



DWP DC Reform Policy Team  
Department for Work and Pensions

Your ref  
Our ref      CY/JMR  
Date         14 January 2025

By email to: [quarryhouse.pensionsinvestmentreviewdcreforms@dwp.gov.uk](mailto:quarryhouse.pensionsinvestmentreviewdcreforms@dwp.gov.uk)

Dear DWP DC Reform Policy Team

**USS response: Pensions Investment Review: Unlocking the UK pensions market for growth**

I am writing in response to your consultation on proposed changes to the DC occupational pensions market, and in particular the proposals it contains to increase scale and drive improved investment practices. Whilst we understand the rationale for these proposals, we believe that applying them to USS will have the reverse impact to that intended.

***About USS***

Universities Superannuation Scheme (USS) was established in 1974 as the principal pension scheme for universities and higher education institutions in the UK. We work with around 330 employers to help build a secure financial future for over 550,000 members and their families. We are one of the largest pension schemes in the UK, with total assets of around £78bn (on 31 March 2024). USS has a wholly owned subsidiary, USS Investment Management (USSIM), which acts as primary investment manager for the scheme, which is its sole client.

USS is authorised as a master trust by the Pensions Regulator and is therefore in scope of these proposals. However, it currently provides active members with a combination of DB benefits (for earnings up to a salary threshold of around £70,000) and DC benefits (for earnings above this level and for any additional contributions or transfers in). From a member's perspective, these hybrid benefits jointly form their USS retirement pension. As of 31 March 2024, around 185,000 of our 554,000 members have some DC benefits in the scheme (all have DB), and DC benefits make up around £3bn of our £78bn assets. In addition to retirement benefits, USS provides members with death in service and incapacity cover.

USS offers a single default fund to members, which is designed to reflect the hybrid nature of the USS benefits and is "life-styled" using 3 multi-asset building block funds and a liquidity fund. All USS Trustee assets – both DB and DC and provisions for death and incapacity benefits - are held in a single trust and the majority of the costs of administering the scheme (including investment management) are met from the Trust funds, rather than charged to individual members and employers.

***Effective scale to drive positive outcomes for members and the UK.***

We understand the drive for scale in DC provision. The impacts of scale are more complex than simply "bigger is better", but we believe USS is an example of how large asset owners are generally able to

**UNIVERSITIES SUPERANNUATION SCHEME LTD**

"USS" and the USS logo are both trademarks of Universities Superannuation Scheme Limited. All rights reserved.

Head Office: Royal Liver Building, Liverpool L3 1PY Tel: +44 (0)151 227 4711 Local: 0845 068 1110 Fax: +44 (0)151 236 3173 Website: [www.uss.co.uk](http://www.uss.co.uk)

Registered in England & Wales No. 1167127 Registered Office: Royal Liver Building, Liverpool L3 1PY Regulated by The Pensions Regulator

deliver greater professionalism in governance and in-house investment capabilities including long term planning, responsible investment and integration of private markets, all focused ultimately on producing the best value for members.

However, based on the current USS design, our DC default arrangement will not exceed £25bn by 2030 and is unlikely to in the medium term. We strongly believe that applying this policy to an active, open, hybrid scheme like USS is inappropriate and would result in material detriment to our members and employers. The remainder of this letter sets out our reasons and supporting evidence, as an answer to Q7 of the consultation. We offer answers to some of the other consultation questions, as well as some extra information on how USS invests, in the Appendices.

## 1. A hybrid scheme, for the higher education sector

USS was established by the higher education sector to allow for the pooling of assets, sharing of risks and easy movement of staff between employers. Although USS is an authorised master trust, it is not a DC-only scheme - the large majority of benefits presently being built up by members (and an even larger proportion of our assets) are DB. The fundamental design of the scheme benefits is decided by the sector via a Joint Negotiating Committee, which is made up of employer and union representatives and an independent chair. This means that employers and members do not face the same choices about their pension provision as in the broader DC market this consultation addresses.

From our employers' perspective there is no alternative hybrid pension provider and even if there were, there are practical restrictions on leaving the scheme, including a moratorium on exits and s75 debts to be paid.

From our members' perspective, the DC element is specifically designed to be part of their hybrid benefits. The default fund strategy, including the decumulation pathway, reflects that most members will have a significant DB pension and can take their benefits combined at retirement to increase their tax free lump sum. Communications and support are also designed around the hybrid structure, including the member portal, annual statements, benefit calculators and at-retirement guidance services.

