UNIVERSITIES UK PROPOSAL TO THE JOINT NEGOTIATING COMMITTEE FOR FUTURE BENEFIT REFORM – 13 NOVEMBER 2017

(AS SUBMITTED TO THE JNC ON 13 NOVEMBER – RESUBMITTED TO JNC ON 18 DECEMBER)

1. SUMMARY BENEFIT REFORM PROPOSAL

1.1 Universities UK (UUK) proposes an approach to future benefits at this valuation that applies the full flexibility of the current hybrid scheme: modifying the salary threshold so that there is no further defined pension benefit accrual and offering market-leading defined contribution (DC) saving (through the USS Investment Builder) to all employees.

1.2 The University and College Union (UCU) have made clear that defined benefit (DB) provision is greatly valued and employers appreciate that the current hybrid scheme is still in its infancy. For this reason, the proposal is to maintain the existing hybrid structure, albeit without further accrual in the USS Retirement Income Builder at this valuation.

2. WHY A SUSTAINABLE SOLUTION IS NECESSARY

2.1 The USS trustee has a fiduciary duty to secure accrued member benefits. It therefore needs to carefully assess the cost of benefits in order that it has (or can obtain) sufficient funds to meet all pension promises when they fall due. The trustee has engaged extensively with all stakeholders on both the method and assumptions by which the cost of benefits at the 2017 valuation is determined, and has sought professional advice on risk capacity. UUK understands that the trustee has used all the information provided to reach a professional judgement on its technical provisions.

2.2 The trustee's analysis concludes that:

- The cost of providing current future service benefits has risen by over a third since the last valuation.
- A substantial past service deficit of £7.5 billion remains.
- Reliance on the sponsoring employers has grown significantly since the last valuation, it was £23 billon at the valuation date (compared to £14 billion at the 2014 valuation).

2.3 USS is designed to meet the retirement needs of the higher education sector, and must be configured in line with the requirements of both employers and employees. Most USS employers are registered charities, many of which carry out the critical public functions of teaching, research and knowledge exchange. Failure to address the rise in cost and risk of USS would not be justifiable to students, current and future employees or the other funders of the higher education sector.

2.4 USS employers remain committed to paying 18% of salaries in total towards pensions. Institutions' ability to prioritise financial commitments is essential so they can remain successful and manage risks. If pension costs are prioritised over other financial commitments it risks weakening the covenant supporting the scheme by impacting on institutions' ability to fulfil their core mission.

2.5 It is essential to resolve the funding issues facing USS so that member benefits accrued to date are protected, so that the higher education sector's funding position remains sustainable and so that employees can continue to benefit from generous employer contributions towards their retirement savings in the long term. Employers are concerned that if USS risk is left unaddressed, a possible further deterioration of the scheme's funding position would preclude them from offering market leading DC retirement benefits in the future. This would likely be the case, for example, if more money was required to address a past service deficit or if the USS trustee was forced to move to a low risk investment portfolio. These risks are real, and if they are not appropriately addressed they will lead to greater intergenerational unfairness. Employers want the value from the contributions paid towards pensions to be maximised for all employees, and the proposed approach achieves that.

3. BENEFIT REFORM

3.1 The space within which a sustainable solution can be found at this valuation is very narrow. Employers must balance costs and maximise the value of the contributions paid towards pensions in an extremely challenging economic environment. It would be irresponsible for employers to put forward an approach that is not sustainable. There is a widely held view that future investment returns are expected to be lower, and economic forecasts remain challenging in the context of greater uncertainty.

3.2 A majority of employers agree that using the full flexibility of the current hybrid scheme is the best outcome at this valuation for three key reasons:

- First, modifying the salary threshold at this valuation is the most effective method of managing risk, and is therefore the most certain way of enabling accrued benefit security and long-term sustainability.
- Second, because the trustee has indicated that deficit recovery contributions will be higher if a level of DB is maintained, modifying the salary threshold so that there is no further defined pension benefit accrual at this valuation maximises the share of the 18% employer contribution that goes towards members' future benefits.
- Finally, DC offers great flexibility to members, which could help address affordability concerns raised by parts of the membership. Maintaining even a small amount of DB will likely prevent members from benefiting fully from flexibility in the employee contribution rate and the benefits that DC offers.

3.3 UUK could advocate a position that involves moving USS to a full DC scheme. However, employers do understand the value of the current hybrid scheme and as such UUK proposes to maintain the current structure.

4. PROPOSALS TO SUPPORT MEMBERS IN THIS APPROACH

4.1 The proposal is that all future benefits would be provided in the USS Investment Builder section of the scheme at this valuation. In doing so, much of the excellent work to develop the new hybrid scheme can be built upon and extended. UUK envisages an evolution of USS into a scheme that offers greater flexibility and choice to meet the increasingly diverse needs of employers and employees. UUK wants to ensure that members are supported and protected throughout this change, and therefore proposes the following measures:

- First, employers propose maintaining the provision of death and incapacity benefits on a defined basis so that employers continue to carry the risk in the most difficult of circumstances. Employers recognise the peace of mind that these benefits offer and want to continue to offer these valuable benefits in the future.
- Second, employers want members to have a cost-effective means of saving for their retirement, and as such propose continued commitment to the employer subsidy of administration and investment management charges.
- Third, employers are keen to work closely with members and their representatives on designing the benefits that can be afforded at this valuation. This means thinking carefully about flexibility and choice for members, as well as the availability of financial guidance and support.
- Fourth, employers are clear that benefit reform is needed to ensure that current *and* future employees can benefit from high employer contributions towards retirement saving. UUK's proposal maintains the same scheme for all eligible employees, rather than introducing different arrangements for new entrants.
- Finally, employers are clear that this change is not driven by a desire to cut costs, with employers committing fully to maintaining their contribution to USS at 18% at this valuation.

4.2 UUK seeks to work with UCU to ensure that this proposal can be further developed and to ensure a positive outcome from negotiations.

UNIVERSITIES UK
13 NOVEMBER 2017