Submission No 2

FIFTH REVIEW OF THE EXERCISE OF THE FUNCTIONS OF THE LIFETIME CARE AND SUPPORT AUTHORITY

Organisation: Suncorp Group

Date received: 29/10/2013

One Company
Many Brands

SUNCORP GROUP

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29 October 2013

The Hon David Clark MLC
Committee Chair
Standing Committee on Law and Justice
Parliament House
Macquarie Street
SYDNEY NSW 2000

By email: lawandjustice@parliament.nsw.gov.au

RE: THE EXERCISE OF THE FUNCTIONS OF THE MOTOR ACCIDENTS AUTHORITY - TWELFTH REVIEW AND THE EXERCISE OF THE FUNCTIONS OF THE LIFETIME CARE AND SUPPORT AUTHORITY - FIFTH REVIEW

I refer to the *Exercise of the Functions of the Motor Accidents Authority - Twelfth Review and the Exercise of the Functions of the Lifetime Care & Support Authority - Fifth Review.* Suncorp welcomes the opportunity to contribute to the Standing Committee on Law and Justice's (the Committee) review into these authorities.

The Suncorp Group

Suncorp Group Limited and its related bodies corporate and subsidiaries (collectively 'Suncorp') offer a range of financial products and services in banking (Suncorp Bank), general insurance, life insurance and superannuation (Suncorp Life) across Australia and New Zealand. Suncorp has over 15,000 employees and relationships with over nine million customers nationally.

Nationally, Suncorp is the largest personal injury insurer. This submission is made on behalf of the Suncorp Commercial Insurance division which operates Suncorp's statutory insurance products, including workers' compensation and compulsory third party (CTP) insurance. Suncorp has over 85 years of personal injury insurance experience, with our Suncorp, AAMI, GIO and Vero brands.

In respect to statutory classes of insurance, our community focused activity is centred on risk management, injury prevention, social participation and quality of care for those injured or with a disability.

We actively support Wheelchair Sports, which encourages individuals back into the community, improving rehabilitation and work capacity. Our long-term association with Youngcare has created housing and support for young people with disability in Queensland and New South Wales. We are also interacting with State Treasuries and providing information for consideration in regard to implementing a National Disability Insurance Scheme (NDIS) and the National Injury Insurance Scheme (NIIS).

Sharing of ideas is part of our collaborative approach, and as Australia's largest personal injury insurer, Suncorp is often asked to undertake research and comment on industrial and societal issues.

We also participate in wider industry matters through our involvement with the Insurance Council of Australia and relationships with scheme regulators and State Treasurers.

Terms of Reference

The Terms of Reference require a very broad inquiry into the exercise of functions of the Motor Accidents Authority (MAA); the Lifetime Care and Support Authority (LTCSA) and their advisory committees. It is noted that this review will be based in part on the 2010/2011; 2011/2012 and the 2012/2013 Annual Reports of the MAA[1] and LTCSA.[2] However the 2012/2013 reports are not due to be tabled in Parliament until the end of November.

The Parliamentary reports on the Eleventh Review of the Exercise of the Functions of the Motor Accidents Authority and the Motor Accidents Council and the Fourth Review of the Exercise of the Functions of the Lifetime Care & Support Authority and the Lifetime Care and Support Advisory Council were released in December 2011, with the Government response being released in July 2012.

In respect to that review, Suncorp relied on the insurance industry submission.[3] In addition, Suncorp lodged a separate submission[4] focussing on insurer profits, committing to reducing fatalities and personal injuries arising from motor vehicle accidents and CTP personal injury claims management. Our submissions are broadly consistent with the State Government's response to the review.

Economic Challenges

It is worthwhile to consider the role of Australia's accident compensation schemes, specifically the NSW CTP scheme and the LTCS in the context of ongoing economic challenges facing Australia. *The Intergenerational Report* 2010[5] identifies the ageing population as a key challenge over the next forty years.

Specifically, it is expected that the proportion of working age people is projected to fall, with only 2.7 people of working age to support each Australian aged 65 years and over by 2050 compared to 5 working aged people per aged person currently and 7.5 in 1970.[6]

With the ageing of the population reducing workforce participation, it will be crucial to enhance productivity growth to maintain our overall standard of living nationally. Whilst this is indeed a national issue, it is incumbent upon State Governments to work co-operatively in achieving enhanced

[1] NSW Government - *Motor Accidents Authority of NSW Annual report 2011-2012* - http://www.maa.nsw.gov.au/default.aspx?MenuID=136
[2] NSW Government – *Lifetime Care & Support Authority of NSW Annual Report 2011 – 2012* - http://www.lifetimecare.nsw.gov.au/Annual_Reports.aspx
[3] Submission No 7 – *Insurance Council of Australia* - http://www.parliament.nsw.gov.au/prod/parlment/committee.nsf/0/db86c5053dfe4993ca2578f4001b95d6/$FILE/Submission%200007.pdf
[4] Submission No 3 – *Suncorp* - http://www.parliament.nsw.gov.au/prod/parlment/committee.nsf/0/9fdd2a62eac26d0fca2578f4001b0869/$FILE/Submission%200003.pdf
[5] Australia to 2050: Future Challenges - http://archive.treasury.gov.au/igr/igr2010/report/pdf/IGR_2010.pdf
[6] Australia to 2050: Future Challenges - at page viii - http://archive.treasury.gov.au/igr/igr2010/report/pdf/IGR_2010.pdf

productivity growth by ensuring state based accident compensation schemes are designed to support those injured into early self determination both socially and economically.

The implications of workforce participation rates declining as the 'baby boomers move into retirement, without policy settings reducing the impact include:

- reducing tax revenue base;
- increasing demand on health and welfare services; and
- slowing of economic performance where productivity levels do not increase.

It is in this environment that the economic argument for disability reform is compelling.[7] An objective of a fully implemented NDIS and NIIS is to support individuals becoming self-sufficient both socially and economically. Supporting those who have a disability and have capacity[8] and their carers[9] into the workforce would assist in expanding the tax revenue base, which in turn should assist with productivity growth.

Accident compensation schemes designed to support individuals in becoming self-sufficient both socially and economically in a timely fashion after an injury is also crucial in arresting any decline in workforce participation rates. These considerations form the basis of our comments in this submission.

The NSW Lifetime Care and Support Scheme

Suncorp is of the view the LTCS scheme is working well to provide support to people who are catastrophically injured in motor vehicle accidents. The most recent annual report[10] does not reveal any significant issue of concern and indeed reports an improvement in the financial position from the previous reporting period.

