Government Actuary's Department

Clair Alcock
Head of Pensions
Local Government Association
18 Smith Square, London SW1P 3HZ

6th Floor
10 South Colonnade
London
E14 4PU

matt.gurden@gad.gov.uk
07814 940 830
gov.uk/gad

20 June 2025

Dear Clair

Subject: SAB basis for standardised funding calculations for LGPS (England & Wales) Fund valuations as at 31 March 2025

Further to discussions at the CMBDA on 24 February, the SAB secretariat have commissioned me to provide advice on the SAB basis for standardised funding calculations for Local Government Pension Scheme (England & Wales) Fund valuations as at 31 March 2025. The current basis was set for use in the 2022 Fund valuations and needs to be reviewed to consider any change in conditions since 2022. The purpose of this letter is to provide recommended updates to the SAB basis for use in the 2025 valuations.

Background and objectives

As previously discussed, the purpose of the SAB basis is to enable cross comparison of Funds. It is set by the SAB, having obtained actuarial advice. The local valuations for each Fund use financial assumptions specific to that Fund, and so the funding levels (assets divided by liabilities) on the local Fund bases are not directly comparable.

Cross comparison of Funds can be considered in several ways, and it is therefore appropriate to consider the overall objectives to ensure the approach adopted best meets those objectives. Set out below are possible objectives:

- **Local variation** – Provides comparison of Funds allowing for legitimate local differences
- **No local variation** – Provides comparison of Funds assuming all are the same way
- **Consistent** – Provides comparison between Funds and across valuation dates
- **Market reflective** - Provides comparison between Funds but less so over time

The SAB basis has previously been set for the 31 March 2016, 31 March 2019 and 31 March 2022 valuations. Over this period the approach adopted has been to allow for local variation in demographic assumptions, ie the experience of individual members, and for the financial assumptions to be more stable over time, linked to the HM Treasury set SCAPE discount rate, and without allowance for local variation. The table in the Annex sets out the past assumptions.

I have assumed for the purposes of the advice below, that this remains the preferred approach, and that you would prefer to retain the existing SAB basis. If this is not the case, changes to the proposed 2025 SAB basis may be necessary.

The remainder of this note sets out the options and underlying rationale for consideration.

Note that the proposed SAB basis does not value assets and liabilities consistently, and so it is not suitable for Funds to use for their funding valuation and should not be seen as a 'target' or 'minimum funding requirement' basis. As a result, it is **not** appropriate to use the SAB basis to:

- Assess whether a particular Fund is fully funded or has a deficit (whether the funding level on the SAB basis is more or less than 100% is irrelevant, only the SAB funding level relative to other Funds is meaningful)
- Compare SAB basis funding levels at 2025 with the SAB basis funding levels at the previous valuation in 2022

Setting the basis

The most impactful decision when setting the SAB basis relates to the discount rate to be adopted.

Discount rate & CPI

The discount rate used for previous SAB bases has been set in line with the nominal SCAPE discount rate set by HM Treasury. For the 2022 basis, it was set at 4.45% p.a. which was consistent with the nominal SCAPE discount rate in force at the time the basis was set and in line with the rate set for the 2019 basis.

HM Treasury issued a consultation[1] on the SCAPE discount rate methodology on 24 June 2021, and responded to the consultation in March 2023. As a result of the consultation the SCAPE discount rate was reduced from 2.4% above CPI to 1.7% above CPI.

Since the 2022 basis was set market interest rates and future return expectations have changed considerably. Long term interest rates have risen and asset values have changed. We expect these changes will make comparisons between valuation cycles, and across Funds more challenging. The consistent SAB basis will therefore be of particular interest.

If the SAB views consistency of process as the most important guideline, then updating the SAB basis to reflect the latest SCAPE discount rate might be appropriate. This would align the assumptions with those used for the most recent assessment of the HM Treasury Cost Cap Mechanism (carried out by GAD at 2020). This would take into account the long-term health of the economy at that time – as the SCAPE discount rate is based on the Office of Budget Responsibility's view of long-term economic growth.

[1] https://www.gov.uk/government/consultations/public-service-pensions-consultation-on-the-discount-rate-methodology

A different approach to consistency would be to focus on alignment between 2022 and 2025. This would suggest that the SAB basis remains linked to the same financial assumptions that were adopted at the previous exercise. This would maximise comparability between liabilities produced at the two valuation dates, would also align with the 2019 basis, and would suggest maintaining the same assumptions at future valuations.

