Bandwagon

The BWCI Group Newsletter

BWCI

Quarter 2 - 2016

Inside this issue:

DC Exam Success

BWCI Innovation Award winners

Left to right -
Ian Champion, Stephen Ainsworth (BWCI), Paul Sykes, Rob Fletcher and John Rowson

Aon Insurance Managers (Guernsey) Limited were announced as the winners of the 2015 BWCI Innovation Award at the 30th Annual Guernsey Awards for Achievement gala evening. Aon Guernsey's impressive submission was one of 5 to be short-listed from a record 12 entries.

Aon's entry focused on their innovative approach to the creation of their bespoke reinsurance management platform, which was developed to enable them to support two commercially rated reinsurance companies; Kelvin Re and Humboldt Re.

The judges were particularly impressed by the way that the platform had made a significant contribution to the growth of the company locally, as well as helping to put Guernsey on the reinsurance map.

The judges also recognised that the innovation would be good for Guernsey's economy generally, as Aon is breaking into a market which has traditionally been dominated by Bermuda, demonstrating that there was potential for significant growth in the future.

Chairman of the judging panel, BWCI's senior partner, Stephen Ainsworth, said:

"The breadth of entries for our latest innovation award underlines the range of skills and talent on the island; Aon's entry stood out amongst the short-listed candidates and they are a very worthy winner."

AWARDS FOR ACHIEVEMENT 2015

DC Governance Qualification

Left to right -
Michelle Galpin, Carl Hansen and Carl Stanford

We are delighted to be able to announce that three members of BWCI's Governance Group, Michelle Galpin, Carl Hansen and Carl Stanford, have recently been awarded the Pensions Management Institute's ("PMI") Certificate in DC Governance.

This new qualification was launched in 2015, in response to the increasing focus on ensuring that defined contribution ("DC") schemes are well-run. The UK has recently introduced minimum governance standards for DC schemes, acknowledging that the standard of governance is central to achieving good retirement outcomes for members.

Carl Hansen, who chairs the Governance Group, said:

"The wide-ranging course covered all aspects of DC scheme governance best practice. While it was a UK exam, the topics are equally relevant in a local context".

Carl Stanford, a Partner in BWCI's investment team said:

"The course focussed on the roles of the trustees and the employer in ensuring their schemes are well run. In addition, it provided a good background to emerging areas, such as assessing value for members and improving member engagement".

Michelle Galpin, a Partner in BWCI's actuarial pensions team, added:

"We know that qualifying schemes in Guernsey's Secondary Pension System will need to evidence good governance. Gaining this new qualification means that our team is well-placed to support local schemes in this area".

Brexit Thoughts

"Diversification is your friend in adversity"
Mark Colton

There are certainly many more questions than answers, but voters will still have to decide one way or the other on 23 June 2016 on whether the UK should "remain" or "leave" the EU.

There will undoubtedly be consequences as well for the Crown Dependencies and the British Overseas Territories which need to be thought through, a task made especially difficult because the future is so uncertain. But if you have investments, including pension plan assets, then you need to take a view.

In the complexity of the arrangements between Britain and the EU, overlaid with the Crown Dependencies' and British Overseas Territories' relationships with Britain and/or the EU directly, it is easy to see why a wall of uncertainty is advancing like fog from the sea.

Currently the polls are finely balanced, so it would be unwise to rely too heavily on a particular outcome; efforts must be directed at sizing up the consequences of both options and considering whether any of the risks identified could or should be mitigated.

Remain vote

This ought to be the easier one to consider; if the UK votes to stay in, life is expected to continue much as it did before the referendum appeared on the horizon and we will return to those challenges which had been temporarily left to one side.

Leave vote

But what if the UK votes to leave? This is much more difficult, but we can perhaps look to recent history for guidance.

Might it be a bit like Scotland leaving the UK? "Scoxit", as it was not called, did not happen; the Scottish electorate voted to "remain". But we now have the benefit of hindsight. A year after a vote for independence, the links with the rest of the UK would have begun to fall away. But what looked like reasonable projections from oil revenues in 2014 proved to be spectacularly inaccurate. Scotland would have been suddenly very poor and utterly unable to fulfil its spending promises.

