

Consultation

on proposals for changes to USS

October 2010

Following many months of discussions about changes to Universities Superannuation Scheme (USS), a package of proposals put forward by the USS Joint Negotiating Committee (JNC) has been accepted by the USS Trustee Board, subject to this consultation.

The proposals must now be communicated and consulted upon by each relevant USS employer as required by law, and this document provides you with information on:

- the proposed changes;
- where you can find out more; and
- how you can express your views.

You have received this document because you are either an active member of, or are eligible to join, the scheme. It is also being given to recognised trade union or other representatives who are also part of the consultation process.

For existing scheme members, the proposals continue final salary pension arrangements, and benefits accrued up to 31 March 2011 will be protected.

USS is hugely valued by its members, something that is fully acknowledged by both your employer and the USS Trustee Board. Inside you will see some explanation of the funding challenges that the scheme faces and why changes are being proposed.

The proposed changes aim to maintain USS's status as a scheme that offers an excellent level of pension benefits. They will help safeguard the future of the scheme, keeping it viable for employers and attractive for members. An overview of the proposed changes is shown in the 'at a glance' box and explained in more detail inside.

The consultation will last for a minimum of 60 days and will close on Wednesday 22 December 2010. The responses will then be considered by the Trustee Board early in 2011 before final decisions are made. If you wish to respond, you should do so before the closing date.

The proposed changes at a glance...

For existing USS members

Under the proposals, existing USS members would retain final salary scheme benefits. The following changes are proposed in respect of your benefits accruing from 1 April 2011 onwards. Benefits accrued up to 31 March 2011 will be fully protected in accordance with the USS rules and also in line with pensions legislation.

Changing the Normal Pension Age – Increase in Normal Pension Age to 65 **page 5**

Contribution increases and cost sharing – member contributions would increase from 6.35% to 7.5% of salary, and cost sharing would be introduced **pages 6, 7, 9**

Introduction of flexible retirement – a new arrangement giving the option of taking some benefits from age 55 whilst continuing to work part time **page 8**

Introduction of a cap on increases to pensions and on revaluation of deferred benefits **page 9**

For new USS members

(as from 1 April 2011) **pages 10-11**

A new benefits section for new USS members who join on or after 1 April 2011 – these would be defined benefits calculated using a career average revalued earnings (CARE) type approach, with the following features:

- Normal Pension Age of 65;
- Member contributions at 6.5% of salary and cost sharing would be introduced;
- A pension of 1/80th and a lump sum of 3/80ths of salary would accrue each year;
- The benefits would be revalued every 1 April, up to retirement or leaving the scheme;
- A cap would be implemented on the amount of annual increases to pensions once in payment, and to the revaluation of deferred benefits; and
- Flexible retirement – the option of taking some benefits from age 55 whilst continuing to work part time.

Background to the changes

Over the last 18 months, employer representatives have been in discussions with University and College Union (UCU) representatives about potential changes to USS.

They had hoped to reach an agreed outcome from the discussions but, despite the very best efforts of those involved, that was not possible. While both sides confirmed that some level of change was necessary, there was no agreement between them on the scale of the change required.

It was agreed that both parties would put forward a package of proposed scheme changes to the USS Joint Negotiating Committee (JNC), which includes an independent chairman as well as an equal number of employer and UCU representatives. A decision was taken by the JNC to recommend proposals put forward by the employers. Following this, on 22 July 2010, the USS Trustee Board received the recommendation and agreed to take steps to implement the proposals, subject to the statutory information and consultation requirements.

The need for change

Employers within USS are committed to the proposed changes as necessary to safeguard the long-term sustainability of the scheme. The scheme is not in crisis (though it is in danger of becoming unaffordable) and the proposed changes are designed to ensure that the scheme is sustainable and will continue to be so in the future. The proposals come at a time when mounting financial and other pressures are putting a strain on the scheme.

