

Increasing Choice in Workplace Accident Compensation

Insurance Council of New Zealand Submission

Feedback Form

This discussion document seeks feedback and comments on proposals to:

- extend the Accredited Employers Programme and offer other risk-sharing options
- introduce choice in the ACC Work Account.

These proposals are described in the discussion document at www.dol.govt.nz/consultation/increasing-choice/increasing-choice.pdf

You can also download this form from the Department of Labour's website at www.dol.govt.nz/consultation.

Please post your completed form to:
 Department of Labour (Attention: ACC discussion)
 PO Box 3075
 Wellington 6140
 or email your completed form to ACCdiscussion@dol.govt.nz

Please make your submission *by 5pm on 15 July, 2011*

Details of respondent:

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I am responding:

- as an individual
 on behalf of an organisation

Organisation/business name (if applicable):

Insurance Council of New Zealand

Please tick which description best suits you or your organisation:

- Employee
 Self-employed
 Employer (please tick number of employees)
 up to 10 10-50 50-250 250-1000 over 1000
 Insurance company

- Business representative organisation/industry group
 Trade Union
 Treatment provider
 Other (please describe)

Treatment providers only:

Please tick the types of treatments that you, or your organisation, provide:

- | | |
|---|---|
| <input type="checkbox"/> Acupuncturist | <input type="checkbox"/> Audiologist |
| <input type="checkbox"/> Chiropractor | <input type="checkbox"/> Counsellor |
| <input type="checkbox"/> Dentist | <input type="checkbox"/> Medical laboratory technologist |
| <input type="checkbox"/> Medical practitioner | <input type="checkbox"/> Nurse |
| <input type="checkbox"/> Occupational therapist | <input type="checkbox"/> Optometrist |
| <input type="checkbox"/> Osteopath | <input type="checkbox"/> Physiotherapist |
| <input type="checkbox"/> Podiatrist | <input type="checkbox"/> Radiologist/X-ray provider |
| <input type="checkbox"/> Speech therapist | <input type="checkbox"/> other type of treatment provider |

Is your organisation:

- a general practice organisation?
 a District Health Board?
 another type of treatment provider (please describe)
-

Official Information Act requirements

Please note that submission contents and your individual or organisational details may be released publicly if a request is made for this information under the Official Information Act 1982.

Please let us know if you do not want your submission contents and/or your individual or organisational details to be made available to requesters and we will take this into account when responding to requests.

Increasing Choice in Workplace Accident Compensation

Insurance Council of New Zealand Submission

Executive Summary

Introduction

- 0.1 This submission outlines the response of the Insurance Council of New Zealand ("the Council") to the Government's discussion document "Increasing Choice in Workplace Accident Compensation" released 1 June 2011.
- 0.2 In Parts A, B and C of this submission, the Council responds to the Government's current proposal as set out in the discussion document noted above. Then, in part D of this submission, the Council addresses the specific questions raised by the Government in its discussion document.
- 0.3 As a foreword, the Council believes a significant objective for any adopted proposal should be the establishment of a sustainable accident insurance scheme for the future benefit of all New Zealanders.

Part A - Benefits of Choice

- 0.4 The Council welcomes the introduction of choice in the ACC market and the benefits this will bring. We fully encourage the Government to proceed with its proposal to allow choice in the Work Account and to also investigate opening the Earner and Motor Accounts to choice in the future.
- 0.5 While the Council welcomes the Government's decision to introduce choice into the ACC Work Account, the Council is concerned the Government's current proposal may not achieve its objectives of reducing workplace accidents, improving rehabilitation rates and reducing Work Account operating costs.

Part B - Issues with the Current Proposal

- 0.6 The Government's current proposal, which is based around employers being able to opt-out from cover with ACC, would not fully achieve the benefits that could be obtained if the market was fully opened to choice. The following significant issues identified by the Council mean that the Government risks little or no insurer participation in the Work Account.
- 0.7 *Uneven Playing Field:* The current proposal does not provide a level playing field between ACC and private insurers. It does not provide insurers with a reasonable prospect of achieving the market share necessary to justify the significant establishment costs inherent in entering the market. Nor does it provide insurers with the ability to establish any real benefits in the market.
- 0.8 *Uncertainty of Tenure:* The current approach does not provide insurers with confidence that there is commitment to a long term sustainable market. A market dominated by ACC as a default insurer does not optimise the benefits that could be achieved from a competitive market.

- 0.9 *Opt-Out Model:* An opt-out model does not encourage employers to actively take responsibility for who manages their workplace injury claims. Instead, it continues to promote the general culture of apathy in New Zealand towards workplace accident cover. Furthermore, provision of an automatic default to ACC, without the requirement for ACC to operate as an SOE, entrenches the ACC's position as the dominant market provider and does not encourage employers to actively consider the alternatives.
- 0.10 *Prudential Regulations – Capital Requirements:* The Government's proposal indicates that ACC would not be subject to the same prudential requirements as private insurers. In particular, it appears ACC would have the ability to price premium without being required to meet the normal commercial requirements associated with the use of capital. This would seriously impede the viability of the market for private insurers and therefore threaten the long-term sustainability of the accident insurance scheme.

Part C - Recommended Adjustments

- 0.11 The Council recommends the following adjustments to the Government's proposal. We believe these adjustments will support the Government's intention of reducing workplace accidents, improving rehabilitation rates, reducing Work Account operating costs and therefore allowing for long-term sustainability of the scheme.
- 0.12 *SOE Status and Prudential Regulation:* All insurers should be required to comply with the same prudential requirements to ensure market pricing is both competitive and sustainable. The best way to achieve this would be for ACC to compete in the Work Account as a State Owned Enterprise (SOE). This would guarantee ACC were not able to undermine competitive pricing in the market and would therefore increase the likelihood of insurer participation.
- 0.13 *Opt-In v Opt-Out:* To ensure employers actively take responsibility for safety in the workplace there should be a requirement for employers to actively select which insurer provides cover for their workplace accidents. Should the Government adopt a model with ACC competing as an SOE, then insurers should be required to opt-in to cover with a private insurer or the SOE, as opposed to opt-out of cover with ACC. The promotion of responsibility towards workplace accidents would lead to reductions in workplace injuries and rehabilitation periods and help bring about a change to the current culture of apathy in New Zealand towards workplace accident cover.

