USS 2018 valuation

November 2019

Headline

At the time of writing on 5 November 2019, the University and College Union (UCU) has announced 8 days of strike action at 60 universities from Monday 25 November. 46 universities will be affected by strike action over the Universities Superannuation Scheme (USS) pensions dispute, and 14 other universities will be affected by strike action over pay and conditions.

This briefing provides background and context on the USS dispute and sets out the efforts made by the affected universities to resolve the dispute satisfactorily.

Summary

The University and College Union (UCU) has been in dispute with 69 universities in the pre-92 higher education sector over the latest valuation of the Universities Superannuation Scheme (USS) – the largest private sector pension scheme in the UK. Over 50,000 members of staff were balloted for strike action between by UCU in opposition to the outcome of the 2018 valuation, which determined that an increase in contributions is required by the scheme to ensure benefits can be maintained at their current level.

The ballot was disaggregated, meaning that individual branches were required to meet the 50% turnout threshold in order for strike action to be held at their institution. The ballot opened on 9 September and closed on 30 October 2019. The earliest date that strike action could take place is 15 November 2019, but any mandate that arises from the ballot will remain live for six months.

Universities UK (UUK) is the nominated formal representative for 340 employers participating in USS since the scheme was formed in 1975. UUK is responsible for determining a collective employer position to inform negotiations with UCU, who formally represent the scheme members. UUK is also responsible for communicating the views of employers to USS on a range of matters related to the management of the scheme.

UUK supports the outcome of the 2018 valuation. Following consultation, a majority of employers agreed to increase contributions to the level required by the USS Trustee (a total of 30.7% of salary) in order to keep benefits at their current level in the face of a challenging economic environment. This support was conditional on the increase being a short-term holding position, while a longer-term solution to the rising costs of the scheme is found.

UCU does not support the valuation outcome, as they do not believe that an increase in contributions is justified. Their formal ‘no detriment’ policy states that reforms to USS’s governance and valuation methodology will result in a more optimistic outlook for the scheme. As a result, they are unwilling to consider any contributions increases or changes to the benefit structure

However, in advance of the next valuation of the scheme (currently scheduled to begin in March 2020) an independent panel of experts chosen jointly by UCU and UUK will publish recommendations on how USS’ valuation processes and governance could be reformed to secure the sustainability of the scheme. The report is expected to be published before the end of 2019.

This briefing provides background and context on the dispute and sets out the efforts made by the affected universities to resolve the dispute satisfactorily. It also clarifies why UUK cannot support UCU’s positions.

The 2017 valuation and industrial action

The 2017 valuation of USS revealed that the cost of providing future pensions had grown to unsustainable levels, and the scheme’s projected liabilities outweighed its projected assets, leading to a deficit. The total contribution rate at the time was 26% of salary, with employers paying 18% and members 8%. USS eventually calculated that total contributions needed to rise to 35.6% to maintain the scheme and tackle the deficit.

As a result, UUK, representing the scheme employers, put forward a proposal to change USS from its present defined benefit/defined contribution hybrid (see Annexe for definitions), to a wholly defined contribution scheme, and keep the contribution rate at 26% of salary.

This proposal was met with opposition by UCU and led to unprecedented strike action in the pre-92 higher education sector. Beginning in February 2018, fourteen days of strike action eventually led to the withdrawal of the proposal, and subsequent talks between UCU and UUK mediated by Acas in March.

A Joint Expert Panel (JEP) was then convened by UUK and UCU, to examine the 2017 valuation, and make recommendations for adjustments that could bring costs down. As part of the agreement to establish the panel, UCU suspended the strike action.

The USS Trustee then concluded the 2017 valuation by implementing the 35.6% of salaries contribution rate from April 2020, with phased increases in April 2019, October 2019 and April 2020. The benefit structure of the scheme remained the same.

USS also agreed to carry out a 2018 valuation (two years earlier than the statutory requirement) to consider the recommendations made by the JEP, and incorporate latest market data, which had improved as of March 2018.

The 2018 valuation

The 2018 valuation resulted in a 30.7% contribution solution to supersede the much higher rates under the previous valuation. This solution is close to what the JEP recommended, and retains the current level of benefits at a lower price for both members and employers than the 2017 valuation backstop.

Employers supported this solution in May 2019 and proposed to pay the bigger share of the contributions increases. In August, the scheme's Joint Negotiating Committee, made up of UUK and UCU representatives, decided that the extra contributions should be split 65:35 between employers and scheme members, resulting in employers paying 21.1% of salary, and members 9.6%. This decision was made in line with the default in the scheme's rules, which state that contributions increases should be split 65:35 when UUK and UCU cannot agree a way forward.