Among these pressures are longevity, salary increases, and levels and volatility of investment returns:

- **Longevity** – members are living longer and are receiving their pensions for many more years than was anticipated when the scheme was originally designed. The life expectancy of an individual retiring today is many years longer than it was when the scheme was set up in 1975; longevity is predicted to continue to increase and new joiners are expected to live even longer.
- **Salary increases** – salaries in the higher education sector have risen faster than anticipated in recent years and these increases have led to continuing increased pension costs. Under a final salary arrangement, trends of higher than expected pay rises result in an increase in the amount of benefits payable in respect of all previous service.
- **Investment returns and volatility** – while investment markets are recovering, they remain well below their expected levels. Ongoing volatility is causing uncertainty over future returns. As USS matures with increasing numbers of pensioners and relatively fewer active members, the scheme will tend to invest more of the fund in secure assets which inherently have lower investment returns. For these reasons, future investment returns are expected to be lower than before the financial crisis of 2008.

Regulatory and governmental pressures are also adding to USS's funding concerns, with the statutory Pensions Regulator placing stronger, shorter-term funding demands on pension schemes across the UK. Many of the above factors, and indeed others, have led to a large reduction in the number of final salary, defined benefit pension schemes in the private sector over the last few years.

“Members are living longer and are receiving their pensions for many more years than was anticipated when the scheme was originally designed.”

Higher education also faces additional pressures as the Government moves to cut its funding for the sector. In the emergency budget on 22 June, the Chancellor announced that the coalition Government would seek to remove the UK's deficit entirely by 2015/16. As a result, it seems certain that higher education will be facing significant funding cuts over this period. The current spending review outcome is to be announced this month. In this environment, failure to control rising pension costs can only lead to additional reductions in staff numbers with a consequent impact on the student

experience and research. The higher education sector is still significantly publicly funded and it would, understandably, be considered unacceptable to use additional public funds to meet increased pension costs.

There is also wider political pressure for reform, reflecting the Government's view that final salary pension schemes, particularly those funded from the public purse, are no longer affordable in their current form. The Independent Public Service Pensions Commission, which was established in the summer, has been given a very short timescale in which to make its recommendations on public sector pension scheme reform underlining the political pressure for change. These reforms will have an impact on members of those schemes employed in higher education.

The next valuation of USS will take place as at March 2011 and there is a strong chance that it will result in a funding deficit. The changes put forward in these proposals will help to reduce the likelihood of additional contributions to fund

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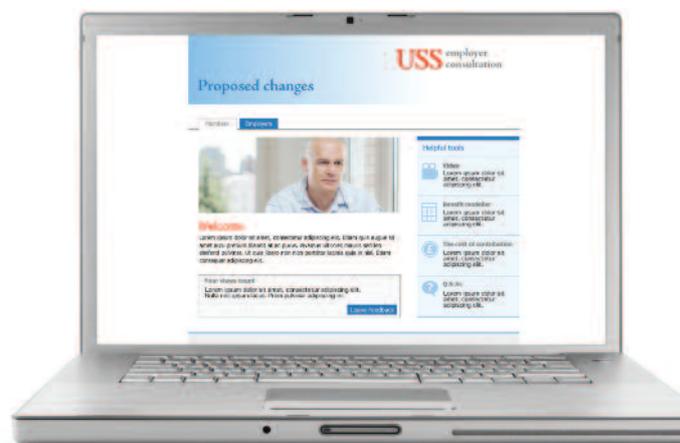
that deficit being required. Without scheme changes, any further increase in employer contributions, in addition to the 2% required from 2009, could make the scheme unaffordable to employers.

Further information from the employers setting out the reasons for reform of USS can be found in the document ‘USS – the need for reform’, prepared by the Employers Pensions Forum.



www.ussconsultation.co.uk

A website has been created to provide you with further information on the proposed changes and to give you the opportunity to express your views. If you prefer, you may make your views known to your trade union or other recognised representatives (as set out in the legal rules relating to consultation), as they will be consulted separately by your employer. Further details of the website can be found on page 4.



Consultation process

The period for the consultation starts on **Wednesday 20 October 2010** and will run until **Wednesday 22 December 2010**. During the consultation period, USS members and those who are eligible to join USS, together with recognised employee representatives, have the opportunity to consider the proposed changes and provide their responses.

Your employer knows how much USS members value the scheme and it welcomes your views on the proposed changes. The consultation must, by law, last for a minimum of 60 days.

