UniSuper

UniSuper's Defined Benefit Division explained

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

June 2017

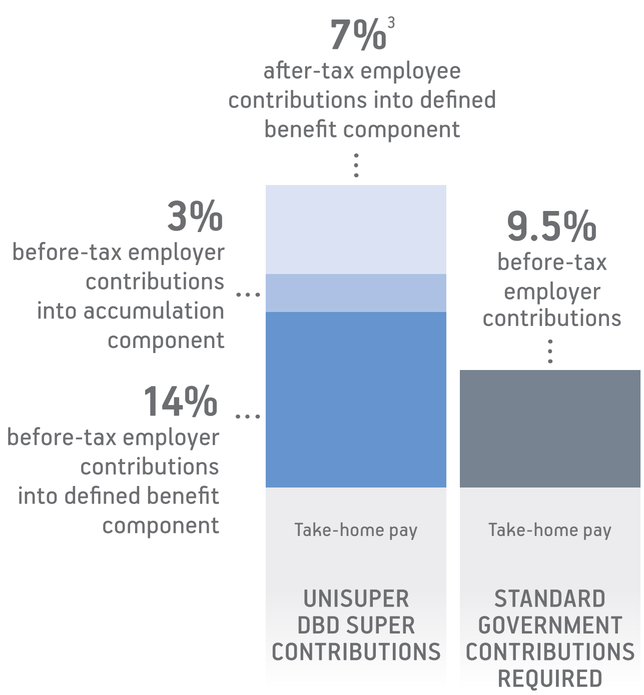
What is the Defined Benefit Division?

The Defined Benefit Division (DBD) is a $22 billion[1] asset pool invested in shares, property, infrastructure, bonds and cash. Most DBD members' contributions are invested in this DBD asset pool. The remaining portion is usually allocated to the member's accumulation component and can be invested in up to 16 investment options. Final member benefits are the total of both the defined benefit component and the accumulation component.

The defined benefit component is 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[2] funds work where accounts are directly 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—currently 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 DBD 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 portfolio of pooled assets which are professionally 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 (GFC), see our case study on pages 5 to 6.

[1] Approximate as at 30 April 2017.
[2] An accumulation fund comprises member and employer contributions, investment returns, less fees, costs, insurance premiums and taxes.
[3] Contribution flexibility allows most members to reduce down to zero how much they pay.

Who can join the DBD?

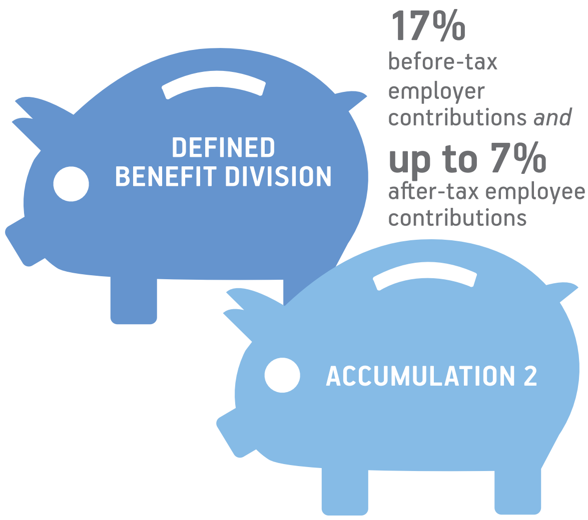
A member's employment contract will determine whether they're entitled to join the DBD. For example, most permanent employees in the higher education and research sector join the DBD while most employees on short-term contracts are only eligible for accumulation-style benefits.

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

You can easily identify your nominated membership category by referring to your benefit statement, MemberOnline or welcome letter.

If you'd like more information, you can also call us on **1800 331 685**.

PERMANENT EMPLOYEES:



SHORT-TERM CONTRACTORS:

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 before May 2009

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

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

Managing the DBD for the long term

The DBD is backed by a $22 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.

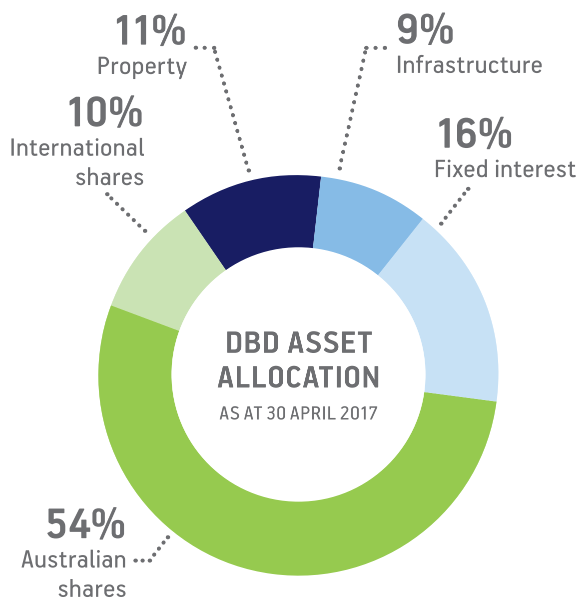
The composition of the portfolio supporting the defined benefits— for example, its mix between growth and defensive assets, and between domestic and international investments —is set by the Trustee, having regard to the need to pay out all members' benefits as they fall due.

