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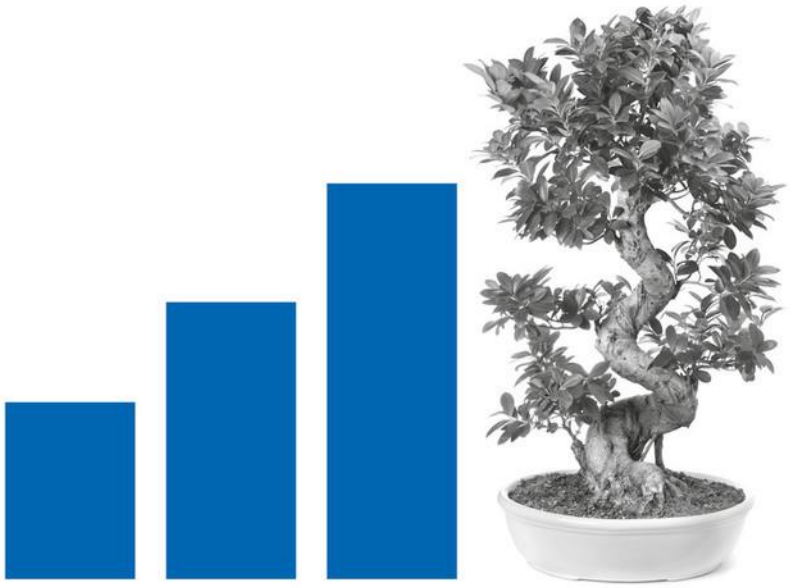
Universities UK

Advice Note for employers on USS Proposals



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Universities UK
Advice Note for employers on USS Proposals

This advice note has been prepared solely for Universities UK ("**UUK**") and unless expressly agreed in writing, we do not accept liability to any other person in respect of the advice provided. While we understand that this advice note may be shared with other USS employers, our client is UUK and others should take their own legal advice on the issues set out in this advice note. Sharing of this advice note with others or their advisers does not amount to a waiver of legal privilege.

1. Background

1.1 Unless and until the 2018 valuation of the USS is finalised, the contribution changes previously announced under the 2017 valuation will be applied. As part of the 2018 valuation process, the Trustee has put forward three options:

Option 1 - 33.7% fixed rate and reviewed in 2021/22

1.2 This is the rate the Trustee would require in the absence of sufficiently strong contingent contribution arrangements. In the event that the Joint Negotiating Committee (JNC) could not decide on an alternative approach, the default cost-sharing rule would see members paying 10.7% of salary and employers paying 23% from 1 April 2020. The next scheduled valuation would be as at 31 March 2021 (the outcome of which would be expected in 2022).

Option 2 - 29.7% increasing in certain conditions and reviewed in 21/22

1.3 If sufficiently strong contingent contribution arrangements can be agreed, members would pay 9.3% of salary under the cost-sharing rule and employers would pay 20.4%. Contingent contributions could be triggered in certain conditions. The next scheduled valuation would be as at 31 March 2021.

Option 3 - 30.7% fixed rate until October 2021 and reviewed in 20/21

1.4 This rate could be applied as an alternative to contingent contributions but is subject to a valuation in 2020 – a year earlier than scheduled. Under cost-sharing, members would pay 9.6% of salary and employers 21.1% until October 2021. If the contribution rate arising from a 2020 valuation cannot be agreed and implemented before 1 October 2021, the rate would then rise to 34.7%.

2. **Option 3 Conditions**

2.1 UUK has received an indicative preference from employers representing a significant number of the active membership to further explore Option 3 with the Trustee.

2.2 As part of Option 3, the Trustee is proposing a package of measures designed to address the key areas identified by PwC, its covenant advisers. The purpose of these measures is to ensure the covenant standing behind the USS is protected in the longer term, and will have an immediate effect of ensuring the current covenant rating of "strong" for the 2018 valuation.

2.3 The Trustee has moved forward with the 2018 valuation on the assumption that the covenant would remain "strong", and so would need to revisit the position (and, it is indicated, the contribution levels set out in section 1 of this note) if the measures are not agreed. This is likely to affect timescales for completion of the 2018 valuation and implementation of a new Schedule of Contributions to replace the contribution rates arising from the 2017 valuation.

2.4 The Option 3 measures include:

2.4.1 pari passu security for the USS in relation to secured debt being taken on by employers;

2.4.2 the introduction of a framework to monitor employers' debt levels; and

2.4.3 an amendment to the scheme rules which it is stated would "clarify and strengthen" the Trustee's discretionary powers on employer withdrawal from the USS.

