

## **NCIs' comment on Diocesan Synod Motions calling for a new 'diocesan settlement'**

### **Summary**

This paper responds to Diocesan Synod Motions under consideration calling for a transfer of £2.6 billion of financial resources from the Church's nationally managed endowment directly to Diocesan Stipends Funds.

The key points are:

- The National Church Institutions (NCIs) recognise that dioceses, cathedrals and parishes are facing considerable financial challenges.
- Work looking at the quantum and allocation of distributions from the Church's nationally managed endowment in 2026-28 to support the mission and ministry of the Church across the country will begin in autumn 2024. This will, as usual, include a thorough review of the needs and opportunities facing the Church in the context of all the competing funding obligations and demands for national church funding, alongside evaluation of how much funding can be distributed sustainably.
- To feed into this planning and recognising the particular financial challenges at this time, work involving diocesan colleagues is already underway to develop options on how best to respond to (i) the challenge of diocesan deficits and (ii) the General Synod motion seeking to improve stipends and the starting level of clergy pension, both of which have been adversely impacted by a period of high inflation.
- The significant transfer of assets proposed by the Diocesan Synod motions would not create any additional money. If this happened the Church Commissioners would immediately need to reduce their distributions to reflect the lower asset base, all other things being equal.
- In fact, given the likely impact and risks of such a proposal as described in this paper, such a move could more likely result in an overall reduction in the level of funding ultimately available to support the mission and ministry of the Church across the country.

This note also:

- Sets out the responsibilities of the Church Commissioners and Archbishops' Council in relation to stewardship of the national church endowment and funding.
- Suggests associated issues for consideration by Diocesan Boards of Finance and Diocesan Synods.
- Includes two appendices covering (1) a brief history of the Church of England's pension arrangements for clergy since a contributory scheme was established in 1927 and (2) more detail on the asset transfer proposal.

## Existing and planned National Church work around the financial and missional challenges facing the Church

1. The NCIs recognise and share the concern of dioceses and the wider Church about the financial and missional challenges faced and have commissioned a Review of Funding Arrangements (underpinned by a robust data collection exercise) to:

*Identify mechanisms to **ease dioceses' current financial stress** in a way which helps to develop the Church's **longer-term missional and financial health**, focusing on:*

- a) *The financial support of dioceses by the national Church*
  - b) *The simplification of the Church's financial systems primarily in respect of financial flows between dioceses and the National Church Institutions*
2. This work is being overseen by a Steering Group, chaired by the Chair of the Archbishops' Council Finance Committee. The membership of the Steering Group comprises two Diocesan Secretaries, a Diocesan Finance Director, the Chair of the Diocesan Secretaries and Chief Executive's network as well as NCI trustees, an Archbishops' Council Finance Committee member (elected to that Committee by the General Synod and who is also a clergy spouse) and staff. The work (which is well-progressed) will develop clear, costed, coherent proposals for reform of key financial funding flows between the National Church and dioceses.
  3. The Church of England financial system is complex and needs to be considered in an integrated way, in order to ensure the full implications of any proposed changes are understood. Therefore, time and care is being given to evaluating the available options, using a data-led approach.
  4. These proposals will inform the Triennium Funding process developing plans for the allocation of national Church expenditure from 2026 in the light of the needs and priorities of the Church. One clear need is to find ways to help dioceses to improve their missional and financial strength, recognising dioceses reported aggregate structural deficits of £30m in 2022 and forecast to increase to £50m-£60m p.a. in 2023 and 2024. The NCIs are also aware of the range of financial challenges in parishes. Although 2022 (the most recent year for which validated data is available) was the eleventh successive year in which PCCs achieved an aggregate surplus and that in only three years of this century (2009-2011) PCCs have seen an aggregate deficit, it is recognised that just over 5,000 of our PCCs (41%) individually recorded a deficit in 2022.
  5. It is too early to be specific about what changes will be proposed. Decisions about how funding made available from the national Church endowment (managed by the Church Commissioners) is used to support the mission and ministry of the Church will need to be made in the light of many competing demands and recognising the current challenges and opportunities. Key inputs to this work include recognition of the financial challenge in dioceses, the aspiration to improve clergy stipends and future pensions (the value of which have fallen in real terms in the light of a period of high inflation) and address other issues related to the wellbeing of our clergy who are vital to the mission and ministry of the Church of England throughout the country. There is also a significant desire to reduce the complexity of current funding flows and improve transparency about how monies are allocated and spent.

