

Bath & North East Somerset Council		
MEETING:	AVON PENSION FUND COMMITTEE	
MEETING DATE:	27 March 2026	AGENDA 10 ITEM NUMBER
TITLE:	ACTUARIAL VALUATION 2025 & UPDATED FUNDING STRATEGY STATEMENT	
WARD:	ALL	
AN OPEN PUBLIC ITEM		
List of attachments to this report: Appendix 1 – 2025 Funding Strategy Statement		

1 THE ISSUE

- 1.1 The Local Government Pension Scheme (LGPS) Regulations require LGPS funds to have an actuarial valuation every three years. The 2025 valuation has a base date of 31 March 2025 with new employer contribution requirements becoming effective from 1 April 2026.
- 1.2 In calculating the contribution rates, surpluses and deficit recovery payments for the period from 1 April 2026, the Actuary has taken the Funding Strategy Statement (FSS) into account.
- 1.3 The Actuary will finalise the actuarial valuation report before 31 March 2026 which will be circulated to all employing bodies. In the meantime, the employing bodies have been notified of their revised contribution requirements for the period 1 April 2026 to 31 March 2029.
- 1.4 This report examines the final outcome of the valuation process for the whole fund and highlights the principal changes which have occurred since the 2022 valuation.
- 1.5 The latest version of the Funding Strategy Statement is included for information only. This will be included on the Fund website and considered for accessibility requirements in due course.

2 RECOMMENDATION

The Committee:

2.1 Notes the outcome of the 2025 actuarial valuation exercise.

2.2 Delegates the finalisation of the Funding Strategy Statement to Officers.

3 FINANCIAL IMPLICATIONS

- 3.1 The actuarial valuation assesses the funding position of the Fund as a whole. For the individual employers it sets the contribution rates due from all employers for the 3 years commencing 1 April 2026. The costs for completing the valuation are provided for in the 2025/26 budget.

4 Background and valuation approach

- 4.1 The long-term funding objective is to achieve a 100% solvency over a reasonable length of time and then maintain that position. Contributions are set in relation to this objective which means that once 100% solvency is achieved, if the assumptions are borne out in practice, there would be sufficient assets to pay all benefits earned up to the valuation date as they fall due.

As market conditions change between valuations, the assumptions may need to change at subsequent valuations in order to meet this objective; hence contribution rates will vary from one valuation to the next. The Actuary will also incorporate an allowance for long term “tail risks” such as the potential impact of Climate Change on financial markets, life expectancy and contributions affordability.

The Fund’s approach is that the assumptions used will be chosen with sufficient prudence for this objective to be reasonably achieved in the long term at every valuation.

- 4.2 Alongside this overarching objective, employer contributions are set to achieve long-term cost efficiency, meaning the funding plan must provide equity between different generations of taxpayers. Therefore, contributions must not be set at a level that is likely to give rise to additional costs to future taxpayers or that puts too high a burden on current taxpayers. Given the difficult economic and public sector funding environment at the time of the 2025 valuation, significant consideration was given to both the solvency and long-term cost efficiency objectives.
- 4.3 Finally, the 2025 valuation sought to balance the current and future interests of employers in terms of making reductions to contributions now and the likelihood that contributions can remain sustainable over a number of valuation cycles. The financial assumptions have been set taking account of the investment strategy of the Fund and the link between the funding and investment strategies. The FSS, which was approved by the Committee in September 2025, set out the parameters as to how these aims would be met. In particular, the inclusion of the Surplus policy which sets out how any surplus will be utilised to reduce employer rates and the inclusion of a surplus reserve to manage contribution sustainability.
- 4.4 By utilising the flexibility allowed within the FSS, the 2025 funding plans objectively balance affordability for individual employers and solvency of the Fund. In terms of setting contributions, the relationship of the expected investment return on assets compared to the rate of expected future increases in benefit payments (i.e. CPI inflation) is critical (in other words we need to reflect the “real” investment return expected on the Fund assets and the degree of certainty in the assets delivering that real return when setting the real discount rate assumption).
- 4.5 Higher return and lower further inflation expectations at the 2025 valuation, based on long-term financial modelling, has resulted in a more optimistic contribution outlook due to the improved funding levels along with a lower cost of future ongoing benefit cost which has reduced the employers future service rate. The introduction of a surplus reserve has meant for employers, a proportion or all of the surplus is

not being returned to employers via contribution rates as the offsets only relate to surplus in excess of a 105% funding level. However, in a lot of cases there would be reduced or no deficit contributions payable as certified at the previous valuation.

