Members’ Annual Report
2011

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Statement from the Chairman of USS

Last year I updated you on the ongoing discussions between the University and College Union (UCU) and the employers, that have been taking place since 2009 to reform USS. I can now confirm that the review process has been completed and the changes that have been agreed came into effect on 1 October 2011.

The changes include increased employee contributions for current members of the Final Salary section of the scheme. Joiners after October will enter a new Career Revalued Benefits section. Member benefits after this date will be calculated on a retirement age of 65 and a flexible retirement facility will be provided. There are also changes to the way pensions are increased, which are explained on page 6.

Current members will have received a revised ‘Guide for members’ from their employer, and further details of the changes can be found on the USS website.

During 2010, the fund increased by 11.7% in line with the scheme’s strategic asset allocation benchmark, and well ahead of inflation. The funding level increased from 91% in March 2010 to 98% in March 2011, on the scheme’s technical provisions basis. These figures are measured against the most recent triennial valuation dated March 2008. The latest valuation commenced on 31 March 2011, and it is expected to show a reduced funding level as further provisions are likely to be made for continuing improvements in mortality.

During the year, the scheme continued to provide a high level of service to members, with a further 95% of cases being dealt with within five working days. For the first time, USS decided to benchmark our administration performance against relevant peer groups and engaged a professional benchmarking company to carry this out. USS was benchmarked as a high service, low cost scheme, showing it to be “particularly cost effective, especially taking into account a high service score presented”.

Sir Martin Harris
Chairman
Important changes to tax relief

In the UK we have historically enjoyed generous tax treatment in terms of tax relief on pension contributions and also the ability to draw part of our retirement benefits as a tax-free lump sum.

There have always been limits to how much you can build up in a pension scheme in the UK and still enjoy these tax privileges. Up until April 2011, there was an Annual Allowance of £255,000 a year, meaning you could build up retirement benefits in any year up to that value and still receive tax relief. In USS it was very difficult for even the highest earners to exceed this allowance.

There is also a limit at retirement called the Lifetime Allowance: this is currently £1.8 million. Currently, in USS you would need around 40 years’ service and a salary of around £140,000 a year to exceed that value.

The Annual Allowance has recently changed and the Lifetime Allowance is due to change in April 2012, so it is important that you are aware of the changes. If you exceed the allowances, you could be subject to a tax charge.

The changes
From April 2011, the Annual Allowance reduced to £50,000 a year.

From April 2012, the Lifetime Allowance will reduce to £1.5 million.
Important changes to tax relief continued

What you need to do

Annual Allowance
Many members will be unaffected by the reduced Annual Allowance. You can check if you are affected by using the Benefit Modeller on the USS website (www.uss.co.uk). You are able to login if you received a Service Statement in July, or you can enter the information required manually.

Within the Benefit Modeller there is an Annual Allowance checking tool that will give you an indication if you are close to or will exceed the Annual Allowance. If it looks like you will exceed the limit, you can check if there is scope to utilise unused allowances from up to the previous three years.

In any case, if you are close to or have exceeded the limits, you will receive further guidance on what you should do next.

Lifetime Allowance
Most USS members will not be affected by the Lifetime Allowance, as affected members will need a lot of service and a large salary.

However, if you have already accrued a benefit that has a Lifetime Allowance value in excess of £1.5 million, then you can protect this against any tax charge by registering with HM Revenue & Customs (HMRC) for something called Fixed Protection.

You must register for Fixed Protection before 6 April 2012. To register for Fixed Protection, you will need to download an HMRC form from:

www.hmrc.gov.uk/pensionschemes/apss227.pdf

There is one restriction if you elect for Fixed Protection – you must not build up any further pension benefits (in any scheme except state benefits) after 5 April 2012.

More information

Please refer to the factsheet ‘Limits to tax relief and tax-free benefits’ available on the USS website for full details.
USSonline modelling tools update

Updated Benefit Modeller

The USS Benefit Modeller has been amended and extra features added.

If you are currently contributing to USS, you can now login and automatically see your information, instead of manually entering your data.