6. Work on developing spending plans for the 2026-28 triennium and beyond will begin in autumn 2024. In line with the usual practice, the allocation of sums available for distribution from the funds managed by the Commissioners will be reviewed in consultation with the Archbishops' Council and with the involvement of the House of Bishops. This process is carried out in parallel with a full triennial review of the Commissioners' fund by independent actuaries, which includes a comprehensive review of all assumptions including those for clergy longevity, investment returns and inflationary factors.
7. The triennium funding process is designed to agree a framework for the distribution of national funds available to support the Church's current and evolving priorities. The existence of a national fund enables strategic support to be targeted where it is most needed. Having the on-going ability to reprioritise and target the overall allocation of national funding if the situation demands, provides the Church (as a whole) with greater flexibility and security than would a one-off transfer of a quarter of the fund to multiple separate (diocesan) funds with a restricted purpose.
8. Changes made in the two most recent triennial spending plans have resulted in planned distributions to support the Church's mission and ministry throughout the country in 2023-25 being 54% more than in 2017-19. Planned core and strategic on-going distributions (those which are expected to continue for the long term) have more than doubled over that period. Non-pensions distributions have grown by three-times the rate of inflation over the 15 years through to the 2023-25 funding plan. The 2023 triennium funding plans amount to £400m per annum, £1.2bn over the 2023-25 triennium, and the Church Commissioners indicated their aim to maintain this level over the next two triennia – a total of £3.6bn over nine years (2023-31).
9. This growth in distributions has been achieved through a mix of strong investment performance, rigorous review of actuarial assumptions and a broadening of the principle of inter-generational equity to include qualitative as well as quantitative considerations. This, for example, enabled the significant fixed-term funding of the net zero programme which is expected to deliver benefits for future generations as well as help the Church work towards the aspiration to achieve net zero by 2030 set by the General Synod.
10. In response to the needs of the Church at the time, the distribution of monies from the Church's national permanent endowment has included a significantly increased level of strategic funding to support diocesan plans in support of the Church's Vision and Strategy in their parishes and communities in ways most appropriate to the local context of each. It has also released specific support towards the cost of ordinands, curates and clergy moving into Posts of First Responsibility (largely incumbents).
11. These spending plans built on pre-existing national Church funding for dioceses through Lowest Income Communities grants support (distributed to 29 dioceses to help fund the cost of mission and ministry in the most deprived areas), meeting the full cost of diocesan bishops' ministry and funding towards the cost of suffragan bishops, deans and other cathedral clergy.
12. Between the implementation of the financial settlement that was agreed in 1997 and the end of 2024, the Church Commissioners will have distributed £6.0bn in support of the Church of England's mission and ministry across the country. This comprises

£3.0bn in respect of clergy pensions (for service pre-1998), £0.1bn of transitional relief to meet pension contributions which would otherwise have been met by dioceses and £2.9bn for purposes other than pensions, some examples of which have been given above.

13. Although the above sums are significant, it is recognised that around two-thirds of total Church of England income originated in its parishes and that giving accounts for around two-thirds of parish incomes. The Church of England's worshipping communities are at its heart and are key to addressing its missional challenges, of which its financial challenges are a symptom.

### **Likely impact and risks of transferring assets**

14. The Diocesan Synod motions call for a transfer of assets from the Church Commissioners' managed endowment fund to the Diocesan Stipend Funds held by each diocese. The first point to make is that transferring assets from the management of the Commissioners to the management of Diocesan Boards of Finance, or any other Church entities, would not create additional money and indeed risks reducing the sums available to support mission and ministry. It would simply be moving the oversight and management (both for investment and distribution) of the funds in question.

#### *Investment*

15. In practice, such a move is likely to lead to less money in aggregate being available to the Church from its investments and this detrimental impact would be expected to increase over time. There would be significant one-off costs involved in realising around a quarter of the funds under the Commissioners' management (which could include being forced sellers of some assets at prices below valuation) and costs to establish new arrangements. Future investment returns (both for the Commissioners and for dioceses) may be impacted detrimentally compared with the current arrangements and on-going investment management costs are likely to increase with more fragmented asset management arrangements. A significant decline in the Commissioners' fund size is also likely to have an impact on their ability to continue to attract talent within their investment team, which could in time also impact the funds' performance
16. The Commissioners would be more constrained in how their assets could be invested in the future, with a smaller fund and a relatively higher share of 'non-discretionary' (or 'statutory') distributions. This would be likely to result in a sub-optimal asset allocation leading to lower prospective future returns and hence reduced distributions.
17. Monies for existing planned distributions and any called-for transfer of investments would largely have to be realised through the sale of the most liquid assets, resulting in the portfolio becoming unbalanced and leaving the fund overly reliant on illiquid assets in the short term. This would increase the risk of the fund not being able to meet planned distributions on a sustained basis. Over time, a higher proportion of the fund would need to be held in relatively low returning cash and cash like assets so that the Commissioners could be sure of meeting their distribution commitments and existing investment obligations.

