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Academies Briefing

Background

This last year has seen a significant increase in the number of schools converting to academy status and the creation of new academies.

A new academy under the 2010 Academies Act becomes a pension scheme employer (known as a scheduled body) within the Local Government Pension Scheme (LGPS) and needs to pay the cost of providing pensions to its employees.

The academy is responsible for any deficit for its eligible employees. The main issue covered in this briefing note is the pension deficit in respect of eligible employees prior to becoming academies - how it is allocated and how it is funded.

The Pensions Advisory Panel (PAP) at Southwark is a Panel made up of elected members and officers. The primary objective of the PAP is to assist the Finance Director in the management of the pensions function within the Council, and this remit covers setting Southwark's policy on such issues as funding strategy. Policy decisions regarding the treatment of new academies in the Southwark Fund therefore are discussed and agreed by the PAP. Decisions of PAP are treated as advice to the Finance Director, who is the ultimate decision maker for the Fund. The Finance Director reports to PAP where he is unable or unwilling to implement their decisions.

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Asset (deficit) allocation

Guidance from Department for Education (DFE) suggests that the shortfall (i.e. deficit) in respect of the members that transfer to the new academy should transfer to the new academy

There are a number of existing academies in the Southwark Fund and these were given a fully funded starting position (i.e. no deficit at commencement). At the time there was no guidance on this subject (the DfE briefing was only produced in 2010). A large number of authorities acted in the same way as Southwark (i.e. they provided notional asset transfers equal to 100% of the academy's liabilities).

Following the issuing of the DfE briefing in 2010 (coinciding with the Academies Act) Southwark enacted a policy change. Future academies would be responsible for the deficit existing at the start of the contract, to ensure consistency with central guidelines.

We are not aware of any Funds who are not transferring a funding deficit to newly forming academies.

There are many different, equally valid ways to allocate assets (and hence deficit) to the new academy. Communities and Local Government (CLG) and DfE guidelines are limited simply to the statement that the deficit should be transferred. Consequently different approaches have been used by different Funds and actuaries. The decision on the level of assets to allocate to the new academy is a decision for the Borough, as the Scheme employer from which the members are transferring.

Of the methods used to allocate assets to academies, the method used in the Southwark Fund at the current time is the most generous to the academy of the commonly used approaches.

The Southwark method only assigns the deficit for the active membership i.e. the staff currently employed at the academy. Alternative methods would assume that the academy also takes over the deficits for all the staff that have ever worked for the school (i.e. the staff that have left with frozen pension benefits, or are currently being paid a pension). The alternative methods would lead to the academies having significantly higher deficits

It should be noted that the notional assets that are transferred to the new academy can rise or fall in value each valuation so the past service deficit amount will change every three years (the first change being April 2014)

Funding Strategy

There are two main elements to funding strategy - the funding assumptions used and the recovery period used to calculate the contributions to make good any deficit.

The academies have been valued using the Scheduled Body funding assumptions used at the 2010 valuation which are the same as the main Southwark fund. The Scheduled Body approach is based on the principle that Scheduled Bodies have an almost infinite covenant and cannot fail in practice.

The guaranteed funding stream for academies is based on a 7 year period. Therefore, use of these 'optimistic' assumptions has currently been tempered by use of a shorter 7 year recovery period (compared to the Borough's 23 year recovery period). A number of other authorities are also using a shorter recovery period for academies than for other scheduled bodies, given the uncertainties surrounding what would happen should an academy fail. However, in exceptional circumstances (e.g. deficit repayments challenge the financial viability of the academy) the Borough is prepared to discuss the use of a longer recovery period.

The policy for the admission of academies is at the end of this briefing note.

The employers rate (which is based on future service assumptions for the active staff at the academy) can be different to the main Southwark rate depending on the membership demographic of the academy (particularly the age demographic) The employers rate for both Southwark and each individual academy will be reviewed as part of the scheme triennial valuation (the next valuation being on the 31 March 2013)

Way forward

The objectives of Southwark and of the new academy are competing. Southwark would like to ensure that contributions are sufficient to meet the deficit and are in total at least as much as before conversion of the school to minimise the financial risk to the Fund and to safeguard the interests of its employees in the LGPS and the council tax payers of Southwark/the general fund. The new academy wants the contribution rate to be no more than it was effectively paying as a school. Southwark will also want minimal impact on their long term contribution rate due to the conversion of schools to academies.

There is a direct conflict therefore between Southwark and affordability for the academy and a balance must be struck between these competing objectives that is fair and workable for all parties.

POLICY FOR THE ADMISSION OF ACADEMIES INTO THE LONDON BOROUGH OF SOUTHWARK PENSION FUND

- Academies will be given an initial past service deficit recovery period of 7 years. The seven year recovery period is linked to their guaranteed funding stream from the DfE (as set out in the statutory Funding Agreement between the DfE and the Academy Trust)

- If the individual circumstances of an academy warrant or require a longer recovery period, the period can be extended to up to 10 years. The approval of a recovery period of between 8-10 years is delegated to the Assistant Director, Strategy and Support, in consultation with the Finance Director. Such circumstances may include:
  - Where the academy has produced evidence of financial viability beyond 7 years (for example evidence of future funding streams).
  - The higher contribution rate due to the shorter recovery period is such that it causes the academy financial difficulty.

- Deviations from the policy above would only be allowed on approval of the Finance Director, in consultation with the Pensions Advisory Panel.