



The proposed changes to USS – what does this mean for affected members?

Background

USS is legally required to undertake a triennial valuation to ensure that it has enough funds in the pension scheme to pay retirement benefits to its scheme members in the future.

The 31 March 2017 valuation identified a deficit of around £7.5 billion. As a result USS is required to produce a recovery plan which will reduce the deficit and ensure that the schemes funding position is sustainable. The deadline to submit both the valuation and a recovery plan to the Pension Regulator is 30 June 2018.

The USS scheme trustee establishes what contributions are payable to maintain the current level of benefits in the scheme. The USS Joint Negotiating committee (comprised of equal representation from Universities UK (UUK) and the University and College Union (UCU) with an independent chair with a casting vote) is required to decide on how the cost of the increase can be met. This can result in a change to future benefits, future contributions or both.

The JNC met on 23 January 2018 to consider proposals from UUK and UCU. The JNC voted to support the UUK proposal. The result was determined by the casting vote of the JNC chair.

A formal employer consultation will begin on 19 March 2018 and all affected employees will be invited to participate.

What is a defined benefit pension?

A defined benefit pension is whereby an employer provides a pension and lump sum on retirement which is based on pensionable earnings and is calculated by using a predetermined formula.

What is a defined contribution pension?

A defined contribution pension arrangement is a retirement plan consisting of employer and employee contributions. A member can decide how to invest the joint contributions and can purchase a pension (annuity), access a cash sum or both on retirement. The fund includes tax free contributions and investment returns.

What sections of USS pensions are based on defined benefit and defined contribution?

USS pensions can be made up of two sections – a defined benefit section called the USS Retirement Income Builder and a defined contribution section called the USS Investment Builder.

USS proposes removing the option for the 'USS Retirement Income Builder' (based on defined benefit) from **1 April 2019** (at the earliest), making USS pensions wholly based on defined contributions through the USS Investment Builder.

Options to contribute to a defined benefit section, such as the USS Retirement Income Builder, may be reintroduced in the future if the scheme funding position is more favourable.

What is the 'USS Retirement Income Builder'?

The 'USS Retirement Income Builder', based on a defined benefit, was introduced on 1 April 2016. It is a Career Average Revalued Earnings (CARE) defined benefit arrangement which is calculated by dividing the pensionable salary earned within a tax year by a factor of 75. Annual increases linked to Consumer Price Indexing (CPI) are then applied to the resulting pension and lump sum until retirement.

Contributions to the USS Retirement Income Builder are currently capped at **£55,550** for the **2017/18** tax year. The proposed changes by USS would remove the option for this type of pension plan by reducing the defined benefit section of USS to zero from **1 April 2019** (at the earliest).

What is the 'USS Investment Builder'?

The USS Investment Builder, based on a defined contribution from employees and employers, allow USS members to select from a range of investment options (low, medium, high risk & ethical) to invest the combined employee and employer contributions via an online service (MyUSS). Default investments (managed by USS) are applied if a member does not self-select.

Currently, USS members contribute to the USS Investment Builder from pensionable earnings exceeding **£55,550**. USS propose to move to a wholly defined contribution scheme from **1 April 2019** when the option for the USS Retirement Income Builder is removed.

The proposal would maintain the current level of pension deductions (**18%** employers and **8%** employees). The amount invested into the USS Investment Builder section will amount to:

Employees 7.65%

Employers 13.25%

Total investment 20.90%

Example of annual pension accrual (USS Retirement Income Builder)

Pensionable Earnings for the 2017/2018 tax year **£45,000**

Factor used to calculate pension **75**

Employee Contribution (8%) **£3,600**

Employer Contribution (18%) **£8,100**

Formula - Annual Pension **Pensionable Earnings / 75 = Annual Pension**

Formula – Lump Sum **Annual Pension x 3 = Tax Free Lump Sum**

		<u>Secured Benefits</u>
Calculation - Annual Pension	£45,000 / 75	£600
Calculation – Lump Sum	£600 x 3	£1,800

Annual increases as defined by the scheme rules are applied to the pension and lump sum by USS until retirement.

