USSEmployers

THE USS 2020 VALUATION

Higher education finances: a briefing for employers

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SUMMARY OF FINANCIAL POSITION OF UNIVERSITIES

- The higher education system has weathered the Covid pandemic better than expected.

- This has relied on the hard work of university leadership teams working together with staff to manage a very difficult and changing set of circumstances, but also on pay and hiring freezes, postponing investment, and deferring repair and maintenance – these are short-term, emergency financial stabilisation measures, none of which is sustainable longer term.

- The budget position for universities is likely to become significantly more challenging over the next 2–3 years.

- Employers (and employees) will be paying an additional 1.25% National Insurance contribution from April 2022, equivalent to £131 million across the sector.

- The most difficult challenge is the growing mismatch between student fees and costs. Funding per student has fallen steadily in real terms over the last six years – 17% in England (13% in Scotland since 2014–15, where it is primarily grant funding rather than student fees) and this will be eroded further as inflation climbs higher.

- University planning is hampered by continuing doubt over future levels of funding, with the UK government considering a review panel recommendation for a reduction in tuition fee levels – with the 'best case' expectation being a continued freeze of tuition fee levels, meaning a further fall in real terms value. There are also risks of student number control measures such as minimum entry requirements and restrictions on foundation years funding.

- There is ongoing uncertainty over the rate at which international student demand will recover, given the continuing challenges of the pandemic and the potential impact on post-pandemic behaviours. Those universities that can't increase the proportion of higher-paying international students will be particularly badly affected by the continued domestic tuition fees freeze.

- Many universities have delivered significant efficiencies during 2020–21 to offset the impact of the pandemic and will take several years to recover to pre-Covid financial size.

- Employer contributions across all of the main higher education pension schemes have been facing unprecedented increases for a number of years. These scheme cost increases mean that the financial consequences of this important part of the employment package could be significant.

- Surpluses and deficits reported in university accounts are affected by non-cash accounting adjustments for pensions valuations and other factors that can disguise true operating performance.

SUMMARY OF USS PENSIONS

- The Universities Superannuation Scheme (USS) is a multi-employer scheme consisting of large and smaller higher education institutions and small research-based charities, with widely varying financial positions and abilities to pay into the scheme.

- All 340 USS employers must contribute 21.4% of salary for each scheme member, regardless of their own financial status.

- There has been a 50% increase in the employer contribution rate over the last 12 years, which has already forced employers within the scheme to cut budgets and caused job losses. In 2009 the employer contribution to USS was 14% of salary.

- Each additional 1% employer contribution to USS equates to around an extra £90 million per year, which is equivalent to employing approximately 2,000 individual members of staff in USS institutions.

- New stringent covenant support measures put forward by USS employers to sustain the Defined Benefits part of the scheme – worth an additional £1.3 billion a year in total – place constraints on the ability of institutions to borrow money.

- USS sponsoring employers have provided a clear message that the current contribution rates are at the limits of both affordability and sustainability – and to pay any more to USS pensions now will have significant impact across the sector on its collective ability to continue to deliver global leading higher education.

FURTHER INFORMATION

GENERAL FINANCIAL POSITION OF HIGHER EDUCATION

A recent Office for Students (OfS) report shows that, despite student recruitment proving more resilient than feared, income overall fell in 2020–21 and net liquidity (the cash universities hold net of their liabilities) continues to decrease.

Net operating cashflow, necessary to support future investment and longer-term sustainability, fell from 8.4% of total income in 2019–20 to 4.2% in 2020–21. The OfS report says that this level appears to be manageable in the short term but will not support sustainability in the longer term.

WIDE RANGE OF FINANCIAL POSITIONS ACROSS SECTOR

The Covid pandemic caused serious financial difficulties for the higher education sector. Universities needed investment from government to protect the student interest, to maintain research capacity, and to ensure that universities are able to play a central role in the UK's economic and social recovery following the crisis. Many universities only weathered covid financial pressures because of short-term cost control – pausing recruitment and major capital development – all of which will have an impact on students and research if continued.

Changes to blended working and learning practices implemented to improve safety and flexibility will require substantial upfront investment (IT, training, estates), and will not lead to the immediate costs-savings, as might be assumed. A survey of institutions by Universities UK found that 98% of respondents have or expect to have committed all additional OfS hardship funds by the 31 March 2021 spending deadline and that the vast majority needed to supplement rising hardship requests with additional contributions from university funds. If we see Covid restrictions affect students again (eg part-time job losses, increased caring needs, worsening family circumstances) we can expect hardship requests to rise again.