It is noted with interest that over one third of adults in the LTCS scheme were drivers in vehicles at the time of the accident[11] and presumably a number of these participants would be considered 'at fault' drivers in a fault based scheme. In a fault based scheme, those catastrophically injured would have to rely on the public health system until such time their compensation claims were settled, which could take years. This is not conducive to early, appropriate medical and rehabilitation intervention to maximise functionality.

Suncorp maintains the view that like the NDIS, underwriting and claims management of catastrophic injuries is best placed outside the private insurance industry. The LTCS, like the NDIS has moved away from a lump sum entitlements system to a system that provides care and support on a needs

[7] Productivity Commission – Disability Care and Support, Volume 2, chapter 20 –The benefits of reform - http://www.pc.gov.au/__data/assets/pdf_file/0018/111294/23-disability-support-chapter20.pdf
[8] The Productivity Commission estimated that implementation of the NDIS, if combined with DSP reform to encourage greater participation, could lead to an increase in employment of people with a disability of some 220,000 by 2050: source: *Future Growth in DSP receipt – not all bad news* - http://parlinfo.aph.gov.au/parlInfo/search/display/display.w3p;query=Id%3A%22library%2Fprspub%2F2783695%22
[9]Of the 2.6 million carers, almost 2 million are of workforce age: Source: Australian Bureau of Statistics 2006.
[10] NSW Government – *Lifetime Care & Support Authority of NSW Annual Report 2011 – 2012* - http://www.lifetimecare.nsw.gov.au/Annual_Reports.aspx
[11] NSW Government – *Lifetime Care & Support Authority of NSW Annual Report 2011 – 2012* – at page 13 http://www.lifetimecare.nsw.gov.au/Annual_Reports.aspx

basis, only. In this operating environment, the Government is best placed to allow a long-term, holistic approach in respect of the rehabilitation and care of people with catastrophic disabilities and a centralised scheme underwritten by Government would deliver the best outcome.

The LTCS scheme is aligned with this view, and aligned with the key objectives of the NIIS. There is an expectation that the NIIS will be fully implemented nationally by 2018. The LTCS scheme is a very good model to expand and implement nationally, as the NIIS.

The NSW CTP Scheme

In respect to non catastrophic injuries, Suncorp is of the view that the CTP scheme benefits from private underwriting by licensed private insurers. Privatisation drives market outcomes through:

- separation of interest between the regulator, the Government and the regulated activity, and
- competition in capital markets tending to make private companies more focussed on shareholder value creation.

The net economic benefit to Government in privatising accident compensation schemes outside of the LTCS scheme or the NIIS include:

- keeping systemic and investment risks away from Government and placed onto private insurers and claims agents;
- keeping scheme liabilities away from Government and placed onto private insurers, which protects public funds against adverse market movements and protects Government credit rating; and
- improving the Government's capital management strategy by unlocking capital to re-allocate to economic growth initiatives.

In economically challenging times (such as the relatively recent Global Financial Crises and the European Debt Crisis) investment income is impacted negatively by low bond yields. This represents a real challenge for 'long tail' accident compensation schemes where investment income is reduced due to lower bond yields creating a shortfall in premiums.

Insurers in privately underwritten schemes are prudentially supervised by APRA to ensure sufficient capital adequacy to meet outstanding liabilities. The benefit for Government is the protection of balance sheets and credit ratings. This leaves Government in a position to focus on the core role of scheme regulation, without the need to underwrite and manage schemes.

As the CTP regulator, the MAA is perfectly placed to focus on CTP regulation, in times of

- increasing upward pressure on premiums, in light of current low investment yields and developing scheme design; and
- the need to improve scheme design to enhance support for individuals in becoming self-sufficient both socially and economically in a timely fashion after an injury.

NSW CTP Reform

Suncorp supports reform of the CTP scheme in NSW. Indeed without reform Green slip prices are due to rise. Suncorp submits that CTP reforms should be based on the following principles:

- optimal health outcomes for those who suffer injuries as a result of a motor vehicle accident;
- improved scheme efficiency to deliver a greater proportion of collected premiums to those injured;
- improved affordability of green slips;
- scheme structure that supports premium stabilisation;
- universal cover; and
- consistency of administration, benefits and dispute resolution with the NDIS and the NIIS.

Scheme Design Principles

Suncorp considers the three key aims for an effective personal injury insurance scheme are fairness, outcomes and affordability. There are six guiding principles which define an effective personal injury insurance scheme across all statutory classes. These principles guide our input into scheme design and improvement with each of our regulators and governments nationally and guide our input into this current review.

- *Social Outcomes* - The scheme's emphasis needs to be on the individual's health and social outcomes (wellbeing), with a reduced focus on compensation payments. The ideal scheme should seek to support individuals in becoming self-sufficient both socially and economically.

- *Sustainability* - The scheme should be self-sustaining and operated with sound pricing and capital management practices so that liabilities remain fully funded. The Suncorp paper titled "*How international financial markets impact personal injury insurance*" provides an extensive discussion of the impact that bond yields have on the premium rate and capital requirements of insuring in a long-tail scheme.[12]

- *Competition* – Private competition is a key driver of innovation and can lead to improvements in pricing, claims management and health outcomes for claimants. The advantages of scheme privatisation are discussed more extensively in the white paper produced by Suncorp, titled "*Reflections on underwriting options for personal injury insurance*."[13]

- *Defined and Controlled Benefits* - Benefits that are clearly defined by realistic timeframes, dollar amounts, caps and limits reduce ambiguity and inconsistent outcomes. This reduces complaints, disputes, litigation and volatility which would otherwise have adverse impacts on the scheme's affordability and financial viability.

- *National Consistency* – Progressing national harmonisation of personal injury schemes will see fair and consistent benefits for all individuals, regardless of state of residence and/or

[12] See Appendix A
[13] See Appendix B

location of the accident. Employers, consumers and insurers will also gain benefits from a consistent approach across jurisdictions.

- *Dispute Resolution* – All decisions should be reviewable through a robust and cost effective dispute resolution system. It is important that all participants of the scheme, particularly claimants, have the opportunity to have their cases independently reviewed in a low cost, expedient and objective manner.

Suncorp contends that a scheme designed with these principles in mind will achieve the best possible outcome for its participants and claimants. These principles form the basis of our comments on key areas identified below and Suncorp is of the view the MAA should consider economic modelling of the proposed reforms identified.

Universal & First Party Cover

Suncorp supports the introduction of universal and first party cover in personal injury insurance schemes in all Australian jurisdictions. Schemes that offer universal and first party cover ensure that all Australians receive appropriate medical and income support in a timely fashion after sustaining an injury in a motor vehicle accident.

The design of any compulsory personal injury insurance scheme must aim to get the most effective balance between social outcomes for the injured party, affordability for the consumer and ongoing scheme sustainability. With this in mind, designing a scheme that provides both universal and first party cover needs to strike the right balance, which is a difficult task shaped by the diverse needs of the schemes stakeholders.

