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High level review of the New South Wales Bar Association, Law Society of NSW and Australian Lawyers Alliance submission, to the NSW CTP Scheme Review, of an alternative benefit design proposal

The Motor Accidents Authority (MAA) has requested Ernst & Young (EY) to perform a high level review of the New South Wales Bar Association, Law Society of NSW and Australian Lawyers Alliance's proposal for changes to the NSW CTP scheme (Lawyer's proposal) in relation to expanding ANF coverage from \$5,000 to \$20,000, combined with changes in legal cost restrictions.

For our high level review we have:

1. Performed a high level review of the Lawyer's proposal costing "The New South Wales Bar Association, The Law Society of NSW, and, Australian Lawyers Alliance NSW CTP Costing 4 April 2013" (Deloitte's costing or Deloitte's report) which have been performed by Deloitte Actuaries and Consultants (Deloitte)
2. Performed a high level independent costing of the Lawyer's proposal.

This document sets out the findings of our review.

There is generally a lack of detail as to how the Lawyer's proposal will operate which could mean there may be other costs and effects associated with the proposed changes that have practical implementation issues that we have not identified. The Lawyer's proposal in summary is:

- ▶ To expand ANF coverage from \$5,000 to \$20,000, combined with change in legal costs restrictions
- ▶ Costs in small claims
 - ▶ Remove party/party legal costs for settlements or awards under \$20,000
 - ▶ Restrict recovery of solicitor/client legal fees to a maximum of \$2,000 for any settlement or award under \$20,000.

1. General comments on Deloitte's costing

We have been provided with Deloitte's report which sets out details of their costing including the data used, methodology, assumptions and results. Our general comments on Deloitte's report are:

- ▶ Deloitte's estimated savings costed from each element of the Lawyer's proposal includes the impact on claims handling costs (where appropriate) and GST. We have adopted the same approach
- ▶ Deloitte recognise that their work is limited by the information and data they have access to, specifically:
 - ▶ For the NSW CTP scheme they only have access to publicly available data and information and as such do not have access to individual claims data the MAA collects from insurers. This is a very significant limitation on their work and their results
- ▶ Due to the above point there is a very large degree of uncertainty in Deloitte's costing and their results could show substantial differences compared to the same analysis conducted by an actuary with access to individual claims data

- ▶ It is not clear if there is a recognition in the Deloitte costing for the erosion over time of the expected savings of the Lawyer's proposal.

2. EY high level independent costing of the Lawyer's proposal

We performed a high level independent costing of the Lawyer's proposal using NSW scheme data and claims data from the Transport Accident Scheme (TAC) as a comparative to the Deloitte costing which used public information. Similar to Deloitte, we have estimated the potential savings resulting from the benefit changes. TAC claims data was used to estimate the average claims size of ANFs if the maximum ANF was increased to \$20,000.

We have assessed the impact of this change in three parts:

- ▶ At-fault ANFs – we have assumed that this change will result in more at-fault ANFs and at a higher average ANF claim size and the actual cost will depend on how many at-fault ANFs are received

We have estimated the additional number of ANFs by comparing the propensity to claim for at-fault ANFs in the current NSW scheme and the propensity to claim for at-fault claims in the TAC scheme. As the impact of this change is uncertain we have derived a low and high estimate of the premium increase arising from this change. We have estimated the average size of these ANFs based on the cost of at-fault claims in the TAC scheme.

- ▶ Not at-fault ANFs and full claims – we have used the experience of the increase in the ANF maximum from \$500 to \$5,000 as an indication of the possible cost impact. When the ANF maximum was increased to \$5,000 there was no reduction in the cost of the Scheme, instead the cost increased mainly due to an increase in the number of full claims. We have assumed no reduction or increase in costs if the ANF maximum is increased to \$20,000

It is not clear if the higher ANF limit will reduce the conversion rate to full claim. Despite the substantial increase in ANFs when the \$5,000 limit was introduced there has not been a material offsetting reduction in the conversion of ANFs to full claims.

