

Report and Accounts

for the year ended
31 March 2006

Universities Superannuation Scheme Limited is the corporate trustee of one of the largest private sector pension funds in the UK with assets at 31 March 2006 of around £28 billion.

It was established in 1974 to administer the principal pension scheme for academic and senior administrative staff in UK universities and other higher education and research institutions.

The head office is at Royal Liver Building, Liverpool and the London Investment Office is at 99 Bishopsgate, London.

The registered number of the Trustee Company (USS Ltd) at Companies House is 1167127

The reference number of the Scheme (USS) at the Pension Schemes Registry is 100201003

USS

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The year to 31 March 2006 was another very busy year for pension schemes including USS with, in particular, changes to the tax rules governing pension schemes coming into effect on 6 April 2006 (A-day). Membership of the scheme continues to grow while another year of positive investment performance has seen the value of the fund rise to over £28 billion. The scheme's active membership increased by 5.1% from 110,000 to 115,600 and there was substantial growth in the numbers of pensioners and those entitled to deferred benefits to 44,700 (up by 5.9%) and 66,100 (up by 5.4%) respectively. The total membership at 31 March 2006 was almost 224,400, an increase of 33% in five years.

The fund's investment return for the calendar year to 31 December 2005 of 24% exceeded its benchmark of 22.8% and this helped the total value of the fund to increase to £28.3 billion at 31 March 2006. The ten-year return of the fund of 7.9% per annum comfortably exceeds both earnings growth and retail price inflation over the same period.

The officers carried out a review during the year of potential systems to replace the scheme's existing pensions administration software, the Universal Pensions Management System (UPM) from Comino plc. In July 2005, the trustee company decided that Comino's replacement software, UPM version 2, was the best solution for the company's business needs. Following a detailed feasibility study and extensive contractual negotiations, the project to replace the pensions administration system commenced in February 2006 with the system being successfully implemented to our test environment in March. The new system is scheduled to go live during 2007/08 and we are confident that it will provide a good technology platform from which we can continue to provide more than satisfactory service levels across more diverse media to an ever increasing membership.

The results of the last triennial actuarial valuation of the scheme as at 31 March 2005 revealed that the assets of the scheme at the valuation date were 77% of the accrued liabilities, having been 101% of the liabilities at 31 March 2002. The fall in the funding level arose primarily as a result of the fall in equity markets since the last valuation. The fund continues to enjoy a positive cashflow with the aggregate of contributions and investment income exceeding benefit payments, and this is expected to continue for many years. In these circumstances the deficit is not of immediate concern since USS has no requirement to realise investments to meet its pensions liabilities. There is considerable scope for variation in the funding level, depending on the various economic circumstances that can arise and assumptions used to measure the value of the scheme's liabilities, and indeed, following the excellent investment performance since the valuation date, the funding level had increased to around 89% at 31 March 2006. Nevertheless, there are increasing pressures

on the funding of the scheme - a more competitive recruitment market in the sector, improving mortality and new statutory funding regulations - and these and other issues will need to be considered by the trustee company, and indeed the sector, in the coming months. We shall, however, continue to do what is necessary to ensure that the scheme can meet its obligations while remaining affordable for both employers and members.

