UniSuper's Defined Benefit Division explained

This booklet summarises how the Defined Benefit Division (DBD) works. It covers membership advantages and risks. For more detailed information, see the product disclosure statement at **unisuper.com.au/pds**

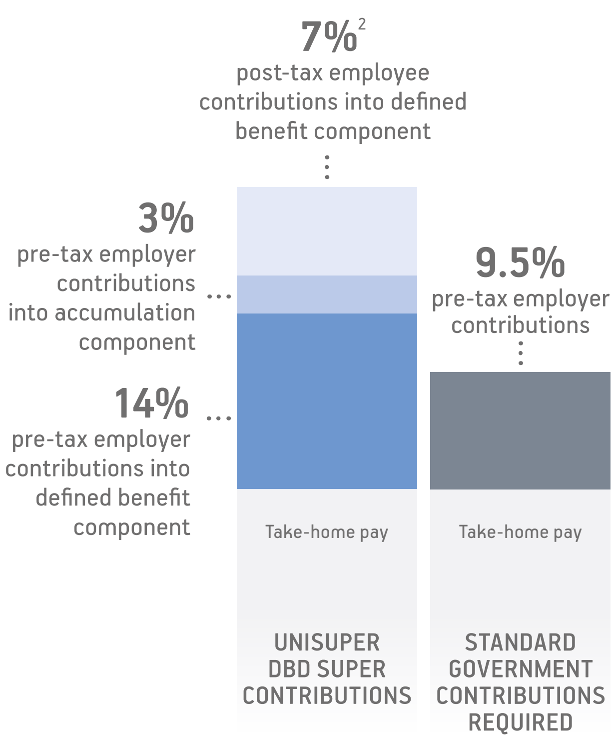
What is the Defined Benefit Division?

The Defined Benefit Division (DBD) is a $21 billion asset pool invested in shares, property, infrastructure, bonds and cash. Most contributions of DBD members are invested in this DBD asset pool. The remaining portion is usually allocated to the Accumulation component and can be invested in up to 16 investment options. Final member benefits are the total of both portions.

DBD member defined benefits are determined by an employment-based formula (see page 4) that isn't directly affected by the DBD's investment performance. This is different to how accumulation[1] funds work where accounts are impacted by the investment performance of the investment option(s) in which an accumulation member invests their account balance.

UniSuper DBD members can have a combined contribution rate of up to 24% of their salary. This 24% is made up of the contributions shown below. The employer contribution rate is almost double the 9.5% rate—required under the Government's Superannuation Guarantee legislation—that most Australian employees receive.

UNISUPER'S STANDARD DBD CONTRIBUTION RATE VS THE STANDARD GOVERNMENT RATE



DBD overview

Over three decades, and many economic cycles, no DB member has had any reduction to their accrued benefit. Even after the Global Financial Crisis (GFC), benefits accrued by members have not been impacted. Many Australians have not been so fortunate.

An employment-based formula is likely to provide a greater degree of certainty about members' benefits at retirement than would be provided by an accumulation arrangement where members are directly exposed to investment market performance.

The DBD's benefits are provided via a $16 billion portfolio of pooled assets which are expertly managed. A large number of members are in the DBD for a long time, remaining entitled to its many benefits.

FIND OUT MORE

For an example of how the DBD provided protection to DBD members from the impact of the Global Financial Crisis, see our case study demonstrating sample benefits on pages 5 to 6.

[1] An accumulation fund comprises member and employer contributions, investment returns, less fees, costs, insurance premiums and taxes.

[2] Contribution flexibility allows most members to reduce down to zero how much they pay.

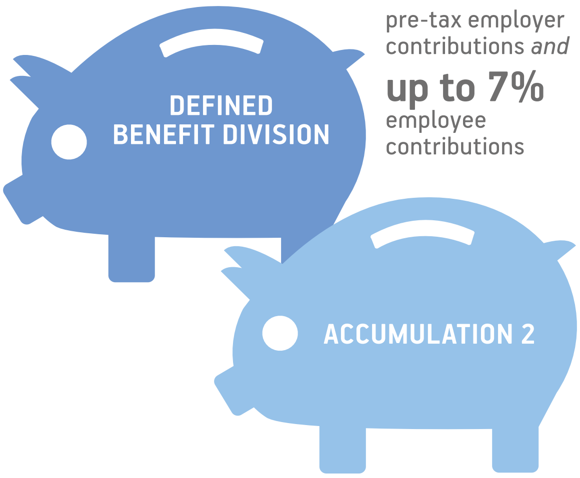
Who can join the DBD?

