USS
UNIVERSITIES SUPERANNUATION SCHEME

Summary Funding Statement

as at 31 March 2012

The USS Summary Funding Statement is issued to all scheme members and beneficiaries with information on the financial position of USS updated to 31 March 2012.

The trustee board has recently completed the scheme's valuation, which takes place every three years, and the results are explained in this statement. This latest triennial valuation took place as at 31 March 2011, when the funding level of the scheme on its technical provisions basis was 92%.

By March 2012, the funding position had deteriorated to 77% due to a 24% increase in the liabilities, which had not been matched by a 4.4% increase in the assets. The liabilities of the scheme, that is the present value of the benefit payments to be made in the future, is calculated by 'discounting' the future payments by a factor based on the yield on long-dated UK government bonds (gilts). When gilt yields rise, the discounted value of the liabilities of the scheme reduces. However, the gilt yield is currently at an historically low level because of the current economic climate and the Bank of England's policy of buying gilts, known as 'quantitative easing'.

Whilst members and beneficiaries can take comfort from the fact that their benefits are secure in the UK's second largest pension scheme, backed by a substantial covenant, these are undoubtedly challenging times for pension schemes generally.

USS is a long-term scheme and the trustee board has a long time horizon over which funding can be planned, given the status and longevity of the scheme's sponsoring employers. USS provides secure benefits to almost 300,000 active, deferred and pensioner members, and the trustee board will continue to manage the scheme diligently and, where necessary, to revise scheme funding in conjunction with the scheme's sponsoring employers and other stakeholders to ensure that it continues to meet its commitments both now and in the future.

This statement contains a number of key questions and answers which I trust you will find helpful. A copy of the complete 'Scheme Funding Report' is available on the USS website (**www.uss.co.uk**).

T H Merchant
Chief Executive
Universities Superannuation Scheme Limited

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How does USS work?

USS delivers a defined set of benefits as set out in the scheme rules. The financing of these benefits is provided by contributions from the sponsoring institutions and from the scheme members, which are paid into the USS fund. Together with the investment returns achieved on the fund's assets, these cover the payment of benefits to scheme members or to their dependants, as well as operating costs for the scheme.

How is the financial position of the scheme measured?

The current financial position is determined by comparing the value of the assets of the fund with an estimate of the current value of the scheme's liabilities, which are the total of all benefits that members have accrued to date and which are to be paid in the future.

Whilst the current value of the scheme's assets is relatively easy to determine, there are always uncertainties inherent in estimating the current value of the accrued liabilities, for example, for what duration a pension might be paid, what level of survivor's benefits might be paid, what rate of return will be received on investments in the future etc. This last factor is used to determine the assets that would be required today to enable the scheme to meet the projected future benefits already accrued by scheme members.

The starting point for determining the assumed rate of return on investments is the yield on UK government bonds, or gilts. This is known as the risk free-rate and a margin is added to this to reflect the trustee board's expectations of future returns given the asset mix in the scheme.

The gilt yield is currently at an historically low level because of the current economic climate, which results in a higher than otherwise value of the scheme's liabilities. Looking over the longer term, a gilt yield averaged over, say, the last twenty years would result in a much improved funding position.

The scheme actuary carries out a full valuation of the scheme every three years. This compares the value of the scheme's assets to its liabilities using two approaches, the technical provisions basis and the buy-out basis, as required by statutory regulations. The technical provisions basis requires the trustee board to adopt a prudent set of assumptions and it is this basis that is used to determine the funding level and, where appropriate, the extent of any deficit or surplus. The buy-out basis assumes that all of the liabilities of the scheme are to be secured through an insurance company, which would as you might expect be a very expensive way to provide pensions. The fact that we are required to report the position if the scheme were wound up does not, of course, mean that consideration is being given to doing so.

In calculating the value of the scheme's liabilities on any basis, the trustee board must make a number of assumptions about the financial and demographic factors that have an effect. These assumptions, which are explained in greater detail in the Scheme Funding Report, are critical to the valuation process and a great deal of care is taken in deciding upon them. For calculating the value on the technical provisions basis, one of the most important factors is the estimate of future returns from the fund's investments. In calculating the funding on the technical provisions basis, the scheme actuary has assumed that the long-term investment returns for the fund overall will be 1.7% per annum above the return that could be achieved on UK government bonds.

Regardless of the basis adopted, the financial position of the scheme is measured by the funding ratio, which shows what proportion of the scheme's future liabilities, in respect of past service, are covered by the scheme's assets.

What was the position at the last actuarial valuation?

The latest full valuation, as at 31 March 2011, indicated that the funding level was 92% on the technical provisions basis. The assets of the scheme fell short of the total amount required to meet all liabilities, by £2.9 billion.

Funding position as at 31 March 2011, technical provisions basis

Assets	£32.4 billion
Liabilities	£35.3 billion
Deficit	£2.9 billion
Funding level	92%

The funding level on the buy-out basis was 57%.

What has happened since the last statement?

Since the last statement, a number of changes to the benefits provided by the scheme came into force from 1 October 2011. These changes, which will help control the cost of future benefits, but do not affect the liabilities already accrued, include:

- The scheme benefits for new entrants, other than in specific, limited circumstances, are now provided on a Career Revalued Benefits basis rather than a Final Salary basis. This change has created two sections of the scheme, the Final Salary section (generally for those who joined the scheme before 1 October 2011) and the Career Revalued Benefits section for new entrants after 1 October 2011.
- The Normal Pension Age was increased for the future service of existing members and new entrants to age 65. This is likely to increase further in the future in line with increases in state pension age.
- A flexible retirement option was introduced.
- Member contributions increased to 7.5% of salary for Final Salary section members and were set at 6.5% for Career Revalued Benefits section members.
- Cost sharing was introduced so that, in the event that the total contribution level exceeds 23.5% of salary, changes to future benefits may be agreed by the JNC or, failing that, the employers will pay contributions to fund 65% of the additional cost and members would pay a 35% share.
- Increases to pensions in payment or in deferment have been capped for service after 30 September 2011. USS will match increases in 'official pensions' i.e. the pensions payable to members of the public service pension schemes, for the first 5%. If official pensions increase by more than 5% then USS will pay half of the difference up to a maximum increase of 10%.

