# A consultation by Universities UK with employers on the indicative outcomes of the 2020 valuation

## University of Leeds response May 2021

In April-May 2021, UUK consulted the 340 employers in USS on options for reforms to address a sizeable scheme deficit and to tackle an increasing high opt-out rate.

More than 1000 eligible Leeds staff responded to a survey about aspects of the scheme so that University Council could take account of member opinions in its response to UUK.

What follows is a transcript of the University of Leeds submission to UUK, May 2021.

**MAKING YOUR RESPONSE** TO THE CONSULTATION

We welcome responses to this consultation from each and every one of the scheme’s participating employers.

We are keen to have the widest possible range of views and perspectives ahead of the next steps of the 2020 valuation.

Through this consultation we are formally seeking views and direction from employers on some key questions, particularly on:

* Covenant support measures
* Contributions
* Future benefit structures
* Addressing the high opt-out rate and flexibilities
* Governance
* UUK’s Alternative Approach

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With these views, UUK can then progress the negotiations with the University and College Union (UCU) within the Joint Negotiating Committee (JNC).

# COVENANT SUPPORT MEASURES

1. Would you be willing to support the alternative covenant support package which UUK has outlined in section 4, as the means to achieve a solution which might be acceptable in the round (see also question 15)?

We are broadly supportive of the alternative covenant support package which UUK has put forward, including the proposal for an appropriate rolling moratorium on institutions leaving.

1. If the USS Trustee is not willing to accept UUK’s alternative proposal (should there be employer support for it), would you be willing to support the USS Trustee’s scenario 3 covenant support package to obtain a ‘strong’ covenant rating? If not, why is this and what level of covenant support would you be willing to provide?

We are not comfortable with the Metric E threshold proposed in the USS Trustee’s Scenario 3 for *pari-passu* security on new secured debt. As implied in our answer to Question 1 above, we would not object to the threshold being set at 15 per cent of net assets and 15 per cent of gross assets, but we consider that the threshold proposed by the Trustee – 10 per cent – is too low, making it unnecessarily difficult for universities to borrow money to help them to achieve their strategic objectives.

Whilst we are not averse to the principle of debt monitoring, this should not apply to existing (as opposed to future) debt; and we would like to see more information about how the arrangement would work in practice.

Fundamentally, however, we are concerned that an aggregate contribution level of 42.1 per cent, as implied by the Trustee’s Scenario 3, is simply not affordable. As we have said before, we believe that, both from the perspective of employers and from the perspective of individual members, current contribution rates are at the limits of affordability.

We therefore do not consider Scenario 3 to be a sustainable solution.

1. Are there areas of the covenant support measures which cause you particular concern, or which you would wish to see modified? Please provide details.

We have nothing to add to our answers above.

1. Are there other areas of covenant support you would wish to consider such as contingent contributions or asset pledges?

There are no other areas of covenant support that we would wish to see considered. We remain of the view that we have no capacity to accept more risk from USS than we already carry; and, because it is difficult to see how such an arrangement could be fair between different employers, we have significant reservations about the idea of asset pledges.

# CONTRIBUTIONS

1. Do you agree that the current levels of employer contribution (21.1% of salary) and member contribution (9.6%) are the maximum sustainable – and should be the foundation for any solution?
   1. If not, please state the level of employer contribution you would be willing to pay to

USS following the 2020 valuation.

* 1. We would welcome any commentary on the reasons for your views.
  2. We would also welcome employer views on the level of member contribution.

We strongly agree that the current levels of employer contribution and member contribution are the maximum sustainable – and should be the foundation for any solution.

As we have said previously, increasing the total employer contribution would restrict strategic development plans, place cost pressure on all areas of University activity, put employment security at risk, and potentially raise concerns from students about this use of the fees that they pay. Ultimately, it could threaten the financial sustainability of the University.

Increasing employee contributions would, in our view, risk greater numbers dropping out of the scheme, thus both undermining the long-term sustainability of USS and giving rise to greater inter-generational unfairness. Our recent survey of staff – which had a participation rate of just under 20 per cent – revealed that 85 per cent of respondents would be concerned about affordability if contributions were to increase, with 34 per cent being ‘very concerned’. 13 per cent said that they would consider opting out if contributions were to increase, with a further saying that they might consider opting out depending on the level of increase.

High drop-out rates are not only bad for the scheme’s future, but can create problems for the individuals who drop out because they do not receive any employer contributions towards their pension provision, storing up problems for themselves, as well as society more generally, later in life.

# BENEFITS

1. Do you support the broad principle of seeking to retain the hybrid benefit structure?

We do support the broad principle of retaining the hybrid benefit structure, at least for the time being.

It is clear that individual members greatly value the Defined Benefit (DB) element – 54 per cent of the respondents to our recent survey indicated that they would wish to retain such benefits ‘no matter the cost’ to members. Moreover, moving to a wholly Defined Contribution (DC) scheme seems prohibitively expensive at this stage, given the need to address the scheme deficit.

1. Looking at the illustrative hybrid benefits which UUK has put forward, would you consider this an acceptable outcome in terms of benefits at this valuation – based on the positions on covenant support and contributions laid out?

