

CABINET SOCIAL POLICY COMMITTEE

Process for investigating the introduction of competition to the ACC Work Account

Proposal

- 1 This paper advises that I have instructed the Department of Labour to investigate the introduction of competition to the ACC Work Account. I wish the Treasury and the Department of the Prime Minister and Cabinet to be involved in the work, with a view to Cabinet making decisions on this matter in late July 2010.

Executive summary

- 2 The scale of the problems I encountered when I became Minister for ACC meant that immediate cost containment matters took priority in this portfolio. ACC will report a significantly improved bottom line for 2009/10. Nevertheless there are still concerns that the Crown's finances are fully exposed to the risks of ACC's Accounts.
- 3 It is therefore time to consider the commitment we made pre-election to investigate opening the ACC Work Account up to competition. Although the interim report from the Stocktake of ACC Accounts advised that competition in the Earners' and Motor Vehicle Accounts is also meritorious and feasible, that path may be difficult to implement. My intention, therefore, is to focus on the work required on introducing competition in the Work Account. The post-1999 portion of the Work Account is the only levied Account that is currently solvent.
- 4 In addition to advice being received from the Stocktake of ACC Accounts, officials will need to undertake work to ensure Ministers are fully informed before taking final decisions at the end of July 2010 on the type and form of competition in the Work Account. The package of work proposed is set out in paragraph 18.
- 5 Implementation work on market design could be significant, because policy settings are different now than when competition was last introduced. We will need to make a series of decisions as work progresses. I have asked officials to work to a timeline that would see legislation introduced before the end of 2010, and be enacted by May 2011.

Background

- 6 Our pre-election manifesto stated that we would investigate opening the ACC Work Account to competition, after full evaluation of the benefits. The scale of the problems I encountered in ACC when we first took office meant that immediate cost containment had to take priority. The issue of competition was therefore included in the terms of reference for the Stocktake of ACC Accounts. Nevertheless there are still concerns that the Crown's finances are fully exposed to the risks of ACC's Accounts.
- 7 It is therefore time to consider the commitment we made pre-election to investigate opening the ACC Work Account up to competition. In mid-April I received the interim report from the Stocktake of ACC Accounts, which sets out the merits and feasibility of introducing competitive delivery of accident compensation services in

New Zealand. The Stocktake found that competition would be feasible and of merit in three Accounts, and advised Ministers to seek further detailed advice before taking decisions on the policy direction.

- 8 Although the Stocktake advised that competition in the Earners' and Motor Vehicle Accounts is also meritorious and feasible, that path may be difficult to implement and would need to be done in stages. The post-1999 portion of the Work Account is the only levied Account that is currently solvent.
- 9 The interim report is part of the advice we will receive to inform our decision making. I am still awaiting the final report from the Stocktake of ACC Accounts, due at the end of June. That report will cover the remaining terms of reference, which relate to wider issues in the Scheme and potential solutions.

Context

- 10 The issues facing the accident compensation scheme include:
 - the financial sustainability of the scheme as a fair, efficient, 24/7 no fault insurance scheme for all New Zealanders
 - issues facing the Crown as owner, such as: the financial risk of having all ACC's Accounts on the Crown balance sheet; the Crown's mixed roles as shareholder in ACC, funder of the Non-Earners' Account, levy setter, and policy maker on the nature of entitlements
 - ensuring steady, stable, and efficient levy rates.
- 11 Introducing competition in the Work Account can potentially help with:
 - reducing future financial risks to the Crown
 - efficiency of contracts – by companies offering insurance packages to employers (integrating companies' accident insurance with their health insurance schemes), and instigating innovative practices
 - stronger pricing signals being provided to the market
 - exposing ACC to competitive pressure and benchmarking
 - Innovation in claims management and strengthened ability to negotiate or develop new approaches to health sector service provision, thereby improving rehabilitation rates, controlling costs, and reducing future levy increases
 - accelerating the use of experience rating for employers, groups or individuals, and offering more self insurance and risk sharing options
 - improved health and safety and injury prevention initiatives.
- 12 Competition offers dynamic efficiency gains over the medium and long term, but will not deal with immediate cost pressures throughout the wider Scheme. There may also be wider economic impacts that are as yet unexplored, and potential impacts on the fabric of the wider Scheme. Claim trends in the Work Account have been on a better path than those in other Accounts.