18. Each diocese would need to decide how to invest any funds transferred. Any such arrangement would be likely to be more costly than the current arrangements. It would also be unable to replicate the Commissioners' asset allocation with the resulting benefits of diversification and access to investment opportunities that only a fund of significant scale can invest in such as infrastructure, private equity and timberland.
19. It has been suggested that if such a transfer were to take place, the Commissioners might be asked to manage the assets for some or all dioceses. This would require the Commissioners to be regulated by the Financial Conduct Authority (FCA), resulting in additional cost and complexity (as each diocese would have to provide the Commissioners with instructions on their investment strategy and liquidity requirements rather than the current approach of focussing on one fund with a single strategy and target).
20. It would also probably generate lower returns as a result of increased complexity (managing funds for many clients) and a loss of investment focus. Returns for each diocese would vary depending on their instructions and asset performance. Overall it is likely that a greater proportion of Church assets would end up held as cash (or equivalent lower-returning assets) to facilitate responding to the liquidity requirements of over 40 clients.
21. The Commissioners' credit rating would be reviewed with a high likelihood of a downgrade given higher gearing which could breach committed levels and undermine the impression of robust governance and financial planning which underpin the Credit Rating and the Commissioners' listed Bond programme. This would reduce/remove the ability to issue further bonds as part of the overall investment strategy and indeed such a significant unplanned distribution might lead the Commissioners to consider it necessary to buy back the existing bonds – which would incur a significant financial penalty – from a financial, reputational and integrity perspective. (The Listing Particulars for the £550m of bonds issued in 2022 included information of planned future distributions as a proportion of assets.)

### *Distribution*

22. If funds were transferred to dioceses, the Commissioners would need to immediately reduce their distributions to reflect their lower asset base. All other things being equal, based on the end 2021 full actuarial review on which the spending plans for 2023-25 and indications for the following six years were made, this would require the immediate end to all "strategic on-going distributions": around £70m a year in 2022 money terms (planned to grow at an inflationary factor), the majority of which funds the Strategic Mission & Ministry diocesan investment programme which seeks to support dioceses in their plans to support and develop existing ministry as well as new initiatives.
23. Given the motion's supposed linkage to pension contributions paid since the start of 1998, it may be assumed by those considering the Diocesan Synod Motion that any funds distributed to dioceses under the proposed 'settlement' would be allocated in proportion to clergy numbers (or pension contributions paid) over the period since then. This would be a very different approach than typically used when making decisions over the distribution of the Church's funds held nationally, where a key factor has been to consider relative needs and resources. Distributions by the

Commissioners and Council from the national endowment seek to ensure a fair and equitable distribution method, aligned with the inter-generational equity principle and the responsibility to support mission and ministry in the poorest communities, which could result in a very different outcome to the one some dioceses might expect.

24. Were there to be a new 'settlement', each diocese would need to decide how much to distribute from any funds transferred. This might result in higher (or lower) distributions in the short term. But increased distributions in the short term would lead to fewer assets held by dioceses to support future distributions. In which case the medium to longer term distributions would be lower than they would otherwise have been. And of course, not all dioceses may be welcoming of the proposal which would only be workable if it applied to all.

### **The responsibility of the Church Commissioners and Archbishops' Council**

25. If the General Synod were to pass a Diocesan Synod motion calling for a redistribution of financial resources currently managed by the Church Commissioners to DBFs or other Church entities, it would not be binding on the Commissioners. The Board of Governors of the Commissioners would, under charity law, remain under the same duty to act prudently in the best interests of their charity: they cannot be directed by the Synod in how they carry out their functions.
26. It is likely that primary legislation would be required to achieve any such redistribution. If the General Synod were to pass the Diocesan Settlement resolution, the Archbishops' Council would need to consider whether to introduce such legislation. It seems unlikely that the Council would do so if the Commissioners (and indeed Council) were strongly opposed, given the arguments outlined in this paper.
27. Legislation would also require Parliamentary approval. Parliament took a strong interest in the work that led to the Pensions Measure 1997 that established the funded clergy pension scheme and gave the Church Commissioners a time-limited power to meet clergy pension payments from capital. Parliament has maintained its interest in the outworking of this arrangement, including by insisting that the Commissioners continue to seek a renewal of this power every seven years. In January 2024, when a Measure extending this power to the end of 2032 received the Royal Assent, a significant change in the use of the Commissioners' funds was not envisaged.

