The Treasury

Budget 2015 Information Release

Release Document July 2015

www.treasury.govt.nz/publications/informationreleases/budget/2015

Key to sections of the Official Information Act 1982 under which information has been withheld.

Certain information in this document has been withheld under one or more of the following sections of the Official Information Act, as applicable:

[1] 6(a) - to prevent prejudice to the security or defence of New Zealand or the international relations of the government

[2] 6(c) - to prevent prejudice to the maintenance of the law, including the prevention, investigation, and detection of offences, and the right to a fair trial

[3] 6(e)(iv) - to damage seriously the economy of New Zealand by disclosing prematurely decisions to change or continue government economic or financial policies relating to the entering into of overseas trade agreements.

[4] 9(2)(a) - to protect the privacy of natural persons, including deceased people

[5] 9(2)(b)(ii) - to protect the commercial position of the person who supplied the information or who is the subject of the information

[6] 9(2)(ba)(i) - to prevent prejudice to the supply of similar information, or information from the same source, and it is in the public interest that such information should continue to be supplied.

[6a] 9(2)(ba)(ii) - to protect information, where the making available of the information would be likely otherwise to damage the public interest

[7] 9(2)(d) - to avoid prejudice to the substantial economic interests of New Zealand

[8] 9(2)(f)(iv) - to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials

[8a] 9(2)(f)(ii) - to maintain the current constitutional conventions protecting the collective and individual ministerial responsibility

[9] 9(2)(g)(i) - to maintain the effective conduct of public affairs through the free and frank expression of opinions

[10] 9(2)(h) - to maintain legal professional privilege

[11] 9(2)(i) - to enable the Crown to carry out commercial activities without disadvantage or prejudice

[12] 9(2)(j) - to enable the Crown to negotiate without disadvantage or prejudice

[13] 9(2)(k) - to prevent the disclosure of official information for improper gain or improper advantage

[14] Not in scope

Where information has been withheld, a numbered reference to the applicable section of the Official Information Act has been made, as listed above. For example, a [4] appearing where information has been withheld in a release document refers to section 9(2)(a).

In preparing this Information Release, the Treasury has considered the public interest considerations in section 9(1) of the Official Information Act.

Reference: T2015/351 CM-1-3-1-2-3

THE TREASURY
Kaitohutohu Kaupapa Rawa

Date: 19 March 2015

To: Minister of Finance (Hon Bill English)
Associate Minister of Finance (Hon Steven Joyce)
Associate Minister of Finance (Hon Paula Bennett)

Deadline: Budget Ministers' meeting on 23 March 2015

Aide Memoire: ACC Non-Earners' Account at Budget 2015

This aide memoire provides our recommendation on Budget 2015 funding for the ACC Non-Earners' Account, which funds treatment and other care and support costs for injured people not in the paid workforce.[1]

ACC is seeking an increase of $180m to the approved 2015/16 baseline of $1,091m. The requested increase is driven by large falls in discount rates. It also reflects the funding policy for the account, which makes funding estimates more volatile.

On balance, we recommend not approving the $180m increase. The Non-Earners' Account is expected to remain in surplus in 2015/16 even if the additional amount is not funded. Services would not be affected. If the extra funding were approved, net debt would increase, although there would be no impact on OBEGAL. There are no major risks in not funding the additional amount.

ACC is seeking additional funding for the Non-Earners' Account

The table below shows the additional funding sought by ACC at Budget 2015. MBIE supports the proposed increase.

Table 1: Funding sought by ACC for the Non-Earners' Account at Budget 2015

$ million	2015/16	2016/17	2017/18	2018/19	2019/20
Current baseline	1,091	1,205	1,310	1,417	N/A
ACC requested	1,271	1,319	1,384	1,459	1,519
Difference	180	114	75	43	N/A

1 The Non-Earners' Account is also used to fund a portion of the Treatment Injury Account, which covers injuries arising from medical treatment.

The projected increase is due mainly to changes in discount rates

The cost of claims in the Non-Earners' Account is affected by a range of factors. All else being equal, costs are expected to rise gradually over time, because the ACC scheme is not yet mature.[2] But in practice, costs are highly uncertain because of the long-term nature of ACC's claims pool and the impact of economic changes.

This year's funding request is driven by falling discount rates, which have worsened the account's funding position and increased estimated future claim costs (in today's money). The number of claims per non-earner and the cost of claims have increased. The breakdown of changes underlying the funding request is shown below.