- 4.6 Individual employer results will vary significantly due to other factors such as changes in the membership profile and salary growth (versus assumptions).
- 4.7 Whilst contribution reductions have applied for many employers, employers have been given the option to retain contributions at a higher level or apply a partial reduction (for example to only reduce the primary rate whilst not taking the surplus off-set contribution), allowing them to influence the balance between their short and longer term budgetary risks and some employers have utilised this option to overpay relative to the minimum contribution requirements.
- 4.8 The level of contributions sustainability will be monitored in the inter-valuation period for the total Fund and certain individual employers. This is with a view to inform employers of any emerging trends to consider in terms of their own budget sustainability as well as provide oversight to the Committee in relation to funding risk. This will take into account changes in market and economic outlook as well as any investment strategy changes (where appropriate) emerging from the current strategy review being undertaken by LPPI. The Actuary is not proposing any consideration of any potential investment strategy changes when setting the assumptions at this valuation given the objectives agreed as part of the review being undertaken. The Actuary will note this in his final valuation report.

5 ACTUARIAL VALUATION 2025 FINAL OUTCOME

- 5.1 The current valuation has been taken at 31 March 2025 and a summary of the valuation is in the table below.
- 5.2 The FSS provides a flexible framework to take account of affordability when setting contribution rates and deficit recovery payments as follows:
 - a) Options to overpay the minimum contributions arising from the funding strategy (as noted above)
 - b) Phased in increases in future service rates over a maximum of 3 years (despite increases in return expectations, other factors have led to an increase in future service rates for employers in isolated circumstances)
 - c) Option to pay deficit contributions in advance to benefit from a monetary discount.
 - d) Options to bring forwards surplus off-sets to the beginning of the year, for certain employers, subject to a minimum contribution of zero in any month

Initial Fund Outcome:

	2022	2025
Surplus (Deficit)	(£238m)	£339m
Funding Level	96%	106%
Value of assets	£5,822m	£5,787m
Value of Liabilities	£6,060m*	£5,447m*
Average employee contribution rate	6.4% of pay	6.4% of pay
Average future service rate (employer)**	18.6% of pay	16.3% of pay
Average Period for deficit/run-off and for surpluses/run-off (years)	12	12

Notes:

* Includes lower risk strategy results for employers within that strategy at the valuation date

** this is the average ongoing open future service rate allowing for each employer's circumstances

5.3 The average run off period for deficit/surplus for the Fund has remained at 12 years for the 2025 valuation, which is the medium-term target for the Fund. However, a large number of employers have now moved into surplus or seen an increase in surplus. The main drivers of the valuation outcome are:

- a. The impact of investment returns. Change in the past service real discount rate (from CPI+1.5% p.a. to CPI + 3.3% p.a.) over the 3-year period to 31 March 2025, has had a combined positive impact of c£869m on the funding position.
- b. The impact of high observed CPI inflation over the 3-year period (and average pension increase of 6.1% p.a.) has reduced the funding position by c£366m.
- c. The increase in return expectations has also affected the Future Service Rate (FSR). The Actuary uses a "smoothed" discount rate to value future accruals, in order to keep the FSR as stable as possible in line with the Regulations. The 2022 real discount rate of CPI + 2.0% was increased to reflect the improved outlook at 31 March 2025 but recognising the requirement for stability in the long-term cost of benefit provision. Therefore, the real discount rate for future service was increased by 0.25% p.a. to CPI + 2.25% p.a. This has reduced the future service rate by 1.4% of pay in isolation.
- d. At each valuation the actuary uses an analysis of the life expectancy experienced by the Fund and other LGPS funds alongside improvement trend models from the Continuous Mortality Investigation (CMI) to assess the adequacy of the longevity assumptions.

The assumption is made up of two elements, the current life expectancy (or baseline assumption) and an assumption of future improvement / deterioration around the baseline assumption. The Actuary has altered the baseline assumption for the 2025 valuation reflecting the updated membership information to include the Fund's experience since 2022. For the long-term life expectancy improvement assumption, the latest 2024 CMI tables have been

used with a long-term rate of improvement of 1.5% p.a. which show a slowing in the rate of improvement evidenced by mortality data and has, as a result, reduced liabilities overall.

The Actuary has considered life expectancy impacts in the climate risk scenario analysis undertaken in line with the principles document published by the Scheme Advisory Board.

The Actuary also considers other demographic assumptions (ill health, normal retirement, commutation rates etc) based on aggregate data along with the Fund data. These assumptions have been updated which had a marginal effect on the overall liabilities and future service rate.

In combination the impact of the change in the demographic assumptions has had a positive impact of c£213m on the funding position. The impact of the change on the future service rate has been a reduction of 0.4% of pay.

- e. There are other factors which have an impact on the valuation outcomes such as pay awards to members, employer contributions paid and change in age/gender profile. These impact on the funding position and future service rate to a different extent and can vary considerably at an individual employer level. We have shown the combined impacts in the reconciliation in paragraph 5.5 below.
- f. Allowance for any known benefit changes (e.g. survivor benefits) has been made to the extent this is built into the assumptions or data used by the Fund Actuary for the valuation calculations. In addition, the Actuary has prepared the Gender Pensions Gap Analysis for the Fund as a whole in line with the instructions from the Government Actuary Department and individual employer statistics have been provided to major employers as part of their valuation results.

