11 September 2019

Dear Bill

Consultation on proposed changes to the Schedule of Contributions and Recovery Plan for the 2018 actuarial valuation

Thank you for your letter dated 23 August 2019 regarding the above, which advises employers of proposed rates of contributions due from 1 October 2019, and related matters. This consultation follows the trustee’s finalisation of a valuation report under sub-rule 76.1 and the decisions made by the Joint Negotiating Committee (JNC) on that valuation report on 22 August 2019.

Responses to the schedule of contributions and recovery plan consultations

The trustee is proposing to finalise the valuation in a way which is in line with its proposed option 3 outcome. It is clear that employers have expressed their support for option 3 on specific terms. These terms include that the option 3 outcome represents a short-term solution, in order to allow the Joint Expert Panel (JEP) to publish its recommendations so that they can be taken into account in the March 2020 actuarial valuation. Also, that the contribution rates arising from option 3 will be implemented from 1 October 2019, thereby replacing the rates from the 2017 actuarial valuation which would otherwise apply. This provides an important context for the consideration by employers of these consultation documents; their responses are set out below.

Recovery plan

The responses from employers indicate that, ordinarily, they would have substantial difficulties with the recovery plan proposed by the trustee in terms of the calculation of the deficit, the plan length, and the allowance for expected investment outperformance over that period. In particular, employers note that the trustee:

- is proposing to finalise the 2018 valuation based upon assumed covenant reliance in 20 years’ time of £10bn, rather than £13bn as recommended by the Joint Expert Panel (and the trustee had earlier suggested that the assumptions underpinning the option 3 outcome would be consistent with those for its option 2, which used a £13bn reliance figure);
intends to adopt a recovery plan of 10 years duration when measured from the 2018 valuation date – and 8½ years from the proposed commencement date of recovery plan contributions – which is much shorter than employers believe is justified; and
- has included no allowance for asset outperformance in the recovery plan, when at previous valuations such an allowance has been justifiably included.

As mentioned above, the context for this valuation is quite specific and it is only on this basis that employers consider the recovery plan proposals to be in any way acceptable. These views are entirely without prejudice; employers do not believe that the outcomes reached on the recovery plan would set any kind of precedent or template for what they might consider reasonable and justifiable at the next and subsequent valuations.

With regard to the detailed text of the proposed plan, we would ask that the trustee reviews the wording which states when a review of this recovery plan will take place. The draft plan states that such a review will occur “following the Trustee’s next valuation under section 224 of the Pensions Act 2004, or earlier if the Trustee so determines”. We would ask the trustee to make clear, on the face of the recovery plan, that the next valuation will take place on 31 March 2020.

Schedule of contributions

We have no comments on the draft schedule of contributions, other than to note that the revaluation of the salary threshold is a matter which needs the JNC’s attention and to ask that the trustee bring this forward for consideration at the earliest opportunity.

Engagement with the Pensions Regulator (tPR)

We are grateful for sight of the letter from Mike Birch at tPR to the Chair of the trustee board dated 6 August 2019, and it is helpful for employers to see the views of tPR should the 2018 actuarial valuation be concluded in line with option 3 (such views we assume being subject to these consultations on the recovery plan and schedule of contributions, and to the finalisation by the trustee of the valuation report). The letter contains a number of references to Universities UK and to employers, and we will look forward to discussing these specific points with tPR representatives at the next of our regular exchanges.

Conditions in financial markets

Thank you for the additional information contained in your letter on the latest market developments, which indeed are concerning, but which we think we must continue to see in perspective. We recognise that the current economic uncertainties will undoubtedly have been a factor in the assumptions formed by the trustee in relation to the recovery plan, however we would emphasise that weight must be given to the enduring nature of the covenant provided to the scheme by its sponsors. We also note that the upcoming March 2020 valuation provides an early opportunity to further consider market developments.

We hope that the JEP’s second report can be a prompt for the trustee and stakeholders to consider which risk metrics are most appropriate for USS, and how they can give a longer-term perspective to the management of the scheme’s funding approach.
The moratorium rule change, debt monitoring and pari passu arrangements

We are grateful for the trustee’s support over recent weeks in implementing the rule changes, in moratorium form, relating to employer participation. We have also found the initial communications from the trustee relating to debt monitoring and pari passu on any new secured debt to be useful. We do recognise, however, that much work remains on each of these initiatives. In particular, we are conscious that the indicative support from employers for debt monitoring and pari passu provisions is subject to further definition of the proposed arrangements, and as a result we have assembled a list of individuals who would be willing to take part in a joint technical group to work with the USS trustee on the details. We look forward to progressing this with you in the coming months.

I hope that the above responses are helpful to the trustee board as it finalises the 2018 actuarial valuation, and of course please let me know if you require any further information.

Yours sincerely

Alistair Jarvis
Chief Executive