Submission

By

BusinessNZ
The voice of business

to the

Accident Compensation Corporation

on the

Levy Consultation 2014/15 Proposed Rates

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ACC LEVY CONSULTATION 2014/15 PROPOSED RATES
SUBMISSION BY BUSINESSNZ[1]

1.0 INTRODUCTION

1.1 BusinessNZ welcomes the opportunity to comment on the proposed levy rate changes set out in the ACC Levy Consultation 2014/15 document.

1.2 Employers, employees and motorists will welcome the levy cuts of between 15 and 17 per cent proposed for the 2014/15 year (with further cuts projected the following year). The cuts are significant and will effectively provide a slight boost in take-home pay while reducing non-wage labour costs for employers.

1.3 A 17% reduction is proposed for the average Work levy (from $1.15 to $0.95 for every $100 of liable earnings), a decrease of 15% for the Earners Account (from $1.48 to $1.26), with the Motor Vehicle account levy projected to drop by 15%. As ACC progresses towards full funding and no longer needs to collect a residual levy to fund past claims, overall reductions become possible. The Work and Earners Accounts are already fully funded, while the Motor Vehicle Account has improved relatively strongly from its significantly underfunded position a few short years ago.

1.4 Nevertheless, the reasoning behind levy reductions should be more transparent, so that it is clear whether or not proposed reductions are based on fully funded accounts. Rehabilitation improvements and improved investment income, not fully funded accounts, have consistently been given as the key reasons for previous levy decreases and it seems improved investment income has been the true key driver of past reductions. But reductions should not be based on investment income improvements as investment income will always fluctuate.

1.5 Notwithstanding the significant levy reductions outlined above, BusinessNZ has major and continuing concerns about levy transparency and the various accounts. This submission covers four areas:

- First, ACC's overall funding policy aimed at ensuring full funding across accounts within a "funding band" of between 100% and 140% funded. Proposed funding levels in the out years appear excessive given ACC is a state monopoly with the power to tax future employers, earners and motorists;

- Second, transparency in premium setting without undue political interference;

- Third, the significant degree of continued cross-subsidisation in the Motor Vehicle Account, a situation not adequately addressed in the proposed premium setting for 2014/15; and

[1] Background information on BusinessNZ is attached as Appendix 1.

- Fourth, a lack of contestability in the ACC market preventing the implementation of wider insurance mechanisms that would provide further incentives to reduce the number and severity of accidents and assist with the early rehabilitation of injured persons. ACC has made some progress towards bringing in greater insurance-based disciplines (such as limited experience-rating and proposed moves to introduce risk-rating for cars based on crash results) but these developments have been rather tentative to date and cannot be considered the justification for reduced levies.

RECOMMENDATIONS

BusinessNZ **recommends** that:

1. **ACC re-examine whether an effective funded risk margin of between 0 and 40% is justified for the Work, Earners' and Motor Vehicle Accounts given the unique circumstances of New Zealand's ACC scheme (i.e. the power to tax future levy payers) with its implications for costs on levy payers across the various ACC accounts.**

2. **ACC premiums should be set by the ACC Board, audited by independent third party actuaries - with the results made public - and their rationale explained, to ensure transparency in the premium-setting process.**

3. **The Minister's reasons for rejecting or modifying the ACC Board's recommendations, including the actuarial analysis (should this occur) be made public so both premium payers and ACC can scrutinise the decisions made, limiting the potential for political opportunism.**

4. **The significant cross-subsidisation of motor cyclists by motorists be urgently addressed, recognising that over the next 3-5 years, current cross-subsidisation will make necessary a staged levy review process to reflect risk more accurately.**

5. **Consideration be given to introducing mechanisms to ensure all road users (whether motorists, truck drivers, motorcyclists, or cyclists) pay the real costs associated with road use.**

6. **The various ACC Accounts, where applicable, be progressively opened up to competition from private sector providers (starting with the Work Account), with the Government's role ultimately restricted to ensuring minimum service and delivery standards within a risk-based, 24-hour universal no-fault system.**

2.0 OVERALL ACC FUNDING POLICY

2.1 It is important for both the ACC Board, and ultimately the Minister, to be held to account for setting premium rates which reflect sound commercial practice and minimise the risk of on-going interference to meet political objectives.

2.2 While levy stability is a desirable objective, it should not override the important signals which levy payers ought to receive about the true costs associated with accidents (whether the result is a reduction or an increase in premiums over time).

2.3 Notwithstanding factors that affect the number and cost of claims and make forecasting future liabilities difficult, Business NZ considers ACC's need for a fully funded risk margin is open to question. In BusinessNZ's view the margin (if any) should be more in the order of 5 – 15 per cent than the 0 – 40 per cent band proposed, for three reasons.

2.4 First, while BusinessNZ accepts that some private sector insurers may build in an additional risk margin to cover unexpected risks in insurance premium setting, it is not at all obvious why ACC should do likewise. As ACC is effectively a state-monopoly provider of accident insurance, it has (via government legislation) the power to tax future employers if premiums collected in any one year are insufficient to fund the on-going costs of the claims associated with accidents in that particular year.

