



Hewitt Bacon & Woodrow Limited



Guide to the Universities UK Pension Benefits Strategic Enquiry

Prepared for
**Higher Education
Institutions**

Prepared by
**Hewitt and Stanton
Marris in
conjunction with
Universities UK**

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Introduction

Introduction

Universities UK with financial support from HEFCE and the SFC is sponsoring a strategic enquiry into the pension arrangements of the Higher Education sector. This review takes place against a background of unprecedented change in pensions in both the private and public sector.

We are seeking the views of the institutions of the HE sector on how they see the current system of pension provision and how, if at all, they would like to see changes made.

Last autumn USS carried out a consultation with its member institutions on the options for future funding of the USS scheme. While the decisions reached have relevance for this enquiry, it is worth noting that the USS funding consultation did not set out to address the wider issues covered by this strategic enquiry. We are aware that the USS board will consider the results of this survey in informing its future strategic plans. We hope that respondents will reply accordingly.

We would also like to record here our appreciation and thanks to the twelve institutions which kindly agreed to take part in the pilot survey.

Terms of Reference

The terms of reference for this project were to develop a comprehensive pensions strategy for the higher education sector covering the next ten years. The project will identify options for the development of sustainable and affordable pensions provision that the sector will need to make if it is to continue to recruit and retain high quality staff at all levels, taking into account the potentially diverse requirements of academic, academic-related and support staff and the parallel development of pay and reward policies by the institutions themselves.

The project must be set in the context of the government's ongoing pensions reform programme and the impact on the sector of legislation already introduced to improve the security of members' benefits, which has imposed considerable additional financial burdens.

The project will also identify the actions that will be needed to develop these options, including the appropriate structure for gaining consensus and authoritative decision making and the practical options for cost-effective long term management. It will also need to consider the barriers to change, including those relating to the sector's participation in TPS and LGPS.

Principles

Universities UK in conjunction with Guild HE and the Universities and Colleges Employers Association has developed a set of principles to shape the current enquiry. Those principles are as follows:

- **Sustainability** – future pensions provision must be robust to cope with further periods of great change in the sector and society generally.
- **Affordability** – the cost of pensions payable from a set age is rising inexorably as people live longer. HE is not immune from this - some of the smaller local schemes for support staff are particularly affected.
- **Flexibility** – the differing needs of institutions in recruiting both academic and non-academic staff at all ages must be provided for. This must translate into real and cost effective choices for member institutions.
- **Relevance to the future of HE** – the solution must exhibit a good fit with future strategic developments in HE.
- **Effective governance** – a process for representation and accountability within a legal framework is essential, to create unity of purpose and compatibility.
- **Consensus** – the strategy must gain broad acceptance within the sector, from employers, employees and their representatives. It must also be acceptable to external stakeholders.

Adviser

This briefing has been prepared by the advisers selected by Universities UK to assist in this review, namely Hewitt Associates and Stanton Marris.

Hewitt Associates

- Top three benefit consultancy in the UK and the largest global provider of complete HR solutions.
- Reputation for clear communication and genuine consultancy.
- It combines the businesses of Hewitt Associates and the former UK Partnership of Bacon & Woodrow (originally formed in 1924).

Stanton Marris

- An independent consultancy with a reputation for helping organisations navigate complex people and organisation issues and deliver marked performance improvement.
 - Based in London and established in 1998 by three directors, all well known in their field and partners in major consultancies.
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Consultation Process

The process agreed for the first phase of this project is as follows:

- the selection of the advisers, after establishment of the terms of reference and the principles behind the project.
 - development of a test phase of consultation questions. These were tested on a trial group of 12 institutions. In addition structured interviews were held with each of these institutions in order to verify that the correct issues were being addressed and that the context was clearly understood.
 - following this test phase, the enclosed consultation pack and questionnaire is being sent to all HE institutions.
 - conversations will be held, and views will be sought, from other relevant parties including USS, TPS, DfES, the funding councils and the trade unions.
 - the results of this survey will be analysed by the Steering Group later in 2007 and shared with participants, and a series of proposals developed as possible routes ahead.
-

This Document

This document aims to provide background information on the current pension provision in the Higher Education sector, and on the factors which influence the cost of pensions. Turning then to the questionnaire which is being sent to all of the 160 HE institutions in the UK, this document provides further explanation of some of the questions being asked, and background information on each specific issue. There is also a glossary of pension terms, since the subject is notoriously jargon ridden.

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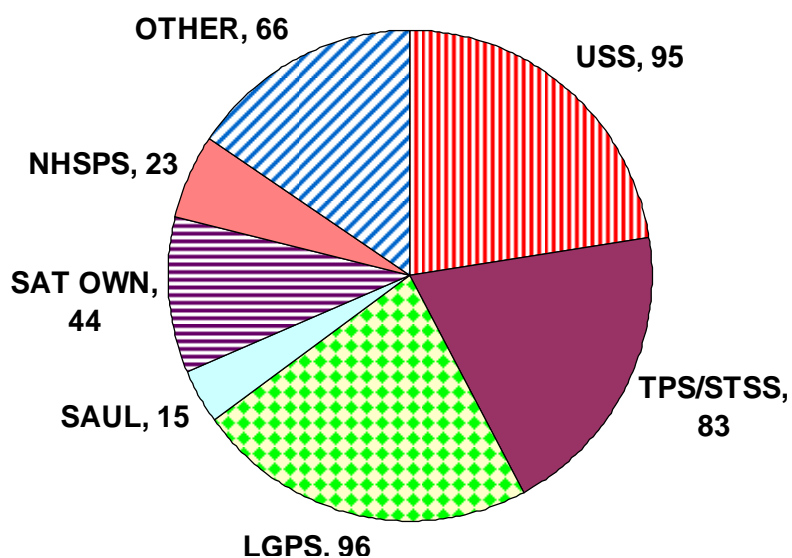
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Current Pension Provision

