HAMPSHIRE COUNTY COUNCIL

Report

Decision Maker:	Cabinet
Date:	3 February 2020
Title:	Insurance Strategy
Report From:	Director of Transformation and Governance

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Purpose of this Report

1. The purpose of this paper is to outline to the Cabinet the County Council's approach to insurance that is articulated in an Insurance Strategy, which Cabinet is asked to adopt.

Recommendations

2. **That Cabinet:**

   a. Notes the contents of this Report.

   b. Agrees that the County Council should continue to maintain its overall approach to insurance whereby the County Council self-insures its assets and liabilities, subject to appropriate catastrophe insurance cover purchased from the commercial insurance market, supplemented by commercial insurance where necessary and appropriate.

   c. Approves the adoption of an Insurance Strategy (Appendix 1).

   d. Delegates authority to the Head of Law and Governance, in consultation with the Director of Corporate Resources, to review and update the Insurance Strategy on an annual basis.

   e. Recommends to the Full Council that Financial Regulations are amended by the addition of the wording set out in Paragraph 42 of this Report.

   f. Notes the changes to Financial Procedures set out in Paragraph 43 of this Report.

Executive Summary

3. This paper seeks to provide the Cabinet with comprehensive and accessible details of the County Councils insurance arrangements, in accordance with the County Council's Financial Regulations, and seeks approval of an Insurance Strategy (attached to this report as Appendix 1).

4. The report focuses on the County Council's arrangements for risk financing, specifically its insurance arrangements.

5. A key element of its overall approach to risk is the strategic approach the County Council follows towards self-funding insurable losses; that is, using commercial insurance only where there are compulsory requirements or where it has deemed it more appropriate to do so, particularly to provide a cap to its financial liabilities in respect of third-party liability claims.

6. The County Council's insurance arrangements are a mixture of self-insurance and commercially purchased insurance, with decisions on the balance between the two based on risk. The insurance arrangements cover the various activities and services undertaken by the County Council and include both staff and Members.

7. A review of the County Council's insurance arrangements has been undertaken in conjunction with the County Councils Insurance Brokers and Insurers. A number of changes have been implemented, with further options for improvements to be included in the tender of the major insurance contracts scheduled for 2020, with details of those improvements included in this paper.

8. This also paper advises the Cabinet as to recent developments in the local authority insurance arena, including changes to the calculation of the discount rate and associated changes in premiums in consequence.

Insurance Strategy

9. The County Council's insurance strategy provides the framework to ensure that the County Council has in place an optimal balance between external insurance and self-insurance, an evidence based calculation and maintenance of the insurance reserve, and that appropriate and robust arrangements are in place for the handling of insurance claims. As a large organisation, with a diverse portfolio of assets and liabilities, it is prudent for the County Council to insure itself against the financial consequences of unexpected events.

10. Insurance comes at a cost however, and the County Council has to undertake a number of risk-based decisions to determine the most effective balance between the cost of commercial insurance and the cost of retaining the risk through self-insurance.

11. Insurance is a financial mechanism through which an individual or organisation can transfer an unknown potential liability into the certainty of a smaller but fixed annual cost. By combining a large number of exposures into a group, the insurer can predict the probability of loss relating to uncertain events with a degree of accuracy for the group as a whole. With large organisations, such as the County Council, that combining of large numbers of exposures can be undertaken across the organisation with similar degrees of accuracy in relation to possible losses to the whole organisation.

12. The County Council has, for the last 40 years, followed the strategic approach of self-funding insurable losses, using commercial insurance only where there are compulsory requirements or where it has deemed it more appropriate to do so, particularly to provide a cap to its financial liabilities in respect of third-party liability claims.

13. The County Council's insurance arrangements are therefore a mixture of self-insurance and commercially purchased insurance, with decisions on the balance between the two based on risk.

