

Changes to the Universities Superannuation Scheme (USS)

This briefing provides some background in relation to the changes that have now been agreed for the Universities Superannuation Scheme.

What are the changes and when will they start?

The USS Trustee Board approved the changes to USS benefits at its meeting on 9 June following a final decision by the Joint Negotiating Committee (JNC) on 10 May. This formal process completes an extended period of discussion and negotiation between the employers and the University and College Union (UCU) which dates back to 2006, when USS first identified the need for changes to the scheme.

The USS has confirmed that the agreed changes will take effect from 1 October 2011.

Current USS members will continue to build up benefits based on 1/80th of their final salary for each year of pensionable service, plus, a 3/80th tax free cash lump sum. However, from 1 October there will be some changes which will apply *for future service only*. This will also be the case for people who have been a USS member and who re-join by returning to work at a USS employer in under 30 months. These changes include:

- an increase in the employee contribution rate to 7.5%,
- a normal pension age of 65 (for those under 55 at 1 October only) rising in line with the State Pension age, and
- a cap to pension increases for service after the 1 October implementation.

New entrants to USS from 1 October onwards who are not re-joiners (entitled to rejoin the final salary section) will enter a new section of the scheme and build up benefits in a slightly different way. For these members each year they will accrue a portion of pension based on 1/80th of the salary they earn *in that year* plus, a 3/80th tax free cash lump sum. In each subsequent year, this portion of their pension will be increased in line with official pensions – payable to those in public service pension schemes such as TPS - until they reach retirement. At retirement the amount of pension paid will be the sum total of all of these pension elements. The corresponding tax free cash lump sum will build up in the same way. This is commonly known as a CARE (Career Average Revalued Earnings) scheme. The employee contribution rate for the new CARE section will be 6.5% of salary and the normal pension age will also be 65, rising in line with the State Pension age.

The retention of a final salary pension scheme for all existing USS members and many re-joiners is an exceptional benefit. The new CARE scheme, for future employees, is an attractive scheme providing a good level of income in retirement. There are also many additional benefits provided through the USS including life cover, spouse and child pensions and incapacity cover which all remain unchanged.

None of the agreed changes will affect pensions that have been deferred, or, are in payment before 1 October 2011.

Why was there a need for these changes and is this still the case?

The case for change to the USS was based on the need to ensure a sustainable, attractive and affordable scheme for all employers and members, current and future. Pressures on USS have arisen from increasing life expectancy as well as other factors, including the uncertainty and volatility now seen in investment returns. This still remains the case. The actuarial report in 2010 indicated that there was a substantial deficit in the scheme at that point. If, as expected, the situation is the same in the 2011 valuation, the USS will be required by the Pensions Regulator to agree a recovery plan that would seek to fund this deficit over a number of years. The 2010 results suggested that at least an additional 2% contribution for the next 30 years would be required. The 2011 valuation is currently under way and it is prudent to be prepared to provide for a level of additional funding. The employers are already contributing at 16% as a 2% employer contribution rise was required following the valuation in 2009, costing employers an estimated £110m per annum.

It is worth noting that the “buffer” described by UCU will only be created in relation to new employees who join the CARE section after 1 October. It is not known yet how many such new members there will be. The bulk of the costs of USS will remain attributable to the final salary section members and there is not expected to be a “buffer” built up in relation to these employees. The current estimate of the future service cost for the CARE section members is also based on the 2008 valuation assumptions. These are expected to change, in particular the assumptions made on life expectancy, bringing an expectation of an increasing cost for future service.

Why does the UCU’s current industrial action ballot carry concerns?

Any ballot for industrial action that targets students is a serious concern, and minimising potential damage to students remains of paramount importance.

The changes to USS are the result of nearly three years of negotiations between the employers and UCU, culminating in approval at the USS JNC (via the casting vote of the independent chair Sir Andrew Cubie who was nominated by UCU) and the USS Trustee Board (UCU has full representation on both bodies), and was subject to an extensive member consultation. Students, taxpayers and others looking in on higher education may not regard further industrial action as a justified response to such moderate and now agreed and irreversible changes. The sector’s scarce financial resources and future fee income cannot be used to fund an unreformed pension scheme; USS needs to remain sustainable, attractive and affordable for all: employers and members, current and future.

What exactly were the agreed changes and how do these compare to other pensions schemes reforms?

For full details on the changes please go to the **USS website homepage** <http://www.uss.co.uk> and see “Changes to USS”. Then go to ‘More information’ <http://www.uss.co.uk/news/Documents/Important%20Info%20for%20USS%20members.pdf> and ‘Background to scheme changes’ <http://www.uss.co.uk/HowUssIsRun/Schemereview/Pages/default.aspx>

The changes to USS are extremely moderate compared to those made to many schemes over the past decade. Many employers have closed their defined benefit schemes to future accrual or closed them entirely and moved employees to different, more affordable types of pension scheme, such as defined contribution, where all the risks fall to the employee with no guarantee of the income they will receive in retirement. For existing members retaining a final salary pension is an exceptionally good benefit and USS is likely to be one of the last schemes in the UK doing this. Unlike other schemes, USS recognises the mobility of staff within the sector, so it will even be possible for existing members to

leave for up to two and a half years and rejoin, still retaining this exceptional benefit. HE employers remain committed to providing defined benefit pensions and will retain the majority of the cost and the associated risks involved in doing so. However, this commitment could not be made if the steps now agreed were not in place to manage the risks and the increasing costs going forward. The new section of the scheme presents a very attractive defined benefit pension for future employees. It mirrors the 1/80th pension plus 3/80th lump sum that is available to the final salary section members and now has an improved revaluation rate for the accrual of benefits.

Increases in longevity alone are requiring changes in pension schemes everywhere; and academics are amongst the longest living of working groups. Lord Hutton's review of public sector pensions recommends that CARE schemes replace final salary provision for all, as a means to provide fair and affordable pensions.

Is UCU's claim true that the employers want to introduce more changes?

No, the employers have given their full support to the package of changes as now agreed. These changes are designed to ensure that the scheme will be both sustainable and affordable over the long term. Establishing the new section on a CARE basis enables the employers to contain both the cost and the risks associated with the scheme into the future as new members join. The cost and risks need to be managed over the very long term, usually 40 years or more. By using the CARE basis, rather than final salary, for new entrants, the risk associated with salary increases is reduced gradually over time. In the last valuation the underestimation of salary increases required an additional fund of £1.35 million to be set aside, purely to meet this risk. Increasing the normal pension age for future service also reduces some of the risk associated with increases in longevity, which is one of the most costly risks associated with pension schemes. In the last valuation improvements in life expectancy added 2.4% to the future service contribution rate. This trend is expected to continue. Making these moderate changes to mitigate these future risks, it is believed that the USS will be able to remain open, affordable and sustainable in the long term.

What will happen now?

The USS Trustee Board agreed the execution of a Deed of Amendment at their meeting of 9 June and the changes to USS will take effect from 1 October 2011.

USS will be providing information for existing members with their annual service statements in June setting out the changes that have been agreed and what this will mean for members from 1 October 2011.