Participation

Higher Education Institutions participate in five main pension arrangements, namely: Universities Superannuation Scheme (USS), the Teachers Pension Scheme (TPS) (the Scottish Teachers Superannuation Scheme (STSS) in Scotland), Local Government Pension Scheme (LGPS), the Superannuation Arrangements for the University of London (SAUL) and the National Health Service Pension Scheme (NHSPS). In addition many pre-1992 institutions operate their own in-house arrangements for non-academic/lower pay spine staff. Although some institutions participate in several different arrangements, the number of employees involved in some can be very small.

Number of Institutions participating in each external arrangements

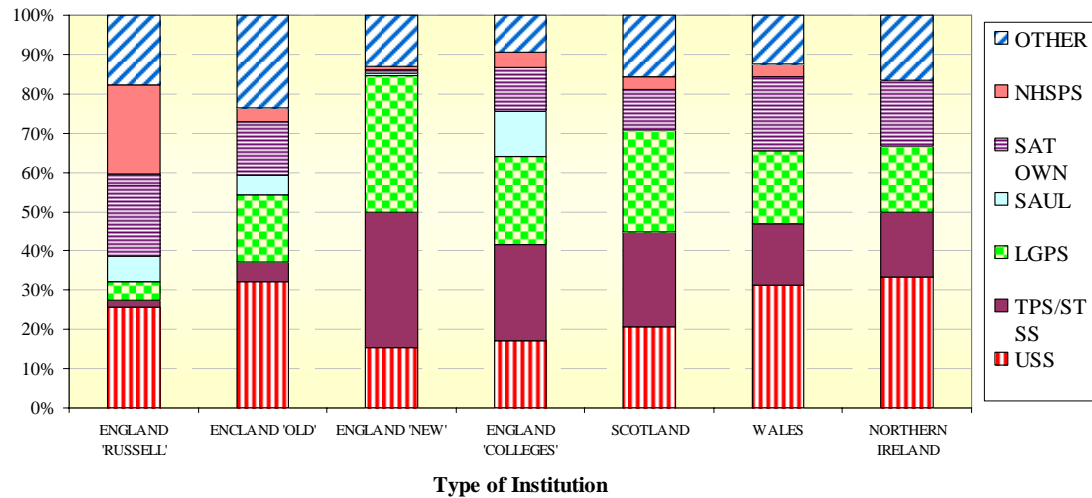


Source: Michael Bourn, 20 Questions Paper

Pensions by Type of Institution

The graph below illustrates how the split of different pension arrangements varies by type of institution.

Institution split by external schemes



Source: Michael Bourn, 20 Questions Paper

Type of pensions provision

There are some strong similarities – and some noticeable differences – between the types of pension provision offered to HE staff.

Similarities

- Final Salary pension provision is almost universal across the HE sector
- There are broadly similar overall level of benefits across schemes (either 1/60ths pension or 1/80ths pension PLUS 3/80ths cash for each year of service)

Differences

- Member contributions - varies from nil to 7% of Pay
- Retirement age – the age at which members can take pension in full ranges from 60 to 65
- Pension increases - varies between full and capped RPI
- Other – differences in terms for ill-health, early retirement benefits etc.

A handful of institutions are providing substantially different benefits for non-academics/low pay spine employees including defined contribution provision.

USS – a summary of benefits

- Final salary scheme (based on the best 12 months' salary in the last 3 years or highest revalued salary over any 3 consecutive years in last 13 years).
- Contribution rate (currently): employer 14% employee 6.35%.
- Normal pension age is 65.
- Unreduced early retirement pension from age 60 in accordance with contract of employment or otherwise at employer's request funded by the scheme pooling of the costs. Unreduced benefits before age 60 at employer's request (or by reason of redundancy) funded by a charge levied upon the employer.
- Pension 1/80ths of final salary for each year's pensionable service plus lump sum (pension x 3).
- Death in service payment: salary x 3.
- Dependants' benefits.
- Ill health retirement pension: unreduced and where the member suffers from total incapacity, enhanced with potential service to age 65.

Governance Issues

One of the issues in the HE sector is the extent to which each institution is in control of its own pension provision and costs. To what extent can the institution influence the pension benefits it provides, or influence the cost – or apparent cost – of the various pension arrangements in which it participates? The table below looks, at a very high level, at the governance features of some of the current arrangements.

