

# Report

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Report to:	<b>Finance and Information Technology Resources Committee</b>
Date of Meeting:	<b>16 March 2010</b>
Report by:	<b>Executive Director (Finance and Information Technology Resources)</b>

Subject:	<b>2009 Actuarial Review of Council's Self Insurance Fund</b>
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## 1. Purpose of Report

1.1. The purpose of the report is to:-

- ♦ provide an update on the financial health of South Lanarkshire Council's self insurance fund, following the regular actuarial review.

## 2. Recommendation(s)

2.1. The Committee is asked to approve the following recommendation(s):-

- (1) that they note that the fund was only marginally in surplus as at 31 March 2009
- (2) that the improvement actions in Appendix 1 are approved
- (3) that a contingent liability of £902,000 should be noted in the 2009/2010 final accounts
- (4) that insurance policy cancellation decisions be delegated to the Executive Director of Finance and Information Technology Resources and the Chair of the Finance and Information Technology Resources Committee in consultation with the Chief Executive and Leader of the Council
- (5) that they note that the fund will be topped up with £4.675million over financial years 2009/10 and 2010/11 to cover future pressures.

## 3. Background

3.1. South Lanarkshire Council (SLC) operates a self insurance fund to pay for purchased insurance cover, the settlement of excesses for liability and property claims against the Council and the cost of administering an in-house risk management section.

3.2. The Local Authority (Scotland) Accounts Advisory Committee (LASAAC) advises that regular actuarial reviews should be undertaken on insurance funds. The last review of the SLC fund took place in 2005. Following a competitive tender exercise HJC Actuarial Consulting Limited was appointed to undertake an updated review as at 31 March 2009.

- 3.3. In 2008 and 2009 a number of disease related claims from employees of former authorities were received and the extent of the Council's exposure to such potentially uninsured claims was unknown. The actuary was asked therefore to extend his study to calculate the likely total cost of potential disease claims. His report was received by the Council in December 2009.

#### **4. Findings**

- 4.1. The actuary's overall conclusion was that the fund has remained relatively stable since the last review, namely that income has largely covered expenditure. In addition, the fund meets the minimum requirement of having a surplus assuming wind-up at 31 March 2009. However, the surplus of £100,000 was very small and insufficient to avoid a deficit occurring by 31 March 2010. In addition, this level of surplus could not be expected to cover all financial pressures associated with disease claims. As well as topping up the fund, other recommendations were also made to improve the management of the fund (see appendix 1). Committee is asked to note the actuarial opinion and the actions being taken to improve fund management.
- 4.2. In relation to the longer term pressures on the fund relating to disease claims, no insurance cover can be proven for the years prior to 1975 so estimated claims of around £3million may need to be funded by the Council. Earlier in house projections of disease claims were estimated at only £600,000.
- 4.3. Whilst there appears to be some insurance cover in place with a mutual insurance company covering the period 1975 to 1993, the financial stability of this insurer is weak. This means, firstly, there is an increased likelihood that "incurred but not yet reported" (IBNR) claims from the SLC area may need to be paid by the Council (around £1million) and secondly a substantial cash contribution may be called for under a "scheme of arrangement" agreed by insured bodies in 1993.
- 4.4. The "scheme of arrangement" allows the Board of the mutual company to declare the company insolvent when it is unable to fund losses and to call in a final contribution from insured members. This is known as "claw back" and is estimated at £902,000 for the former authorities now covered by SLC. This will be included as a contingent liability in the 2009/10 annual accounts.
- 4.5. It may be possible to mitigate against payment of some of the claw back and this is being explored at present. Committee is asked to note this research and is asked to approve delegation of related decisions to the Executive Director of Finance and Information Technology Resources and the Chair of the Finance and Information Technology Resources Committee in consultation with the Chief Executive and Leader of the Council.

#### **5. Employee Implications**

- 5.1. There are no employee implications associated with the proposals in this report.