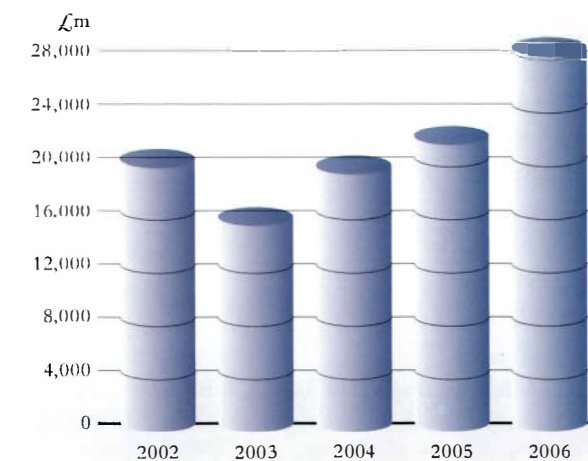


Martin Harris
Chairman



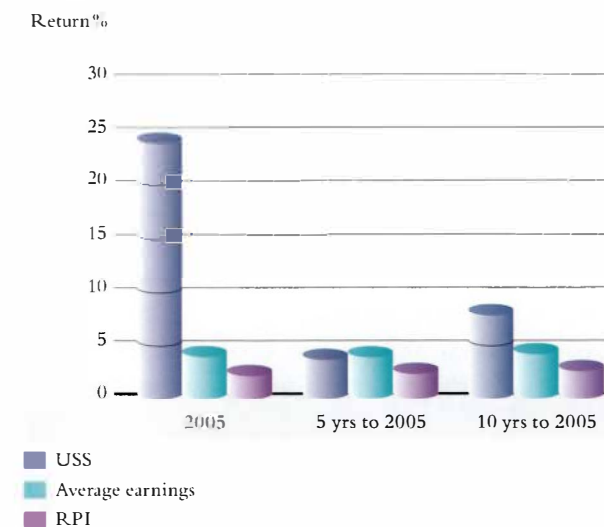
Tom Merchant
Chief Executive

FUND



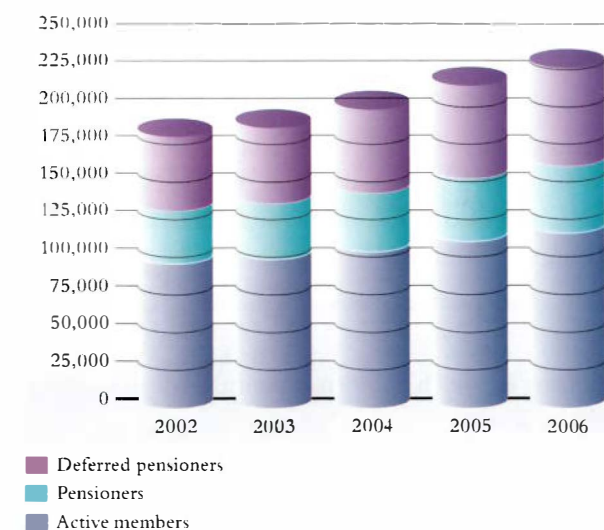
The fund's investments have increased from £20 billion in 2002 to £28.3 billion as at 31 March 2006. More details are given in the investment committee report on page 21 and in the five year summary of the fund accounts on page 77.

PERFORMANCE



Strong investment returns in 2005, together with good returns for 2003 and 2004, have seen the fund's position improve, resulting in the five year return exceeding RPI but slightly below average earnings. Over ten years, the fund has comfortably exceeded both RPI and average earnings. More details are given in the report of the investment committee on page 21.

MEMBERSHIP



PRINCIPAL OFFICERS AND ADVISERS

The principal officers and advisers of the trustee company at 1 August 2006 are:

<i>Chief Executive</i>	T H Merchant
<i>Chief Investment Officer</i>	P G Moon
<i>Chief Financial Officer</i>	C S Hunter
<i>Pensions Policy Manager</i>	B Mulkern
<i>Pensions Operations Manager</i>	B Steventon
<i>Company Secretary</i>	I M Sherlock
<i>Head of IT</i>	I J Hall
<i>Communications Manager</i>	C G Busby
<i>Actuary</i>	E S Topper of Mercer Human Resource Consulting Limited Clarence House, Clarence Street, Manchester M2 4DW
<i>Solicitors</i>	DLA Piper Rudnick Gray Cary UK LLP India Buildings, Liverpool L2 0NH
<i>Auditors</i>	KPMG LLP, St James' Square, Manchester M2 6DS
<i>Bankers</i>	Barclays Bank Plc, 4 Water Street, Liverpool L69 2DU

The principal other organisations acting for the trustee company during the year were:

<i>Solicitors</i>	Clifford Chance, Dundas & Wilson, Lawrence Graham, Mitchells Robertson, Fried Frank Harris Shriver & Jacobson
<i>Investment managers</i>	Capital International Limited, Legal & General Assurance, Wellington Management International, Goldman Sachs Asset Management International Ltd, Merrill Lynch Investment Managers, Henderson Global Investors Limited
<i>Investment consultants</i>	Mercer Investment Consulting
<i>Custodians</i>	State Street, JP Morgan Plc
<i>Investment performance measurement</i>	Investment Property Databank Limited, HSBC
<i>Retail property investment adviser and property manager</i>	Jones Lang LaSalle
<i>Commercial property investment adviser and property manager</i>	DTZ Debenham Tie Leung
<i>Property valuers</i>	Drivas Jonas
<i>Computer software</i>	Comino plc, Morse Limited, General Systems Ltd
<i>Website design</i>	Anthony Hodges Consulting Ltd
<i>Computer hardware</i>	ICM Computer Solutions plc
<i>Business continuity</i>	Synstar/Hewlett Packard
<i>Insurers</i>	Royal & Sun Alliance, AIG Europe (UK)

The trustee of Universities Superannuation Scheme (USS) is the trustee company, Universities Superannuation Scheme Limited (USS Ltd), which is appointed under USS rule 20.1. The statutory power of appointing new trustees applies provided that a new trustee may not be appointed without the approval of the joint negotiating committee.