- ▶ The restriction on legal costs to a maximum of \$2,000 for claims less than \$20,000 will not result in material, if any, savings in the scheme premium. It is actually possible that this change may lead to an increase in the current scheme premium. Our logic is as follows:
 - ▶ Claims less than \$20,000 account for less than 5% of total scheme claims costs and the legal costs relating to these claims are an even smaller proportion of total scheme claims costs
 - ▶ Furthermore, dollar thresholds in any benefit design suffer from bracket creep. The \$20,000 threshold may encourage claimants/lawyers to increase their settlement sizes from below \$20,000 to above \$20,000 to maximise legal fees; this will lead to an increase in the scheme premium.

Based on the above methodology we have derived the following estimates of the impact of the Lawyer's proposal (i.e. cost of claims plus claims handling expenses and GST) which is the same basis adopted by Deloitte.

Benefit changes		Deloitte estimate (expected scenario) per policy	EY estimate per policy	Comments on EY estimate
Expand ANF coverage and implement associated legal cost reductions	At-fault ANFs	-\$4	+\$10	A cost estimate of \$4 to \$16 assumes a propensity to claim of 20% to about 80% to 85% (it is currently around 10%). The midpoint is \$10 (propensity of about 50%). We expect the propensity to claim to increase, potentially significantly and could exceed 50%. Equally it may remain below 50%. If propensity to claim remains at 10% the estimated cost is \$2 per policy.
	Not at-fault ANFs and full claims		No saving \$0* (and possibly an increase)	As discussed above, the impact of this change is uncertain.

We estimate the Lawyer's proposal will increase scheme costs by around \$10 compared to Deloitte's estimated saving of \$4 per policy. There are risks that our estimates may underestimate the impact since:

- ▶ There is a significant risk that over time claims costs will increase as the change is likely to have an impact on the behaviour of lawyers and claimants. With a dollar threshold for legal costs (i.e. \$20,000), even if it is indexed, past scheme experience suggests settlements will be subject to bracket creep
- ▶ Whether a coincidence or not, when the ANF limit was increased to \$5,000 there was also a subsequent increase in the number of represented claims and in the number of full claims. In addition the number of not at-fault ANFs increased substantially. Consequently, based on the Scheme experience when the maximum ANF benefit was increased to \$5,000, there is a risk that increasing the ANF maximum to \$20,000 may result in an additional increase full claims and increased legal representation which would result in an increase in premiums.

3. Uncertainty

There is significant uncertainty associated with actuarial estimates. Estimates of future claims experience (claims numbers and payments) are always inherently uncertain because they depend on the outcome of future events which cannot be forecast precisely. Examples of claims experience that are particularly challenging to forecast include changes to social, economic and legal environments. Therefore, actual claims experience may emerge at levels higher or lower than the actuarial estimates. The level of uncertainty increases for actuarial estimates relating to scheme changes as there is little or no claims experience or other information available in relation to the expected experience under new scheme design.

There is also additional uncertainty due to the lack of detail in the Lawyer's proposal as noted above.

4. Reliance and limitations

We have only undertaken a high level review and our work has been completed within a tight timeframe which has limited the analysis we have been able to undertake.

Our findings are based on a high level review of the New South Wales Bar Association, Law Society of NSW and Australian Lawyers Alliance submission to the CTP Scheme Review. This included a report prepared by Deloitte estimating the impact of the proposed changes on the NSW CTP premium. We have not had the opportunity to discuss this submission and its details with any of these professional bodies or with Deloitte.

Our independent costing of the proposed changes was performed by using a high level methodology and the results should be seen as indicative only. Our results are based on historical claims experience which may not necessarily reflect future experience. Our costing results are uncertain. We have relied on the data provided by the MAA and TAC and have relied on it being accurate. We have not audited the data but have checked it at a high level for reasonableness.

We have performed the work assigned and have prepared this document in conformity with its intended utilisation by persons technically familiar with the areas addressed and for the stated purposes only. Judgements based on the data, methods and assumptions contained in the report document should be made only after studying the report in its entirety, as conclusions reached by a review of a section or sections on an isolated basis may be incorrect. EY staff are available to explain or amplify any matter presented herein.

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