

On 23 January 2018, at the meeting of the Universities UK-UCU Joint Negotiating Committee, the Chair of the USS Board Sir Andrew Cubie used his casting vote to push Defined Contribution onto all members of USS. We are all being forced to gamble our pensions on the stock market. Our pension contributions have been cut by 6% of salary.

The “deficit”

The £7.5 billion “deficit” is a projection using a methodology that is criticised by mathematicians, actuaries and pensions experts. Called “Test 1”, this was introduced in the 2014 valuation.

- The scheme’s assets have increased at an average of 12% per year over the last 5 years and now value more than £5bn – the scheme is booming
- Projected income and expenditure for 40 years show that payments to pensioners are covered by contributions paid in without touching the assets. See Figure 1.

USS is in a better financial position than in 2014. Why is the scheme in “crisis”?

Test 1 supposes that all universities go bankrupt tomorrow, and USS is closed to new entrants. The deficit model asks, if this happened, could USS afford to pay its pensioners?

The test generates a deficit because it presumes that (due to scheme closure) USS rapidly transfers its assets into government bonds and gilts. Thanks to Quantitative Easing and low Bank of England base rates, government stocks are performing at a level well below inflation. Over time they lose value, and this generates a large deficit. (This is the factor that has worsened since 2014.)

How likely is this scenario?

- The entire UK university sector is not about to go bankrupt. The university sector is booming. See Figure 2.
- USS is a scheme with more than 150 participating employers. Test 1 may be legitimate for a single-employer scheme but not for a multi-employer scheme like USS.
- The mean projected deficit (“best estimate”) in the Test 1 scenario of scheme closure is an £8.3 billion surplus but there is great uncertainty around the actual figure. In November the stated deficit went from £5.1bn to £7.5bn when the employers stated that they would not accept the previous level of risk.

The scheme could pay its way without additional payments from employers, employees or cuts in benefits.

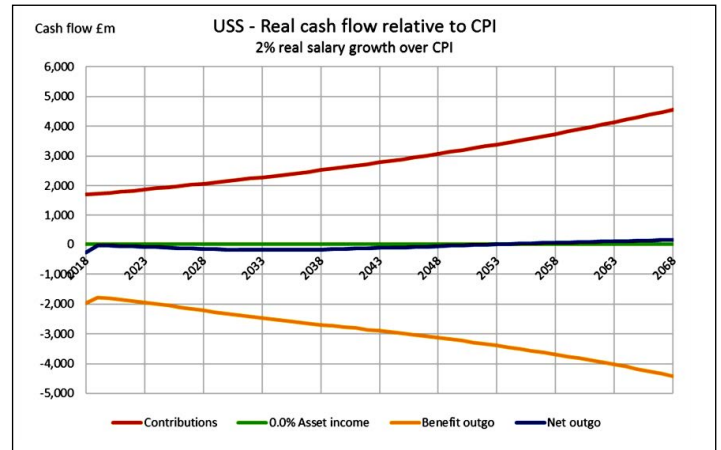


Figure 1: Real-terms cash flow position adjusted for CPI (40 year projection), from Salt and Benstead (2017), Progressing the valuation of USS. London: First Actuarial.

Defined Contribution

The principle of Defined Benefit is that you can predict your pension at retirement. In the days of Final Salary with a 1/80th accrual rate, an employee who worked for 40 years would retire on half their final salary.

When Final Salary was abolished and replaced with Career Average, the calculation changed – for most people, worth less – but it was still possible to get a realistic pension estimate from USS.

With Defined Contribution, all contributions are placed in an individual portfolio of stocks and shares. As everyone knows, the value of stocks and shares can go down as well as up. If you are unlucky, your DC pension might be worth less in five years time than now. A DC pension is a long-term bet on the stock market – a notoriously risky thing to do.

