USSEmployers

2018 valuation webinar Q&A – February 2019

The following questions and answers are drawn from two webinars on the 2018 USS valuation hosted by Universities UK (UUK), which provided further information on the 2018 technical provisions consultation, and examined the 'contingent support' required by the USS Trustee to back the additional risk associated with the lower overall contributions deemed possible by the Joint Expert Panel (JEP). They accompany the webinar slides which are available on the USS Employers website.

For further assistance in answering questions about the 2018 valuation process, please contact pensions@universitiesuk.ac.uk.

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1. What is the likelihood of employers and members facing the higher contributions from October 2019, because the 2018 valuation cannot be concluded in time?
2. What does USS mean by a 'rebate' on contributions in its framework for contingent support?
3. Why are rule amendments needed to introduce cost sharing of any contingent contributions – and what are the implications?
4. My employer offered its support for the JEP recommendations on the basis that 20.1% was the absolute limit for employer contributions. It now seems that there are a number of scenarios in which contributions could go higher (a mid-bookend outcome, and not avoiding the October 2019 increases). How is this being taken into account?
5. Can you recap why the deficit recovery contributions for both the 2017 valuation and the 2018 valuation are 5% of salary, when the proposed deficits are very different?
6. Would contingent contributions under cost sharing require an employer consultation with staff?
7. When will the next valuation take place? March 2020 or March 2021?
8. Will phase two of the JEP lead to any meaningful change in the valuation methodology, or will accepting contingent support set a precedent?
9. What work is being done to mitigate the massive 31 July increase in the institutions' balance sheet pension provision related to the deficit recovery contributions change?
10. Will phase two of the JEP have anything to say on USS's rejection of the specific proposals made in the panel's first report?

11. What discussions are taking place with UCU on cost sharing of contingent contributions?

12. Might different Brexit scenarios and potential economic impacts influence contingent contributions proposals/triggers? And if so, in what ways?

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1. What is the likelihood of employers and members facing the higher contributions from October 2019, because the 2018 valuation cannot be concluded in time?

The latest information shared with employers by the USS Trustee indicates that the timeline to completing the valuation by its 30 June deadline is tight, and made even more challenging by the rule changes that UUK believes are needed to implement the contingent contribution arrangements required by the Trustee.

The prospect that October 2019's increases may come in to effect therefore cannot be ruled out, although there are areas where time could be saved. For example, if there is a will from both employers and members, there may be no need for the Joint Negotiating Committee (JNC) to use all of its allotted time to consider the outcome of the valuation.

It is UUK's hope that by October 2019 an agreeable outcome to the 2018 valuation will be within reach, so that the increases, should they come into effect, would only apply for a very short period.

2. What does USS mean by a 'rebate' on contributions in its framework for contingent support?

As detailed in its 2018 technical provisions consultation document, the USS Trustee has calculated that contributions of 33.7% are required to fund benefits at their current level, and with the level of risk they deem appropriate.

However, in its recently published framework for a contingent support arrangement, the Trustee has confirmed it is willing to offer employers a rebate on the required contributions, which could take the future cost to below 30% of salary if contingent contributions can be agreed. A contingent contribution arrangement will allow the USS Trustee to take more risk in the valuation assumptions, with a 'safety net' of contingent contributions being payable should the scheme funding level deteriorate. It is an important principle of USS that contributions are split 65:35 between employers and scheme members, and UUK believes this principle should extend to any contingent contribution arrangement, so that employers and members both benefit from the rebate through lower contribution levels.

3. Why are rule amendments needed to introduce cost sharing of any contingent contributions – and what are the implications?

As contingent contributions will be a new feature of the scheme, UUK understands it will be necessary to make rule changes to accommodate them, regardless of the specific features of the proposal. Again, UUK believes the contingent contributions should be cost shared to ensure both members and employers can benefit from the rebate the USS Trustee is offering in return.

Rule changes will impact the chances of submitting the valuation by its statutory deadline of June 30, and in turn of avoiding the October 2019 increases, as the JNC must consent to any rule amendments.

4. My employer offered its support for the JEP recommendations on the basis that 20.1% was the absolute limit for employer contributions. It now seems that there are a number of scenarios in which contributions could go higher (a mid-bookend outcome, and not avoiding the October 2019 increases). How is this being taken into account?

There are indeed possible scenarios where employer contributions may exceed 20.1% of salary (and where member contributions would be much higher too), not least if the October 2019 increases cannot be avoided.

The second phase of the JEP will look at the longer-term structure of the scheme – potentially including flexibility over contributions – so while the higher contributions under these scenarios may be unsustainable for some employers (and members), these concerns will be considered by both the JEP and the usual stakeholder forums ahead of the next scheme valuation.

5. Can you recap why the deficit recovery contributions for both the 2017 valuation and the 2018 valuation are 5% of salary, when the proposed deficits are very different?

According to the USS Trustee, the level of deficit recovery contributions (DRCs) remains high in relation to the deficit because of the risk associated with short-term reliance on the employer covenant. There is further information on this on page 4 of USS' framework for contingent contributions document.

UUK has asked the USS Trustee to clarify and better explain its rationale for proposing DRCs at this level.

6. Would contingent contributions under cost sharing require an employer consultation with staff?

Yes, a contingent contributions arrangement with cost sharing will require a 60-day consultation with scheme members. It is expected that this consultation would begin at the outset of any such agreed arrangement.

7. When will the next valuation will take place? March 2020 or March 2021?

In its consultation material the USS Trustee set out that the next valuation is scheduled for March 2021. However, if funding conditions deteriorate in the meantime, the USS Trustee does have powers under the scheme rules to call an earlier valuation.

8. Will phase two of the JEP lead to any meaningful change in the valuation methodology, or will accepting contingent support set a precedent?

It is not envisaged that contingent support will become a recurrent component of every valuation, but much will depend on how the current proposal for contingent contributions is adopted into the scheme rules, and indeed, how it is received by stakeholders.

The second phase of the panel's work will review the governance and valuation process of USS, including the valuation of technical provisions and other aspects of the methodology. Once the panel has published its report the scheme stakeholders will consider how best to adopt its recommendations.

9. What work is being done to mitigate the massive 31 July increase in the institutions' balance sheet pension provision related to the deficit recovery contributions change?

UUK has asked the USS Trustee to provide more information to employers in support of the accounting aspects of the valuation. Concluding the 2018 valuation with a better outcome ahead of 31 July remains a priority, although this will be difficult given the time constraints noted above.

10. Will phase two of the JEP have anything to say on USS's rejection of the specific proposals made in the panel's first report?

The panel will likely comment on USS's reaction to their first report.

USS has accepted the JEP recommendations which, in their view, don't increase the risk in the scheme (updated mortality and updated realised investment returns), and will consider adopting additional recommendations subject to an agreed proposal for contingent support.

11. What discussions are taking place with UCU on cost sharing of contingent contributions?

Discussions with UCU are taking place through the JNC in relation to cost sharing ('rebate sharing' in USS' terminology) of any contingent contributions. It is important to note that these discussions remain theoretical at this stage, as employers are currently being consulted on their support for contingent contributions (having previously confirmed a willingness to take greater levels of risk).

12. Might different Brexit scenarios and potential economic impacts influence contingent contributions proposals/triggers? And if so, in what ways?

Yes. Big economic shocks that aren't already priced into markets could make the scheme's funding position worse, and therefore increase the likelihood of contingent contributions being triggered. UUK is engaging with the Trustee to model the likelihood of contingent contributions being triggered under a range of economic scenarios, examples of which can be found in the contingent contributions proposal developed by UUK's actuarial adviser, Aon.