



2026 DB outlook: Opportunity and innovation

Whether you are considering buyout,
run-on or both, we are here to help build a
bridge to your chosen endgame destination.



2026 DB outlook



Will Riley
Head of Solutions



Mark Johnson
Head of UK - Institutional and Wholesale

The 2020s have been a transformational period for UK DB pension schemes, with a shift driven by evolving regulations, new requirements and the ongoing buyout or run-on debate. Rather than viewing these changes as obstacles, we see them as catalysts for opportunity and innovation.

In **'A time for opportunity'** we discuss the recently published [Pension Schemes Bill](#) and how it opens the door for meaningful discussion and engagement. The part of the Bill focussed on surplus release provides a blueprint for the 'rules of the road'

ahead of final regulation expected in 2027. We assess what we do know, and look forward to the opportunity the industry has to pause, discuss and consider the right way forward.

Interest in run-on has continued to build in 2025, with the proportion¹ of schemes adopting run-on as a long-term strategy up by around 10% compared to 2024. In **'Investing for run-on'** we assess whether this is really a new concept, before delving into some of the practical investment considerations. Drawing lessons from life insurers, we also highlight the unique flexibility available to pension funds and the ability to access the 'best of both worlds'. In a low-credit-spread environment, there are still a number of other levers that pension investors can pull to target returns within a cashflow-aware framework.

For those pension funds with a long-term time horizon, what innovations in the responsible investment space should trustees have in mind in 2026? In **'Responsible innovation'** we revisit climate and nature, where engagement remains crucial, in our view, for driving meaningful, real-world change.

Buyout will continue to be the near-term direction of travel for many schemes. After all, 54% of UK DB schemes were in surplus on a buyout basis at the end of 2024, equivalent to c.600bn of buyout liabilities². However, with 'only' around £40bn³ of transactions in 2025 as a whole, it will take many years for schemes to collectively achieve their buyout goals.

In **'Seeking value in bulk annuity transactions'** we look at the importance of preserving buyout affordability, improving pricing and managing residual asset surplus. In 2026 we expect continued innovation in 'route to buyout' approaches that allow well-funded schemes to seek value in bulk annuities.

Going full circle, it is clear that 'a time of opportunity' comes with increased choice and challenge. In 2025 we saw the new DB funding code come into force and the requirement for trustees to document their long-term plan for either buyout or run-on. In **'Evolving your investment strategy'** we set out our hot topics for 2026 in light of recent regulatory change. For those considering long-term run-on, we believe that good governance, clear policies, effective delegation and ongoing collaboration will be essential to achieving the best outcomes for both members and sponsors.

Thank you for reading our latest DB outlook. At L&G we will seek to continue to innovate across the full breadth of solutions to help you achieve your objectives in 2026 and beyond.

1. Aon 2025 Endgames Survey indicated 28% (up from 17% in 2024) looking to run on beyond point needed for settlement readiness of those who had made a decision [Aon-2025-DB-Endgames-Survey.pdf](#)
2. The Pension Regulator's Annual Funding Statement 2025
3. [LCP November 2025](#)

DB schemes: A time for opportunity

The publication of the highly anticipated Pension Schemes Bill in 2025 has been a welcome moment across the pensions industry.



Lara Edmonstone-West
Head of Solutions Distribution

The impact of the recently published [Pension Schemes Bill](#) is only just beginning, with changes influencing DB and DC schemes, master trusts and superfunds. The bill marks a change in UK pension policy, building upon an earlier objective of multiple governments to maximise pension participation – by both extending into seeking to optimise investment returns for individuals and in leveraging the UK’s large pool of pension assets as fuel for domestic economic growth.

Looking at DB schemes, the part of the bill focused on surplus release mechanisms is driving conversation. In recent years, we have seen many DB schemes’ funding levels increase, often to the point of surplus. The bill introduces a resolution-making power that will allow trustees to modify scheme rules to share surplus funds – perhaps unlocking capital that can be injected into the domestic economy.

Surplus detail?

The detail of how surplus extraction will be governed remains in draft, and in the coming months trustees, corporates and their advisers will collectively learn the ‘rules of the road’ as final regulation is expected to be published in 2027. But what do we know today?

Firstly, we know that where scheme rules do not allow for surplus sharing, trustees will be granted power to amend these. Secondly, we know that the threshold for measuring

when surplus can be shared will change from a buyout basis to a ‘low-dependency funding basis’. Thirdly, we know there will be measures in place that aim to manage risks to both members and employers, including a requirement for actuarial certification for surplus release. Finally, we also know the government will not mandate how extracted surplus is to be used.

