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MELVILLE JESSUP WEAVER
CONSULTING ACTUARIES TOWERS PERRIN ALLIANCE PARTNER

October 2009

ACC – 2010/11 Proposed Levy Rates

1. Summary

While the size of the proposed levy rate increases for the 2010/11 year comes as a surprise, the fact that ACC levy payers were in for some major future increases was apparent in the Consultation Documents of September 2008.

The published levy rates for 2010/11 still assume that pre 1999 claims will be fully funded by 2014; however legislation will be introduced to push this date back to 2019. The impact of the legislative changes and improvements in ACC's claims management will be to reduce the proposed rates.

Good news for ACCPP

The good news for employers in the ACCPP is threefold:

1. The reduction in the stop loss rates: The decrease will vary depending on the level of cover and also the High Cost Claims Cover taken by the employer.
2. The standard levy now reflects the full ongoing costs of injury claims. So an employer comparing their experience to the alternative of paying the standard levy will see a significant improvement due to the 50% plus increase in the standard levy rates. We expect there will be employers who decide to join the ACCPP as a result of the rate increases.
3. The Residual Claims Account Levy is expected to decrease by around 36% with the pending decision to change the funding date to 2019, but it will be payable for an extra 5 years.

Content

In this newsletter we detail the proposed levy rates for 2010/11 and look at the reasons behind the major rate increases. Information is provided on the future projected rates for the Work, Residual, Earners' and Motor Vehicle Accounts, making comparisons with the previous year's projections and looking in detail at the funding position of each account.

We have also included details of the ACCPP and give an example of the rates for stop loss and High Claims Cost Cover.

The newsletter is based on the information in the Consultative Documents published on 14th October and those of September 2008.

Consultation closure deadline

Consultation closes at 5 pm on 10 November 2009. Submissions need to be made by then.

We would be pleased to assist with submissions.

2. Proposed rates details

The table below summarises the proposed levy rates for the Combined Work, Earners' and Motor Vehicle Accounts based on both funding dates.

Work Account levy rates ($ per $100 liable earnings)

	Current	Residual	Combined
2009/10 Actual	0.75	0.56	1.31
2010/11 Proposed[1]	1.18	0.71	1.89
Increase	57%	27%	44%
2010/11 Proposed[2]	1.11	0.36	1.47
Increase	48%	-36%	12%

Earners' Account levy rates ($ per $100 liable earnings)

	Current	Residual	Combined
2009/10 Actual	1.61	0.09	1.70
2010/11 Proposed[1]	2.60	0.20	2.80
Increase	62%	120%	65%
2010/11 Proposed[2]	n.a	n.a	2.45
Increase			44%

Motor Account levy rates ($ per vehicle)

	Current	Residual	Combined
2009/10 Actual	$119	$168	$287
2010/11 Proposed[1]	$205	$213	$417
Increase	72%	27%	45%
2010/11 Proposed[2]	n.a	n.a	$317
Increase			11%

1 Based on 2014 fully funded deadline.
2 Based on 2019 fully funded deadline.

3. Increases in the cost of claims

The table on the next page shows the increases in the projected cost of claims for the three accounts for the 2010/11 year over the current 2009/10 year.

Account	2009/10 $m	Levy Year 2010/11 $m	Increase %
Work	576	597	3.6%
Earners'	1,318	1,383	4.9%
Motor	498	531	6.6%

The interesting aspect of the table is that the increases are relatively minor, contrary to the proposed levy rate increases.

To explore this further, we compared the change in the projected cost of claims for the 2008/09 year (taken from the September 2008 Consultation Documents) with the current projected cost of claims for 2010/11, i.e. we are looking at the increase over a two year period.

Account	2008/09 $m	Levy Year 2010/11 $m	Increase %
Work	520	597	14.8%
Earners'	953	1,383	45.1%
Motor	397	531	33.8%

The two-year comparison shows a very different picture, particularly for the Earners' and Motor Accounts, where the increases in the projected cost of claims of 45.1% and 33.8% respectively are significant. We explain the factors behind the rise in section 5.

The table below compares the components of the levies for the projected 2009/10 claims in the Consultative Documents of September 2008 and October 2009 with the projected 2010/11 costs in the October 2009 document. To illustrate, the increase in the cost of the claims for 2010/11 compared to those projected in September 2008 for the 2009/10 year is 4.8%.

