347,577
Current assets and liabilities	11	190,999	298,852
		<hr/>	<hr/>
Net assets of the Scheme at 31 March 2003		11,619,220	12,646,429
		<hr/>	<hr/>

The notes on pages 22 to 28 form part of these Financial Statements.

D W CHRISTIAN, JP
Chairman
Policy and Resources Committee
Borough of Douglas

11 August 2003

G M BOLT, CPFA
Borough Treasurer
Borough of Douglas

11 August 2003

Notes to the Financial Statements

1. Basis of Preparation

The financial statements have been prepared in accordance with The Occupational Pension Schemes (Requirement to obtain Audited Accounts and a Statement from the Auditor) Regulations 1996 (as amended) and with the guidelines set out in the Statement of Recommended Practice, "Financial Reports of Pension Schemes" ("the SORP") as far as is practicable.

The financial statements summarise the transactions of the Scheme and deal with the net assets at the disposal of the Isle of Man Local Government Pension Scheme. They do not take account of obligations to pay pensions and benefits which fall due after the end of the Scheme year. The actuarial position of the Scheme, which does take account of such obligations, is dealt with in the Actuarial Statement on pages 15 to 16 and these financial statements should be read in conjunction with that Statement.

2. Accounting Policies

Contributions

Contributions represent the total amounts receivable from Local Government employers and Admitted Bodies on the Isle of Man in respect of their own contributions and from active members. The employers' contributions are made at a rate determined by the Consulting Actuary necessary to ensure that the Scheme is able to meet its existing and prospective liabilities including indexation.

Benefits, refunds of contributions and transfer values

Benefits, refunds of contributions and transfer values paid and received are brought into the financial statements on a cash basis.

Administration expenses

Gross administration expenses are charged on the accruals basis to the Scheme.

Investment income

Investment income is accounted for on the accruals basis. For securities, the effective date used to bring income into the financial statements is the due date of payment. However, for government securities the ex-dividend date is the effective date used.

Investments

The financial statements for the year have been prepared on the basis of stating investments at their market values which in the case of listed securities are determined by reference to the middle market price at the year end.

Notes to the Financial Statements - continued

2. Accounting Policies (continued)

Exchange rates

Current assets and liabilities arising from investments in overseas securities purchased in foreign currency have been translated at the mid-market closing rates of exchange ruling at the year end.

Taxation

- **Income tax and capital gains tax**

The Scheme is exempt approved under the Income Tax (Retirement Benefits Schemes) Act 1978 and Part I of the Income Tax Act 1989 (Acts of Tynwald). Therefore, it is not liable to Isle of Man income tax on interest and dividend income, or to capital gains tax.

- **Value added tax**

By virtue of the Borough of Douglas being the administering authority, VAT input tax is recoverable on all Scheme activities including expenditure on investment expenses.

- **US withholding tax**

The income earned from investments in stocks and securities in the United States is exempt from US tax pursuant to Section 892 of the Income Tax Code and is not subject to withholding of any tax under Section 1441. This exemption has continued to be applied thus far under the US Tax Reform Act of 1986.

- **Overseas tax deductions**

Where possible, tax deducted at source is recovered by the investment manager.

Notes to the Financial Statements - continued

3. Contributions Receivable

	2003 £	2002 £
Employers		
normal	1,308,125	1,189,591
special – Ramsey Town Commissioners	11,191	-
Members		
normal	384,124	345,146
Scheme additional	7,410	10,625
	<u>1,710,850</u>	<u>1,545,362</u>