Requiring USS to consolidate its DC provision into another DC provider would result in *deconsolidation* of their pension overall, leaving them with multiple active pensions to manage. This would lead to an inferior savings and retirement journey, while increasing the administrative burden on our employers.

## 2. Effective scale to deliver good investment outcomes

The USS default arrangement (or fund) is very unlikely to reach the minimum scale requirements proposed, even if they were reduced from the £25bn proposed. However, USS is already a very large *asset owner*, and is organised in a way to ensure that the DC element can leverage this scale effectively in selecting and managing the assets where members' investments are held.

At the core of the approach is an in-house investment capability provided by USSIM, shared across both DB and DC parts of the scheme. This model results in the following benefits to members:

- **Scale to invest in private markets:** Members have access to a diversified default arrangement, managed by an in-house investment capability that is shared across both DB and DC elements. At the total scheme level, this includes access to a private markets programme of £25bn as at 31 March 2024 (45% of which invested in the UK), including £8.1bn in infrastructure. The DC part alone invested £503m (17% of its total assets) in private markets as at 31 March 2024 with two thirds of this (>10% of total assets) invested in the UK.

- **Value and suitability for members:** The DC part is based on a flexible operational model that allows it to innovate across several aspects of the investment offering, which is developed in a bespoke way to fit USS's members' requirements. This includes the above inclusion of private markets, but also offering investment options catering to members' ethical preferences and introducing a foreign exchange overlay. The shared in-house investment capabilities allow USS to leverage its total scale and offer these to members at a competitive price point, resulting in a high-quality offering at a low cost.
- **Enhanced governance:** The same Trustee body oversees both the DB and DC parts of the Scheme, which ensures the same set of Investment Beliefs and investment policies (as set out in the Scheme's [Statement of Investment Principles](#)) are used in the design, management and oversight of the respective investment strategies. This results in a better understanding from the members as to how their investments are managed and the Trustee's position on matters such as how financially material environmental, social and governance factors are considered. The Trustee is also able to have a holistic view of the members' benefits which is incorporated in all DC investment arrangement suitability analysis.

We have included more detail about the way USS invests in Appendix B.

Crucially, USS is operating this way today and, we do not see many other providers offering members the same access to illiquid investments at this point. If these measures forced USS to consolidate our members funds into a larger DC default, this would likely result in lower investment in productive assets - including UK illiquid assets – both now and in the future.

#### ***Exempting hybrid schemes offering value for money***

We understand that you will want to limit exemptions to ensure that you achieve the overall objectives across the DC market. But we are very concerned about the impact on our members and employers. With that in mind we believe that providers who are authorised master trusts but a) provide members with ongoing accrual of hybrid benefits; and b) meet other DC regulatory requirements such as providing value for money, should be exempted from these scale requirements. We would like to work with your officials to develop appropriate exemptions that could facilitate ongoing hybrid and sector-specific schemes whilst maintaining the focus on driving scale in the DC default system.

While this exemption is the critical issue for us, we have offered some limited feedback on other questions in the annex to this letter, as well as answers to Chapter 5 for your market analysis (see Appendix A). Specifically with regards to our private markets investing experience, we note that our team has previously met with officials to discuss our investing model and its benefits. We would be happy to expand these discussions if helpful.

I hope the above is helpful as you continue to consider these proposals.

Yours sincerely

Carol Young  
Group Chief Executive Officer

**Appendix A: Responses to other questions**

**Question 1: Do you think that providers should be restricted to a limited number of default funds, and if not why? Please consider any equality considerations, conditions and to what extent saver choice could be impacted.**

We can understand the attraction to restricting the number of distinct default funds, as having large numbers of defaults increases costs and reduces focus on the governance of each. However, there are many circumstances where employers or trustees have information about the population they serve that gives them valid reasons to tailor default products, particularly where this may target a specific decumulation pathway. In practice, we expect providers offering more than one default fund would be using a limited combination of 'building block' funds, so facilitating effective scale in asset allocation in the same way as if they offered a single default.

**Question 29: Do you think establishing a named executive with responsibility for retirement outcomes of staff could shift from the focus on cost and improve the quality of employer decision-making on pensions?**

This provision would need to reflect that in some pension arrangements, such as USS, employers act collectively. Whilst employers will take an interest and make representations to their provider, they do not have the same degree of individual choice or control as individual employers who choose a Master Trust or contract-based arrangement.

**Question 33: How many AE workplace default arrangements and default funds do you have?**

USS provides one default arrangement, which is lifestyled using four building block funds.