If an employer failed to opt-in to accident insurance cover with a particular insurer or the SOE within a specified time frame then the employer could be allocated to a default insurer, at a penalty rate elected by the insurer.

- 0.14 *New Zealand Registered Insurers:* To ensure the Government retains its ability to protect New Zealander's ACC entitlements, the Council recommends that all insurers should be required to be registered and incorporated in New Zealand. This would ensure that the limited jurisdiction and supervisory control of a New Zealand regulator would not be undermined and it would also help ease any perceived public concerns around solvency and the protection of employee rights and entitlements.
- 0.15 *Regulation of Broker Commissions:* We recommend that compliance and administration costs of the ACC system are minimised wherever possible. One factor that will significantly impact on the overall cost of the scheme is an unregulated broker commission's framework for what is a statutory class product with legislated benefits. The Council recommends that brokerage commissions are closely

regulated so that employer's premium levels are kept at a reasonable rate. This would still allow brokers to negotiate an additional fee from the employer on a value added basis for advice or services provided in respect of the accident business.

- 0.16 *Claims Data*: Insurers need all relevant claims data immediately so that they can begin actuarial work on likely rates, thus enabling an informed assessment about whether to enter the market. The minimum data set insurers require is outlined in a paper prepared by Melville Jessup Weaver ("MJW"), a copy of which has been provided to the Department of Labour. There should be clear instructions and controls put in place to facilitate the distribution of claims data.
- 0.17 *Limited Catastrophe and Terrorism Cover*: For some time insurers have been unable to source "unlimited, per event" reinsurance protection on workers compensation portfolios. The Government should place a legislative cap on insurer liability for multiple claims arising from a single catastrophic event and provide cover for claims arising from terrorist acts through a funding pool established by the Government.

Part D - Questions Raised in the Discussion Document

- 0.18 Further to our recommendations to the Government in Part C, we also wish to respond to the particular questions raised in the Government's discussion document. These are set out in the main body of our submission.

Conclusion

- 0.19 The Council welcomes the Government's decision to introduce choice into the ACC Work Account and we encourage the Government to proceed with its proposal to allow choice. Together with the Government's stated objectives, a significant objective should be the establishment of a sustainable accident insurance scheme for the future benefit of all New Zealanders.
- 0.20 Whilst the Council welcomes the introduction of choice into the Work Account, the Council believes the current proposal does not go far enough towards creating a sustainable market which will realise the full benefits of choice.
- 0.21 In order to fully benefit from the introduction of choice, the Council recommends the Government adopt the proposals outlined in Part C of this submission, together with our recommendations regarding the discussion document questions outlined in Part D. The Council, through its Accident Insurance Committee, is committed to working constructively with the Government in order to develop the current proposal it has put forward.

Increasing Choice in Workplace Accident Compensation

Insurance Council of New Zealand Submission

1 Introduction

- 1.1 This submission outlines the response of the Council to the Government's discussion document "Increasing Choice in Workplace Accident Compensation" released 1 June 2011.
- 1.2 In Parts A, B and C of this submission, the Council responds to the Government's current proposal as set out in the discussion document. Then, in part D of this submission, the Council addresses the specific questions raised by the Government in its discussion document.
- 1.3 The Council believes the primary objective for any adopted proposal should be the establishment of a sustainable accident insurance scheme for the future benefit of all New Zealanders. The current ACC system has not served to provide such a sustainable scheme and as a result the scheme has had to undergo a major review at least once every decade since its inception. The Council therefore welcomes the Government's proposal to address these concerns by introducing choice into the Work Account. We also welcome the prospect that the Earners and Motor Accounts may also be opened to choice.

2 Background

The Insurance Council of New Zealand

- 2.1 The Council is the industry representation body for fire and general insurance in New Zealand. The Council has 25 members which write the substantial majority of New Zealanders' insurance business.
- 2.2 The Council is active in self-regulating the insurance industry. We promote the Fair Insurance Code that requires insurers to act ethically. We fund the Insurance & Savings Ombudsman Scheme that offers independent review of decisions and we apply a Council solvency test that confirms the financial stability of our members. We also require members to be independently rated and to publish these ratings. We perform an important role in informing and educating consumers about key insurance issues and risks.
- 2.3 Members currently protect approximately \$0.5 trillion of New Zealanders' assets and last year paid \$2.1 billion in claims, not including the estimated \$10 billion currently being contributed towards the recovery of Canterbury following recent earthquakes.

Government Decisions

- 2.4 On 1 June 2011, the Minister for ACC, Nick Smith, released a Government discussion document on reforms to ACC. The discussion document sets out proposals on introducing choice into the Work Account and extending the Accredited Employers Programme.
- 2.5 The significant proposal for Council members relates to the introduction of choice in the Work Account. The introduction of choice is intended to provide greater

incentives for safer work places, better rehabilitation rates and improved cost effectiveness in the Work Account. The Government wants employers to be able to choose to either continue to purchase work-related personal injury insurance for their workers from ACC or to alternatively purchase cover from a private insurance company.

2.6 The proposals as they currently stand are that:

- ACC continues to operate as a Crown agent, but with increased market transparency;
- ACC be the default insurer;
- ACC's Work Account products and prices be deregulated to allow it to compete;
- employers be legally required to ensure their workers have continuous cover and a register of employers and their provider be kept;
- insurers be required to provide at least the minimum level of cover currently set out in the Accident Compensation Act 2001;
- participating insurers be subject to specific prudential regulations;
- if an insurer becomes insolvent, ACC takes over claims management and costs be met by a levy on all other participating insurers;
- a market regulator be responsible for monitoring and enforcing employer and insurer compliance with legal requirements;
- dispute resolution be independent and aligned with other existing frameworks;
- a single claims lodgement unit be set up;
- methods be established for private insurers to contribute towards public health acute services; and
- minimum prices and conditions for treatment services be required unless an insurer agrees with a treatment provider on alternative arrangements.

2.7 The Government intends to make final decisions on the proposals for choice in the Work Account before the November election this year.

