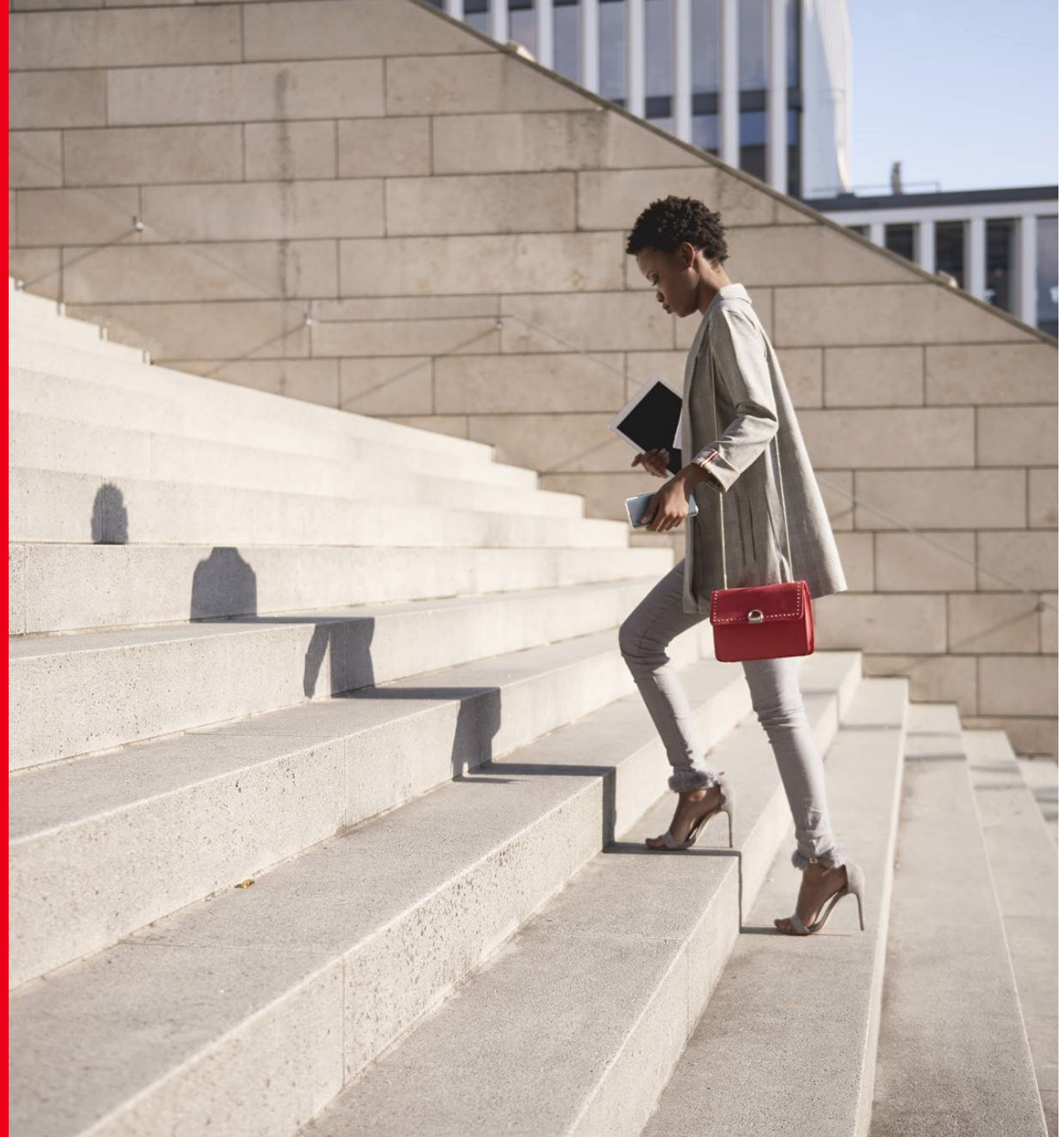

Conditional Indexation

Employer briefing

Prepared for: UCEA

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30 January 2026

Overview

UCEA and UCU have been working with support from the USS trustee to consider how to achieve greater stability in the USS over time.