- 13 Even if the Work Account were fully open to competition, because historic claims would remain, ACC's net deficit (forecast to be \$10.5 billion at 30 June 2010) would stay on the Crown accounts.
- 14 I have also assumed that a market in the Work Account would commence with no change to existing benefits and entitlements, but the level of benefits and entitlements provided under the wider accident compensation scheme may need to be addressed in the future.

Work required to assist decisions in late July

- 15 As noted earlier, I am expecting further advice from the Stocktake at the end of June. I propose that in the meantime officials undertake additional work to support the advice I have received to date, to better inform the decisions to be taken by Cabinet at the end of July.
- 16 I propose that the Department of Labour leads work on the issues set out below, in conjunction with the Treasury and in consultation with the Department of the Prime Minister and Cabinet. It is likely that the Department of Labour will engage external consultants to assist with this. I do not intend that officials duplicate the work being done in the Stocktake.
- 17 My aim is incremental, rather than wholesale, change. Keeping ACC in the market would allow a smooth transition. It will bring competitive pressure to bear on the Corporation to achieve better performance, without large scale disruption to claimants and employers. The work to be undertaken will better inform decisions on exactly how the Corporation would operate.
- 18 The package of work required would include the following:

A: Type and form of competition:

 - exploration of options for the introduction of competition into the Work Account, including having a public and private mix of providers (hybrid scheme) such as exist in Australia
 - Institutional arrangements to ensure the competitive part of ACC is financially transparent and operates on a level playing field with private companies
 - Investigating options to ensure all-size employers have choice, including self insurance options and options for claims management and other services, including opt-in or opt-out arrangements
 - giving Ministers a sense of indicative costs, risks, and benefits of those options relative to the existing arrangements
 - understanding how the changes will impact on particular sectors/ industries/ groups in society, and their broader economic impact
 - management of the current assets and liabilities in the Work Account, that is, options for managing the existing portfolio of claims (by ACC and/or market providers)
 - the conditions and constraints under which private firms would consider entry to, or participation in, this market, and how to avoid 'cherry picking'. There will be a need to engage with insurers on these issues at a later stage.

- consideration of how residual risk should be managed (the response if any private scheme were to fall over; for example, whether ACC or other insurers would assume these responsibilities) and the possible role of government in such a scenario.

B: Impact on wider health and welfare sectors

There is a need to actively examine the risk that costs could be transferred from private insurers to public services. If this means that costs fall where they rightly should be, this is not in itself a problem. But Insurers (including ACC) have an incentive to move work injury claimants into the health and welfare sectors with a potential impact on core Crown costs. Work should therefore be undertaken to assess options for off-setting any inappropriate cost shifting.

Timing

- 19 The Stocktake will present its final report at the end of June. Advice to Cabinet on the investigation into introducing competition in the Work Account will be delivered at the end of July. I have asked officials to assume that legislation is introduced by the end of 2010, with a view to it being passed by May 2011.

Consultation

- 20 The Treasury has been consulted on this paper and DPMC has been informed.

Treasury comment

- 21 "ACC continuing to underwrite future workplace injury risks would simplify implementation, would avoid any perception of favouring private sector providers and would achieve some gains from contestable claims management. However, to achieve genuine competition in underwriting injury risks it would be necessary to significantly constrain ACC's ability to cross-subsidise the contestable components of its operations and to ensure that ACC faces the equivalent of the cost of capital that new entrants would need to meet. This could involve significant new expenditure for the Crown.
- 22 Treasury recommends that Ministers note that allowing ACC, as it is currently structured, to compete for future Work Account claims would mean other firms would be less likely to enter the market.
- 23 Other options that are not considered in the paper are:
- close the Work Account to new claims from a specified date, with every firm either selecting an underwriter or being allocated to one of a list of default underwriters
 - alternative structures for the State to participate in the market for underwriting future Work Account claims, such as establishing a new State-Owned Enterprise. This would involve the extra cost of capitalising, establishing, and monitoring the new entity but may be necessary to achieve a level playing field necessary for firms to enter the market.
 - competition in the earners and motor vehicle segments as well as workplace injury. The gains from competition would be larger if its scope is wider.
- 24 Treasury considers that further developing these other options at this stage would enable Ministers' decision point in July to select the option which strikes the best balance between the economic gains and the implementation risks."