PART A

3 Council Welcomes Choice

Benefits of Choice

3.1 The Council welcomes the introduction of choice in the ACC market and the benefits this will bring. We encourage the Government to proceed with its proposal to allow choice in the provision of the Work Account. We also support the introduction of choice in the Earners and Motor accounts and are committed to working constructively with the Government in this respect.

3.2 By the Minister's own admission the current ACC system is in poor health and requires fixing. In the "Ministers Foreword" of the discussion document, the Minister states:

"The scheme has repeatedly got into financial difficulty triggering reviews in the 70s, 80s, 90s, and the most recent in 2010. The scheme needs modernising to work well into the future."

- 3.3 It is only through the introduction of choice in ACC that these issues will be addressed and the full benefits of competition will be realised. These benefits, as identified in the “Ministers Foreword” of the discussion document will include the:
- reduction of workplace injuries and deaths;
 - promotion of better workplace safety;
 - reversal of deteriorating rehabilitation rates;
 - provision of stronger incentives for employers to manage ACC costs; and
 - reduction of large ACC deficits and financial difficulties.
- 3.4 The Council’s previous report to the Department of Labour dated 2 February 2011 set out the following benefits from the introduction of choice, if premium payers were free to choose between insurers who in turn were free to compete for business on both price and service:
- actuarially fair and sustainable premiums that will be lower over the long term because the market will recognise and reward employers that provide safer work places;
 - more attention to injury prevention – because insurers will tailor premiums to reflect risk and claims history and through risk management programmes will support premium payers to reduce risks that might lead to injury and costs to themselves and insurers;
 - more focus on effective claims management and rehabilitation – because in a competitive market long tail insurers make money by effectively managing claims. Early medical treatment and procedures coupled with timely and effective rehabilitation help ensure claimants return to work as quickly as possible;
 - more innovation – because it is in the financial interests of competing insurers to constantly introduce more effective approaches to administration, injury prevention, case management and rehabilitation to get better outcomes. In addition, insurers may provide add on benefits to meet their customer’s needs;
 - administrative efficiency – because poor administration increases costs to insurers; and
 - less risk to the Crown – because risks associated with underwriting accident insurance claims are transferred from the Crown’s balance sheet to the private sector going forward.
- 3.5 The objectives of both the Government and private insurers are similarly aligned. In order for insurers to thrive in the accident insurance market they need to meet the Government’s objectives of reducing workplace accidents, improving rehabilitation rates and reducing Work Account operating costs. Therefore, the more insurers there are in the market and the greater their market share, the more likely it is the Government will meet its objectives.
- 3.6 As the Council has previously indicated to the Government, the above dynamic cannot be replicated or achieved in a monopoly market. In order to fully benefit from the introduction of choice, a sustainable competitive market needs to be established so that ACC does not monopolise the market. This is also in accordance with recommendations from the ACC Stocktake Steering Group and the Treasury.

Stocktake Report

- 3.7 The ACC Stocktake Steering Group and the Treasury recommended the establishment of a competitive environment without ACC participation. However, the Government’s proposal effectively runs counter to this advice.

- 3.8 The Government feels it is presently not in a position to follow the advice of the ACC Stocktake Steering Group and the Treasury. The Government has instead recommended the implementation of an “evolutionary” model of change which would see the gradual introduction of a competitive market. As such, the Government’s proposal only goes part way towards creating the necessary conditions for achieving the full benefits of choice and runs the risk of not achieving real choice at all.
- 3.9 While the Council welcomes the Government’s decision to introduce choice into the ACC Work Account, we urge the Government to reconsider whether its objectives of reducing workplace accidents, improving rehabilitation rates and reducing Work Account operating costs will be achieved through its current proposal.

PART B

4 Issues with the Current Proposal

Current Industry Concerns

- 4.1 In the Council’s opinion, the discussion document does not go far enough towards promoting choice. The Government’s current proposal, which is based around employers being able to opt-out from cover with ACC, would not fully achieve the benefits that could be obtained if the market was fully opened to choice. The following significant issues identified by the Council mean that the Government risks little or no insurer participation in the Work Account.

Uneven Playing Field

- 4.2 The current proposal does not provide a level playing field between ACC and private insurers. It does not provide insurers with a reasonable prospect of achieving the market share necessary to justify the significant establishment costs and capital injection required to enter the market. Nor does it provide insurers with the ability to establish any real benefits in the market.
- 4.3 The available market share is severely limited by ACC’s proposed role as the default insurer. Moreover, insurers’ ability to gain market share is constrained by ACC’s dominant market position, its ability to price premium without the need to meet normal commercial and prudential requirements associated with the use of capital and the requirement that employers opt-out of ACC cover rather than make a proactive decision on their preferred insurer when choice is introduced.
- 4.4 While a small stake in the market would require less prudential capital to underwrite the business, the establishment costs for each insurer are similar whether they obtain 1% market share or 20% market share.
- 4.5 The prospect of a very small market share means an insurer:
- has a higher risk of not being able to establish a viable business that enables them to recoup their establishment costs and achieve a fair return on their investment;
 - is unlikely to be able to leverage any economies of scale inherent in a larger market share; and

- as a consequence of the higher risks and diminished benefits inherent in the market, is unlikely to commit the initial capital and resources required to scope and establish the business.

Uncertainty of Tenure

- 4.6 The current approach does not provide insurers with confidence that the Government is committed to a long term sustainable market.
- 4.7 A market dominated by ACC as a default insurer does not optimise the benefits that could be achieved from a competitive market (i.e. the benefits set out at clause 3.3). A failure to optimise the benefits of competition would inevitably heighten the risk that a future Government may reverse the reforms, thus making the decision to enter the market an even riskier one.
- 4.8 Leaving ACC as a competitor and default provider to the market tilts the playing field hugely in ACC's favour and thus makes reversing reforms relatively easy for any future Government. This provides little or no medium to long-term certainty for insurers who are concerned that the current approach appears to have been adopted in part because it would reduce the cost of future policy reversal.¹ This gives no comfort to insurers about the longevity of the Government's proposals.

