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DEATH-IN-SERVICE BENEFITS

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EXPERIENCE | EXPERTISE | EXCELLENCE

A close-up photograph of a white computer keyboard. The focus is on a key labeled "benefits" in a lowercase, sans-serif font. Other keys visible include a key with a question mark and a vertical line, and a key with a tilde (~) and a vertical line. The lighting is soft, creating subtle shadows between the keys.

INTRODUCTION

Life insurance coverage is a common employee benefit offered by companies in India. The payout is typically a proportion of salary and can be as high as 10 times the employee's annual salary.

Companies can offer these benefits in one of the following ways:



Purchase a group term insurance policy whereby an insurance company will pay the death benefit to the deceased employee's estate in exchange for premiums.



Pay the amount directly from the company's funds in the event of the employee's death.

ACCOUNTING TREATMENT

Insurance premiums or death benefits are paid in lieu of services offered by employees during a particular accounting period. An employee does not accrue these benefits over their period of service.

From an accounting perspective, it is therefore not necessary to build a provision over the working lifetime of the employee.

Exposure drafts of IAS 19 have opined that companies should recognize these costs (annual premiums or death benefit payments) as and when they arise during the reporting period.

MARKET TRENDS

1

Purchasing group-term insurance policies is currently the preferred approach for most employers because of competitive premium rates.

Why have premium rates been competitive?

- Lower reinsurance premiums allowed insurance companies to pass on the benefits of these reduced costs to their policyholders.
- Group-term, being highly commoditized as a product, encourages healthy competition between insurance companies.

2

Insurers and reinsurers are now finding it harder to sustain business at these rates and have consequently increased premiums.

Why are premium rates increasing?

- Actual claim payouts for insurers have been higher than what was expected while setting premiums.
- This adverse experience was exacerbated by the higher mortality witnessed during COVID-19.

3

Higher premium rates are making employers consider an alternative approach i.e. providing these benefits directly.

BENEFITS AND CHALLENGES

ADVANTAGES OF PURCHASING GROUP-TERM INSURANCE



Insurance removes any potential volatility and leads to a consistent annual P&L charge. It also helps the employer safeguard itself against a period of large number of deaths in the workforce.



This is even more critical for employers with small headcounts as one-off events (such as the COVID-19 pandemic) can have a significant impact on their books.



Insurance reduces the need for liquidity as large payments will not be required by the company at unexpected times.

ADVANTAGES OF PAYING DEATH BENEFITS DIRECTLY

Insurance premiums include margins for the insurer's profitability, expenses and other components. Employers can avoid these costs by paying death benefits directly.



Employers with large headcounts should be able to predict their future experience reasonably well and their year-on-year experience is likely to be stable. They should be able to absorb the risk of minor fluctuations that might arise due to adverse experiences.



The employer will not have to make any payments during a year with highly favourable experience i.e. no deaths within the workforce. It also saves time and costs pertaining to the administration of the insurance policies.



CONCLUSION

Companies can choose to adopt the most suitable approach, bearing in mind the risks and advantages associated with them. The eventual decision should be determined by the potential cost-savings for the company vis-à-vis the level of risk that the company is willing to take on.

For any questions about death-in-service benefits, please feel free to get in touch.

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Disclaimer: Please note that this material is only for informational purposes and is based on our understanding of the subject. It should not be relied upon or constructed as a legal opinion or advice regarding any specific issue or factual circumstance.