SUBMISSION TO STANDING COMMITTEE ON LAW & JUSTICE

SUPPLEMENTARY SUBMISSION OF NEW SOUTH WALES BAR ASSOCIATION REGARDING 2012-13 MOTOR ACCIDENTS AUTHORITY ANNUAL REPORT

1. Subsequent to providing submissions to the Standing Committee on Law and Justice for its Twelfth Review of the exercise of the functions of the Motor Accidents Authority ("MAA"), the New South Wales Bar Association has been invited to provide supplementary submissions following release of the 2012-13 MAA Annual Report.

2. The contents of the Annual Report support and confirm the submissions made by the Association:

   (i) The scheme is generally performing well and is stable.

   (ii) There is no super-imposed inflation or scheme based pressure on premiums.

   (iii) The only pressures on premiums come from internationally low interest rates and the failure of the MAA to properly regulate insurer profit.

   (iv) The recent performance of the NSW scheme is comparable to other privately underwritten schemes once catastrophic claims (LTCS cases) are added back in to make a fair comparison with the relevant interstate jurisdiction (such as Queensland).

ADDITIONAL SUBMISSIONS

PRICES

3. Annexed to this submission are extracts from the March 2013 Newsletter *D'Finitive* published by Finity Actuaries. Finity are one of the leading actuarial specialists in Compulsory Third Party ("CTP") insurance in Australia. From time to time they provide independent advice to the MAA.

4. Page 4 of the newsletter shows that between 1 July 2012 and 1 April 2013, CTP premiums in Queensland were permitted to rise from $319 to $332. This represented an increase of only $14 over a twelve month period. [It should be noted that the Queensland price is significantly cheaper than that in New South Wales for a variety of reasons addressed in the Bar Association's substantive submission. One of the main reasons is that Queensland does not have a no fault LTCS scheme. As and when they have to introduce such a scheme, their premiums will rise significantly.]

5. By way of comparison, premium increases permitted by the MAA in New South Wales between October 2012 and February 2013 were an average of $42, with some insurers being permitted to increase premium by up to $67.

6. The NSW and Queensland schemes are broadly similar. Any super-imposed inflationary factors that could be at play in both schemes are similar. The need to return a profit to private underwriters is a common feature of both schemes.

7. A very good question for the Standing Committee on Law and Justice to address to the MAA is why have New South Wales premiums increased so significantly over a period where Queensland premiums were held relatively stable? This question becomes even more critical when considering projected super profits for NSW insurers outlined below.

8. Part of the answer may be that the MAA does not have the appropriate statutory tools or powers to sufficiently regulate insurer premium setting profit.

9. During the CTP Roundtable hosted by the NSW Government on 24 July 2013, the then head of the Department of Finance and Services, Michael Coutts-Trotter, advocated for the Government's proposed reform Bill on the basis that part of the package was increased powers for the MAA to regulate pricing and profits. When directly questioned by the Bar Association representative at the Roundtable, Andrew Stone, Mr. Coutts-Trotter ultimately conceded that the regulatory control measures contained within the Bill were stand-alone provisions that could equally well be legislated independent of the radical restructuring of benefits. In short, there is no reason that legislation cannot be brought forth now giving the MAA the regulatory power necessary to better control prices and profits.

10. The Standing Committee on Law and Justice is invited to explore with the MAA whether it needs better regulatory powers to keep premiums in check and restrain insurer profits. The Standing Committee is also invited to ask the MAA to explain exactly why NSW premiums increased so significantly during 2012-13 as compared to Queensland premiums that remained relatively stable. Finally, the Committee may wish to ask why this unenviable comparison was not raised or addressed in the annual report.

PROFITS

11. NSW CTP insurers are meant to keep about 8% of the premium written as profit. That is one of the fundamental structural principles of the scheme. An 8% return is considered a fair profit. Unfortunately, the scheme has never succeeded in confining insurers to recovering just that 8% profit. Historically, the insurers have kept upwards of 20% of the premium as profit.

12. The key evidence in this regard is contained within the table on page 35 of the MAA Annual Report. This table contains the estimate of the premium that is predicted that CTP insurers will ultimately retain as profit for each premium collection year.

13. Whilst the table on page 35 presents a snapshot, the MAA continually emphasise that early projections are just that – an early effort to assess what will ultimately have to be paid out over the claims life of each premium collection year.

14. One of the difficulties with the MAA "*snapshot*" presentation is that it does not take into account the fact that, in the long-run, the profit projections for the most recent years usually seriously under-estimate the degree of profit that will ultimately be retained.

15. It is for this reason that the Association has regularly produced (and again annexes) a table summarising the profit projections in MAA Annual Reports from 2003/4 through 2012/13.

16. What this table shows is that the profit projections for recent years have significantly increased since estimates were first provided. For example, the first estimate for the 2009 premium collection year was that insurers would lose money (a -1% profit). Four years later that estimate is up to a much healthier 7%.