A member's employment contract will determine whether they're entitled to join the DBD. For example, most permanent employees in the higher education and research sector join the DBD while most employees on short-term contracts are only eligible for accumulation-style benefits.

Within their first 24 months of membership, members eligible to join the DBD can choose to opt out of the DBD and move to an accumulation-style benefit. During this time, UniSuper provides members with tools and seminars to assist in making this important decision.

Members can easily identify their nominated membership category by referring to their benefit statement, MemberOnline or welcome letter. UniSuper's Helpline can also provide more information on **1800 331 685**.

PERMANENT EMPLOYEES:



17% pre-tax employer contributions *and* **up to 7%** employee contributions

FIXED TERM CONTRACTORS:

9.5% pre-tax employer contributions

Eight advantages of being a DBD member

PROTECTION FROM MARKET DOWNTURNS
With the pooling of assets across the membership, the DBD provides benefits that are not directly subject to volatile market movements

SALARY LINKED BENEFITS
These provide members with an increased ability to more effectively estimate their benefit at retirement

INSURANCE
Inbuilt death and disablement benefits

STEADY, STABLE, RELIABLE GROWTH
See case study on pages 5 and 6

TRANSFERABLE MEMBERSHIP
Membership is transferable to many other university and research employers

GENEROUS TAX RULES
These apply on contributions, particularly for those who joined prior to May 2009

STRONG FINANCIAL MANAGEMENT
This is provided through the Board and industry leading advisors

EXPERT ANALYSIS
The DBD investment strategy is managed by UniSuper experts and advisors with no requirement for members to actively monitor markets

Managing the DBD for the long term

The DBD is backed by a $16 billion portfolio of pooled assets, with strong financial management.

The DBD's central investment objective is to maximise the probability of generating sufficient returns to meet its future benefit payments.

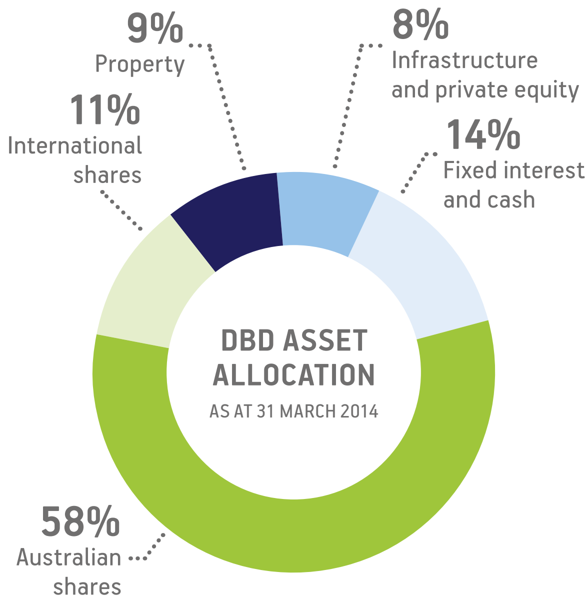
As outlined earlier, a member's individual defined benefit is not directly determined by the market performance of these assets. Instead, all contributions are invested collectively in a diversified portfolio. This pool of funds is then drawn upon to meet members' resignation, retirement, death and disablement benefits when they become payable.

Although defined benefits are not directly affected by market movements, an effective investment strategy is crucial to maximise the likelihood that DBD members' benefits will be paid into the future.

The composition of the portfolio supporting the defined benefits—for example, its mix between growth and defensive assets, and between domestic and international markets—is set by the Trustee, having regard to the need to pay out all members' benefits as they fall due.

In managing this portfolio, UniSuper has a preference for assets which are expected to deliver reliable income streams with potential for capital growth. Some assets that the DBD has exposure to include:

- 'Blue chip' companies within the Australian stock market, such as our major banks, retail property trusts (Colonial Retail, GPT and Scentre Group), listed infrastructure companies (Transurban and Sydney Airport) and Telstra.
- International shares heavily skewed to the higher growth markets of Asia, and high growth US companies, particularly in the technology sector.
- UniSuper owns 49% of Adelaide airport and has direct investments in property concentrated in the very resilient retail sector. As an example, the Fund owns 100% of Karrinyup, arguably Perth's premier shopping centre.