Work Account levy rates ($ per $100 liable earnings)

Projected costs	CD 08 09/10	09/10	CD 09 10/11	Increase
Cost of claims	0.83	0.84	0.87	4.8%
Scheme costs	0.16	0.18	0.19	18.8%
Funding adj.	-0.27	-0.31	0.08	
WSMP	0.03	0.04	0.04	33.3%
Total	0.75	0.75	1.18	57.3%

Earners' Account levy rates ($ per $100 liable earnings)

Projected costs	CD 08 09/10	09/10	CD 09 10/11	Increase
Cost of claims	1.41	1.51	1.58	12.1%
Scheme costs	0.27	0.37	0.40	48.1%
Funding adj.	-0.25	-0.45	0.34	
Total	1.43	1.43	2.32	62.2%

Motor Account levy rates ($, post 1999 claims, ex GST)

Projected costs	CD 08 09/10	09/10	CD 09 10/11	Increase
Cost of claims	139	158	167	20.1%
Scheme costs	15	18	20	33.3%
Funding adj.	-35	-57	17	
Total	119	119	204	71.4%

The costs shown are all in respect of post 1999 injuries.

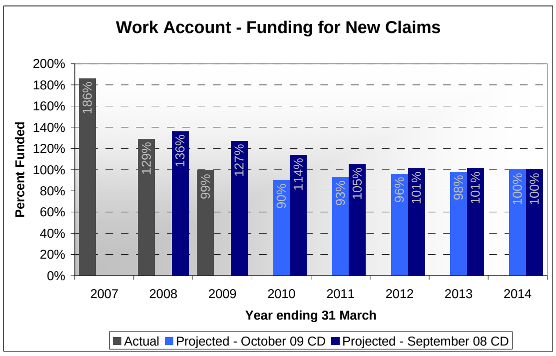
The reason why the proposed rates have risen so much is therefore primarily due to the change in the funding adjustment (or reserves). The tables also show the levy rates charged for the 2009/10 year were less than the projected cost of the claims as at September 2008.

The Work Account started the year with positive reserves; however the Earners' and the Motor Accounts did not. ACC was therefore budgeting on a run down of the reserves and a general weakening of its finances. We explore this further in the next section.

4. Account Reserves

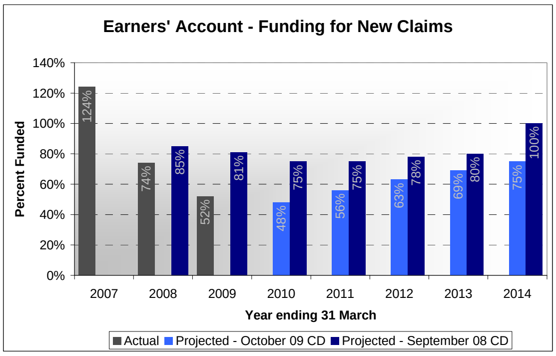
The next three charts show the percentage of assets held over the value of the projected claims costs for post 1999 injuries.

Work Account



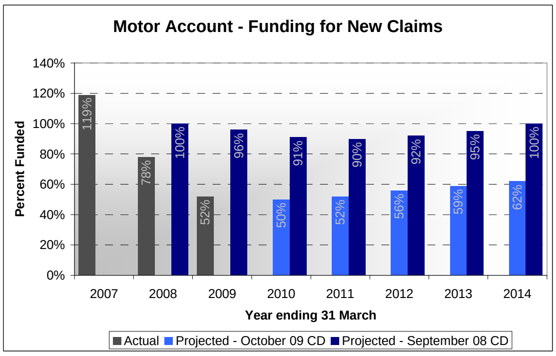
The change in the Work Account's finances since March 2007 is dramatic. At that time the reserves were 186% of the projected cost of claims. As at March 2009 that had reduced to 99% compared to the 127% projected in the September 2008 Consultation Document. As the current (2009/10) levy is insufficient to meet the cost of the current claims, it is projected that the reserves will reduce further to 90% at March 2010.