The Pensions Regulator, an important stakeholder made it clear that it is concerned that the rate of 30.7% may be too low, and it is therefore at the limit of what they are prepared to accept. This solution is therefore the most viable route to maintaining member benefits while keeping the contribution increases to a minimum that is acceptable for USS and The Pensions Regulator.

Re-ignition of the dispute

In May 2018 during the course of the 2018 valuation process, Dr Jo Grady was elected as UCU's General Secretary following the departure of the previous incumbent Sally Hunt. Dr Grady pledged her commitment to UCU's 'no detriment' position, which was subsequently adopted as formal policy by the union's Higher Education Committee. Although some senior UCU staff saw the 30.7% contribution rate (which emerged from the 2018 valuation) as a good outcome, by 19 June 2019 UCU's leadership had formally commenced a trade dispute with 69 universities in the pre-92 sector, as the planned increase in contributions contravened the now formal 'no detriment' policy.

Why employers cannot support UCU's positions

In setting out the terms of their dispute, UCU stated their view that the current level of benefits can be maintained with an overall contribution rate of 26% or less. However, The Pensions Regulator has publicly made clear that it regards a 30.7% rate as at the limit of what is acceptable and does not account for the market experience post-March 2018 which has been poor. In short, a rate of 26% would involve taking far more risk than the USS Trustee or the Regulator is prepared to accept.

In response, UCU maintained that employers should pay the full cost of the increase to 30.7% and keep the member contribution at 8% of salary. Such an ask would have a serious impact on the financial health of many employers. A 22.7% salary employer contribution would equate to an extra £373 million per year – £123 million more than employers have already committed to additionally pay. Contributions at this level would be equivalent to the funding required for nearly 8,500 full-time average roles across the higher education sector. Most employers in the scheme would not be able to absorb increases at this level without material changes to their operating model, including reducing staffing costs. Additionally, the scheme's rules set out that contributions increases should be shared 65:35 between employers and members by default if the scheme's stakeholders cannot agree a way forward.

Since the dispute began in 2017 UCU have consistently demanded that defined benefits must be maintained at their current level. The solution to the 2018 valuation meets this demand – it proposes no changes to benefits but requires a rise in contributions to fund them: the employers have agreed to pay the majority of this increase.

Efforts employers have made to resolve the dispute

Since the strike action in 2018, the scheme employers have gone to great lengths to resolve the ongoing dispute. UUK proposed setting up the Joint Expert Panel to examine the valuation, and following consultation, supported the recommendations the panel made.

An extensive period of engagement with the USS Trustee followed, resulting in the 2018 valuation and a reduction in the overall rate from 35.6% of salary in 2017, to 30.7% in 2018.

UUK also spent considerable time and resource developing a credible 'contingent contributions' proposal to bring the required rate down even further – to 29.7% – although the USS Trustee ultimately did not accept this proposal.

Following consultation by UUK, the scheme employers also agreed to additional measures to ensure that the scheme's 'covenant' – or collective financial strength – continues to be regarded as strong in the Trustee and Regulator's view, to make the 30.7% rate acceptable. This involved agreeing to ongoing debt monitoring, prioritisation of USS as a creditor, and a moratorium on employers exiting the scheme.

These efforts were made in response to the firm view expressed by UCU that the scheme's benefit structure should be preserved, and in view of their demand for lower contributions, despite the prevailing economic conditions.

In recognition of the concerns raised by UCU over member contributions at 9.6% of salary, UUK offered to pay an additional 0.5% at the 2018 valuation – reducing the member contribution to 9.1% of salary – on the condition that UCU withdraw their current ballot for industrial action. The offer, if accepted, would have been subject to consultation with the scheme employers, but UCU's Higher Education Committee chose to reject the offer, without consulting the wider union membership.

UUK has created a new website – www.ussemployers.org.uk, and Twitter feed @USSEmployers, to increase transparency in the valuation process and to ensure both employers and scheme members are informed with the latest developments.

The JEP will report again in late 2019 with recommendations to reform scheme governance and future valuations. It will suggest options for the 2020 valuation and consider whether there are alternative medium-term options to reform USS to ensure benefits remain attractive and affordable for the long-term.

UUK looks forward to receiving the report and working with UCU to take it forward.