The process of estimating the DBD's future liabilities is based on expert inputs and assumptions, which can be changed from time to time. These assumptions relate not just to investment market conditions, but to other factors, such as higher education sector employment trends, expected salary growth and health and longevity (life expectancy) trends among the fund's membership base.

Rather than using a static investment approach which many other DB funds employ, the Trustee has implemented a dynamic asset allocation approach for the DBD's assets.

Under this approach, the assets are invested by reference to the level of the DB funding ratios. In simple terms, as the funding ratios improve, the allocation to defensive assets is increased.

This innovative strategy aims to smooth out volatility and reduce the risk of future falls in funding levels.

The DB formula

Benefit salary ✖ Benefit service ✖ Lump sum factor

The benefit salary in respect of membership is averaged over five years instead of three and is no longer indexed by CPI. See page 7 for more information.

Members who joined prior to 1998 may choose to take a lifetime pension.

Note: the benefit amount will be reduced by certain factors if the member has elected Contribution Flexibility or has not always been in full-time employment (e.g. had periods of part-time service, leave without pay or breaks in employment). These factors have been excluded here for the purposes of simplicity.

Age-based lump sum factors and time in the higher education and research sector

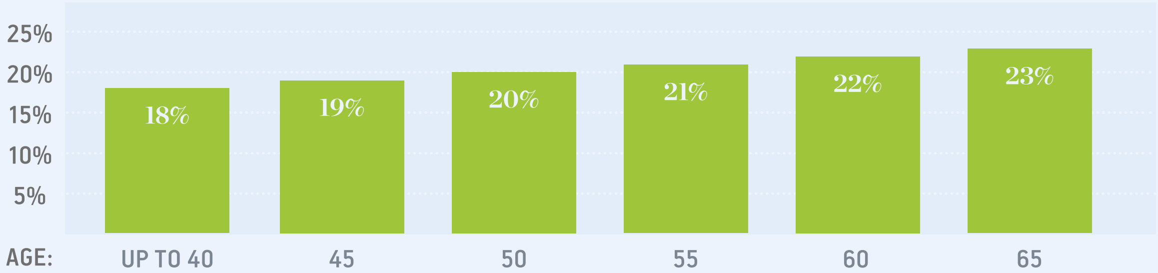
While employer contributions to the DBD are made at the same percentage of pay for most DBD members, the lump sum factors that determine a member's ultimate defined benefit increase with age.

Lump sum factors are based on the member's age when he/she leaves the DBD (not the age at which the member joins the DBD).

The graph below shows how the lump sum factor changes as a member nears retirement age. As older members tend to have contributed for longer than younger members, lump sum factors increase with age.

Importantly, the DBD *does not* require young members to remain in the DBD to cross subsidise the benefit accruals of older members.

Superannuation lump sum factors by age



While members young and old can benefit from the many advantages of the DBD, such as having their benefits linked to their salary, the DBD particularly rewards members planning a longer term career in the sector.

DBD members can better plan their benefit at retirement with greater certainty than accumulation members (see pages 5 and 6 for more information).

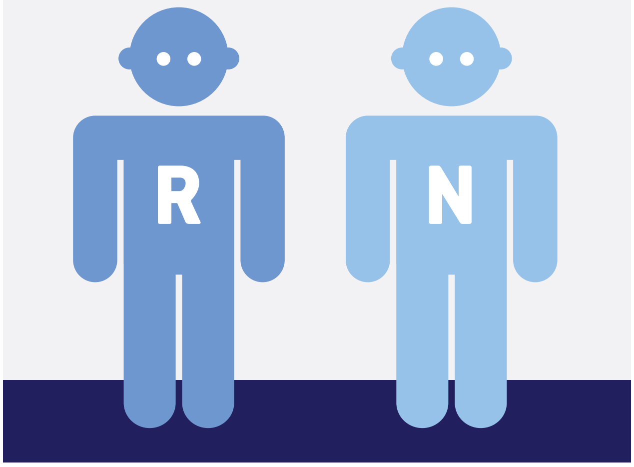
The DBD was established for permanent staff in the higher education and research sector. It's important to note that the age at which a member leaves the sector determines their lump sum — not their joining age. The member's salary and service also play a very important role.