Perhaps it is the last point that is really driving the conversations we see at trustee tables. How the surplus could be used – for example to enhance member benefits (where the [government has indicated](#) that it will make it easier for one-off payments without incurring large tax bills), or to be returned to the employer (where the authorised surplus payment tax charge has been reduced from 35% to 25%), or to be transferred into a DC pot (where we also expect legislation and market innovation⁴ to make this easier to implement tax efficiently).

How to extract?

Another critical question is: what is the mechanism for surplus extraction? For example, little and often or lump sum? How does the mechanism one chooses ensure we retain fairness – to prevent one layer of membership not getting all the benefits out of a surplus position, while another layer retains the risk of not settling the liability sooner.

The conversations on ‘whom’ and ‘how’ will keep going – and we believe this is good news for the industry. These conversations allow trustees and corporates to consider what surplus extraction means for them – but one thing can be sure – what is right for one scheme will be different for another.

The conversations also drive innovation, especially around the question of how schemes can best invest assets to run on for longer and (perhaps) access surplus. So this brings me back to the title of this piece ‘a time for opportunity’.

Today is just that. An opportunity to pause, discuss and consider the right way forward. Perhaps retaining the status-quo is right, perhaps a change in direction is needed – but the Pensions Schemes Bill provides the industry with an opportunity to consider these points. It’s one we should all embrace.



4. See our press release [L&G facilitates DB surplus transfer to DC schemes](#)

Investing for run-on

Surplus generation and extraction or benefit enhancement provide an additional layer of complexity, but is this really a new concept?



When considering the recent industry discussions around ‘run-on’, many trustees may wonder what all the fuss is about. After all, most pension schemes have ‘run on’ for several decades, often while maintaining a surplus on their technical provisions basis – is there really anything new to consider here?

A sceptic's view

Of course, the fundamentals of pension scheme investment haven't really changed – pension schemes are still long-term investors who must meet liabilities. Surplus generation and benefit enhancement or payment to the sponsor can in some sense just be considered a form of future liability accrual, and pension schemes have dealt with this for decades. The exact form of the new liabilities accrued will depend on how trustees and sponsors plan to use the surplus, and these new liabilities would have increasingly shorter duration and be contingent upon favourable investment returns, but the concept remains broadly similar.

So pension schemes will still need to agree their strategy, define their risk tolerance, and then invest in an efficient portfolio which they believe will generate the highest return while staying within that tolerance. They will still need to diversify rewarded risks, seek to protect against unrewarded risks, and carefully manage liquidity.

And as ever, there will be many different views on what the most ‘efficient’ portfolio looks like. While there is general consensus these days that it can make sense to hedge interest rate and inflation risk using bonds, views on the best way to target additional returns can be much more varied. Some will argue that credit has a special place in liability-matching portfolios, while others will make the case for less liquid assets

delivering income in a more flexible manner. Alpha generation and absolute return strategies will have their proponents of course, while recent equity market performance may lead others to conclude that traditional growth assets still offer the best long-term value. So who's right?

Lessons from life insurers

Before getting lost in the detail of these well-tested arguments, sometimes it's helpful to take a step back and think about the problem from another perspective. Life insurers are the ultimate long-term, low-risk, liability-aware, run-on investors – so what do they do, and why? Sure, they operate under a different regulatory framework, which influences their behaviour to a degree, but that framework is different for a reason. Without recourse to a ‘sponsor’ who can provide deficit payments when needed, and with an ongoing requirement to pay out significant cashflows to meet liabilities each year, they are more vulnerable to short-term changes in their funding position. To seek to avoid the risk of a downwards spiral following a market drawdown, full cashflow matching takes centre stage, alongside an additional capital risk buffer.

So could pension schemes follow the same approach? And should they? Or does the pensions regulatory regime provide them with a competitive advantage and greater flexibility?

The ‘best of both worlds’

Full cashflow matching has undoubted appeal where possible, but it may be challenging for some pension schemes to achieve. And with spreads currently very tight, do liquid cashflow-matching assets provide enough return? Life insurers can access higher yields while still achieving a true cashflow match by investing in long-term illiquid assets such as private credit, but this may not work for pension schemes who still have an eye on a longer-term buyout.