Opt-Out Model

- 4.9 There is currently a general culture of apathy in New Zealand towards workplace accident cover. To address this culture and ensure employers actively take responsibility for safety in the workplace, employers should be required to actively consider who is best suited to provide their workplace accident cover. The opt-out model, without the requirement for ACC to operate as an SOE, does not encourage employers to take responsibility for who manages their workplace injury claims. If employers are required to take responsibility in this area there will inevitably be decreases in injury rates and rehabilitation periods.
- 4.10 Furthermore, the opt-out model, without the requirement for ACC to operate as an SOE, benefits the incumbent insurance provider ACC by not requiring employers to actively consider alternative providers. Provision of an automatic default to ACC entrenches the ACC's position as the dominant market provider and does not encourage employers to actively consider the alternatives.

Prudential Regulations – Capital Requirements

- 4.11 The Government's proposal indicates that ACC would not be subject to the same prudential requirements as private insurers. This would unfairly disadvantage private insurers, as these insurers are subject to the following prudential requirements under the Insurance (Prudential Supervision) Act 2010:
- to comply with prescribed fit and proper standards;
 - to adopt an adequate risk management programme;
 - to maintain minimum capital amounts;
 - to comply with prescribed solvency standards;
 - to have a current financial strength rating; and
 - to complete all necessary reporting requirements.

¹ Office of the Minister for ACC, *Next Steps on ACC* (Cabinet Paper), p 10.

Each of these prudential requirements imposes significant financial and other costs on insurers that ACC would not be required to bear. This puts ACC at a significant competitive advantage and effectively means that insurers would never be able to compete on price.

- 4.12 In particular, ACC would have the ability to price premium without being required to meet the normal commercial requirements associated with the use of capital. As stated in the discussion document, “...ACC would continue to be exempt from paying business income tax and from general insurance prudential requirements, and would not be required to make a return on capital.” ACC would be effectively unrestrained in its price setting without any meaningful consequence should they get it wrong.
- 4.13 The Government has raised a concern in its discussion document that insurers may potentially “cherry-pick” low-risk customers. However, in reality ACC would be the insurer most able to “cherry-pick” low-risk customers through their ability to undercut the minimum premiums able to be set by private insurers. Insurers find it difficult to escape the conclusion that ACC would protect its best accounts through pricing which is unrestrained by the need for a return on capital. Under the current proposal insurers would likely be left with the riskier, less profitable end of the market.
- 4.14 This could seriously impede the viability of the market for private insurers and therefore threaten the long term sustainability of the scheme for all New Zealanders.

AEP Extension

- 4.15 The Council does not believe there would be any benefit in extending the AEP programme in April 2012, if the Government intends to introduce a wide range of choice only six months later. The Council believes the proposed extension of the AEP programme in April 2012 would significantly increase the administrative burden and compliance costs for providers without providing any benefit for employers, injured workers or the overall scheme; especially given that the Government intends to introduce market choice, and flexibility for the ACC Work Account to provide whatever products it likes, only six months later.
- 4.16 The current claims lodgement and invoicing process with the existing 136 AEP participants already results in additional provider costs because of claims lodgement and invoicing issues. This leads to delays in payment for the provider. An increase in the number of AEP participants would only exacerbate this issue. The creation of the additional burden and cost for providers to identify, lodge claims and invoice an increased number of AEP participants is unwarranted when there is no additional benefit for the overall scheme, employers or injured workers. The proposed benefits from the extension of the AEP would already be achieved through a market opened up to choice.
- 4.17 Expanding the AEP scheme also raises issues, as discussed in Section 6.5 (question 21), around the allocation of operating costs for the proposed clearing house and how or if AEP employers and TPAs would be subject to any insurer protocols that may be agreed. Further, the proposed expansion limits the potential market share available to insurers, thus diminishing the attractiveness of the market, the likelihood of insurer entry and therefore the possible benefits for employers and injured workers.

Summary

- 4.18 The issues addressed in this Part B mean that private insurers are less likely to enter the market on a prolonged and meaningful basis. Accordingly, the Council recommends implementing the following adjustments to the Government's current proposal, so as to ensure meaningful and sustained insurer participation.

PART C

5 Recommended Adjustments

- 5.1 The environment that will optimise the benefits of choice is one in which a state-owned insurer does not monopolise the market. The Council proposes the following adjustments to the Government's proposal so as to ensure meaningful insurer participation. We believe these adjustments would support the Government's intention of reducing workplace accidents, improving rehabilitation rates, reducing Work Account operating costs and therefore allowing for long-term sustainability of New Zealand's accident compensation scheme.

SOE Status and Prudential Regulation

- 5.2 All insurers should be required to comply with the same prudential requirements to ensure market pricing is both competitive and sustainable. The most effective way to achieve this would be for ACC to compete in the Work Account as a State Owned Enterprise (SOE) with the same prudential requirements as private insurers (i.e. the requirements set out at clause 4.11 and in particular the same requirement to comply with prescribed solvency standards).
- 5.3 ACC should be provided with a set amount of capital which would represent the Government's appetite for real insurance risk. This would ensure that any under pricing would result in a loss of capital and thus a reduced ability to write future risks at an unsustainable level, unless New Zealand taxpayers injected more capital to support the poorly managed entity. This would help ensure ACC were not able to undermine sustainable pricing in the market and would increase insurer's likelihood of market entry. At the very least, a market regulator should be able to look at ACC's pricing to ensure they are pricing responsibly.
- 5.4 The Council believe the introduction of an SOE is still a viable and workable option for the Government and would not add significant cost or complexity to its proposal. This would go further towards achieving the full benefits of choice and it would not unduly burden the Government with future financial risk, as it currently bears. It would enable insurers to enter the market on a basis that at least begins to represent a level playing field and thus would go some way towards creating a sustainable market of choice.

Opt-In v Opt-Out

- 5.5 Should the Government adopt a model with ACC competing as an SOE, there appears to be no convincing reason why employers should be required to opt-out of ACC rather than opt-in to an elected insurer or SOE. The opt-out mechanism encourages employers to stay with ACC because of employer apathy and gives ACC an unreasonable and unfair advantage in the market. Further, the opt-out mechanism does not incentivise employers to take responsibility for safety in the

workplace. Instead it continues to promote the current general culture of apathy in New Zealand towards workplace accident cover.