The trustee company is also the scheme administrator of the scheme for the purposes of the Finance Act 2004.

The registered office of the trustee company to which enquiries about the scheme generally or about an individual's entitlement should be sent is:

Universities Superannuation Scheme Limited
Royal Liver Building, Liverpool L3 1PY

The membership at 31 March 2006 of the principal committees was as follows:

Management Committee

Appointed by Universities UK (UUK)

Sir Graeme Davies (Chairman), Sir Martin Harris (Deputy Chairman),
M S Potts, Baroness Warwick of Undercliffe

Appointed by the Association of University Teachers (AUT)

D Guppy, Lady Merrison, Professor Charles Sutcliffe

Appointed by the Higher Education Funding Councils (HEFCs)

S Egan

Co-opted

Professor John Bull, M Butcher, V Holmes, H R Jacobs

Finance & General Purposes Committee

Appointed by the management committee

Sir Martin Harris (Chairman), Professor John Bull, D Guppy, H R Jacobs,
Lady Merrison, M S Potts, Baroness Warwick of Undercliffe

Investment Committee

Appointed by the management committee

V Holmes (Chairman), G Allen, Professor John Bull, H R Jacobs,
Dr D C Nicholls, D Robins, Professor Charles Sutcliffe

Audit Committee

Appointed by the management committee

Dr Christine Challis (Chairman), Professor John Bull, Lady Merrison,
M S Potts, Professor Charles Sutcliffe

Remuneration Committee

Appointed by the management committee

H R Jacobs (Chairman), M Butcher, Lady Merrison, M S Potts,
Baroness Warwick of Undercliffe

Rules Committee

Appointed by the management committee

H R Jacobs (Chairman), A D Linfoot, J W D Trythall

Advisory Committee

Appointed by UUK

Dr A Bruce, A D Linfoot, C Vidgeon

Appointed by AUT

Dr A Roger (Chairperson

	Management	Investment	F&GPC	Audit	Remuneration	Rules	Nominations
Michael Potts	6 (7)	—	5 (5)	4 (4)	2 (3)	—	—
Professor Charles Sutcliffe	6 (7)	4 (4)	—	3 (4)	—	—	2(2)
J W D Trythall	3 (3)	2 (2)	2 (2)	—	2 (3)	2 (2)	—
Baroness Warwick	6 (7)	—	5 (5)	—	3 (3)	—	2(2)
Virginia Holmes	3 (4)	2 (2)	—	—	—	—	—
Dave Guppy	4 (4)	—	3 (3)	—	—	—	—
Steve Egan	1 (1)	—	—	—	—	—	—

*Mr Bell was absent from a number of meetings due to ill-health.

**Sir Howard Newby was absent from a number of meetings due to a clash in dates with HEFCE board meetings.

Regular reports and papers are circulated to committee members in a timely manner in preparation for all committee meetings. These papers are supplemented by information specifically requested by committee members from time to time. The management committee papers include the minutes of the meetings of all the principal committees of USS.

Institutions

At 31 March 2006 there were 378 institutions which had become member institutions by completing a deed of accession. They comprised all the 'old' UK universities (ie those established prior to 1992), including the constituent schools and colleges of the universities of London and Wales, all the colleges of the universities of Oxford and Cambridge and 238 other institutions.

Changes in institutions participating occurred as follows:

New participating institutions:

St Benet's Hall*	UK Socrates-Erasmus Council
Lhasa Limited	The Challenge Fund Trading Company Ltd*
The Biochemical Society*	University of Wolverhampton*
Society for Experimental Biology*	Glasgow Caledonian University*
Arts and Humanities Research Council*	University of the West of England*
Liverpool University Press 2004 Limited	University of Bolton*
The Young Foundation	Canterbury Christ Church University*
Educational Competencies Consortium Ltd	University of Winchester*
Florida State University IPA UK*	Oxford Said Business School
Open College Network Eastern Region	

* denotes an institution admitted only for employees who had been members of USS whilst in a previous employment.

Institutions which ceased to participate:

Ludwig Institute St Mary's Branch	International Research Foundation
Royal Institute of International Affairs	for Open Learning
Brunel Institute of Organisation and Social Studies	The Arts and Humanities Research Board
University College Winchester	Xceleron Ltd
University of Cambridge Challenge Fund	Sams Ardtoe

Scheme membership

During the year 18,664 new members joined the scheme and at 31 March 2006 the total membership, including pensioners and those entitled to deferred benefits, was 226,400 compared with 214,900 a year earlier. Further details of the changes in membership during the year are contained in the section "Membership Statistics" on page 48 and over the five years ended 31 March 2006 in the Summary on page 77.