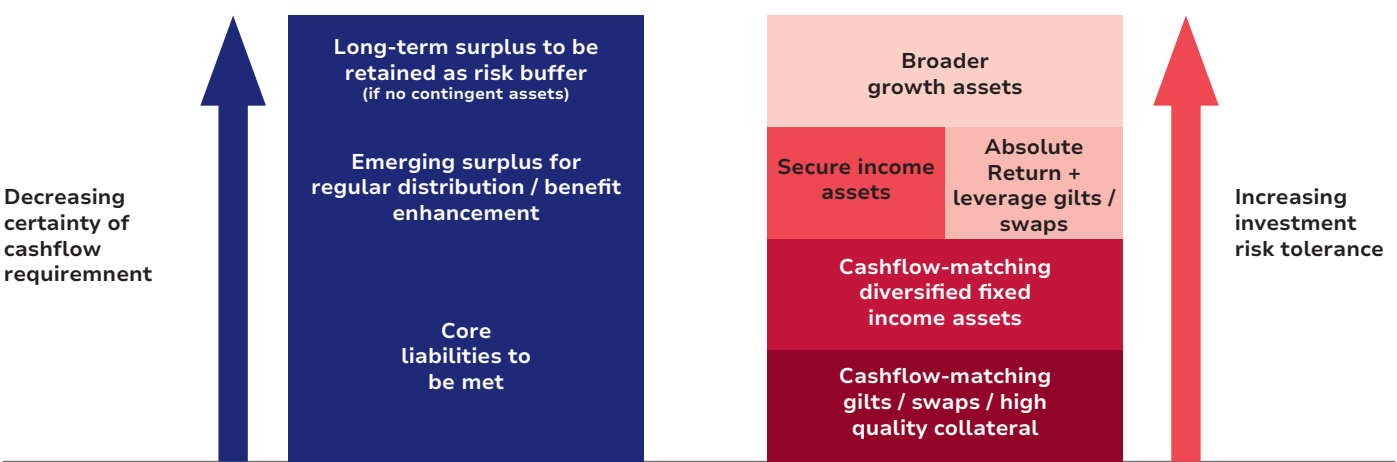
Luckily there are a number of other levers that pension investors can pull to target returns within a cashflow-aware framework. A broad range of alternative credit assets such as emerging market debt and various forms of securitised debt can be incorporated into a cashflow-matching mandate alongside sovereign and corporate bonds. For schemes that can tolerate some illiquidity, this can be supplemented by additional exposure to various forms of cashflow-matching private credit. Further relaxing the requirement for perfect cashflow matching also opens the door to a broader range of ‘secure income’ assets such as infrastructure, real estate and natural capital. And absolute return or short-duration bond

assets can also be incorporated in conjunction with swaps or leveraged gilts, effectively generating hybrid matching/growth exposure.

Some schemes and sponsors may use contingent asset vehicles to provide a risk buffer, or else place more implicit reliance on the sponsor covenant over the long term. But where additional surplus is held in the scheme, a larger surplus cushion provides additional risk tolerance, facilitating potential allocations to assets with greater exposure to the market cycle, such as public and private equity, or lower quality credit or alternative assets.

So will a long-term run-on portfolio look very different to what pension schemes have seen before? Different tolerances for illiquidity, ability to achieve a true cashflow match, and investment beliefs will mean that there is no ‘one-size-fits-all’ answer. Certainly some of the asset classes will look familiar, but trustees’ investment frameworks will need to be refined, risk models made more robust, and investment considered through the lens of cashflow certainty.