### **Summary**

28. This paper is offered as a contribution to any discussions on this issue by DBFs and Diocesan Synods. It is hoped that this will avoid potential misconceptions.
29. The most important point is that the proposed new 'settlement' would **not create additional resources, rather simply move funds from one place to another**. In fact, **it is likely that overall over time it would reduce available resources for the Church** with less efficient investment strategies, fund management arrangements/costs and potential adverse consequences for the funds remaining under the Commissioners' management to the detriment of the wider Church of England.

30. The proposal would run counter to the original principle that today's mission and ministry should be funded by today's giving, which was the underpinning of the strategy that took effect from the start of 1998. This principle remains fundamental when it comes to long-run financial sustainability for the Church of England.
31. The suggestion that since the change in pension funding arrangements there has been a transfer of assets 'from dioceses' and 'to the Church Commissioners' is erroneous. It is based on two separate trends which are not connected, and the resulting changes in balance sheets are not in any meaningful sense a 'transfer' from one part of the Church to another.
- the investment performance of the Church Commissioners, which has enabled the assets held by the Commissioners on behalf of the Church to grow substantially and hence has enabled significant increases in the distributions by the Commissioners to the Church.
  - the decline in congregations, and the subsequent lack of growth in income, in all dioceses, which has made it harder for dioceses to sustain the full costs of the clergy that are deployed in those dioceses.
32. In any case, we consider that the analysis which arrived at the proposed £2.6billion transfer is flawed. It focuses on pension contributions paid by dioceses since 1998 (compounded at an assumed rate of potential investment returns over that period), describing this as the cost of 'disendowment' from DBFs/PCCs to establish the Church of England Funded Pension Scheme (CEFPS). It makes no allowance for distributions paid by the Church Commissioners to Dioceses over that same period - had the Church Commissioners continued to meet the cost of clergy pensions after 1998, they would not have been able to make anything like the same quantum of considerable non-pensions related distributions to dioceses and the wider Church (estimated to be £2.9bn over 1998-2024 in addition to pension payments of £3.0billion and £0.1bn of transitional relief to meet pension contributions which would otherwise have been paid by dioceses) that have been made instead.

## **Conclusion**

33. Representatives from the Church Commissioners and / or the Archbishops' Council would welcome the opportunity to address Diocesan Synods if they are considering any motion concerning the potential transfer of assets from the Church's national endowment (managed by the Church Commissioners)
34. The Church Commissioners and the Archbishops' Council (in partnership with sisters and brothers around the Church) look forward to continuing to support the work of the Church of England through its parishes, dioceses, cathedrals and other entities and participating in discussions how this can be best achieved. This is in line with guiding principle in section 67 of the Ecclesiastical Commissioners Act 1840 which has served the Church well for almost two centuries that "additional provision shall be made for the cure of souls in parishes where such assistance is most required, in such manner as shall be deemed most conducive to the efficiency of the Established Church".

### The Church of England's clergy pension arrangements

1. A compulsory contributory pension scheme for the clergy was first established in 1927. Active clergy paid 3% of their income to the newly created Church of England Pensions Board which managed and administered the scheme. The Church Commissioners did not pay for these pensions. Before that there were only very limited arrangements for pensions: clergy only retired if they had the means to do so. It was more usual for clergy "to hang on to the end, and employ a curate or curates."<sup>1</sup>
2. Occupational pensions are regarded as a form of deferred pay. So invariably pension contributions are paid by the organisation paying the office holder or employee, by the office holder or employee themselves or by a combination of the two. So, it could be regarded that the Church Commissioners funding clergy pensions (which was only the case between 1954 and 1997) was an exception from the general rule.
3. During the period the Commissioners had responsibility for clergy pensions, significant improvements to the pension package<sup>2</sup> were agreed by the General Synod. These changes increased the Commissioners' obligations which at the time were not costed by actuaries - their services had been dispensed with a few years after the 1954 transfer. Therefore, in the absence of a robust actuarial assessment of affordability, the extent of the obligations the Commissioners were building up was not fully understood.
4. By the early 1990s, the increased pension commitments and significant increase in the range and level of support for other parts of the Church – mainly dioceses and cathedrals – meant that, if the prevailing commitments had been maintained, the Commissioners' fund was broadly committed twice over. After widespread consultation with beneficiaries, General Synod and Parliament, this led to the decision, brought into effect by the Pensions Measure 1997, to create a funded clergy pension scheme and reduce the level of grants to a sustainable level, preserving the ability of the national Church to make strategic grants based on the prevailing and evolving needs and opportunities facing the Church as a whole.
5. The option of the Commissioners becoming solely a pension fund was considered and rejected. There was widespread agreement that the optimal way forward was to preserve national funding for certain aspects of the Church's work, such as bishops and cathedrals, and strategic, targeted, flexible funding for parish mission and ministry.
6. By the end of 1997, actuaries had calculated that just over half the fund managed by the Commissioners was expected to be paid out to meet their pension obligations with the remainder available to fund distributions to support the evolving priorities of the Church. As clergy pensions have been paid out to pensioners since that time, this proportion has gradually reduced (as expected) - at the time of the last triennial