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 toward established companies with a record of stable earnings. Examples of holdings include global listed infrastructure and quality household names such as Colgate-Palmolive, Nestlé and Johnson & Johnson.
- 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 following pie chart shows the general asset allocation of the DBD portfolio at 30 April 2017.



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 defined benefit (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 generally increased.

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

How your defined benefit is calculated

The benefit salary in respect of membership is generally averaged over five years. See page 7 for more information. Members who joined before 1998 may choose to take a lifetime pension.

Benefit salary × Benefit service × Lump sum factor

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

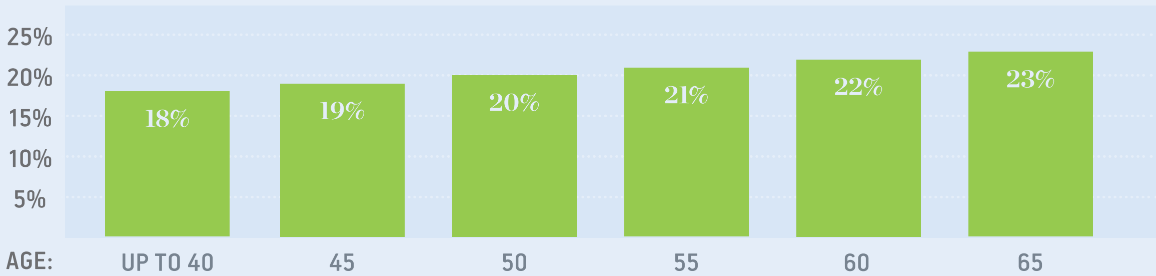
While employer contributions to the DBD are made at the same percentage of pay for most DBD members, the lump sum factor that determines a member's ultimate defined benefit increases with age.

The lump sum factor is based on the member's age when they leave the DBD (not the age at which the member joins the DBD).

The following 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, the lump sum factor increases 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 factor 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 generally 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.

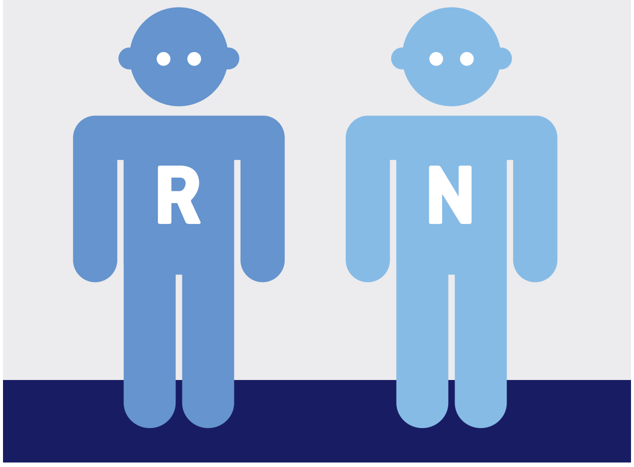
It's important to note that the age at which a member leaves the sector determines their lump sum—not their joining age. The member's salary and service also play a very important role.

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

HOW THE DBD PROVIDES GREATER CERTAINTY

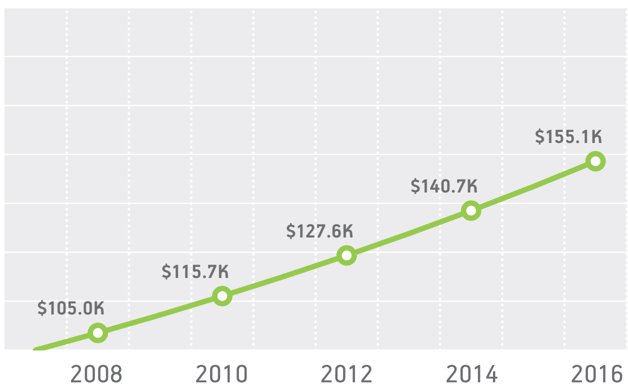
One of the key advantages offered by the DBD is greater protection from the effects of poor investment market performance, as occurred during the GFC. Here we illustrate how the respective benefits of a DBD member and an Accumulation 2 member would have been impacted by investment performance over a 10-year period beginning 1 July 2007.