Figure 1: Liability cashflow certainty and investment risk tolerance

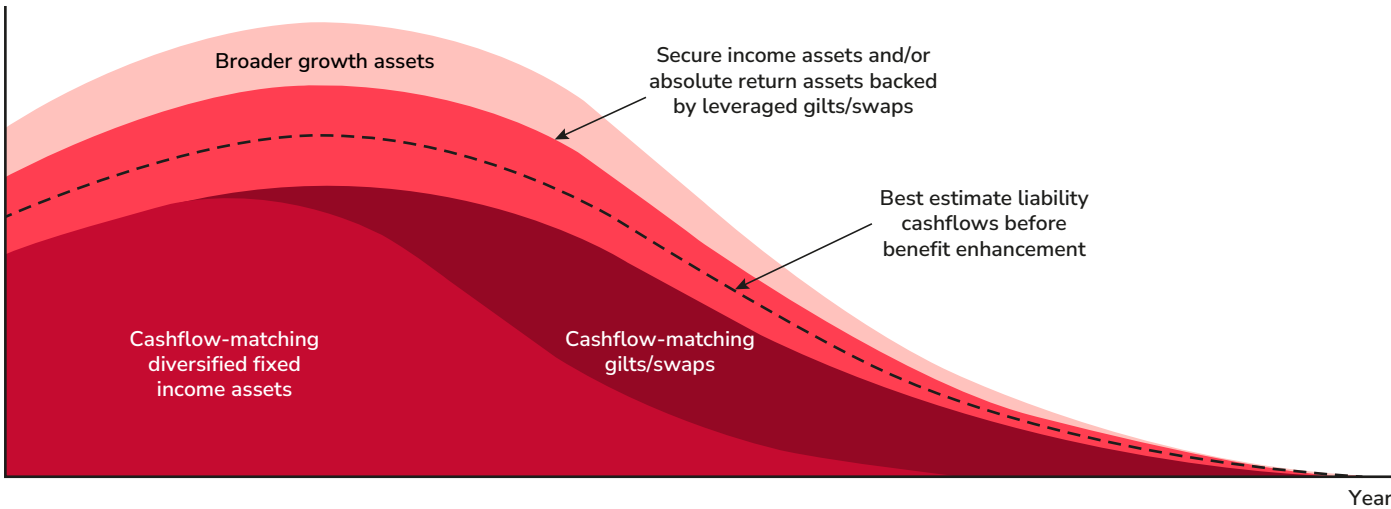


For illustrative purposes only

Key risks
The value of an investment and any income taken from it is not guaranteed and can go down as well as up, and the investor may get back less than the original amount invested. It should be noted that diversification is no guarantee against a loss in a declining market. Assumptions, opinions, and estimates are provided for illustrative purposes only.



Figure 2: Using assets to meet existing liability cashflows, enhance benefits or distribute surplus



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Figure 3: Example asset classes

Category	Asset classes
Cashflow-matching diversified fixed income	Corporate bonds, corporate hybrids, emerging market debt, asset-backed securities (ABS), mortgage-backed securities (MBS, CMBS, RMBS), collateralised loan obligations (CLOs), private corporate debt, infrastructure debt, real-estate debt, alternative private debt
Secure income	Infrastructure, real estate, ground rents, natural capital
Absolute return / Short-duration bonds	Absolute return bonds, alternative risk premia, insurance-linked securities, direct lending, hedge funds
Broader growth assets	Equity, private equity, other alternatives

Responsible innovation

What evolutions in the responsible investment arena should DB trustees have in mind in 2026?



Suzanna Ellard
Solutions Strategy Associate

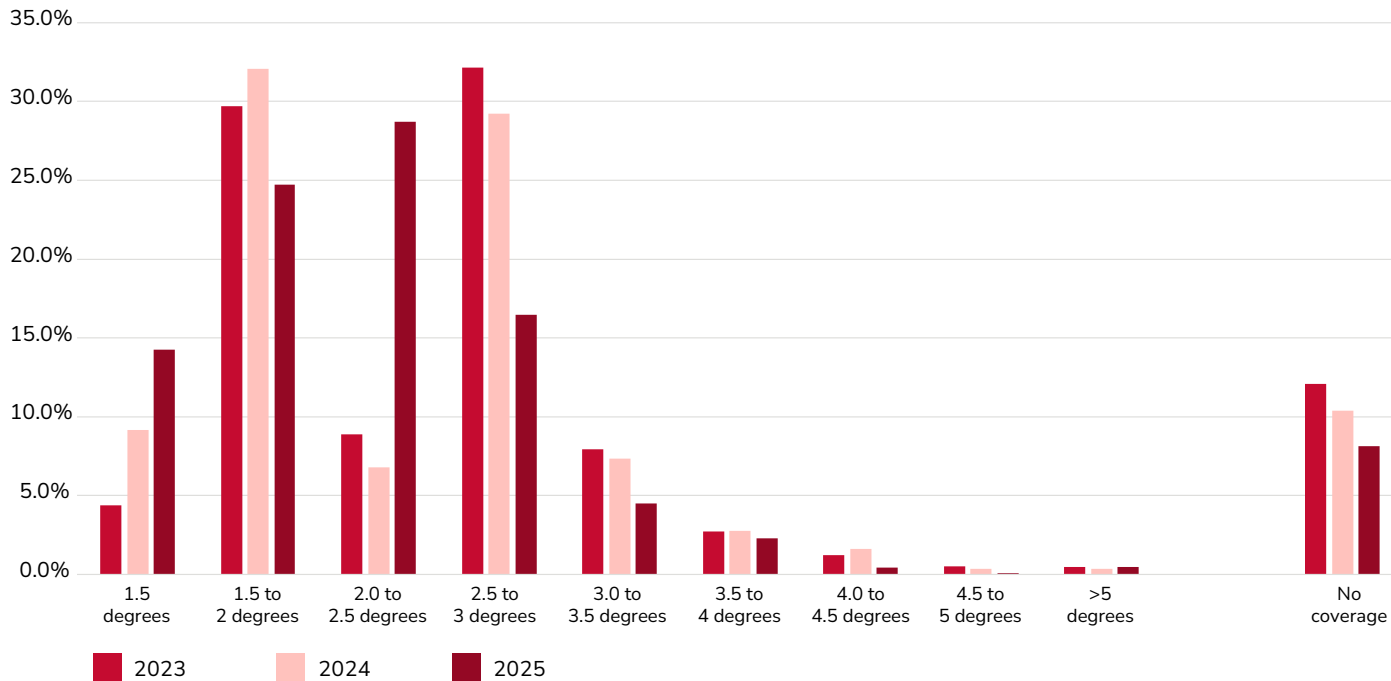
Trustees face an increasingly crowded responsible investment agenda in 2026, with multiple priorities competing for attention. Climate change remains paramount – particularly as commitments from some countries and companies begin to falter, underscoring the need for sustained action. Closely linked to this, nature-related risks such as biodiversity loss and water security are rapidly rising on the investor agenda. Both topics underscore how critical engagement remains for driving meaningful, real-world change.