UniSuper members can contribute to the DBD as long as they continue working in the higher education and research sector. Membership is transferable to many other university and research employers.

HOW THE DBD PROVIDES GREATER CERTAINTY

One of the key advantages offered by the DBD is greater protection from the effects of poor investment market performance, as occurred most recently during the Global Financial Crisis (GFC). Here we illustrate how the respective benefits of a DBD member and an Accumulation 2 member would have been impacted by investment performance over a 13 year period beginning 1 July 2000.

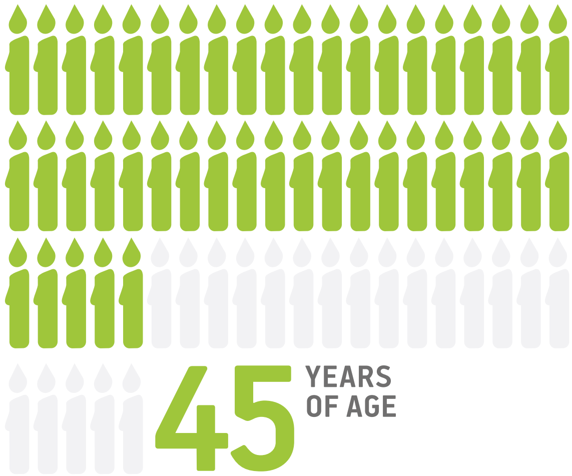
JULY 2000: ROB AND NICK ARE UNISUPER MEMBERS WITH A LOT IN COMMON



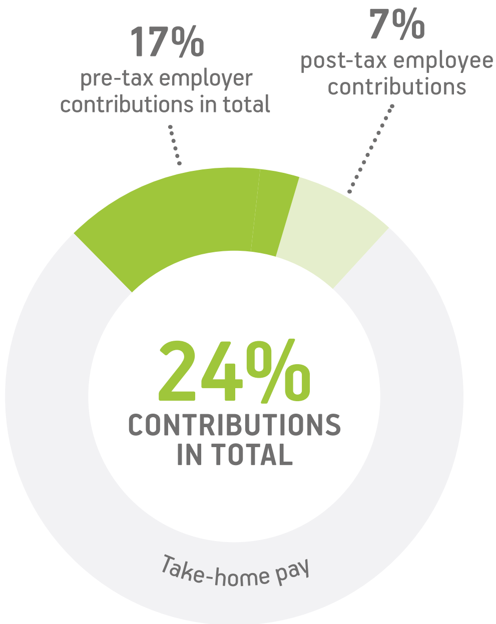
SAME ANNUAL SALARY

$100,000 P.A. WITH 5% GROWTH EACH YEAR

SAME AGE

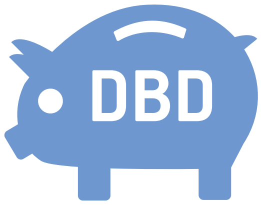


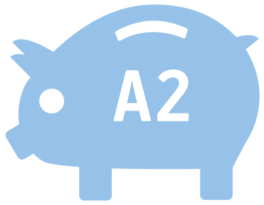
SAME SUPER CONTRIBUTIONS



SAME RETIREMENT SAVINGS

DIFFERENT PRODUCTS





ROB IS A UNISUPER DEFINED BENEFIT DIVISION MEMBER OF 15 YEARS

Formula-based benefits, based on salary and years of service. The main advantage of the DBD is a cost-effective smoothing of investment returns achieved through collective risk-sharing.

NICK IS AN ACCUMULATION 2 (A2) MEMBER INVESTED IN THE BALANCED OPTION

Market-based benefits, determined by a number of potential investment options covering a range of sectors and risk categories.