2.5 UUK wrote to the Trustee on 19 June 2019 raising the challenging timeframes under which employers are being asked to consider the proposals and therefore put forward an alternative proposal of a 'moratorium' on employers exiting the USS without the Trustee's consent. This would give greater time for the employers to consider the suggested permanent rule amendments in more detail so that UUK can receive greater consensus from employers on long-term changes.

2.6 After consideration, the Trustee has agreed in principle that it would be prepared to accept an interim moratorium proposal on the basis it would apply until the 2020 actuarial valuation is completed (through the signing of the new Schedule of Contributions), unless the permanent rule amendment is completed and executed before this date. The Trustee expects the rule change to be implemented in advance of the valuation being completed so that it can be reflected in the consideration of a 2020 valuation.

2.7 It is not clear if the USS is intending for the permanent Rule amendments to be effective as soon as the moratorium ends or whether there will be a window of opportunity for employers to potentially exit the USS, without requiring the consent of the Trustee, before any final Rule amendments are introduced.

3. **Introducing the Moratorium**

3.1 Whilst we understand that UUK would like to keep open the option of agreeing the moratorium in some form of legal agreement (like the 2015 contributions letter), in reality a formal rule amendment appears to be the only way to make the moratorium legally binding.

3.2 It is unclear whether the Trustee has the unilateral power under the existing Rules to prevent an employer from becoming a withdrawing institution and triggering its Section 75 debt. In particular under the proviso (B) within the "withdrawing institution" definition states:

"if at any time it appears to the trustee company that the fulfilment by the institution of the conditions in any of paragraphs (a) to (h) above has not resulted, and is unlikely to result, in the occurrence in relation to that institution of a "relevant event" (as defined in (A) above), it may treat any such conditions as not having been so fulfilled."

3.3 If the Trustee is to have a permanent power to prevent an employer from becoming a withdrawing institution without its consent then there should be an amendment to the Rules to clarify this.

3.4 A moratorium would therefore be an interim measure to stop employers from leaving the USS for a limited period.

3.5 The Trustee has already asked UUK to confirm as soon as possible how it would prefer to see the moratorium structured in the Rules. This suggests the Trustee also believes that a Rule amendment is necessary to introduce a moratorium. They refer to a separate standalone clause with its own sunset mechanic or amendments to the existing employer exit provisions.

4. **Rule Amendment**

4.1 A separate standalone clause with its own sunset mechanic inserted as part of Rule 46 or new Rule 46A would be the most straightforward way of introducing the moratorium by effectively freezing the "withdrawing institution" provisions (without Trustee consent) for an interim period.

4.2 In terms of the sequencing of the amendment process, the Trustee has suggested that UUK proposes the necessary amendments to the JNC.

4.3 Under Rule 64.1, one of the functions of the JNC is to initiate or consider amendments to the Rules. Rule 79.7 gives the JNC the specific power to recommend Rule amendments to the Trustee. This power sits with the JNC as a whole and not with any individual members of the JNC such as the UUK appointees.

4.4 It should be noted that any proposals whether for an interim moratorium or for permanent rule changes to give the Trustee a power to stop employers from becoming withdrawing institutions and/or extending employer contribution rules to allow the Trustee to seek further employer contributions after a Section 75 debt has been paid, would be significant rule amendments which would fundamentally change the employers' position within the USS and grant the Trustee with more explicit and potentially new powers.

4.5 Whilst few USS employers may actually have the financial ability to exit the USS, the impact of the proposals on any employers who may be considering this option should still be considered.

4.6 In order to take a proposal for the approval of the JNC, the UUK appointees would ideally have a strong mandate from the employers which has been given from an informed position. In practice, this would come through engagement with employers undertaken by UUK.

4.7 Given the number of employers in the USS, it seems highly unlikely that unanimous support would ever be provided for such proposals. However, the JNC members would be able to take into account the extent of the consensus which exists across the USS employers, for example in terms of employer numbers and also liability share, for a particular view or proposal.

4.8 Where the JNC recommends to the Trustee any amendment of the Rules under Rule 79.7, the Trustee shall, in accordance with that Rule, take steps to implement the recommendation, unless it appears to the Trustee, acting on actuarial advice, to breach any of the caveats to that Sub-Rule.

4.9 In particular, these caveats include any amendment which impose any unfair liability upon any one or more of the institutions or upon the Trustee or is undesirable for any other reason which the Trustee notifies in writing to the JNC. We understand that the Trustee is unlikely to raise any issue with such a recommendation from the JNC.

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