You can:

• See what your benefits are worth today
• See what your benefits might be worth at retirement, including early retirement from age 60
• Vary your retirement package to see the impact on your pension and tax-free cash
• See the value of the benefits paid to your beneficiaries if you die whilst paying into USS
• See what impact paying additional contributions will have on your benefits
• Check how close you are to the new HMRC Annual Allowance.

Enhanced Annual Allowance modeller

If you want to see how close you are to the Annual Allowance, you can use the Benefit Modeller to see how much of the allowance you’ve used up this year. If it looks like you have exceeded or will exceed it, you can now go one stage further and check to see if there’s any scope to offset any potential tax charge by using unused allowances from up to the previous three years.

Coming soon!

In the coming months, the modeller will be developed to allow members to get estimated pension figures for early retirement before age 60 and also estimates for the new flexible retirement option available from 1 October 2011.
Pensions increases

USS pensions in payment and deferred benefits from the main section of the scheme are reviewed annually and increases applied in line with the rise in 'official pensions', such as those paid to members of the Civil Service, Teachers and NHS schemes.

In the past, those increases have matched price inflation based on the movement of the Retail Prices Index (RPI) in the 12 months to the preceding September. In July 2010 the Chancellor announced that from April 2011 the Consumer Prices Index would replace the Retail Prices Index as the basis for uplifting official pensions. This is not a USS rule change and has not come about because of the scheme review. This change is in accordance with the USS rules.

There are important differences in the way increases are applied for different types of member, which depend upon when the service was accrued.

Pension already in payment

If you are already receiving a pension from USS, then the increase will reflect the full rise in official pensions for service accrued prior to 1 October 2011. Increases payable on pension in respect of service accrued from 1 October 2011 will match the rise in official pensions for the first 5%. If official pensions increase by more than 5%, then USS will match half the difference to a maximum increase of 10%.

Deferred Final Salary benefits

Increases payable on deferred benefits (benefits held by the scheme for former members who have yet to retire) will reflect the full rise in official pensions for service accrued prior to 1 October 2011. Increases payable on benefits in respect of service accrued from 1 October 2011 will match the rise in official pensions for the first 5%. If official pensions increase by more than 5% then USS will match half the difference to a maximum increase of 10%.
Active Final Salary section members

If you are currently paying into the Final Salary section of the scheme, then your pension will be calculated based on your final pensionable salary and pensionable service when you retire or leave. If you retire or leave, increases to benefits will be applied reflecting the full rise in official pensions on that part of the pension payable in respect of service you accrued prior to 1 October 2011. Increases payable on benefits in respect of service accrued from 1 October 2011 will match the rise in official pensions for the first 5%. If official pensions increase by more than 5%, then USS will match half the difference to a maximum increase of 10%.

It is important to note for all members of USS that in periods of negative inflation (deflation) pensions are not reduced but no increase is applied.

The supplementary section provides pensions paid following a service enhancement in the case of incapacity or death in service (this is indicated on payslips). For all members in receipt of benefits payable from the supplementary section of the scheme, benefits are increased to the extent that the Trustee Company, acting on actuarial advice, decides. In the past, pensions payable from the supplementary section have been paid at the same rate as those paid from the main section. Pension increases are applied with effect from 21 April each year, as shown above.

Career Revalued Benefits section members

Increases payable on your Career Revalued Benefits will match the rise in official pensions for the first 5%. If official pensions increase by more than 5%, then USS will match half the difference to a maximum increase of 10%.

<table>
<thead>
<tr>
<th>Year</th>
<th>% increase</th>
</tr>
</thead>
<tbody>
<tr>
<td>2011</td>
<td>3.1</td>
</tr>
<tr>
<td>2010</td>
<td>0.0*</td>
</tr>
<tr>
<td>2009</td>
<td>5.0</td>
</tr>
<tr>
<td>2008</td>
<td>3.9</td>
</tr>
<tr>
<td>2007</td>
<td>3.6</td>
</tr>
<tr>
<td>2006</td>
<td>2.7</td>
</tr>
</tbody>
</table>

*In periods of negative inflation pensions are not reduced but no increase is applied.
Are you making the most of your USS AVC options?

