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Maximising the value from self insuring your ACC liabilities

The ACC self insurance option offers larger employers the opportunity to benefit directly from their investment in good health and safety practices. But how well do employers understand the options, including the full extent of the liabilities they are assuming? This newsletter reviews this important insurance programme for companies.

1. Introduction

Most large employers choose to self insure their ACC liability. They decide on this option rather than fully insuring the liability with ACC for a fixed determined premium. Why do they choose this option?

Experience shows that this approach delivers important financial benefits to them. In this newsletter we:

- Ask the question of why self insure
- Provide basic details on the self insurance options
- Highlight the different liabilities that thereby arise to an employer
- Illustrate how we derive the liabilities for an employer's financial accounts
- Look at some experience results to date
- Ask the question of where the ACC standard premium is going in the next few years and what this means to self insurers
- Look at the options available when budgeting for ACC annual costs.
- Address the issue for large employers of how to allocate costs between different operating divisions: so necessary in order to emphasise to line managers the key role health and safety plays in bringing down accident costs.
- Assessing the performance of the claims administrator

2. Why self insure?

The reasons for self insuring are:

- The expectation that when compared to the option of paying the standard ACC premium, the total cost to the employer will be less under the self insurance option.
- This lower cost will be primarily due to the ability of the employer to manage their own claims and look after their own people which in the main they would be better placed to do than ACC. An example of this is that the employee can be put on light duties and be better managed back to full time employment. Also having the employee on light duties will eliminate the need to employ another temporary person to take up the work load of the injured worker.
- The employer will realise and benefit directly from their investment in good health and safety practices in the work place.

3. Basic scheme details

There are 2 insurance scheme options:

- The full self cover option (FSCP) where the employer assumes all the future costs, subject to certain limits, but with the claims management period is limited to 4 years.
- The limited insurance option (PDP) where the employer has the ability over either a 1 or 2 year period to manage their own claims, with no open ended liability from thereon.

An employer will choose to either manage their own claims or employ a third party administrator (TPA). They have 4 or possibly 5 providers to choose from.

The employer pays a reduced premium which covers:

- ACC administration costs including levy setting costs, injury prevention and health and safety programme costs.
- Unallocated primary health costs which should be paid by the employer but where ACC is unable to allocate the costs of a claim back to an employer
- Bulk funded public health costs which principally cover the cost of accidents admitted to hospitals
- Insurance (the employer's liability cap).

An employer has to go through an accreditation process to be admitted into the self insurance programme. There are also regular audits of their health and safety processes plus claims management processes.

4. The different insurance options

FSCP Under the FSCP an employer is required to have stop loss insurance to protect itself from poor claims experience in a cover period. The employer can select any level between a set minimum and maximum amount. The minimum is set at 160% of the expected claims costs and the maximum at 250% of the expected claims costs. If the limit is breached, including the cost of any hand back claims, the employer's costs are capped at this level and ACC meets all the residual costs.

The most likely way of breaching the stop loss limit is if the employer has either a small number of large claims or one extremely large claim.

For some employers, just using stop loss cover will mean their potential total claims cost could still be higher than they would like. To limit this cost an employer can effect High Cost Claims Cover *(HCCC)* to cover any one event irrespective of the number of claims made. Cover is available for claim amounts in excess of $250k, $500k, $750k and $1 million. The cost of each of these options can be assessed using the calculator on the ACC website.

PDP Under the PDP option ACC provides the employer with a credit for what the claims would have cost them and it is up to the employer to bring their costs in below this amount. The credit given by ACC varies on the risk group but in the current year is on average worth 51.5% for a 1 year claims management period and 58.5% for a 2 year period.

Note that on average 30% of claims costs will be paid during within 12 months after the accident and 55% by 24 months, so under the PDP all but a few claims of a long term nature will have been dealt with. In addition the number of claims left after 24 months should be minimal.

Accordingly an employer may choose the PDP option if they want to manage their own claims, are prepared to pay up to a certain cost for this but do not want a large variability in the cost involved.

5. Deriving liabilities for the financial accounts

The accident costs in respect of any one cover period could continue over the lifetime of an injured worker. While the basic weekly income benefit to an employee ceases at age 65 the other costs comprising ongoing medical treatment could well be lifetime costs continuing after age 65.