JULY 2007: ROB AND NICK ARE UNISUPER MEMBERS WITH A LOT IN COMMON.

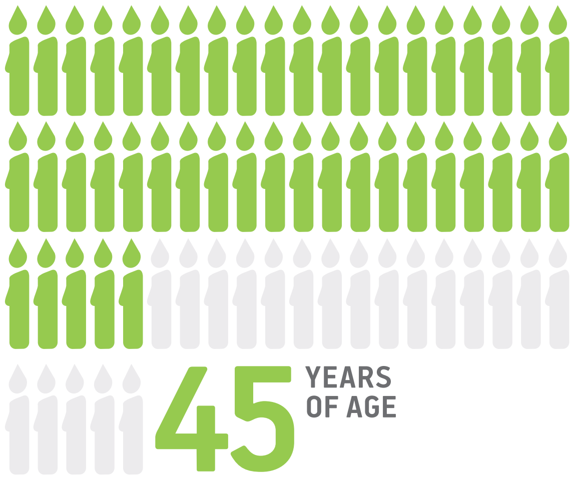


SAME ANNUAL SALARY

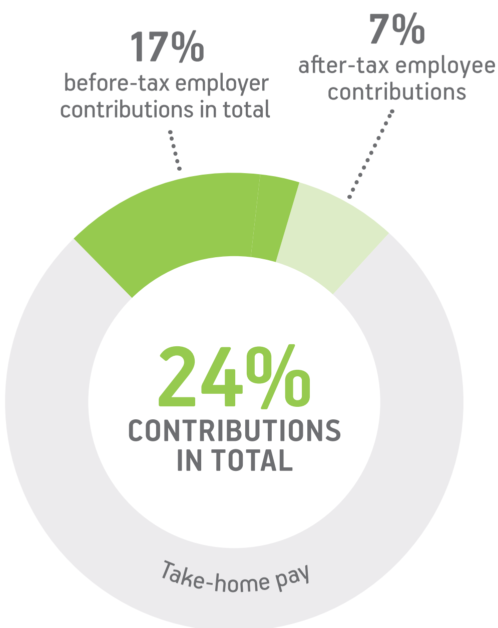
$100,000 P.A. WITH 5% GROWTH EACH YEAR



SAME AGE

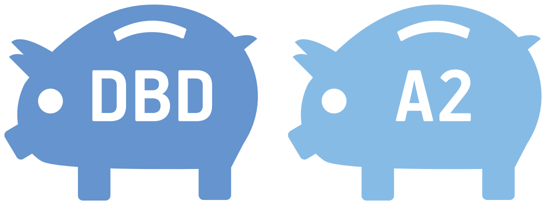


SAME SUPER CONTRIBUTIONS



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

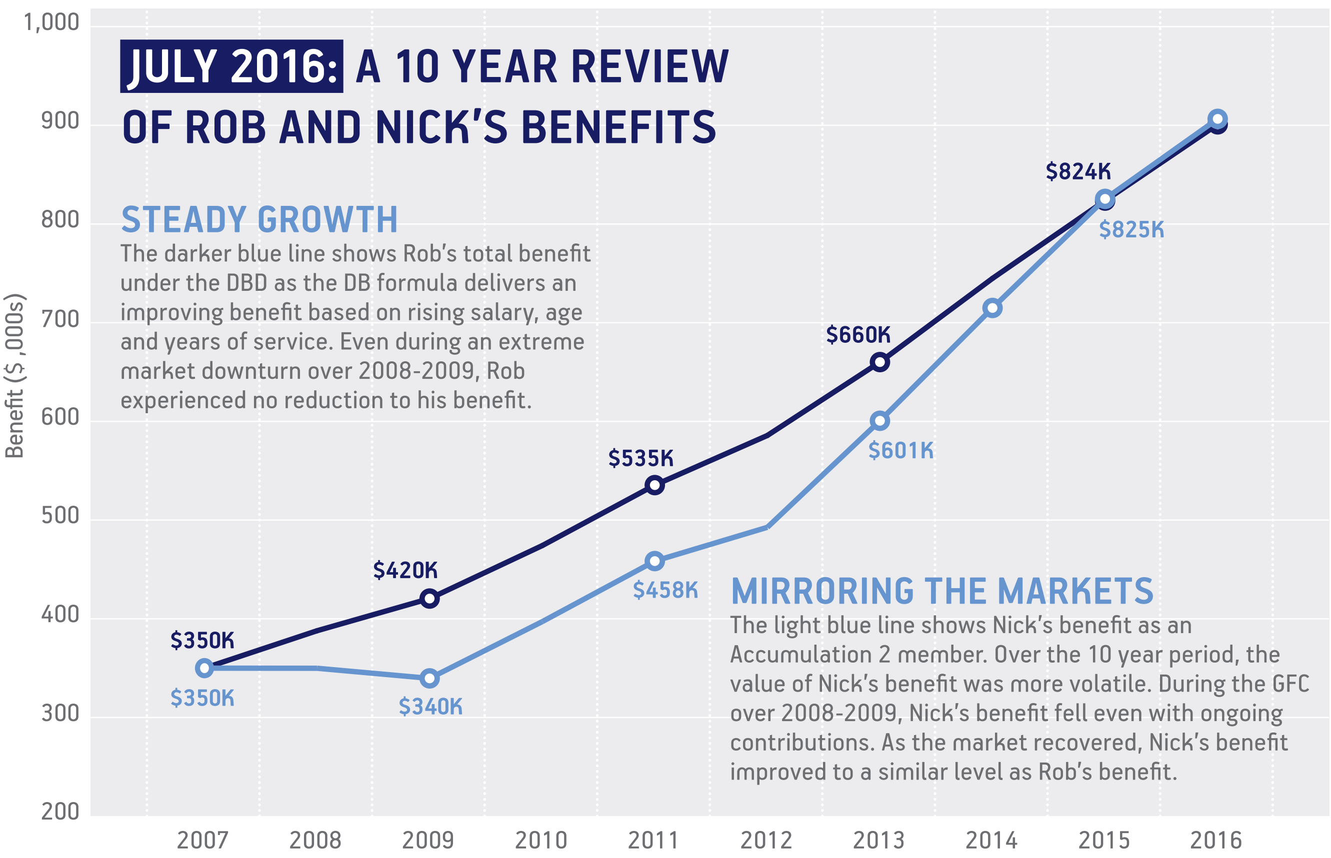
Using actual investment returns, the graph below shows two key DBD strengths when compared with an accumulation-style benefit:

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 10-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. Difference results could also arise depending on the profile of the particular member (age, salary and service length) and the accumulation investment option selected.