Financial implications

- 25 The Department of Labour has received money in the Budget for policy advice. There are no direct costs arising from the recommendations in this paper, but there will be financial implications from decisions to be made in July, including the cost of funding a regulatory regime. These will be discussed at that time.

Human rights

- 26 There are no human rights issues arising from the proposals in this paper.

Legislative implications

- 27 There are no legislative implications arising from the proposals in this paper.

Gender and disability implications

- 28 There are no gender or disability implications arising from the proposals in this paper.

Publicity

- 29 To date I have not generally released Stocktake documents, and consider no information beyond the purely factual should be released until after decisions have been taken in July. I note that Ministers will require a public communications strategy after decisions have been made in July.

Recommendations

- 30 I recommend that Cabinet Social Policy Committee:
- 1 **note** that while awaiting the final report from the Stocktake of ACC Accounts at the end of June 2010, the Minister for ACC intends to direct Department of Labour officials to undertake work investigating the introduction of competition in the ACC Work Account, on the basis that ACC remains as a competitive provider;
 - 2 **note** that the Minister for ACC considers that this further work is necessary to more fully inform Cabinet decisions at the end of July 2010 on introducing competition in the Work Account;
 - 3 **note** that the Minister for ACC considers ACC should remain as a competitor when competition is introduced in the Work Account;
 - 4 **note** that Treasury considers that allowing ACC, as it is currently structured, to compete for future Work Account claims would mean other firms would be less likely to enter the market;
 - 5 **note** the assumption that a market in the Work Account would commence with no change to existing benefits and entitlements, but the level of benefits and entitlements provided under the wider accident compensation scheme may need to be addressed in the future;
 - 6 **direct** officials from the Department of Labour (lead agency), in conjunction with Treasury and in consultation with the Department of the Prime Minister and Cabinet, to undertake the following work during June and July 2010:

- exploration of options for the introduction of competition into the Work Account, including having a public and private mix of providers (hybrid scheme) such as exist in Australia
 - Institutional arrangements to ensure the competitive part of ACC is financially transparent and operates on a level playing field with private companies
 - Investigating options to ensure all-size employers have choice, such as self insurance options and options for claims management and other services, including opt-in or opt-out arrangements
 - giving Ministers a sense of indicative costs, risks, and benefits of those options relative to the existing arrangements
 - understanding how the changes will impact on particular sectors/ industries/ groups in society, and their broader economic impact
 - management of the current assets and liabilities in the Work Account, that is, options for managing the existing portfolio of claims (by ACC and/or market providers)
 - the conditions and constraints under which private firms would consider entry to, or participation in, this market, and how to avoid 'cherry picking'. There will be a need to engage with insurers on these issues at a later stage.
 - consideration of how residual risk should be managed (the response if any private scheme were to fall over; for example, whether ACC or other insurers would assume these responsibilities) and the possible role of government in such a scenario
 - assessment of options to off-set any inappropriate cost shifting to the wider health and disability sectors;
- 7 **note** that officials will engage with key officials at the Treasury, Department of the Prime Minister and Cabinet, Ministry of Health, and ACC, as part of the work set out in recommendation 6;
- 8 **invite** the Minister for ACC to report back to Cabinet Social Policy Committee at the end of July 2010 with advice following the work in recommendation 6 and cognisant of the advice in the final report from the Stocktake, with the aim of supporting decisions on introducing competition to the ACC Work Account.


 Hon. Dr Nick Smith
 Minister for ACC

26 / 5 / 2010