The proportion of eligible new employees of participating institutions choosing not to join USS was 17% compared with 18% last year.

Members are now able to share pension scheme benefits with their ex-spouse in the event of divorce. There were 3,063 requests for information up to 31 March 2006 and 226 ex-spouses now have benefits in the scheme in their own right as a result of pension sharing.

Expansion and flexibility

In February 2006 the trustee company lifted the moratorium on mergers with other pension schemes in the higher education sector. This followed a detailed review of the expansion policy during 2005, which concluded that it was appropriate for USS to continue to extend an option for schemes in the sector to merge with USS. Some of the terms for merging have changed, in that only limited benefit variations are acceptable for deferred and pensioner members that transfer, and there will be a limitation on the number of mergers undertaken in any one year (a maximum of three to four). The financial terms for merging remain largely unchanged.

The government's pensions reform

There have been major legislative changes during the year to implement the government's radical revisions to the occupational pension scheme environment. On 6 April 2005 a number of features of the Pensions Act 2004 came into effect, notably with the creation of the Pensions Regulator, which is the new regulatory body for work-based pension schemes in the UK. The Pension Protection Fund (PPF) also opened for business at the start of the year, to provide compensation to members of defined benefit pension schemes formerly operated by insolvent employers. During the year, USS has been in liaison with the Board of the PPF as it has developed its format for the risk-based levy

Working parties

Over the year a number of working parties were set up to review and make recommendations on specific issues:

Expansion working party

At its meeting on 6 May 2005 the working party finalised its recommendations for the future policy for expansion of the scheme. During the year these recommendations were considered by the Finance and General Purposes Committee and Management Committee which has resulted in the lifting of the moratorium described in the "Expansion and flexibility" section above.

Irregular working party

The working party met on two occasions during the year to continue its development of refinements to the rules for members who have more than one pensionable employment. Meetings have also been held with relevant institutions to discuss some of the initial proposals and work will continue in 2006 to finalise the details of the recommendations to management committee.

Pension increases

Rule 15 of USS provides that pensions in payment, deferred pensions and deferred lump sums payable from the main section shall be increased in a similar manner to the increases provided for official pensions under the Pensions (Increase) Act 1971 (although increases on the amount of pension which represents the Guaranteed Minimum Pension (GMP) are treated differently – see below). USS pensions were increased by 3.1% on 21 April 2005.

On 21 April 2006 USS pensions which satisfied certain qualifying conditions and began before 26 April 2005 were increased by 2.7% with smaller increases applying for pensions which began after that date. Deferred pensions and deferred lump sums were increased by the same rate.

That part of the pension payable from the main section of USS which represents the pre-1988 GMP is generally not increased by USS as increases are paid by the Department of Work & Pensions Benefits Agency, as are increases in excess of 3% on that part of the pension which represents the post-1988 GMP. More detail on the way in which increases are applied to the GMP is given in the USS booklet *Pension Increases - Information for USS Pensioners* which has been issued to all USS pensioners and also on the USS website in the section 'Other Publications' entitled *Payment of Retirement Benefits*.

Rule 15 also provides that pensions payable from the supplementary section shall be increased to the extent that the trustee company, acting on actuarial advice, decides. As a result, pensions arising from the supplementary section were increased at the same rate as those that applied to the main section.

Contribution rates

The rates of contributions payable by members and institutions between 1 April 2005 and 31 March 2006 were as follows, unchanged from the previous year:

USS Main Section	Member	6% of salary
	Institution	14% of salary
USS Supplementary Section	Member	0.35% of salary
	Institution	Nil

Actuarial matters

The last full actuarial valuation of the scheme was carried out as at 31 March 2005. This revealed that the assets of the scheme at the valuation date were 77% of the accrued liabilities based on projected pensionable salaries with a past service deficit of £6,568 million. The institutions' contribution rate was maintained at 14% of annual salary and the employees' contribution rate was maintained at 6.35% of pensionable salary.

The results of the actuarial valuation were discussed at the meeting for representatives of USS institutions which was held in London on 1 December 2005. The full text of the actuary's report to the institutions' meeting has been published and copies were sent to all institutions in February 2006. It is also available on the USS Ltd website.