- 5.6 To ensure employers actively take responsibility for safety in the workplace then there should be a requirement for employers to actively select which insurer provides cover for their workplace accidents (i.e. either a private insurer or the SOE). The promotion of responsibility towards accidents would in turn lead to reductions in workplace injury rates and rehabilitation periods. This proactive opt-in approach, rather than a default opt-out approach which places no responsibility on the employer, would help bring about a change to the current general workplace culture of apathy towards accident cover. If the Government did not adopt a model with ACC competing as an SOE, then the Council believes the opt-out model under the current proposal should be retained.
- 5.7 *Default Insurer where there is an SOE:* If an employer failed to opt-in to insurance cover with a particular insurer or the SOE within a specified time frame (i.e. a 'hard date'), then the employer should be randomly allocated to the SOE or an insurer (possibly based on market share at the time, of employers who have made the positive decision to enter the market) at a penalty rate elected by the insurer.
- 5.8 Another option may be to follow a similar arrangement to that which was adopted under the KiwiSaver scheme. A selection of insurers could be elected as the default insurers by competitive tender. Those who have failed to select an insurer by a set date would be automatically allocated to the SOE or an insurer that was selected through the open, competitive tender process.
- 5.9 Under either of these arrangements all employees would remain protected. Employers who were defaulted to an insurer or the SOE should not be permitted to change insurers within a minimum cover period (i.e. 6 months). Default insurer's premiums should have to be fully paid before a change was possible and a default insurer should not go off risk until they have proof the employer has arranged alternative cover with a registered insurer.
- 5.10 This default provision would provide further incentive for employers to take active responsibility for who manages their workplace injury claims.

New Zealand Registered Insurers

- 5.11 To ensure that the Government retains its ability to protect New Zealander's ACC entitlements, the Council recommends that insurers must be registered and incorporated in New Zealand. This would ensure that the limited jurisdiction and supervisory control of a New Zealand regulator would not be undermined and would also help ease concerns around insurer solvency and the protection of employee rights and entitlements.
- 5.12 As it stands, the Government and other New Zealand based insurers risk assuming responsibility for outstanding claims and policies left by offshore based insurers that either voluntarily or involuntarily (i.e. through insolvency) leave the market.
- 5.13 Furthermore, allowing offshore insurers to write business in New Zealand would undermine the Government's ability to protect New Zealander's ACC entitlements as the New Zealand regulator would have limited jurisdiction and supervisory control.
- 5.14 Only insurers registered and incorporated in New Zealand should be permitted to take on risk under the ACC legislation, including any excess of loss or stop loss

arrangements under the Accredited Employer Programme (AEP) or any risk sharing arrangements.

Regulation of Broker Commissions

- 5.15 We recommend that compliance and administration costs of the ACC system are minimised wherever possible. One factor that will significantly impact on the overall cost of the scheme is an unregulated broker commission's framework for what is a statutory class product with legislated benefits.
- 5.16 In return for remuneration, brokers can provide a valuable service to employers. Brokers can make it easier for employers to make an informed decision about the best insurer for their particular circumstances. They can therefore, act as a significant and positive facilitator in a competitive market.
- 5.17 However, because broking commissions represent an additional cost over and above those that ACC currently incur it would be prudent for officials to assess whether the existing regulatory provisions are appropriate to ensure the Government's objectives are reached. The Council recommends that brokerage commissions are closely regulated, so that employer's premium levels are kept at a reasonable rate. This would still allow brokers to negotiate an additional fee from the employer on a value added basis, for advice or services provided in respect of the accident business.
- 5.18 Given the unique characteristics of the accident insurance line of business and its compulsory nature, officials should assess the benefits associated with regulating the maximum commission available for brokers. In Australia the levels are pegged at 3-4% and something similar to this would be appropriate in New Zealand.
- 5.19 Commissions should be defined to include any profit shares, incentives, volume discounts, fees or any other form of remuneration which is retained or received by the broker from the accident insurer's premium fund. It should also be regulated that brokers cannot demand any form of remuneration from other insurance products based upon their placement of accident business.

Claims Data

- 5.20 Insurers need all relevant claims data immediately so that they can begin actuarial work on likely rates, thus enabling an informed assessment about whether to enter the market.
- 5.21 The minimum data set insurers require is outlined in the paper prepared by Melville Jessup Weaver ("MJW"), a copy of which has been provided to the Department of Labour. The Department of Labour should seek Cabinet approval for the data to be released to the Council immediately on behalf of its members. This is necessary to facilitate insurer entry to the market. We assume that private insurers and the separate ACC Work Account Division will be provided with the exact same data so as to ensure a competitively fair and neutral playing field.
- 5.22 Any data provided to the Council will not need to identify specific individuals. Accordingly, any data provided could not be used for an insurer's own benefit should the Government decide not to proceed with the introduction of choice. Also because the information would not be personalised it should not create any privacy issues. Any insurer member of the Council wishing to have this data should sign a full confidentiality agreement stating it will only be used for the purposes for which it is

provided. This being to analyse the risks and premium rates required to insure this line of business.

- 5.23 Last time the Work Account was opened to choice, the receipt of data was frustrated by the requirement to obtain information directly from ACC, who were reportedly quite obstructive in their behaviour. There should be clear instructions and controls put in place to facilitate the Council's right to receive a timely distribution of all required data and any other information ACC are sharing with the Independent ACC Work Account division or SOE. This will require more than a direction from the Government as this was insufficient last time. There may be some merit in forming a working group so that insurers can have direct access to the data. Any disruption to the receipt of data may further compromise the likelihood of insurer entry into the market.
- 5.24 We are aware that ACC holds other data than that set out in the MJW paper that may also be useful to insurers. At a later date we would wish to agree arrangements for obtaining this additional information from ACC in addition to receiving periodic updates of the minimum data set leading up to the establishment of the competitive market.

