Local Government Pension Scheme funding for converted academies in the Surrey Pension Fund

On conversion, the new Academy assumes responsibility for the pension obligations of all active employees of the maintained school who are entitled to membership of the Fund. Responsibility for meeting any deferred or pensioner benefits for ex-employees of the maintained school remains with Surrey County Council (the Council).

The Academy is recognised as a separate employer in the Fund. The Administering Authority's role, in consultation with its actuary, is to set a starting asset position and ongoing contribution rate that reflects the risk that the Academy poses to the Fund, and which is fair to all other employers participating in the Fund.

The Academy starting asset position

Non-statutory joint guidance was issued by the Department for Communities and Local Government (DCLG) and the Department for Education (DfE). It contains broad principles about Academies assuming responsibility for a share of the past service deficit at conversion, and that funds should aim to set contribution rates that are similar to those payable by the Council. However, the guidance is high level only – the specific approach to asset allocation and contribution rate setting for Academies is not prescribed. As a result, LGPS funds have adopted a variety of funding approaches.

New Academies will be regarded as a separate employer in their own right and will not be pooled with other employers in the Fund. The only exception is when the academy is part of a Multi Academy Trust (MAT) in which case the academy's figures can be combined with those of the other academies in the MAT;

The Academy's past service liabilities on conversion will be calculated based on its active Fund members on the day before conversion. For the avoidance of doubt, these liabilities will include all past service of those members, but will exclude the liabilities relating to any ex-employees of the school who have deferred or pensioner status.

The Academy will be allocated an initial asset share from the ceding Council's assets in the Fund. This asset share will be calculated using the estimated funding position of the ceding Council at the date of academy conversion. The share will be based on the active members' funding level, having first allocated assets in the Council's share to fully fund deferred and pensioner members. The asset allocation will be based on market conditions and the academy's active Fund membership on the day prior to conversion; and

An equitable split of past service deficit is allocated to new Academies at conversion. This is achieved by allowing for the liabilities for deferred and pensioner members that are left behind with the Council to be fully funded.

At the point of conversion, the Council has a funding level of, say, 70%. This means it has £70 to cover the £100 of liabilities assumed to have arisen from the maintained school. Under this deficit allocation approach, £60 of the £70 would be held back to fund the deferred and pensioner members (since £60 is assumed to have arisen from former employees of the maintained school). This leaves £10 of assets to be allocated to the new Academy, which is only responsible for the £40 worth of liabilities relating to active members.

The approach is equitable as the assumed deficit amount is unchanged immediately before and after the school's conversion to an Academy. The pre-conversion deficit is £30 (£100 minus £70). The post-conversion deficit is also £30 (£40 minus £10). The funding level is clearly lower for the Academy (25% versus the Council's 70%) but the Academy has no responsibility for funding benefits for ex-employees as the Council retains this liability and the risk of future movements in the position relative to former employees of the maintained school.

Following its initial assessment at conversion, an Academy's contribution rate will be reassessed at each formal triennial valuation. For the period following the next formal valuation (1 April 2017 to 31 March 2020) the contribution rate will be calculated with the objective of keeping this as stable as possible taking into account a number of factors such as risk posed to the Fund and the long term nature of the academy's participation.

Support for this approach has been provided by The Pensions Ombudsman. In April 2015 the Pensions Ombudsman Service published its response to an appeal from an Academy school in the East Riding of Yorkshire Council Pension Fund. The Academy disputed the East Riding Fund's approach to asset allocation, which is to fully fund the notional deferred and pensioner liabilities of the maintained school that are left with the ceding Council on conversion to Academy status (i.e. the same approach taken by the Fund). The Pensions Ombudsman Service determined that the complaint should not be upheld, stating that the Administering Authority had reached a decision that was reasonable, and that it was empowered to do so.

The Academy ongoing contribution rate

The Academy's initial contribution rate will be calculated using market conditions, the Council funding position and membership data, all as at the day prior to conversion. Any deficit will be funded by an addition to the contribution rate which aims to eliminate the deficit over a period of 20 years ("deficit recovery period").

When setting the ongoing contribution rate of the Academy, instead of calculating contributions based on a single set of assumptions, as has been used in previous valuations, the actuary will consider numerous possible future economic scenarios when assessing the likelihood of contributions being sufficient to meet your funding obligations. The Fund has established risk covenant categories which will determine the specific likelihood of meeting the employer funding target.

By adopting this approach, the Fund is aiming to reduce cross-subsidy across employers and to reduce the risk to other employers being asked to pay off a debt left behind by a failing employer.

The categories are as follows:

- Category 1A – a tax-raising or precepting employer
- Category 1B – an employer with a guarantee from a tax-raising employer or an academy which is part of a pooled multi-academy or umbrella trust (MAT/UT)
- Category 2 – an employer with a satisfactory third-party guarantee or that can provide evidence of a strong covenant through financial or other information, and a willingness and ability to pay scheme contributions as appropriate through an independent assessment approved by the Fund
- Category 3 – stand-alone employers with no guarantee

As Academies have backing in the form of the DfE guarantee they are categorised as a Category 2 employer. Based on this categorisation, the Fund will calculate the contribution rate using the stabilisation approach and a time horizon appropriate to your expected participation in the Fund, based on an appropriate likelihood of being fully funded within this agreed time horizon.

If an academy elects to become part of a MAT/UT and if all academies participating in this MAT/UT agree to pool their risks, the Fund would change the categorisation for each academy in the MAT/UT to Category 1B. This would reflect the additional guarantee that, in the event of one of the academies failing, the remaining academies in the MAT/UT would share any debt.