	Control	Mutuality
USS	Little influence for individual institutions. The nominated employer and trade union representatives can influence to a limited extent. Funded by Scheme contributions. The only scheme available for all academics (and related staff) in participating Institutions. Optional for other staff as determined by Institution. Elected representative body can influence benefit changes but ‘complex’ governance framework. Established under a Trust.	Full cross subsidies – common contribution rates across all institutions (including the impact of early retirement) after age 60.
LGPS	No influence for individual employer. Funded by Scheme contributions which depend on historic scheme experience and advice of actuary. Benefits set by Government Regulations. Institutions participate in over 50 financially independent regional LGPS schemes run by County/Unitary Councils.	Limited cross subsidies – contribution rates broadly sets to reflect each employer’s experience (eg pay increases, retirements) and membership profile. It is proposed to introduce tiered member contribution rates.
TPS	Not funded. Benefits paid directly by Government. Government sets contribution rate and decides on benefits following consultation.	Cross subsidies. Government sets one contribution rate to apply to all. Case for differential employer contribution rates examined in the past but differences were then found to be marginal.
Saul	Multi-employer, funded scheme, for colleges and others linked to the University of London.	Common employer contribution rates (but early retirement actuarial costs are allocated to individual employers).
NHS	Not funded. Benefits paid directly by Government. Government decides benefits and contributions.	Common employer contribution rates. It is proposed to introduce tiered member contribution rates.
Own ‘in-house’	Individual institutions can influence decisions on benefits, on pace of funding and investment strategy. Need to work in partnership with Scheme Trustees who are generally a mixture of member and employer elected. Funded by contributions from employers and members, under a trust agreement. In theory each Institution has control over benefits provided and eligibility. In practice most tend to ‘mirror’ USS provisions with minor ‘tweaks’.	No cross subsidies – each institution bears cost of own Scheme.

The Costs of Pension

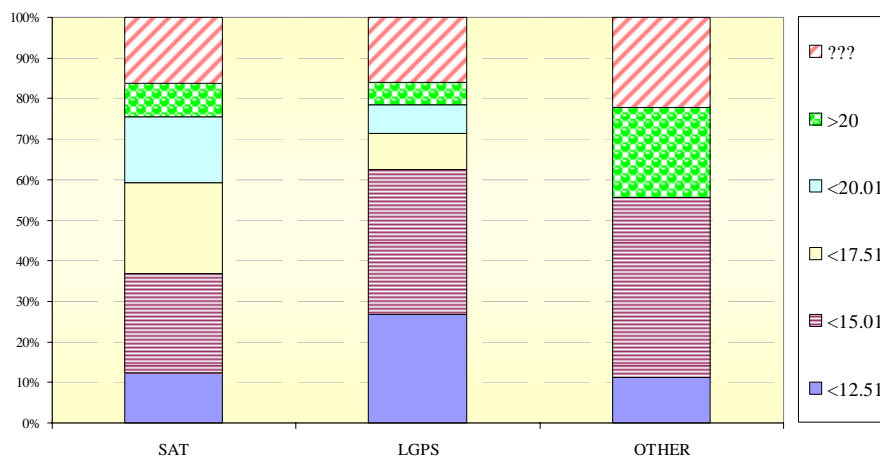
Employer Contributions Rates

Employers in the HE sector pay different amounts to their current pension arrangements. Rates for the major schemes are as follows:

- USS: 14% of pay.
- TPS: 14.1% of pay from 1 January 2007 (previously 13.5% and due to be capped at 14% of pay from 2008).
- STSS: 13.5% of pay from 1 April 2007 (previously 12.5%).
- NHSPS: 14% of pay.

Rates for the other schemes vary as follows:

Contribution rates across Scheme types



Source: Michael Bourn, 20 Questions Paper

SAT (Self Administered Trust)

Pension Costs

The key points about current employer contribution rates are as follows:

- Additional contributions are typically being paid into local (SAT) schemes to fund deficits.
- Increases in rates are expected/being phased in across most schemes. There is increasing cost pressure across all schemes, but this is more immediate and apparent for in-house schemes (SAT). The balance of employer: employee contributions is moving out from its historic average of 2:1 to 2.5:1 or more.
- There are variable scheme funding levels. However using FRS 17 (the accounting measure) the combined pension deficit across the HE sector is estimated around £5bn.

In accounting for their pension costs, institutions' contributions to TPS and NHSPS are accounted for on an "as paid" basis. By contrast, deficits on SAT schemes appear on the balance sheet of the institution and so may impact on banking covenants, borrowing ability etc. There is little doubt that the accounting treatment of defined benefit pension deficits – with their full disclosure on the face of company accounts – has been a major factor leading to the demise of these plans.

Costs of Provision

It might be thought to be a simple matter to answer the question "how much does a pension cost". The answer is far from simple. One of the key reasons for this is that the cost can be affected by how fast the investments that back the pensions promise grow – or are assumed to grow. The greater the growth in assets, then the lower the amount needed today to pay a future commitment such as a pension.

Economists might argue that the true economic cost of a pension should be assessed by using the returns on very low risk investments – i.e. assets such as long term government bonds. In practice, pension schemes invest in assets intended to give higher returns than this, but this carries with it greater risk. There are no assets backing the unfunded schemes, but a "notional" asset or interest rate is often assumed.

