

Bath & North East Somerset Council		
MEETING:	AVON PENSION FUND COMMITTEE	
MEETING DATE:	26 SEPTEMBER 2025	AGENDA ITEM NUMBER
TITLE:	FUNDING STRATEGY STATEMENT 2025	
WARD:	ALL	
AN OPEN PUBLIC ITEM		
<p>List of attachments to this report:</p> <p>Appendix 1 – Funding Strategy Statement</p> <p>Appendix 2 – Responses to Funding Strategy Statement Consultation</p> <p>Appendix 3 – SAB guidance checklist</p>		

## **1 THE ISSUE**

- 1.1 The Local Government Pension Scheme (LGPS) regulations require each administering authority to prepare and publish a Funding Strategy Statement (FSS). The FSS sets out the key assumptions which the actuary has used in preparing the actuarial valuation and, in those cases where the Administering Authority has some discretion, the policies adopted by the Administering Authority. The Committee approved a draft FSS at its meeting on 27 June 2025 which has been circulated to the employing bodies for comment.
- 1.2 An updated draft FSS is attached as Appendix 1 which, after consideration by Fund Officers and the Actuary, takes into account the comments received from the employing bodies following the consultation period. The Actuary will attend the meeting to discuss the comments and any changes to the draft FSS.
- 1.3 As the body responsible for agreeing the Funding Strategy, the Committee must consider the FSS within the regulatory framework;
  - a) Ensure that the benefits paid out in the future will be reasonably met (the Solvency Objective)
  - b) That the amount paid in annually covers the current cost of the pension benefit accrued
  - c) That current pension debt is not deferred for future generations to fund (the Long-Term Cost Efficiency Objective).
- 1.4 Given the FSS includes regulatory/legal matters/technical updates that are yet to be confirmed, delegated authority is requested for Officers to finalise before 31/03/26 having taken advice from the Actuary.
- 1.5 Individual employer results will be disseminated from late October. Meetings will be held with employers to explain the outcome as required.

## **2 RECOMMENDATION**

The Committee:

- 2.1 Notes the feedback responses received, and the proposed amendments to the FSS.**
- 2.2 Approves the FSS as set out in Appendix 1, subject to the insertion of information which can only be included when the actuarial valuation is complete.**
- 2.3 Delegates the refinement and finalisation of the FSS to Fund Officers, with assistance of Fund Actuary.**

## **3 FINANCIAL IMPLICATIONS**

- 3.1 The actuarial costs for reviewing the FSS is included in the 2022 actuarial valuation fee and is provided for in the 2025/26 budget.

## **4 THE REPORT**

- 4.1 The LGPS regulations require each administering authority to prepare and publish an FSS. The key points of the regulation for the FSS are as follows:
  - After consultation with all employing bodies, the administering authority must prepare and publish their funding strategy
  - In preparing the FSS, the administering authority must have regard to:
    - (i) FSS guidance issued by MHCLG in January 2025
    - (ii) The Investment Strategy Statement (ISS) under Regulation 12 of the LGPS (Management and Investment of Funds) Regulations 2016
  - The FSS must be revised and published whenever there is a material change in either the policy on the matters set out in the FSS or ISS.
  - The Fund's actuary must have regard to the FSS as part of the valuation process.
- 4.2 The FSS sets out all the key assumptions which the actuary has used in preparing the actuarial valuation, together with the Administering Authority's policies in the areas where the Administering Authority has discretion to manage the funding position of the Fund.
- 4.3 Procedurally, the Fund's actuary cannot finalise the valuation until the FSS has been approved by the Committee.
- 4.4 There are outstanding technical (and potentially regulatory) matters that will need to be included in the FSS which may affect the contributions and /or funding policy (e.g. review of the termination policy assumptions and the finalisation of the ill health and death in service captive premiums). These will be resolved as the valuation progresses. As these are technical in nature, it is recommended that Officers are given delegated powers to finalise the FSS having received full advice from the Actuary, should there need to be any changes as a result of further development on these or similar matters.
- 4.5 As per in previous valuations, it is reasonable to assume that the FSS will be reviewed before the next valuation in 2028 – for example if New Fair Deal comes into force. Any revisions will be brought to Committee for full consideration.