Once the consultation period ends, the USS Trustee Board will consider all the comments received from affected members and their representatives before it decides on the final form of any changes. You will then receive further information about the final shape of the proposed changes.

Key dates

Consultation

20 October 2010

Consultation starts:

- read this document
- visit the website to find more information and give your response

22 December 2010

Consultation ends:

- deadline for receipt of your response

Post consultation

January 2011

The USS Trustee Board considers responses and finalises decisions on the proposed changes

March 2011

Members receive information on the USS Trustee Board's decision

1 April 2011

Proposed date of implementation of any changes

Please note you do not need to take any action during the consultation period unless you would like to provide a response.

Where to find out more

visit www.ussconsultation.co.uk

Where you can:

- Read Q&As and refer to a glossary of useful terms.
- Use interactive modellers to see the effect of the changes.
- View a video explaining the changes
- Provide your response.

The website will be available throughout the consultation period and will be regularly updated with new Q&As as questions are received.

Give your response

- 1 Visit www.ussconsultation.co.uk
- 2 Select the respond icon

Follow the instructions on the website. Your response will be anonymous unless you decide to add your name.

Please note that you can provide a response on the proposed changes only once.

Other ways to provide a response:

- Contact your recognised trade union or representative body and express your views, as it will be separately consulted by your employer, or
- If you do not have online access you can express your views in writing to your employer through the usual contact for pensions (clearly marking your response 'USS Consultation').

Proposed changes in detail

The following pages explain the proposed changes in detail.

Changing the Normal Pension Age

From April 2011, the Normal Pension Age is to move to 65.

The Normal Pension Age is the earliest age at which a member has the right to draw benefits from the scheme without actuarial reduction (in the absence of special circumstances, such as incapacity). The Normal Pension Age would be age 65 for new entrants to the scheme from 1 April 2011, and for the future service, after 31 March 2011, of existing members of the scheme not already 55 years of age.

Importantly, this does not mean that you have to work until age 65 to receive retirement benefits. As explained in more detail below, under the proposals it will be easier to retire and claim your benefits from as early as age 55. However, if you do so, the benefits that you receive would be lower because – for service from April 2011 – they would be paid on an unreduced basis only if drawn from age 65 (and actuarially reduced if drawn before that age).

Changing the Normal Pension Age is a way of addressing the fact that generally people are living longer and as a result receiving their pensions for longer. The proposed changes allow the Normal Pension Age to be extended further in the future, so that in future years it would move in line with changes decided by the Government in relation to the State Pension Age.

Importantly, existing members of the scheme aged 55 or over at 1 April 2011 would be exempt from the changes to Normal Pension Age. While they will be unaffected by the Normal Pension Age changes in the proposals, the other proposed changes would apply to them.

Here are some examples of the way that the proposed changes to Normal Pension Age would work:

example

John is age 63, and plans to stay in the scheme until retirement at age 65 in April 2013 when he will have completed 23 years of pensionable service in USS.

John is unaffected by the changes to Normal Pension Age because he will be over age 55 at the date of the changes (1 April 2011). The calculation of his benefits is straightforward, in that he will have a pension of 23/80ths of his final salary, together with a standard lump sum of three times the amount of his pension.

example

Janet is age 53, and plans to retire at age 65 in 2023 when she will have completed 30 years of pensionable service.

She will be under age 55 at the time of the changes to Normal Pension Age, so she is not exempt from the changes. However, so long as she remains in the scheme and works until age 65, the proposed changes to Normal Pension Age will not affect the amount of her retirement benefits. When she retires at age 65, Janet will receive 30/80ths of her final salary as a pension, and three times that amount as her standard lump sum.

example

Michael is age 53 and plans to retire at age 60, with his employer's consent, on 31 March 2018 (7 years following the start of the proposed change).

His benefits are based on 23 years' pensionable service but, because he is retiring before age 65, his benefits would be calculated in 'tranches' as follows:

- 7 years of service (the period from the date of the change, 1 April 2011, to 31 March 2018) would have a Normal Pension Age of 65, so an actuarial reduction to account for taking benefits 5 years early would apply to the calculation of this tranche of Michael's benefits; and
- 16 years of service (from 1 April 1995 to 31 March 2011) would have no reduction applied because he is retiring at age 60 and he has his employer's consent to retire at that age.



