<table>
<tr><th colspan="3">Bath & North East Somerset Council</th></tr>
<tr><td>MEETING:</td><td colspan="2">LOCAL PENSION BOARD - AVON PENSION FUND</td></tr>
<tr><td>MEETING DATE:</td><td>07 December 2023</td><td>AGENDA ITEM NUMBER</td></tr>
<tr><td>TITLE:</td><td colspan="2">Death in Service Captive Insurance Consultation</td></tr>
<tr><td>WARD:</td><td colspan="2">ALL</td></tr>
<tr><td colspan="3">AN OPEN PUBLIC ITEM</td></tr>
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Appendix 1 –Death In Service Captive Insurance Consultation</td></tr>
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1 THE ISSUE

1.1 One risk for employers is the potential rise in liabilities when an active member dies, as their beneficiary receives a lump sum and partner's pension earlier than they ordinarily would. Although the actuary includes an allowance for 'strain' costs due to Death in Service (DIS) when setting future service contributions, actual strain or indeed saving, is determined by the member's profile and can be far greater (or less) than the allowance assumed by the Actuary.

1.2 If there is a strain, it can significantly increase the liabilities and will feed through into the employer funding plan at the next valuation. For small employers the higher costs can be difficult to manage especially when they occur close to the employer's exit from the Fund.

1.3 The feasible options to mitigate this risk are (i) captive insurance and (ii) 3rd party insurance. Maintaining the status quo will not manage the risk. The Actuary is proposing the Fund implements a captive insurance arrangement covering all employers within the Fund. The Fund already has a similar arrangement for managing ill-health retirement costs for smaller employers.

1.4 The Pensions Committee approved implementing a DIS captive arrangement at its meeting in June 2023, subject to employer consultation which ended on 30 September 2023. The purpose of this paper is to consult with the Local Pensions Board. Once the consultation is complete the Funding Strategy Statement (FSS) will be updated.

2 RECOMMENDATIONS

2.1 That the Board provides feedback on the proposed DIS captive insurance for employers in Avon Pension Fund.

3 FINANCIAL IMPLICATIONS

3.1 There are no extra direct costs as a result of this arrangement as currently any strain costs are picked up by employers at the subsequent valuation. The captive would aggregate the 'notional premiums' based on the actuarial assumptions and these premiums will be used to meet any future DIS strain costs.

4. DEATH IN SERVICE CAPTIVE ARRANGEMENT

4.1 The Mercer's paper (appendix 1) was sent to employers for their feedback. It sets out the rationale for setting up a DIS captive arrangement.

4.2 A captive arrangement is a cost effective and transparent method of managing this financial risk for smaller employers. However, to ensure the captive arrangement has adequate funds to meet any strain cost that may arise, all employers will be included in the arrangement.

4.3 The captive would work as follows:

(a) Notional average 'premiums' will be paid into a captive fund by all employers, based on same actuarial assumptions. The actuary will monitor the captive and update at each triennial valuation (as they do with the ill health captive arrangement).

(b) The captive is used to meet any strain costs or receive any gains, therefore there is no funding gain or loss on the funding position of employers.

(c) The premium charged will be reviewed each triennial valuation and if excess premiums build up they will be used to offset future adverse experience and/or lower premiums based on the advice of the Actuary. Likewise any excess costs will be recovered via an increase in the premium.

4.4 In the 2022 valuation the **average** DIS allowance at the overall Fund level was 0.5% of pensionable pay, determined for each individual employer by their member profile. Based on 2022 valuation payroll this is equivalent to £4.14m p.a.

4.5 If only the smallest employers were in the captive, the premium would have to be far higher to cover potential strain costs. Therefore it is proposed that all employers would be included in the captive.

4.6 Alternatives:

(i) 3rd party insurance. The main disadvantage of 3rd party insurance is that the spouse's/partner's pension is not normally insurable so the Fund would have to insure a far higher DIS lump sum to cover the costs. The premium would be reset periodically based on experience and demographics which could lead to higher or lower costs. In addition there would be greater governance and admin costs for the Fund.

(ii) Maintain the status quo. This does not enable the Fund to manage the risk DIS poses to smaller employers within the Fund.

4.7 Across the LGPS there are different models in place. Some have no arrangement in place (like Avon currently), some pool risks by employer groups and some use captive arrangements. There is no standard approach.

4.8 Having considered the alternatives, a captive DIS arrangement is considered the most efficient approach for the Fund to manage the risk of adverse strain costs for smaller employers.

4.9 The Fund will review the insurance arrangements at least every 3 years at the time of the triennial valuation. This will include market testing 3rd party pricing.

4.10 The employing bodies have been consulted about the change and the results of the consultation were as follows:

Summary of Consulation Responses		
Town and Parish Councils	8	3 - no comments, 4 - support, 1 queries responded to and no furthur reply.
Admitted Bodies	1	Wanted to understand DIS benefits so as not to duplicate costs
Academy Trusts	2	1- no comments, 1 - support
Higher Education employer	2	2 - support, 1 - requested supplementary report at trienniel valuations
Principal Council	1	Queries responded to and no furthur reply.
Total	14	

4.11 Following the consultation, as there are no substantive amendments to the proposed policy approved by the Committee, the FSS will be updated to include the new policy.

4 RISK MANAGEMENT

4.1 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 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.

5 EQUALITIES STATEMENT

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

6 CLIMATE CHANGE

6.1 The Fund is implementing a digital strategy across all its operations and communications with stakeholders to reduce its internal carbon footprint in line with the Council's Climate Strategy. The Fund acknowledges the financial risk to its assets from climate change and is addressing this through its strategic asset allocation to Paris Aligned Global Equities, Sustainable Equities and renewable energy opportunities. The strategy is monitored and reviewed by the Committee

7 OTHER OPTIONS CONSIDERED

7.1 Are contained in the Report.

8 CONSULTATION

8.1 The Report and its contents have been discussed with the Head of Pensions representing the Avon Pension Fund and the Service Director – One West representing the administering authority.

Contact person	Liz Woodyard, Group Manager Funding, Investments and Risk 01225 395306
Background papers	None
Please contact the report author if you need to access this report in an alternative format	