The slump in oil prices was not expected to happen, but it is illustrative of the dangers of leaning too heavily on economic projections.

There's Grexit too, of course, where the Greeks appeared to be all too keen to bale out if the EU troika did not bend to their will. But, in the end, they put up with considerable financial hardship because they considered the alternative of life outside the EU to be even worse.

Having said this, there are countries outside the EU which function perfectly adequately and have no need or desire to join a bloc or union of other countries. So we can imagine a place for the UK in the modern world outside the EU. However, getting there would be something else. Political and economic energies would be sucked into the unravelling process, rather than being used more productively elsewhere; the EU would probably not be disposed to make the UK's exit easy.

Investment implications

How does all this analysis help in arriving at a sensible approach to investment? The risks around the Brexit vote are certainly something that all investors, including pension scheme trustees and members of defined contribution schemes, need to consider.

There are two key points:

- Diversification is your friend in adversity
- Plan according to your time horizon

Not retiring for another 30 years? If you had a good investment strategy before, then it's probably still a good strategy now, subject to the diversity argument; try not to have everything in UK equities, perhaps?

If the time frame is shorter then focus on the more immediate benefits you want to take: a tax free cash sum in Sterling perhaps? In this case you care not for the vagaries of the foreign exchange markets and should search out high quality Sterling Money Market funds.

New Guernsey RATS Rules

New Practice Notes for Guernsey Retirement Annuity Trust Schemes and Retirement Annuity Schemes were published on 18 April 2016.

The update reflects the flexibilities for transferred-in funds which were introduced by the Income Tax (Pension Amendments) (Guernsey) Ordinance 2015. In addition, minor clarification amendments have also been made. The latest Practice Notes can be found under "document downloads" at https://www.gov.gg/article/151880/Income-Tax-on-pensions.

Engaging members

"Feedback from member presentations is always very positive"
Carl Stanford

For many employers, contributions to their pension scheme represents a significant HR spend. Considerable time and effort is also spent ensuring that the scheme is well run. However, despite this, many members do not appreciate the value of their retirement provision or make appropriate choices, leading to poor member outcomes at retirement.

In this article we look at how improving member engagement can maximise the scheme's potential as a key recruitment and retention tool for employers and ensure that members achieve good outcomes at retirement. We also provide some simple steps that employers and trustees can take to achieve this.

Generally in a DC scheme the decisions around how to invest the pot and about how and when to take retirement benefits are made by the members. Often they will also have a choice about the level of contributions to pay in.

All of this can be quite daunting for many employees, but with each decision potentially affecting the ultimate level of benefits, it is vital that trustees and employers consider what they can do to support members to engage with their retirement saving throughout their careers; not only as they approach retirement.

The likelihood of a good member outcome can be increased if the member is encouraged to be proactive at an early stage, taking appropriate actions at the right time and making the best decisions in the light of their own personal circumstances.

The colour-coded headings in this article link to the suggested actions in the table. This table illustrates how a few simple steps could potentially help members to engage more with their DC scheme and achieve a better outcome at retirement.

Lack of active decision making

It would not be unusual for more than 75% of members in a DC scheme to be invested in the trustees' chosen default option. While some members may have actively selected the default strategy, the majority will not have made any positive investment choices. The trustees can support members' decision-making processes by considering how many different fund choices they should offer.

It is important that the fund range is tailored to the financial sophistication of the members. Often it is a case of "less is more". Evidence shows that the more funds offered, the more difficult it becomes for members to make a decision and so they are more likely to opt for the default option.

With such a large proportion of members relying on the default strategy, this places a significant responsibility on trustees to ensure that the default option is appropriate, not only when the scheme is first established, but also as the scheme matures. The default strategy needs to be reviewed regularly as the scheme membership profile could change over time.

While the default strategy may be appropriate for an "average member", each individual member will have different personal circumstances and risk tolerances. This means that the default strategy may not be optimal for everyone.

In response to this some schemes are beginning to offer multiple lifestyle options, which cater for different member risk profiles and can help address this point.

Poor investment strategy choices

Members who make an active decision not to select the default strategy could still end up with a sub-optimal investment strategy for their own circumstances. This could be because they do not understand the investment options fully, including the risks associated with each type of asset. Really clear and engaging member communications can help to address this.