No changes were made to the funding objective or the method of valuation, which was a market value approach. The assumptions which have the most significant effect on the result of the valuation are those relating to the rate of return on investments (i.e. the valuation rate of interest) and the rates of increase in salaries and pensions. In relation to the past service liabilities the financial assumptions were derived from market yields prevailing at the valuation date. It was assumed that the valuation rate of interest would be 4.5% per annum, salary increases would be 3.9% per annum (plus an additional allowance for increases in salaries due to age and promotion in line with recent experience) and pensions would increase by 2.9% per annum. In relation to the future service liabilities it was assumed that the valuation rate of interest would be 6.2% per annum, including an additional investment return assumption of 1.7% per annum, salary increases would be 3.9% per annum (also plus an allowance for increases in salaries due to age and promotion) and pensions would increase by 2.9% per annum.

The actuary examined the mortality experience of active members and pensioners and was comfortable with maintaining the existing assumptions for deaths pre and post retirement based on that experience. He also maintained the same allowance for ill-health retirements as was adopted for the 2002 valuation, based on experience since the last valuation.

The result of the actuarial calculations is that the scheme has moved from having a past service surplus of assets over liabilities at 31 March 2002 of £162 million to a deficit of £6,568 million at 31 March 2005. There is a surplus of £56 million attributable to the supplementary section leaving a past service deficit of £6,624 million in the main section.

The actuary also carried out valuations of the scheme at 31 March 2005 on different bases. At that date, the scheme was 126% funded using the MFR prescribed assumptions introduced by the Pensions Act 1995 and 110% funded in terms of the Pension Protection Fund regulations introduced by the Pensions Act 2004. Although not referred to in the valuation report, and not a requirement for USS, the actuary estimated that the funding level at 31 March 2005 using the FRS 17 formula was approximately 90%.

The institution contribution rate required for the future service benefits alone is 14.3% of salaries. The management committee, acting on actuar

Nevertheless, the management committee recognises that there are a number of issues which it, and indeed the sector, needs to address in the coming months which impact on the funding of the scheme. The increase in the promotional salary scale already experienced, the implementation of the new pay spine and the move to a more competitive recruitment market in higher education with the potential for further salary increases arising from the introduction of increased student fees are important factors. Also, improving mortality, the introduction of the Pension Protection Fund levy and new statutory funding regulations all put pressure on the funding of the scheme and increase the likelihood of an increase in the contribution rate at some point in the near future. These are issues which the management committee will be considering and on which it will be consulting with employers during 2006.

The actuary monitors movements in the funding level of the scheme on an ongoing basis and reports on this regularly to the USS committees and officers. The strong investment performance of the scheme has seen the funding level increase during the year and, as at 31 March 2006, the actuary estimated that the assets of the scheme had increased to approximately 89% of the liabilities. He also estimated that, on the FRS 17 basis, the scheme would be over 100% funded at that date.

Further information on the funding of the scheme is given in the trustee's funding statement on page 36.

Accounting matters

The financial statements of the scheme for the year ended 31 March 2006 are set out on pages 61 to 69; and the auditors' statement about contributions and trustee's summary of contributions are set out on pages 71 and 74. The financial statements have been prepared and audited in accordance with Sections 41(1) and (6) of the Pensions Act 1995.

The accounts of Universities Superannuation Scheme Limited (the trustee company) are set out in pages 78 to 89 and show an increase in operating costs from £25.1 million in 2004/2005 to £32.5 million in 2005/2006. This represents a 29% increase in administration costs (to £11.8 million) and a 30% increase in investment management costs (to £20.7 million).

The increase in administration costs is due almost entirely to the payment this year, for the first time, of the Pension Protection Fund levy of £2.6 million. The levy was introduced by the Pensions Act 2004. Excluding this amount, administration costs increased by approximately 1%.

The increase in investment costs is due partly to increases in the base fees of the external managers, which are linked to market values, and to the performance fee for one manager whose performance has significantly exceeded target.

Full details of the operating costs and a review of the activities for the year are given in the Directors' Report & Accounts on page 78.

Investment policy

The arrangements for management of the assets and custody, together with the approximate proportion managed by each manager at 31 March 2006, were as follows:

- (a) 59.3% was managed internally by the trustee company's London Investment Office (with JP Morgan as custodian), of which 52.0% were securities (or alternative investments or cash) and 7.3% were property assets. The internally managed fund has a balanced mandate.

- (b) 4.5% (which until 23 March 2006 had been managed by Goldman Sachs Asset Management International with a UK equity mandate) was held by the London Investment Office (with JP Morgan as custodian) in a transition account;
- (c) 9.5% was managed by Capital International Limited (with State Street as custodian) with a global equity mandate;
- (d) 9.6% was managed by Wellington Management Company (with State Street as custodian) with a global equity mandate;
- (e) 3.8% was managed by Legal & General Investment Management (with State Street as custodian) with a UK corporate bond mandate;
- (f) 12.1% was administered internally on the advice of HSBC James Capel Quantitative Techniques with a mandate to track the FTSE All-Share Index of UK equities (with JP Morgan as custodian);
- (g) 1.1% was managed by Henderson Global Investors Limited with a mandate to provide an enhanced return to that of the FTSE All-Share Index of UK equities (with JP Morgan as custodian).