Earners' Account



The deterioration in the Earners' Account as at March 2009 can be seen when we compare the September 2008 projected funding level of 81% with the actual level of 52%, which is projected to fall further to 48% at March. Back in March 2007 the value of the assets was 124% of the value of the claim costs.

Motor Account



We see the same picture in the Motor Account with the September 2008 projected funding position at March 2009 of 96% becoming an actual 52%, a huge reduction.

We look at the reasons for the large reductions in the reserves in section 5.

Pre 1999 funding positions

While there is only a separate account for the work accidents (the Residual Claims Account), both the Earners' and Motor Accounts keep a record of the cost of the pre-1999 injuries. Their funding position has not deteriorated as badly as for the post-1999 injury accounts. Details are shown for all three accounts in Appendix A.

5. Why have the reserves reduced by so much?

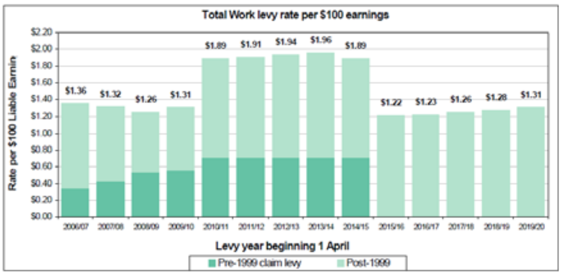
ACC is a so called "long tail" business and some claims require long term care and major ongoing claims costs. The reason for the deterioration in the finances is that the actuaries have determined that previous assumptions made for future claims costs were too optimistic and are now no longer consistent with ACC's actual experience. Accordingly we see that the duration of the longer term claims has increased, and the weighted average term to settle claims has moved from 11 years, 1 month in June 2008 to 12 years, 11 months as at June 2009, a 16% increase. At the same time, the provisions made for the cost of social rehabilitation benefits for both serious and non serious injuries, hospital rehabilitation and medical costs have all jumped for the June 2009 valuation.

The investment climate has impacted ACC to a lesser extent than might have been expected. Over the last two years, ACC has budgeted for investment income of $1.578 billion while it earned $357 million. The difference, while a substantial $1.2 billion, would not have made a huge impact on the level of the current reserves.

6. Work Account Projected rates to 2019/20

Current projection

The chart below, taken from the October 2009 Consultative Document, shows the projected levy rates through to 2019/20.



The key points from the chart are:

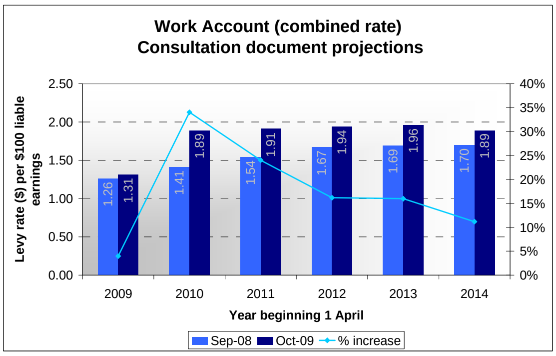
- The levy rate stays at a high level till 2014/15 when the residual claims are due to be fully funded according to the current legislative position.
- Ignoring the residual claims, the levy rates are reasonably stable, showing small consistent increases from 2015/16 onwards.

The chart illustrates the impact of the new funding policy announced by ACC, which will look to fund any surpluses and deficits over a 10 year period in order to smooth and stabilise the levy rates charged. A further important change is the decision that, when an account is in deficit, the next year's levy shall not be less than the projected claims costs.

Looking back, ACC chose to dilute the impact of the cost of the hearing loss claims by reducing the levy rate for new claims in order to balance out the combined levy, which would have otherwise significantly increased due to the sizeable increase in the RCA levy. With the benefit of hindsight, it might have been better to spread the value of the surplus out over a longer period and focus less on deriving a flat combined levy rate through to 2014.

Comparison with the 2008 projections

In the table below we have illustrated how the projected Combined Work rates have increased compared to those projected in the September 2008 Consultative Document.



The current projected levy rates are, with the exception of those for the year beginning April 2014 over 15% higher than those projected in September 2008.

The prime reason for the increase is the rise in costs in the Residual Claims Account. The proposed levy rate for pre-1999 claims is due to rise from 56 cents to 71 cents per $100 liable earnings. The reasons for the increase are the same as discussed in section 5.

