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FURTHER RESPONSES FROM EMPLOYERS REGARDING THREE OPTIONS PRESENTED BY THE USS TRUSTEE FOR THE CONCLUSION OF THE 2018 VALUATION

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Introduction

In light of the more detailed information provided by the USS Trustee, together with their 'in principle' agreement to a 'moratorium' approach on the rule change on employer exits, Universities UK (UUK) has continued to consult with employers in relation to conditions attached the Trustee's proposed 'Option 3' as a way to conclude the 2018 actuarial valuation.

UUK has received 95 responses to this part of the consultation from employers which, taken together, represent over 89% of the active membership of USS.

It is clear to UUK that despite the difficulty and complexity of the consultation - and indeed its short timescale - employers continue to engage constructively with the issues, and the USS Trustee's continued support in securing this is recognised. UUK trusts that the USS Trustee will appreciate employers responding in a timely manner, where possible, and acknowledge that this is done to allow the trustee sufficient time to progress matters to conclude the 2018 valuation ahead of the planned October 2019 contribution increases.

In headline terms, UUK has received a preference from the majority of responding employers (72 employers, representing 81% of the active membership of those employers responding) that they are willing to support the package of covenant protecting measures to allow the covenant to be confirmed as 'strong' and to conclude the 2018 valuation in line with Option 3. Fourteen responding employers did not explicitly confirm their view on the entire package, but instead commented individually on the three elements. This information is contained within the detail below.

General observations

Employers remain to be convinced in relation to the rationale for the Trustee's covenant protecting requirements. It is expected that the employer webinar of 11 July will have been helpful in employers understanding the Trustee's rationale. At the time of writing, it is too early to comment on the feedback from the webinar, although it is expected that future such engagement between employers and the USS covenant advisor will be helpful in the longer-term discussions on supporting the covenant.

Employers have again raised concern about the timescale for considering such important matters, with a main issue being that the covenant supporting requirements have materialised very late in the 2018 valuation process. This is something that employers would have expected to see at the outset of any valuation process, and consider that this could have been incorporated at the next valuation. This is especially the case given that the 2017 valuation was concluded with a 'strong' covenant assessment, and it is the Trustee that preferred to consider the Joint Expert Panel's (JEP) recommendations through a new 2018 valuation.

Employers remain supportive of the JEP, and have again commented that the valuation could and should be concluded with a rate close to the JEP, and without the need for the employer requirements the USS Trustee has now requested in relation to the covenant and in addition to increased contribution rates.

Employers are supportive of Option 3 but see this as an immediate solution ahead of the

JEP's second report. Employers acknowledge that a review of the valuation methodology and the governance around the valuation process are needed ahead of the proposed 2020 valuation.

Temporary amendment to the scheme rules to clarify and strengthen the Trustee's discretionary powers on employer withdrawal from the Scheme

Employers recognise the importance of the covenant issues, and agree that a more detailed review of the scheme rules on employer withdrawals and exclusivity should be undertaken. This review would need to be thorough and considered, and agreeing a moratorium on employer withdrawals for a period to the next valuation will create the time and space for such a wide ranging review to be undertaken. Employers would be concerned if they had to commit to longer term rule amendments up front and in advance of such a review taking place.

The majority of responding employers (77 employers, representing 84% of the active membership of those employers responding) recognise that the moratorium offers a practical way forward to ensure the covenant remains strong and agree to discuss the need for a permanent rule change. However, employers remain concerned that this would permanently change the position of employers in the scheme and give more power to the Trustee. It is therefore fundamental that any permanent rule change is considered alongside a necessary review in USS governance in order to ensure accountability and a long-term sustainable pension scheme which realistically considers affordable benefits and contributions.

Some employers and in particular a number of smaller colleges (6 employers, representing 3% of the active membership of those employers responding) have expressed that they find the proposal unacceptable in its current form and are not agreeable to the proposed moratorium. Indeed, some believe that approving such a moratorium may well breach their fiduciary duties as trustees of the colleges. It is expected that the USS Trustee would consider this position and provide reassurance that it would be lawful for the Trustee to make the rule amendments proposed.

Debt monitoring

The majority of responding employers (76 employers, representing 81% of the active membership of those employers responding) are receptive to the Trustee's ask in terms of debt monitoring on the basis that the requests are proportionate. Many employers make the point that debt information is already a matter of public record enabling USS to monitor debt levels accurately. Such debt monitoring should be kept under review (perhaps by a joint USS / employer working group) to ensure that the process does not become too onerous or costly to employers or USS. It is expected that the information needed would be consistent with that already provided to the Office for Students, and other such bodies.

Pari Passu on secured debt

Employers have acknowledged the potential advantages in terms of covenant protection of granting security to USS which is co-terminous with the security to other lenders, as set out in Aon's advisory note, but have also added to the now numerous issues and questions which will need to be worked through in detail in due course.

A majority of responding employers (66 employers, representing 72% of the active membership of those employers responding) have expressed agreement in principle, to the USS trustee's proposals, subject to the practicalities being worked through so that employers can consider fully the detail of the implementation. A key aspect of this agreement is the establishment of a joint USS / employer working group being established involving institutions' finance directors to agree the finer detail and review and refine this arrangement over time to ensure a mutually balanced approach.

Employers note that whilst most sector borrowing in the recent past has been raised on an unsecured basis, this might not always be the case. Employers would want to consult with lenders to understand the implications for these proposals.

Employers have concerns over the potential implications upon future plans for growth and development, and want to understand any possible constraints upon an employer's ability to legitimately and prudently use borrowing to support, enhance and develop as may have been the case in the past.

Employers also have concerns about providing any firm commitment when the detail, which is important, is at present lacking. The USS convent advisor, PwC, acknowledged this point in the recent employer webinar and agreed that an agreement in principle should be sufficient to allow the conclusion of the 2018 valuation in line with Option 3, and that the establishment of a joint working group to consider the detail would be an appropriate way forward.

It should also be noted that a number of employers (14 employers, representing 9% of the active membership of those employers responding) stated clear opposition to this suggested condition.

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