The year to 31 December 2005 was an excellent year for pension fund performance with positive returns for the average fund for the third consecutive year following three years of negative performance. The fund returned 24% for the year, comfortably ahead of its benchmark return of 22.8%.

Further details of the investment targets, investment performance and amounts managed by each manager are given in the report of the investment committee.

It is a requirement of the Pensions Act 1995 that the trustees of each pension scheme draw up and maintain a statement of investment principles. This statement must lay down the investment objectives of the pension scheme and explain why these objectives are suitable for the particular circumstances of the scheme. The management committee has taken the view that, for USS, this statement should provide significantly greater information about the management of the scheme's investments than is required under the Act. The statement was revised during the year to reflect the revised investment management structure. The final text, which was agreed following consultation with the participating employers, appears on pages 42 to 47.

The paragraphs on corporate social responsibility have been simplified from those which were included in the original statement which was first published in 1997. A more detailed briefing on this issue, which may be amended from time to time, and USS's policy statements on corporate governance, are published on the USS Ltd website, as is the full statement of investment principles.

Corporate governance

The directors of USS Ltd continue to acknowledge their responsibility for ensuring that the company has in place appropriate systems of internal control which are designed to give reasonable assurance that:

- financial information used within the scheme or for publication is reliable and that proper accounting records are maintained;
- assets are safeguarded against unauthorised use or disposition;
- the trustee company and the scheme are being operated efficiently and effectively;
- relevant legislation is complied with;
- appropriate risk management systems are in place.

DISTRIBUTION OF ASSETS

The portfolio distribution as at 31 March 2006, along with the comparative figures for the preceding year, is set out below:

	2006			2005		
	£m	£m	%	£m	£m	%
UK fixed interest						
British Government						
Conventional	144.7			222.4		
Index-linked	—			—		
Other debentures & loan stocks	982.7			924.8		
		1,127.4	4.0		1,147.2	5.3
Overseas fixed interest						
North America	226.3			316.2		
Europe	354.9			99.9		
Japan	218.4			143.7		
Far East	—			—		
Other	—			—		
		799.6	2.8		559.8	2.6
Total fixed interest		1,927.0	6.8		1,707.0	7.9
UK equities						
Resources	1,596.1			1,430.0		
Basic industries	791.1			259.4		
General industrials	871.5			285.6		
Consumer goods	856.8			1,402.7		
Services	2,747.3			2,211.7		
Utilities	366.9			291.2		
Information technology	120.8			149.7		
Financials	2,846.7			2,195.9		
Collective investment schemes	5.7			3.2		
Managed funds	326.8			252.8		
Derivatives	—			—		
		10,529.7	37.2		8,482.2	39.1
Overseas equities						
America	3,431.6			2,587.6		
Japan	2,890.2			1,761.2		
Europe	4,065.2			2,853.1		
Far East	2,439.5			1,761.9		
Other	490.0			345.0		
		13,316.5	47.2		9,308.8	42.9
Total equities		23,846.2	84.4		17,791.0	82.0
Total securities		25,773.2	91.2		19,498.0	89.9
Property (incl. indirect property)		2,056.4	7.3		1,799.6	8.3
Cash deposits		300.1	1.1		280.6	1.3
Other Investment balances		116.3	0.4		105.1	0.5
Total investments		28,246.0	100.0		21,683.3	100.0

LARGEST EQUITY HOLDINGS

A list of the fund's largest twenty equity holdings together with the percentage of the fund which they represent, is shown below:

FINANCE & GENERAL PURPOSES COMMITTEE

The finance & general purposes committee was established under the authority of the management committee in January 1984.

Its purpose is to consider and report to the management committee on any matters relating to the structure and management of USS Ltd as the corporate trustee of USS, other than those which have been allocated to the investment, audit, remuneration and rules committees.

In essence, inter alia, it:

- Undertakes detailed work on behalf of the management committee and makes recommendations to it on major policy issues.
- Gives preliminary consideration to major issues, which it is intended should be brought to the management committee.
- Oversees the detail of revisions to the USS Ltd risk management profile and policy and submits annual reports to the management committee.
- Gives detailed consideration to financial estimates and performance against estimates.
- Approves capital expenditure with limits agreed by the management committee.
- Monitors communication with, and levels and quality of service provided to, member institutions and individual members.

