Accounting tricks and pension deficits

We have been told that the Universities Superannuation Scheme's deficit has grown so large in the past year as to threaten its survival ("Deficit puts pension scheme in jeopardy", News, 13 September). Its funding level plummeted to 77 per cent in the year to March 2012, but we have been given no satisfactory explanation why. There are grounds for believing that the figures do not reflect fair value accounting.

The deficit is the difference between assets (USS investments) and liabilities (future and present pensions). The former have increased by £1.5 billion, so the explanation is not poor investment performance. The problem is that liabilities have ballooned by £8.4 billion in just one year. This is all the more astonishing since the rule changes that were introduced last October ought to have reduced liabilities, not increased them: the introduction of the career average section, increasing the pension age to 65, flexible retirement, and so on.

The reason for the increase is that the figure is artificial and misleading due to the way it is calculated under legislative rules, introduced in the Pensions Act 2004, that now apply to all private sector defined-benefit pension schemes (including USS). It is worked out as a present value capital sum using a discount rate based on gilt rates that are currently very low, hence the large figure. The actual liabilities are the same as they were before.

It is worth reminding ourselves how a private pension scheme works: a group of employers and workers pay contributions into a collective fund, from which pensions are paid to retirees under defined rules and surplus funds invested to earn dividends and interest for the future. It should be judged simply on whether its income exceeds expenditure on a sustainable basis, taking account of foreseeable changes.

From this point of view the USS is not in bad shape. The latest published accounts show that annual investment returns (including dividends from investments in highly profitable companies such as Vodafone, plus government bonds) were about £2.4 billion, easily footing the current bill. On top of that, rising contribution income from members and employers brought in another £1.5 billion a year.

The same bogus calculation that makes the USS seem to be in trouble has led to yawning deficits in many company pension schemes. In August, the Office for National Statistics reported the combined deficit on this basis was £280 billion, which has led to calls for emergency extra funding from employers. The artificiality of all this has led bodies such as the National Association of Pension Funds to call on the government to change the rules.

The emerging fiasco in private pension schemes is the result of the overeager application of neoliberal economic thinking during the boom years. What is happening to USS and the other final-salary pension schemes is the logical culmination of a process based on the philosophy that "there is no such thing as society, only individuals and their families".

We must defend the USS for the success it is and campaign for the government to return to fair value accounting.

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● *For the full version of this letter, see http://tinyurl.com/92lk3nn*