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 is one monitoring period that concludes on 30 June 2017. At the end of the period the Trustee may consider if defined benefit reductions are required. For more historical information about the DBD, see **unisuper.com.au/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, for example, 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 otherwise saw significant reductions in accumulation-style benefits.

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 DBD 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.

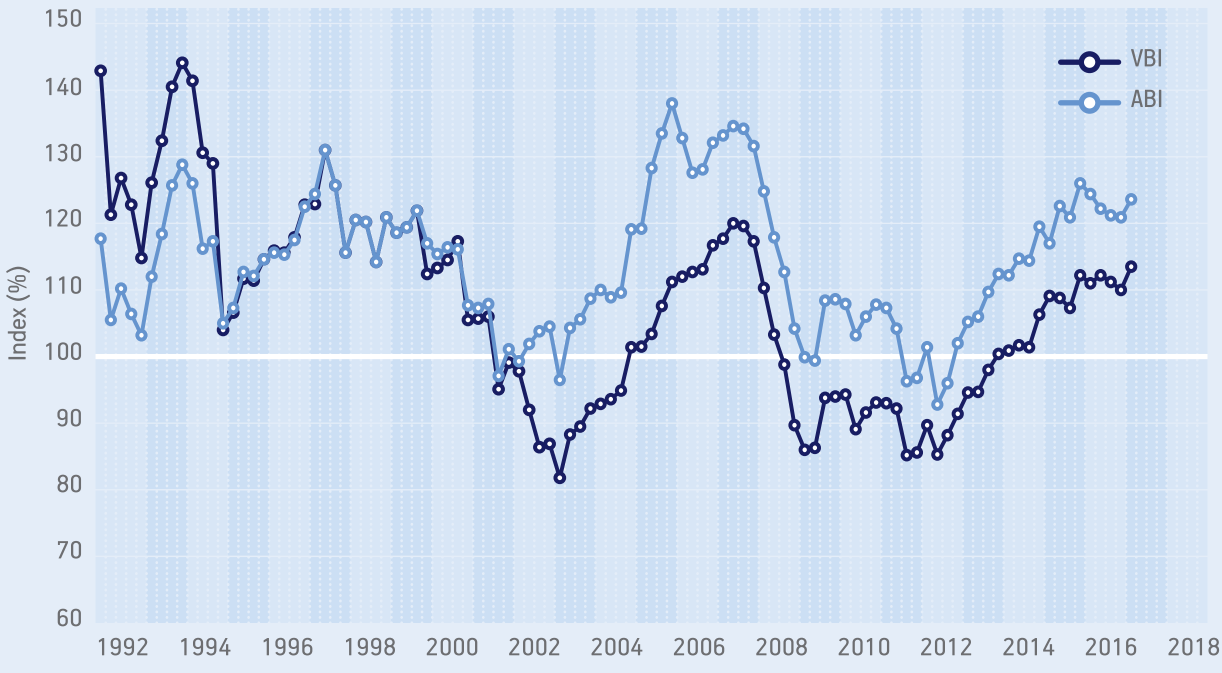
UniSuper regularly reports this measure to the Australian Prudential Regulatory Authority (APRA).