#### **6. Financial Implications**

- 6.1. The following table indicates the minimum expected financial pressures on the SLC self insurance fund.

Table 1 – Probable outturn 31 March 2010

Item no	Item	Value in £millions	Notes
1	Insurance fund balance at 31 March 2009	+£4.300	
2	Estimated value of claims still to be paid out for claims occurring prior between 1 April 1996 and 31 March 2009	-£4.200	
<b>3</b>	<b>Estimated surplus at 31 March 2009 pre disease claims</b>	<b>+£0.100</b>	<b>Item 1 less item 2</b>
4	Potential mutual scheme of arrangement claw back	-£0.902	High risk contingent liability <ul style="list-style-type: none"> <li>• Clydesdale £0.087</li> <li>• Hamilton £0.437</li> <li>• SRC £0.368</li> <li>• East Kilbride £0</li> <li>• R'Glen/Cambuslang £0.010</li> </ul>
5	Reserve build up (Property including climate change risks)	-£1.000	Maximum property exposure of £1million per annum (aggregate limits) and flexibility to reduce external premium spend in future.
6	Potential non payment by mutual of future claims i.e. IBNR claims 1975-1995	-£1.000	High risk contingent liability
7	IBNR disease claims pre 1975	-£3.000	Pessimistic view based on latest cases. Previous in-house projections £500k to £650k
<b>8</b>	<b>Estimated deficit at 31 March 2009 including disease claims</b>	<b>-£5.802</b>	<b>Item 3 less items 4 to 7</b>
9	Estimated 09/10 payments	-£4.450	Premiums £1.45 Overheads £0.40 Actuary claims est. £2.10 Handler addn. est. £0.50
10	Expected contribution from Resources for 09/10	+£3.462	
<b>11</b>	<b>Estimated deficit at 31 March 2010</b>	<b>-£6.790</b>	<b>Item 8 less item 9 plus item 10</b>
12	Further reductions	+£1.902	<ul style="list-style-type: none"> <li>• Use of actuarial estimates rather than external reserving £0.500</li> <li>• Treat "claw back" as contingent liability in note to accounts rather than a pressure on insurance fund £0.920 (refer to note 4 above)</li> <li>• Reduction of 50% in property reserves build up £0.500</li> </ul>
<b>13</b>	<b>Net likely maximum deficit at 31 March 2010</b>	<b>-£4.888</b>	
14	March/April 2010 year end proposed fund top-up	+£4.675	2009/10 year end 2010/11 budgeted contribution
15	Resultant fund deficit going forward	-£0.213	

- 6.2. Committee is asked to note that the insurance fund will be topped up with £2.5m from 2009/10 year end reserves and £2.175m from 2010/11 budget. Although these projections show a marginal deficit, it is likely many claims will be settled after 31 March 2010, therefore this will be managed through cash flow.

## **7. Other Implications**

- 7.1. Mitigation activity in relation to the scheme of arrangement claw back could risk insolvency for the mutual insurer providing cover between 1975 and 1993. This, in turn, could financially impact other insured bodies. SLC is mindful of this financial risk to other authorities so is restricting its activity at present.

## **8. Equality Impact Assessment and Consultation Arrangements**

- 8.1. There are no equalities issues related to the proposals in this report. North Lanarkshire, Renfrewshire and Glasgow City Councils are being consulted in relation to the scheme of arrangement.

**Linda Hardie**

**Executive Director (Finance and Information Technology Resources)**

24 February 2010

### **Link(s) to Council Values and Objectives**

- ♦ Value: Accountable, effective and efficient

### **Previous References**

None

### **List of Background Papers**

- ♦ Letter from actuary and executive summary of Independent Actuarial Review
- ♦ Four actuarial draft reports December 2009
- ♦ Commutation report January 2010

### **Contact for Further Information**

If you would like to inspect the background papers or want further information, please contact:-

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## Appendix 1

### Proposed improvement actions to be taken by SLC re self insurance fund following receipt of actuarial recommendations

