University response to UUK employer consultation
26 October 2018

To: UUK

From: (Acting) President & Vice-Chancellor and Chair of Council
University of Sheffield

RE: Employer consultation on JEP report and recommendations

Please find below the agreed position of the University of Sheffield in response to the above employer consultation.

1. Would your institution support the JEP recommendation regarding the 2017 valuation, in overall terms, subject to the acceptance of such a position from the USS Trustee (and tPR as appropriate)?

The University of Sheffield welcomes the report of the JEP and supports its recommendations.

Looking at each recommendation in more detail:

1. A re-evaluation of the employers’ willingness and ability to bear risk – this would mean re-assessing the reliance on sponsor covenant.

In the September 2017 UUK consultation response the University questioned the rationale behind Test 1 and the actions it drove. The JEP states that Test 1 is overly complex and plays too significant a role in determining investment strategy – the valuation, it says, has become “model driven, not model informed”. The University concurs with this view.

In light of this, and recognising the recent developments regarding this matter, the University encourages the JEP, in Phase 2 of its work, to look at alternative, more logical and transparent means of assessing risk. Only then can a proper determination of the employers’ attitude to risk be established.

The University also urges UUK and the JEP to explore with the USS Trustee whether the current governance arrangements in USS are appropriate and if so, are working well.

Notwithstanding those points, the University recognises that it is likely that for the purposes of the 2017 valuation Test 1 will remain. Our response therefore assumes that it is in place.
The University response to the September 2017 UUK consultation process stated a broad acceptance of the “September 2017” levels of risk and employer covenant assessment. On that basis, notwithstanding the HE environment and political/economic position having moved on since September 2017, the University continues to support the recommendation to move back to the September 2017 levels of risk (including no de-risking of investments in years 1-10) and the level of reliance on covenant suggested by the JEP (£13bn vs £10bn).

The JEP has indicated that it could be sensible to call for a further widening of the ‘reliance on covenant’ amount, which would further reduce costs at the expense of a lower amount of investment risk reduction. Given the lack of information on the effects of such a decision, the University is unable to make an informed recommendation regarding this. The University would encourage the JEP, in Phase 2 of its work, to fully explore means by which the levels of risk in the scheme can be transparently assessed in a way that is easy to understand and that ensure an appropriate, but not excessive level of prudence is built into it.

For the purposes of this response, the University understands “ability to bear risk” as the University’s capacity and willingness to accept that with prudent assumptions and an investment strategy similar to that currently adopted by USS there remains the possibility that an adverse outcome will arise that could require additional contributions from the employers.

2. Adopting a greater consistency of approach between the 2014 and 2017 valuations – this would mean changing the approach to deficit recovery contributions.

The JEP states that a significant contributor to the increase in deficit contributions from 2.1% of salaries following the 2014 valuation to a proposed 6% in the 2017 valuation is due to USS not making any allowance for out-performance of assets above the discount rate in the 2017 calculation. This, the JEP claims, is an excessive level of prudence, not least because at a point now almost 18 months on from the valuation date, such outperformance is evidenced in the investment returns.

The JEP makes reference to the USS Trustee preference for the inclusion of such outperformance to be linked to the availability of additional contributions from employers which are linked to a failure to achieve the level of return targeted. The JEP concludes that this issue should be addressed in the longer term as part of a wider review.

The University supports the view of the JEP in this element. However, the University is not prepared to pledge particular assets (e.g. buildings) to the scheme by way of security.

On the subject of contingent or trigger contributions, the University would wish to consider its position based on the outcomes of Phase 2 of the JEP’s work when, ideally, a more transparent approach to assessing risk in the scheme will be determined.

3. Achieving greater fairness and equality between generations of Scheme members – this would mean smoothing future service contributions.

The JEP suggests the approach to determining future service contributions adopted by the USS Trustee, based only on the figure for the year following the valuation, is a non-standard actuarial approach. The JEP suggests that, on the basis of advice from AoN and
First Actuarial (actuarial advisers to UUK and UCU respectively) that future service contributions could fall during the next six years, the future service contribution rate is determined using an average over a period not shorter than two valuation cycles (six years).

This would support intergenerational fairness allowing more members to benefit from a lower average rate of contributions over the period.

The University supports the view of the JEP regarding the smoothing of future service contributions.

4. **Ensuring the valuation uses the most recently available information – this would mean using latest available data and taking account of recent investment considerations and outcomes.**

Given the time lapse between the valuation date (31 March 2017) and now, and the accurate data and latest assumptions now available, the University can see no reason not to support the use of this information to better inform the valuation process by the Trustee.

