

# Universities Superannuation Scheme

## Debt monitoring framework – how we will work with you

Updated 9 June 2023

### Introduction

The Trustee has, in collaboration with employers, developed plans to introduce a debt monitoring framework as part of a package of measures to protect the strength of the Covenant. In operating this framework, the Trustee will:

- be pragmatic in operating the framework recognising the overriding objective of supporting and protecting the Covenant;
- be open, co-operative and transparent in all discussions with employers, listen to any employer views and representations and consider them fairly and on a timely basis;
- share with an employer any relevant analysis of that employer’s position, information it has received (including third party advice where possible), and the considerations it has taken into account in reaching its conclusions (unless prevented by law or regulation);
- consider representations from employers as part of periodic reviews of how the framework has operated; and publish an assessment of the framework’s effectiveness as part of the early stages of future valuations; and
- make any material changes required in the future in collaboration with employers.

This document sets out the Trustee’s approach to the operation of the debt monitoring framework (“the framework”) and engagement with employers. Whilst nothing in the document can fetter the Trustee’s discretion which must remain unfettered, it does represent the Trustee’s view on the operation of the framework over multiple valuation periods. To give employers further assurance, the Trustee will establish a process for an employer to request a review of any decision made in their case under this framework by the Trustee Board.

Note that throughout this note, the capitalised term “Covenant” refers to the covenant provided to the Scheme by the employers as a whole. All other uses of the word “covenant” apply to the covenant provided by an individual employer.

### 1. Data collection and review

The Trustee will collect data from employers annually and in certain circumstances on an ad hoc basis. The debt framework will set out clear guidance and definitions on what information is required and how the metrics will be calculated, including exemptions which may apply for employers which are able to self-certify compliance.

The Trustee will be understanding of other pressures employers may have at that time, and if an employer proactively engages with the Trustee, the Trustee will be flexible, for example agreeing a 30-day extension on request.

The Trustee will review data received and raise questions with employers if needed. Any and all data provided will be kept confidential and will not be disclosed beyond the Trustee, and its advisers without explicit permission (unless required by law or compliance with regulatory obligations).

## 2. Calculation of metrics

The Trustee will use the data provided for the purposes of calculating the agreed debt monitoring metrics, for ongoing monitoring and to support related discussions with individual employers.

The metrics are designed so that in combination they will alert the Trustee to seek further information where necessary. The debt framework sets out triggers for further action based on exceeding a number of metrics.

The Trustee wishes to protect the Covenant and make sure that the way it operates these provisions is proportionate and reasonable. We recognise that some smaller employers are not material in the context of the Covenant as a whole. Limits are set in the framework so that smaller employers are considered 'de minimis'. No further action would be taken under the framework in respect of de minimis employers.

## 3. Engagement where the published debt monitoring metrics exceed thresholds

Where the Trustee has calculated the metrics, and finds for a particular employer that it has exceeded, or is expected to exceed the trigger level set out in the framework, the Trustee will seek to engage with that employer:

- To review the data and the metrics calculations, to ensure the assessment is correct and appropriate; if any corrections are needed these will be made before any further engagement takes place;
- To understand the wider position of the employer and any mitigating factors, for example where a plan is in place to reduce the current level of borrowing;
- To understand the employer's funding strategy and how this might impact their metrics going forwards e.g. does the employer's strategy mean that it will revert to a position where the metrics are not exceeded within a defined and acceptable timeframe?
- To determine if there is any other relevant information the Trustee should be aware of; for example, the potential impact of any requirement by the Scheme for additional support for the covenant from the employer.

The Trustee would hope that in most cases, after evaluation of the employer's data and/or following initial discussion with the employer, no immediate further action will be necessary. The Trustee's intent is not to improve its position relative to other creditors. For example, if there has been no overall increase in borrowing, but a reduction in revenue has caused a metric to be exceeded, the Trustee would not, all other things being equal, expect to take action. Similarly, we would not seek to prevent an employer from continuing to properly manage its affairs in the event of a downturn in income save, for example, to be kept informed of any plans to discharge material creditors where so doing might prejudice the Scheme's position.

The Trustee will need to assess each case on its own particular facts and if it concludes that there is a material weakening of the employer's covenant, the Trustee will enter into further discussion with the employer to try to agree suitable mitigation measures.

#### 4. Engagement in relation to secured debt and potential *pari passu* security

As the Scheme is an unsecured creditor (without security or other collateral), there is a significant risk to Covenant strength if an employer's assets are pledged to lenders or other third parties.

This is because the Scheme's position as a creditor in the event of insolvency is subordinated.

The debt monitoring thresholds related to secured debt are therefore set so that there is an agreed point at which the Trustee will enter into discussions with the employer to try to agree suitable measures to prevent further subordination and typically to seek *pari passu* security for the Scheme.

The Trustee's considerations here are guided by the following principles:

1. The Trustee is not seeking to enhance the Scheme's position relative to the position of other secured creditors in existence at 1 August 2021.
2. The Trustee will operate at an appropriate and agreed level of materiality. To this end, there are a number of thresholds and exemptions set within the framework.
3. There is an exemption for new borrowing, raised solely for the acquisition of new, revenue generating assets and which is secured only on the assets acquired. The principle here is that the Trustee does not wish to have a role in validating an employer's plans but does need to ensure that in financing them, the Trustee's position is not prejudiced by granting other creditors preferential claims over existing assets. More detailed guidance and examples will be set out within the framework.
4. As every situation will have its own particular facts, the Trustee will always consider the particular circumstances of each employer individually and on a case by case basis at the relevant time before exercising the requirement for *pari passu* security.
5. No Trustee decision will set a binding precedent for any future decisions.