Suncorp considers an ideal scheme design would include:

- a range of defined benefits varying according to severity and impact of injury and fault status of the injured party;
- a focus on health and wellbeing outcomes for injured people rather than a focus on compensation;
- a mixture of Government underwriting (NIIS – for severe and profound injuries) and private underwriting (for all other claims ranging from serious to minor), and
- a competitive pricing model that rewards safe driving but is based upon community rating to maintain affordability.

The introduction of universal and first party cover in NSW has the greatest potential to provide:

- fair and equitable cover for all those in NSW;
- choice of insurer who will manage the claim – an essential benefit of first party cover to promote claims management competition between insurers;
- excellent health and well being outcomes through appropriate levels of care and medical treatment for all injured parties, regardless of fault;
- appropriate economic loss recompense based on defined benefits, level of injury and fault status;
- defined general damages compensation for injured people with severe injuries who are not at fault, and

- an affordable and sustainable scheme.

Suncorp's recommendations regarding scheme design are made with particular consideration of keeping premiums in NSW as low as possible. We believe that the correct scheme design can achieve cost savings (in both claims and administration) significant enough to fund a no-fault scheme, without premium increases.

Defined benefits

There are significant advantages in introducing defined benefits into a personal injury scheme for motorist, such as;

- certainty of benefits for those who suffer injuries;
- targeting a higher proportion of benefits to those most seriously injured;
- earlier resolution of claims, which provides greater certainty for insurers to maintain capital, as required by the prudential regulator after taking into account movements in bond yields;
- consistent and objective levels of benefits, which provides greater stability in premium pricing;
- reducing legal and other friction costs within the scheme;
- managing superimposed inflation; and
- reducing disputes on quantum.

For less significant injuries, a defined benefits structure potentially changes the culture of returning the claimant to early self determination socially and economically rather than building a case for compensation. This approach is a crucial lever against falling workforce participation rates which would ultimately impact upon productivity.

Cumulatively, the advantages of a defined benefits structure are likely to deliver a scheme that is fair, promotes positive outcomes, is affordable and financially sustainable. This is consistent with the guiding principles for the most effective personal injury scheme for motorists.

For motorists that desire a higher level of cover, especially in regard to economic loss, the competitive market in the NSW scheme allows insurers to offer a range of 'value added' options and products to meet these needs in a way that can reward and attract customers.

Suncorp is proud of its current market leading first party cover, with an extensive list of defined benefits for serious injuries under our GIO Driver Cover Plus policies.[14] It is acknowledged that this cover offering is limited as it is offered in the current fault based scheme for no additional fee on the CTP policy, as an incentive for a safe driving record.

Dispute Resolution

Suncorp considers it crucial that an effective, streamlined dispute resolution process is available that is readily accessible, transparent and cost effective. The dispute resolution process should comply

[14] GIO – NSW CTP Insurance Driver Cover Plus - http://www.gio.com.au/sites/default/files/fm/pdf/ctp_booklet.pdf

with the Australian Standard Customer Satisfaction[15] and run by non Statutory Bodies to provide low cost, timely, independent resolution to consumers that are supported by industry. It is recommended that this model be further explored.

For complex disputes, legal representation should be permitted but legal fees be fixed for services and there should be a prohibition on contracting out.

Other Issues

Suncorp identifies other areas for consideration, such as:

- sharing the costs and findings of the injury grant program for medical research[16] across the MAA, LTCS, WorkCover Authority, the Workers' Compensation (Dust Diseases) Board and ultimately the NDIS, where appropriate;
- moving to a full on-line transaction process between the customer, the Road and Maritime Services NSW and insurers for CTP quotes, new business and claims lodgement;
- considering the appropriate level of transparency between customers and their legal advisers in the payment of legal costs to ascertain the cost to the scheme; and following from this point
- considering the objectives of the prohibition[17] on legal practitioners advertising their legal services for personal injury compensation in the current environment of how legal firms are advertising their services.

Conclusion

Suncorp has outlined the benefits of privatisation of motor accident compensation schemes in terms of driving productivity improvements for long-term economic growth. This is particularly importantly in light of expected productivity challenges as a result of Australia's ageing population. In this submission, Suncorp has raised a number of scheme design reforms to enhance the efficiencies of the current scheme to achieve the stated outcomes identified in this submission. Economic modelling of the suggested reforms would be prudent and Suncorp suggests that as the regulator, the MAA is best place to facilitate this.

[15] Australian Standard™ Customer satisfaction—Guidelines for complaints handling in organizations(ISO 10002:2004, MOD) - http://www.scribd.com/doc/27288652/AS-ISO-10002-2006
[16] NSW Government - *Motor Accidents Authority of NSW Annual report 2011-2012 – at page 19 -* http://www.maa.nsw.gov.au/default.aspx?MenuID=136
[17] *Legal Profession Regulation 2005 (NSW)* – Clauses 23-31.

Suncorp is happy to elaborate further on any aspect of this submission and to work collaboratively with the Parliamentary Committee and relevant stakeholders upon request. Once the 2012/2013 Annual Reports are published, Suncorp would appreciate an opportunity to consider the reports and comment to the Committee, if relevant.

If you wish to discuss this submission further please contact me on or my Manager of Group Government and Stakeholder Relations,

Yours faithfully

Chris McHugh
Executive General Manager
Statutory Portfolio & Underwriting Management
Commercial Insurance

Appendix A

Suncorp White Paper: ***How international financial markets impact personal injury insurance***

August 2012

Insurance Insights

When markets hit motorists

How international financial markets impact Compulsory Third Party insurance

August 2012

Chris McHugh
Executive General Manager
Statutory Portfolio
Commercial Insurance
Suncorp

Summary

When interest rates fall, many home owners enjoy the benefit of lower repayments on their mortgage.

But they are also likely to find that the cost of their Compulsory Third Party (CTP) insurance policy has increased.

It is not widely understood how and why the two events are related.

When insurers – be they private or publicly owned – collect premiums, they hold this money to pay future claims. This money is invested in order to generate income for the insurer.

The longer the investment period, the greater the significance of investment income as a source of revenue, and thus the insurer's ability to reduce the initial premium paid by customers.

CTP and Workers Compensation claims involve injured people and are therefore complex, often taking years to resolve as a person's medical condition must first stabilise.

On average, CTP claims are paid around five years after the premium is collected, making the investment income highly significant for CTP insurers.

As interest rates – or more specifically, bond rates – fall, the implications for insurers are material.

When economic conditions result in a drop in the yields of Australian Federal Government bonds, CTP and Workers Compensation premiums can be expected to rise.

This is precisely what has occurred in Australia in the 12 months from June 2011 to June 2012 as the three year bond yield has halved.