HE Pension Costs

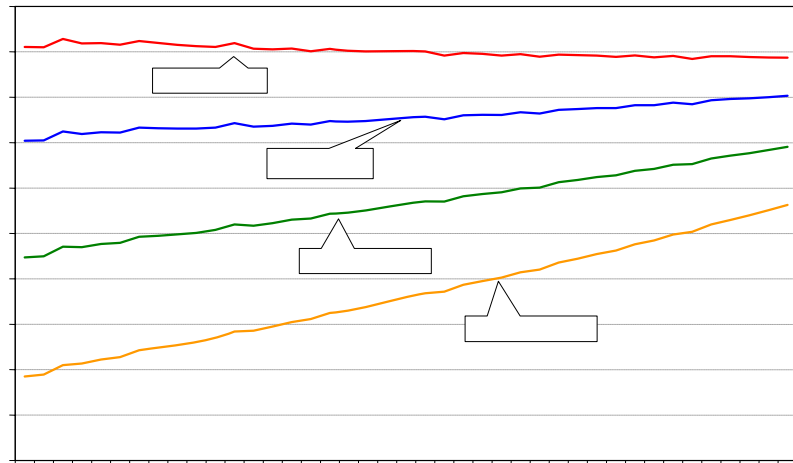
The interaction between anticipated future returns and pension cost in the HE sector is illustrated vividly in the charts below. In each case we show the cost of providing a pension of $1/80^{\text{th}}$ of final pay and $3/80^{\text{th}}$ cash for males who will retire at age 65, based on a common benefit structure. The cost is expressed as a percentage of pay. Costs increase with age since there is less of a period for an older person to benefit from future investment returns.

The lines on the chart show the cost according to the following patterns of assumed rates of investment return (net of inflation):

- 3.5% p.a. (e.g. the Teachers Pension Scheme)
- 2.5% p.a. (e.g. a typical Local Government scheme)
- 1.75% p.a. (e.g. the typical guidelines for private sector schemes)

We have also shown, for comparison, the "economic cost" of the benefits (based on an assumption of investment in government stocks, assumed to return 1.25% p.a. more than inflation).

Pension costs and assumed returns



Source: Hewitt Associates

The point about this chart is that the apparent cost of a pension promise can vary materially according to the level of future investment returns assumed in funding the benefit. This does not mean that the actual cost will be equal to the assumed cost. The disclosed cost may not be a reliable guide to the true cost. Or equivalently a more generous pension benefit can appear to be cheaper than another, lower scale of benefit, simply because of the approach chosen to fund the benefits.

Cost differences by member

Even if we put aside factors such as the investment return issue above, the cost of Final Salary benefits varies by an individual's circumstances. This is illustrated by the chart below, which compares the average cost of benefits for three sample individuals with different career paths. Whilst institutions might pay a single, 'standard' contribution rate, these cross subsidies do exist due to different membership profiles etc.

- Member A receives "regular" pay increases and remains in service to age 65.
- Member B receives two significant promotions and then retires early on an undiscounted pension at age 60.
- Member C receives modest pay rises and then leaves service (and the scheme) at age 40.

Cost of benefit accrual



Source: Hewitt Associates

Other costs subsidies

Within a typical final salary scheme there are many other cross subsidies or examples where individuals within a common scheme (and for whom the employer may, for convenience, pay a common contribution rate) fare better than others:

- those with high pay rises do better than those with moderate pay rises.
- married members do better than single members.
- those who retire early, on preferential terms, do better than those who retire at normal retirement age.
- a member who chooses to join late in career incurs a higher cost to the scheme per quantum of pension benefit than an earlier joiner, due to shorter investment period.

Pension Changes

A Pensions crisis?

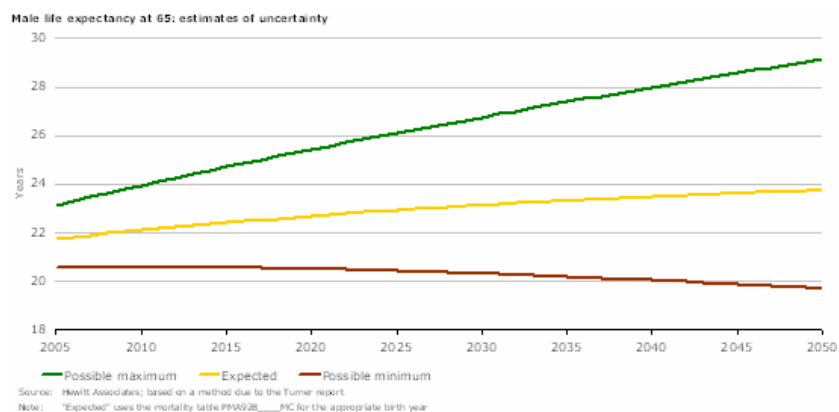
- Many factors are contributing to the so-called ‘pensions crisis’ in the UK, chief among them being significant increases in life expectancy and falling real investment yields which increase the cost of purchasing annuities, and stock market falls eroding the value of the assets held to back the liabilities.
- The combined impact has been to increase deficits in UK pension schemes substantially. The introduction of The Pensions Regulator (TPR) in the UK, together with new funding legislation giving greater power to Trustees of occupational schemes has added to the pressure.
- It could be argued that some of these features are “real” whereas others represent a change in the accounting mechanisms for pensions. Equally it is true to say that accounting changes have led to real benefit changes, as companies have had to face increasing scrutiny from shareholders and analysts about how they are dealing with their (apparently) ever increasing deficits.