Whilst retaining the existing SCAPE discount rate could be viewed as using ‘out of date’ information, we note that the SAB basis does not attempt to precisely reflect conditions at the valuation date. We also note that HMT are currently reviewing the SCAPE rate, and that a new rate is likely to be set around the time that the 2025 valuations are published. At the time of reporting, neither of the rates currently considered may therefore be the latest available when the valuations are completed.

An alternative approach might therefore be to adopt a SAB basis that more closely reflects the average discount rate being adopted across the various Funds, and hence the aggregate funding level should be similar under both. However, each individual Fund might have a SAB funding level quite distinct from their ongoing funding level. This has the possible advantage that the aggregate SAB position should be close to that from the Fund valuations, but might cause confusion why it’s not being used for contribution setting. Additionally, the discount rates adopted by Funds are likely to vary quite substantially and hence an average rate may be difficult to determine and not representative of any group of Funds. This approach would also mark a material change relative to the SAB basis at previous valuations.

On balance, and considering the current review in isolation, we propose continuing to set the discount rate in line with the SCAPE discount rate used for the 2022 valuations.

To set the nominal discount rate it is necessary to set an assumption for CPI, which will also be used for pension increases. Consistent with previous SAB bases and the government’s long-term target for CPI, I propose continuing to set this as 2% per annum. The nominal discount rate is then 4.45% per annum (calculated as 1.02 x 1.024).

Whilst it would be possible to make the decision now to fix the rate over time for future valuations, it may be preferable to maintain the flexibility to reconsider at future exercises.

Public sector earnings growth

The public sector earnings growth assumption should be consistent with the approach adopted for the discount rate. The SCAPE discount rate, which has been adopted for the SAB basis, is based on the Office for Budget Responsibility’s (OBRs) expectations for long-term GDP growth. Therefore, when setting the public sector earnings growth assumption, the SAB basis has used the OBRs expectations for long-term public sector earnings growth from the same date as their long-term GDP growth expectations.

If the SAB decides to continue adopting the same discount rate assumption as at the previous review, then we would suggest that a similar approach should be adopted for the earnings assumption.

If the SAB opted to update to the latest SCAPE discount rate of 1.7% above CPI, it would be based on the OBRs expected long-term GDP growth figures published in 2022[2]. At this time, the

---

[2] https://obr.uk/frs/fiscal-risks-and-sustainability-july-2022/

OBRs expected long-term public sector earnings growth was 3.8% per annum. In that situation I would therefore propose adopting an earnings growth assumption of 3.8% per annum.

Other assumptions

If the SCAPE rate were maintained in line with its 2022 valuation level, then there may be persuasive arguments to retain the 2022 basis in its entirety, to maximise comparability.

However, given the interactions with local experience and assumptions, we suggest updating the non-financial assumptions to reflect recent experience. Whilst this will affect comparisons between SAB liabilities at 2022 and 2025, the differences will be much smaller than those which would result from changes to the discount rate and should be more reflective of actual local experience.

Assuming that you want to update these assumptions, adopting the approach outlined above, I propose continuing to allow most demographic assumptions to be set based on local Fund experience. The two areas of divergence from this approach are the projection of future mortality improvements, where it is less clear local differences are appropriate, and the allowance for 50/50 take-up.

Future mortality improvements

The Continuous Mortality Investigation (CMI) issues a Mortality Projections Model annually, with each model taking into account the most recently available population mortality data at the time the model is issued. The model provides a framework for setting future mortality improvement factors, and a version of the model has been adopted in each of the last three SAB bases. The 2022 SAB basis adopted the CMI 2021[3] model, with an assumed long-term reduction in mortality rates of 1.5% per annum.

The CMI is currently consulting on significant changes to the model for 2024. Given these are still under consultation and hence not yet finalised, I suggest adopting the CMI 2023[4] model. The CMI 2023 model makes some allowance for observed mortality experience during the period of the COVID pandemic, with a 15% allowance for 2022, 2023 but no allowance for 2020 and 2021 mortality.