The nature of the global economy is such that seemingly unrelated external events can have an impact.

The Greek debt crisis may be half a world away but it's been pushing up the price of your CTP premium.

The degree to which premiums are able to respond to this price pressure is very much determined by the particular regulatory framework.

Background

Each state and territory government in Australia administers their own CTP scheme.

Many of Australia's CTP schemes are publicly underwritten, meaning the state or territory government sets the price, holds the risk and pays the claims.

Two of the largest, New South Wales (NSW) and Queensland, have private underwriting and multiple insurers operating within their CTP schemes.

The Australian Capital Territory (ACT) has a privately underwritten scheme but NRMA is currently the only provider.

All remaining jurisdictions are publicly underwritten.

The brands that offer CTP insurance in NSW or Queensland include Suncorp, GIO, AAMI, NRMA, RACQ, Allianz, Zurich and QBE.

Another class of insurance that involves personal injury claims is Workers Compensation.

CTP and Workers Compensation are referred to as 'long tail' classes as they take significantly longer on average for the claims to be finalised than 'short tail' classes such Motor and Home insurance.

Whilst only one of several factors that impact premium rates, investment income is far more significant for long tail insurance classes than short tail classes due to the average duration of the claims.

The dynamics discussed here regarding CTP insurance are equally relevant to Workers Compensation and Liability classes of insurance.

Whilst investment income is of greater importance to long tail classes due to longer average claims durations, it is relevant to all general insurance classes.

Investment income and premiums

CTP and Workers Compensation insurance classes are capital intensive. A single catastrophic claim can cost tens of millions of dollars and take decades to resolve.

This means that vast amounts of money (reserves) have to be held to pay future claims.

For example, Suncorp estimate that insurers operating in the Queensland and NSW CTP schemes currently hold around $15 billion in reserves, risk margin and capital.

Despite being largely invested in relatively low-risk and low yielding instruments, the revenue generated from this investment is significant.

This has a noticeable impact on CTP and Workers Compensation premiums.

In simple terms, if an insurer knows it needs to have $100 to pay a claim in five years' time, it only needs to put aside $78 if the relevant bond yields are 5%[18].

The investment by insurers of the money set aside to pay future claims reduces the premiums paid by CTP and Workers Compensation customers.

If insurers did not generate investment income, a CTP premium of $315 would cost $390[19], assuming a 5% bond yield and scheme dynamics similar to the Queensland CTP scheme.

What goes down…

A primary investment instrument for CTP and Workers Compensation reserves is Federal Government bonds.

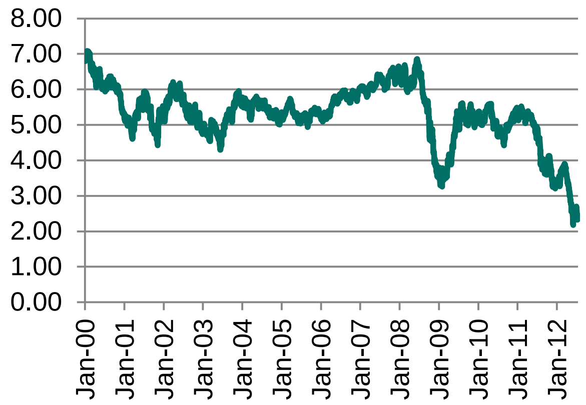
These bonds are also the benchmark used for accounting purposes when insurers calculate their reserves and future claims liabilities.

As bond yields change over time, so should CTP and other long tail premiums.

The actuarial rule of thumb is that for every 1% drop in bond yields, insurer premiums have to rise around 4% to remain sustainable.

If, as has occurred recently, bond yields slump from 5% to 2.5%, then rather than putting aside $78 to pay a $100 claim in five years, an insurer would have to put aside $88 – an increase of 13%.

The same drop in bond yields means that a $315 CTP premium would have to rise to $350 in order to remain sustainable – a $35 or 11% increase.



5-year bond yields (%) 2000 to 2012

This volatility is one of the core challenges faced by all CTP and long tail insurers.

A key mechanism to limit the ability for this volatility to dramatically affect the financial viability of an insurer is through 'locking in' investments so they mature when the claims costs are due.

This process is referred to as 'duration matching'.

Duration matching

Given that an insurer's reserves (money set aside to pay future claims) and liabilities (the estimate of future claims costs) are often in the billions of dollars, there's considerable risk that large holes can appear in the balance sheet when bond yields change.

For private insurers, the Australian Prudential Regulatory Authority (APRA) requires all liabilities to be fully funded, meaning that any hole in the balance sheet has to be filled immediately.

When reserves are insufficient to cover liabilities then this gap has to be filled, which is referred to as 'reserve strengthening'.

This reduces the profitability of an insurer, and the impact can be dramatic – hence the practice of duration matching.

[18] Bond yields vary depending on the length of maturity of the bond, with a longer maturity typically giving a high yield. The 'yield curve' can be simplified to a single rate commonly referred to as the 'discount rate'.

[19] The total paid by a CTP customer typically includes levies and taxes in addition to the insurer premium. This calculation refers to the insurer premium only.

In simple terms, if the insurer expects to have a $500 claims bill due in three years, they will purchase a bond that will mature on average in three years to a total value of $500.

By adopting an investment strategy of duration matching, insurers can protect their balance sheet and reduce the volatility of their year-on-year results.

An insurer that has a robust duration matching investment program will significantly reduce the impact of changing bond yields on their existing liabilities.

The issue for CTP and Workers Compensation insurers when bond yields drop is the fact that the premiums derived from policies being written today may be insufficient to cover future claims cost.

Of significance is the ability of private insurers to respond when bond yields change.

Changing the premium

CTP and Workers Compensation are highly regulated classes of insurance.

A key feature is that insurers cannot refuse to offer CTP insurance to a customer, which ensures that everyone can obtain insurance as long as they can pay the premium.

In the jurisdictions where CTP insurance is underwritten by private insurance companies (Queensland, NSW and the ACT) the government regulators maintain a high degree of control over premium rates.

The mechanism through which this control is exercised differs between Queensland and NSW.

Queensland

In Queensland the Motor Accident Insurance Commission (MAIC) manages a pricing process that is undertaken every three months.

The process begins with the MAIC inviting insurers to provide a submission outlining their analysis of the trends and factors influencing CTP premiums and providing recommendations on appropriate adjustments to pricing.

The MAIC also obtains independent actuarial advice, and then sets an upper and lower price limit for each of the 24 classes of vehicle.

All insurers are then required to file their rates for each vehicle class, ensuring that their rates are within the band as prescribed by the MAIC.

In Queensland, insurers nominate a single premium rate for each vehicle class.