REAL TERMS FALL IN TUITION FEES AND TEACHING FUNDING

An increase in recruitment for domestic students does not mean universities have additional funds, as teaching of domestic students is delivered at a (small) deficit. An OfS report finds that the unit of resource for home and EU students studying in England has been decreasing steadily since 2015–16. £9,250 fixed in 2012–13 is worth about £7,500 today in real terms, due to the impact of inflation. This means that, after adjusting for inflation, universities have 17% less resource per student fee now than a decade ago.

Scottish Government funding for university teaching has declined by 13% since 2014–15, to the extent that each undergraduate now has £869 less spent on their education each year compared to 2014–15.

Annual inflation rate in the UK jumped to 5.1% in November 2021, its highest level since December of 2011, and is forecast to peak above 6% in April 2022, which is placing greater financial pressure on institutions.

Over recent years, the value of public support for teaching at English providers has not kept pace with inflation or increases in student numbers, with recurrent teaching funding falling from £1,290 million in 2018–19 to £1,266 million in 2021–22.

The recent changes in how the OfS allocates public funding has left some providers facing reductions in recurrent funding of over 70% for 2021–22 when compared with the previous year.

CONTINUED UNCERTAINTY OVER FUTURE FUNDING

The UK government is considering a reduction in tuition fees in England and other policy measures – foundation degree funding cuts and minimum entry requirements – which would restrict student numbers and harm the income flow for universities. The ongoing uncertainty over future income levels makes planning and increasing investment in any areas very difficult for universities.

USS IS A MULTI-EMPLOYER SCHEME

There are 340 employers within USS, ranging from the largest pre-1992 Russell Group institutions through to small charities with a few employees. All employers pay in the same amount – 21.4% of salary for each employee in the scheme – a rate which is 50% higher than twelve years ago. Many of these institutions are charities and have a totally different funding model to higher education. Affordability is key to both employers and employees. The ODI, a global think tank working to inspire people to act on injustice and inequality, offers USS pensions to its staff and reports that: "the escalating contribution rate to the pension scheme is having real impact on our business model in terms of affordability".

UUK, as the employer representative, has consulted employers throughout the valuation process and the clear message is that the current contribution rates are at the limit of sustainability.

USS employers have also agreed to provide an unprecedented level of additional support measures to the scheme, known as covenant support, which the USS Trustee values at around £1.3 billion per year. However, these measures could limit employers' ability to borrow money in the future and/or lead to higher borrowing costs, and be a barrier to improving courses, facilities, and services to students and staff. It will likely be the financially weaker employers that will be most severely impacted, since they rely on secured borrowing the most, and this could feed immediately through to cost-cutting. Despite this, employers consider this extra covenant support necessary to continue to provide attractive future benefits which contain an element of both Defined Benefit and Defined Contribution pension saving.

THE COST OF HIGHER PENSION CONTRIBUTIONS

The active pensionable payroll of USS members as at 31 March 2020 was £8.962 billion per annum. The total monetary contribution to pensions by USS employers is therefore currently £1.89 billion per annum, meaning each additional 1% contribution to USS equates to around an extra £90 million per annum, equivalent to the cost of employing approximately 2,000 individual members in USS institutions (based on an active membership of 200,355 and average USS member salary levels, as detailed in the rule 76 report presented by USS to the Joint Negotiating Committee).

UNIVERSITY ACCOUNTS INFORMATION

It is difficult to draw reliable conclusions on the financial health of the university sector from surpluses published in university accounts because the required accounting treatment for pension liabilities can cause large movements in reported surplus and deficit levels between years, making it difficult to assess the underlying financial performance. Pension liabilities reflect future commitments to pay down the deficit in the USS, the main pension scheme for the sector, over many years and do not reflect the cash or day-to-day spending position of universities.

The USS deficit was halved in the most recent completed valuation (£7.5 billion in 2017 valuation, to £3.6 billion in 2018 valuation) which means that university accounts reflect the lower level of future commitments to pay down the pension scheme deficit and the effect will be that many universities will move toward reporting an accounting surplus. This will be reversed once the 2020 valuation is concluded with a much higher deficit (£14.1 billion) reported by the USS Trustee, which is responsible for the scheme, and likely to result in many more universities reporting accounting deficits.

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