PROTECTION + PREDICTABILITY

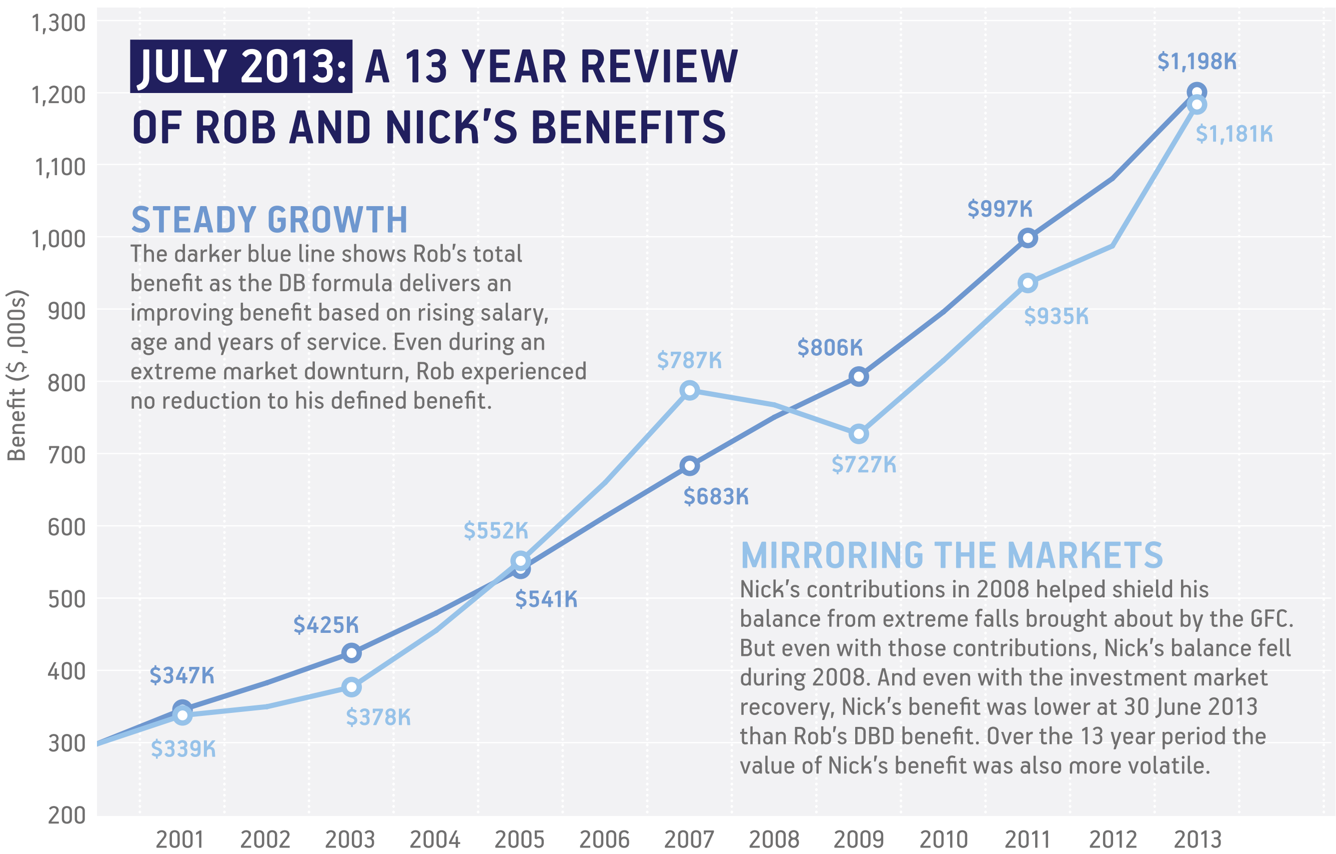
Using actual investment returns, the graph below shows two key DBD strengths when compared with an accumulation-style benefit:

1 PROTECTION FROM INVESTMENT MARKET DOWNTURNS

With the pooling of assets across the DBD membership, the DBD can provide benefits that are not directly subject to volatile market movements. Even during the GFC, one of the worst economic downturns in recent history, defined benefits were paid in full.

2 INCREASED ABILITY TO PREDICT FUTURE BENEFITS

Unlike an Accumulation arrangement, DBD members can better plan for their retirement as defined benefits are based on a salary-based formula and are not directly exposed to investment market downturns.



A 13 year period, which encompassed the GFC, has been chosen to illustrate that the DBD can provide members with a greater degree of certainty than an accumulation-style benefit, which can be quite volatile. For some members this greater certainty may be very important, particularly as they approach retirement. If we were to consider different periods, the results could be very different from those indicated above. Different results could also arise depending on the profile of the particular member (age, salary and service length) and the accumulation investment option selected. Note also that the Trustee has announced reductions to how future benefits will accrue from 1 January 2015. See page 7 for more information.