Regular ongoing member communications are also important as it is not just a case of choosing an investment strategy when joining the scheme. Members' circumstances change and what was right for them 5 years ago may no longer be the best approach now.

Evidence shows that once individuals have made their selections, the majority of them do not then regularly review their investment choices. This is particularly true for deferred members. A survey of DC pension scheme members conducted by the UK Pensions Regulator found that only 7% of deferred members had reviewed their fund allocation since they had left their employer.

Not reviewing investment strategy regularly enough can result in a member's fund allocation becoming less appropriate over time, as fund allocations drift from that originally selected due to market movements. In addition the risk profile of the member may change. This could, for example, result in members remaining in high volatility asset classes as they approach retirement.

Lack of retirement planning

Many members do not fully appreciate the size of the pension pot required to deliver the desired level of income in retirement and so do not start contributing until later in their careers or at too low a level. This results in some members having to defer retirement and/or have a lower standard of living in retirement than they expected.

Regular reporting of projected benefits at retirement and access to an online projector tool can assist members with retirement planning. This is particularly effective when combined with regular member presentations, to remind members of the importance of planning for the future. The projector tool provides a practical way to do this.

Under appreciation of pension benefits

Lack of a clear understanding of how the pension scheme operates and the value of the benefits provided can result in members opting out of membership of a contributory scheme or members not appreciating the value of their pension benefits when considering the overall value of their total employee benefits package.

Total reward statements and improved member understanding of their retirement benefits through member presentations can go a long way to improve a member's appreciation of these benefits.

Selecting wrong benefit options

Whether at retirement or on leaving service, members have important decisions to make about how they take their benefits. The timing and content of member communications and signposting members to additional advice at these times are extremely important to ensure good outcomes.

With DC members now able to take all their retirement pot as a lump sum in the UK and the increased popularity of drawdown options generally, this is becoming an area of increasing importance and understandably subject to increasing regulation in the UK.

Summary of solutions

The majority of issues relating to poor member engagement can be addressed through regular member presentations and timely well drafted member communications. In our experience, feedback from member presentations is always very positive. While particularly important for new staff, we have also found that many long-standing employees welcome the opportunity to attend an annual presentation to keep them up to date with pension developments and the investment performance of their funds.

Actions to Promote Member Engagement

	Lack of active decision making	Poor investment strategy choices	Lack of retirement planning	Under appreciation of pension benefits	Selecting wrong benefit options
Review communication material		✓			✓
Ensure engaging, clear, accurate and up to date	■	■			■
Ensure clear risk rating of funds options	■	■			
Signpost members to additional advice		■			■
Timing of member communications during career		■			■
Provide benefit illustrations			✓	✓	✓
Total reward statements				■	
Annual benefit projection statements			■	■	■
Access to online pension projector tool			■	■	■
Analysis to identify members with low projected benefits			■		
Regular Member presentations covering	✓	✓	✓	✓	✓
What the employer pays			■	■	■
Review of benefit options			■	■	■
Review of investment options	■	■			
Retirement planning awareness			■	■	■
Demonstration of online tools			■	■	■
Review investment performance of funds	■	■			
Investment options review	✓	✓			
Expand/simplify fund range	■	■			
Introduce alternative lifestyle strategies	■	■			
Analysis to identify members with inappropriate strategies	■	■			

Guernsey's Evolving Insurance Industry

"Recent trends indicate a move towards a more diverse range of insurance entities"

Ian Morris

Historically Guernsey's insurance industry has been best known for its captive insurers covering general insurance risks for parent groups. In addition, Guernsey is home to a small number of life insurers operating on a cross-border basis. However, recent trends indicate a move towards a more diverse range of insurance entities. We expect this to continue, together with an expansion and deepening of the reinsurance market in Guernsey.

Longevity insurance

The trustees and sponsors of many defined benefit pension schemes are concerned about longevity risk, as this can represent a substantial risk to the adequacy of the assets held to meet the scheme's liabilities. We discussed this in detail in the Quarter 3 2015 edition of Bandwagon, as well as how the BT pension scheme had sought to manage the risk.