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 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 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 super 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 nearly 35 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 $22 billion asset base across more than 80,000 members.

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

It is important to note that funding shortfalls are not required to be covered by employers. The DBD's benefits are therefore 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 may be paid as they fall due.

THE DBD BY NUMBERS*

OVER
80,000
CONTRIBUTING MEMBERS FROM AUSTRALIA'S HIGHER EDUCATION AND RESEARCH SECTOR

$21B
IN ASSETS UNDER MANAGEMENT

45 YRS
AVERAGE AGE OF DBD MEMBERS

OVER
8,000
MEMBERS RECEIVING A DBD PENSION

$320M
ANNUAL BENEFITS PAID TO DBD PENSIONERS

*These figures are approximate as at 30 June 2016

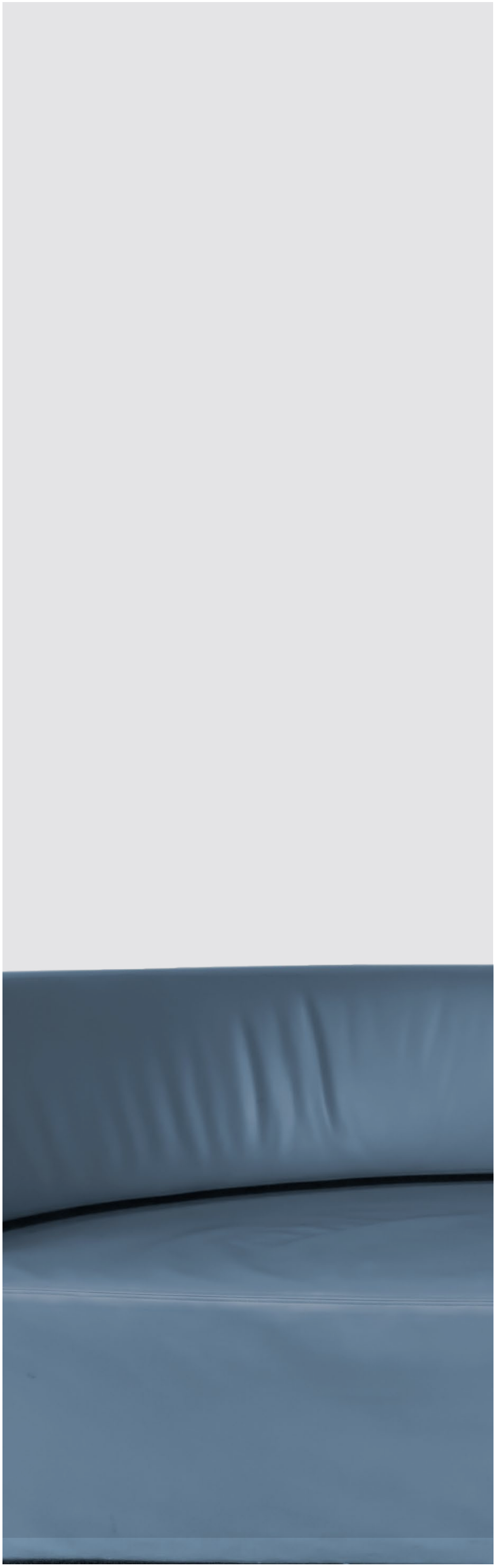
HELPLINE
1800 331 685

WEBSITE
unisuper.com.au

EMAIL
enquiry@unisuper.com.au

FAX
+61 3 9910 6141

ADDRESS
UniSuper,
Level 1,
385 Bourke Street,
Melbourne, VIC 3000,
Australia



Prepared by UniSuper Management PTY LTD (ABN 91 006 961 799, AFSL No. 235907) on behalf of UniSuper Limited (ABN 54 006 027 121) the trustee of UniSuper (ABN 91 385 943 850).

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