A modeller is available on the consultation website to allow members to assess the impact of this proposed change on their future benefits should they retire upon reaching age 60 (or later). Members would be able to convert pension to lump sum, or vice versa, as they can under the present rules.

Please refer to the Q&A section on the website for further information on the implications of this proposed change if a member retires early before reaching the age of 60.

Increase to employee contributions

The rate of ordinary employee contributions for existing members is proposed to increase to 7.5% of salary with effect from 1 April 2011.

This represents an increase of 1.15% of salary. There are a small number of members who joined the scheme after age 60 who currently pay an extra 1% contribution, but this extra contribution would cease and all existing members would pay the 7.5% contribution rate.

Regarding rates of contributions, the proposals contain important provisions relating to the contributions payable by employers. The introduction of these changes will not trigger lower employer contributions. The employer contributions to USS will remain at 16% of salary from 1 April 2011, subject to any requirements arising from the March 2011 actuarial valuation. The employers have emphasised that the objective in proposing these changes is to mitigate the risks to the scheme, and not to cut their pension contributions.

The following examples give you an idea of the proposed changes in employee contributions, based on different salary levels and assuming no change from the present in tax and National Insurance rates, allowances and thresholds:



What would it cost me?

To find out how much you would pay each month under the proposed changes, visit www.ussconsultation.co.uk and select the 'modeller' icon.



example

Robert has an annual salary of £30,000 and pays monthly contributions of £158.75, using the existing contribution rate of 6.35%. His monthly payslip with the existing 6.35% contributions rate is shown below:

Employee Name – Robert Smith

Annual salary	Monthly salary	Deductions	Amount	Take home pay per month
£30,000	£2,500.00	Tax Pension Nat Insurance	£360.33* £158.75 £189.38	
Total	£2,500.00	Total	£708.46	£1,791.54

*based on a basic rate taxpayer with standard personal allowances for the tax year 2010/11

If the proposed changes went ahead, he would pay monthly contributions of £187.50, using the proposed contribution rate of 7.5%. After the effect of tax relief, **Robert would pay £23.00 a month more under the new arrangements. Robert's revised monthly payslip is shown below:**

Employee Name – Robert Smith

Annual salary	Monthly salary	Deductions	Amount	Take home pay per month
£30,000	£2,500.00	Tax Pension Nat Insurance	£354.58* £187.50 £189.38	
Total	£2,500.00	Total	£731.46	£1,768.54

*based on a basic rate taxpayer with standard personal allowances for the tax year 2010/11

Sarah has an annual salary of £40,000 and pays monthly contributions of £211.67, using the existing contribution rate of 6.35%. Her monthly payslip with the existing 6.35% contribution rate is shown below:

Employee Name – Sarah Taylor

Annual salary	Monthly salary	Deductions	Amount	Take home pay per month
£40,000	£3,333.33	Tax Pension Nat Insurance	£517.42* £211.67 £267.71	
Total	£3,333.33	Total	£996.80	£2,336.53

*based on a basic rate tax payer with standard personal allowances for the tax year 2010/11

If the proposed changes went ahead, she would pay monthly contributions of £250.00, using the proposed contribution rate of 7.5%. After the effect of tax relief, Sarah would pay £29.66 a month more under the new arrangements. Sarah’s revised monthly payslip is shown below:

Employee Name – Sarah Taylor

Annual salary	Monthly salary	Deductions	Amount	Take home pay per month
£40,000	£3,333.33	Tax Pension Nat Insurance	£508.75* £250.00 £267.71	
Total	£3,333.33	Total	£1,026.46	£2,306.87

*based on a basic rate tax payer with standard personal allowances for the tax year 2010/11

Note: the two examples shown are for members who are not part of arrangements for the salary sacrifice of ordinary pension contributions. Additional savings in National Insurance contributions would be secured for members who are part of salary sacrifice for pension contributions arrangements.

“The employers have emphasised that the objective in proposing these changes is to mitigate the risks to scheme, and not to cut their pension contributions.”