Contributions breakdown

	2003			2002	
	Employees Normal £	Employers Normal £	Employees Scheme Additional £	Total £	Total £
Douglas Corporation	205,903	705,122	6,057	917,082	834,369
Braddan Church, Vicar & Wardens	786	1,933	-	2,719	1,965
Braddan Parish Commissioners	2,023	6,574	-	8,597	-
Castletown Commissioners	13,173	46,748	-	59,921	54,459
Crossroads Caring for Carers	3,332	6,663	-	9,995	8,730
The Dept. of Tourism & Leisure	4,196	13,637	-	17,833	5,746
Kirk Michael Commissioners	21	67	-	88	-
Kirk Onchan St Peters Church	815	2,649	-	3,464	3,249
Leonard Cheshire Foundation	1,829	3,293	-	5,122	5,563
Malew Parish Commissioners	4,392	14,840	-	19,232	14,618
Manx Churches Adoption & Welfare	5,471	17,781	-	23,252	25,117
Manx Foundation for Physically Disabled	1,645	5,348	-	6,993	6,530
Marashen Crescent Housing Committee	1,691	6,158	-	7,849	6,935
Northern Authority Swimming Pool Board	3,688	12,153	-	15,841	14,564
Onchan District Commissioners	44,912	154,120	-	199,032	186,477
Peel Town Commissioners	17,277	61,946	-	79,223	74,695
Port Erin Commissioners	10,615	36,301	-	46,916	45,111
Port St Mary Commissioners	11,021	35,817	-	46,838	51,249
Ramsey & Northern District Housing Committee	3,859	14,851	-	18,710	17,421
Ramsey Town Commissioners	39,743	135,136	1,353	176,232	155,641
Southern Authority Swimming Pool Board	6,367	22,548	-	28,915	32,923
Southern Civic Amenity Site Board	1,365	4,440	-	5,805	-
	<u>384,124</u>	<u>1,308,125</u>	<u>7,410</u>	<u>1,699,659</u>	<u>1,545,362</u>
Special Contributions					
Ramsey Town Commissioners				11,191	-
				<u>1,710,850</u>	<u>1,545,362</u>

Notes to the Financial Statements - continued

4. Transfer Values Received

£	2003	2002 £
Individual transfers in from other pension Schemes and Private Sector Institutions	431,033	135,702

5. Benefits Payable

£	2003	2002 £
Retirement and dependants' pensions	631,306	579,800
Lump sum retirement grants	138,501	176,653
Lump sum death grants	44,385	64,205
	814,192	820,658

The value of pensions is arrived at after netting off employers recharge of £47,984 (2002: £48,429).

6. Payments To and On Account of Leavers

£	2003	2002 £
Refunds of contributions	6,616	11,118
Payments to SERPS	5,396	7,699
Individual transfers to other schemes	114,429	59,626
	126,441	78,443

7. Administration Expenses

	2003 £	2002 £
Scheme administration and actuarial costs	126,053	74,913

During the year exceptional expenditure was incurred. This was in respect of the triannual valuation asset liability study from the Actuary and significant expenditure on introducing superannuation regulations.

Notes to the Financial Statements - continued

8. Investment Income

£	2003	2002 £
Income from fixed interest securities	149,060	148,358
Dividends from equities	170,808	135,235
Interest on cash deposits	29,173	41,116
	<u>349,041</u>	<u>324,709</u>

9. Investments

	Value at 1.4.02 £	Purchases at Cost £	Sales Proceeds £	Change in Market Value £	Value at 31.3.03 £
Fixed interest securities	1,769,870	414,014	(348,859)	128,558	1,963,583
Equities	7,263,187	3,196,441	(1,200,089)	(2,685,856)	6,573,683
Property unit trusts	-	1,098,435	-	46,496	1,144,931
Index-linked securities	2,288,939	-	(1,140,750)	123,384	1,271,573
Cash deposits	989,530	-	(562,433)	-	427,097
	<u>12,311,526</u>	<u>4,708,890</u>	<u>(3,252,131)</u>	<u>(2,387,418)</u>	<u>11,380,867</u>
Other	36,051				47,354
	<u>12,347,577</u>				<u>11,428,221</u>

The change in market value of investments during the year comprises all increases and decreases in the market value of investments held at any time during the year, including profits and losses realised on sales of investments during the year.

