

To: Vice-Chancellors/Heads of USS Institutions
CC: Finance Directors, Official contacts

Our ref: I.887/BG/MB/ES
22 July 2019

Dear Colleague

Consultation on changes to the USS Statement of Investment Principles

I am writing to you to begin a formal consultation on the revised Statement of Investment Principles ('SIP'), which the Trustee (Universities Superannuation Scheme Limited or 'USSL') has prepared following the completion of the 31 March 2017 Actuarial Valuation. This letter summarises the context and details of the changes made, and a copy of the SIP is attached. If you wish to provide a response to the consultation, please do so by emailing SIPConsultation@uss.co.uk no later than 4 September 2019.

Under the Pensions Act 1995, as amended by the Pensions Act 2004, and other relevant regulations, the Trustee is required to prepare and maintain a written SIP governing decisions about investments for the purposes of the Universities Superannuation Scheme ('USS' or the 'Scheme'). This SIP can only be finalised by the Trustee following consultation with the sponsoring employers.

Timing of this SIP consultation

This consultation on the SIP comes at a time when we have finalised the 31 March 2017 Actuarial Valuation, and are in the process of discussing (and have consulted upon) an Actuarial Valuation as at 31 March 2018. Whilst the principles and beliefs that underpin the Trustee Board's investment strategy and approach to investing remain largely consistent, this Statement of Investment Principles has been reviewed in light of the finalised 31 March 2017 Actuarial Valuation and the latest discussions on the 31 March 2018 Actuarial Valuation. Upon completion of the 31 March 2018 Actuarial Valuation, the Trustee will review the Statement of Investment Principles again, and if necessary, consult on any changes that might be required to reflect the outcomes from that valuation process.

Changes proposed to the SIP

The SIP was last updated in 2016 following the 31 March 2014 Actuarial Valuation and in advance of the launch of the USS Investment Builder ('**Defined Contribution section**' or '**DC Section**') under the Scheme that year. As the Scheme's benefit structure has not changed considerably since this time, much of the information contained within the SIP remains appropriate. However, reviewing the document afresh, the Trustee believes that the document could benefit from simplification. As such, with the assistance of its legal and investment advisers, the Trustee has re-structured its SIP to follow the Pensions Regulator's guidance on such documents and simplified much of the content. Where the Trustee has separate policies on matters (such as its Responsible Investment statement), the high level principles are contained within the SIP with a reference to where the Trustee provides access to its full detailed policies on its website.

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Other than to review and simplify it, the greatest change to the SIP is the expansion of the aspects relating to the Trustee's policies on responsible investment and engagement and the Trustee's arrangements with its investment managers in this area (items 1.4 and 1.5 in the proposed SIP). Whilst the Trustee has had publicly available policies and statements in this area for some time, new pension regulations¹ now require pension trustees to confirm their policies in this area within their SIPs. The Trustee has also decided to pre-comply with further obligations which will apply under these rules from 1 October 2020. As such the Trustee's SIP has been updated to confirm the Trustee's approach to: how financially material considerations are taken into account in the Trustee's approach to investment, how members' views and non-financial matters are taken into account, the Trustee's approach to stewardship, engagement and voting rights and the Trustee's arrangements with asset managers.

Changes to the Trustee's Investment Beliefs (For information, not part of the consultation)

Whilst not included within the new proposed SIP and not part of this consultation exercise, I wanted to draw your attention to the fact that the Trustee completed a review of its Investment Beliefs at the same time as reviewing its SIP. As a result of this review, the Trustee has agreed to include **two new DC Investment Beliefs** to bring the DC Investment Beliefs into line with those of the DB Investment Beliefs, and slight amendments to the wording of these for consistency of application across the two sections of the Scheme. The two new Investment Beliefs are:

- ***Private markets provide investment opportunities and structures not available in public markets.*** They may provide opportunities for additional returns (including illiquidity premia), diversification, protections or other desired characteristics relative to public market assets.
- ***As a large pension scheme, there may be cost, alignment and time-horizon advantages in investing via in-house investment capabilities.*** The internal manager (USSIM) will use in-house investment management expertise where beneficial to the Scheme and members. However external managers will be used where internal resources cannot be justified, developed or obtained for the desired allocations, and suitable terms and alignment can be established externally.

Having operated the DC Section since its launch in October 2016 and with rapidly growing assets in this section of the Scheme, the Trustee believes that these two Investment Beliefs should apply across both sections of the Scheme (DB and DC). As such the Trustee has been working with its in-house investment manager (**USS Investment Management Limited** or '**USSIM**') to see how USSIM's investment expertise (in private market investments for example) and the cost savings that can be made through USSIM's investment management, might be able to be made accessible to DC members' investments, now that there is sufficient scale.

The Trustee has reached these conclusions based on the benefits that both private markets and in house investment can deliver to members' retirement savings, but were also informed by research carried out with members in 2017 that suggested:

- Members understand and are positive about the concept of increasing returns through holding onto an asset for longer (illiquidity premia) as they may have experience of bonds;
- Outside of the question of risk vs. return, members like the idea of tangible investments, which they can imagine or actually see, and the idea of contributing to infrastructure projects (e.g. investment in wind farms.)

¹ The Pension Protection Fund (Pensionable Service) and Occupational Pension Schemes (Investment and Disclosure) (Amendment and Modification) Regulations 2018 and the Occupational Pension Schemes (Investment and Disclosure) (Amendment) Regulations 2019

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The inclusion of an Investment Belief regarding private market investment is also in line with the Department of Work and Pensions' recent consultation² published on 5 February 2019, regarding innovation in DC schemes, encouraging DC schemes to consider a wider range of investments and suggesting that larger schemes be required to document and publish their policy in relation to investment in illiquid assets.

The Trustee's full list of investment beliefs are available in the 'How USS Invests' area of the USS website www.uss.co.uk.

SIP consultation responses

In preparing this SIP for consultation, the Trustee has considered the written advice of an independent investment adviser, Mercer. The Trustee believes that the proposed amendments are beneficial to the Scheme and members and we would welcome the views of employers in this regard. If you wish to provide a response to the consultation, please do so by emailing SIPConsultation@uss.co.uk no later than 4 September 2019.

The Trustee's goal remains to deliver a high quality, value-for-money and sustainable pension scheme, tailored to employers' requirements and members' needs.

I am aware that we have undertaken a number of consultations with employers (either directly or through Universities UK) and once again I thank you for your continued engagement and support for what is legally required and necessary to the sound governance of the Scheme.

Yours faithfully



B Galvin
Group Chief Executive Officer

² DWP consultation – 'Investment Innovation and Future Consolidation: A Consultation on the Consideration of Illiquid Assets and the Development of Scale in Occupational Defined Contribution schemes', 5 February 2019

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