Early and late retirement

The proposed changes would introduce a right for members to retire from age 55 and draw immediate benefits, but these would normally be actuarially reduced unless retirement was at age 65 or later.

Under this proposed change, a member who has at least two years' scheme service would have the right to retire early from age 55 (or earlier protected pension age under the Finance Act 2004) without the consent of the employer or USS, and would be entitled to actuarially reduced benefits. The amount of the actuarial reduction would reflect the number of years and months before the Normal Pension Age of the member taking the pension. Such benefits can be augmented at the discretion of the employer.

The proposals also take account of members who continue in the scheme after age 65. It is likely that more people in the future will work beyond age 65 given the planned removal of the default retirement age, so this proposed change will have increasing importance. Where a member continues in service beyond age 65, he or she will continue to have the option to pay pension contributions. If the member so decides, his or her employer would now be required to pay contributions. Benefits would be calculated for periods of membership after age 65 in the same way as for service prior to age 65.



Redundancy

A further proposed change relates to retirement on the grounds of redundancy.

In such cases, scheme benefits would remain payable without actuarial reduction from age 55 (or earlier protected pension age) where a member with five or more years' pensionable service retires early on the grounds of redundancy before 1 April 2013. However, where a member retires early by reason of redundancy after 31 March 2013, his/her entire benefits would be actuarially reduced.

Introduction of flexible retirement

It is proposed that flexible retirement would be made available to members, subject to the consent of the member's employer.

This means that from age 55, a member would be able to draw between 20% and 80% of the pension and lump sum that has been built up, whilst he or she continues in pensionable employment. A condition would be that the member's working hours and salary are both reduced by a percentage between a minimum of 20% and the maximum of 80%.

“From age 55, a member would be able to draw between 20% and 80% of the pension and lump sum that has been built up, whilst he or she continues in pensionable employment.”

The employer must certify that the reduction to working hours and salary will be for a minimum of 12 months.

A member would be permitted to have a maximum of two flexible retirements before drawing the entirety of his or her USS benefits on a third occasion. Whenever benefits are drawn before Normal Pension Age, under the proposed flexible retirement arrangements, the amount payable would be reduced for early retirement.

Increases to pensions

You may be aware that once a member reaches retirement and starts to receive his or her pension, that pension is subject to review annually so that its value keeps pace with inflation.

Where people leave the scheme before reaching retirement age, they become entitled to deferred benefits (held in the scheme until payable), which are similarly revalued in line with inflation. As a way of addressing inflationary risk, it is proposed that the rates of pension increases and revaluation of deferred benefits – for service after 31 March 2011 – would be capped.

The proposed change is that increases to pensions in payment for future service after 31 March 2011 would be subject to a maximum of 5% a year and that the rate of revaluation of deferred benefits in the scheme for future service after 31 March 2011 would be subject to a maximum of 2.5% a year.



The trustee company would have discretion to award increases and revaluation above the proposed caps, subject to the availability of scheme funds and by reference to the prevailing rate of Consumer Prices Index (or ‘CPI’) increases.

“Quite separately from these proposals, the Government has recently announced that increases and revaluation for official pensions will change from being based on increases in the Retail Prices Index to being based on increases in the CPI.”

USS pension increases and revaluation of deferred benefits are currently based on the increases and revaluation required for ‘official pensions’ under public sector pension schemes. Quite separately from these proposals, the Government has recently announced that increases and revaluation for official pensions will change from being based on increases in the Retail Prices Index to being based on increases in the CPI.

Future cost sharing

Part of the proposed new contribution arrangements is the introduction of cost sharing.

Every three years there is a valuation of the scheme and this exercise may result in a change in the level of total pension contributions required to be paid.

In the first instance the Joint Negotiating Committee (JNC) is to determine how any increase in the contribution rate for the scheme above the base level (which from 1 April 2011 is to be 23.5% of salary, i.e. 16% + 7.5%) is to be addressed, including any requirement to pay deficit contributions as part of a recovery plan for past service funding.

The JNC would also determine how any decrease in the contribution rate required for the scheme is to be addressed.