Drivers of change

Increases in pension costs have been the key issue leading to wholesale changes in private sector pension arrangements in the UK. Cost increases can arise from a variety of factors, including:

- Lower interest rates and low investment returns.
- Pensioners living longer. It is an acknowledged fact that pensioners are now living longer than previous generations, and longer than most previous pension funding patterns assumed. What is less clear cut is just how fast or for how long the improvement in longevity will continue. See the chart below, taken from the Turner Commission Report.
- Tax burden – the removal of tax reclaim on UK dividend payments.
- Compliance costs and other administrative overheads, such as Pension Protection Fund levies.

The Uncertainty of Future Longevity



Source: The Turner Commission

Private sector changes

Changes to private sector arrangements have been substantial and include the following:

- **Benefit Changes**, including closure to new entrants, changing to career average plans, cash balance plans or most typically to defined contribution plans, as well as removal of favourable early retirement terms or freezing of pensionable pay.
- **Contribution Changes**, including increased member contributions, multiple benefit scales (eg a lower benefit scale for members who do not wish to increase their costs) formal cost sharing arrangements, 'smart' pensions (where NI is saved, as recently proposed for USS) or putting pensions into flexible benefits packages.
- **Funding Changes**, most notably special (company) contributions, or higher deficit contributions, companies looking to borrow to fund deficits, or the use of contingent assets and parent company guarantees.
- **Investment Changes**, which often means more bonds and fewer equities, but can also include alternative assets, risk budgeting and Liability Driven Investment (LDI).

Public sector changes

The public sector is not immune from these pressures. Reviews of public sector arrangements such as PCSPS and LGPS have attracted a lot of press coverage. With many institutions in the HE sector currently to participating in sector-wide arrangements (such as TPS, LGPS and USS) will pension changes be forced on institutions for some, but not all, of their staff? Where does that leave institutions' own schemes? Against this background, the HE sector is changing, with perhaps a greater focus than ever before on its public/private status. Some of the major changes to public sector schemes are set out below.

LGPS

For full details, please refer to UCEA Update 06/143. The government is currently consulting on a final salary scheme effective from April 2008 as follows:

- a final salary scheme with a pension age of 65 for existing and new members based on 1/60th of final salary for each year of pensionable service with option to commute up to 25% of pension fund to cash; service up to April 2008 under the current 1/80th scheme will be protected for existing members;
 - phased retirement facility to draw pension while continuing in work;
 - two-tier employee contribution rates: 5.5% on the first £12,000 and 7.5% on the excess over £12,000 (estimated average rate of 6.3%);
 - a facility to purchase up to a maximum £5,000 of additional annual pension;
 - earnings cap already removed from 1 April 2006;
 - three-tier ill health benefits related to capacity to work;
 - the cost of future actuarial increases will be shared equally between employer and employee contribution rates.
-

TPS

For full details, please refer to UCEA Update 06/146. The new TPS is a final salary scheme effective from 1 January 2007 and includes:

- the existing TPS continues for current members at 31 December 2006 with pension age 60 and pension calculated on 1/80s with lump sum;
 - a new TPS for new starters from January 2007, with a pension age of 65 and pension calculated on 1/60s with the option of up to 25% of pension fund as cash;
 - phased retirement facility to draw pension while continuing in work;
 - the employer contribution rate increases to 14.1% and the employee contribution rate to 6.4%;
 - a facility to purchase up to a maximum £5,000 of additional annual pension;
 - earnings cap remains;
 - two-tier ill-health pension related to capacity to work;
 - the cost of future actuarial increases will be shared equally between employer and employee contribution rates with a maximum 14% employer contribution rate from 2008.
-

NHSPS

For full details, please refer to UCEA Update 06/123. The Government has not yet issued a response to consultation on changes. They include a final salary scheme from April 2008 as follows:

- existing scheme continues for current members with pension age 60 (in some cases 55) and pension calculated on 1/80s with lump sum with a one-off choice to transfer to the new scheme;
- a new scheme for new staff with a pension age of 65 and pension calculated on 1/60s with the option of up to 25% of pension fund as cash;
- a facility to purchase up to a maximum £5,000 of additional annual pension;
- four-tier employee contribution rate related to pay: 5% up to £15,107; 6.5% £15,107-£60,880; 7.5% £60,880 to £100,000; 8.5% above £100,000;
- Employers will continue to contribute 14% (2/3rds of the overall cost);
- practitioners (GPs and dentists) will have a career average (CARE) pension scheme with accrual rate of 1.4% and a 4.2% lump sum for existing members and 1.87%, revalued by RPI plus 1.5% for new members;
- earnings cap will be removed at April 2008.

Civil Service

A new pension arrangement is being introduced for new joiners from 1 July 2007.

- The new arrangement will provide CARE benefits, with pensions linked to price inflation prior to retirement.
- Members will have a choice of when to draw pension, with actuarial adjustments applied based on a normal retirement age of 65.
- The Care pension will accrue initially at the rate of 2.3% of salary per year of service.
- Members will pay 3.5% and have the option to buy additional pension.
- Cost pressures will be shared between the employers and the members, with employers paying no more than 20% of pay. Cost pressures may result in higher member contributions or, alternatively, lower benefits and/or a higher pension age.
- Existing members keep a final salary scheme and normal pension age of 60.