**Question 34: What is the total AUM you have across all these AE workplace default arrangements and default funds?**

£3bn as at March 2024

**Question 35: Do you have a small number (for example 3-5) of AE workplace default arrangements/funds that cover the majority of these assets and if so, how many of these are there?**

USS has a single default arrangement, which is lifestyled using four building block funds.

**Question 36: Have you previously combined default funds or arrangements together within the same organisation?**

No.

**If 'no', do you have an estimate of how much you think this might cost (overall or on a per pot basis)?**

We do not have an estimate.

**Question 37: Have you previously consolidated Single Employer Trust assets into a MT or GPP?**

No.

---

## **Appendix B: USS investment approach**

### **Overall benefits to members from a shared investment capability**

Members' DC investments are managed by USSIM using the same principles and investment philosophy as the DB assets. This delivers several benefits to the members:

- **Funds with competitive charges and access to an employer subsidy:** The hybrid scheme structure allows the Higher Education Sector to have greater visibility, oversight and input into the pension scheme model. The collaboration between the Joint Negotiating Committee (which brings together representatives from USS members and USS employers) and the Scheme has enabled most DC investment and administration charges to be fully subsidised by higher education employers, increasing net returns for members. This is made possible by the bespoke design and delivery of the DC model, which ensures that all investment options available to members are built at a charge of no more than 30bps per annum. This model would be challenging to replicate with other commercial master trusts, where the Joint Negotiating Committee would have less visibility on cost structures and a lower ability to influence the evolution of the cost and charges.
- **Scale:** Managing DB and DC assets in the same Trust enables members to benefit from the combined scale of the total assets. Providing value for members is always considered when selecting investments for the DC part and, where deemed to be in members' best interest, DB and DC jointly invest in the same structures. This is the case for most of DC's assets, including its climate tilted public equity mandate, as well as the private markets mandates. This has enabled the DC Growth Fund (the multi-asset fund used by members more than 10 years from their Target Retirement Age) to allocate 25% to private markets within the 30bps per annum Investment Management Charge for the Fund.
- **Shared governance:** The same Trustee body oversees both the DB and DC parts of the Scheme, which ensures the same set of Investment Beliefs and investment policies (as set out in the Scheme's Statement of Investment Principles) are used in the design, management and oversight of the respective investment strategies. This is expected to result in a better understanding from the members as to how their investments are managed as well as the Trustee's position on financially material ESG matters.
- **Ongoing suitability:** Governing members' DB and DC benefits under the same Trust allows the Trustee to have a holistic view of members' USS's benefits when designing the investment product and engagement strategies. Suitability reviews of the investment strategy took place swiftly after changes to benefit design in 2020 and 2024 affected the role of DC for our members' retirement outcomes. A joined up view of how the DB and DC benefits will grow over time, the impact on members' accumulated pots at retirement and how they are behaving when accessing their benefits allows the Trustee to build an in-depth knowledge of members' profiles and their needs when accessing retirement, and thus creating the most suitable investment strategy to cater for those.
- **Innovation:** By accessing wider USS's resources and scale, the DC part has been able to innovate across several areas of the product offering. Such examples are the inclusion of private market assets in January 2020; the advances made in the product space such as offering a lifestyled investment approach that is structured around members' ethical preferences; and the introduction of a foreign exchange overlay in the lifestyle funds which seeks to improve overall portfolio risk management.

- Open Architecture and operational efficiency:** The direct custodial model with Northern Trust allows for a great degree of flexibility when implementing the investment strategy. This means USS does not use an intermediated insurance platform model, which is often associated with additional operational challenges and constraints. The introduction and ongoing management of private markets has also been achieved in an efficient way, with USS having visibility on the valuation and pricing risks involved. Our open architecture enables our continuous innovation, with a recent example being the inclusion of fee-free co-investments in private equity to the DC default growth funds.

**Investing in Private Markets**

As articulated in the Trustee’s Investment Beliefs, private markets provide investment opportunities and structures not available in Public Markets. Managing the DB and DC assets in the same Trust has enabled the DC part to include a significant allocation to private markets within its lifestyle funds (both the Default Lifestyle Option funds and the self-select Ethical Lifestyle Option).

As at 31 March 2024, USS held:

- £25.9bn AUM in private markets
- £8.1bn in infrastructure
- 45% of investments in the UK

The DC part started accessing private markets in 2020, and as at 31 March 2024 it held:

- £503m AUM in private markets (20% allocation in the DC USS Growth Fund)
- £253m in infrastructure
- 67% of investments in the UK

The current USS Growth Fund strategic asset allocation is shown below.