BT's solution was an evolution of the captive concept, with the scheme using a similar structure to the captives used by corporates to manage risks. However, the innovative features of their approach were the use of the Incorporated Cell Company ("ICC") structure, as well as the scale and long-dated nature of the deal.

It would not be unusual for deals of this type to take several years to implement. The process requires support from both the pension scheme trustees and the employer; and, as with any innovation, the stakeholders are likely to be unfamiliar with the concepts at outset. However, it would appear that progress is being made and we anticipate that further deals are likely to be executed in due course.

There may also be variations on the standard exchange of longevity risk which featured in the BT deal, but such developments have not yet emerged.

Insurance Linked Securities

Insurance linked securities ("ILS") have been a source of growth, with Guernsey's insurance industry running seminars in both London and Switzerland to promote these developments internationally.

Typically, ILS provide reinsurance of catastrophe risk for specific limited covers. These can be in the form of catastrophe ("cat") bonds, collateralised reinsurance or industry loss warrants.

There has been substantial growth in demand for such vehicles, which are perceived as attractive investments at present. So far, over 100 cells of Protected Cell Companies ("PCC") or ICCs have been formed to support ILS vehicles.

Guernsey is seen as particularly advantageous for ILS due to its proximity to London, proportionate and flexible regulation, experienced providers and banking facilities.

Rated Reinsurers

ILS vehicles are an important source of reinsurance capital but are typically formed for each risk covered. An expansion of a different form of reinsurance capacity in Guernsey has arisen from the establishment of Kelvin Re in 2014 and Humboldt Re in 2015.

Kelvin Re was established as the first rated commercial reinsurer in Guernsey to write short-tail property and speciality lines reinsurance. Slightly unusually, its asset investment strategy includes a significant exposure to hedge funds.

Insurance industry credit rating agency AM Best confirmed that Kelvin Re had written over US$120 million of premium in the first three quarters of 2015. This premium relates to a globally diversified portfolio of natural catastrophe risks. AM Best also confirmed the continuation of the credit rating of A- that had been given on the inception of Kelvin Re.

Humboldt Re was established in 2015 with initial capital of CHF 500 million as a further rated commercial reinsurer in Guernsey. Its stated annual premium target was CHF 140 million with a similar target market to Kelvin Re of property catastrophe risks. It is understood to have adopted a more conventional asset investment strategy.

AM Best confirmed that Humboldt Re had been granted a credit rating of A- that had also been given on the inception of Kelvin Re.

Summary

All of these developments illustrate that Guernsey is continuing to develop as an insurance centre, with a range of reinsurance vehicles supporting the primary market.

Guernsey has had a long standing ambition to grow as an alternative centre for reinsurance. Reinsurance in Guernsey currently remains focused on specific sectors and still has some way to go to develop a comparable reinsurance capacity to, say, Bermuda. However, the recent evolution of the insurance industry shows why there is considerable optimism about the potential for growth in this sector going forward.

Further Information

For further information, please contact Ian Morris at imorris@bwcigroup.com.

Guernsey Secondary Pension Update

"two minor amendments"
Michelle Galpin

Jargon buster

Auto enrolment
The process by which employers are required to automatically enrol their employees into a qualifying pension scheme. Employees can then opt out if they wish.

Staging date
The earliest date by which an employer must comply with its duties under the UK automatic enrolment legislation.

In the previous edition of Bandwagon we outlined the high-level policy proposals, from Guernsey's former Social Security Department, to introduce a legal requirement for all employers to automatically enrol their staff into a secondary pension from 2020.

The proposals were accepted at the February States meeting, subject to two minor amendments that will need to be reflected in the second stage of development. These relate to consideration of whether there should be any special arrangements for start-up companies and whether there should be any distinction between employers of different sizes.

With the introduction of a new States structure from 1 May, the implementation of the proposals falls to a new body, the Committee for Employment and Social Security.

Implementing the amendments

So how might the two amendments be factored into this second stage? The UK phased in its own auto enrolment requirements by assigning every employer a "staging date". The largest employers had staging dates in 2012, while the smallest and those established from April 2012 onwards do not have staging dates until 2017 or 2018.

The phased approach in the UK, by size of employer, appears to be progressing well so far. The phasing in period also provided the pensions industry with a longer period over which to refine their systems and processes.