Ref	Actuarial Recommendation	Action	Responsibility	Due date	Status at end February 2010
1	Continue annual data collection	None as twice yearly in-house projections undertaken currently	n/a	n/a	
2	Audit of missing data	None as twice yearly in-house projections undertaken currently	n/a	n/a	
3	"Management letter", "mini review" or "health check" every 24 months	Commission short independent fund health checks in between full actuarial reviews every two years.	Risk Officer	30 July 2011	Annual in-house projections will continue
4	Develop medium term funding strategy	Include longer term insurance funding as part of medium term financial strategy	Head of Finance	30 July 2010	
5	See recommendation 4	Top up insurance fund to a level which provides for a minimum cover for future claims	Head of Finance	30 April 2010	£4.675m approved
6	Review the strategic alternatives available to the mutual "status quo"	Identify costs and benefits of strategic cancellation of some insurance policies as alternatives to mutual "claw back"	Risk and Audit Manager	31 March 2010	WIP
7	Re-assess optimal insurance programme design	Re-assess optimal insurance programme as part of next renewal	Risk Advisor with brokers	31 March 2010	Part of broker contract
8	Transform presentation of risks to insurers	Re-design presentation of risks to market as part of next renewal	Risk Advisor with brokers	31 March 2011	Part of broker contract
9	Improve insurer financial assessment process	Extend the structured review of financial appraisal system to include specifics checks for future insurers	Head of Finance	31 July 2010	Need for structured financial appraisals already identified as a risk control action

Ref	Actuarial Recommendation	Action	Responsibility	Due date	Status at end February 2010
10	Cost/ benefits of joining any future mutual/pooling insurance arrangements	None as already explored pooling with other Scottish Local Authorities at some cost but support lacking from other bigger Councils	n/a	n/a	
11	Review re-charging to services	Revise Resource contributions and decide whether to change in the interest of encouraging claims ownership and introducing incentives for reducing claims	Risk Officer with A and B Manager	30 May 2010	Previous models can quickly be updated
12	Contingent asset provision of £0 in respect of potential future Scheme Commission for the MMI scheme of arrangement	None as no asset held	n/a	n/a	
13	Contingent liability provision of at least £1m in respect of the potential "claw back" for the MMI scheme of arrangement	Include contingent liability of £902,000 in accounts for "claw back" in relation to scheme of arrangement	Head of Finance	31 March 2010	An alternative is to make provision in the annual fund projections
14	Review strategic alternatives for MMI "claw back"	Further research risk mitigation of MMI "claw back"	Risk and Audit Manager	30 April 2010	Further study commissioned
15	See recommendation 14	Liaise with other authorities regarding exposures for former Glasgow and district Councils	Risk and Audit Manager	30 April 2010	Two of three Councils consulted have replied and wish to work jointly
16	Carry out a materiality check on the potential future (IBNR) claims	Monitor disease claims against current estimates as part of annual projections and if significant variances occur, formally review disease exposures within next three years	Risk Officer	31 March 2011	In-house projections are undertaken twice per year

Ref	Actuarial Recommendation	Action	Responsibility	Due date	Status at end February 2010
17	A further "materiality check" project within the next three years, sooner if a significant number or amount of new asbestos claims reported	See action 16	n/a	n/a	
18	Confirm proof of coverage/extent of recoveries/liabilities under Glasgow policies	See action 15	n/a	n/a	
19	Confirm proof of coverage/extent of recoveries under IBNR run-off policy for ex SRC claims	See action 15	n/a	n/a	
20	Research historic risk management standards/historic asbestos incidents	Present historical local agreements for joint management of historic asbestos incidents	Executive Director Finance and IT	30 April 2010	Directors of Finance agreement recovered and approach made to NLC
21	Give serious consideration to commuting all mutual policies (for at least Hamilton, which has the largest "claw back" exposure	Decide on whether to take mitigating action against claw back in relation to selected area/areas	Executive Director Finance and IT	30 April 2010	Preliminary research complete