2.5 Second, if the accounts are effectively "over-funded" (i.e. fully funded plus a substantial margin), the temptation may be for the government of the day to expand the scheme knowing that the costs of expansion will be hidden, at least for the first few years. Given that ACC is a state-sanctioned monopoly, without the on-going discipline that competition would provide, the very conservative approach to funding envisaged in the Discussion Document is unlikely to be necessary.

2.6 Third, tying up unnecessary funding from employers (and earners) effectively means depriving the economy of money. On the margin at least, this will reduce employer investment in plant and equipment thereby limiting economic and employment growth.

BusinessNZ **<u>recommends</u>** that:

1. ACC re-examine whether the proposed effective funded risk margin of between 0 and 40% is justified for the Work, Earners' and Motor Vehicle Accounts given the unique circumstances of New Zealand's ACC scheme (i.e. the power to tax future levy payers) with its implications for costs on levy payers across the various ACC accounts.

3.0 <u>TRANSAPARENCY IN PREMIUM SETTING</u>

3.1 Business New Zealand notes that ACC levy recommendations are not binding on the Minister (of ACC) who can "accept, reject, or modify the Corporation's recommendations". While the Minister should be able to change ACC's premium rate recommendations if new information comes to hand suggesting ACC's actuarial advice was flawed, there has been a tendency over the years for ACC Ministers to tinker with ACC's recommendations and to make recommendations of their own.

3.2 It is possible that ministerial changes will be soundly based on actuarial analysis but there is a danger they may reflect wider political judgements as to what ACC premiums should be. For example, last year's decision by the Government to retain ACC levies at existing levels (i.e. unchanged), despite recommendations by the ACC Board for significant reductions, reeked of political interference and made public consultation on the proposed levies something of a farce. However, since its inception in the early 1970s, and spanning a wide range of governments, the scheme has always been subject to political manipulation when it comes to premium setting.

3.3 Business New Zealand believes that if the Minister decides to reject or modify ACC's recommendation(s), the reasons for non-acceptance should be outlined to the public and premium payers and the actuarial advice on which the changes have been made provided. It is not acceptable for the Minister to change ACC's recommendations without making clear why different decisions have been made.

3.4 Similarly, there needs to be greater transparency over the justification for any levy reductions. We question the stated justification for levy decreases in the 2014/15 ACC Levy Consultation Document – i.e. that "*Strong rehabilitation and financial performance over the last few years has provided the Corporation with the platform to invest back in the business. It has also allowed us to consider a reduction in levies*." This statement is made notwithstanding ACC forecasts that rehabilitation spending is likely to increase in the 2014/15 year.

3.5 It is essential not to base levy reductions on improved investment income as this will always fluctuate. Indeed, one of the highest risks the Corporation identifies is that long-term investment performance could decline, requiring a significant increase in levy rates to achieve the same level of income. It is important to note that under a competitive model premiums/levies would be priced to reflect risk and investment returns appropriately reserved to meet long-tail claims, not to reduce premiums artificially.

3.6 In the absence of transparency, there is a risk that it will be thought, rightly or wrongly, that premiums have been set to take account of political realities rather than sound commercial practice. Clearly the ACC Board is the most appropriate mechanism for setting levy rates, given the Board's responsibility for the efficient running of the current scheme.

Business NZ **recommends** that:

2. ACC premiums be set by the ACC Board, audited by independent third party actuaries - with the results made public - and their rationale explained, to ensure transparency in the premium-setting process.

BusinessNZ **recommends** that:

3. The Minister's reasons for rejecting or modifying the ACC Board's recommendations, including the actuarial analysis (should this occur) be made public so both premium payers and ACC can scrutinise the decisions made, limiting the potential for political opportunism.

4.0 CROSS-SUBSIDISATION IN THE MOTOR VEHICLE ACCOUNT

4.1 BusinessNZ notes that this year some effort has been made to ensure premiums more accurately reflect risk between certain vehicle types. The proposal to introduce risk-rating for cars based on crash results, for example, is a positive move as safety features in newer cars can significantly reduce the number and severity of road injuries.

4.2 Notwithstanding the above, a number of road users, principally cyclists, pay nothing towards the cost of accidents involving motor vehicles (although it is noted that cyclists who also have a car will contribute to ACC costs through both petrol taxes and relicensing fees). And motorcyclists continue to be grossly subsidised by motor vehicle owners.

4.3 The Consultation Document shows cross-subsidisation between transport modes to be both significant and unjustified. The nature of insurance is to pool similar risks within similar risk categories (and as a result some cross-subsidisation is inevitable) but the Consultation Document shows that little progress has been made to address the issue.