- 4.6 The draft FSS was circulated to the employing bodies with comments required by 22 August 2025. Those comments which have been received are summarised in Appendix 2.
- 4.7 The Pension Board confirmed that the draft FSS complies with the LGPS regulations and MHCLG guidance following their meeting on 2 September 2025. The Fund's checklist of compliance is provided in Appendix 3.
- 4.8 The comments received via the consultation were considered carefully and it has been concluded that no fundamental changes to the draft FSS are required (other than to update the technical information as the valuation progresses) as it was felt that the framework covered the issues raised and there was sufficient flexibility within the FSS to address the points raised where appropriate.
- 4.9 The draft FSS for approval is attached as Appendix 1, which includes estimates of certain information that can only be confirmed once the valuation and associated analysis has been completed. Once the valuation is finalised, the FSS will be updated and published. For admissions and exits, the 2025 FSS actuarial assumptions will be effective from 1 April 2026. This is consistent with our current policy.

## 5 COMMENTS ON RESPONSES FROM EMPLOYING BODIES

5.1 The consultation asked specifically for comments about:

- a) The appropriateness of the assumptions and in particular those that relate to them e.g. the pay increases they expect to award over the next few years?
- b) In relation to the affordability of contributions and in particular whether there is any particular year over 2026/2029 which will be more challenging. This will help us form a view on any further flexibility required.
- c) Additional comments or feedback employers wanted to make on specific areas of the FSS such as the assumptions or the policies.

5.2 The responses are summarised by employer in Appendix 2. They highlight the funding pressures in the public sector. The main themes are summarised below with a response from the Fund to each:

- a) **Surplus policy - approach: mixed responses have been received in relation to the use of a surplus reserve and the policy. Two employers challenge the reserve approach, including requesting contributions are reduced in line with current fund surplus/a lower surplus reserve for tax-backed employers and proposing employers are given flexibility to manage surplus as part of the management of their reserves. Other employers have welcomed the surplus approach as a means to support long-term stability and cost efficiency.**

Officers and the Actuary are aware of the cost pressures facing all employers and the uncertainty of funding/support from government. The FSS builds in flexibility and officers have discretion to flex the funding plans further within the 3-year valuation period at the employer level. The aim of the surplus reserve approach is to support longer term sustainable contribution reductions which in turn supports intergenerational fairness for taxpayers who underwrite pension costs. The surplus is retained in the Fund for the future benefit of employers. Whilst the current cost pressures are clear, there is currently no strong evidence to support the position will materially improve in the future and a greater step down in contributions at the current valuation increases the risk of a greater step increase at a future valuation. Fund officers will continue the dialogue with employers on

affordability so that this can be factored into monitoring against the Fund's objectives.

The Fund considered whether to adopt a higher surplus reserve for non-tax-payer backed employers but on balance felt the 105% level was appropriate for these employers also, taking into account the introduction of this new policy. However for closed and/or exiting employers the surplus reserve is higher, and reflects the termination funding level for that employer, such that surplus is not returned if the employer is in deficit relative to their termination basis.

The Fund has taken actuarial advice and considered scenario analysis, stochastic analysis looking at the potential progression of surplus over time and likelihood of contribution increases longer term as well as current employer affordability requirements and given consideration to key systemic risks such as climate risk in formulation of the approach for the 2025 valuation. After consideration of feedback received, the Fund remains of the view that the proposed balance of cost versus risk (both current and longer-term), built into the surplus policy and wider funding approach, is appropriate. This will be monitored in the inter valuation to ensure that the current funding plan remains sustainable in the longer term.

- b) **Surplus policy – clarifications:** (i) clarity has been requested on when deficit funding is triggered (i.e. below 100% funding level or below 105% funding level); (ii) There has been challenge to the restriction that prevents pre-payments for employers in surplus (iii) The approach for MATs that are not currently pooled has been queried: whether the past service can be pooled so that surplus in one academy can be used to mitigate the need for deficit contributions in another, whilst at the same time retaining individual future service contribution rates based on individual employer member profiles.