Climate

The feasibility of the world meeting the objectives set in the Paris Agreement has been and will continue to be called into question. COP 30 has highlighted that despite general agreement about the importance of meeting these goals, the journey remains foggy.

In the last three years we've seen encouraging progress made by companies to meet their climate commitments, with c.10% of the global credit universe improving to a temperature alignment of 1.5 degrees Celsius, although the majority of the global credit universe currently still sits above 2 degrees.

Figure 4: Distribution of the global credit universe as assessed by L&G Destination@Risk



Source: L&G, 31 March 2025. The data presented is that of the Bloomberg USD/EUR/GBP 1% Issuer Capped index. Temperature alignment distribution is based upon L&G Destination@Risk temperature alignment assessment (change in Celsius degrees above pre-industrial levels). Provided for illustrative purposes only.

As we look ahead to 2026, there are three key forces we believe that have the potential to re-define the landscape:

1. Political tensions and the impact on country and company net-zero commitments:

When it comes to progress on climate goals, the global political and economic backdrop is challenging, while the energy landscape is fast evolving. Despite the political backdrop this year, the UK submitted new Nationally Determined Contributions (NDCs) in January, committing to ending petrol car sales by 2030 and reaffirming £11.6bn of international climate finance to be spent between April 2021 and March 2026, with £3bn earmarked for nature protection.* Over 2025 so far, the European Council have amended the EU Climate Law to introduce a binding intermediate 2040 climate target, strengthened the EU Emissions Trading Scheme with the EU Carbon Border Adjustment Mechanism and confirmed that in 2024 the EU contributed €31.7bn in climate finance to support developing countries. Bright spots remain in this stormy sky.

2. The AI data centre build-out and the energy required to support this:

Facing the prospective staggering demand for energy by AI data centres, we expect this will require more power generation than current energy infrastructure supports. This may encourage many to consider less clean energy sources to meet demand. The World Energy Outlook, published by the International Energy Agency, recently warned that global oil and gas demand will rise for the next 25 years without a course correction. This is despite investment in renewable energy continuing to ramp up, especially in China, where investment in renewable energy sources comprises 70% of total investment in energy in 2025 (IEA, World Energy Outlook 2025). As innovation in climate technology accelerates, the future energy-mix to support AI remains up in the air.

3. Investment opportunities in a world where adaptation is the answer:

The independent Climate Change Committee warned in October that the UK must prepare for weather extremes in the scenario that global warming reaches two degrees by 2050. With that in mind, should investors look to support more climate adaption solutions? With estimates of the adaption financing required between 2025 and 2030 in the region of \$200-\$300bn (Investment Opportunities in the Climate A&R Market | BCG) and stark warnings from the World Economic Forum, we believe this may present a potentially attractive investment opportunity.

*Source: <https://eur03.safelinks.protection.outlook.com> and <https://eur03.safelinks.protection.outlook.com>

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The removal of climate objectives for companies and countries may be fed through to the dataset more immediately, while divergence from previously predicted carbon emissions pathways will be fed through slower due to the lags used in carbon emissions datasets. Therefore, we believe that its important pension schemes continue to focus on climate and review the prudence of any objectives in the context of the real world.