As part of this work, UCEA and UCU agreed to explore Conditional Indexation (CI) which could be an alternative benefit design for the future.

CI pension schemes have been used in other countries (Canada and the Netherlands) but there is limited direct experience of CI in the UK.

Over 2025 a Working Group with representatives from UCEA and UCU prepared two reports to the JNC exploring different aspects of CI. These reports have now been published.

This presentation to employers provides a high-level overview of some of the areas covered in these reports including:

- What is CI?
- Why are we considering CI?
- What impact could CI have on member outcomes?
- How could a CI scheme be governed?

UCEA are seeking employers' views on whether there is appetite to continue exploring CI as an alternative benefit design with a view to potentially implement a CI benefit structure for future benefits in coming years.



USS history

Benefit changes

2014 valuation & 2016 benefit changes
Everyone moves to 75^{ths} CARE benefits, salary threshold introduced (£55k initially), member and employer contributions increased

1

2017 valuation
Initial results show similar deficit to 2014, but huge increase in cost of new benefits

2

January 2018
Benefit changes proposed
Move to DC for all from 1 April 2019

May 2018
Benefit change proposals withdrawn. Joint Expert Panel established to independently review approach

January 2019
2017 valuation finalised - staggered contribution increases to 2020

September 2019
2018 valuation finalised - staggered contribution increases to 2021

3

2020 valuation
Large deficit. Valuation signed off in September 2021. Contributions conditional on whether JNC recommended benefit changes made

4

April 2022
JNC recommended benefit changes implemented
85^{ths} CARE for all, Salary Threshold reduced £40K, member and employer contributions increased

April 2024
Pre-2022 benefit structure reinstated, member and employer contributions reduced

5

2023 valuation
Higher yields lead to surplus and reduced cost of benefits. Valuation concludes on expedited basis by Jan 2024 with aim for benefits to return to pre-2022 levels.

What is Conditional Indexation?

In the USS (and other UK Defined Benefit schemes) increases applied to pension (indexation) are typically guaranteed regardless of how the scheme is performing.

In the USS, the level of indexation that is applied to pension is linked to CPI inflation – every year the increase applied to pensions currently being built up is in line with full CPI up to 5% plus half the excess above 5%, up to a maximum of 10%.

In a defined benefit scheme with Conditional Indexation, the defining feature is that future benefit increases are conditional on the scheme's health.

This means

- There is a target level of indexation (for example the scheme could target increases in line with CPI each year)
- In poor market conditions there is flexibility to award increases below target (e.g. 2% when inflation is 3%)
- If conditions subsequently improve, any "missing" increases can be granted
- Once increases are given, they become part of the guaranteed benefits
- Increases post-retirement are subject to a statutory minimum (CPI capped at 2.5% p.a.)



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Why are we considering Conditional Indexation?

Whether CI offers better outcomes is considered versus four criteria

1

Likelihood of Retaining DB

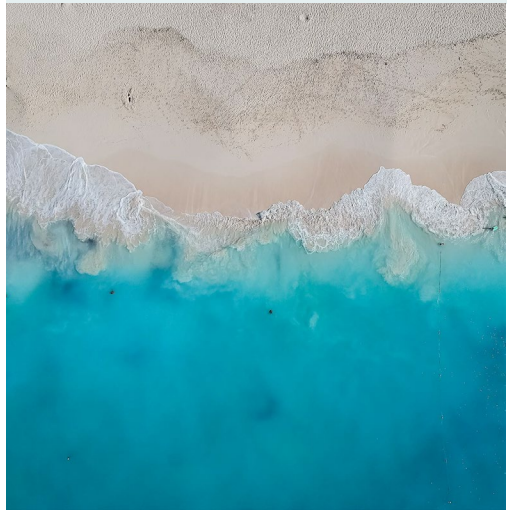
Increase the chances of retaining a predominantly DB benefit structure over the long term



2

More stable contributions for members and employers

Total contributions should be more likely to remain within an agreed range in the short-medium term



3

Higher overall benefits

Higher expected benefits in the vast majority of scenarios with acceptable outcomes in poor scenarios supported by a catch up mechanism.