17. The increase in profit projections since the last Annual Report is an extra $173 million to the NSW CTP insurers over and above the super profits they have already been booking.

18. Particularly troubling are the profit projections for 2010 and 2011. They are already up to 15% and 16% of premium collected respectively.

19. Only two years after the 2011 premium was collected, insurers already look like pocketing twice the profit they should be allowed (16% rather than 8%).

20. This in turn begs the question, how did the filing process go so horribly wrong so quickly? How did the MAA permit insurers to put in filings that would almost immediately yield such significant profits? The Association understands that the CTP insurers persuaded the MAA to make substantial allowances for contingencies such as super-imposed inflation. The super-imposed inflation has not occurred and the contingencies allowances are being retained by the insurers as profits.

21. The substantial profit projections for 2010 (15%) and 2011 (16%) are unacceptable in the context of the Scheme. The NSW scheme is not so unpredictable that insurers ought to be projected making such high profits so early after the premium was collected. Given the manner in which the projections grow over time, it seems inevitable that the ultimate profit for 2010 and 2011 will be in excess of 20% of the premium written.

22. The Association emphasises that the Government's proposed changes to the CTP scheme from early in 2013 are not the solution. Those proposals sought to substantially cut the benefits to the injured in the hope that this would help reduce profit margins. However, shifting to an entirely new and actuarially untested scheme would only have seen insurers claiming much larger amounts for contingencies and uncertainties and even larger profits whilst the radical new scheme was bedded down.

23. The Association invites the Committee to ask the MAA the following questions:

    (i) Why are the profit projections so high for 2010 (15%) and 2011 (16%)?

    (ii) In hindsight, what could and should have been done differently to prevent such high projected profits arising? (i.e. what has been learnt?)

    (iii) Why is there no analysis in the Annual Report of these profit figures and why are there no recommendations in the Annual Report as to mechanisms to prevent these blow out figures from reocurring?

(iv) Does the MAA acknowledge that the total projected profit for CTP insurers over the life of the 1999 scheme to date is in excess of $3.6 billion? Allowing for 8% of that premium as reasonable profit ($1.477 billion), does the MAA acknowledge that the projected super profit for this decade will be in excess of $2 billion? How was this allowed to happen?

(v) What plans does the MAA have to reign in insurer profits within the context of the existing scheme? Does the MAA need further powers? If so, what powers does it need?

QUESTIONS FOR THE INSURANCE INDUSTRY

24. It is noted that the Standing Committee usually invites representatives of the Insurance Council of Australia (ICA) and the CTP insurers to appear at its hearings. The Committee may care to put some questions regarding insurer profits to the insurer representatives. Such questions could include:

(i) What is the explanation for the significant jump in projected profits for the 2010 and 2011 premium collection year? Why are such high projected profits emerging so early in the development of those premium collections years? [Accepting all the usual caveats about it being early days, the figures only being projections etc.]

(ii) Does the insurance industry acknowledge that it has made or will make in excess of $2 billion in super profits from the NSW CTP scheme over the past decade? Does the insurance industry suggest that this is an acceptable return for the risk or are NSW motorists paying too much?

(iii) Why have premiums in NSW increased at a far greater rate than those in Queensland? What can be done to reign in NSW premiums in the manner which occurs in Queensland?

(iv) Are NSW CTP insurers really prepared to write a premium that allows only 8% of the premium written to be kept as profit or, do CTP insurers "*know*" that they will ultimately end up keeping 15% to 20% of the premium and participate in the scheme because that is the sort of profit that is on offer? [i.e. if the CTP insurers could genuinely be held to an 8% return, would they still be interested in the NSW CTP market?]

(v) If international bond rates rise within the next two to three years, will insurers end up making an even greater profit on the recent premium collection years? [It should be noted that international bond rates cannot go any lower. There is no longer any downside risk in terms of bond rates in the premium currently being written.]

CONCLUSIONS

25. The New South Wales Bar Association is concerned about increases in premiums in NSW against a background of insurer super profits. There is a concern that these super profits are due to inadequate regulatory control. There is concern that the MAA needs

additional regulatory powers and that these powers have not been delivered. It is anticipated that there would be cross-party support for a Bill limited to giving the MAA the regulatory power it needed to reign in excess profits, continue to deliver benefits to the innocent accident victims and stabilise premium for motorists.

26. If the MAA needs more powers to regulate insurer conduct then they should be provided with them. The issue should not be linked to an unpopular and divisive plan to radically slash benefits so as to extend benefits to drivers who cause accidents.

27. The Association looks forward to discussing these premium and profit issues during the course of the Standing Committee inquiry.

Annexures:

- Page 8 of *D'Finitive* March 2013 – NSW Scheme Performance
- Page 9 of *D'Finitive* March 2013 – QLD Scheme Performance
- Summary of insurer profitability projections from MAA scheme performance reports 2003/4 to 2012/13, with calculations as to projected super profits.

31 January 2014