JNC benefit proposals: Member Impact Analysis – updated November 2023

Introduction

This paper provides information on the member impacts of the proposed benefit changes employers have consulted on with members. It is based on presenting a limited number of illustrative member scenarios, as well as available information and commentary on how impacts could differ between groups. The proposal includes the following changes to future accrual of benefits from April 2024:

- An increase in the salary threshold to £66,400[1]
- An increase in the accrual rate from 1/85ths to 1/75ths (with 3/75ths lump sum)
- Revaluation and indexation of benefits - including those accrued between April 2022 and April 2024 - based on CPI, soft-capped at 5%

Other elements would remain unchanged, including:

- 20% contributions to members' DC accounts over the salary threshold
- Ancillary benefits (although these are impacted by changes in the future accrual parameters)

All figures are presented in real terms and are based on default assumptions that will be used in the member consultation modeller except where noted. We have included the full assumptions for completeness at Appendix A.

Note on the purpose of this analysis:

The USS Executive has prepared this member impact analysis to support the JNC and the USS Trustee Board in considering these proposals and exercising their duties under the scheme rules. It explores the potential impacts of the proposals above on the pensions outcomes of members in different circumstances, as well as providing information on the impacts on different equalities groups[1]. It is based only on information about members and opt outs that the Trustee holds, is intended to provide illustrative input only and should be used for this purpose only. It does not represent either legal or actuarial advice. The Trustee's internal function and its external advisers are advisers to the Trustee and are unable to provide advice to the JNC or the

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[1] Note that since this analysis was conducted - the level of the salary threshold has since been confirmed to be £70,296 from 1 April 2024. This will increase the DB benefits and decrease the DC benefits for Example member F but is not material to the analysis.

[1] Neither the JNC nor USSL are public authorities subject to Public Sector Equalities Duties, but this information was provided on request to inform their decision-making processes.

stakeholders. The comments and information in this member impact assessment are provided for information only and the parties should take their own legal and actuarial advice on any issues raised. The Trustee does not accept any liability if this member impact analysis is used for an alternative purpose from that which is intended, nor to any third party in respect of this report.

Member impact examples

Table 1 shows the range of example members that were discussed at the JNC's benefit design subgroup. The intention is not to show a full 'global' analysis of how the overall membership would be affected by the proposed benefit changes, but to demonstrate how the changes impact on members in different circumstances, such as age, salary and previous benefit accrual. A heat map showing the full distribution of USS members by age and salary is included in Appendix A.

Table 1: Example members

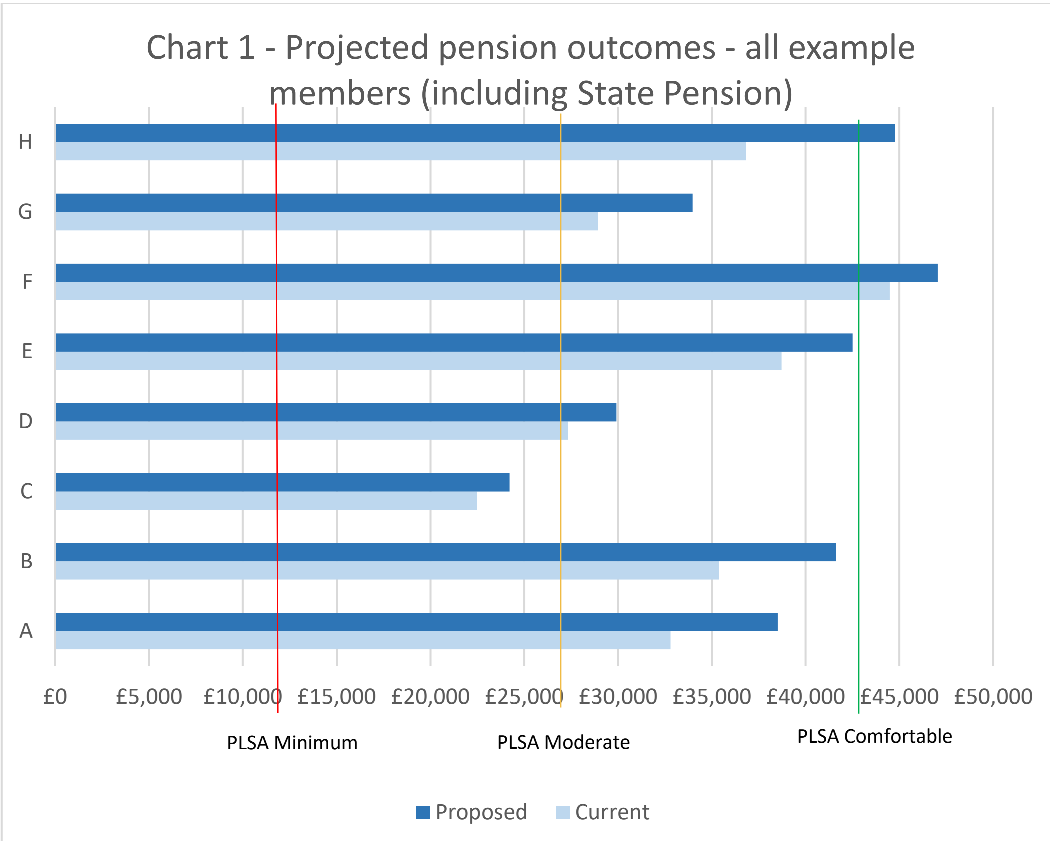
Member	Age	Salary	Assumed Tenure (yrs)	Accrued DB pension (income)	Accrued DC pension (pot)
A	30	£40000	5	£2,500	0
B	35	£50000	7	£4,000	£2,000
C	40	£25000	8	£2,500	0
D	45	£40000	10	£5,000	0
E	50	£65000	20	£13,500	£10,000
F	55	£85000	25	£19,500	£30,000
G	25	£32000	0	0	0
H	25	£32000*	0	0	0