How the DBD is monitored

UniSuper's Trustee—its Board of Directors—manages the financial position and long-term sustainability of the DBD by adhering to the Trust Deed.

The Trust Deed sets out the rules and processes the Trustee follows. Clause 34 of the Trust Deed provides a process to manage the DBD's financial position, including a mechanism to reduce benefits if necessary.

The Trustee uses two key actuarial measures to track the health of the fund; the Vested Benefits Index (VBI) and the Accrued Benefits Index (ABI). Under Clause 34, if the Actuary's Board report advises that those measures have fallen below particular levels, UniSuper must notify members and employers.

Four years after receiving this advice, if the Actuary's subsequent report advises that the fund's position has not improved sufficiently, the Trustee must consider whether it is in the interests of all DBD members to reduce defined benefits payable.

To ensure the DBD delivers against its investment performance objectives, the Trustee requires reasonable time to closely monitor the DBD's financial position. Four year monitoring periods mean that the Trustee can make decisions in DBD members' best interests. If benefit reductions are required, the Trustee must do this on a fair and equitable basis for all DBD members.

Under clause 34 there are now three concurrent four year monitoring periods. They conclude on 30 June 2015, 30 June 2016 and 30 June 2017 respectively. At the end of these periods the Trustee may consider if defined benefit reductions are required. For more DBD information see **unisuper.com/dbdupdate**.

Key risk

While the DBD provides many member advantages, like all investments, it carries some risk. In the event of a shortfall of assets caused by a prolonged market downturn or other factors, the Trustee may reduce defined benefits in the future. Therefore members must consider this risk.

Strong financial management and excellent investment returns have ensured that the fund has paid in full the benefits of all DBD members leaving the fund, even during the GFC (see pages 5 and 6) , which saw significant reductions in accumulation-style benefits.

Salary formula change from 1 January 2015

Changing investment market expectations have influenced the anticipated cost of providing benefits. Increased life expectancy and changes to salary growth since the DBD was established are additional factors that the Trustee must take into account in managing the fund's sustainability. The DBD needs to adapt to changing membership needs and economic times.

To protect the DBD's ability to pay future benefits, the Board decided (under Clause 34) that members' Benefit Salary will be averaged over the last five years of employment (instead of three years) and will no longer be indexed with changes in the consumer price index.

Benefits DBD members accrue up to 1 January 2015 will not be affected. The previous three-year average and indexed Benefit Salary definition will continue to apply to service accrued prior to this date.

The ongoing risk of having to reduce benefits under Clause 34 is mitigated by the pooling of DB assets and the approach taken to manage these assets. For a more detailed overview of the risks, refer to the product disclosure statement (PDS) available at **unisuper.com.au/pds**. To understand the risks that Accumulation 1 and 2 members must consider, see the relevant PDS.

