



29 May 2006

Professor Alan Robson
Vice-Chancellor & President
The University of Western Australia
25 Stirling Highway
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Dear Professor Robson

I write to inform you of changes in the underlying management of the UniSuper Defined Benefit Plan (DBP). Whilst I have been consulting with you on the consultation paper the Board has also been furthering its work in ensuring that the DBP is managed prudently ensuring that the risk of returning to an unsatisfactory financial position is minimised.

You will recall from previous communications that, over the full life of the DBP (now approaching 25 years), the general experience has been for the Plan's assets to comfortably exceed its liabilities, based on a constant contribution rate of 21% and a relatively aggressive allocation of investments to growth asset markets such as shares, property and infrastructure. Indeed, during the 1990s, the financial experience of the Plan was so positive that the Trustee was able, on actuarial advice, to make surplus distributions to members and pensioners on a number of occasions.

However, the downturn in investment markets in the years 2002 and 2003 presented a significant challenge to the DBP, with the requirement imposed by regulations for UniSuper to disclose an "unsatisfactory financial position" for the Plan during those years when its Vested Benefit Index (VBI) fell to below 100% of liabilities.

The Trustee and Actuary affirmed at the time that an alternative measure, the Accrued Benefit Index (ABI) was in fact a more suitable measure to consider, in the case of a large multi-employer plan like UniSuper. Nevertheless, even though the ABI did not fall below 100%, the experience of the market downturn did pause the Trustee to consider a range of initiatives to ensure the on-going prudent management of the Plan including a decision to invoke Clause 34 (a) of the UniSuper Trust Deed.

A further, medium-term initiative was to commence a comprehensive review of the asset and liability structure of the DBP, having regard to the changed investment environment. Among the issues addressed by this review were:

- Whether there were any structural changes in the global investment environment that might warrant a re-consideration of the Plan's investment objectives, asset mix and benefit structure; and

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- Whether a suitable balance existed in the DBP's asset portfolio between maximising the likelihood of meeting the Plan's liabilities at an acceptable level of investment risk on the one hand, and making further potential gains from market upturns on the other.

This review has resulted in two significant changes to the management of the DBP as follows.

i) Surplus Distribution Policy

The Board's previous surplus distribution policy, adopted in 2000, was that the Trustee could consider surplus distributions when the VBI exceeded 110% of liabilities. The Board has now formally cancelled that policy. In its place, the Board has adopted a surplus distribution policy consisting of the following components:

- A surplus distribution threshold equal to a VBI of 130%;
- Distribution of half the surplus above this threshold, when it is available, with the balance carried forward;
- Yearly reviews (as at 30 June) of distributable surplus for the active member component; and
- Three-yearly reviews (also at 30 June) for the pensioner component.

ii) Change to DBP Asset Allocation

As you would expect the Board considers one of its major roles to be the continual monitoring of the risk within the DBP and so when the VBI reached 113% at 31 December 2005 the Investment staff revisited the asset liability study to reassess the risk appetite of the Plan.

As a result of this further review the Trustee in February this year reduced the level of the DBP's exposure to growth asset markets from a total of 85% of the portfolio to 70%.

In investment terms, this transition involved considerable implementation logistics and the utmost confidentiality. The transition involved the transfer of roughly \$1.3 billion of assets from Australian and international equities, to Australian and international fixed interest assets within a period of only a few weeks, without disturbing the markets or allowing other market participants to foreshadow our moves and seek to exploit them for their own purposes. This transition exercise commenced in mid February 2006 and was completed in early March 2006.

It is important to emphasise that this change in asset allocation should in no way be seen as being a short-term 'tactical' move reflecting a particular view about the immediate-term risks inherent in investment markets. Rather, it is a strategic change driven by a re-assessment of the underlying drivers of the DBP's benefit structure, its liability profile, and the need to align the asset allocation more closely with the Plan's primary objective, which is to deliver on its liabilities to members.

It should also be emphasised that, with a 70% exposure to growth assets, the DBP is still positioned to participate strongly in the upside of current and future market movements, and to retain a significant exposure to alternative assets such as infrastructure and private equity, which have contributed to the returns achieved over the past few years.

The two actions detailed above have been taken in pursuit of the underlying objectives of ensuring that the Defined Benefit Plan has the greatest chance of delivery on the promise to members.

We are also planning to communicate with DBP members on the risks within the Plan in tandem with our Annual Report distribution, scheduled for the August-September period.

Please do not hesitate to contact me if you would like any further clarification of the matters raised in this letter, either by telephone on (03) 9691 4102 or by email to ann.byrne@unisuper.com.au.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'A Byrne', written in a cursive style.

Ann Byrne
Chief Executive Officer
UniSuper Limited

cc Mr Bob Farrelly
Director, Human Resources