Melville Jessup Weaver

Topix

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Consulting Actuaries

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ACC 2006/07 proposed levy rates and current issues

Introduction

This issue of Topix sets out some of the items raised in the recently released ACC document *Accident Compensation Corporation 2006/07 Levy Rates for Employers Consultation Document* that may be of interest to employers, particularly those that are participating employers under the ACC Partnership Programme. Submissions on the Document are due by 3 November 2005.

A. Proposed Levies for 2006/07 – Employers' and Residual Claims Accounts

1. Employer levy rates

Process for setting the rate

From 1 July 1999, ACC has set its levies based on the "fully funded" concept, with the levy charged to an employer set to cover the expected future costs of all benefits for claims arising in that levy year. Employers are also charged a "residual" levy that is intended, by 2014, to establish a fund sufficient to meet the expected future costs of benefits for claims that occurred prior to 1 July 1999. The deficiency for these past claims arose from the time ACC was funded on more of a pay-as-you-go basis.

Given the uncertainties involved in estimating the future benefit costs of claims that may last up to 40 years, setting the levy rates is a difficult process with further uncertainties arising from estimating the costs of administering claims and future interest rates changes.

ACC needs to charge rates that equitably reflect the expected future cost of claims for each industry standard levy rating group – of which there are currently 129, with 127 proposed for next year. This process involves striking a balance between having too many groups, with potentially volatile levies, or too few groups, with the consequent inequities that arise from lower risk companies and industries being grouped in with higher risk ones. There is no correct answer to this issue; it is a matter of striking a balance and attempting to maintain a reasonably consistent treatment from year to year.

Proposed rates for 2006/07

The proposed composite levy rate for the 2006/07 year is the same as for the current year, with an offsetting $0.02 change for the standard and residual levies, as the table below shows.

	Current rates	Proposed rates
Average levy rate for 2006/07 claims (standard levy rate)	$0.88	$0.86
Average levy rate for pre-1999 claims (residual levy rate)	$0.33	$0.35
Average levy rate per $100 payroll (composite levy rate)	$1.21	$1.21

The ACC document forecasts levy rates increasing steadily over the next few years to $0.93 for 2009/10. The underlying drivers for the steady increase in levy rates are the increasing number and average cost of claims, in particular entitlement claims (e.g. weekly compensation benefits), although for the next year the costs for an entitlement claim are forecast to fall. As well, the rates in the shorter term are benefiting from the use of the current excess reserves. Conscious of this future trend, ACC has resisted the opportunity to reduce the 2006/07 standard levy rate to $0.84.

The average rates in the table above set out an aggregated position. Currently each employer is classified into one of 554 "classification units", based on the ANZSIC industrial classification system.

Each of these classification units is then grouped into one of the proposed 127 standard levy rating groups. The concept is that employers or industry groups with similar claims experience and activities are grouped together for rating purposes. From time to time, based on a re-evaluation of their claims experience, some classification units may move to another levy rating group.

Top increases, decreases

The table below shows the top five increases and decreases for the levy rating groups.

Levy Code	Description	Current 2005/06 rate	Proposed 2006/07 rate	% increase
682	Equestrian Activities	$4.81	$6.01	24.9%
686	Sports & Services to Sport	$5.18	$6.47	24.9%
122	Poultry Farming	$2.09	$2.61	24.9%
730	Fire Brigade Services	$1.38	$1.72	24.6%
610	Property Services, Business Services & Animal Care	$0.35	$0.43	22.9%
Levy Code	**Description**	**Current 2005/06 rate**	**Proposed 2006/07 rate**	**% decrease**
652	Medical and Optical Services	$0.11	$0.08	27.3%
352	Iron & Steel Casting & Forging	$3.96	$3.05	23.0%
327	Chemical Products	$0.76	$0.61	19.7%
273	Textile Floor Covering Manufacturing	$2.87	$2.32	19.2%
280	Skin & Hide Processing	$3.07	$2.51	18.2%

2. Proposed Levies for 2006/07 – Other Accounts

Self-employed – The work claims average levy rate net of GST is proposed to increase to $2.06 per $100 payroll from the current year's rate of $1.82. The increase in the average rate is primarily due to the lower than expected incomes being declared by the self-employed, which must still support a high and steadily growing cost of claims.

The residual average, net of GST, levy rate for the self-employed, as for the employers' account, is proposed to increase to $0.35 from $0.33 in the current year.

Earners - The proposed average levy rate net of GST for non-work injuries for earners is $1.16 per $100 liable earnings, up from $1.07 last year. The proposed increase is driven by a steady increase in claim costs.

Motor vehicle levy - The proposed average net of GST motor vehicle levy is $190.00 per vehicle, a reduction from the current year's $206.93. The petrol levy rate is proposed to be maintained at 5.78 cents per litre. The proposed reduction is driven by a reduced cost of claims and a higher than expected number of vehicles on the road consuming more petrol than expected.