Two key measures used by the Trustee to monitor the DBD's financial health

VESTED BENEFITS INDEX

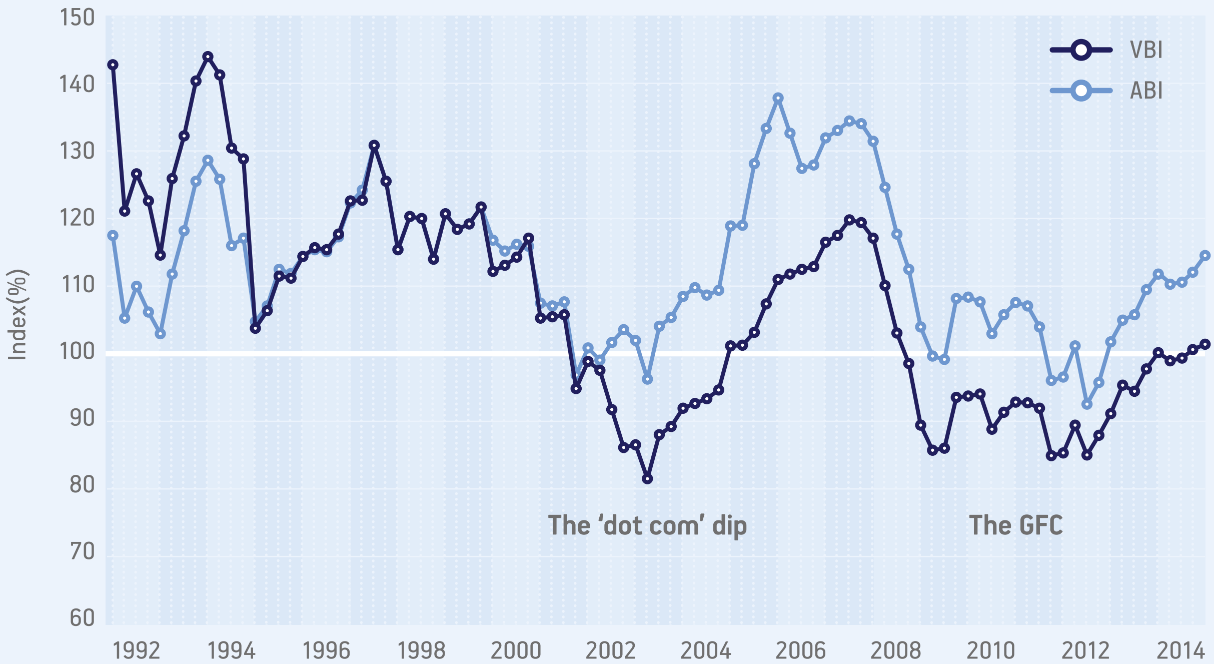
The Vested Benefits Index (VBI) reflects the capacity of the DB to pay out all members' defined benefits from existing assets in the highly unlikely event that *all* members were to exit the DBD on the date of the calculation.

UniSuper regularly reports this measure to the Australian Prudential Regulatory Authority (APRA).

ACCRUED BENEFITS INDEX

The Accrued Benefits Index (ABI) is the ratio of assets to a different measure of the DBD's liabilities. It measures the ability of the Fund to pay, over the long term, benefits accrued to date. The ABI is the ratio of assets to liabilities, taking into account the expected rates at which members resign, die or retire from the Fund and the benefits they would receive at the time due to service at the date the ABI is calculated. Each quarter UniSuper publishes an estimate of the ABI and VBI measures at **unisuper.com.au/dbdupdate**.

Defined Benefit Division VBI and ABI



The above graph illustrates the history of the DBD's funding position since 1991. The ABI tends to be the more relevant index to consider as it represents the best estimate of the value of the liabilities on the more realistic assumption that not all members would leave the DBD on a single day. Both measures are based on a range of assumptions that can and do change from time to time. More information about the ABI and VBI is available at **unisuper.com.au/dbdupdate**.

Why the DBD remains an open fund

UniSuper DBD members have access to an extremely valuable package of superannuation benefits that stand out in today's complex and crowded financial services market place.

UniSuper is one of the few defined benefit funds in the country that remains open and continues to accept new members. It has been specifically designed for the higher education and research sector.

For 31 years, UniSuper has committed the time, resources and independent expert advice necessary to ensure strong management of the DBD and its long-term viability.

Key stakeholders in UniSuper, including the Trustee and employers, recognise that the profile of UniSuper's DBD membership and the DBD's advantages continue to position it as a valuable product.

It provides permanent higher education and research staff with attractive superannuation benefits. The DBD has a track record of enduring challenging economic times, in part due to pooling the $16 billion asset base across almost 80,000 members.

UniSuper's DBD members are regarded as defined benefit members under Australian superannuation law. This is why the fund is called the Defined Benefit Division.

Funding shortfalls are not required to be covered by employers. The benefits provided by the DBD are hence not guaranteed to be paid. However, even without an employer guarantee, the expert management of the Fund by the Trustee should reassure members that the defined benefits will be paid as they fall due.

THE DBD BY NUMBERS*

78,000

CONTRIBUTING MEMBERS FROM AUSTRALIA'S HIGHER EDUCATION AND RESEARCH SECTOR

$16B

IN ASSETS UNDER MANAGEMENT

44 YRS

AVERAGE AGE OF DBD MEMBERS

8,000

MEMBERS RECEIVING A DBD PENSION

$250M

ANNUAL BENEFITS PAID TO DBD PENSIONERS

* These figures are approximate as at 30 June 2014.

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