Independent schools briefing, Quarter 2 2023
2020 TPS valuation: The (indicative) results are in

They say public service pensions don't move quickly, but fewer than three months after the (much delayed) response on the SCAPE discount rate consultation, HM Treasury (HMT) has provided indicative results for the 2020 TPS valuation.

Courtesy of ISBA, we understand from HMT and the Department for Education that ***"the direction of travel is in the order of 5% point increase in the employer's contribution rate".***

In this briefing we discuss why this is the indicative outcome, what it means for independent schools, and what the options are.

Why is the employer rate going up?

An increase of 5% of salaries would not be a surprise. Indeed, this is at the lower end of where the employer rate could have ended up.

The increase has been driven by the reduction in the **SCAPE discount rate**, which we covered in more detail in our Q1 briefing.

In short, the SCAPE discount rate has fallen, as it remains linked to long-term projections of economic growth (which have fallen in recent years). A lower discount rate means higher contribution rates.

On its own, the lower SCAPE discount rate could have increased the contribution rate for schools by much more than 10% of salaries.

There have been a number of offsetting factors – the slowing of improvements in life expectancy and overpayments made since the last valuation – but these have only partially offset the impact of the reduced discount rate.

At the ISBA conference in Manchester earlier this year, we put a question to delegates: From 2024, will the TPS cost for schools be higher or lower than 30% of salaries? Respondents tended towards under 30%, but being right will not make financial budgeting any easier.

When will the new rate be payable from?

The message from HMT suggests an expectation that the valuation will be finalised by September 2023. This would confirm the employer rate and effective date at that point, finally giving schools some certainty after a long period in limbo.

Official word remains that the rate will increase from April 2024, but that might not be the end of the matter. We would not be surprised to see this pushed back to September 2024 to align with the academic year – but that's not a given at this stage.

If the contribution rate increase is pushed back, there will be an additional increase in the employer rate to pay for this delay. The five-month delay in 2019 increased the employer rate by 0.8% of salaries.

Could anything change before then?

Yes. HMT has emphasised that these results are **indicative** at this stage, and so may change before the valuation is finalised. We would, however, expect any changes resulting from the calculations being finalised to be fairly small – unless there is a dramatic, last-gasp change to the valuation directions.

Another issue that could have a material impact is the High Court appeal being made by several public service unions around the treatment of the additional labilities arising from the **McCloud judgment**.

The crux of the dispute is a disagreement over the treatment of these additional liabilities under the employer cost cap mechanism (covered in our Q1 2021 and Q3 2022 briefings).

A successful appeal by the unions is likely to lead to improved benefits for TPS members and a corresponding increase in the employer rate.

A stark reminder of escalating TPS costs

As recently as August 2019, the contribution rate paid by schools was only 16.48% of salaries.

The increase to 23.68% of salaries in September 2019 represented a 43% increase in TPS costs for schools. We now have another increase in the offing.

Let's not forget that the TPS was reformed in April 2015, introducing a career average benefit structure with benefits payable from State Pension age (which is 67 or 68 for most workers today).

The executive summary of the Independent Public Service Pensions Commission's final report on pension reform in March 2011 stated that public service pensions should be "*affordable and sustainable*" and that:

"…taxpayers must be able to feel confident that risks and costs [associated with public service pensions] are shared fairly: in particular that the cost of increasing longevity is being managed and that there are safety valves in place to control future cost."

A further increase by 5% of salaries in 2024, would put TPS costs for schools in the region of 75% higher than in 2018/19.

Who would have predicted that this is where we would end up?

What about state schools?

A statement from HMT in March 2023 included the following statement:

"…the Government has committed to providing funding for increases in employer contribution rates resulting from the 2020 valuations as a consequence of changes to the SCAPE discount rate; this commitment is for employers whose employment costs are centrally funded through departmental expenditure."

This announcement from HMT suggests that the state sector will be insulated from the TPS cost increases. While extra funding for pension costs has been signposted for state schools, there are, of course, other ways to control the wider budget for the state sector.

While TPS regulations require that state schools must provide the TPS for all teaching staff, there is some flexibility for independent schools.

What are the options for schools?

While the indicative results are not as bad as they could have been, an increase of 5% of salaries is still significant and will make financial planning that bit harder.

This increased cost also comes at a challenging time for independent schools, with high inflation impacting other costs and significant political uncertainty ahead.

Schools will be busy running their financial forecasts to see whether the expected TPS cost increase can be absorbed. If not, then contingencies – such as increasing fees, selling assets, reducing staff costs and cutting back development plans – may need to be investigated, along with a review of pensions.

Our Q1 briefing looked in detail at some of the options available and timescales for change.

The financial package (salary + pension) is hugely important for and highly valued by teaching staff.

While some schools will seek to make changes, others may aim to manage finances and retain the TPS for recruitment and retention purposes.

Hybrid strategies have become popular. Schools that have already introduced a cost-control method – which may involve levying TPS cost increases on staff – may need to put in place a programme of support to help decision-making.

First Actuarial's support for schools

We help independent schools understand all the options available so governing bodies can make informed decisions and make robust plans.

We can provide all the support your school needs through a pension review project, helping you:

- Developing a pension strategy
- Design an alternative scheme
- Choose a suitable Defined Contribution (DC) provider
- Explain pensions (and any proposed changes) to affected staff in sensitive but clear and factual ways.

Find out more about **our services for independent schools**. To discuss any of the areas explored in this briefing, **contact our specialist team for independent schools**.

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