14. The arrangements fall into three groupings:
    a) risks that the County Council entirely self-insures
    b) risks that the County Council self-insures, with commercially obtained insurance that caps the amount of losses
    c) risks that have the benefit of commercially obtained insurance cover

15. Under the self-insuring arrangements (a & b), losses are met from monies set aside for the purpose, on the basis of defined events, just as though there was conventional insurance cover. At the County Council this is referred to as the Insurance Fund.

16. Each year the County Council sets aside an insurance provision in the Insurance Fund to meet claims resulting from incidents that have occurred during the year, along with reserves to cover potential claims arising from incidents in that year but where the claims are received in the future.

17. Decisions about the risks and the appropriate self-funding provision for them are made based on a balance of four factors:
    a) **Risk Tolerance**: The County Council's capability to withstand shocks.
    b) **Risk Appetite**: The County Council's willingness to assume insurance risk

c) **Risk Modelling**: The profile of our insurance loss distributions (e.g. previous claims)

d) **Market Pricing**: How insurers will price our risk.

18. Details of the decisions that are made to balance the risk between self-insurance and commercial insurance (risk retention versus risk transfer) and an outline of the various insurances are outlined in Sections 2 and 3 of the Insurance Strategy that is appended to this report.

19. The Insurance Strategy will be reviewed, and updated as appropriate, on an annual basis by the Head of Law and Governance, in consultation with the Director of Corporate Resources, to ensure its continual fitness for purpose.

Details of the actuarial reports that inform the funding provision in the Insurance Fund.

20. The principle of self-insurance is that the County Council sets aside a sum of money from which insurable losses (i.e. claims) can be met.

21. To assist in the calculation of the appropriate sum to set aside in its Insurance Fund, the County Council uses the services of external actuaries employed by its broker.

22. The Insurance Fund maintained by the County Council has been subject to regular actuarial review and the conclusions of the most recent review are explored in more detail below. In addition, the claims handling processes operated by the County Council's Legal Services are audited by insurers to ensure that they comply with best practice.

23. Actuarial reviews were held in 2011 and 2014, both of which recommended no significant changes. A further actuarial review of the County Council's Insurance Fund was undertaken in 2017.

24. The broad assessment of the actuary was that the amount set aside for claims occurring and paid in each financial year was appropriate, but that there was a possible shortfall in the amount set aside for historic claims. The review recommended increasing the amount set aside to reserve against future claims for historic events.

25. A proportionate and long-term approach has been taken to adjusting the Insurance Fund to reflect the assumptions of the 2017 actuarial review, given that the County Council would not expect all potential liabilities to arise at the same time. An adjustment was made as part of the final accounts for 2017/18 with an additional year end contribution.

26. The intention is to regularly review the Insurance Fund and to make year end contributions that move the County Council towards the level outlined in the latest actuarial assessment over time.

27. A further actuarial report was commissioned as part of a biannual programme and to provide background information in advance of tendering the major commercial insurance policies later in the year. The County Council is awaiting the conclusion of the actuarial evaluation and will take a proportionate and long-term approach to any recommended adjustments.

28. The difference in the conclusions reached by the actuaries in 2011, 2014 and those in 2017 is due to increasing claims costs and the rising number of complex historic claims being made. This has led to actuaries altering the methodology and assumptions they use when calculating reserves for historic claims. It is fair to say that the conclusions of the 2017 actuarial report are in line with the experience of those insurance companies that are underwriting business in the local authority marketplace.

29. In coming to these conclusions, the actuaries have also taken into consideration the potential for occupational disease claims which may take decades to gestate, including: mesothelioma, fibrosis of the lung tissue, lung cancer, noise induced deafness, vibration white finger, upper limb disorders, skin diseases and asthma, along with emerging losses such as stress, post-traumatic stress disorder, bullying, abuse and sexual harassment.

Review of the County Councils Purchased Insurance

30. In consultation with the County Council's Insurance Brokers and Insurers, Officers have undertaken a focused review of the County Council's insurance arrangements. A number of changes have been implemented as a result, with further options being explored as part of the tender of the commercially purchased major insurance policies for April 2020.