What is the position of the scheme as at 31 March 2012?

The funding level of the scheme on its technical provisions basis has fallen significantly due to a large increase, 23.8%, in the liabilities, which has not been matched by the 4.4% increase in the assets over the year. The increase in liabilities has primarily been brought about by the historically low yield on gilts resulting from the current economic climate and the Bank of England's policy of buying gilts, which is also known as 'quantitative easing'. This fall in the discount rate means that the present value of future liabilities has increased. It does not mean that the future cashflows are significantly different from those predicted at the last valuation.

Funding position as at 31 March 2012, technical provisions basis

Assets	£33.9 billion
Liabilities	£43.7 billion
Deficit	£9.8 billion
Funding level	77%

The funding level on the buy-out basis was 50%.

The buy-out basis is just one of the alternative bases upon which scheme liabilities can be measured, and historically, the trustee board has used an additional benchmark, the gilts basis, for measuring the financial position of USS compared to the technical provisions basis.

If, instead of assuming a 1.7% per annum return above gilts, we apply a tougher benchmark (a basis that the trustee board has used previously), and assume that we will achieve investment returns equivalent to the whole of the fund being invested in gilts, the funding position had moved from 68% as at the triennial valuation to 56% as at 31 March 2012.

What is the trustee board's funding plan?

The scheme's investment strategy can lead to short-term volatility, but USS is a long-term investor and is able to look ahead 15 or 20 years because of the financial standing of the sponsoring employers, the strength of their commitment to the scheme, and the scheme's positive cash flow.

To correct the shortfall in the funding level at the date of the valuation, the trustee board has determined, after consulting the employers, a plan to eliminate the shortfall of £2.9 billion over a period of ten years. There are two components to this deficit recovery plan; the payment of additional contributions and the assumption that the scheme's investments will deliver a return 0.51% per annum greater than the assumption made in the triennial valuation. The first component will involve the employers making payments in the first six years of the recovery plan period at 16% of salaries, which is 3.4% above the cost of accrual determined in the valuation. For the remaining four years the employers will make payments at 2% of salaries in excess of the (then) estimated future cost of accruals.

The trustee board is aware of the need to take all possible steps to maximise the return on the scheme's investments for a given level of risk. The global economic factors which continue to cause volatility in investment markets and, the response of the UK government to the current situation, which is keeping the yield on gilts very low, are affecting all forms of investment and are not matters which the trustee board can directly influence. However, USS has a broad portfolio of investments and has continued to diversify further, including investment grade bonds, emerging market debt and further investments in infrastructure. This strategy is designed to manage the volatility and risk associated with the funding level. The trustee board believes this is the most appropriate response to these extraordinary conditions and will continue to monitor the situation and adjust the strategy as necessary.

USS can meet all its current pension commitments because the fund continues to have a positive cash flow, in that the fund receives substantially more in contributions and income from investments in a year than it pays out in benefits, which leaves it in a better position to weather these difficult conditions relative to many other schemes in the UK.

More information about the policies of the trustee board can be found in the Statement of Funding Principles and the Statement of Investment Principles, available from the USS website.

What happens if the scheme is wound up and there is not enough money to pay all benefits?

The Government has set up the Pension Protection Fund (PPF) to pay benefits to members in the event that employers become insolvent and are unable to meet their pension commitments. USS is a 'last-man-standing scheme' for PPF purposes, which means that it would only become eligible for the PPF if the vast majority (if not all of) employers in the higher education sector were to become insolvent. Clearly, this is a remote possibility.

However, if such circumstances were ever to occur, the pension you would receive from the PPF might be less than the full benefit you had earned in the scheme, depending on your age, when your benefits were earned and the size of your benefits.

Further information and guidance 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.

Where can you get more information?

If you have any other questions, or would like any more information, please contact the person at your employer who deals with USS matters. A list of documents which provide further information is set out on page 5. If you would like a copy of any of these documents please refer to the USS website (**www.uss.co.uk**) or contact USS's Liverpool office. If you require advice about any choice you have to make in relation to USS you should consult a professional adviser.

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Additional documents available on the USS website or on request

Statement of Investment Principles
This explains how we invest the money paid into the scheme.

Statement of Funding Principles
This sets out the policies of the trustee board for ensuring that the funding objectives are met and was published as part of the Scheme Funding Report dated 15 June 2012.

USS Investment Beliefs and Guiding Principles
These outline how USS addresses investment and risk management for the scheme.

Schedule of Contributions
This shows how much money is being paid into the scheme by the institutions and the contributing members, and includes a certificate from the actuary showing that it is sufficient.

Report and Accounts for year ended 31 March 2012
This shows the scheme's income and expenditure in 2011/12 and the net assets at the year end.

Scheme Funding Report as at 31 March 2011
This contains the details of the actuary's calculation of the scheme's financial position as at 31 March 2011.

Guide for USS members
This is the members' handbook for the scheme. Members should have been given a copy when they joined the scheme, but any member can get a further copy from their employer.