4

Stability of core benefits

Achieve greater stability over time in the core level of benefit accrual (accrual rate and salary threshold)



Designing a CI scheme

There are multiple design features that can be varied in a CI Scheme.

The second report focused on Design 1 below, but similar results are possible by amending different design aspects (for example having a higher accrual rate and lower target indexation).

Design feature	Current benefits	Design 1
Accrual rate	1/75 pension, 3/75 lump sum	1/75 pension, 3/75 lump sum
Pre-retirement indexation	Guaranteed: "Soft cap" CPI*	Target: **CPI+1%** Minimum: 0%
Post-retirement indexation	Guaranteed: "Soft cap" CPI*	Target: CPI Minimum: Statutory**
Backdating of increases foregone?	N/A	Yes – members eligible for "missing" increases up to target
Salary Threshold	Current (c.£70K)	
Investment builder	20% overall contribution above Salary Threshold	

**CPI up to 5%, plus half the excess above 5%, up to a maximum of 10%*
***CPI capped at 2.5% p.a.*

Assessment criteria

When carrying out the CI modelling the designs have been selected with the assessment criteria in mind

- **More stable contributions -** All the CI designs considered were modelled with a fixed contribution rate of 20% over time i.e. the contributions do not vary from valuation to valuation
- **Higher overall benefits -** All the CI designs considered would give higher overall benefits if target indexation was awarded – the key question is what is the likelihood (for a given contribution rate) of the target indexation being awarded

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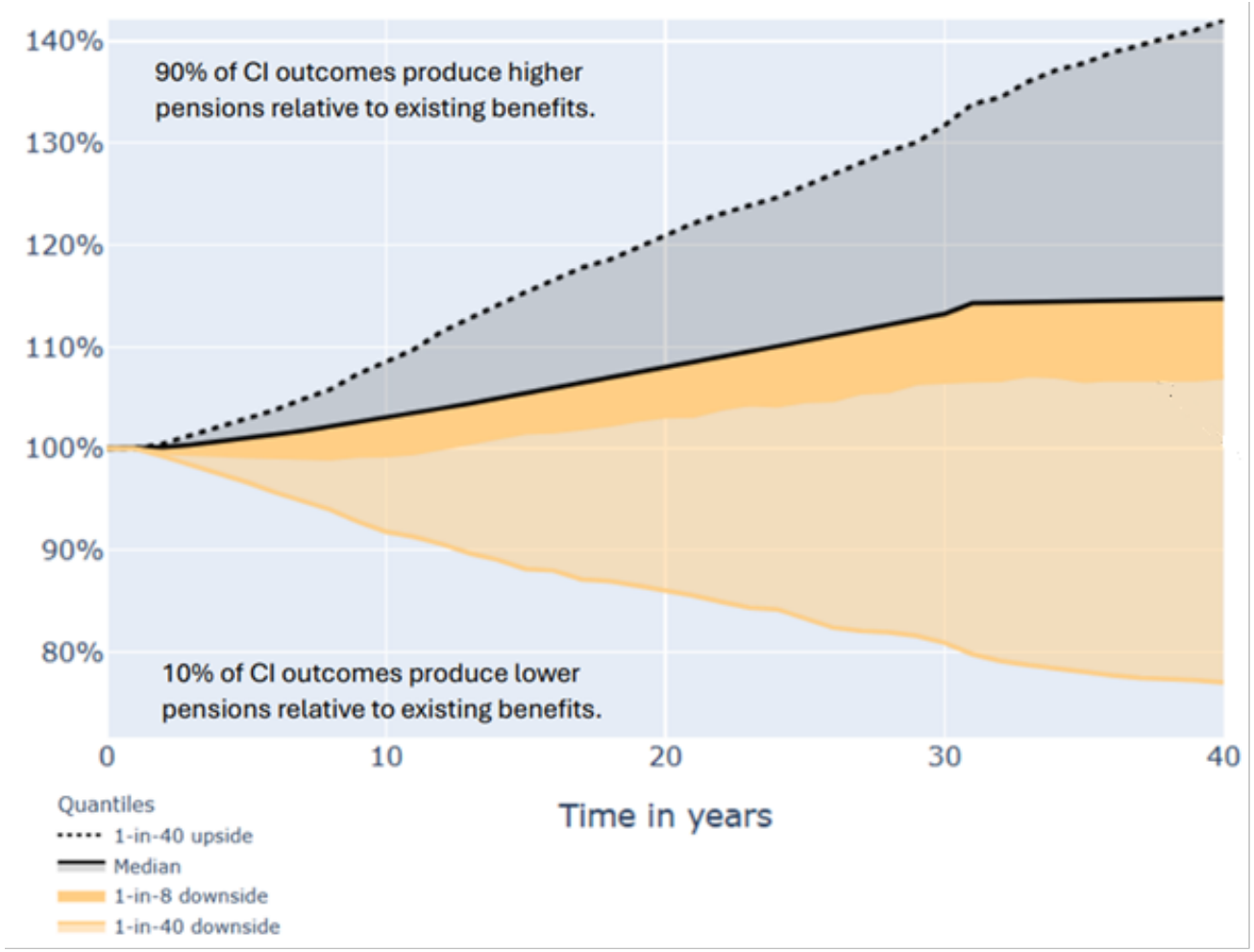
What the modelling shows