As a member of USS, you can pay extra contributions called Additional Voluntary Contributions (AVCs) to either buy additional benefits directly from USS or to invest in the USS Money Purchase AVC (MPAVC).

If you pay into the MPAVC, administered by Prudential, it is important you review your investment fund(s) regularly to make sure that they are appropriate for your circumstances. Prudential sends you a statement each year, usually in May, and this can be a good time to review your fund(s).

It is just as important to review your fund(s) if you are no longer paying into the MPAVC, either because you have left or just stopped paying in.

It is easy to forget your MPAVC as retirement seems so far off, but this could be a mistake. You should review your MPAVC for a number of reasons:

- Are your chosen investment funds still relevant? For example, you may have chosen an equity fund when you first started, but as you get older you might want to think about moving to something a bit more predictable. It is your responsibility to manage your investment.

- Are you within the revised Annual Allowance introduced in April 2011? See pages 3 and 4 for details.

- Are you saving enough towards your retirement goals?

Did you know that you are able to review your AVC information online at any time?

If you already have a MPAVC, then you can access your account online at www.pru.co.uk/uss and follow the links to your online account, where you can find information on:

- Fund values
- Viewing individual contribution/plan records
- Switching funds
- Redirecting contributions
- Changing personal details
The first time you log into the site, your username and password will be the plan number U291 and your national insurance number, for example:

**Username:** U291TN010760F  
**Password:** TN010760F

**Contacting Prudential**

Existing MPAVC members who wish to switch funds can use the online facility www.pru.co.uk/uss or can call Prudential’s Customer Services team on 0845 6000 343 from 8:30am to 6:00pm, Monday to Friday.

Or, if you want to investigate taking out an AVC, you can speak to a Prudential AVC specialist by calling 0800 515 914.

Prudential provides:

- A UK-based team
- Knowledge of your USS pension scheme
- Appointed as sole provider for the USS MPAVC provider
- No pressure
- You can speak to the same person each time
- Set up or increase your AVC over the phone.

**Meet with Prudential**

Did you know that you may be able to meet with a Prudential consultant to discuss both the USS AVC options? They can go over the options and work through some figures with you.

Call **0800 515 914** to find out more.
Since September 2009, the London Investment Office (LIO) has made steady progress, but markets have remained unsettled with two significant bouts of market stress.

The first period of stress was triggered by concerns over the debt of ‘peripheral’ countries within the European Monetary Union. Markets then recovered, despite continuing problems with debt, fiscal deficits and growth in parts of the Eurozone. Global economic growth remained adequate – propelled by emerging markets and countries well-placed to meet their demand.

The scheme’s funding ratio improved cumulatively, until sharply deteriorating late in 2011. Peripheral European debt was again a prime cause, joined by fears that global growth would stall. It appeared the developed world might tip into recession, burdened by excessive private and/or public debt and by the need to cut fiscal deficits, while momentum in emerging markets also slowed.

Government bond yields have recently fallen to exceptionally low levels. With the scheme’s liabilities discounted by reference to UK gilt yields, and in the context of sharp falls in equity markets, the funding ratio has suffered. Time will tell, but we believe there is a silver lining. Markets appear to have over-reacted and returns may therefore recover.

Overall performance has been satisfactory over the past two years relative to the scheme’s strategic asset allocation benchmark. Within the LIO, the global emerging markets equities team has performed well. We have strengthened the resources focused on the scheme’s asset allocation, as well as building out all control functions. The Alternative Assets programme has developed further, reaching 17% of USS assets. We have recently added a senior professional specialising in infrastructure.

Unsettled periods tend to create dislocation in markets. With its long-term investment horizon and range of investment capabilities, USS is well placed to take advantage of the opportunities presented. We remain focused on securing sufficient returns to navigate these challenging times.

Roger Gray
Chief Investment Officer
Responsible investment

Over many years, USS has developed its processes and procedures to assist its portfolio managers in the integration of environmental, social and governance (ESG) issues into the investment decisions, and to engage with companies when the scheme believes these issues add to financial risk. This approach to responsible investment (RI) differs from ethical or Socially Responsible Investment (SRI), whereby a retail investor would choose to avoid investing in certain sectors, products or countries on personal, ethical or moral grounds. The legal position given to the scheme is very clear: a pension fund’s primary responsibility is to generate appropriate risk-adjusted returns to meet its pension liabilities.