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<sup>1</sup> Temporal Pillars, GFA Best (1964)

<sup>2</sup> Most notably, the 'three aspirations' of the 1980s which: (i) increased the full service pension to two-thirds of the national minimum stipend, (ii) increased the surviving spouse pension to two thirds of the pension and (iii) increased the retirement lump sum to three times the initial pension.

assessment, it was evaluated that around 14% of the fund was required to meet the Commissioners' remaining pension obligations. Similarly, as hoped, the remaining half of 'the 1997 fund' has grown in size enabling a very significant increase in the level of distributions for the benefit of the wider Church (as described earlier).

7. When the Church of England Funded Pension Scheme (CEFPS – often referred to as the clergy pension scheme) was established at the start of 1998, it was agreed that it was important that the scheme remained non-contributory for clergy. Thus, in line with the deferred pay principle, contributions have been paid by the Responsible Bodies, of which there are over 200. Over 90% of the pension contributions are paid by dioceses, reflecting their responsibility for funding clergy remuneration. The National Church Institutions (NCIs) pay 5% of contributions – mostly the Church Commissioners through paying contributions for bishops and most cathedral clergy.
8. In respect of the clergy pension obligations arising from service to the end of 1997 - which remain the Commissioners' responsibility - between 1998 and 2024, £3.0bn will have been paid out. In addition, as well as paying pension contributions for clergy whose stipends they fund (bishops and most cathedral clergy), the Commissioners have provided £0.1bn of transitional relief to meet pension contributions which would otherwise have been met by dioceses.

### The asset transfer proposal: more detailed comments

1. The supporting paper behind the Diocesan Synod motions suggests that if DBFs had not paid clergy pension contributions since the start of 1998 and had instead invested equivalent sums in the CBF Church of England Investment Fund, the aggregate value of those investments would now be worth in the region of £2.6 billion. It then asserts that this represents a transfer of assets from DBFs and PCCs to the NCIs, whereas in reality those funds are now held in the Church of England Funded Pension Scheme to meet clergy pension obligations arising from service since 1998 (apart from those which have already been paid out to clergy pensioners) – they are not ‘benefitting’ the NCIs as such.
2. Over the same period, the Church Commissioners has used its investment assets to meet clergy pension obligations arising from service until the end of 1997, to make other distributions (which have grown significantly in that time as noted earlier) to support the Church’s mission and ministry and to underpin such distributions continuing in the future having regard to its status as a permanent endowment.
3. The £2.6 billion is a notional figure. We are told that it is based on pension contributions paid by DBFs<sup>3</sup> from a variety of income sources over the period since 1998. Parish share is likely to have been the main income source, but no doubt asset sales will have been part of the funding picture, as will diocesan investment income and parochial fees.
4. The inclusion of investment return to calculate the £2.6 billion figure is hypothetical, illustrating the retrospective result of a particular potential investment choice. It is not stated to what extent, if any, the illustration has taken the use of investment returns into account. If the return of the CBF funds had been different over the period, that number would be different. As the assessment is a retrospective view, it makes no allowance for risk.
5. The analysis takes no account of Commissioners’ distributions. Across 1998-2024 it is expected that £3bn will be distributed for purposes other than pensions – much of which has been used to pay grants to dioceses. Such grants would necessarily have been significantly lower had the Commissioners funded clergy pension contributions instead of DBFs. The net figure will be very different for each diocese – in some cases, the grants received by a diocese might even have been materially similar to the pension contributions that they paid. And as noted earlier in the paper, the Church Commissioners also paid £0.1bn in transitional relief to dioceses to help with the payment of pension contributions and £3bn in pensions relating to service prior to the funded scheme being established.

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<sup>3</sup> Although DBFs have made the large majority of contributions into the scheme since the start of 1998, pension contributions are paid by over 200 Responsible Bodies. The analysis does not take the contributions of other Responsible Bodies into account.