Individual modelling for a 36-year-old active member under CI Design 1



- The interim report contains stochastic modelling of individual member outcomes under the three designs comparing them to the current design
- In the Median scenario (the black line) the “Target” benefits are achieved
- The grey dashed section shows scenarios where inflation is high and the current inflation “Soft Cap” bites – so CI benefits are more generous
- The downside scenarios where CI delivers less than the current benefit structure (because target increases are not awarded) are also shown. However, these scenarios assume no changes were made to the current benefit structure
- The modelling shows that in this scenario 90% of outcomes provide higher pensions to this member relative to existing benefits (assuming the existing benefits are unchanged)

What the modelling shows

Scheme wide outcomes are considered over 60 years

Design 1	Standing Start		Steady state (Assuming current DB as starting poin	
Member outcomes				
Likelihood of members receiving less/more than current benefits	Less than current benefits	More than current benefits	Less than current benefits	More than curren benefits
	4%	96%	1%	99%
Expected level of benefit provision	86%	120%	93%	123%
Overall average level of benefits compared with current benefits	119%		122%	
CI Outcomes				
Likelihood that catch-up indexation required at some point	100%	31%	100%	22%
Likelihood that indexation below target in any given year	69%	5%	67%	4%
Funding Outcomes				
Existing structure: Likelihood average funding < 80%	76%	<1%	43%	<1%
CI structure: Likelihood average funding < 80%	30%	<1%	14%	<1%

The second report shows stochastic modelling of scheme wide outcomes for Design 1 from both a **"Standing Start"** (years 0–59) and **"Steady State"** (years 30–89, when CI is the main benefit).

Key points to draw out include

- On average, members can expect to receive **c20% more than current benefits**
- In the 4% of scenarios where CI gives less than current DB, there would also have been pressure and/or extra cost under the existing DB design.
- Once in Steady State, the chance of members being worse off vs current benefits falls.
- In the Standing Start runs, the worst negative outcomes arise when legacy non-CI benefits are under strain.
- Initial analysis shows this risk can be **substantially reduced** by ring-fencing surplus to support CI in the early years: setting aside about £1.5bn of surplus could reduce the chance of CI paying less than current benefits from 4% to under 0.5%

Evaluating CI against agreed assessment criteria

The report evaluates CI against the agreed assessment criteria

1

Likelihood of Retaining DB

Introducing CI would increase the likelihood of retaining a predominantly DB benefit structure over the long term.

Being able to award less than target indexation is a valuable additional lever when the scheme is under stress in addition to the current options of increasing contributions or reducing future benefits.

2

More stable contributions for members and employers

CI helps reduce contribution volatility for members and employers.

The modelling carried out in the report assumes a fixed contribution rate is adopted (although the power to change the contribution rate would still exist).