This means that all customers owning the same class of vehicle will pay the same CTP premium regardless of their age, location or driving history.

Accompanying the price for each vehicle class, insurers also provide their projected profitability for the quarter.

NSW

The process in NSW is regulated by the Motor Accidents Authority (MAA).

Whilst the MAA does issue mandatory premium filings on occasion, an insurer can provide a submission to change their premium rates any time.

Most insurers tend to submit rate filings between two and four times a year.

Unlike Queensland, no upper and lower price limit is set, but a complex formula plays a critical role determining premium rates.

Insurers in NSW are able to charge different premium rates for the same class of vehicle.

Factors such as how old the vehicle is, where it is garaged, the age of the driver and their driving history can all be used to determine the level of risk.

Mature drivers with a clean record will tend to be charged less, while young drivers who have had accidents will have a higher CTP premium.

Insurers determine a base rate for each vehicle class and are then able to discount or increase the premium depending on their assessment of the risk.

The MAA formula restricts insurers in the degree of discount or loading they can apply in relation to their base rate.

A maximum of 15% discount[20] and loading of between approximately 25% and 45% can be applied, depending on what the formula stipulates.

The formula ensures that if an insurer wishes to reduce its rates to attract more low-risk drivers, it will also have to reduce rates for high-risk drivers.

Further, the proportion of customers to whom a particular insurer can offer discounts is limited by the formula to ensure each insurer is providing cover to a reasonable spread of both high and low risk drivers.

The result is a degree of correlation between the risk and the premium paid, whilst maintaining affordability for high-risk drivers by having them effectively subsidised by low-risk drivers.

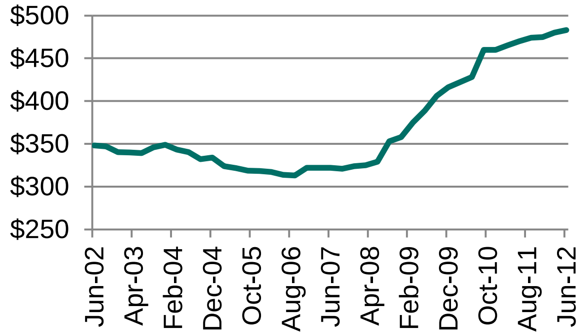
For an insurer to change its CTP premium rates it must submit its proposed rates to the MAA, accompanied by its projected profitability.

The MAA will then either approve or decline the new premium rates.

Premium trends

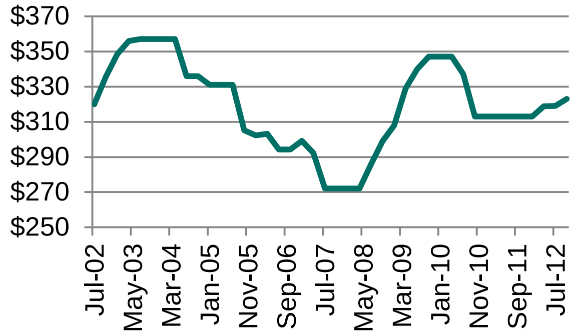
An examination of CTP premiums over the last decade presents an interesting story.

The average NSW Class metro 1 premium decreased for the first half of the last decade, but has increased significantly since the onset of the global financial crisis.



NSW average Class 1 metro CTP premium

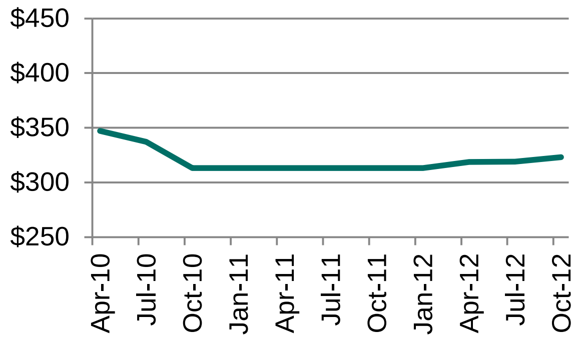
In Queensland the Class 1[21] upper price limit set by the MAIC has gone from $357 in 2003, down to $272 in 2007, up again to $347 in 2009 and then down again to $313 in 2011.



QLD CTP Class 1 Upper Price Limit (inclusive of levies and GST on insurer premiums)

Significantly, from October 2010 to March 2012, the upper price limit remained at $313 for six quarters, before rising $5 in April 2012 to $318.

In July 2012 an adjustment to fees and levies resulted in an 80 cent increase. A further $5 rise in the upper price limit to $323.80 has been approved for the October 2012 quarter.



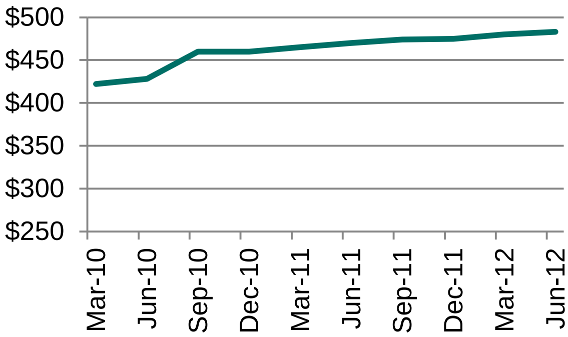
QLD CTP Class 1 Upper Price Limit (inclusive of levies and GST on insurer premiums)

This contrasts with the changes in the NSW average metro Class 1 premium for the period from March 2010 to June 2012 where the average Class 1 metro premium rose from $422 to $483[22].

[20] The 15% discount from the base rate is referred to as the 'headline rate' and applies to drivers under 55 years of age. Drivers 55 and over may be eligible for a maximum discount of 25%.

[21] Approximately 68% of vehicles registered in Queensland are Class 1.

[22] When comparing CTP premium rates between schemes, it is necessary to consider the benefits each scheme provides to injured people. Average CTP premiums are higher in NSW in comparison to Queensland, reflecting additional benefits such



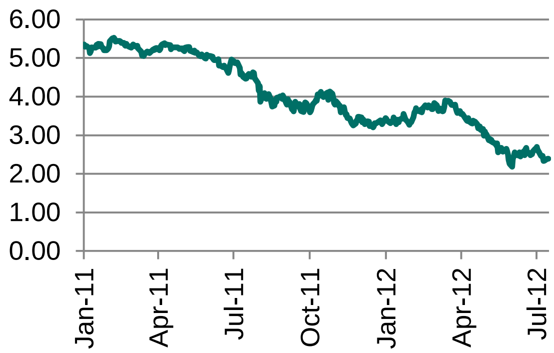
NSW average metro Class 1 CTP premium

Premiums and bond rates

Multiple factors influence CTP premiums including accident rates, inflation, scheme design and the efficiency of claims management.