Nature

Following roughly three years of climate reporting to meet TCFD requirements for the majority of pension schemes, many now recognize that this is only one piece of the puzzle that affects the resilience of our world as we know it. The Taskforce for Nature-Related Disclosures (TNFD), although voluntary at present, provides a framework for companies and pension schemes to leverage as focus sharpens on this topic.

The data to support many of the proposed metrics lacks the integrity that has been developed in the climate change reporting sphere. Much of the existing data relies on estimates with varying approaches to materiality across the industry, making assessment and management complex. However, company disclosures required in the UK and EU may change this in the coming years with EU anti-deforestation regulation, although delayed to December 2026, and work between TNFD and ISSB to build awareness and capabilities, which would improve scheme's ability to invest in a manner consistent with their responsible investment principles.

Engagement

For trustees, engagement is a powerful mechanism for shaping the future by encouraging more sustainable, long-term practices from companies. Despite regulatory uncertainty and political pushback, engagement continues to be a cornerstone of effective stewardship. We believe transparent engagement strategies are essential for targeting sustainable returns in an increasingly complex global environment, where climate and nature , social factors, and corporate governance practices continue to present material risks to long-term portfolio performance. Our commitment to active ownership remains unwavering through our aim to support long-term value creation through addressing financially material and systemic risks and opportunities.

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Seeking value in bulk annuity transactions

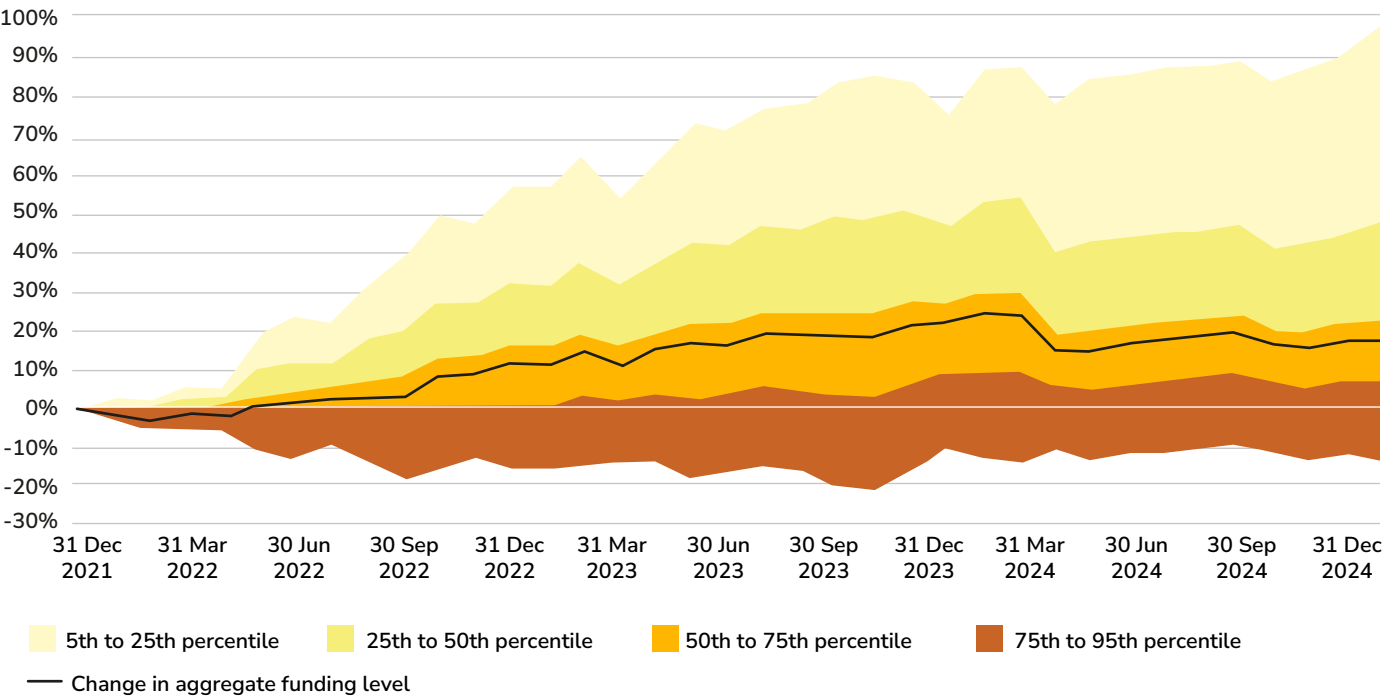
With record numbers of well-funded pension schemes seeking to insure, the question isn't just about affordability and readiness, but how to maximise overall value safely?