Notes to the Financial Statements - continued

9. Investments (continued)

£	2003	2002 £
Fixed interest securities		
UK public sector quoted	1,963,583	1,769,870
Equities		
UK quoted	4,314,591	4,797,981
Overseas quoted	2,259,092	2,465,206
	6,573,683	7,263,187
Property Unit Trust	1,144,931	-
Index-linked securities		
UK quoted	1,271,573	2,288,939
Cash deposits		
Sterling	427,097	989,530
Other		
Accrued investment income	47,354	36,051

10. Investment Management Expenses

£	2003	2002 £
Administration, management and custody	64,029	65,350

Notes to the Financial Statements - continued

11. Current Assets and Liabilities

	2003	2002
£		£
Debtors		
Amounts due from employers	146,838	196,991
Other	9,815	2,430
Cash	198,700	159,764
	<u>355,353</u>	<u>359,185</u>
Creditors	(164,354)	(60,333)
	<u>190,999</u>	<u>298,852</u>

Amounts due from employers are employers' and employees' contributions of £113,594 (2002: £152,461) and £33,244 (2002: £44,530) respectively, outstanding in the normal course of collection at the year end.

12. Related Party Transactions

There were no related party transactions.

SCHEME RULES AND BENEFITS

SCHEME MEMBERSHIP AND INCOME

- (a) All employees of the Borough of Douglas, other local authority and admitted body employers on the Isle of Man under the age of 65 are eligible for membership of the Isle of Man Local Government Pension Scheme 1996. Whole-time and part-time employees, whether permanent or temporary, become members automatically with the right to opt out (back-dated to the start of their membership if made within three months).

Members' contributions from pensionable pay are 6%, except for employees who were carrying out manual duties immediately before 1 April 1998. For as long as they remain on manual duties their contributions are 5% of pensionable pay.

- (b) Transfer payments for pension rights in almost any other scheme can be accepted by the Scheme to increase benefits which may eventually become payable.
- (c) The participating employers must make the balancing contribution required to keep the Scheme solvent, having regard to existing and prospective liabilities. This is usually determined as a percentage of the members' normal contributions by the Consulting Actuary following each triennial actuarial valuation of the Scheme.
- (d) Employers are now required to fund early retirements (other than ill-health) and discretionary added years by making up front payments.
- (e) Monies not immediately required for the payment of benefits and other outgoings have to be invested in accordance with the provisions of Part L of the Scheme.

BENEFITS AVAILABLE

Two or more years' membership (or a transfer from a personal pension plan has been received):

- A. Retirement pension and lump sum awarded:
1. Payable immediately on cessation of employment:
 - (i) through permanent incapacity at any age, or
 - (ii) as a result of redundancy after age 50.
 2. Preserved and payable from retirement age in any other circumstances.

SCHEME RULES AND BENEFITS - continued

BENEFITS AVAILABLE (continued)

- B. Spouses' and children's pensions and a tax free lump sum death grant following death:
- (i) in employment,
 - (ii) in receipt of retirement pension (a lump sum may **not** always be payable),
or
 - (iii) before preserved benefits become payable.

Under two years' membership (and no transfer has been received from a personal pension plan):

- A. Retirement pension and lump sum on retirement at age 65.
- B. Lump sum payable on retirement through permanent incapacity.
- C. Spouses' limited period pensions and a tax free lump sum death grant on death in employment.
- D. Children's continuing pensions.
- E. Refund of contributions when no other benefit payable.

PENSIONS INCREASE AWARDS

Retirement and dependants' pensions in payment and preserved are increased each year by the same Retail Prices Index percentage rate as that applied to State pensions.

TRANSFERS TO OTHER SCHEMES

When benefits are not payable immediately, a transfer can usually be made to another employer's pension scheme or to a personal pension plan or to purchase an insurance annuity bond.

Any enquiries regarding this Report should be addressed to:

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