If the JNC does not agree to specific cost sharing arrangements, nor to other benefit modifications, future cost increases and decreases (from above the base level) would be shared between employees and employers in the ratio 35:65.

A new benefit section for people who join USS on or after 1 April 2011

The following information will apply to you if you join the scheme (or re-join it) on or after 1 April 2011.

If you are an existing contributing member of the USS final salary section who leaves the scheme, this new section would not apply to you if you leave for a period of less than six months (or up to five years in special circumstances explained below) and subsequently re-join it.

The new section is to provide secure, defined benefits that are similar to those provided under a career average revalued earnings ('CARE') formula.

The benefits under the new section, would be a pension of 1/80th and a lump sum of 3/80ths of salary for each year. Each year's accrued pension and lump sum would be revalued every 1 April, up to retirement or leaving the scheme. The rate of revaluation would be in line with CPI up to a maximum of 5% a year, plus one half of any excess of the increase in the CPI above 5% a year. This would be subject to the total revaluation not exceeding 7.5% a year.

“The new section is to provide secure, defined benefits that are similar to those provided under a career average revalued earnings ('CARE') formula.”

All the other benefits associated with the scheme would be similar to those in the final salary section of USS, except that the CARE-like formula of benefits would be used as the basis rather than final salary benefits.

A member of the final salary section of the scheme at 31 March 2011 who leaves the scheme and later re-joins the scheme within six months would re-join as a member of the final salary section. However, if such a member leaves and re-joins the scheme with more than a six month gap, the member would re-join as a member of the new section. Special circumstances apply if the member of the final salary section were to leave the scheme and re-join it with the same

or an associated employer, within five years. In these circumstances, with the prior agreement of the original employer, the member would be able to re-join the final salary section. For this exemption to operate, the employer must certify before the member leaves the scheme that there is a reasonable expectation of him/her re-joining the scheme within five years.

If you are currently a deferred member of the scheme, as at 31 March 2011, then you would re-join the final salary section if you re-join the scheme before 1 July 2011. A deferred pensioner who re-joins the scheme after 30 June 2011 would re-join as a member of the new section, and would have no option to link past service benefits prior to that date to future final salary in the scheme. Such past service benefits would remain deferred benefits in the scheme.

The example opposite shows how benefits would build up over a three-year period, assuming a salary of £40,000 in year one (increasing by £2,000 each year) and CPI of 2.5% a year.



Example of benefits provided by the new, CARE-like benefits section

Year	Salary	Amount of pension earned in the year	Plus previous year's pension revalued	Cumulative total pension accrued
1	£40,000	£500.00	–	£500.00
2	£42,000	£525.00	£512.50 (£500.00 + 2.5%, total pension earned at end of year 1 revalued)	£1,037.50
3	£44,000	£550.00	£1,063.44 (£1,037.50 + 2.5%, total pension earned at end of year 2 revalued)	£1,613.44

All pension values shown are per annum. Under the proposals, the new CARE-like section will also provide a lump sum calculated at three times the amount of the annual pension and would permit conversion of one to the other in the same way as under the present rules.

In this example, the assumed rate of revaluation of the benefits is 2.5% (reflecting an assumed rate of change in the Consumer Prices Index).

The new benefit section and prospective scheme members

If you are not currently a member of the scheme, but are eligible to join, it is most likely that at some point you decided not to join or opted-out.

In this case, you are eligible to join (or re-join, whichever applies) the scheme, subject to your being in good health. If you do so before 1 April 2011, then you would join (or re-join) the final salary section. However, please do not leave it too late to make these arrangements – it could take at least two months for your application to be processed and for admission or re-admission to the scheme to be confirmed. If you are in this category and wish to re-join the scheme, please contact the usual pensions contact at your employer as soon as possible.

Give your response

If you would like to give a response on the proposed changes:

visit www.ussconsultation.co.uk

Follow the instructions on the website.
Your response will be anonymous unless
you decide to add your name.



Other ways to provide a response:

Contact your recognised trade union or representative body and express your views, as it will be separately consulted by your employer,

OR

If you do not have online access you can express your views in writing to your employer through the usual contact for pensions (clearly marking your response 'USS Consultation').