Mathew Webb
Head of Endgame Solutions

The Pension Regulator's Annual Funding Statement 2025 estimated that 54% of UK DB schemes were in surplus on a buyout basis as at the end of 2024, equivalent to c.£600bn of buyout liabilities, with a wide dispersion of funding levels on an individual scheme basis.

Figure 5: Variation of impact on funding levels – all schemes (5%, 25%, 50%, 27%, 95% percentiles, 2021-2024)



Source: [TPR Annual Funding Statement analysis 2025](#) (TPR, BoE, LSEG)

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Meanwhile, 2025 is expected to have been another strong year for pension risk transfer, with [LCP estimating](#) c.350 buy-in/out transactions with aggregate value of c.£40bn in 2025.

Put this together and one thing is certain – it will take several years for fully funded schemes to collectively achieve their buyout objectives. Whilst they are preparing for buyout, schemes will want to seek to preserve affordability, improve pricing and manage any residual asset surplus.

Preserving affordability – hedging buyout pricing

Trying to hedge buyout pricing is easier said than done for three main reasons:

- **Liability target:** Liability cashflows within LDI mandates are typically calculated on a technical provisions basis, from member data as at the latest actuarial valuation and rolled forward over time. By contrast, insurers will project a liability profile using up-to-date member data and by adopting their own views on demographic and other liability risks, resulting in a liability profile with a different shape.
- **Discount rate:** A pension scheme may make a prudent assumption on a solvency discount rate – for example 'gilts-flat'. By contrast, live buyout pricing, expressed on a 'gilts+x%' basis is variable over time, primarily because investment opportunities change, for example we have seen insurers move away from corporate bond based investment strategies towards more gilts heavy approaches⁵, and because pricing is also dominated by structural pricing factors⁶.
- **Differences between insurers:** While all insurers are bound by the same Solvency UK framework, each will invest and price differently to achieve the most competitive price to win business.

A pragmatic approach? We believe the best way to hedge buyout pricing is to transact, but before that, pragmatic steps include updating the liability cashflow target to better reflect solvency assumptions (and regularly recalibrating over time) and hedging to a pragmatic prudent discount rate that evolves over time to reflect current pricing levels, including credit sensitivity.

Improving pricing – is time is on your side?

For schemes that can afford to pause, pricing could be improved through:

- **Maturing liabilities:** As a generalisation, it costs less to insure pensioners than deferred pensioners, largely due to risk and uncertainty of both demographic factors (e.g. longevity) and member optionality (e.g. commutation), so the implied buyout price for a scheme should (all else equal) improve over time as members age.

- **Asset returns and realisation:** If the implied buyout price evolves at, for example, gilts+0.25%, but the scheme assets can generate more than that (net of costs), then the buyout surplus can increase. In addition, restructuring illiquid assets before a transaction⁷ may reduce costs and simplify the transaction process, albeit that the insurance market has developed several innovative illiquid asset solutions for buyout⁸.
- **Trigger monitoring:** However, as set above, hedging buyout pricing is difficult – there will always be volatility between a scheme's assets and live insurance pricing, which could be a significant benefit...or detriment to the ultimate price achieved by a scheme. Being in a position where you can not only monitor the scheme's buyout funding level over time, but also transact quickly when the buyout funding level reaches a target level, could generate significant value⁹.

Managing residual asset surplus – what's your target?

Finally, for schemes that transact insurance, there will be a pause between executing a buy-in and then executing a buyout, realising surplus and winding up the scheme.

In this period, how might schemes best invest residual assets? This depends on the purpose of the surplus:

- **Augment member benefits:** Where the final benefits paid to members under the buyout policy can be augmented (increased) with any residual surplus assets, then these assets can be invested to hedge the buyout pricing basis that is defined in the augmentation provision. An investment strategy can be implemented to seek to hedge the augmentation pricing provisions specified by the insurance provider.
- **Transfer surplus to DC:** Where the surplus is to be transferred to an associated DC scheme¹⁰, to be used to fund future contributions, then the associated DB assets could be invested in a similar way to the intended investment strategy to be applied in the DC strategy, preferably so that the assets are easily transferable (or capable of novation) to the DC scheme.
- **Release to the employer:** Finally, if assets are to be repaid to the employer, then these assets could be invested to seek to maintain or grow the expected value to the employer, for example by investing in a low volatility absolute return or short-dated credit investment approach.