5.5 The changes are summarised in the following tables:

Changes to past service position since 2022 valuation

	£m
Deficit at 31 March 2022	-238
Unwinding of Interest on deficit	-34
Impact of investment returns and change in past service financial assumptions	+869
Observed CPI pension increases/inflation vs 2022 assumption	-366
Change in demographic assumptions	+213
Pay increases, contributions, and other factors	-105
Surplus at 31 March 2025	339

Changes to future service rate

Average Employer Rate at 31 March 2022	18.6% of pay
Change in membership profile	-0.5% of pay
Change in discount rate	-1.4% of pay
Change in demographic assumptions	-0.4% of pay
Average Employer Rate at 31 March 2025	16.3% of pay

6 COMMUNICATION WITH EMPLOYING BODIES

- 6.1 The 2025 actuarial report will be published by 31 March 2026. In the meantime, the employing bodies have been notified of their revised rates and officers have been responding to queries from employers.
- 6.2 A substantive employer communication and engagement programme has been implemented over the course of 2025 and 2026 to support employer understanding and engagement to provide for optimal outcomes for both the Fund (in terms of management of risk) and the employers (in terms of contribution affordability and longer-term sustainability). This included employer meetings tailored for specific groups: Councils, HE/FE and Academy employers, explanatory videos in relation to the process, the FSS and employer results, as well as written Q&A supporting materials.
- 6.3 The Fund has already reported on the outcomes of the FSS employer consultation and will report again following completion of the employer results process. An appropriate communication strategy will be implemented over the inter-valuation period as part of the overall employer risk management strategy taking into account the contribution sustainability monitoring framework.

7 FUNDING STRATEGY STATEMENT (FSS)

- 7.1 The 2025 FSS was approved by Committee in September 2025, and finalisation of the FSS was delegated to Fund Officers, with assistance of Fund Actuary.
- 7.2 The version in Appendix 10 has been updated for the actuarial and financial assumptions/data and miscellaneous minor policy clarifications as employer results have been worked through.
- 7.3 In addition, based on the advice from the Actuary when considering the final employer rates, an update has been made to the death in service captive policy in order to allow for the policy to be backdated to cover the full inter-valuation period i.e. commencing with effect from 1 April 2022 as opposed to 1 April 2023, in light of the surplus position in the captive and death strains experience over the period for some smaller employers in the Fund.
- 7.4 The Actuary's review of the termination policy actuarial assumptions, including the approach to setting of the lower risk discount rate has now been completed. The termination policy has been updated to reflect updates to the assumptions for determining the discount rate, life expectancy assumption and an allowance for administration expenses in respect of administering benefits for orphan liabilities after an employer exits the Fund. The updated assumptions have been implemented for calculations for cases with an effective termination date on or after 1 January 2026.

8 RISK MANAGEMENT

8.1 A key risk to the Fund is the inability of an individual employer to meet its liabilities, especially when it ceases to be an employing body within the Fund. The Funding Strategy is designed to manage this risk to ensure the Fund achieves and maintains full solvency over an appropriate period. Assessing the strength of an employing body's covenant is also a crucial component in managing the potential risk of default to the Fund and is incorporated in the contribution plans. The Fund officers will undertake a review of this process in the intervaluation period in conjunction with the Actuary.

9 EQUALITIES STATEMENT

9.1 A proportionate equalities impact assessment has been carried out using corporate guidelines and no significant issues have been identified.

10 CLIMATE CHANGE

10.1 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 addresses this through its strategic asset allocation to Paris Aligned Global Equities and renewable energy opportunities. The strategy is monitored and reviewed by the Committee.

10.2 In terms of the current valuation, an analysis of different climate change scenarios at the Whole Fund level has been undertaken relative to the baseline position assuming that the funding assumptions are played out on a best estimate basis. The projections are meant to illustrate the different elements of risk under four climate change scenarios based on the current strategic allocation. The scenarios are not meant to be predictors of what may happen and are only a small subset of a very wide range of scenarios that could arise. The analysis considers a projection of the funding levels under the scenarios considered which are designed to illustrate the transition and physical risks over different periods depending on what actions are taken globally on climate change. Further detail is set out in the FSS appended to this report (pages 14 to and 17), and a summary of the results of the analysis will be included in the Actuary's final valuation report. This analysis also considered the impacts on life expectancy under the scenarios and UK GDP to support further consideration of employer covenant as part of the analysis.

11 OTHER OPTIONS CONSIDERED

11.1 Report for information only.

12 CONSULTATION

12.1 The Council's Director of Assurance, Risk & Pensions has had the opportunity to input to this report and has cleared it for publication.

Contact person	Julia Grace, Pensions Valuation Advisor 01225 395392
Background papers	Actuary reports and presentations at previous committee meetings; 2025 draft and final FSS

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