I recommend adopting the CMI 2023 model and maintaining the assumed long-term reduction in mortality rates of 1.5% per annum as has been adopted in each of the previous SAB bases.

50/50 take up

There has been some variation in approach to 50/50 take up in the SAB basis previously. The initial 2016 basis made no explicit allowance, but the 2019 and 2022 bases assumed a 5% take up. Analysis of experience for the 31 March 2020 SAB cost management process indicated lower take up of the option than 5% and adopted an assumption of 1%.

Although changing this assumption reduces the comparability of outcomes over time, I would propose updating this assumption to align with the 2020 SAB cost management process and better reflect the overall experience. I therefore propose updating this assumption to 1% take up.

[3] https://www.actuaries.org.uk/learn-and-develop/continuous-mortality-investigation/cmi-working-papers/mortality-projections/cmi-working-paper-160

[4] https://www.actuaries.org.uk/learn-and-develop/continuous-mortality-investigation/cmi-working-papers/mortality-projections/cmi-working-paper-189

Implications

Adopting the proposed assumptions for the 2025 SAB basis would be expected to produce liabilities broadly similar to those produced using the 2022 SAB basis, aiding comparability. We would therefore generally expect SAB basis funding level between 31 March 2022 and 31 March 2025 also be similarly stable, with individual Fund experience over the period being the key driver for changes in specific Funds' levels.

Compliance and limitations

This letter is intended solely for the use of the SAB. It sets out the proposed SAB basis for standardised funding calculations for Local Government Pension Scheme (England & Wales) Fund valuations as at 31 March 2025. The letter should not be relied on, or assumed to be appropriate for, any other purpose or by any other person.

I am content for the SAB to release this letter to third parties, provided that:

- it is released in full
- the advice is not quoted selectively or partially
- GAD is identified as the source of the letter
- GAD is notified of such release

Third parties whose interests may differ from the SAB should be encouraged to seek their own actuarial advice where appropriate.

Other than the SAB, no person or third party is entitled to place any reliance on the contents of this letter, except to any extent explicitly stated herein. GAD has no liability to any person or third party for any action taken or for any failure to act, either in whole or in part, on the basis of this letter.

This work has been carried out in accordance with the applicable Technical Actuarial Standard: TAS 100 issued by the Financial Reporting Council (FRC). The FRC sets technical standards for actuarial work in the UK.

Yours sincerely

Matt Gurden FIA
Deputy Government Actuary

Government Actuary's Department

Annex A – SAB basis for standardised funding calculations for LGPS EW fund valuations

Assumption	Basis as at 31 Mar 2016	Basis as at 31 Mar 2019	Basis as at 31 Mar 2022	Proposed basis as at 31 Mar 2025
Methodology	Projected Unit Methodology with 1 year control period			
Rate of pension increases	2% per annum			
Public sector earnings growth	3.5% per annum			
Discount rate	5.06% per annum	4.45% per annum	4.45% per annum	4.45% per annum
Pensioner baseline mortality	Set locally based on Fund experience			
Mortality improvements	Core CMI_201X with long term reduction in mortality rates of 1.5% per annum	Core CMI_2018 with long term reduction in mortality rates of 1.5% per annum	Core CMI_2021 (no allowance for 2020 and 2021 mortality data) with long term reduction in mortality rates of 1.5% per annum	Core CMI_2023 with long term reduction in mortality rates of 1.5% per annum
Changes to state pension age	As legislated			
Age retirement	Set locally based on Fund experience			

Navigating risk | Cutting through complexity

The Government Actuary's Department is proud to be accredited under the Institute and Faculty of Actuaries' Quality Assurance Scheme.
Our website describes the standards we apply.

Assumption	Basis as at 31 Mar 2016	Basis as at 31 Mar 2019	Basis as at 31 Mar 2022	Proposed basis as at 31 Mar 2025
Ill health retirement rates	Set locally based on Fund experience			
Withdrawal rates	Set locally based on Fund experience			
Death before retirement rates	Set locally based on Fund experience			
Promotional salary scales	None			
Commutation	SAB future service cost assumption of 65% of the maximum allowable amount			
Family statistics	Set locally based on Fund experience			
50/50 take up	n/a	5% of all members take the 50/50 option	5% of all members take the 50/50 option	1% of all members take the 50/50 option