5. **Taking the uniqueness of the Scheme and the HE sector more fully into account.**

The JEP references the work it plans to undertake in Phase 2 of its remit. The crux of this will look at whether there is a different way of reaching a conclusion that could provide longer term stability to the valuation process and have the support and confidence of all parties.

The University supports this proposed work and urges UUK and the JEP to note the points raised earlier in this response regarding the need to identify simpler and more transparent assessments of risk and would encourage the JEP to consider this as part of its assessment of alternative ways to undertake the valuation process. From an employer perspective, it is critical that Phase 2 of the JEP work creates a stable and predictable platform on which the Valuations are made.

The University acknowledges that it is unlikely that responses will be provided before the consultation deadline of 30 October 2018, however the University is seeking clarification on two points.

Following the criticism of the way in which previous consultations were run the University is seeking clarity from UUK over how it will consider the responses submitted to it from the various 350+ participating employers. The University wishes to understand what, if any, weighting will be attributed to employers such as the University of Sheffield who collectively have a stronger presence in USS in terms of members, contributions and exposure to risk. In broad terms those larger, pre-92 Universities tend to be the strongest financially and so, in a scheme such as USS which is a “last man standing” scheme it is more likely to be those Universities which own most of the risk of negative consequences on the scheme in future. The University considers this should be recognised by UUK in forming its collective view of the
feedback from employers. The University is also urging UUK to publish its position regarding this weighting of responses in the interests of transparency.

The University notes that the JEP report makes no reference to any equality impact in relation to the recommendations and is seeking to understand from UUK whether any such assessment has been or is planned to be carried out at a sector level. The University will undertake an equality impact assessment of the JEP proposals at a local level in addition.

| 3 | Employers currently pay 18% towards the USS scheme, and the mandate agreed immediately following the ACAS discussions [during the strikes] was 19.3%. If the recommendations for the JEP were accepted in full by all parties, the outcome would be that existing benefits – minus the employer match of 1% - could be provided at an indicative employer contribution of 20.1% of salary (with a member contribution of 9.1%):
  - Would you accept employer contributions at that level?
  - If not, what balance of additional risk, higher contributions and/or benefit change would you prefer to see as an outcome? |

The University acknowledges that, should the JEP recommendations be agreed and implemented it would result in indicative increases in costs for members (of c1.1% of salaries) and the University (of c2.1% of USS member salaries). This follows the 65:35 cost sharing principle agreed by the JNC following the 2014 USS Valuation and now incorporated into the scheme rules.

For this University such an increase would amount to approximately an extra £4m per annum to maintain existing benefits in USS. To fund this the University will need to make difficult decisions regarding how it allocates its limited resources.

Notwithstanding that, the University would support the acceptance of these higher levels of contribution, acknowledging that the 2020 valuation may, following further work by the JEP in its Phase 2, produce a different outcome regarding the stating of a deficit in USS. The University recognises the JEP proposals are based on estimated figures. If the proposals are agreed and implemented, should the USS Trustee determine after accurately costing those proposals that a greater level of increase in contributions is needed from employers, the University would wish to be consulted again so as to make an informed decision on the detail.

Following the outcomes of the JEP Phase 2 work relating to the valuation methodology and in particular the means of assessment of risk, and subsequently the 2020 USS Valuation, if it is recognised that the cost of maintaining benefits is lower than the cost indicated by the JEP report, the University would welcome consideration of a commensurate reduction in contribution levels for both employers and members.

**Conclusion**

The University appreciates the work of the JEP over the summer months and welcomes the report which offers a potentially viable solution to the current dispute over USS which has been so damaging for the sector.

The University is reassured that the recommendations of the JEP align closely with this University's stated position from the original UUK consultation in September 2017 and that, like this University the JEP is unconvinced as to the merits of and actions driven by the USS Test 1.
Whilst any further pressures on our financial sustainability are challenging, there is a need to balance a desire for lower contributions now with the University’s capacity and willingness to accept a greater level of risk that an adverse outcome will arise that could require additional contributions from the employers in future. It is the University’s view that the proposals put forward by the JEP report strike a reasonable balance between these elements.

Looking to the future and Phase 2 of the JEP’s work, the University welcomes the opportunity and prospect of seeking a more suitable, transparent and stable position from which to assess the health of USS at the 2020 valuation and beyond.

The University wishes to thank those involved in the work of the JEP and the members of the University of Sheffield USS Valuation Working Group who have contributed significantly to the position taken by the University.

This University response has been agreed by the University’s Council as it’s governing body, following consultation with a representative stakeholder group including UCU and academic staff representation and the University’s Executive Board. As such it stands as the formal position of the University of Sheffield regarding the October 2018 UUK consultation with USS employers on the JEP recommendations.