At the end of a financial year we consider the following when deriving the outstanding liability:

- The value of the currently open claims. Estimates will need to be put on these claims, and allowance for future development of the costs.
- The claims previously closed may well re open and a provision is required for this.
- An allowance must be made for those claims which have yet to be reported but which can be attributable to a past cover period. Included in this category are gradual process claims.

An illustrative example of how we present the results is attached in Appendix A.

As noted above, an important component of the liability is the open claims estimates. We are able to compare how previous estimates against current cost assessments. If there is a clear divergence then an adjustment may be warranted.

6. Review of some employers ACC experience

As a consequence of determining an employer's liability, it is straightforward then to compare the results with the costs an employer would have incurred if they had fully insured.

Data tends to show the following:

- With few exceptions, the costs are less than the standard premium costs.
- There is the occasional year when poor experience with 1 or 2 claims will see a jump in the employer's costs.
- There are very few cases where the HCCC is breached and even fewer cases where the stop loss is breached.
- Despite the significant recent reduction in the levels of standard ACC premiums this has not made a marked difference in the value of the self insurance compared to the employer paying the standard ACC premium.

An example of the results of comparing an employer's experience with paying the ACC premium is included in Appendix B.

7. Using the results of the actuarial review as part of the health and safety regime

ACC costs have two components, the frequency of accidents and the claims costs. The former costs will depend very much on the health and safety regime in place. The latter costs depend on the rehabilitation regime. Both are equally important.

What statistics can we usefully provide as we review the claims data? These include:

- Dollar costs by development year for each cover period.
- Number of claims split by medical only and entitlement claims.
- Duration of claims.
- Comparison of costs by injury type by operating site or division.
- Comparison of costs by cover period.
- Delay in reporting accident and when it occurred.

Where possible we will supply a comparison with the expected result based on ACC statistics.

While the claims administrator will report regularly on the cost of claims the actuarial review provides a once a year opportunity for these statistics to be carefully reviewed for what they say about worksite safety.

8. Hand back claims

Employers arguably have their greatest frustrations around hand back claims and the estimates ACC puts on these. The only comment one can make is that by definition the assessment will be somewhat subjective and based solely on how they assess the future costs. Where these charges look high they will rightly be contested by an employer.

The only way to avoid this issue is to not to have any hand back claims!

9. Assessing the third party administrator

The role of the TPA is all important in achieving good rehabilitation outcomes for the employer. At the same time, its general knowledge will be a contributor to the employer's health and safety strategy.

It is hard to make a definite assessment of the TPA's performance although the ability to form a view on this is important. The only organisation which can be used in comparison against the TPA's is ACC itself. However a review of outcomes for the employer over a period of time will provide a starting basis for the employer to ask some real questions of the TPA.

10. Future increases in premiums

ACC cost pressures have been well publicised, particularly since the new Government took power in November 2008.

Our newsletter in September 2008 which reviewed the rates proposed for the 2009/10 year included the following:

- Cost of claims for 2009/10 ignoring the surplus is $1.09 per $100 liable earnings.
- This compares to the rate proposed of 70 cents, and a projected rate for 2010/11 year of 85 cents.

Since these premium calculations were done, the financial crisis will have impacted adversely on ACC investments and reduced the existing reserves meaning that the required premium for 2010/11 could well be around the 90 cents level up 20% from the current 75 cents rate.

The expected increase in the ACC premium will only increase the attraction of the self insurance option to employers.

11. Budgeting the annual ACC costs

What does an employer in the self insurance arrangement include in their financial budgets? The starting point is the ACC premium for the year. Allowance could be made for the expectation that costs will be less than the ACC premium. The actual cost for the year will be derived from the actual amounts paid plus the change in the actuarial liability over the year ends. The costs of the claims administration must be included in the total cost.

If requested, it is possible for the actuary to make a projection of the expected costs and the outstanding liability at the end of the financial year.

12. Splitting the costs between the different operating divisions

An employer who is self insuring their costs will want to ensure that each operating division is allocated its own accident costs correctly. Just allocating all these costs to "corporate" will not assist the people at the front line who can by their actions make a difference to the accident incident rate. The one difficulty in this area is that allowance has to be made for the cost of large claims in one division.