Investment income is just one ingredient, but when bond yields change rapidly and significantly, it becomes a highly influential ingredient.

From January 2011 to July 2012, five-year bond rates have dropped from approximately 5.2% to 2.5%.



5-year bond yields (%) Jan 2011 to July 2012

Adopting the rule of thumb that stipulates a 1% drop in bond yields requires a 4% rise in premium to compensate, this 2.7% drop would necessitate approximately a 10.8% rise[23] to maintain profitability[24].

Over that same period the CTP upper price limit in Queensland has risen by $5.80 or 1.9%. The additional $5 rise that will take effect in October 2012 will take the total rise to $10.80 or 3.5%.

By comparison, in NSW from December 2010 to June 2012 the average metro Class 1 premium has risen by $23 or 5% from $460 to $483.

Further MAA-approved price rises have occurred since June, due in significant part to the dramatic decline in bond yields over the previous 18 months.

As bond yields have dropped, prices in NSW have steadily risen, yet in Queensland prices have remained relatively flat.

Competition

Given these statistics, it perhaps comes as no surprise that insurers in Queensland are becoming increasingly vocal in regard to the need to have premiums increase as investment returns drop.

There has consistently been minimal difference between the prices of various insurers in Queensland – far less variation than has occurred in NSW where no upper price limit is set and competitive market forces are able to operate more freely.

Since 2009 there has been a reduction in the degree to which insurers are filing rates below the upper price limit set by the MAIC.

From January 2011 to January 2012, of the six participating insurers, four consistently filed at the highest permissible Class 1 price, with AAMI and Allianz filing no more than $6 below this upper price limit.

For the last three quarters (April, July and October 2012) all six insurers have filed at the Class 1 upper price limit, meaning that there is effectively zero price competition in the Queensland CTP Class 1 market.

Since the first of April 2012, all Class 1 motorists have paid exactly the same CTP price regardless of which insurer they chose – the maximum price permitted by the MAIC.

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as the Lifetime Care Scheme that covers ‘at fault’ drivers in NSW. No equivalent exists in the Queensland scheme.

[23] The ACT CTP regulator approved a 10% rise in CTP premiums, effective September 2012.

[24] A partial offset to the upward pressure lower bond yields put on insurance premiums is the downward pressure that the same economic conditions that reduce bond yields put on average weekly earnings, which in turn reduces personal injury insurance premiums.

The MAIC policy of minimal rises in the CTP upper price limit has contained prices in Queensland, but it has come at the expense of competition.

Sustainability

State and territory governments have the power to determine how much motorists pay for their CTP insurance.

In publicly underwritten schemes, if the price is set too low, the scheme is at risk of falling into deficit and having a negative impact on the government's balance sheet.

This has occurred recently in the NSW Workers Compensation scheme, where a deficit of over $4 billion has emerged, due in significant part to a reduction in investment income from declining bond yields.

This unsustainable financial position has led the NSW Government to undertake reform and cut benefits in order to contain further premium rises.

In privately underwritten CTP schemes, it is insurance companies that hold the risk and have their balance sheets exposed to fluctuations in bond yields that can stem from both domestic and international financial conditions.

Given this exposure, private insurers arguably have a right to expect CTP premiums to respond to significant and sustained changes in bond yields.

Conclusion

The relationship between bond yields and CTP prices is well understood by insurance analysts.

It is a direct relationship and has a material impact on the financial sustainability of CTP insurers, both public and private.

Private insurers that participate in CTP schemes are required by the Australian Prudential and Regulatory Authority to have sufficient reserves to cover all future claims.

When bond yields drop, if premiums do not correspondingly rise then it's shareholders who pay to fill the gap between reserves and liabilities.

An unresponsive regulatory framework reduces competition and undermines confidence in a private insurer's ability to operate sustainably in a CTP scheme.

It is in the interests of the community to ensure that, even if bond yields crash, a viable CTP scheme is there to support Australian motorists who do the same.

The Suncorp Group

Suncorp Group Limited and its related bodies corporate and subsidiaries (collectively 'Suncorp') offer a range of financial products and services including banking (Suncorp Bank), general insurance, compulsory third party (CTP) insurance, workers compensation insurance, life insurance and superannuation (Suncorp Life) across Australia and New Zealand. Suncorp has more than 15,000 employees and relationships with over nine million customers.

Appendix B

Suncorp White Paper: ***Reflections on underwriting options for personal injury insurance***

November 2012

Insurance Insights

What scheme works when people get hurt?
Reflections on underwriting options for personal injury insurance

November 2012
Anthony Day
Chief Executive Officer
Commercial Insurance
Suncorp

Summary

In 2004 the Productivity Commission concluded that private underwriting of Workers Compensation schemes was preferable to government underwriting.

Today, eight years later, many personal injury schemes around Australia continue to be underwritten by the public.

The New South Wales (NSW) Workers Compensation scheme is currently remediating a deficit greater than $4 billion, which has involved a Parliamentary Inquiry and controversial cuts to benefits designed to avoid projected premium rises of 28%.

Those in favour of government underwriting of the personal injury classes of Workers Compensation and Compulsory Third Party (CTP) insurance argue that it provides certainty and facilitates the broad pooling of risk, backed up by the strength of a state government balance sheet.

An argument for private underwriting is that it reduces the risk to state governments and ultimately to taxpayers by avoiding exposure to significant liabilities when schemes fall into deficit.

Further, a private scheme can arguably deliver better health outcomes to people who have been injured and provide incentive for policy holders to reduce risk.

In a well-regulated environment with a robust insurance industry like Australia, the case for private underwriting and claims management appears strong, but is it sufficiently compelling to prompt government schemes to transition to private underwriting?

This paper examines the question of public versus private underwriting of personal injury insurance schemes.

Background

Each state and territory in Australia has personal injury schemes for both their Workers Compensation and CTP insurance.

The scheme designs range from full state administration of underwriting, policy and claims management to fully privatised schemes with multiple insurers operating – with a number of variations in between. Federal schemes such as Comcare also exist.

Workers Compensation in NSW and Victoria are referred to as ‘managed fund’ schemes with state government underwriting the risk and providing the capital, whilst policy administration and claims management is outsourced to ‘scheme agents’ who are paid on a fee for service basis.

Scheme agents are often insurance companies and include GIO, QBE, Allianz and CGU. Third party administrators such as EML, Xchanging and Gallagher Basset also operate as scheme agents.

In South Australia, a single agent (EML) has provided all Workers Compensation policy and claims management. A second claims manager will commence on 1 January 2013[25].

Queensland Workers Compensation is entirely government run with no insurer or agent involvement[26].

Western Australia (WA), Tasmania (TAS), the Northern Territory (NT) and the Australian Capital Territory (ACT) have privately underwritten Workers Compensation schemes with multiple insurers operating within them.