Point and Counterpoint

Introduction

The 'Point' and 'Counterpoint' grid consists of a series of propositions and the contrary propositions about pension provision in the HE sector. Each institution is invited to indicate the extent to which it agrees or disagrees with the proposition. To further clarify the propositions some explanation is set out below.

Examples

In order to illustrate some of the issues, a number of example benefit scales or cost figures are indicated. It should be stressed that these are purely for illustration and should not be taken as proposals for future benefit changes in the sector. At this stage there are no such proposals developed by Universities UK for any changes, and there is no commitment as to the legal, technical or financial feasibility of any option.

Sample

A sample of the grid is set out below.

The screenshot shows the 'Hewitt Surveys: POINT | COUNTERPOINT' interface. It includes a header with the survey title, a user greeting 'Hello Richard 9', and the survey title 'Higher education sector - pension benefits review'. Below this is an introductory paragraph explaining the survey's purpose and instructions. A table of survey questions is displayed, with columns for 'the point', 'more like which?', and 'the counterpoint'. Each question has a corresponding grid for selection and a 'click to add comments' button.

the point	more like which?	the counterpoint
All institutions in the HE sector should have the same pension arrangement		All institutions in the HE sector need not have the same pension arrangement
Staff should have a menu of pensions options to choose from rather than a single take-it-or-leave-it package		Staff should not have a menu of pensions options to choose from
Employers should have a menu of pension options to offer to their staff		Employers should be free to offer what pensions they want

Question 1: Uniformity of the Sector

Under the 'Point' position, the pensions offered by all institutions in the HE sector would be the same – for example final salary schemes paying a pension from age 65. Under the 'Counterpoint' the type of pension provision offered by each institution could vary, according to what it felt was relevant to its circumstances. So this might include a particular institution deciding they wished to offer say a Stakeholder pension, or a career average pension or a choice of pensions. Under the 'Point' position this would not be allowed and there would be uniformity across the sector.

**Question 2:
Individual Choice?**

Should individuals have a choice of pensions? The ‘Counterpoint’ position says there should only be one scale and type of benefit for everybody – for example this could be a 1/60th final salary pension which costs employees 6% of pay. The ‘Point’ position says that even within a uniform system there could be a choice for members. Members might then decide to chose from a ‘menu’:

- 1/60th Final salary from 60 – cost to member 10% of pay
- 1/80th CARE from 65 – cost to member 4% of pay

Once again we need to stress that this is only one illustration of possible future outcomes, and does not constitute a proposal at this stage.

**Question 3:
Menu or A La Carte?**

Under the Point position there would be a limited range of pension options available across the sector. So this limited menu might include:

- 1/60th final salary from age 60
- 1/50th CARE from age 65
- 6% defined contribution plan

and so forth. One could envisage a choice of up to a dozen “approved” types of plan design. Each institution could then decide which options from the menu to offer to its staff.

The Counterpoint says there is no material advantage in restricting choice in this fashion, and that individual institutions should be able to design whatever types of plan they feel they need.

**Question 4:
Cooperation or
competition?**

This question looks at whether institutions should be prepared to adopt a common approach or whether they should be able to adjust the pension packages (subject to employment and pensions law requirements) to suit their specific funding circumstances. Under the ‘Point’ position all institutions would have the same pension cost, for example expressed as a percentage of payroll. (To the extent that institutions’ staff structure, age profile etc differs, the ‘Point’ position would imply some degree of cross subsidy between institutions.) Under the ‘Counterpoint’ institutions would be able to adjust the type of packages or methods of funding which suits them most. This would imply attribution of actual costs to each institution, ie no cross subsidy. The ‘Counterpoint’ would have greater clarity of individual accountability but might result in higher costs.

**Question 5:
Central or local
negotiation?**

Under the 'Point' position the HE sector would negotiate on funding and benefit issues with central government and consult with the trade unions/staff side on benefits as a single group in respect of any pension changes. This will mean compromises will be necessary that may not suit individual institutions in order to get to an agreed position.

Under the 'Counterpoint' it will be left to each individual institution to decide and negotiate on any pension changes. This will lead to a lack of uniformity in the system but may lead individual institutions to have greater control over their pension cost.

**Question 6:
Economies of scale**

The 'Point' position says that the sector should look to exploit its collective buying power and should pursue the greatest administrative economies of scale in offering pensions benefits. The logical conclusion of the 'Point' argument would be a single central point of provision of all benefits for the sector. Administrative costs, including increasing legislative costs can be a particular burden for smaller in house schemes.

The 'Counterpoint' says that individual institutions should be free to pursue their own policies of providing benefits, if they feel this delivers greater overall cost control. The administrative economies could include the terms on which any new arrangements are provided or how the existing schemes are funded.

**Question 7: Cross
subsidies**

The 'Point' position recognises that there are cross subsidies between different institutions but that these cross subsidies are acceptable.