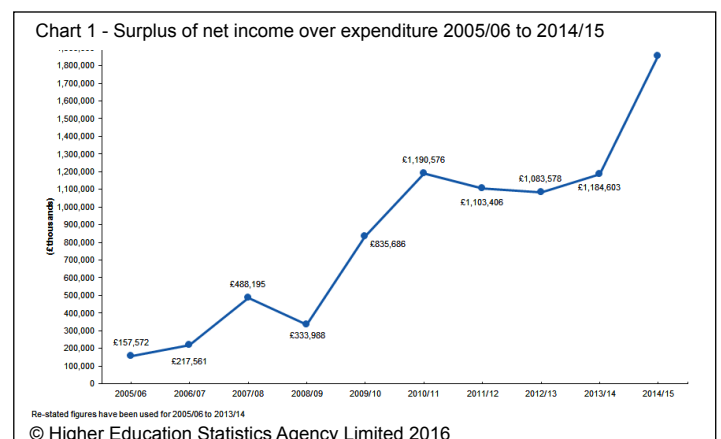


Figure 2: University sector total surplus (including non-USS institutions) over the ten years to 2014/15 (Source: HESA).

Colleagues with savings in banks might decide to invest in the stock market but would be foolish to invest savings they could not afford to lose.

- USS can pool risk across investments using its income to guard against short-term fluctuations. It can choose to sell stock at a time that benefits the fund.
- Individuals have no such flexibility. We can choose to gamble our pension by investing in higher-yield and higher-risk stocks and shares, or act conservatively and put our savings into low-interest gilts (and watch inflation erode value). As we age we will be forced into low-risk, low-yield options.

The pension cut

Payments into your pension will be cut by almost a quarter. Currently employers contribute 18% of salary before tax, and employees 8% of salary, totalling 26%. In the proposed DC scheme, employers contribute 12%, with 6% going into a separate “deficit recovery” pot to protect the employers’ pension liability.

This cut will discriminate by age. Those close to retirement may be OK but our youngest colleagues will have a larger DC pension and face a bigger cut.

The uncertainty of stocks and shares makes it difficult to estimate how these cuts translate into pension losses. A study by First Actuarial, commissioned by the UCU, estimates a 20 to 40% loss in future pension value and that a typical new employee would lose around £200,000 in pension on retirement. The employers’ actuaries AON put the loss at between 10% and 20%, making some more optimistic assumptions and by including the state pension!

Not all employers agree with the UUK hard-line position, apparently held by a minority 42% of institutions. Warwick and Lancaster, have argued for a much more flexible approach:

“I am firmly of the belief – as indicated in commentary already in the public domain – that there is a need to maintain a meaningful defined benefit scheme for those members of staff, present and future, who perceive pension provision as a key factor in their choice entering or remaining in higher education.”

(Prof Stuart Croft, Vice Chancellor of Warwick University, 18 Jan)

The USS cut will impact terribly on the next generation of university staff. A generation already carrying large student debts, and whose early career salaries are mostly spent on private sector rents, now face uncertainty in retirement.

Our defence of USS is not based on self-interest. We also believe in inter-generational solidarity and the future of our universities.

These changes can trigger a spiral of future cuts if staff opt out. Some may prefer to take salary after tax into savings schemes, and forgo the 12% employer contribution. The next generation of staff may opt out of USS due to poor performance and cost. USS could then find itself in a real deficit, and unable to pay pensioners.

What can we do?

The decision of the USS Board to impose the employers’ 100% Defined Contribution plan now means that the only way of saving our pensions will be by pressure on university employers.

UCU has just completed an industrial action ballot of its members. Nationally, 58% of eligible UCU members returned their ballot papers with 88% voting for strike action and 93% for action short of a strike.

Strike action is planned to be hard-hitting and is likely to begin soon. It will be tough, but then the losses we face are devastating. The aim is to pressure the employers to reach a collective agreement with UCU that protects pensions.

Now is the time to join the union and take part in the action alongside your colleagues. UCU members will be asking colleagues to support them and respect the action, whether or not they are union members.

The employers could go back to USS to extend negotiations. The Board decision could be rescinded. We know that the Pension Regulator (the government regulator) is flexible around the valuation method and negotiation time-scale. The alternative, involving compensating staff for pension losses of hundreds of thousands of pounds, is far more expensive!

A key reason that we are in this ‘crisis’ concerns the estimated risk (liability) of employers that is factored into the deficit calculation. Like many VCs, we think that there is a lot more that Government could do to shoulder some, if not all, of this risk.

Our colleagues in many other European countries, post-92 universities, schools and FE colleges, the NHS and government, all have pensions underwritten and guaranteed by the state. Why should UK pre-92 universities have a pension scheme with no government guarantee? The employers have to pay their fair share but we need to put pressure on the Government to step in and support the pension fund.

More information and to join the UCU go to ucu.org.uk/strikeforuss