This does not mean that USS should not assess or address ESG or ethical issues. On the contrary, where these issues represent a financial risk to the scheme, we should and do take them into account.

The scheme will therefore continue with its objective of integrating material ESG issues into its investment processes across asset classes, as USS believes that this will help both protect and enhance the long-term value of its investments.

Focus on engagement

BP – a year to forget

BP was a focus of engagement attention in 2010. The start of the year saw the spotlight on the company’s oil sands operations, which were the subject of a shareholder resolution at its Annual General Meeting (AGM). Following detailed engagement with the company on this issue (engagement which pre-dated the shareholder resolution), USS decided that the company had fulfilled the requirements of the resolution and therefore voted in support of management.

However, just days after the AGM, the Macondo deep water well in the Gulf of Mexico exploded, with the tragic loss of 11 lives and significant environmental and social impacts. Following the disaster, a combination of the Chief Investment Officer, portfolio managers and RI team members met on several occasions with the Chairman, Senior Independent Director, Head of Investor Relations and other senior employees to discuss how the company was dealing with the situation and how it could prevent a similar situation from happening again.

Although the company has committed itself to improve safety, process management and performance, and indeed appeared
Responsible investment continued

to do so before both the Texas City and Macondo accidents, there is clearly work to be done to re-establish its credibility and limit damage to its future prospects.

Policy level engagement
Engagement with policy makers remains a key focus of the RI strategy, as we often believe this to be a more efficient and effective way to generate change in corporate behaviour across a market. Examples of policy engagement include meetings with UK ministers and civil servants, and with the President of the European Union, Mr Barossa, to reinforce the need for appropriate regulation to encourage investment in renewable energy and clean technology.

USS has been leading efforts by a group of international investors in hedge funds to engage with the offshore regulator in Cayman, where many of these funds are domiciled. The aim of this activity is to improve governance practices and standards of disclosure amongst hedge funds.

USS has also actively participated in and responded to numerous public consultations associated with the UK stewardship code and EC consultations, and has met with regulators in Brussels, Taiwan, Japan and USA to discuss other governance-related issues.

Other engagements
USS has engaged extensively with banks on remuneration issues and undertaken in-depth analyses and engagements with many other companies in USS’ global portfolio on a range of governance, strategic and operational issues. USS prioritises engagement activity on companies in which we have a significant holding and can see opportunities to improve shareholder value through improved governance, management and oversight of its operations.

Voting at company meetings
One of the central planks of RI is exercising voting rights at company meetings. Given the large number of companies in which USS invests at a global level, this is quite an undertaking and requires a significant allocation of resource in order to maximise the effectiveness of this engagement tool. To assist with voting in the UK, USS has set up a voting and engagement alliance with the UK rail workers pension scheme (Railpen).
In 2010-2011, USS voted on 12,274 individual resolutions at 1,153 corporate events. In its voting, the scheme voted in favour of approximately 89% of resolutions, abstained in 4% of cases and voted against 7% of proposed resolutions.

The UN PRI
The scheme continues to be perceived as a leader in RI globally and in its endeavours to integrate RI issues into the investment process. Our involvement with the United Nations-backed Principles for Responsible Investment (PRI) provides an example of this leadership role. USS has been involved in the principles since PRI’s inception, and currently provides one of the organisation’s elected board members. USS supports the continued development and growth of the PRI as it is in the scheme’s and, therefore, in its members’ interests to encourage other investors around the world to focus on ESG issues.

Integration
The RI team has continued to work with internal fund managers to integrate extra financial information into investment decisions and processes. Outside public equities, the scheme has been particularly active in private equity and hedge funds. The RI team actively participates in the due diligence processes prior to investment in both asset classes and in the subsequent monitoring of the progress made on investment managers’ commitment to improve their fund governance structures and/or approaches to ESG issues in their investment processes.