As we look ahead to 2026, we expect continued innovation in 'Route to Buyout' approaches that allow well-funded schemes to seek to maximise value in bulk annuity transactions.

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5. See our blog [Investing like an insurer? This seems familiar!](#)
6. See our blog [Interested in Buyout? Strategies for estimating the sensitivity of liabilities to interest rates](#)
7. See our blog [Illiquidity innovation](#)
8. See our website [Illiquid Asset Solutions](#)
9. See our blog [Volatility in the endgame - friend or foe?](#)
10. See our press release

Rising to the challenge

We have now seen the first schemes enter their valuation cycles under the new DB funding code. There is now no option but to have a formal and documented plan.



Victoria Myers
Head of Investment Advisory

Every scheme is in a unique position. Yet integrating funding, investment and covenant matters will continue to be central for trustees seeking to make the best decisions for their members. The strategy conversations we are having with clients are evolving to meet the new challenges; we believe the following key areas will be hot topics for 2026:

Funding and investment strategy alignment

Trustees are now required to document their long-term plan for either buyout or run-on. A wider range of uses for surplus than previously expected will be a major influence on strategic planning for many schemes. A key decision is the intended duration of any run-on arrangement and whether a buyout is targeted at the end of that period.

Running on (rather than buying out at the earliest opportunity) can offer several potential advantages:

- Provide additional or discretionary benefits to members
- Retaining control over member experience and benefit options
- Use surplus to fund employer DC payments or return surplus to the employer
- Allow illiquid assets to mature without forced sales
- Position for a more favourable buyout in future

An investment strategy designed to maintain or grow surplus must be compatible with the new funding code's low-risk investment strategy requirements for mature schemes, balancing liability matching with the pursuit of returns. Notably, the regulator has clarified that the requirement for low-dependency investment does not extend to surplus assets.

Running on will mean a plan for surplus is needed

If a scheme, once it is mature and well-funded, runs a prudent investment strategy with appropriate risk buffers built in, then it can expect to target surplus unless one of its risk events happens. Trustees will then need to have a plan for any surplus generated. A crucial factor here is the minimum funding threshold, above which surplus can be used or refunded. While the government is inclined to allow refunds above the low-dependency funding level, trustees and sponsors may wish to set the bar at the buyout level, possibly with an added buffer for safety.

Trustees and sponsors must agree on safeguards – actions to be taken if funding dips below the agreed threshold. This could involve halting surplus utilisation or taking specific steps to seek to strengthen investments or employer support. Early warning triggers are extremely useful in this context, and can be adapted for surplus upside and downside events.

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Wider factors relating to the value proposition of running on for surplus generation include understanding scheme rules on surplus use, tax implications and systemic risks over the scheme's time horizon such as technological and climate change.

Employer covenant and risk underwriting

The strength of the employer covenant underpins trustees' appetite for risk, investment strategy, and the robustness of run-on arrangements. Trustees must assess the sponsor's willingness and ability to support the scheme, and build this into surplus sharing plans. Sharing surplus as regular payments of a known size may be appealing for the sponsor for planning purposes.

However, this essentially creates additional liabilities, and therefore is likely to impact a scheme's ability to take risk. A contingent approach may be more flexible, but will need to be very clearly documented to ensure expectations are very clear on all sides.

Reducing reliance on the sponsor covenant

For those schemes without the covenant strength to support long-term run-on, the new freedoms may ignite interest in downside risk management, to support run-on. Capital-backed journey plans and self-insurance may see a wider range of use cases. Replacing the covenant may also become more attractive if members benefit from, for example, consolidating with a pension superfund.

Operational and governance considerations

Effective scheme governance is critical for running on successfully. Trustees must already assess their own expertise, seek advice where necessary, and ensure robust policies for cost management and adviser/provider oversight. Running on whilst distributing surplus extends the discussions needed around intergenerational and cross member fairness of distributions or benefit changes.

Recent regulatory change – that is encouraging DB pension schemes to run on and target value for members and their sponsors – is opening up more choice for trustees. Whilst this is welcome, it creates further work for trustees to assess the options. For those considering long-term run-on, it is our view that good governance, clear policies, effective delegation, and ongoing collaboration will be essential to achieving the best outcomes for both members and sponsors.

Risk management cannot fully eliminate the risk of investment loss.



Contact us:

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