3. Workplace Safety discounts programme for small employers and self-employed

The claims incidence and average costs for small businesses are worse than for large employers, and ACC has identified six particular industry sectors that generate a disproportionate level of claims: agriculture, forestry, construction, road freight, motor trades and fishing.

Currently ACC recognises good safety practices for larger employers by way of the Workplace Safety Management Practices Programme, which offers levy discounts of 10%, 15% and 20% for qualifying employers. This programme is not available for smaller employers or for the self-employed.

ACC now proposes to offer a 10% discount to small employers that meet the criteria, which principally involves demonstrating a credible level of hazard management. Random, on-site audits of successful applicants will be used to verify compliance.

4. Proposed changes in classification units

ACC proposes to introduce a new classification system for the 2007/08 levy year, with this change driven by the development of a new industry classification system, ANZSIC 2006. The new system has been developed in response to technological changes which have brought about significant changes in the way certain industries and businesses operate. The key changes are identified as:

- Increase in number of divisions (a high level grouping) from 17 to 19,
- Creation of a new division "Information Media and Telecommunications", and
- Separation of "Property and Business Services" into three new divisions:
  - Rental, Hiring and Real Estate Services,
  - Professional, Scientific and Technical Services, and
  - Administrative and Support Services.

ACC has indicated that the proposed change in the classification structure will not impact on the average levy rate assessment, and we would expect this to be the case. As yet however there are no details as to how these changes might influence rates for particular levy groups.

B. ACC's Statement of Financial Performance for June 2005

The table below summarises the ACC accounts for the June 2005 year.

	Group Actual 2005 $billion	**Group Actual 2004 $billion**
Total net levy income	2.735	2.655
Total claims cost	(1.937)	(1.798)
Operating, injury prevention and collection costs	(0.337)	(0.302)
Adjustment to claims liability	(2.037)	(0.170)
Total expenditure	(4.311)	(2.270)
Net investment income	0.777	0.489
Other income	0.005	0.002
Net surplus / (deficit) after tax	(0.794)	0.876

The unfunded liability as at 30 June 2005 was $4.167 billion, compared to $3.375 billion the previous year. The increase is primarily due to a reduction in the discount rate used to value the liabilities and an increase in the expected future cost of current claims. The Employer Account surplus for the year was $90.3 million compared to $208.9 million the previous year. The account itself has an excess of assets over liabilities of $407.6 million, which provides a useful cushion for future levy rates.

C. ACC Partnership Programme (ACCPP)

Apart from some changes to the various fees, no changes are proposed to the structure of either the Partnership Discount Plan (PDP) or the Full Self Cover Plan (FSCP) for the 2006/07 cover year.

1. Changes to fees

The changes to the fees common to both Plans are:

- the administration fee reduces to 1.5% from 2.0%,
- the primary healthcare fee increases to 1.2% from 1.0%,
- the public health care services levy increases to 4.3% from 4.0% last year, and
- relatively small changes have been made to the stoploss levy rates and high cost claim cover levy rates for both PDP and FSCP.

2. Partnership Discount Plan

The significant change is the increase in the levy discounts. For the one year claims management period the average discount has increased from 39% to 47%. For the two year claims management period the discount has increased from 47% to 54%.

3. FSCP Claims Liabilities

Under the FSCP, the participating employer is responsible for the lifetime cost of claims arising from accidents in cover periods for which it is on risk. This includes responsibility for the cost of claims beyond the end of the claims management period.

Most accidents resulting in injury are relatively minor, and their claim costs are correspondingly small. Serious accidents that cause severe injury or death however may create large liabilities extending over many years – some of them well into or even beyond the end of the claims management period.

Serious injuries under the ACCPP causing claims payments beyond the end of a company's financial year end need to be recognised in the participating employer's balance sheet if they arise from events prior to the balance date, are likely to occur and can be reliably estimated. ACCPP long term claims meet all of these criteria.

Many participating employers will now have their first experience of transferring back to ACC claims that have reached the end of their claims management period. This will have increased their awareness of the potentially long-term nature of ACC claims and the costs of transferring them back. Around 25% of employees in New Zealand are covered under the ACCPP.

ACC's most recent financial statements show a value for the claims liability under the Employers' Account of $894 million. This amount is exclusive of claims that are currently the liability of employers in the ACCPP. Given the number of employees covered under the ACCPP compared to those covered directly but ACC, it is clear that there should be in aggregate substantial provisions in participating employers' balance sheets for these liabilities. The aggregate cost to employers would seem to lie around the $200 million plus level.

Having an estimate of the claims liabilities under the ACCPP allows companies to also make a far more realistic estimate of their actual experience under the programme and therefore make a better informed decision about the benefits or otherwise of remaining in it. Of equal importance is the opportunity to analysis their own claims experience, to see to what extent the statistics can be used to change and improve existing workplace practices and reduce future costs.

For further information please contact:
Auckland
Neil Christie *Phone (09) 300 7571*
Mark Weaver *Phone (09) 300 7156*
Wellington
Janet Lockett *Phone (04) 499 0277*