UCU
University and College Union

USS valuation report

UCU briefing note

The USS valuation is not a wholly objective process. It is based on a set of assumptions and projections in relation to the elements which contribute to the cost of providing pensions over the next 40 years or so.

The USS board will agree its approach to the valuation on 17 November. From discussion with USS officers and the scheme's actuary, it seems that USS will base its valuation on unnecessarily conservative accounting assumptions about the health of the pension fund. The effect of this is to artificially inflate the size of any problems and make USS look less 'funded' than it is. It also creates a retrospective justification for the employers' reforms, railroaded through the scheme earlier this year.

UCU's own actuarial advice indicates that the scheme's assumptions are ultra-conservative. If they are changed even slightly, the fund looks healthier. Further, this bolsters the case that there is room to enable a negotiated settlement that preserves the attractiveness of the scheme

How is USS inflating the sense of a problem?

Perhaps the key conservative assumption underpinning USS's valuation is its use of a low discount rate. The discount rate is an accounting tool used to judge the 'assets' of the scheme (savings invested) against its liabilities (its commitment to pay out pensions to scheme members). It is effectively the rate which determines how much money needs to be set aside now to pay our pensions when they fall due.

USS's discount rate takes into account the extent of USS's investment in higher risk equities, and low risk or risk free 'gilts'. USS is traditionally heavily invested in equities.

USS's new discount rate assumes:

- that the scheme will lower the proportion of its investment in growth equity investments from 85% to 70% to 'de-risk' the scheme
- a marked fall in the rate of performance in USS's equity investments.

UCU's response

In response, UCU notes that:

- Our actuarial advice questions the wisdom of selling equity assets at the rate proposed because the condition of the equity market would make it unlikely that USS would get a good price.
- It also questions USS's proposed reduction in the rate at which equities will perform.

In line with our actuarial advice, UCU proposed that a very slightly higher discount rate (6.4% as opposed to USS's 6.1%) would make a significant difference to the assessment of the fund's health. In fact, such a change in the assumptions would dramatically reduce the calculation of USS's liabilities, from £35.3billion to £33.5 billion, reducing the shortfall in funding from £2.9 billion to £1.8 billion.

In addition, UCU proposes that USS could reduce the scheme's liabilities still further by raising the assumption of the difference between CPI and RPI by 0.2%. This would reduce the shortfall to £0.6 billion.

Finally, and again on the basis of independent actuarial advice, we have made a number of additional recommendations for further changes to some of the other less significant but equally unrealistic assumptions used in the valuation process, including salary growth and life expectancy. If these were adopted, the scheme would show a £1 billion surplus.

In summary, UCU argues that USS has set itself unnecessarily conservative assumptions that generated an unnecessarily gloomy picture of the fund's health.

In reality, changing these assumptions very slightly and resettling them on a basis that our actuarial advice indicates would be realistic and would produce a picture of a far more healthily funded scheme.

Why is USS doing this?

There are several possible reasons why USS might do this.

One is that the board are attempting to retrospectively justify changes that they helped railroad through the scheme in May this year.

It is certain that the employers will try to make use of this to predetermine the talks brought about by UCU's industrial action. However, there may be a longer range reason as well.

Private providers are looking to expand, with the active encouragement of the Coalition Government. But one of the biggest barriers to their ability to compete or to form partnerships with 'public' universities is the current levels of pension provision. Private sector
employers cannot compete and do not want to pay the current contribution rates.

Yet the employers' long term aim to reduce contributions to 10% does represent movement in the right direction as far as the private sector is concerned. As Aldwyn Cooper, principal of the private sector Regent's College recently wrote:

'Pension provision is the one area where the non-state-funded sector necessarily falls behind the current position in publicly funded institutions because the cost of establishing final-salary schemes is unsustainable. On the other hand, state-funded bodies are now coming to the same conclusion: annual employer contributions exceeding 20 per cent cannot be maintained and the demise of such deals is inevitable.'

Could it be that USS and the employers have their sights on removing the barriers to private providers entering the sector in force?