The 'Counterpoint' suggests that there should be no cross subsidies. Cross subsidies arise from a variety of sources. So for example under USS an institution which regularly gives higher pay rises than the average, or which allows greater numbers of its members to retire on with unreduced benefits after age 60 will be a "winner", given that a common contribution rate is paid by all employees.

Under the 'Counterpoint' there will be a need to isolate the actuarial cost to the scheme of each institution's pension provision - which in an extreme case would mean separate funding arrangements. Intermediate positions might seek to identify the biggest or most variable sources of cross subsidies and to make explicit charges for them, for employers participating in a centralised scheme.

Question 8: Treating Staff Equally

The 'Point' position says that the same broad value of pension arrangements should be offered to all employees.

This is not the case at present and a number of institutions offer different arrangements to their non-academic staff from those offered to academic staff.

The 'Counterpoint' position says that this differential position is acceptable. Having the same pension system does not necessarily mean that the same pension would be provided to all. For example it could be possible to offer a range of choices for employees but the level of choice could differ between academic and non-academic staff. This question seeks to answer the question as to whether you believe that any such differentials are valid.

One reason why different choice or different pension provision might be made is because the requirements for and sources of different types of employee varies.

Question 9: Targeting

All pension schemes distribute the available spend in a variety of ways; some members of the scheme will "cost" more than other members, even though the employer may pay a uniform contribution rate for all. The current system could be characterised as benefiting longer serving employees, those who gain higher than average pay rises (but also short-service staff joining late in career), and those who retire early (see the diagram and discussion on page 12).

Under the 'Counterpoint' position, pension benefit should be distributed more uniformly. The ultimate reflection of this would be in a Defined Contribution scheme where everybody receives benefits equal to e.g. 10% of pay. A corollary of this system is that the eventual pension will be proportionately less for people with the characteristics noted above!

Other pension types will distribute resources in a less extreme fashion - but all designs will favour some groups of individuals.

Question 10: Pensions or not?

Under the 'Point' position your institution is saying that you favour providing a package of pension benefits, broadly at the current level of cost to the institution.

Under the 'Counterpoint' your institution would want to have the ability to offer lower pension benefits for example but to compensate employees elsewhere in their reward package (or conceivably *vice versa*). In an extreme case an institution might decide that it doesn't want to provide pensions to some or all of its employees but would prefer to pay higher cash (having due regard to the pay spine where relevant). Examples of this are already found in the private sector.

Question 11: Pensions paternalism

Under the 'Point' position the institutions are taking a degree of responsibility for ensuring sensible pension provision for their employees. If an employee chooses to reject the provision offered then no cash alternative would be available.

Under the 'Counterpoint' position, employees would be given a choice as to whether to take the pension provision or receive a realistic cash alternative. This might suit individuals who did not need or do not want pension provision for whatever reason – because they have their own arrangements that are more than substantial, or even at the other end of the scale because they believe that additional saving for retirement would be offset by means tested benefits.

Under the 'Counterpoint' individuals could make this choice but under the 'Point' position this is made for them by the employer.

Question 12: The cost of pensions

The 'Point' position says that your institution can broadly survive with the current level of pension costs.

The 'Counterpoint' says that pension costs are acceptable providing that there are no increases beyond the current level.

Note that costs can be high because of the continuing scale of benefits or because of the need to finance past service shortfalls. In this question we are looking at the combined effect of these two features as they impact on the amounts paid by your institution.

Question 13: Member contributions

Under the 'Point' position member contributions towards the cost of benefits would remain fixed at broadly their current levels e.g. 6.35% of pay for members of USS.

The 'Counterpoint' position argues that if the cost of benefits increases e.g. as a result of greater longevity - then member contributions should be increased accordingly. These increases could be expressed as a constant fraction of the total additional cost e.g. 1/3 members and 2/3 institutions or they could be simply adjusted in some ad hoc fashion from time to time. The 'Counterpoint' may also include a view that members should pay more to keep the current arrangements.

Question 14: Risk sharing

Under the current system, all of the inherent risks associated with pension provision fall to the institutions. So if for example investment returns prove to be less favourable than expected this will be reflected in a deficit which will require increased funding from the institutions. Similarly if actuarial predictions of pensioners' survival rates are exceeded, the employer will have to increase its funding.

The 'Point' position says that the institutions accept this position. The 'Counterpoint' says that employees should bear all of the consequences of unpredicted future events. The purest form of this would be a defined contribution arrangement under which the amount of the member's pension depends on investment returns and annuity rates and the level of pay rises experienced and dates of contributions (reflecting salary history) made by the member and employer.

It should be noted that these are the two extremes and that other pension arrangements are becoming more widespread which share or divide the risks more evenly between institutions and employees.

Question 15: The Degree of Change

The Point Position argues that the current arrangements are broadly satisfactory, and that only relatively minor 'tweaks' are needed to benefits or the financing and governance arrangements. The Counterpoint argues that more fundamental changes are needed to the style, structure, costs and financing of pensions in the HE sector.

Question 16: Staff understanding

The 'Point' position says that staff have a good understanding of the way the current schemes operate and the level of pension benefits they might expect.

The 'Counterpoint' says that staff have a poor understanding of current schemes and cannot readily plan for their retirement.

The understanding of the schemes can also relate to the implications of e.g. transfers or changes of status or changes in hours such as phasing of hours closer to retirement.