Limited Catastrophe and Terrorism Cover

- 5.25 For some time insurers have been unable to source "unlimited, per event" reinsurance protection on workers compensation portfolios due to the potential accumulation exposures in earthquake exposed countries, a position which will be reinforced by recent events in Christchurch. While claimants should continue to have access to an 'unlimited' policy, the Government should place a legislative cap on insurer liability for multiple claims arising from a single catastrophic event. Further analysis is required to establish the final quantum of any cap. Once determined it would define the upper boundary of claims exposure for insurers and reinsurers.
- 5.26 This approach reflects the current situation where the Government is already exposed to any liability incurred by ACC as a result of a catastrophic event. It would still transfer almost all foreseeable accident insurance liabilities from the Crown to the private sector. The Crown would however, retain ultimate liability for claims costs that exceed the cap in the unlikely event of an extreme catastrophe, which could be funded from an ex-post levy. This approach would reduce insurers' capital requirements, enable lower premium rates to be established and is likely to encourage a broader range of insurers to enter the market thus fostering greater competition.
- 5.27 Cover for claims arising from terrorist acts should also be funded from a central pool established by the Government again, because reinsurance is unlikely to be available. For example, the Australian experience post-9/11 was that terrorism exclusions introduced by reinsurers resulted in workers' compensation insurers being unwilling to carry this exposure. Accordingly, legislative action was taken by state Governments with privately underwritten schemes to deal with the exposure and effectively remove the liability from insurers' balance sheets. To the best of our knowledge there has been no return to workers' compensation terrorism reinsurance cover in Australian state schemes but we are also unaware of any claims of this type either.
- 5.28 The benefits of this approach reflect the case made for a limit on insurer liabilities for multiple claims arising from other catastrophe events or terrorist acts. A government-funded pool is likely to provide market conditions that maximise insurer participation and the benefits this will bring. Premium rates would be more competitive as insurers

would not need to make provision for very low likelihood/high impact terrorist acts and catastrophe events.

PART D

6 Questions Raised in the Discussion Document

6.1 Further to our recommendations to the Government in Part C, we also wish to respond to the particular questions raised in the Government's discussion document. We have answered the questions in the discussion document in the same numbered order.

6.2 The key details the Government are seeking consultation on are whether to:

- extend the Accredited Employer Programme (AEP) from April 2012;
- allow choice of workplace insurance cover from October 2012;
- require at least existing minimum worker cover and entitlements;
- require participating insurers to meet minimum prudential requirements;
- require participating insurers to pay a levy, in the event of an insurer failing;
- implement a market regulator to monitor and enforce employer/insurance compliance;
- create a single claim lodgement unit;
- implement minimum prices and conditions for treatment service providers like GPs;
- implement easily accessible and independent dispute resolution service; and
- require contributions from all insurers for acute hospital/ambulance care.

Extending the Accredited Employers Programme

6.3 As suggested at clause 4.15, the Council does not believe there would be any merit in extending the AEP programme in April 2012, if the Government intends to introduce a wide range of choice only six months later. Nevertheless, we have answered the following questions raised by the Government.

1. Do you agree that there should be a greater range of claims management periods? Why or why not?

Yes with a condition

This should be acceptable, as long as the employer has a suitable level of financial backing and protection in place for the injured worker to ensure they are fully and appropriately rehabilitated.

2. Do you agree that the claims management period should be measured from the date of injury, rather than from the end of the current levy year?

Yes

This would be a true reflection of the claims history and so would provide better accuracy of data for financial reporting.

3. Do you agree that there should be more flexibility in the purchase of high cost claims cover and stop loss cover? If not, why not?

Yes

4. Do you agree that employers should be able to purchase high cost claims cover and stop loss cover from an approved third party? If not, why not?

Yes with a condition

As long as they are New Zealand registered and they meet all requirements of the Prudential Supervision Act 2010.

5. Do you agree that an employer's claims history should be taken into account when setting PDP levies? Why or why not?

Yes

This is a truer reflection of the individual business and would ensure that "good" employers are not subsidising "bad" employers. It would encourage employers to actively manage risk.

6. Do you agree that ACC should be required to take over management of any claim at the employer's request and cost? Why or why not?

Possibly

There would need to be tight guidelines about how and when this would occur to ensure that employers fully understand their responsibilities from the outset and that they don't use this as a means to pass on claims they simply don't want to deal with.

7. Do you agree that in the Full Self Cover option, there should be a choice of a full and final settlement? Why or why not?

Possibly

Only if a true assessment of future costs can be assessed to ensure the Crown does not end up absorbing these costs and that the settlement will be used for the injured persons benefit and long-term rehabilitation and care. The methodology needs to be agreed up front for all employers and it must be transparent.

8. Do you think that co-operatives, franchises or other groups should be able to enter the AEP? Why or why not?

Possibly

As long as stability of the group is ascertained. Consideration would need to be given to what should happen if a group or part of a group disbanded at any point during the partnership and how claims (new and existing) should be managed, reported and apportioned.

9. Do you agree with the proposal to allow employers to use financial instruments or other forms of security as a means of meeting the AEP financial requirements? Why or why not?

No

This could result in claimants not receiving entitlements and rehabilitation. Employers must be able to prove they are able to cover all costs for all claims for the period they are in the AEP without incurring additional debt to do so. This is particularly important given the long tail nature of these claims and it is an area of the current AEP which is not properly recognised or controlled.

10. Do you agree with the proposals to streamline injury management practice audits? If not, why not?

Possibly

There needs to be minimum standards across all businesses. If streamlined audits were imposed they should support a reduction in risk and be set to achieve positive outcomes rather than be compliance or process driven, as is currently the case. Any requirement should also be imposed on ACC for all its accounts and/or any SOE.

11. Should health and safety audits be voluntary? If not, why not?

No

Health and safety audits, provided they are not overly burdensome, may help maintain standards and assist in the improvement of work place environments. Audits would need to serve a useful purpose and be backed by appropriate and effective compliance regimes.

12. Do you agree with offering a range of claims excess options outside the AEP? Why or why not?

Yes

This would help encourage workplace safety and a reduction in work accidents. Nevertheless, this question is irrelevant in a competitive environment where an SOE has the flexibility to provide whatever products it likes.

6.4 Greater Choice for Self-Employed People

13. Do you agree that self-employed people should be able to choose to purchase cover for both work-related and for non-work injuries from a private insurer? Why or why not?

Yes

The Council welcomes this proposal for the self-employed.

6.5 Choice in the Work Account

14. Do you agree that transparency and flexibility are necessary to facilitate a competitive environment? Are these proposals adequate? Why or why not?