In property, USS hired a specialist environmental manager in 2010, so as to maximise the opportunity to reduce costs of energy, waste and water etc, in its direct UK property portfolio. The scheme also received a Platinum Award for Outstanding Industry Contribution for an initiative, set up jointly with the Dutch pension funds APG and PGGM, to establish a global environmental benchmark for the property sector (and in fact won the same award for the project in 2011).
# Income and expenditure

USS fund account for the year ended 31 March 2011.

## Contributions and benefits

<table>
<thead>
<tr>
<th>Description</th>
<th>2011 £m</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fund at start of year</td>
<td>30,197.9</td>
</tr>
<tr>
<td>Contributions from members and institutions</td>
<td>1,422.1</td>
</tr>
<tr>
<td>Premature retirement scheme receipts</td>
<td>30.1</td>
</tr>
<tr>
<td>Transfers-in from other schemes</td>
<td>101.5</td>
</tr>
<tr>
<td><strong>Total member income</strong></td>
<td><strong>1,553.7</strong></td>
</tr>
</tbody>
</table>

## Expenditure for the year

<table>
<thead>
<tr>
<th>Description</th>
<th>£m</th>
</tr>
</thead>
<tbody>
<tr>
<td>Benefits paid</td>
<td>1,329.9</td>
</tr>
<tr>
<td>Refunds</td>
<td>45.7</td>
</tr>
<tr>
<td>Administration costs</td>
<td>20.6</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>1,396.2</strong></td>
</tr>
</tbody>
</table>

## Returns on investments

<table>
<thead>
<tr>
<th>Description</th>
<th>£m</th>
</tr>
</thead>
<tbody>
<tr>
<td>Investment income</td>
<td>749.6</td>
</tr>
<tr>
<td>Change in market value of investments</td>
<td>1,719.5</td>
</tr>
<tr>
<td>Investment management expenses</td>
<td>- 44.8</td>
</tr>
<tr>
<td><strong>Net returns on investments</strong></td>
<td><strong>2,424.3</strong></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Description</th>
<th>£m</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net increase in the fund during the year</td>
<td>2,581.8</td>
</tr>
<tr>
<td><strong>Fund at the end of the year</strong></td>
<td><strong>32,779.7</strong></td>
</tr>
</tbody>
</table>

\[
\text{Net increase in the fund during the year} = \text{Fund at start of year} + \text{Income} - \text{Expenditure} + \text{Investment return} = \text{Fund at end of year}
\]

\[
\begin{align*}
\text{Net increase in the fund during the year} &= 32,779.7m - 30,197.9m + 1,553.7m - 1,396.2m + 2,424.3m \\
&= 2,581.8m
\end{align*}
\]
Asset Management, Legal & General Investment Management and Royal London Asset Management, who have each been appointed to manage a strategic allocation to non-government bonds. A separate fund designed to match the performance of the FTSE All Share Index is run in-house on advice provided by HSBC Quantitative Techniques. In addition, within the LIO both the alternative assets and property teams manage their respective portfolios with the assistance of external managers and investment advisers.

The appointment of the new credit mandates, together with an increased allocation to global emerging market equities and the continued expansion of the alternatives portfolio, have been financed by reducing allocations to developed market equities. The alternative assets portfolio now accounts for 16% of the fund. The aim over the medium term is to hold 20% in this asset class, embracing a wide spectrum of alternative assets, including private equity, absolute returns and commodities.

The value of the fund increased from £29.8 billion at 31 March 2010 to £32.4 billion at 31 March 2011 (excluding money purchase AVC investments held with the Prudential). The distribution of assets at that date is shown above. Included within these figures are £5,221 million of alternative assets.

The fund’s investments are divided between those directly managed by the scheme’s in-house investment management team, the London Investment Office (LIO), which currently manages the majority of assets, and those outsourced to external managers selected on the advice of LIO. External managers comprise Capital International, who manage a specialist global equity mandate, together with BlueBay

### Distribution of assets

<table>
<thead>
<tr>
<th>Category</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>UK equities</td>
<td>22</td>
</tr>
<tr>
<td>Cash and other assets</td>
<td>8</td>
</tr>
<tr>
<td>Property</td>
<td>7</td>
</tr>
<tr>
<td>Alternative investments</td>
<td>16</td>
</tr>
<tr>
<td>Fixed interest</td>
<td>13</td>
</tr>
<tr>
<td>Overseas equities</td>
<td>34</td>
</tr>
<tr>
<td>Total</td>
<td>100</td>
</tr>
</tbody>
</table>