The existing DB benefit structure is more likely to result in a valuation that requires contribution or benefit changes than a CI structure – even if indexation is always paid at target.

3

Higher overall benefits

All the benefit designs considered in the modelling are expected to deliver higher overall benefits.

The probability of the CI structure delivers lower benefits is low, and limited to scenarios where the current structure would be under stress.

The next phase of work would involve selecting a preferred CI design, with decisions to be made about the desired contribution rate and the target benefits.

4

Stability of core benefits

CI helps achieve greater stability over time in the core benefits.

When the Scheme is under stress the first “lever” under CI would be to award indexation below target, but alternatives would still be available.

If the Scheme recovered there could also be a mechanism to “catch-up” missed indexation.

What are the risks and challenges with CI?

The report describes three key challenges for CI

1

There is less certainty for members over inflation protection

Inflation protection would be linked to investment and funding outcomes, shifting more risk to members who may receive more or less in retirement than currently. This risk may be experienced differently by different membership groups.



2

It is more complex

which means it may be harder for members to understand, and for USS to communicate and operate than the current arrangement.



3

There are trade-offs

between higher target benefits, intergenerational fairness and stability.



What are the risks and challenges?

The report also discusses various areas that would require more detailed consideration in the next phase of work

1

Risk

The levels, types and transfer of risk and reward from employers to scheme members must be understood and acceptable.

Inflation protection would be linked to investment and funding outcomes, shifting more risk to members who may receive more or less in retirement than currently.

Whether this risk is acceptable relative to the benefits and how best to mitigate would be a key question for the next phase.

2

Clear, transparent approach for managing CI

Transparent decision-making process established for determining annual CI increases, with clarity on the roles and responsibilities of different bodies.

The report explores how a CI scheme could operate under the current governance structure i.e. how the current roles and responsibilities of the Trustee and JNC could map to decision making for CI.

3

Member fairness and equity

The risk and reward trade-offs between different groups of members must be understood, proportionate and more intergenerationally fair.

Current employees and employers experience two key risks: their costs may increase or future benefits reduced. Under CI the risks of these taking place are reduced but a wider group of members (all with CI benefits) experience the risk that indexation is awarded below target. This trade-off would be further explored in the next phase.

4

Communicable and implementable

The benefit design should not be unnecessarily complex, should be capable of being clearly communicated and understood by members and employers and implemented in a way that represents good value for members and employers

This area has not been considered in detail to date but would be a key feature of the next phase of work.

Potential timeline for consideration of Conditional Indexation



Investigation

- ✓ June - Publication of interim report
- ✓ July – Employer engagement sessions
- ✓ July – UCU briefings
- ✓ Work to support the further report
- ✓ Publication of Second report

Review point / 2026 valuation

- **Q1 - CI employer engagement**
- UCU briefings
- Decide whether to investigate CI further
- Consultation on 2026 valuation
- Agree terms for continued CI development?

2026 valuation / CI development

- 2026 valuation agreed
- Development work on CI
- Employer / Employee engagement on CI design

CI development

- Development work on CI
- Employer / Employee engagement on CI design
- Agree proposed CI design for consultation