Charts showing the projected levy rates for the Earners' and Motor Accounts and comparisons with those projected in September 2008 are included in Appendix B.

7. Partnership Programme

There have been no changes to the structure of the ACCPP. The table below summarises the change in the rates applying.

Item		2009/10	2010/11
Admin fee		4.0	2.3
Primary Health Costs		1.5	1.5
Bulk Funded Health Costs		4.0	2.8
PDP discounts	1 year	51.5%	49.8%
	2 year	58.8%	58.6%
Stoploss limits (FSCP)	Minimum	211%	110%
	Maximum	330%	173%
HCCC (FSCP)	Minimum		$0.25m
	Maximum		$2.50m

The stoploss rates have been substantially reduced for the 2010/11 year.

The table below compares the stoploss and HCCC rates for 2009/10 with the proposed 2010/11 rates. The figures are based on an employer with liable earnings of $200m, 15% WSMP discount and $0.74 standard levy for 2009/10.

	HCCC Cover			
Premium	**nil**	**$250k**	**$1m**	**$2.5m**
2009/10				
Stoploss	142,144	1,992	71,072	122,550
HCCC	0	366,652	82,530	19,428
Total	142,144	368,644	153,602	141,978
2010/11				
Stoploss	35,490	70,689	28,363	31,127
HCCC	0	165,961	28,363	11,490
Total	35,490	236,650	56,726	42,617
% change	-75%	-36%	-63%	-70%

8. Reduction in levy rates due to change in funding date to 2019

In section 2 we illustrated how the increase in the levy rates will be reduced by changing the funding date for pre 1999 injury claims from 2014 to 2019. The estimates also include allowance for the following:

- A reduction in the duration of the long term claims
- Changing the way ACC purchases physiotherapy
- Reviewing the contribution ACC makes to non-injury related hearing loss claims.

9. Possible changes to benefit entitlements

While any benefit changes have yet to be introduced to the House, the following are among the proposals being considered:

- Currently claimants have to be able to work for 35 hours a week before they can be vocationally assessed and their benefit cease. It is proposed to change this to 30 hours a week.
- The weekly compensation income levels for part time and casual workers will revert back to being based on their income over the last 12 months rather than what they were earning at the time of the accident.
- The threshold for hearing loss claims will be increased from the current 5% level.

10. Should the Scheme continue to be fully funded?

The large increases in the proposed 2010/11 levy rates have sparked discussion about whether the Scheme should continue to be fully funded. Of course, the advantage of a fully funded scheme is that the true cost of the benefits the Scheme is providing is known. Reverting to a "pay as you go" system runs the risk of cost blow-outs in the future as was the case in the 1980's and early 1990's and all the hard work to restore the finances of the Scheme from the mid 1990's to 3/4 years ago would be lost. The question really could be rephrased as is it reasonable for the current generation to enjoy benefit levels which future generations will have to pay for? As part of the current review it would be useful to know how much each benefit cost and then decisions on what benefits to provide can be made on an informed basis.

11. General cost pressures

It is important to note that there are cost pressures on the Scheme which will inevitably push up the rates on a year by year basis.

The workforce is getting older, medical advances keep seriously ill people alive longer and the cost of treatment rises at more than the CPI rate. Further evidence of this is apparent from Southern Cross' annual report which notes the rising cost of medical procedures impacting on its financial position.

These are the same cost pressures as exist in the public health system.

The only way to reduce these inevitable increases will be to reduce the current entitlement levels.