- (i) The main body of the FSS (page 24) sets out

“If the funding level of an employer is below 100% at the valuation date (i.e. the assets of the employer are less than the liabilities), a deficit recovery plan needs to be implemented such that additional contributions are paid into the Fund to meet the shortfall.” However, an additional statement within the surplus policy itself to clarify this point will be added.

- (ii) The Fund has opted to restrict pre-payments where an employer is in surplus as the costs outweigh the benefits of the approach. There is a significant practical administrative complexity of managing prepayments due to uncertainty in estimating contributions that are linked to a percentage of pay which will be the basis for contributions where there is a surplus as well as future service contributions. Where prepayments that are linked to a percentage of pay are made, then a “true-up” at the end of the year needs to be made based on actual pay to comply with regulatory requirements. For employers in deficit the situation is different as deficit contributions are fixed £s amounts so known in advance with certainty. Also, in the current environment of higher borrowing costs for employers and lower reserves/affordability, the financial benefit of offering the discount for pre-payments is generally expected to be much lower than in the past for all employers. For both these reasons we believe the cost/complexity vs versus benefit to employers is much diminished so the facility will be restricted going forward.

- (iii) Whilst the surplus reserve is retained in the Fund, it is retained on the employer's notional balance sheet for the benefit of future contribution

smoothing for individual employers. The rationale for pooling is that this is a shared risk approach whereby all academies in a trust pay the same rate for past benefits and future benefits building up. A quasi approach to pooling could create inequalities in terms of how risk is distributed and how costs are met across the trust that contradict the principles of pooling. For example, the quasi-approach could mean that an employer with younger members has the benefit of the lower future service rate (reflecting the younger age profile) but then the higher risk associated with younger members (as they are being funded over a longer time horizon which is more uncertain) is pooled with other employers in terms of deficit contributions/surplus off-sets. It can also create operational complexities.

We are not aware of a quasi-approach to pooling being made available by other Funds and it is not something the Avon Fund would be looking to offer. The Fund already offers the option for full academy trust pooling i.e. sharing of cost right across past and future benefit calculations, and if concerned about an individual employer surplus reserve then the MAT and constituent academies could opt to fully pool which would deal with this issue.

- c) **Pay/inflation increases:** Comments are generally supporting a slightly lower salary increase assumption over the next three years with more uncertain outlook longer term, although generally anticipated to be below the assumption. There has been a mixture of both challenge and agreement for the long-term salary and inflation assumptions in responses provided.

The valuation is using an average real salary growth assumption of 1.5% p.a. above inflation, and this includes allowance for promotional pay scales. This translates into a long-term assumption of 4.1% p.a. for employers on the higher risk funding strategy and (reflecting inflation hedging) 4.6% for ongoing employers in the lower risk strategy, with no short-term pay adjustment. Employer feedback received has been in respect of employers in the higher risk strategy so 4.1% p.a. assumption. Feedback would support a short term pay assumption of 3% or 3.5% over the period to the next valuation, although there is less visibility longer term. However, in general, the proportion of liabilities linked to salary increases is diminishing and this means the impact on the average funding level of making a short-term pay adjustment of this magnitude would be less than 0.5% on the funding level (and nil in many cases). The salary increase assumption does not impact the future service contribution rate as these liabilities are not linked to final pay at retirement or leaving. Therefore, making no short-term adjustment seems reasonable but where an employer demonstrates affordability challenges then there is discretion within the policy to adjust funding plans on these grounds where evidence is provided.

- d) **Guarantee of last resort:** request for clarification

Further detail has been requested by DfE regarding the practical meaning of 'guarantor of last resort,' including its implications for employer contribution rates and deficit recovery periods. How is risk applied under a 'guarantee of last resort' compared with the treatment of a full guarantor.