The committee members are appointed by the management committee and currently comprise seven members. Of the committee's seven members, three are UUK appointees to the management committee, two are AUT (now UCU) appointees and two are co-opted appointees. Mr A S Bell retired on 31 July 2005 and Mr J W D Trythall on 31 August 2005. We thank Mr Bell and Mr Trythall for their significant contribution as committee members. Mr D Guppy was appointed to the committee with effect from 1 September 2005.

During the year, the committee met on five occasions and considered matters such as the actuarial valuation of USS, cross-border pension activities, preservation, expansion of USS, insolvency and withdrawal of institutions from USS, the admission of new institutions to USS, corporate performance of USS Ltd, USS Ltd's business plan and the government's pensions reform.

Signed on behalf of the finance & general purposes committee.

Professor John Bull
Chairman

AUDIT COMMITTEE

The audit committee was established under the authority of the management committee in March 1982.

Its purpose is to consider and report on any matters relating to internal control systems, financial reporting arrangements and corporate governance.

In essence, it examines management's processes for ensuring the appropriateness and effectiveness of systems and controls and arrangements to ensure compliance with standards and arrangements under appropriate regulatory systems.

In addition it:

- Reviews the scope, planned programmes of work and findings of both the internal and external auditors and the compliance officer.
- Ensures that the accounting and reporting policies are in line with legal requirements, Financial Services Authority and other appropriate regulatory body requirements and best practice.

The committee members are appointed by the management committee and currently comprise five members; one is a UUK appointee to the management committee, two are AUT (now UCU) appointees and one is a co-opted appointee. The committee is chaired by Dr Christine Challis, an independent appointment made by the management committee. More than one member of the committee possesses what the Smith Report describes as recent and relevant experience. During the year, the committee met on four occasions. It has also met with the external auditor and the internal auditor privately each on one occasion without any officers being present. During the year, the committee has, inter alia:

- reviewed the accounts of both the trustee company and the scheme prior to approval by the management committee;
- reviewed the the external auditor's strategy for the audit of the accounts of the trustee company and the scheme;
- reviewed the internal audit function's terms of reference, its work programme and quarterly reports on its work during the year;
- received regular reports from the compliance officer;
- overseen an appraisal of the performance of the management committee and the chairman;
- expressed its continued satisfaction with USS Ltd's approach to identifying and dealing with risks to its business.

Signed on behalf of the audit committee.

Dr C Challis
Chairman

The committee has also considered the scheme's status under the Pension Protection Fund, and has expressed views to the management committee on the proposal to position the scheme as last man standing for those purposes. Administrative problem areas have been brought forward to the committee for consideration, and amendments have been made to the scheme's policy in relation to (i) members joining the scheme at or after age 60, and (ii) members retiring before age 60 and the application of reductions to transferred-in benefits (known as the seven-year rule).

The working party of the JNC dealing with employees who hold regular and variable-time employments met on two occasions during the year, and has continued to develop solutions to deal effectively with members who have more than one employment (and in particular where one of those employments is variable time). The working party's activities continue into 2006.

Signed on behalf of the joint negotiating committee.

Sir Kenneth Berrill
Chairman

ADVISORY COMMITTEE

The functions of the advisory committee are to advise the trustee company on the exercise of its powers and discretions (other than those relating to investment matters), on difficulties in the implementation or application of the rules and on any complaints received from members or participating institutions, and any other matters on which the trustee company requires advice.

Four meetings were held during the year. Dr Roger fulfilled the role of chairperson throughout the year.

The majority of questions raised on the application or interpretation of the rules of USS were dealt with by the senior officers. There were three cases which required detailed consideration by the advisory committee during the year. These cases were all related to members requesting full commutation of their benefits on the grounds of serious ill-health. In each case the full commutation was granted.

It was necessary for the committee, enlarged by two members of the management committee, to meet on four occasions during the year to consider the decision given by the pensions operations manager at stage one of the internal dispute resolution procedure. The second stage considerations were as follows:

- A member complaining about delays affecting his transfer value into the scheme - the committee recommended an award of £500 as a gesture of goodwill.
- A member complaining that they had been missold their AVC contract by the Prudential - the committee decided not to uphold the member's complaint.
- A member complaining about the distribution of the death benefits when his ex-partner died - the committee decided not to uphold the member's complaint.
- A member complaining that his benefits had been overstated and that he had suffered to his detriment as a result of this statement - the committee acknowledged that maladministration had occurred and upheld the member's complaint recommending that an award of £4,000 be paid to the member as compensation.

Signed on behalf of the advisory committee.