Yes and No

The Council agrees that transparency and flexibility are necessary to facilitate a competitive environment.

In terms of transparency, the main areas addressed in the discussion document relate to allocating costs between ACC accounts to ensure there is no cross-subsidisation, together with related auditing, knowledge sharing and reporting requirements. However, the effectiveness of this proposal will be entirely dependent on the quality of the auditors undertaking the independent audit. Furthermore, so long as ACC remains in its current form there will continue to be some concern as to the true transparency and fairness of the cost allocation processes within ACC.

As regards flexibility, the proposal states that “...ACC would continue to be exempt from paying business income tax and from general insurance prudential requirements, and would not be required to make a return on capital.” As set out in Part B above, this approach will not help facilitate a competitive environment between ACC and private insurers. There needs to be flexibility for all competitors, however, they should all be subject to the same level of risk and prudential compliance.

In order to facilitate a competitive environment, ACC should be required to compete independently in the Work Account as an SOE. An SOE would ensure independent governance and remove the risk of cross subsidisation across the ACC accounts. An SOE would be subject to the same prudential requirements and would remove the risk of political interference in levy setting. This would still provide the SOE with the flexibility to compete effectively in the market and would also provide the general public with greater confidence as to the transparency of ACC cost allocation, while ensuring taxpayers do not pay the price for ACC or the SOE getting pricing wrong.

15. For what purposes would you require claims data? What type of and level of data access would be necessary and why?

See 5.20 to 5.24.

16. Do you see any other issues with the proposals to collect and share data? If so, how might they be addressed?

Possibly

We agree with the establishment of a central data pool. However, insurers should be consulted on the type of data to be provided. Aggregated data should be shared with market participants but should not identify individual insurers.

Also see 5.20 to 5.24.

17. Is continuous cover assured by the proposals to have ACC cover all workers unless private insurance is in place, and a register of private insurance cover? Why or why not?

Yes, but this is not an effective proposal

The proposal will provide continuous cover, but will not achieve the full benefits of choice or the Government’s objectives of reducing workplace accidents, improving rehabilitation rates and reducing Work Account operating costs.

Continuous cover could still be achieved by adopting the recommendations set out in Part C of this submission and in taking this approach the Government would ensure it meets the objectives noted above.

In particular, there should be the introduction of an opt-in, rather than opt-out model, together with the requirement for ACC to compete as an SOE. This would ensure that continuous cover is provided by both private insurers and the SOE. Employers would still be covered by a default provider as set out under clauses 5.7 to 5.9 above. Furthermore, higher private insurer participation would help create a Work Account culture where employers take greater responsibility for and are prepared to invest in injury prevention strategies and improved processes, including flexible return to work programmes with health and safety regulations and penalty regimes supporting such objectives.

18. Do you agree that the risks and consequences of insurer insolvency are adequately managed by the proposed approach? Why or why not?

Possibly with further consideration

The current proposal requires some further consideration.

As set out at clauses 5.11 to 5.14 above, only insurers registered and resident in New Zealand should be permitted to write accident related business. Otherwise, the Government opens itself to foreign insurer insolvency risks over which it has little or no control. It is also important for the Government to support local insurer investments in New Zealand as well as jobs for New Zealanders.

There is also a need for further clarification around what levy, if any, would be imposed on participating insurers if there was insurer insolvency. Will an insolvency fund be established and levied from the start as per last time and would ACC contribute to this fund? It is difficult to see how a fund could be established and levied solely on a post-insolvency basis.

Will there be a commutation of all outstanding liabilities for the insolvent insurer, with a levy being applied across all market participants based upon their market share? Or will the levy be charged on an annual basis until all liabilities are extinguished (noting that cover is provided until retirement/death of the claimant), and following the fluctuating market shares of the various market participants?

There are also concerns in the industry regarding ACC's ability to undermine competitive pricing in the market and its effect on insurer insolvency. Under-priced premiums are a real risk to sustainable insurer participation in the market. As set out at clause 5.3 above, ACC should be provided with a set amount of capital so as to ensure responsible pricing, with the usual forces of insurance risk management and financial security prevailing over the amount of business which can be written with that amount of capital. This approach would help increase the viability of the Work Account for private insurers and would ensure taxpayers were not picking up the cost of the ACC entity getting their pricing wrong. This would simultaneously tackle a number of the Government's concerns around potential insolvency for insurers, thus creating a truly dynamic and sustainable Work Account which could also work for other ACC accounts.

19. Do you agree that the establishment of a market regulator would adequately protect workers' rights and entitlements? If not, what additional practical steps could be taken?

Possibly

If a market regulator were established there should be a requirement that all participants in the market, including ACC or any established SOE, should be subject to the supervision of that market regulator so as to ensure a level playing field and consistent standards across the entire industry. An independent market regulator should be able to look at all insurers pricing to ensure they are pricing responsibly on a fully funded basis without recourse to taxpayer or future premium/levy contributions, as is currently the case under the ACC monopoly.

Participants in the market should be party to agreeing the terms of reference of the regulator. Costs and governance associated with any regulator should be transparent and appropriately contributed to by all market participants.

20. Do you agree with the proposal to provide for independent dispute resolution in alignment with existing frameworks? Why or why not?

Yes

The Council welcomes the introduction of an independent dispute resolution service for ACC. The Government should consider whether it would be beneficial to have a single approved scheme. It is imperative to ensure this service will not be placed under pressure to become a point of competitive advantage between insurers. A single scheme would help ensure there was a good concentration of skill and expertise, to ensure proficient and consistent interpretation.

The Government should also consider how complaints would be handled where there is uncertainty as to whether an accident is Work or Non-Work related or whether an insurer is liable to contribute to a gradual process claim (see question 25 below).

21. Do you agree that a single, central claims lodgement process would be effective?

Yes with further consideration

The Council agrees that a central claims lodgement process would be useful for minimising administration burdens and compliance costs for providers. However, there needs to be significant development surrounding the functions of the clearing house, its establishment and operating costs, the proportional share of costs including those for late-entrants and the responsibility for unallocated Work claims before meaningful comment around the proposal can be made.

Also, as discussed at clause 4.17, consideration needs to be given to the expansion of the AEP and issues around the allocation of operating costs for the proposed clearing house and how or if AEP employers and TPAs would be subject to any insurer protocols that may be agreed.

