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FITZWILLIAM COLLEGE
UNIVERSITY OF CAMBRIDGE

3rd August 2020

Stuart McLean MBA FPMI | Head of Pensions | Universities UK
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20 Tavistock Square,
London, WC1H 9HQ

Email: stuart.mclean@universitiesuk.ac.uk

Dear Stuart,

USS consultation - the introduction of new arrangements relating to debt monitoring, and to priority on secured debt

I write on behalf of Fitzwilliam College in the University of Cambridge in response to your email of 8th July 2020 requesting comments on the above consultation.

In our response of 16th July 2019 we said:

> "We support the element of this proposal which relates to debt monitoring, and indeed see benefits to the scheme as a whole for there to be better provision of data to employers generally about debt levels in the sector. However we would add the caveat that the monitoring mechanism needs to be administratively straightforward and transparent."
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> and
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> "If the proposal is developed in more detail, we think it most important that the position of endowed charities – in which there is clear separation between the investing activities of the endowment and the operations of the institution - be carefully considered."

We are disappointed that the metrics and the procedures proposed in this USS consultation do not meet the criteria which we felt important, nor in our opinion do they serve the interests of the Scheme as a whole, because they are structurally biased against small, endowed, asset-rich institutions like ourselves, whose asset base and relatively small membership numbers make them net contributors to the strength of the employer covenant.

The College's opinion, and indeed experience, is that credit markets look to asset cover (metric A) as the predominant factor in assessing credit strength. This is illustrated by the strong credit ratings achieved by Cambridge colleges individually or collectively when raising long term funding. Income related measures (such as metrics B, C and D) are helpful in identifying trends in the underlying economic activities undertaken by individual borrowers, but will vary widely according to the make-up of the income and cost base of the individual institution, and should always be read in the context of the asset strength. Generic thresholds for these income related metrics are therefore inappropriate, and risk diverting USS resources away from interventions which should be directed at strengthening the net asset base of the scheme employers.

Our preliminary calculations suggest that, on current plans (and ignoring the impact of coronavirus), the College would very comfortably meet metric A (Gross debt to net assets), but would certainly fail metric B, and be likely to also fail metrics C and D. We would therefore find ourselves routinely in the category of 'Further Engagement'. Even in a benign scenario, in which the Trustee fully understands the particular position of the College and the benefit which its covenant brings to the scheme, the necessity for further provision of information and formal discussions with USS each year will place a very unwelcome additional burden on our small and already overstretched administrative staff. There are further damaging consequences to the College that could arise from a need to disclose such breaches, and the risk of further 'intervention' from USS.

It is disappointing that none of the worked examples suggest what the USS response might be to an organisation in this position.

The Aon Note of advice highlights the potential negative impacts on small employers and also states that they "have not reviewed the implications of applying the metrics and thresholds to non-HEI employers with potentially materially different activities, finances, capital structures and business models". We consider that the College falls into both categories, having an income mix and cost base that is very different from a normal HEI. Whilst it may be true that "metrics A to D, and the associated thresholds ……… are generally in line with financial covenant tests used in the sector as a whole", that is not the experience of the College for which loan covenants based on net assets and reserves are the norm.

We share the reservations expressed by Aon in relation to metric E, and consider that the proposed 5% threshold is extremely low, and likely to be a significant constraint on an institution's freedom to operate.

In conclusion:

- We consider that the monitoring process set out in section 4.2(a) of the debt monitoring framework fails to recognise the overarching importance of metric A to the overall USS covenant.
- We consider that the position of small, asset-rich, endowed institutions needs specific consideration in the framework.
- We suggest that the approach to monitoring needs to be tuned to the particular circumstances of each member institution, with the metrics weighted differently according to each institution's circumstances in a way that allows the Trustee to monitor the extent of any deterioration in that institution's covenant. If the proposed formulaic approach is pursued we fear that the consequence will simply be to increase the pressure from smaller endowed institutions to seek withdrawal from the Scheme.
- We consider that the proposed 5% threshold for metric E is too low.
- We would also like to see full transparency in the form of publication by USS to all member institutions of the full set of metrics for each employer member of the scheme.

Once again the timing of the USS consultation has fallen outside the College's governance cycle and it has not been possible to discuss and agree this response with the Governing Body of the College. However the response has been reviewed and approved by the College Committee, which is the senior Committee within the College, reporting to the Governing Body.

Please note that the great majority of the Governing Body of Fitzwilliam College have declared themselves conflicted in matters relating to USS because of their personal membership of the scheme.

Yours sincerely,

R A Powell

Bursar

Cc: Master, Fitzwilliam College