USS MEMBERS’ ANNUAL REPORT 2011
Investment performance

The fund’s investments have risen to £32.4 billion as at 31 March 2011 from £29.8 billion in 2010. The fund’s position has continued to recover from the adverse market conditions experienced in 2008. The five-year returns are close to both RPI and average earnings, although the 10-year returns are slightly below both measures. The year to 31 December 2011 was a good year for investment markets generally, reversing much of the fall in values experienced in 2008. The total fund rose 11.7% in the calendar year 2010 almost exactly in line with the return on its strategic asset allocation benchmark and ahead of the UK (RPI) inflation rate of 4.8%. Over the last five years the total fund has returned 3.0% a year, underperforming its benchmark by 0.6% a year.

Largest listed bond and equity holdings

<table>
<thead>
<tr>
<th>£m value</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Royal Dutch Shell</td>
<td>582</td>
</tr>
<tr>
<td>HSBC Holdings</td>
<td>460</td>
</tr>
<tr>
<td>Vodafone Group</td>
<td>436</td>
</tr>
<tr>
<td>BP</td>
<td>361</td>
</tr>
<tr>
<td>BHP Billiton</td>
<td>343</td>
</tr>
<tr>
<td>Rio Tinto</td>
<td>335</td>
</tr>
<tr>
<td>GlaxoSmithKline</td>
<td>247</td>
</tr>
<tr>
<td>UK Treasury 4.5% 07/09/2034</td>
<td>240</td>
</tr>
<tr>
<td>US Treasury 4.75% 15/02/2041</td>
<td>227</td>
</tr>
<tr>
<td>BG Group</td>
<td>220</td>
</tr>
</tbody>
</table>

A full list of all the fund’s holdings, along with information about corporate governance issues, is available from the USS website at www.uss.co.uk/ussinvestments
Membership statistics

20,323 new members joined USS in the 12 months to 31 March 2011.

As at 31 March 2011, USS had 386 participating institutions with the following number of members:

- Active: 139,931
- Deferred: 88,370
- Pensioner: 49,251
- Beneficiaries: 9,991

USS was notified of 4,194 employees who were eligible to join but elected not to do so.

Further information

Active members should contact their employing institution with any enquiries relating to their benefits.

Deferred members, pensioners and beneficiaries should contact USS directly at:
Universities Superannuation Scheme Ltd,
Royal Liver Building, Liverpool L3 1PY
t: 0151 227 4711 (Local rate 0845 068 1110)
f: 0151 236 3173
w: www.uss.co.uk

The Pensions Advisory Service (TPAS) and the Pensions Ombudsman can be contacted at:
11 Belgrave Road, London, SW1V 1RB

TPAS
t: 0845 601 2923
e: enquiries@pensionsadvisoryservice.org.uk
w: www.pensionsadvisoryservice.org.uk

The Pensions Ombudsman
t: 020 7630 2200
f: 020 7821 0065
Management of the scheme

The directors of the trustee company during the year were as follows:

Sir Martin Harris (Chairman)
Co-opted
Professor John Bull CBE (Deputy Chairman)
Michael Butcher
Howard Jacobs
Virginia Holmes
Appointed by HEFCE
Steve Egan
Appointed by UCU
Dave Guppy
Bill Trythall (Pensioner director)
Joseph Devlin
Appointed by UUK
David McDonnell CBE DL
Professor David Eastwood
Professor Glynis Breakwell

The principal officers and advisers of the trustee company at 1 August 2011 were:

Chief Executive: Tom Merchant
Chief Investment Officer: Roger Gray
Chief Financial Officer: David Webster
Pensions Policy Manager: Brendan Mulkern
Pensions Operations Manager: Bernadine Steventon
Company Secretary: Ian Sherlock
Communications Manager: Colin Busby
Head of IT: Steve Grady
Chief Administrative Officer: Andrew Little
Actuary: Edwin Topper of Mercer, Manchester, M2 4AW
Solicitors: DLA Piper LLP, Liverpool, L2 0NH
Auditors: KPMG LLP, Manchester, M2 6DS
Bankers: Barclays Bank Plc, Manchester, M2 1HW
Summary Funding Statement

I am pleased to provide you with the Summary Funding Statement for 2011, which is designed to inform you about the financial position of USS. It is a snapshot of the funding of the scheme at 31 March 2011, and sets out how the position has changed since the last triennial valuation at 31 March 2008. A full valuation as at 31 March 2011 is currently being undertaken, but this is a very significant exercise and the results will not be known until early next year.