In CTP, only NSW and Queensland have private underwriting and multiple insurers operating within their schemes.

The ACT has a privately underwritten scheme but NRMA is currently the only provider. Other insurers are reluctant to enter the market under the current legislation and procedures.

All other CTP schemes are entirely underwritten by government.

Comparing schemes simply on premium rates can be misleading as each jurisdiction has different benefit regimes for those who are injured.

[25] The South Australian Government recently completed a tender process for claims management of its Workers Compensation scheme. A second claims manager, Gallagher Bassett, will enter the scheme on 1 January 2013.
[26] The Queensland Government has brought forward its five-yearly review and created a Parliamentary Committee to oversee the review.

For example, CTP prices are higher in NSW than in WA, but NSW has a lifetime care scheme for all catastrophic injuries while WA does not.

The Workers Compensation average premium rate is significantly lower in Queensland than in NSW, but income replacement in Queensland is capped at five years or $287,605, whilst in NSW income replacement can continue until retirement age for severely injured workers[27].

The underlying dynamics that are present in government and privately underwritten schemes provide a more accurate basis for consideration.

Liability management

State government underwriting means that the relevant government authority is directly able to set the exact premium for personal injury insurance policies.

Critics of the publicly underwritten model contend that a state government is compromised when it comes to the difficult task of managing liabilities for future claims cost in a personal injury scheme.

It is apparent there will always be the potential for a state government to be pressured to reduce premiums or moderate premium increases due to the impact on the electorate.

Business owners and motorists want lower premiums, whilst unions and lawyers who represent the injured advocate for increased benefits.

With no independent regulator requiring the scheme to remain fully funded, arguably there will always be a temptation for a state government to allow the scheme to go into deficit – as has occurred under all major political parties and for both Workers Compensation and CTP schemes.

As noted, the NSW Work Cover scheme is currently remediating a deficit of more than $4 billion. The Queensland Workers Compensation scheme has been on a sharp decline in recent years, managing a thin surplus in 2010/11.

The Transport Accident Commission (TAC) that manages the CTP scheme in Victoria recently reported an increase in net liabilities from $0.24 billion in 2010/11 to $1.40 billion in 2011/12.

In theory a government underwritten scheme is able to provide more consistent premiums by being less responsive to changing market conditions such as investment yields.

But if those premiums are consistently too low, the result can be dramatic.

Prior to privatisation in 1989, the NSW CTP scheme had deteriorated to an alarming degree.

At 30 June 1988 liabilities stood at $3 billion of which $1.87 billion was unfunded. Representing $4.7 billion in today's terms, the NSW deficit was enormous both in percentage and absolute terms.

Every NSW CTP policy had an additional $47 levy for the next 10 years to pay off the debt.

Personal injury claims can be very expensive. They incorporate significant medical, rehabilitation and care expenses, and can include income replacement as well as lump sums for permanent impairment and pain and suffering compensation.

These factors mean that sizable deficits can quickly materialise if liabilities are not monitored closely and urgent remediation undertaken.

Privately underwritten schemes are arguably more effective at discerning emerging trends and responding in a timely fashion, particularly during challenging economic times.

When deficits are allowed to accumulate, this effectively pushes the cost of injuries occurring today onto the employers and motorists of tomorrow.

In schemes that are privately underwritten – WA, ACT, NT and TAS Workers Compensation and NSW, ACT and QLD CTP – there are no deficits that can be carried forward into the future.

The Australian Prudential and Regulatory Authority (APRA) ensure insurance companies fully fund any future claims liabilities.

Any deficit requires an adjustment that has an immediate impact on the insurance company's results.

A failure to do so would result in close supervision from APRA with possible increased prudential

[27] Adjustments to the maximum duration of income replacement payments were legislated in NSW in June 2012. Prior to the new legislation, income replacement could continue until retirement age for workers without severe injuries.

capital requirements and damage to the insurance company's reputation and share price.

There is no APRA equivalent overseeing state government schemes and placing the same conditions on governments that APRA places on private insurers.

This lack of independent regulation allows government underwritten schemes to fall into deficit, with the end result being a significant impact on the state balance sheet and risk of a credit rating downgrade.

Risk, price and behaviour – the relationship

Government underwritten Workers Compensation schemes provide businesses – particularly small businesses – with a high degree of premium stability.

Premiums are determined by the business type and the price is identical regardless of which agent is managing the policy.

This is distinct from a privately underwritten Workers Compensation scheme where, when a policy is issued, an underwriter can look at the profile of the small business, determine the risk and set the premium accordingly – as per normal insurance principles.

A large business with poor safety procedures and un-maintained equipment is a higher risk and will be charged a higher premium. A large business that is serious about avoiding workplace accidents will attract a lower premium.

Insurance companies want to insure businesses that have good risk management practices and will offer a competitive premium to reflect this.

When it is time to renew the policy, the safety record of the business and the frequency and severity of claims they have made will have a direct impact on the premium. This is true for large and small businesses alike.

In a government underwritten Workers Compensation scheme like NSW WorkCover, employers paying less than $10,000 a year in premium – which usually means up to five employees – are immune from claims impacting on their premium.

Whilst this shields these employers from premium rises, the result is that safe business operators effectively subsidise negligent business operators.

Regardless of how many workers are injured at a business and the seriousness of the injuries, the negligent employer will pay the same premium as an equivalent business with a perfect safety record.

Critics point out that this is unfair and provides little incentive to change behaviour and invest in safety.

In a privately underwritten Workers Compensation scheme the same negligent business operators would see their premiums dramatically impacted, delivering a clear message that to stay competitive, safety must be improved.

Similarly in CTP, some insurers in the privately underwritten NSW scheme use risk rating factors such as the number of previous at-fault collisions to determine premium rates, which rewards those with a perfect driving record.

Risk managers and underwriters will tell you that having a clear and direct link between risk and price is essential if you are serious about changing behaviour to reduce risk and injury.

Investing in safety has multiple benefits – it saves lives, improves productivity and reduces insurance premiums. It also promotes a positive safety culture within the business.

One of the strengths of privately underwritten personal injury insurance schemes is that they can be more flexible and responsive, meaning they reward policy holders who look after themselves and the people in their care.

Managing rehabilitation

Personal injury claims management involves a remarkable confluence of objectives – everyone wants the same thing, which is for the injured person to recover as quickly as possible.

In the case of a workplace injury, a speedy return to work is good for the worker, the employer and the underwriter.

In privately underwritten schemes the claims manager is the underwriter, meaning there is a direct link between the quality of the claims management and the bottom line of the underwriter. The underwriter has real 'skin in the game'.

There is a strong incentive to be innovative and proactive in order to avoid a protracted – thus expensive – claim.