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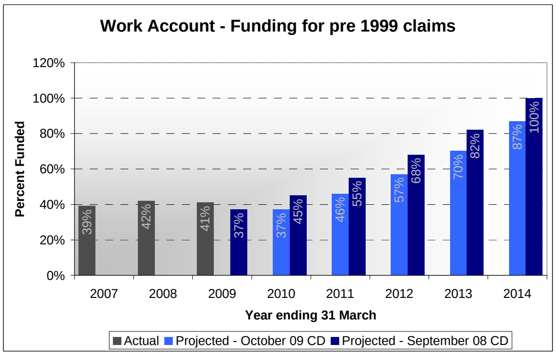
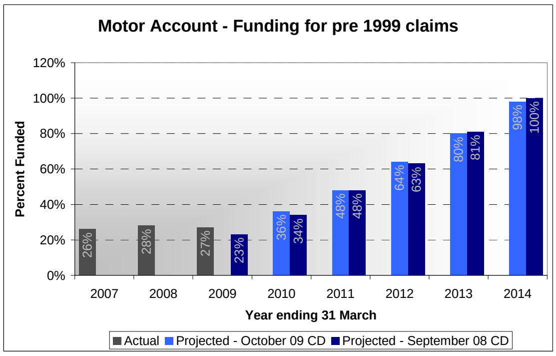
Appendix A

Pre 1999 Injuries – Account funding positions

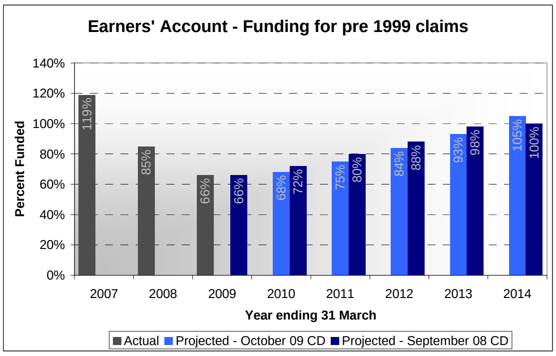
Residual Claims Account



Motor Account



Earners' Account

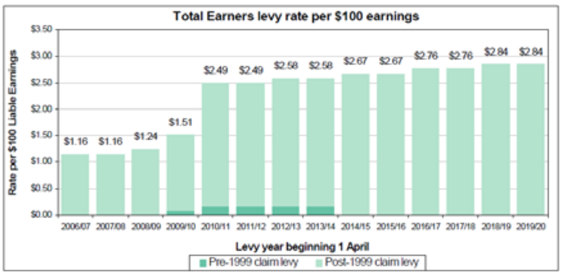


Note that the positions shown for the Earners and Motor Vehicle Accounts are internal to the actual accounts.

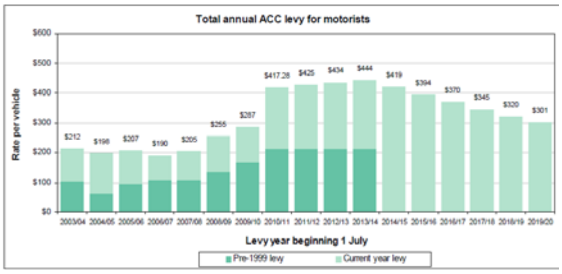
Appendix B

Projected rates to 2019/20

Earners' Account

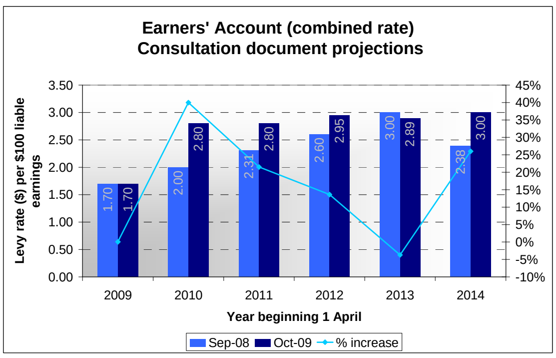


Motor Account

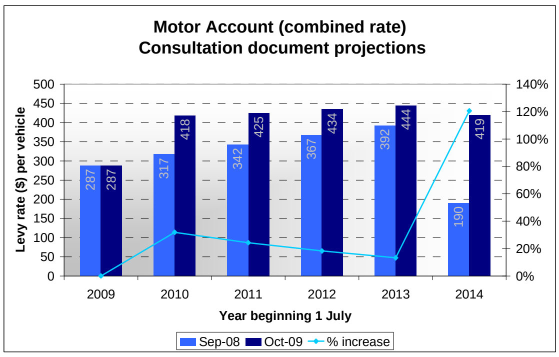


Comparison of current projected rates with those in the September 2008 Consultative Document

Earners' Account



Motor Account



The current projected rates are, with the exception of those for the year beginning April 2014, over 15% higher than those projected in September 2008.