Example of annual pension accrual (USS Retirement Income Builder) plus a defined contribution (USS Investment Builder)

Pensionable Earnings for the 2017/2018 tax year	£70,000	
Factor used to calculate pension	75	
Employee Contribution (8%)	£4,444	
Employer Contribution (18%)	£9,999	
Formula - Annual Pension	Pensionable Earnings / 75 = Annual Pension	
Formula – Lump Sum	Annual Pension x 3 = Tax Free Lump Sum	
		Secured Benefits
Calculation - Annual Pension (with capped salary)	£55,550 / 75	£740.66
Calculation – Lump Sum	£740 x 3	£2,222
Pensionable Earnings above the Cap	£14450	
Employee Contribution above the Salary Cap (8%)	£1156	
Employer Contributions above the Salary Cap (18%)	£2601	
Employee Contribution invested (8%)	£1156	Total Investment
Employer Contribution invested (12%)	£1734	£2890
2.1% Deficit Recovery (employer contribution)	£303.45	

Annual increases as defined by the scheme rules are applied to the Retirement Income Builder (defined benefit) pension and lump sum by USS until retirement.

Proposed changes to USS from 1 April 2019 (at the earliest)

Proposal	How does this affect USS membership
The salary threshold (the salary up to which defined benefits currently build up) will reduce to zero, subject to review at future valuations.	Pensionable service accrual in the Retirement Income Builder (defined benefit) will cease.

	Existing added year and added pension AVC contracts can continue as per the scheme changes of 1 April 2016 Contributions to a defined benefit section can be reintroduced in the future if the scheme funding position is more favourable.
Future benefits will be built up in the USS Investment Builder (the defined contribution part of the scheme).	Comparative modelling between the retention of the Retirement Income Builder and moving solely to the Investment Builder were undertaken by Aon on behalf of UUK. All scenarios predict a fall in retirement income as a result of the proposed changes.
The employer contribution will cover their cost of future benefits in the USS Investment Builder, death and incapacity benefits (still paid out on a defined benefit basis), the subsidy of investment management charges (increased to 0.2% to cover the full period to the next valuation), deficit recovery contributions, and scheme running costs.	This represents an increase from 0.1% to 0.2%. This is a component of the employer contribution.
Members will contribute 8% of pay, but will have access to a lower cost option of contributing 4% while still receiving the full employer contribution into the USS Investment Builder of 13.25%	The default position for employee contributions is 8%. The option to reduce contributions to 4% whilst retaining the same level of employer contributions could be a more affordable option for scheme members. Employer contributions into the Investment Builder would increase from 12% to 13.25%
The 'match' – the additional 1% employer contribution currently available – will be discontinued from the date at which the changes take effect.	USS members can elect to pay non-match additional contributions to the Investment Builder.

Defined contribution (USS Investment Builder) examples with standard employee contributions of 8% and reduced employee contributions of 4%.

Example 1

Pensionable earnings for 2019/2020 tax year £45,000

Employee Contributions (8%) £3,600
Employer Contributions (18%) £8,100

Employee Contribution invested (7.65%) £3,442.50	Total Investment
Employer Contribution invested (13.25%) £5,962.50	£9,405

Pensionable earnings for 2019/2020 tax year £45,000

Employee Contributions (4%) £1800
Employer Contributions (18%) £8100

Employee Contribution invested (3.65%)	£1,642.50	Total Investment
Employer Contribution invested (13.25%)	£5,962.50	£7,605

Example 2

Pensionable earnings for 2019/2020 tax year £70,000

Employee Contributions (8%) £5,600
Employer Contributions (18%) £12,600

Employee Contribution invested (7.65%)	£5,355	Total Investment
Employer Contribution invested (13.25%)	£9,275	£14,630

Pensionable earnings for 2019/2020 tax year £70,000

Employee Contributions (4%) £2,800
Employer Contributions (18%) £12,600

Employee Contribution invested (3.65%)	£2,555	Total Investment
Employer Contribution invested (13.25%)	£9,275	£11,830