ANNEXE

Timeline of key developments

2017

- The 2017 USS valuation shows that the scheme's deficit and cost of future pensions has grown to unsustainable levels, requiring much higher contributions.
- Employers put forward a proposal to change USS from a defined benefit/defined contribution hybrid, to a wholly defined contribution scheme.

2018

- February–March: Unprecedented strike action in the pre-92 higher education sector, orchestrated by the University and College Union (UCU). Proposal withdrawn.
- May: A Joint Expert Panel (JEP) is convened by Universities UK (UUK), representing employers, and UCU, on behalf of members.
- September: The JEP examines the 2017 valuation and makes recommendations for adjustments that could bring costs down.

2019

- January: The USS Trustee concludes the 2017 valuation by implementing a 35.6% of salaries contribution rate from April 2020, with interim increases in April 2019 and October 2019. The benefit structure of the scheme remains the same.
- USS agrees to carry out a 2018 valuation to consider the recommendations made by the JEP.
- May: USS proposes a 30.7% contribution solution to the 2018 valuation, to supersede the timetabled backstop increases under the previous valuation. UUK's actuaries Aon certify that this solution is largely in line with the JEP's first report, and retains current levels of benefits at a lower price for both members and employers than the backstop.
- June: Employers support the solution as the most viable route to maintaining member benefits while keeping the contribution increases to the minimum that is acceptable for USS and The Pensions Regulator.
- September: UCU begin industrial action ballot in opposition to the required increase in member contribution from 8.8% to 9.6% of salary.
- October: Ballots for industrial action over pay and conditions and pensions closes.
- November: UCU announces 8 days of strike action over pay and conditions and the USS dispute.

Background on the scheme

USS is a pension scheme for academic and academic-related staff (including senior administrative staff) employed by 340 UK universities and registered charities (the 'employers'), which consist mainly of institutions that were universities prior to 1992 (staff in the post-92 universities are mostly members of the separate Teachers Pension Scheme). USS is the largest workplace pension scheme in the UK by assets under management (£67.4bn as at 31 March 2019) and is also the largest by the number of members (439,572 as at 31 March 2019, including 202,165 employed active members).

USS is a career average hybrid scheme, in which members accrue 'defined benefits' on salaries up to £58,589 pa (as at 31 March 2019 – this threshold increases annually, broadly in line with the Consumer Price Index of inflation), above which any additional pension is provided in the form of a 'defined contribution' (DC) pension. Defined benefits are guaranteed and are calculated based on a set formula, while the amount received from defined contributions depend on how much has been contributed, and how well the pension scheme's investment fund has performed.

The legal duty of the trustee board overseeing USS is to secure adequate funding to guarantee the affordability of paying pensions and other financial benefits that have been promised to the employees participating as its members. To achieve this the USS trustee board is obliged under law to satisfy The Pensions Regulator's demand to apply a measure of prudence when encountering issues relating to ensuring that the USS is adequately funded.

Under pensions legislation the USS trustee board is obliged to carry out an actuarial valuation every three years (maximum) to assess the pension scheme's overall financial health and sustainability. During a valuation, the USS trustee assesses the scheme's assets and liabilities to ensure that it holds sufficient funds (allowing for investment return) to pay the benefits promised to members upon retirement or death, and that contributions into the scheme cover the cost of benefits that might be promised in future.

Wider economic context

The cost of providing defined benefit pensions has increased by 25% since 2012, due to a challenging economic environment. Gilt yields have fallen to historically low levels, while interest rates have also remained low. Many defined benefit schemes have closed as a result, with only 1 out of 10 extant defined benefit schemes still open to new members as of 2018.

The higher education sector is also facing considerable financial uncertainty. Income from tuition fees has declined in real terms since 2012, while the government's Augar Review of post-18 education and funding recently recommended a cut in tuition fees. Brexit will also have significant financial implications for universities.

Despite this context, universities have continued to invest in staff. 54% of all expenditure across the higher education sector is staff-related, while numbers of staff have grown by 6.4% since 2014–15.

The proposed employer contribution arising from the 2018 valuation – 21.1% – is higher than the national average for private sector defined benefit schemes (19.2%), and the 3.1 percentage point increase in the employers' contribution (from 18% to 21.1%) is equivalent to an extra £250 million per year in employee contributions.

USS benefits remain as some of the very best in the UK, with annual pension payments nearly three times the national average (£19,000 pa as opposed to £7,000 pa). Under the proposed conclusion to the 2018 valuation, these benefits will be maintained.

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