*Member H has a higher assumed salary growth (CPI+3%), with the goal of illustrating how the changes could impact on a new starter advancing through a lifetime career in the HE sector.

To model the impacts, USS has used an Excel version of the consultation modeller that has been tested internally in preparation for the member consultation launch. However, there are some differences in presentation, as for comparative purposes we have converted all benefits to a retirement income.

Overall impacts

Chart 1 and Table 2 show the headline results for all example members retiring at age 66.



The bars show the projected pension at retirement under the current benefit structure and then under the JNC proposal. Included on the charts are the levels of income required to meet the Pensions and Lifetime Association (PLSA) Retirement Living Standards for a single person, living outside of London, at the *minimum, moderate* and *comfortable* expenditure levels[2]. Note – all outcomes in the chart include a full State Pension, which is currently worth £10,600/year from age 66 and can be expected to form an important part of many members' retirement income. The State Pension is excluded from Table 2 below, to focus on the impact on USS benefits only.

[2] The PLSA Living Standards have been developed within the pensions industry to give a rough guide as to how retirement incomes translate into a broad standard of living. The figures presented are for those living as a single person outside of London. The Living Standards for those living inside London are higher, at £32,000 (moderate) £48,000 (comfortable) per annum. Conversely, couples need less income per person than individuals.
Both the incomes shown and the levels of the PLSA living standards are shown gross of tax.

Table 2: Headline results: Detail

	Characteristics		*Current benefits*			*Proposed Benefits*			*Difference*	
Member	**Age**	**Salary**	**DB**	**DC**	**Current**	**DB**	**DC**	**Proposed**	**Total**	**FS only**
A	30	40000	£18,920	£3,270	£22,190	£27,910	£0	£27,910	+26%	+29%
B	35	50000	£18,810	£5,960	£24,770	£30,700	£310	£31,010	+25%	+31%
C	40	25000	£11,870	£0	£11,870	£13,620	£0	£13,620	+15%	+19%
D	45	40000	£15,870	£850	£16,730	£19,310	£0	£19,310	+15%	+23%
E	50	65000	£23,650	£4,470	£28,120	£30,520	£1,380	£31,900	+13%	+32%
F	55	85000	£28,360	£5,520	£33,880	£32,820	£3,610	£36,440	+8%	+26%
G	25	32000	£17,020	£1,310	£18,320	£23,380	£0	£23,380	+28%	+28%
H	25	32000	£17,490	£8,750	£26,230	£31,980	£2,190	£34,170	+30%	+30%

Notes

Columns 4-6 show the projected outcomes under a continuation of the current (since April 2022) benefit structure.
Columns 7-9 show the projected outcome under the JNC proposal.
Columns 10 and 11 show the projected increase in total USS benefits at retirement, including their total benefits and for future service only

Table 2 shows the impacts on DC, DB and total benefits for the example members. All members are projected to see significant increases in their overall retirement income. These increases range from +8% to +30% and looking at future service only they range from +19% to +31%. It is important to note that these are not maximum and minimum impacts, as other examples and assumptions could give larger or small increases.