Question 17: Staff appreciation

The 'Point' position here says that staff have a good appreciation of the financial value of pension benefits. They recognise how much it costs their employer to provide the benefits they receive, and would be prepared to reflect this in negotiations about pay and conditions, for example.

The 'Counterpoint' says that staff have a poor appreciation of the economic value of their pension benefits. They would not accept a lower pay offer, for example, to reflect an increase in the cost of employer pension provision.

Question 18: Cost of early retirement

There is a growing recognition that there is a significant cost to early retirement that needs to be met either by additional contributions or benefit reduction. The ‘Point’ position says that each institution should pay its own direct costs of early retirement – by way of special contributions at the point the member retires or by a higher long term funding rate.

The ‘Counterpoint’ position says that institutions should share the cost of early retirements as part of an overall sector wide funding arrangement. This would lead to cross subsidies and “winners” and losers” in terms of institutions having more or less early retirements. Intermediate solutions are possible, such as the changes recently introduced by USS where costs over a certain age (60) are shared but those under this age are allocated to the specific institution.

Question 19: Traditional or new employment models

The ‘Point’ position says that pensions should be structured around the employment models that have been traditional in the HE sector. It could be argued that the current, predominantly final salary, pension schemes were designed to meet a particular employment model which could be characterised as being long serving with relatively regular pay reviews.

The ‘Counterpoint’ position says that this employment model is now irrelevant, and that pensions should reflect the greater diversity of employment models that now exist.

Question 20: Benchmarking

The ‘Point’ position says that in looking at pension benefits or potential changes in benefits, the HE sector should be looking to benchmark its provision against pensions provided in the broader public sector.

The ‘Counterpoint’ says that increasingly the HE sector should look to the private sector to benchmark pension and other employee benefits.

The difference between these two can be quite stark since pension benefits in the private sector have been substantially revised and changed over the last 5 – 10 years. It is now relatively uncommon in the private sector for a new employee to offered final salary type pensions and alternative types of pension provision such as career average or defined contribution benefits are now the norm. To date the public sector has chosen predominantly defined benefits arrangements such as final salary or indexed career average benefits.

Appendix A: Pensions Terminology

Accrued Pension	The pension earned in a Defined Benefits pension scheme up to a particular point in time. Usually calculated by reference to a defined formula and based on service up to and salary as at, the date in question.
CARE	Career Average Revalued Earnings. Similar to Career Average pension scheme except the accrued pension in any particular year is then revalued from the year of accrual to retirement, death or leaving pensionable service using an appropriate index (usually linked to inflation).
Career Average	A type of Defined Benefit pension scheme in which the accrued pension is calculated for each year of pensionable service based on pensionable earnings in that year.
Cash Balance	A type of Defined Benefit pension scheme that maintains individual employee accounts like a Defined Contribution scheme. A percentage of salary is allocated to the account each year, and the account assets grow at a guaranteed rate to provide retirement benefits.
Defined Benefits (DB)	A type of pension scheme in which the scheme rules define the benefits to be paid on retirement, death or leaving pensionable service. The benefits are not directly related to contributions paid to the plan or investment returns on the contributions.
Defined Contributions (DC)	A type of pension scheme in which the benefits for any individual member at retirement depend on the amount contributed to the plan and the investment returns on the contributions. This usually involves individual accounts and the purchase of annuities on retirement.
Final Pensionable Salary	The earnings on which the benefits are based in a Final Salary pension scheme. The scheme rules will describe the calculation of these earnings. The calculation may be based on pensionable salary in the year prior to retirement, death or leaving pensionable service, or it may be based on pensionable salary over several years prior to retirement, death or leaving pensionable service.

Flexible benefits	An arrangement where employees are able to choose how they receive their remuneration from their employer (usually with some restrictions). For example they may be able to elect to receive more holiday in return for reduced cash pay.
HE Sector	The Higher Education sector.
LGPS	Local Government Pension Scheme.
Liability Driven Investment	The term “Liability Driven Investment” can be understood as simply matching assets to liabilities, but can be defined as any approach that uses a scheme’s liabilities as a starting point for setting investment strategy. The idea is to reduce risk by managing investments in a way that focuses on the liabilities, rather than a general investment index.
PCSPS	The Principal Civil Service Pensions Scheme, the primary pensions vehicle for career civil servants.
PPF	Pension Protection Fund – an umbrella scheme established by the government to pay compensation to members of eligible defined benefit pension schemes when the sponsoring employer becomes insolvent.
Real Returns	The actual return on an investment after removing the effects of inflation i.e. the return achieved above inflation.
SAUL	Superannuation Arrangements of the University of London
Smart Pensions	A pension scheme in which employees do not make any contributions to the pension scheme, but receive a salary reduced by an amount equivalent to their pension contributions, thereby reducing NI contributions payable (by both employee and employer).
The Pension Regulator (TPR)	The regulator of work-based pension schemes in the UK. The objectives of TPR are; to protect the benefits of members of work-based pension schemes; to reduce the risk of situations arising that may lead to claims for compensation from the PPF; and to promote good administration of pension schemes.
TPS	Teachers’ Pension Scheme.
USS	Universities Superannuation Scheme.