

The Pensions Regulator's 2026 Annual Funding Statement

The Pensions Regulator (TPR) has issued its 2026 Annual Funding Statement (AFS). It sets out TPR's expectations for trustees and employers of Defined Benefit (DB) schemes undertaking actuarial valuations with effective dates between 22 September 2025 and 21 September 2026. It also refers to forthcoming guidance on surplus release and clarifies some of TPR's previous guidance on its new DB funding code of practice.

Background

TPR notes that most schemes continue to report strong funding levels, and it expects them to be shifting their focus from deficit recovery to long-term endgame planning.

TPR advises that its experience to-date supports its estimate that around 80% of schemes undertaking valuations should be able to meet their FastTrack parameters when submitting their valuation results. As well as requiring less information to be provided than under the alternative Bespoke approach, a FastTrack approach makes it less likely that TPR will want to engage with the Scheme. There are no changes this year to the FastTrack parameters, but TPR may consider updating them in the future. The current parameters are based on market conditions as at 31 March 2023, and the subsequent rise in bond yields and equity markets could lead to a review of the parameters next year.

As for last year's statement, TPR groups schemes into three broad categories and comments on them separately:

Group 1: funding level is at, or above, low dependency funding target

The focus should be on endgame planning (buy-out, running on or entering a consolidation vehicle, if eligible).

This year, TPR distinguishes between those schemes whose low dependency funding level is above 110%, and those whose funding level is 100%-110%. For the former, it suggests locking down investment risk if the aim is to buy-out in the short term. If the intention is to run on, then more investment risk may be acceptable, but trustees should consider their policy on the use of any surplus. TPR advises that it will issue guidance on surplus release shortly.

TPR suggests that there may be fewer options for schemes whose low dependency funding level is 100-110%. This could indicate that TPR regards 110% funding as a proxy for the cost of a buy-out, or perhaps that it may view 110% as the threshold for any release of surplus to the sponsoring employer.

Group 2: funding level above Technical Provisions (TPs) but below the low dependency funding target

The focus should be on ensuring the scheme continues on the path to achieving the low dependency objective by the relevant date, through ongoing monitoring and management of downside risks.



Group 3: funding level is below TPs

The focus should be on addressing the deficit. TPs should be consistent with the scheme's journey plan to reach low dependency by its relevant date. The level of risk should be dependent on employer covenant support and the maturity of the scheme. Any deficit should be recovered as quickly as the employer can reasonably afford to.

Clarifications on Employer Covenant

TPR advises that if the covenant strength is inadequate to support risk, then this should be clearly acknowledged in the trustees' statement of strategy. This is less likely to trigger regulatory engagement than an assessment of adequacy which may not be justifiable.

Clarifications on Supportable Risk

TPR lists several factors to be considered when trustees are deciding whether to allow for a current surplus when assessing supportable risk. It cautions against using the full amount of any surplus to support a higher-risk funding and investment strategy.

Clarifications on Low Dependency Investment Allocation and Low Dependency Funding Basis

Schemes which are significantly mature and have passed their relevant date should seek to repair any deficit on their low dependency funding basis through employer contributions and/or contingent support, rather than by increasing investment risk.

Under the new funding code, the low dependency funding basis is required to include a reserve for the expenses to be incurred from the relevant date onwards (unless the employer is required to pay expenses). TPR acknowledges that this expense reserve can be significant, particularly for smaller schemes, or where the long-term objective is to run on. It confirms that the expense reserve should be set proportionately and pragmatically, with approximate methods acceptable for long-dated and uncertain expenses. TPR also expects the expense reserve to evolve over time as each scheme's long-term strategy develops, and to see the reserve adjusted at each future valuation.

Comment

The clarifications provided are helpful for schemes currently undertaking their first valuations under the new DB funding code. TPR promises further analysis once it has received and assessed the bulk of the valuation submissions for schemes undertaking valuations in 2024/25, so we may expect further guidance in the coming months.

If you would like to discuss any of these matters further, please get in touch with your usual contact at Cartwright.

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