Dr A Roger
Chairperson

RULES COMMITTEE

In conjunction with the officers and the scheme's professional advisers, the rules committee devises and maintains procedures for all aspects of the rule amendment process, having particular regard to the desirability of simplifying those rules which are most complex, whether in terms of intelligibility or of administration.

During its third year the committee has overseen the Second to the Sixth Supplemental Amending Deeds, further details of which are included in the report from the joint negotiating committee. The committee has also been involved in the following activities:

- Overseeing the implementation of the pensions reform project within the trustee company, so that the rule amendments necessary as a result of the introduction of the Finance Act 2004 and the Pensions Act 2004 were executed effectively, and ensuring that the necessary changes to internal systems, administrative procedures and communication material were undertaken.
- Assisting with the development of the trustee company's response to the cross-border regulations.
- Agreeing the format of the rule amendments and procedural changes necessary to update the USS rules so as to be compatible with the implementation of the Framework Agreement in the higher education sector.
- Continuing the ongoing work to review administrative problem areas and propose alternative solutions.
- Providing technical information to the management committee, and finalising the rule amendments necessary, to secure USS as a 'last man standing' scheme for the purposes of the Pension Protection Fund.

The committee met on six occasions during the year.

Signed on behalf of the rules committee.

H R Jacobs
Chairman

NOMINATIONS COMMITTEE

The nominations committee was established under the authority of the management committee to deal with all matters relating to the appointment of co-opted directors and to make appropriate recommendations to the management committee.

The committee's members are appointed by the management committee and comprise the chairman of the trustee company, a UUK appointed director, an AUT (now UCU) appointed director and a co-opted director who acts as chairman. The committee supplements that membership to include, if necessary, expertise appropriate to the particular appointment.

The committee met on two occasions during the year to select and recommend to the management committee a successor to Mr Bell who retired on 31 July 2005.

Signed on behalf of the nominations committee.

Professor John Bull
Chairman

UNIVERSITIES SUPERANNUATION SCHEME
MEMBERSHIP STATISTICS

The number of members in the scheme and the number receiving pension and annuity benefits at the end of the year are as follows:

SUMMARY OF MOVEMENTS during the year ended 31 March 2006

Members	University Institutions	Non-University Institutions	Totals
Total members at 1 April 2005	106,564	3,402	109,966
New members	17,945	719	18,664
Retirements			
- Ill-health	101	4	105
- Other	1,744	32	1,776
Deaths	81	2	83
Leavers and withdrawals			
- Refunds	1,689	65	1,754
- Deferred/undecided	8,408	276	8,684
- Retrospective*	589	10	599
Total members at 31 March 2006	111,897	3,732	115,629

*Retrospective withdrawals are members who withdrew from USS within three months of the date of joining the scheme with retrospective effect to the date of commencing employment at a USS institution.

In addition USS Ltd was notified during the year of 3,916 employees who became eligible to join the scheme but elected not to do so.

Pensioner Members	University Institutions	Non-University Institutions	Totals
Total pensioners at 1 April 2005	33,715	779	34,494
Mergers			
New pensioners	2,754	80	2,834
Deaths	760	26	786
Total pensioners at 31 March 2006	35,709	833	36,542

In addition at 31 March 2006, there were 7,259 pensions being paid to spouses and dependants and 873 annuities being paid to dependent children. Deferred pensioners not yet receiving a pension totalled 66,065.

Ex-spouse participants

At 31 March 2006, 226 ex-spouse participants have benefits within the scheme in their own right as a result of pension sharing, of whom 16 are now in receipt of their pension and are included in the pensioner member summary above.

UNIVERSITIES SUPERANNUATION SCHEME
USS ACCOUNTS

FUND ACCOUNT for the year ended 31 March 2006

	Note	2006 £m	2005 £m
Contributions and Benefits			
Contributions receivable	3	842.1	783.7
Premature retirement scheme receipts		25.9	32.2
Transfers in	4	145.8	230.1
		1,013.8	1,046.0
Benefits payable	5	789.8	742.1
Payments on account of leavers	6	38.0	57.9
Administration costs	7	11.8	9.1
		839.6	809.1
Net additions from dealings with members		174.2	236.9
Returns on investments			
Investment income	8	686.9	587.6
Change in market value of investments	9	5,722.2	1,485.0
Investment management expenses	10	(20.7)	(15.9)
Net returns on investments		6,388.4	2,056.7
Net increase in the fund during the year		6,562.6	2,293.6
Fund at start of year		21,739.7	19,446.1
Fund at end of year		28,302.3	21,739.7

The notes on pages 63 to 69 form part of these financial statements.