This is covered in the FSS under pages 29 and 30, the termination policy in Appendix G and also the Glossary. However an update to the wording in the FSS has been made to provide further clarity, to rename it 'guarantor of exit debt' as well as referring to instances where the guarantor is not a Fund employer e.g. DfE. The Fund will also respond to DfE to ensure the relevant points have been understood.

**e) Overall approach and ongoing review**

Employer feedback has been supportive of the Fund's engagement and consultation approach including acknowledgement by one employer of the valuable introduction of the explanatory video for 2025 and a helpful layout of the FSS document itself. Supportive comments have also been received by one employer about retaining ongoing review of the discount rate in light of geopolitical and market volatility, with consideration of sector specific experience where possible. One employer requested an annex with details of the statistical methods shown for future employer consultations however it is the Fund's view that this is likely to be too technical for most readers and risks detracting from the headline messages.

**f) Employer covenant: request for transparency on approach and right of appeal and a guidance note to accompany the notifiable event framework**

The Fund's covenant policy aims to be broad to cover the range of information and circumstances when covenant review will be undertaken and this will need to vary depending on the circumstances for which the review is being undertaken. As such too much prescription here would not be appropriate. In addition, the Fund's other policies including for deficit contributions and surplus set out how affordability and employer type is taken into account in determining contribution requirements and it is the Fund's view that this provides sufficient detail balancing the need also to retain flexibility to deviate from the approach where circumstances require. The appeal process is covered in the context of the determination of exit credits in the FSS Termination Policy. However, we have also added additional wording regarding the general right of appeal of a Fund decision within the main section of the FSS with a link to the Fund's disputes policy and also inserted a link to the disputes policy within the termination policy.

In relation to the notifiable events framework, a note has been added upfront to highlight that employers will be notified if the events framework applies to them. The need for a checklist or guidance note around notifiable events will be considered on a case-by-case basis, given the notifiable events framework is usually introduced for employers as part of a wider discussion around a particular event or circumstance in any case.

## **6 PRELIMINARY WHOLE FUND RESULT**

- 6.1 The final actuarial outcome will be reported to Committee at March 2026 meeting and will take into account various refinements to individual employer results e.g. relating to ill-health and death in service captive premiums. The preliminary whole Fund results (based on the proposed assumptions to assess solvency and future service plus updated demographic assumptions) are set out below:

	£m
Assets	5,788
Liabilities	5,450
Surplus	338
Average Funding Level	106%
Average Employer future service contribution rate	16.4% p.a.

## **7 RISK MANAGEMENT**

- 7.1 The Avon Pension Fund Committee is the formal decision-making body for the Fund. As such it has responsibility to ensure adequate risk management processes are in place. It discharges this responsibility by ensuring the Fund has an appropriate investment strategy and investment management structure in place that is regularly monitored. In addition it monitors the benefits administration, the risk register and compliance with relevant investment, finance and administration regulations. The creation of an Investment Panel further strengthens the governance of investment matters and contributes to reduced risk in these areas.

## **8 CLIMATE CHANGE**

- 8.1 The Fund is implementing a digital strategy across all its operations and communications with stakeholders to reduce its internal carbon footprint. The Fund acknowledges the financial risk to its assets from climate change and is in the process of addressing this through its strategic asset allocation to Paris Aligned Equities and renewable energy opportunities. The strategy is monitored and reviewed by the Committee. As part of the valuation the Actuary will report on the potential impact of climate change risks in his final valuation report and the summary outcomes will be included in the FSS in line with best practice.

## **9 OTHER OPTIONS CONSIDERED**

- 9.1 None.

## **10 CONSULTATION**

- 10.1 The Council's Monitoring Officer and Section 151 Officer have had the opportunity to input to this report and have cleared it for publication.

<b>Contact person</b>	Julia Grace, Funding & Valuation Manager
<b>Background papers</b>	MHCLG guidance for preparing and maintaining an FSS Correspondence with actuary Responses to FSS from employing bodies
<b>Please contact the report author if you need to access this report in an alternative format</b>	