4.4 The reference below clearly indicates massive cross-subsidisation between motorcycles and passenger vehicles. It is taken directly from the Frequently asked Questions and Answers (FQAs) section of the ACC Levy Consultation Document. In response to ACC's "question 20" – **What is the true relativity between mopeds or motorcycles and passenger vehicles?** The ACC responded:

- Passenger vehicles 100%
- Mopeds 225%
- Motorcycles (600cc or less) 1000%
- Motorcycles (over 600cc) 1800%

4.5 Given a trend towards the greater use of motor cycles and/or bicycles, there is a need to examine seriously whether ACC premiums should apply to those regularly using their cycles on-road and, as well, whether they should better reflect the cost of motor cycle accidents. Motor Vehicle Account funding currently involves significant cross-subsidisation from motor vehicle owners to motor cyclists, as previously noted. Even accepting that some degree of cross-subsidisation is inevitable in any insurance scheme, here the degree of cross-subsidisation is clearly detrimental to sending accurate information and incentives to motorcyclists and users of other transport modes about the real risks of injury and the associated costs.

4.6 There have been moves over the past few years to reduce cross-subsidisation in Motor Vehicle Account levies but these have been tentative to say the least; mainly they have focused on removing some of the distortions within each class of vehicle (e.g. between small and large motorcycles) rather than on addressing cross-subsidisation of motor cyclists by motorists per se. Business NZ considers a thorough investigation of the funding of the Motor Vehicle Account is justified so that the costs associated with the scheme can be aligned more closely to scheme claimants.

BusinessNZ **recommends** that:

4. The significant cross-subsidisation of motor cyclists by motorists be urgently addressed, recognising that over the next 3-5 years, current cross-subsidisation will make necessary a staged levy review process to reflect risk more accurately.

BusinessNZ **recommends** that:

5. Consideration be given to introducing mechanisms to ensure all road users (whether motorists, truck drivers, motorcyclists, or cyclists) pay the real costs associated with road use.

5.0 BENEFITS OF CONTESTABILITY

5.1 Several BusinessNZ members have raised the issue of contestability in the provision of ACC services.

5.2 Central government does not have to be a monopoly service provider of accident insurance in order to meet its social and economic objectives. Contestability would allow for an improved service to both funders and claimants as providers would need to focus much more closely on efficiency and cost-effectiveness than is currently the case with ACC.

5.3 Contestability in the provision of ACC services and delivery would provide a number of benefits while posing little downside risk. A competitive model would not mean the end of the no-fault nature of the ACC scheme but would more likely provide the following positive outcomes:

- **Monitoring of claims and management of risk would likely be more pronounced.** Employers', earners' and motorists' premiums would more accurately reflect actual risk and claims' history than they do at present. Employers would be rewarded for providing safer workplaces.

- **Under a competitive model, any attempt to pass on an insurer's inefficiencies would result in levy payers shifting their business to another insurer.** Insurers who tried to increase premiums beyond the market-justified level would be penalised through reduced market share. Allowing new insurers to enter the market at any time would keep premiums at actuarially fair levels. Employers who experienced a significant and unwarranted increase in the amount currently paid would have the right to switch insurers.

- **Premium options would more likely meet the unique needs of enterprises rather than the one-size-fits-all approach.** Greater use of risk sharing arrangements would likely be common under a competitive regime. At present, employers have choice only in their ability to partially self-insure through the Accredited Employer Programme (around 160 employers are in this programme covering, it is understood, about 25 per cent of the workforce). For most employers – small and medium sized enterprises – the Accredited Employer Programme is not a realistic option.

- **Private insurers would likely invest significant resources in the monitoring of claims.** Better claims monitoring would ensure claims were dealt with quickly, appropriate treatment given, and claimants encouraged back into work as promptly as possible. Early medical treatment and procedures coupled with timely and effective rehabilitation would help ensure this happened, likely reducing costs over time.

- **Private insurers would encourage greater innovation.** To get better outcomes, it is in the financial interests of competing insurers constantly to introduce more effective approaches to administration, injury prevention, case management and rehabilitation. In addition, insurers would likely provide add-on benefits to meet their customer's particular needs.

- **Under a competitive model there would be less risk to the Crown.** Much of the risk associated with underwriting accident insurance claims would be transferred from the Crown's balance sheet to the private sector.

Business New Zealand **<u>recommends</u>** that:

6. The various ACC Accounts, where applicable, should be progressively opened up to competition from private sector providers (starting with the Work Account), with the Government's role ultimately restricted to ensuring minimum service and delivery standards within a risk-based, 24-hour universal no-fault system.

APPENDIX 1

BACKGROUND INFORMATION ON BUSINESSNZ

BusinessNZ is New Zealand's largest business advocacy organisation.

Through its four founding member organisations – EMA Northern, Employers' Chamber of Commerce Central (ECCC), Canterbury Employers' Chamber of Commerce (CECC), and the Otago-Southland Employers' Association (OSEA) – and 70 affiliated trade and industry associations, Business NZ represents the views of over 76,000 employers and businesses, ranging from the smallest to the largest and reflecting the make-up of the New Zealand economy.

In addition to advocacy on behalf of enterprise, BusinessNZ contributes to Governmental and tripartite working parties and international bodies including the International Labour Organisation (ILO), the International Organisation of Employers (IOE) and the Business and Industry Advisory Council (BIAC) to the Organisation for Economic Cooperation and Development.