

Fund Response to Pension Board – February 2026

Following the Local Pension Board meeting on 4 February, further information is now provided for the Board on why Officers and the Fund Actuary feel the 3% cap on the secondary rate should remain.

The Board's comments and the information below, will be included in the report to be taken to Committee in March 2026, where approval of the final FSS will be recommended, alongside the final valuation details.

The draft FSS was included with the Board report but is attached again for completeness.

FSS – surplus management

- The draft funding strategy statement sets out the Fund's approach to managing surpluses in sections 2.2 and 2.3.
- Table 2.3 sets out the Fund's approach to allow Employers to pay up to a contribution rate less than the Primary Rate (up to a maximum of 3% of pay less)
- This decision has been taken to support the aims of stability and inter-generational fairness and applies to open employers, i.e. those that will continue to admit employee into the scheme for many years to come.

Setting contribution rates – quantitative and qualitative factors

- When setting funding strategy, the Fund considers quantitative factors that can be explicitly modelled to set a contribution rates, such as the level of prudence / likelihood of success and the target funding level.
- These factors aim to provide the necessary prudence, as required by the regulations, and to protect members and employers from future volatility.
- However, the Fund must also consider qualitative factors in addition to the raw modelling results to help meet its longer-term funding objectives.
- The Fund has key funding objectives set out in Section 1.2 of the FSS, which largely mirror the those set out in the Regulations.
- These objectives focus on solvency, long-term cost efficiency, intergenerational fairness and stability (and affordability) of employer contributions – noting there is a difficult balance to be struck to achieve all at once.
- To enable the Fund to continue to meet these objectives over multiple valuation cycles, the Fund takes a long-term view and overlays qualitative factors to arrive at the final funding strategy for employers.
- These factors include the Fund's stabilisation policy - which has been in place for many valuations now and has protected Councils against shorter term market volatility to provide stable rates through good times and bad.
- Other qualitative factors that are relevant at each valuation include consideration of the long-term cost of benefits (i.e. the Primary Rate) and employer long-term affordability, i.e. the difficulty of increasing employer rates in the future (which the fund seeks to avoid).
- To strike a balance of the various funding objectives and qualitative factors, the Fund has decided to anchor rates to the Primary Rate to help meet longer-term cost efficiency, intergenerational fairness and stability – as set out in the Regulations (noting this is a common approach by many other LGPS funds for the same reasons).

3% of pay lower than Primary Rate

- In recognition of the need for shorter term contribution relief for employers, and the current strong funding positions, the Fund has allowed employers to pay up to 3% of pay less than the Primary Rate – effectively using up some of the current surplus.

- The Fund has decided on 3% as the cap, as this is related to the Fund stabilisation policy – which aims to limit increases / decreases to a maximum of 1% of pay pa, or a total of 3% of pay over a valuation cycle (noting this has been widened to 2% of pay in recent years in response to funding circumstances, but will likely to revert back to 1% of pay in the future).
- Furthermore, the Fund has set Council rates using the agreed stabilisation policy, which currently allows 2% of pay pa changes, up to a maximum of 6% of pay reduction over the 3-year period.
- There is an expectation (from DfE and other wider stakeholders) at this valuation to see equitable funding treatment between academies (and colleges) and Councils. In recognition of this point, the Fund has allowed all academies and colleges to reduce rates by at least 6% of pay.
- Furthermore, the Fund has accepted that these employers did not benefit from the protection afforded by stabilisation when in deficit, so the Fund has allowed these employers to benefit from even greater reductions at the 2025 valuation – up to a maximum of 3% of pay less than the Primary Rate.
- The resulting contributions have reduced by up to 16% of pay in some cases – which is a significant reduction and significantly greater than expected across other LGPS funds.
- In addition to these reductions, the Fund has allowed this reduction to take place immediately, as opposed to phasing the reduction in gradually over 3 years - in recognition of current pressures on employers and the strong funding position.
- Conversely, in the past, any increases in contributions have generally been phased to support employer affordability.

Summary

- The current strong funding position has materialised very quickly due to changes in markets expectations for higher future investment returns (in line with rising interest rates).
- However, any employer ‘surplus’ is strictly notional, and is predicated on achieving a level of future returns that is not guaranteed.
- The Fund is keen to return some surplus to employers but is cautious about reducing contributions too low and the risk that employers then need to increase contributions again in the future if market expectations revert, or there is an unexpected crash in asset values.
- The application of qualitative factors, such as those set out above, will always be a subjective decision and therefore open to challenge and scrutiny. However, the Fund is comfortable that this decision is striking a fair balance of the competing funding objectives at this valuation given the current funding and economic environment and the need for a longer-term strategy to the benefit of employers.
- The 3% cap will remain under review at future valuations (as part of the wider ongoing funding strategy review), and if circumstances permit this could be relaxed further. However, the Fund’s long-term strategy will remain unchanged, i.e. to meet the objectives set out in Section 1.2 of the FSS and in the Regulations by striking the appropriate balance of risk management versus employer affordability.

Regards, Ian

Ian Howe

Pensions Manager

Leicestershire County Council