We are therefore reporting funding levels as at 31 March 2011, based on the assumptions used in 2008 (on life expectancy, for example), but updated by the scheme actuary for investment returns and changes in market conditions. The changes include an adjustment in the inflation calculation reflecting the change by the government to ‘official pensions’ which is used by USS in determining the increases to pensions in payment, which from April 2011 links increases to the Consumer Prices Index rather than the Retail Prices Index.

The actuarial assumptions are key in determining the scheme’s funding position. Some of the assumptions are likely to be changed when the USS trustee board considers them later this year as part of the valuation process. Any changes will lead to a change in the funding level reported here. A copy of the valuation report will be available on the USS website early next year.

The statement contains some key questions and answers, which I hope you will find useful.

Tom Merchant
Chief Executive
Universities Superannuation Scheme Ltd

How does USS work?

USS aims to deliver a defined set of benefits, based on each member’s service and salary, 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. Contributions are collected from active members (6.35% of salary) and participating employers (16% of salary). These contributions are paid into the USS fund and, together with the investment returns achieved on the fund’s assets, are used to finance the payment of benefits to members who have retired, or to their dependants.

How do we measure the financial position of the scheme?

There are inherent uncertainties in the funding of a defined benefit scheme, and the finances of the scheme are checked regularly to see how well the fund is shaping up.

The key driver is how well the scheme’s investments have performed relative to changes in its liabilities (ie the benefits
promised). The scheme actuary carries out a full valuation every three years and compares the value of the scheme’s assets with its liabilities using several approaches, as required by regulations.

Work on agreeing the assumptions for the 2011 valuation is not yet finalised but this statement gives you an update on the latest position.

What has happened since the last statement?

World stock markets fell dramatically soon after the 2008 valuation, reaching their lowest point in March 2009. Since then, markets recovered up to 31 March 2011. The value of the scheme’s assets at 31 March 2011, of £32.4 billion, shows an increase compared with last year (£29.7 billion) and compared with the 2008 valuation (£28.8 billion), although the funding level is still lower than at the time of the 2008 valuation.

The volatility in the value of the scheme’s assets remains a matter of concern for the board, but USS is able to take a long-term view of its investments because of the standing of and strength of commitment from the sponsoring employers and the positive cash flow of the scheme.

The board carried out a review of its investment strategy following the completion of the 2008 actuarial valuation and decided to gradually reduce the percentage of the fund held in return-seeking assets, such as company shares, and to increase its holding of risk-reducing assets such as gilts. However, this change can only take place when market conditions allow, and can only be undertaken over a period of many years, given the size of USS and the implications of such a shift for the funding of the scheme. This is a long-term objective and is explained further in the Statement of Investment Principles.

What is the position on scheme funding?

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Assets</td>
<td>£32.4 billion</td>
</tr>
<tr>
<td>Amount needed to pay benefits</td>
<td>£33.1 billion</td>
</tr>
<tr>
<td>Deficit</td>
<td>£0.7 billion</td>
</tr>
<tr>
<td>Funding level</td>
<td>98%</td>
</tr>
</tbody>
</table>

The above table shows the scheme-specific (technical provisions) funding level at 31 March 2011 based on the assumptions and data used in 2008, but updated by the scheme actuary for investment returns and changes in market conditions. The actuarial assumptions are likely to be changed
when the USS trustee board considers them later this year as part of the valuation process.

The funding level as at 31 March 2011 reflects a change in the way price inflation is calculated for the purpose of determining pension increases. USS pensions are increased in the same way as ‘official pensions,’ which are the pensions payable, for example, to those in the NHS, Teachers and Civil Service schemes. With effect from April 2011, the annual increase, prescribed by the government, reflects the change in the Consumer Prices Index instead of the Retail Prices Index.