An independent entity free of ownership and control by any market participant, which utilises available technology and provides efficient and effective processing, is essential to any proposed solution. The Council is prepared to work with all stakeholders to implement a workable solution.

22. What else might be done to streamline claims administration processes and reduce the risk of increased transaction costs for providers?

As noted in question 21 above, there needs to be an effective and independent claims clearing house which is able to efficiently handle claims invoices. The

clearing house should also have the ability to effectively process payments, should this be required by a particular insurer or SOE. Discussions should be held with possible providers that would be able to streamline the claims process and reduce transaction costs.

There needs to be development with any provider around a number of issues such as how the correct insurer will be identified when an employee seeks medical attention. Nevertheless, any clearing house should be independent of all market participants. Also, its primary purpose should be the correct allocating of claims and the correct invoicing and payments for insurers, not the making of decisions in relation to cover.

23. Do you have any comment on how the cost of public health acute services could be fairly allocated?

Yes

The apportionment of these costs must be transparent and fair. Costs should be based on the actual utilisation of services as opposed to a participant's market share. Pure market share apportionment will not promote reduced workplace accidents. The system needs to be structured so that employers with safer workplaces are rewarded with lower levies and employers with unsafe workplaces are encouraged to implement safer workplace practices in order to benefit from lower levies. Payment should be made retrospectively, although for funding purposes we accept that interim payments based on estimates may be required.

Accredited Employers or any other employers with any risk sharing arrangements should also pay a levy towards these costs based on their utilisation of these services.

It will also be necessary to ensure there is a fair and accurate allocation of costs between the Work Account and other Accounts so that an insurer and any SOE do not end up contributing to costs associated with Non-Work Account injuries. Under the current scheme there is some question as to the allocation between accounts being consistent and correct. Participants in the Work Account should not be liable to contribute towards injuries relating to Non-Work accounts. There should be an independent audit, managed by the regulator, of the allocation of costs between the Work and Non-Work Accounts to ensure that Work Account participants do not pick up any costs associated with other accounts.

Furthermore, ambulatory services should also be based on utilisation of services. Again, these charges should be made retrospectively at year end, although for funding purposes we accept that interim payments based on estimates may be required.

Finally, it would be helpful to be provided with the most recent copy of the sector guide for delivering Health and ACC services (i.e. the Blue Book), so that insurers can better understand the proposed market.

24. Do you agree that private insurers should be able to contract with treatment providers for alternatives to the minimum prices and conditions? Why or why not?

Yes

This will ensure that insurers can reduce ultimate claims costs by focussing on effective claims management and rehabilitation, even if initial provider costs are higher in some cases. Early medical treatment and procedures coupled with timely and effective rehabilitation help ensure claimants get back to work as quickly as possible.

25. Do you agree with the proposed approach to managing gradual process claims? Why or why not?

Possibly

The Government needs to propose a rigorous set of rules relating to cost recovery and claims handling before meaningful comment around this proposal can be made. More work is required to determine the fairest model with the best outcome for claimants. There will obviously be issues around proportional payments if a previous insurer has now become insolvent.

Furthermore, there is clearly room for disagreement between parties as to proportional liability. While it is noted that “the insurer at the time the claim is made” is responsible for managing the claim, with the potential to recover costs from any previous insurer (including the ACC), there is no comment on whether these recoveries are proportional as to the exposure period, or the period between initial exposure and initial diagnosis, or any other measure. There should also be clarity around whether an employer, which has no fault or connection to a gradual process claim, is required to contribute to the claim. We propose that a dispute resolution service should be established to deal with any issues relating to apportionment of costs, as suggested in question 20 above.

Also, where there is a consequential injury, there should be the requirement that all insurers involved in the claim allow a single specialist to decide to which degree the initial injury contributed to the secondary one. This should help alleviate the requirement for an employee to visit a number of different specialists on behalf of the different insurers. If there was any disagreement between participants as to the specialist’s opinion, the issue could revert to a dispute resolution service.

Further work is also required to determine how costs would be allocated for gradual process claims relating to the 1999 period, where insurers passed their claims liability back to ACC on payment of an agreed sum to ACC for taking on these claims.

There should also be the ability for an insurer, carrying the lion-share of liability on a gradual process claim, to be “paid-out” by other liable insurers on the claim, so that the insurer can be solely responsible for its management.

6.6 *The Impacts of the Proposed Changes*

26. Do you have any comment on the impacts of the proposed changes?

Yes

As discussed earlier in this submission, the Council welcomes the introduction of choice in the Work Account and the benefits that choice will bring. The introduction of choice will reduce workplace accidents, improve rehabilitation rates and reduce Work Account operating costs in the longer term.

27. Do you think the proposed risk mitigation and management measures would adequately address the risks? If not, do you have any suggestions for alternative ways to manage these risks?

No

A significant risk for the Government from this proposal is from ACC remaining in the market with a large competitive advantage. The Government's proposal compromises the benefits that could be obtained from creating a sustainable, competitive market with meaningful insurer participation. As a result, the Government seriously risks not achieving its stated objectives of improved workplace safety, better rehabilitation rates and stronger incentives for managing ACC costs. If the Government were to adopt the Council's recommendations, as set out in Parts C and D of this submission, it would be much better placed to meet its objectives of providing a sustainable ACC scheme for all New Zealanders going forward.

7 Conclusion

- 7.1 The Council welcomes the decision to introduce choice into the ACC Work Account and we encourage the Government to proceed with its proposal to allow choice. Together with the Government's stated objectives, a significant objective should be the establishment of a sustainable accident insurance scheme for the future benefit of all New Zealanders.
- 7.2 Whilst the Council welcomes the introduction of choice into the Work Account, the Council is of the opinion that the proposal does not go far enough towards creating a sustainable market which will realise the full potential benefits of choice.
- 7.3 In order to fully benefit from choice, the Council recommends the Government adopt the proposals outlined in Part C, together with our recommendations regarding the discussion document questions, as outlined in Part D. The Council, through its Accident Insurance Committee, is committed to working constructively with the Government in order to develop the current proposal it has put forward.

13 July 2011