Regulation of auto-enrolment

Compliance with the UK auto enrolment legislation is monitored by the Pensions Regulator. Every employer is required to declare its compliance with the legislation within 5 months of its staging date.

The Regulator publishes a monthly bulletin on the number of compliant employers. As of the end of March 2016 over 110,000 UK employers had complied with auto-enrolment. Between them they employ almost 22 million workers and over 6 million of these workers have been automatically enrolled into a pension scheme for the first time.

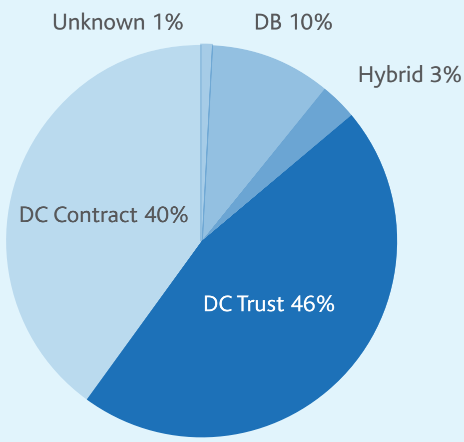
Analysis of UK experience so far

While Guernsey's proposals are at an early stage, as in the UK, it is anticipated that employers will have a choice over the type of pension scheme that they use for auto-enrolment.

The Regulator publishes an annual report analysing how UK employers have chosen to comply with their automatic enrolment obligations. The legislation is very flexible and provided that an existing scheme meets certain minimum criteria, defined contribution (DC), defined benefit (DB) and hybrid schemes may all be used.

The Regulator's latest annual report, which was published in July 2015, shows that 86% of schemes being used for auto enrolment in the UK are DC. 46% of these are trust-based DC arrangements. The remaining 40% of DC schemes were set up on a contract basis with an insurance company.

Types of Schemes used for auto-enrolment in the UK as at 31 March 2015



Source: The Pensions Regulator

2016 BWCI Mini Soccer Festival

2016 marks the tenth anniversary of BWCI's support for the Mini Soccer Festival and we are delighted to report that we have marked the occasion with the signing of an agreement with the Guernsey Football Association to extend BWCI's support as the headline sponsor of the event for a further 3 years.

This year's festival will take place on the weekend of 23 and 24 of July. 23 teams have signed up, including last year's champions Everton. They will also be joined by other UK academy teams including 2009 winners Fulham, as well as two teams from each of Southampton and Bristol City. Also visiting from the UK, for the first time, will be a team from Guildford City.

This year the entrants will be split into two groups of 11 and 12. At the group stage on the first day of the competition each team will play all of the others in its group. The top four teams from each group will then go into the knock-out stage of the competition for the BWCI Trophy. The teams ranked 5th to 8th at the end of the group stage will then compete for the BWCI Plate.

Festival chairman Martyn Banton said: *"It is clear that the reputation of the festival ensures this event continues to not only be the highlight of the Guernsey sporting calendar, but also attracts interest from outside of the island."*

He went on to say that the festival is an important aspect of the football development of Guernsey's young players.

Trauma Teddies

Maria Le Lère(left) with Alison Fossey of Jersey Police

Thanks to a suggestion from Maria Le Lère, an assistant manager in our Pensions Administration Team, the police in Jersey now have "trauma teddies" to comfort children involved in tragic incidents. Maria saw the idea on the internet and contacted the local force to see if they would like some homemade bears.

Volunteers from the group "Hearts and Crafts" have been knitting and crocheting the toys which have now been given to the Police Station.

Only set up in February, already Maria and her fellow volunteers have been asked if they could help provide knitted and crocheted toys and other small items for other local good causes and charities, including the special care baby unit's "Little Miracles", the JSPCA and Jersey Alzheimer's Association.

Chief Inspector Alison Fossey of Jersey Police has welcomed the donation and commented:

"Sometimes a simple thing like a cuddly toy can help children in times of distress and take their mind off difficult circumstances. Our plan is to give out the bears to different sections of the force so they can distribute them to vulnerable children in Jersey."

Diary dates

23/24 July	BWCI Mini Soccer Festival
11 September	BWCI Mind 10K run

Front cover image courtesy of VisitGuernsey

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