There are various ways to approach the calculation of scheme liabilities, and historically the board has used a different standard for measuring the financial position of USS which relates to returns on UK fixed-interest gilts. This standard is still relevant to our long-term funding objective, and is referred to in the table to the right as the historic gilts basis.

The actuary also has to estimate the scheme’s funding position as if the scheme had to be wound-up with all the liabilities secured by purchasing each member’s benefits from an insurance company. This is called the ‘buy-out’ basis and is, as you might expect, a very expensive way to provide your 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 winding up the scheme.

The funding levels for each year since the 2008 valuation are set out in the following table:

<table>
<thead>
<tr>
<th>Funding basis</th>
<th>31 March</th>
<th>31 March</th>
<th>31 March</th>
<th>31 March</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2008</td>
<td>2009</td>
<td>2010</td>
<td>2011</td>
</tr>
<tr>
<td>Scheme-specific</td>
<td>103%</td>
<td>75%</td>
<td>91%</td>
<td>98%</td>
</tr>
<tr>
<td>Historic gilts</td>
<td>71%</td>
<td>52%</td>
<td>63%</td>
<td>69%</td>
</tr>
<tr>
<td>Buy-out</td>
<td>79%</td>
<td>47%</td>
<td>57%</td>
<td>54%</td>
</tr>
</tbody>
</table>

What is the trustee board’s funding plan?

The board remains confident that its long-term funding plan is appropriate. USS has a diversified portfolio of investments and has continued its move into alternative assets, including private equity, absolute return strategies including hedge funds, and commodities. This will help the fund to better manage volatility and risk.

Also the fund continues to have a positive cash flow (because the fund receives more in contributions and dividends in a year than it pays out in benefits), which leaves it in a much stronger position relative to many other schemes in the UK.

However, the cost of providing pensions continues to rise, partly because members are living longer. Consequently the
employers’ contribution rate was increased from 14% to 16% effective from 1 October 2009, to provide for the increased cost of providing future benefits.

After a long period during which a review of the scheme’s benefits was undertaken, followed by a consultation with affected employees and their representatives, a package of scheme rule changes was decided upon with an effective date of 1 October 2011. Further details of the scheme review can be found on the USS website.

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: www.uss.co.uk

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

The government has set up the Pension Protection Fund (PPF) to pay benefits to members in the event that the 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 all employers in the higher education sector were to become insolvent. Clearly, this is a highly unlikely scenario.

However, if such circumstances were ever to occur, the benefits you would receive from the PPF may be less than the full benefit you have earned in the scheme, depending on your age, when your benefits are 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 I 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 attached. If you would like a copy of any of these documents please refer to the USS website (www.uss.co.uk) or contact our Liverpool office. If you require advice about any aspect of USS you should consult a professional adviser.
Additional documents available on request

**Statement of Investment Principles**
This explains how USS invests 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 first published as part of the Actuarial Valuation Report as at 31 March 2008.

**Investment Policy Implementation Document**
This is a working document that contains detailed operational information about the investment policy. A copy can be provided on request.

**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 2011**
This shows the scheme’s income and expenditure in 2010/11.

**Actuarial Valuation Report as at 31 March 2008**
This contains the details of the trustee board’s review of the scheme’s financial position as at 31 March 2008.

**The actuarial report as at 31 March 2010**
This contains the details of the actuary’s check of the scheme’s financial position as at 31 March 2010.

**Guide for USS members**
This is the members’ handbook for the scheme. You should have been given a copy when you joined the scheme, but you can get another copy from your employer.
Contact details update

If you are a deferred or pensioner member of USS, it is important to make sure you keep your details up to date with us, for example, if you move home.

You can use the enclosed form to tell us about any changes. If your surname has changed, you will need to send us a certified copy of an official document supporting the change, so we can update our records.

If you are a member currently contributing to the scheme and have received this report from your institution, then there is no need to worry – your employer will keep these details up to date.

A large print version of this Members’ Annual Report is available on request from USS. Telephone: 0151 227 4711