Looking at DB and DC benefits individually, there are significant increases in DB benefits for all example members. Member B, who is younger and is immediately affected by all of the proposed changes, sees their DB income at retirement increase from £18,810 to £30,700 (+63%). Member C is older and only affected by the changes to revaluation and accrual and sees their DB income at retirement increase from £11,870 to £13,620 (+15%).

Many members will see a reduction or removal of projected DC benefits. Members A, D and G are projected to no longer cross the salary threshold at any point and Member H, whose salary increases at a faster rate, sees their DC benefits reduce from £8,750 to £2,190.

Actual impacts will depend on a number of factors, including how the Investment Builder (DC) funds perform. Whilst the increase in accrual rates and the reinstatement of the pre-1 April 2022 soft cap on revaluation are unambiguously positive for all members, there is a possibility that the increase in the salary cap may result in a member getting lower benefits, if they achieved significantly higher levels of investment returns than we have assumed. Beyond the assumptions made, the relative qualities and risks associated with DB and DC benefits have not been considered here.

Participation impacts

The JNC also asked the Trustee if an assessment could be made on the impact of the changes, including the proposed reduction in member contributions, on scheme participation. In 2022/23, 16% of scheme joiners opted out, including 20% of new joiners only (excluding those who are past members and re-joining). Whilst USS does not hold data on the number of employees in the HE sector who are eligible for USS membership but aren't active members, in 2021, based on information from some larger employers, we estimated it could be around 20,000 at any point in time.

It is not possible to reliably predict the impacts on participation – the experience of automatic enrolment in the UK has shown how inertia, rather than cost, is the most important driver of pensions participation, and the next automatic enrolment window in larger employers is not due until spring/summer 2025. However, survey research carried out on behalf of the JNC in January 2022 suggested that

- Around half of non-members cited affordability as a key reason for not participating
- Certain groups, including women, part time workers and lower earners were more likely to cite affordability
- 70% of those who gave a figure said that they could afford a contribution rate of 5% or higher (if salary sacrifice is used, a 6.1% contribution would result in take home pay reductions of 4.1%).

Inertia will likely prevent a large short-term behavioural response to the changes, but there is potential for employers to make these non-members aware of the change, immediately and in the run up to the automatic re-enrolment window in 2025.

Equalities impacts

As shown in the previous section. all members are expected to have increased benefits following the changes, but there may be variation in the size of the impacts. Analysing and identifying these different effects does not itself suggest they would constitute illegal discrimination for a number of reasons, not least because we consider comparisons across time in a way that does not apply for the legislative discrimination comparisons.

The changes would not affect any member differently based directly on characteristics relevant for equalities analysis. However, to help the JNC and the Trustee board with exercising their duties under the scheme rules we can identify potentially different impacts that are indirectly related to some relevant characteristics.

1. **Increase in accrual rates from 1/85 to 1/75**

   Age: All other things being equal, younger members would benefit more from the increase in accrual rates, as they have lower past benefits (which are unaffected) and they also have longer until retirement to benefit from the higher accrual rate.

2. **Reinstatement of the soft cap on revaluation and pension increases**

   Age: All other things being equal, younger members would benefit more from the reinstatement of the soft cap, as the benefits they accrue would have had longer subject to the hard cap, and therefore would be at greater risk of losing value relative to inflation.

3. **Increase in the salary threshold**

   Age: The relative impact of the salary threshold on members would not be as clearly directional. To the extent that younger members have lower accrued entitlements and longer until retirement, they will see greater relative increases in DB benefits. However, any DC savings they build have longer to grow, so could be expected to be of higher value than an older member. This means the loss of DC contributions in relation to the increased amount of salary threshold might be considered to be a greater risk of disadvantage to those younger members.

   To illustrate, we can consider a 30 year old and a 55 year old member earning £51,004. They will both receive £2,000 in Investment Builder contributions this year. Based on our SMPI assumption of CPI+3% investment returns, by retirement this could be worth £5,800 for the 30 year old, but only £2,750 for the 55 year old – less than half.