31. The limit of indemnity for public indemnity claims, i.e. the maximum amount insured for each claim or series of claims has been reviewed. This is in line with reviews undertaken by a number of local authorities following the Grenfell fire in 2017 and the size of claims arising from that tragic event. In line with decisions made by other large Local Authorities, additional layers of insurance have therefore been purchased to raise the previous limit of indemnity from £50 million per incident to a figure of £200 million, with effect 1 February 2019.

32. The personal accident arrangements for Elected Members have been incorporate into the County Council's Travel Insurance Policy from the previous stand-alone arrangement. The Policy cover remains the same but is now provided more efficiently.

33. Options are being explored with the County Council's current property insurers on the cost effectiveness of providing a possible cap to the County Council's liability for multiple property losses across key parts of the built estate, for example in the event of multiple fires effecting a number of buildings within the same year.

34. Options have also been explored in relation to professional indemnity insurance cover to reflect the increasing commercial activities that the County Council is engaged in, across a wide spectrum of services. Again, insurance brokers have advised to explore options in detail with the current insurers over a period of months leading to implementation of any changes for April 2020.

Recent developments in the local authority insurance arena

35. A number of developments have recently occurred that have affected the Local Authority Insurance Market and Hampshire County Council.

36. In February 2017 the Lord Chancellor announced changes to the calculation of the discount rate used to calculate the appropriate settlement in complex personal injury claims.

37. When victims of life-changing injuries accept lump sum compensation payments, the actual amount they receive is adjusted according to the interest they can expect to earn by investing it. In finalising the compensation amount, courts apply a calculation called the Discount Rate – with the percentage linked in law to returns on the lowest risk investments, typically Index Linked Gilts. The changes announced by the Lord Chancellor increased settlement amounts in such cases, having a significant effect on insurers and organisations like the County Council which bear much of the cost of settlements themselves. On 15 July 2019 the Lord Chancellor announced a slight amendment to the rate that will be in place from 5 August 2020 for the next 5 years.

38. The effect of the changes has caused insurers to raise insurance premiums, with both insurers and self-insurers making greater provisions for higher claims costs in future.

39. In addition, all insurers are seeing a rise in the number of complex major claims that do not fit into previous underwriting models, i.e. they are unexpected and not part of any pattern. This has resulted in insurers making additional provision within premiums for these "black swan" events.

40. On 1 June 2017 the standard rate of Insurance Premium Tax (IPT) increased from 10% to 12%. This followed a previous rise in 2016. This tax is levied on

all insurance premiums. Unlike VAT the County Council is unable to claim back any of this tax. It affects the cost of external insurance premiums, but not any self-insurance costs. Industry commentators are predicting that IPT will eventually level out on a par with VAT.

41. The Local Government Association (LGA) has been working on the establishment of a Local Government Insurance Mutual. This is a stand-alone provider of insurance for Local Authorities through a pooled risk arrangement. Members of the mutual would pay into a central fund, operated by representatives of the members, from which insurance claims could be paid. A similar arrangement was in place up until 1992, in the form of the Municipal Mutual Insurance Company, which went into administration and run off in 1992. An advantage of this arrangement is that any surpluses would be retained by the members of the pool, in the same way that currently any surpluses from the County Council's self-insurance arrangements are retained by the County Council. A disadvantage for the County Council of this arrangement is its newness in a complex marketplace and potential loss of some control over the claims handling and settlement of claims. Officers are taking a watching brief on developments, but do not recommend participation in the LGA mutual at this time as the County Council already benefits from many of the advantages of a mutual through its self-insurance arrangements.

Governance Arrangements

42. In order to provide certainty about the responsibility for the Insurance Fund it is suggested that Financial Regulations are amended as follows:

    a) A new paragraph 3.13 titled 'Maintenance of an Insurance Reserve' is added to Financial Regulations. The new paragraph to be as follows

    'It is the responsibility of the Chief Financial Officer to advise the County Council and the Cabinet on the prudent level of Insurance Reserve required to meet the assessed potential liabilities of the County Council.'