The framework is intended to be collaborative and employers are encouraged to engage with the Trustee as soon as possible if intending to provide debt security outside of the thresholds set out in the framework.

Whether in response to an approach from an employer or in response to its own monitoring, the Trustee's initial response will be to engage with the employer and to work together promptly to:

- review the data provided, including the pre-existing level of security;
- understand the type and amount of any new proposed security, including its catalysts and likely net impact on the employer's covenant to the Scheme;
- understand the scope for, and impact of, *pari passu* security being granted to the Trustee;
- understand the scope for, and scale of, potential alternative protections or security for the Trustee.

The Trustee is very aware that the timescales for completion of security deals can be short and therefore its own participation in the process must be prompt, clear and decisive. In such circumstances, the Trustee will react as promptly as it reasonably can. In general, the Trustee will endeavour to:

- acknowledge any employer’s notification that it intends to take out security within 1 working day;
- seek to hold an initial discussion with that employer within 7 working days of notification, to explore the primary details of the proposed security and its potential background, characteristics and effects;
- provide a summary to that employer of its understanding of the proposed security and any further information it believes it reasonably requires within 2 working days of that discussion, for the employer to review and provide any amendments or further comments;
- provide an initial view on whether the Trustee may require *pari passu* security within 2 working days of receiving the employer’s response to the Trustee’s summary arising out of the initial discussion;
- continue engagement with that employer on a prompt and responsive basis.

It should also be borne in mind that the above considerations are only relevant where the secured debt metric set out in the debt framework is being exceeded.

## 5. Deciding on any resulting actions

If, after engagement with an employer, consideration of all the relevant information, and having taken appropriate expert advice (if necessary), the Trustee feels that an employer’s covenant to the Scheme is affected by its debt or security position, it will:

- Notify the employer in writing of that conclusion, setting out the reasons why it believes that is the case and noting any relevant advice taken;
- Seek further engagement with that employer to explain the Trustee’s decision;
- Seek to discuss matters and listen to further representations from that employer, including any views the employer has on why the Trustee’s conclusions may be invalid or inappropriate;
- Discuss the potential options for addressing the covenant position, which may include enhanced future monitoring for a defined period, acceleration of Scheme contributions, additional security, or any other appropriate solution, to identify which would be acceptable to the employer and the Trustee.

This framework is being introduced in advance of implementation by The Pensions Regulator (TPR) of changes to its notifiable events regime introduced by the Pension Schemes Act 2021 which is expected to include formal requirements of sponsoring employers to notify Trustees of any intention to grant security to creditors.

We will as part of deciding on any action which we wish to take with employers, take account of the regulatory requirements/ expectations of TPR.

Then, taking into account all relevant information and advice received, the Trustee will finalise its decision and inform the employer in writing, after which engagement will continue to complete the exercise.

## 6. Unilateral actions

The Trustee hopes the principles articulated above will avoid the need for it to act unilaterally; it sees the evaluation and protection of the Covenant as a mutual endeavour between it and the employers, with better outcomes achieved through working together. Therefore, the Trustee only anticipates needing to take unilateral action where:

- An employer persistently fails to provide any data requested, despite multiple requests from the Trustee; and/or
- The employer fails to engage with the Trustee to discuss matters or explain its position; and
- The Trustee, having performed its own assessment of that employer's position based on publicly available data and relevant expert advice, concludes that the employer's debt, security position or covenant to the Scheme is a matter of concern.

OR

- Having been through an engagement process with an employer, and having reached a conclusion which it has shared with that employer, the employer does not co-operate in executing remedial action and the Trustee is required to take appropriate action in the best interest of the Scheme.

Unilateral action in these circumstances may include accelerating the payment of outstanding deficit repair contributions, clarification of which will be confirmed at each valuation in the Schedule of Contributions. Other actions could include making the employer a Withdrawing Institution or approaching the Pensions Regulator.

## 7. Challenging/reviewing a Trustee decision

The Trustee will always seek to engage with an employer, listen to and understand their view and consider that view in reaching any decision. The principles in this document set out how the Trustee intends to approach such decisions, though it is important to be clear that as a matter of UK trust law, neither this document nor the framework can fetter the Trustee as to how it might exercise its discretion in the future.

Employers will be able to request the Trustee Board to review a decision through [process to be determined].

## 8. Review of the framework

The framework is intended to be introduced as part of the 2020 valuation. It is hoped that the framework proves to be an appropriate balance between providing effective Covenant support and minimising the extent to which it imposes constraints on employers' operations. The Trustee will, in the next formal valuation following the introduction of the framework, include as part of its communications an assessment of the framework's ongoing effectiveness.

Feedback will be sought from employers on the extent to which they view the measures to have been unduly intrusive or to have constrained their operations.

**Contact:** Any employer who wishes to discuss matters, or who has any queries or concerns about the framework, should contact [debtmonitoring@uss.co.uk](mailto:debtmonitoring@uss.co.uk). This mailbox is monitored daily.