It is not reasonable to allocate all this cost to the one division; the reason being that quite possibly each division would not be able to self insure on its own. A basis has to be found to spread these large claim costs across the whole company. Most approaches to this would involve capping the cost of any one accident that can be charged to each division, but sharing any actual costs above the cap across all divisions. There are several ways of doing this that could range between:

- The simplest approach would apply a set cap for all divisions and divide any excess in proportion to the basic claims costs for each division, and
- For large entities with diverse operations, using formulae based on the size and risk involved in each division's operations to determine appropriate caps and shares of charges. These calculations might refer to the standard ACC rates for the various activities involved.

13. ACC website

More information on the ACC Partnership Programme can be found by clicking here.

ABOUT MELVILLE JESSUP WEAVER

Melville Jessup Weaver is a New Zealand firm of consulting actuaries. The areas in which we provide advice include superannuation, employee benefits, life insurance, general insurance, health insurance, asset consulting, accident insurance and information technology. The firm has offices in Wellington and Auckland.

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Appendix A

Estimation of ACCPP Outstanding Claims Liabilities as at 31 March 2009

Accident/Cover Period	2000/01 $000s	2001/02 $000s	2002/03 $000s	2003/04 $000s	2004/05 $000s	2005/06 $000s	2006/07 $000s	2007/08 $000s	2008/09 $000s	Total $000s
Estimated claims paid										
Claims paid to 31 March 2009 (including handbacks)	666	1,280	1,243	1,235	1,096	1,053	1,034	1,035	658	9,301
Estimated future claims										
IBNR claims	13	17	19	28	39	48	79	114	489	846
Reopened claims	17	35	44	69	95	149	171	208	176	964
Open claims	0	0	0	0	0	31	138	217	493	879
Total future claims	30	53	63	97	134	227	388	539	1,157	2,688
Total estimated claims before stoploss	696	1,332	1,306	1,332	1,230	1,281	1,422	1,574	1,815	11,989
Stoploss cutoff	4,538	5,659	6,230	4,675	5,001	4,973	6,406	9,465	7,548	
Claims in excess of stoploss	0	0	0	0	0	0	0	0	0	0
Total estimated future claims after stoploss	30	53	63	97	134	227	388	539	1,157	2,688
Claims management expenses reserve	2	4	5	7	10	17	29	40	87	202
Total Outstanding Claims Liabilities Required	**32**	**57**	**68**	**104**	**144**	**244**	**417**	**580**	**1,244**	**2,890**

Note: All figures exclude GST unless otherwise stated

Appendix B

ACCPP Experience as at 31 March 2009 (Net of stoploss)

Cover Period	2000/01 $000s	2001/02 $000s	2002/03 $000s	2003/04 $000s	2004/05 $000s	2005/06 $000s	2006/07 $000s	2007/08 $000s	2008/09 $000s	Total $000s
Levies										
Bulk funded health costs	116	115	119	173	169	156	147	116	119	1,230
FSCP Administration Fee	94	135	143	130	157	137	108	168	175	1,249
Stoploss / HCCC	21	33	41	63	79	75	100	150	180	742
Total FSCP Levy (excl. GST)	232	284	303	367	405	368	355	434	474	3,220
Claims										
Estimated claims paid to 31 March 2009	666	1,280	1,243	1,235	1,096	1,053	1,034	1,035	658	9,301
Outstanding Claims Liabilities as at 31 March 2009	32	57	68	104	144	244	417	580	1,244	2,890
Total claims cost (excl. GST)	698	1,336	1,311	1,340	1,240	1,298	1,451	1,614	1,902	12,191
Administration Costs (excl. GST)	267	319	41	475	363	374	352	332	321	2,844
Total Costs (excl. GST)	**1,197**	**1,939**	**1,655**	**2,181**	**2,008**	**2,040**	**2,158**	**2,381**	**2,696**	**18,255**
Standard levy net of SMP discount	**2,672**	**3,112**	**3,293**	**3,688**	**4,448**	**3,894**	**3,408**	**2,642**	**2,475**	**29,632**
Total Costs as % of Standard Levy (net SMP discount)	**45%**	**62%**	**50%**	**59%**	**45%**	**52%**	**63%**	**90%**	**109%**	**62%**