43. In the meantime a new paragraph C1.11 has been added to Financial Procedures as follows:

    a) The Chief Financial Officer has responsibility on the advice of the Head of Law and Governance for determining whether or not a claim (both internal departmental claims on the County Council's Insurance Reserve and third-party claims) are covered by the County Council's self-insurance arrangements.

Finance

44. The decision which is sought to be recommended by this report will have no effect upon the budgetary position of Hampshire County Council.

Performance

45. The recommended decision sought ensures that the County Council continues to maintain appropriate measures to mitigate the financial impact of insurable events.

Conclusions

46. The County Council’s insurance approach has provided a stable and consistent financial platform from which to meet the costs of insurable events to its assets and liabilities, with external spend on insurance being kept at a minimum.

47. The decision to purchase catastrophe cover for its liability programme made by the County Council in 2002 has placed an effective cap on potential costs. However current circumstances mean that it is appropriate that a review of the arrangements for property insurance is undertaken to determine whether similar catastrophe insurance in this area would be cost effective.

48. During the period since 1992, the local authority insurance market has been volatile, with a number of company failures and withdrawals of companies from underwriting local authority business. In addition, premium costs have swung dramatically during this period. The County Council has benefited from a stable cost basis due to the high level of self-insurance it has operated.

49. Regular actuarial reviews on the Insurance Fund have provided assurance that the County Council has been setting aside appropriate levels of funding against future liabilities during this period, although changes to the way that claims will be funded going forward have caused actuaries to alter their calculation models and a need to adopt a long-term approach to increasing that provision going forward.

REQUIRED CORPORATE AND LEGAL INFORMATION:

Links to the Strategic Plan

Hampshire maintains strong and sustainable economic growth and prosperity:	yes
People in Hampshire live safe, healthy and independent lives:	yes
People in Hampshire enjoy a rich and diverse environment:	no
People in Hampshire enjoy being part of strong, inclusive communities:	no

Other Significant Links

Links to previous Member decisions:	
Title	Date
Direct links to specific legislation or Government Directives	
Title	Date

Section 100 D - Local Government Act 1972 - background documents

The following documents discuss facts or matters on which this report, or an important part of it, is based and have been relied upon to a material extent in the preparation of this report. (NB: the list excludes published works and any documents which disclose exempt or confidential information as defined in the Act.)

Document	Location
None	

EQUALITIES IMPACT ASSESSMENT:

1. **Equality Duty**

The County Council has a duty under Section 149 of the Equality Act 2010 ('the Act') to have due regard in the exercise of its functions to the need to:

- Eliminate discrimination, harassment and victimisation and any other conduct prohibited by or under the Act with regard to the protected characteristics as set out in section 4 of the Act (age, disability, gender reassignment, marriage and civil partnership, pregnancy and maternity, race, religion or belief, sex and sexual orientation);
- Advance equality of opportunity between persons who share a relevant protected characteristic within section 149(7) of the Act (age, disability, gender reassignment, pregnancy and maternity, race, religion or belief, sex and sexual orientation) and those who do not share it;
- Foster good relations between persons who share a relevant protected characteristic within section 149(7) of the Act (see above) and persons who do not share it.

Due regard in this context involves having due regard in particular to:

- The need to remove or minimise disadvantages suffered by persons sharing a relevant protected characteristic that are connected to that characteristic;
- Take steps to meet the needs of persons sharing a relevant protected characteristic that are different from the needs of persons who do not share it;
- Encourage persons sharing a relevant protected characteristic to participate in public life or in any other activity in which participation by such persons is disproportionally low.

2. **Equalities Impact Assessment:**

2.1. As there are no proposed changes to the existing self-insurance approach a full Equalities Impact Assessment is not required, however potential impacts have been considered in the development of this report and no adverse impact has been identified.