As Australia's largest personal injury insurer, the Suncorp Group (Suncorp) is highly cognisant of the fact that resolving a claim requires early intervention, the establishment of trust, empathy and the most effective treatment.

Delays, cutting corners and failing to actively monitor progress become very expensive.

In government schemes where the claims management is outsourced, the link between claims management and the bottom line is weakened if strong regulatory monitoring and aligned remuneration models are not in place.

For example, reports have shown that in some government underwritten schemes there has been inadequate monitoring of rehabilitation providers by claims managers.

These reports noted that rehabilitation providers were appointed, but there was insufficient follow-up to ensure actual positive results were being achieved.

This lack of monitoring can allow a protracted claim to develop, dramatically increasing the period of incapacity for the injured person and the cost of the claim.

Best-practice claims management is the key to minimising the negative impact of injuries on people, employers and underwriters.

Competition between independent insurers who underwrite and manage claims, generates a strong motivation for claims managers to be innovative and contain costs, rather than simply following a procedure without active pursuit of an outcome for the injured person.

Competition drives best practice and results in multiple parties working for the ongoing financial sustainability of the scheme.

Certainty and investment

A distinguishing feature of personal injury claims is that they are 'long tail' – they can last a lifetime. As they directly involve people and their families who are coping with physical injuries and financial stress, they're very complex to manage.

Personal injury claims management is a highly specialised industry and establishing the expertise, systems and processes required to do it well is a significant and ongoing investment.

For a business to invest in such an undertaking requires a high degree of certainty.

Managed fund schemes typically offer agents five year contracts to manage policies and claims. The state government authority is able to allocate and remove market share at will.

Over the years the authorities in NSW, Victoria and South Australia have increased and decreased the number of agents, resulting in reduced market share for existing agents when numbers increase, and in agents being removed from the scheme when numbers decrease.

This uncertainty can stifle investment.

By way of illustration, insurers like those within Suncorp who operate in privately underwritten jurisdictions with relative security have made significant investments in the latest claims management computer systems.

Compare that to other Australian jurisdictions where claims management is still paper-based.

The fact that agents operating in government underwritten schemes have less security of tenure is arguably a disincentive to invest.

In a privately underwritten jurisdiction an insurer – assuming they comply with their licence conditions and remain competitive – can expect to remain indefinitely.

This encourages investment in people and systems to build the quality and profitability of their business, and improves the scheme for all participants.

Role of government

Advocates of privately underwritten personal injury schemes argue that they allow government to focus on the critical role they have to play in order to deliver an effective and sustainable scheme – to regulate and provide oversight.

Effectively the scheme is defined by the regulator, which ultimately means the state government.

They set the conditions and dictate what constitutes reasonable and adequate care.

By controlling the benefit structure, the regulator decides if their scheme will have generous benefits and therefore higher premiums, or restricted benefits and lower premiums.

As currently occurs in privately underwritten schemes, premium increases are approved – although not dictated – by the regulator.

The regulator is also responsible for ensuring affordability and universal coverage.

As much as a direct relationship between risk and price has clear benefits in changing behaviour, there are instances where 'community rating' of premiums is appropriate.

For example, whilst an 18 year old should pay more for their CTP insurance, if they were charged the full price for the risk they represent it would be unaffordable, which would increase the likelihood of people driving without insurance.

A government underwritten scheme does give the regulator direct control over the prices consumers will be charged.

However, in privately underwritten schemes the regulator has a high degree of indirect control through setting ceiling prices and rejecting proposed premium increases – as occurred in the NSW CTP scheme in late 2011.

Regardless of whether the underwriter is public or private, the regulator is able to determine what constitutes an appropriate community rating in order to encourage the right behaviour, deliver affordable insurance to all parts of the community and reduce levels of uninsurance.

NDIS

Whilst proponents of private underwriting and claims management contend that this is the best option for over 99% of personal injury claims, it is not necessarily the case for the less than 1% that constitute catastrophic (severe and profound) claims.

Suncorp has consistently argued that insurers have an important role to play in the proposed National Disability Insurance Scheme (NDIS) for acquired disabilities and National Injury Insurance Scheme (NIIS) for disabilities from accidents.

However, that does not include private underwriting of catastrophic components of the NDIS or NIIS.

Catastrophic claims constitute approximately 20% of the total personal injury claims cost of CTP claims.

The capital required for these claims is enormous due to their size and duration, and is impacted by the volatility of investment markets.

If underwritten by entities that are owned by shareholders, these shareholders require a return on this capital, which increases premiums.

Further, the small number of catastrophic claims means that fragmenting the claims management by dividing them amongst several claims managers does not deliver sufficient scale. Aggregating these claims delivers economies of scale.

An NDIS and NIIS will allow a long-term, holistic approach to be taken to the rehabilitation, care and support of people with catastrophic disabilities.

They will be able to have their individual preferences catered for and long-term strategies implemented to maximise function and reduce the call on public medical and hospital resources.

An NDIS and NIIS will also ease the burden on carers, which in turn may increase workforce participation.

The cost benefits of this approach are far preferable to the current situation where insured people with catastrophic claims are generally given a lump sum, which may be inadequate, can be mismanaged and may not produce the desired outcomes.

A system that provides holistic, long-term care to the catastrophically injured is preferable to one that encourages litigation in order to maximise lump-sum payouts, which can hinder early medical and return-to-work intervention.

Underwriting and claims management of catastrophic injuries is best placed outside the private insurance industry due to the high capital requirements.

The benefits that will be derived from a centralised scheme that is underwritten by government will deliver better outcomes for all.

Conclusion

The conclusion of the Productivity Commission in 2004 that private underwriting of Workers Compensation is preferable to government underwriting also stated that the risk of insurer failure would be reduced by prudential supervision.

In the intervening years, prudential control of insurers has proved its worth.

Insurers are less at risk of failure than they were a decade ago due to strengthened capital requirements and greater prudential oversight.

This was evident during the recent global financial crisis where the insurance industry demonstrated its resilience.

Yet government underwritten personal injury schemes continue to dominate the Australian landscape, and no schemes have moved from public to private underwriting since the Productivity Commission made its recommendations in 2004.

The current unfunded liabilities in government underwritten schemes expose future policy holders to increased insurance costs as a result of today's political environment.

Australia has a mature and highly capable insurance industry where competition is delivering competitive pricing, innovation and a high focus on customer experience.

Insurers have the skills, capacity and appetite to underwrite personal injury schemes across the nation.

Moving from public to private underwriting would remove a significant liability or potential liability from the public, as well as arguably increasing efficiency, reducing costs and improving health outcomes for those who are injured.

Perhaps the next decade will see more state governments asking why they continue to be in the insurance business.