Review point / 2029 valuation

- Consultation on 2029 valuation
- Consultation on CI benefit changes

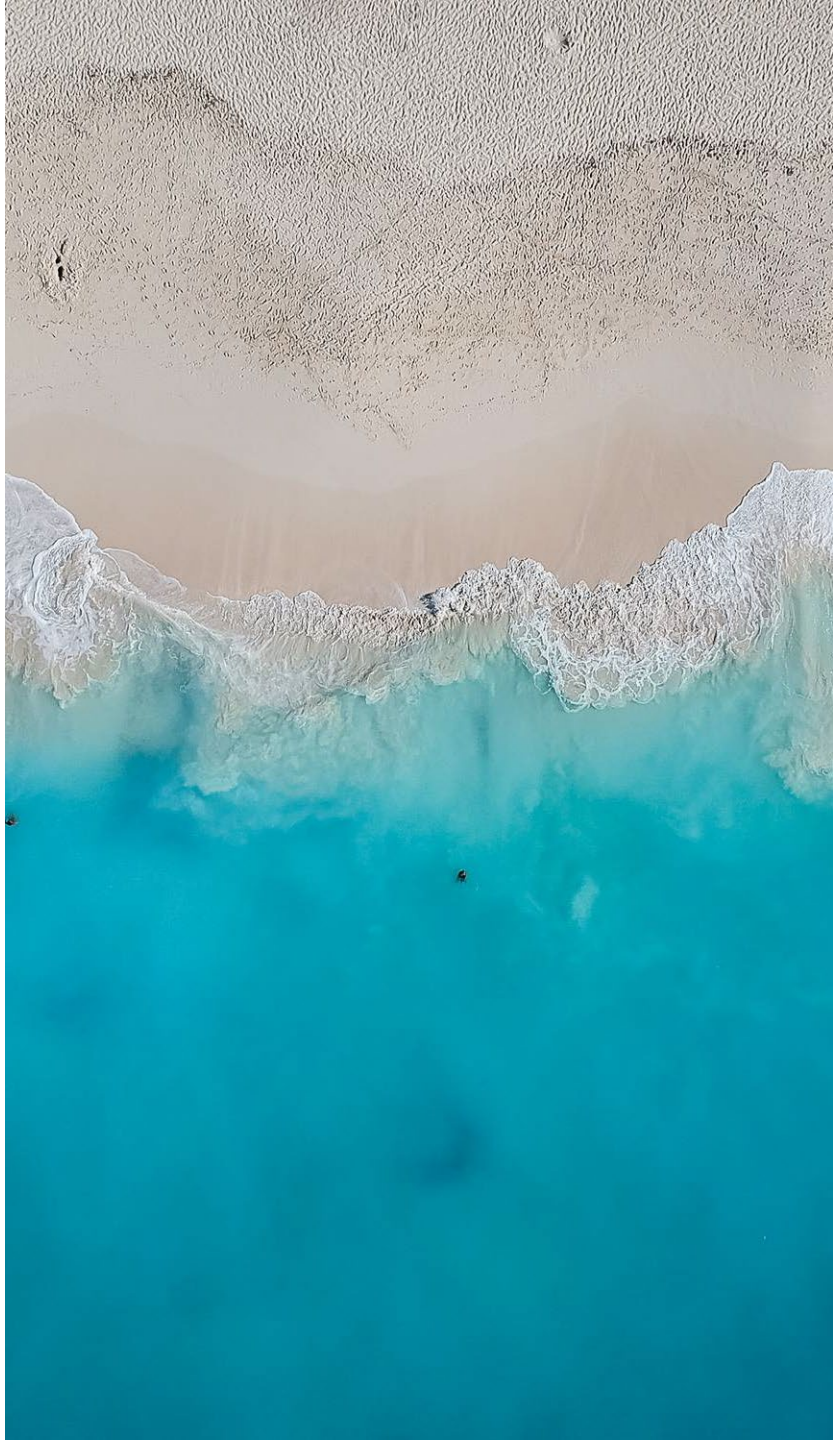
Implementation

- 2029 valuation agreed on CI basis
- CI benefits implemented

What This Could Mean for Employers

From an employer's perspective, there are several potential implications:

- **Cost and funding stability:** Conditional indexation may offer a more stable long-term framework for contributions by reducing the open-ended guarantee on future increases, provided the design and funding target are appropriate.
- **Risk-sharing:** CI changes the balance of risks and rewards between employers and members. Employers may carry less risk for future inflation increases, but that means members carry more variability in future pension awards. The fairness and acceptability of this shift will be a key point of discussion.
- **Governance and communication:** Any move to CI must be underpinned by strong governance and clear, honest communications. Members, unions and other stakeholders will need to understand how decisions are made and what this means for their pensions in different scenarios.
- **Role of employers in design:** Employers will have a central role in shaping the final design – for example, how much risk they are willing to retain; what degree of variability in member outcomes is acceptable; and how strong the commitment is to target certain levels of increases.



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