Our strong preference is to explore a Conditional Indexation model, which we believe could represent a way to put USS on a secure and sustainable footing for the future in a way which meets the wishes of individual members as well as the employers. But, if that model were ultimately deemed not to be viable, we could see no option but to adopt something along the lines of the illustrative benefits proposal put forward by UUK. Although it would lead to a reduction in benefits that we would prefer to avoid if possible, it would seem preferable to the rise in employee and employer contributions inherent in the Trustee’s scenario 3, for example.

In any event, we recognise that the UUK alternative proposal might have to be adopted on a time-limited basis to provide the space in which to evaluate the Conditional Indexation model in more detail (see 9 below).

1. If the illustrated hybrid would not be acceptable, what alternative benefit arrangements would you wish to provide (and please indicate alternative positions on covenant and contributions as appropriate)?

*(For example, if the USS Trustee does not ultimately amend its assumptions, would you wish to offer a hybrid solution as set out in the USS Trustee’s illustrations (p18 of the Update Report) or would you prefer to move to a different offering, such as DC provision?)*

We are attracted by the possibility of adopting a Conditional Indexation benefits model (see below).

1. Would you wish to explore conditional indexation or other conditional benefit models as a possible solution (likely longer-term, beyond the 2020 valuation)?

We are strongly supportive of the notion of exploring Conditional Indexation or other conditional benefit models. Whilst it is too early to be sure, we see such work as potentially allowing us to put USS on a sustainable footing in a way that is acceptable to all stakeholders, including our staff. However, we recognise that exploring that model would take time, and that the immediate challenges highlighted by the 2020 valuation need to be addressed now. We are open to creative proposals but, given that contributions are already at the limits of affordability, we ourselves see no viable option other than adopting the UUK ‘alternative proposal’ as a short-term measure to buy time to explore and potentially implement Conditional Indexation. The only other option we see would be to have another valuation, as at March 2021, and we think that consideration should be given to this possibility too if it might facilitate the path to a CI solution.

# FLEXIBILITIES AND OPTIONS

1. Would you like to see flexibilities implemented for members to move away from the current uniformity of the USS structure, and if so which flexibilities do you think are particularly important?

We consider it to be essential to introduce flexibilities into USS to give members options that suit their personal circumstances.

A flexible DC scheme would provide the option for members to join just the ‘investment builder’ section of the scheme, potentially with different contribution rates. We believe this would be advantageous for staff at the early stages of their careers, and reduce the current level of opting out.

In the same vein, we consider that a tiered contribution structure is worth considering, as would be an arrangement by which younger members in particular could choose to pay lower contributions for lower benefits for a specified period. The important point is to keep contributions affordable for all.

1. Would you support the creation of a lower cost saving option for members and which of the parameters described in this paper are most important / or would need modification?

*(If yes, we would welcome employer views on the options to achieve this*

*(potentially informed via engagement with eligible USS employees).*

The points made in response to question 10 above apply here also.

1. Would you support the creation of an option for members to switch (from the hybrid

structure) to wholly DC pension saving?

*(We invite employer views on whether the same deficit recovery contribution should be made for members choosing any new flexible DC alternative option, and what levels of member and employer contributions devoted to DC pensions saving*

*should apply).*

We are not averse in principle to the notion of creating an option for members to switch to a wholly DC pension saving, but we have concerns about how practicable this would be at a time when the scheme faces a substantial deficit.

In any event, we need to be careful that the mix of DB and DC elements does not increase the overall cost beyond current contribution rates (given that the attraction of the two elements varies according to age). There would anyway have to be limits on flexibility to avoid undue operational complexity and costs.

1. Would you wish to explore options for employers so that they can offer some variations to the USS standard benefits in the future – and if so, what would those variations be?

We struggle to see how USS could remain a truly national scheme if different employers offered different levels of benefit. We consider portability – the ability to move from one institution to another without benefits changing – to be an important feature of the pension scheme.

# GOVERNANCE

1. We would welcome views from employers in relation to the governance of the scheme and the valuation process (including views on the Joint Negotiating Committee). Specifically, would you support a post valuation governance review, and what areas what you like to see covered in such a review?

We remain of the view that the governance of USS is opaque, and we would like to see greater transparency not only in this respect but also in the information flow and accountability to the sector. We therefore strongly favour a post-valuation governance review.

The role, status and composition of the Joint Negotiating Committee need to be considered as part of that review; and we would like to see consideration being given to ways in which views of staff who are not members of the University and College Union can be properly reflected in deliberations about USS.

# UUK ALTERNATIVE APPROACH

1. As part of a solution to the 2020 USS valuation would you support the alternative covenant support package illustrated by UUK *(headlines – moratorium of a minimum of 20-years with debt-monitoring and a pari-passu arrangement for secured borrowing above c15% of gross/net assets)*, to provide a hybrid benefits package at current contribution rates in the order of *(pension accrual of 1/85 of salary [plus 3 times lump sum] up to a salary threshold of £40,000 with the CPI indexation of benefits [for active, deferred and pensioner members] capped at 2.5% per annum, and with DC above the salary threshold at an overall contribution of 20% of salary),* together with a lower cost alternative to address the high opt-out rate, as well as a governance review of the scheme and valuation process?

See responses to questions 2 and 9 above.

**Thank you for taking the time to respond to this consultation.**

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