Income: All other things being equal, higher income members could benefit from the increase in the salary threshold more than lower income members. A member earning £60,000 will see their annual DB accrual increase from £482 to £800 (+66%), whereas a member earning £40,000 will see their annual DB accrual increase from £471 to £533 (+13% due to the accrual rate only). Some of this difference will be offset by a reduction in DC benefits, the effect of which as mentioned above, will differ by age. There is no greater proportionate effect for earners earning beyond the new salary threshold, so there is a ceiling on this higher earner differential.

Age and income combined: Differences in impact depend on a combination of both age and income. A younger, higher earning member will see a bigger increase in DB benefits, but a potentially greater loss in DC benefits. An older, lower earning member will see a smaller increase in DB benefits, but a lower/zero loss in DC benefits. These offsetting impacts make it difficult to clearly identify any group that benefits more, or less, from the proposals.

Quantifying equalities impacts

It is very challenging to quantify the potential impacts identified above, and as agreed by the JNC we have not undertaken a global analysis of all our members. However, at this stage, we have looked at the distribution of USS active members where we hold the data (age, salary and gender), and made some observations. The first tables below show which members are affected by the salary threshold change, because they earn over the current salary threshold.

Table 3: Proportion of members affected by salary threshold change by age & gender

	% affected by salary threshold		
	% of Males	**% of Females**	**% of All**
20-24	2%	1%	2%
25-29	12%	11%	11%
30-34	38%	33%	35%
35-39	63%	50%	56%
40-44	75%	58%	66%
45-49	79%	63%	70%
50-54	80%	65%	72%
55-59	80%	63%	72%
60-65	76%	57%	67%

Note – data extracted from Hartlink as of 31.03.2023. Excludes 2111 member records where salary is unknown

Table 3 shows that younger members are less likely to be affected by the salary threshold change – only 35% of members aged 30-34 will be affected initially, although they could be affected in the future if their salary increases faster than inflation. Younger women are least likely to be affected, and women overall are less likely to be affected than men.

Table 4 goes further showing the immediate increase in annual DB accrual by gender. Male members are more likely to have higher increases, also reflecting their higher salaries and therefore larger impact of the threshold change. Males will on average also see correspondingly larger reductions in DC benefits.

Table 4 – Increase in DB benefit accrual

Increase in DB accrual	**Female**	**Male**	**All**
0-25%	60%	46%	53%
25-50%	16 %	16%	16%
50-75%	11%	15%	13%
75-100%	13%	24%	18%

Note – data extracted from Hartlink as of 31.03.2023. Excludes 2111 member records where salary is unknown. Totals may not sum due to rounding.

USS does not currently hold data that would allow us to look at potential impacts on other equalities groups, but we could look to build on this analysis with other sources of insight should the JNC wish to explore these further.

Appendix A – Example member heat map

See separate file

Appendix B - Assumptions

The model used to produce these projections is an excel version of the member consultation modeller, using all of the same assumptions, but converting all benefits to income to simplify comparison.

- CPI Inflation – 2.5% (consistent with Statutory Money Purchase Illustrations (SMPI).
- Standard pay growth – CPI+1%.
- Salary Threshold increases in line with CPI, including the revaluation adjustment set out below.
- Investment Returns are those used for 2023 SMPI, assuming members are invested in the USS Default Lifestyle Options.
- Investment management costs are not included.
- The retirement age for all examples is 66 – late retirement factors are applied to any benefit tranches pre-2020, but this affects both benefit structures equally
- All USS benefits are converted to income at retirement.
- DB lump sums are converted using the pre-April 22 reverse commutation factor for a 66-year-old (4.03%).
- DC benefits are converted to income using an assumed withdrawal rate of 3.5% per annum.
- Whilst CPI Inflation is set at the 2.5% hard cap, we have included a revaluation adjustment that assumes that on average the excess of CPI over the hard cap is 0.5% per annum. There is no adjustment under the soft cap.
- The state pension increases in line with prices in the future.
- No other pensions provision is included.

<u>Note on the difference between the consultation modeller and these results</u>

As the intention is to look at comparisons of overall pensions outcomes, this analysis assumes all USS benefits are converted into income with the methods above. The modeller being made available to members is aimed at helping them understand their own situation and therefore generates a retirement outcome with a tax-free lump sum made up of a combination of DB and DC benefits, akin to how the retirement process presents benefit options. Therefore, despite using the same assumptions and calculations, these results will not be directly comparable.