Table 2: Drivers of change in actual and expected costs in the Non-Earners' Account

Change	Impact	Comment
Change in discount rate	$328.9m	Based on Treasury discount rate methodology. Discount rates have fallen significantly, and remain volatile.
Better than projected investment returns	($104.0m)	
Change in performance:		
• Higher than projected payments to 30/6/15	$41.7m	Driven by increased claim volumes for medical and non-serious injury social rehabilitation.
• Higher than projected expenses	$13.5m	Reflects increased investment in injury prevention and ACC's Shaping Our Future programme.
• Change in valuation for future claims costs for claims to 30/6/15	($91.3m)	The decrease in costs is largely due to a one-off modelling change. Without this one-off change, requested appropriations for 2015/16 may have been in the order of $85m higher.
• Projected claims performance for claims incurred in 2015/16	($16.2m)	
Subtotal	**($52.2m)**	
Free medical care for injured under-13s	$8.5m	Implements Government policy [SOC Min (15) 1/2 refers].
Sensitive claims	$3.5m	Reflects increased cover for sensitive claims. As a result of this change, sensitive claims are expected to grow by a further 10 per cent per year.
Other miscellaneous	($5.0m)	
Total	**$179.7m**	

2 The ACC scheme is only 40 years old, so there are still more people entering the scheme (including e.g. babies injured at birth, who may need support for 80-plus years) than there are leaving it.

Claims on the Non-Earners' Account after 2001 are funded on a fully-funded basis. When the post-2001 part of the account is in surplus or deficit, funding is adjusted with a view to making up over or under-funding over a three-year timeframe (horizon). Hence, the $180m increase can also be understood as:

- a $60m increase in the cost of accidents expected to happen in 2015/16; and
- a $120m impact from the account being less in surplus than previously expected:
  - Post-2001 claims are projected to be about $280m in surplus at the end of 2014/15. A portion of this over-funding would be returned in 2015/16.
  - This time last year, however, the expected surplus was much higher. The fall in funding position means that less funding would be returned.

If the funding request is approved, the account is projected to stay at around 105 per cent solvency (for post-2001 claims) over the forecast period. If not, it is projected to stay in surplus in 2015/16 before falling to 98 per cent solvency in 2016/17,[3] and sitting around 95-98 per cent for the next few years. These projections will change.

We recommend not funding the projected increase...

On balance, we do not think the $180m increase should be funded. No extra funding is needed to maintain services or improve account solvency in 2015/16. We do not think an increase in net debt to keep the account in surplus is warranted, particularly given that – in any one year – ACC only pays out around 60 per cent of funds collected for the costs of injuries expected to be incurred that year (the remainder is invested).

In addition, experience suggests that forecast funding requirements are unlikely to be a good predictor of actual requirements. The difference between the two is shown in the graph overleaf. For example, at Budget 2013, it was estimated that $1,134m would be needed in 2014, but only $961m was actually needed in 2014. The amount requested in 2015 is higher than projected in 2013.

There are no major risks in not funding the requested increase:

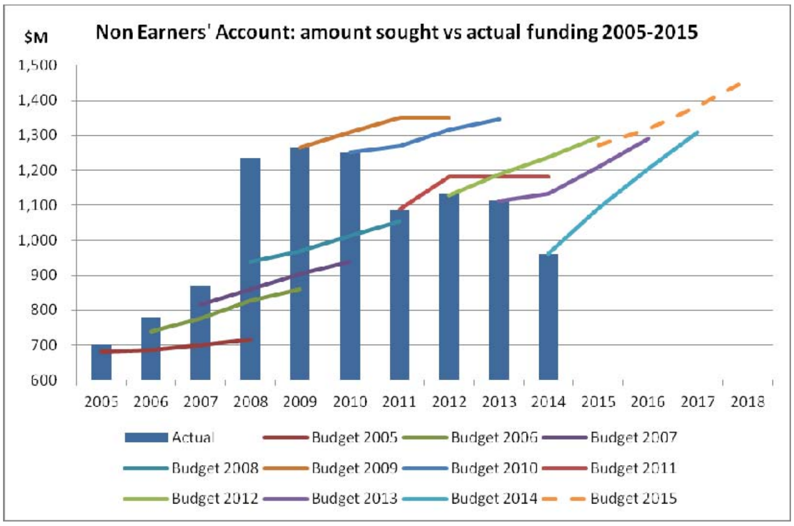
- Although it is inconsistent with the funding policy for the Non-Earners' Account agreed by Cabinet in 2006,[4] this policy does not prescribe every aspect of funding calculations, and officials agree that it needs review (see below).
- Although (all else being equal) further increases to appropriations would be needed in future, and actual funding requirements could turn out to be higher than expected, there is no real risk to ACC even if the account goes into deficit.

  Ministers therefore retain choices over how and when a fall in solvency is made up. This year's funding request builds in rising costs and deliberate increases in investment in certain areas; it is not clear how far ACC has sought to fund these

3 Though the Treatment Injury portion would stay above 100 per cent solvency until 2019/20

4 SDC Min (06) 6/2 refers. The policy includes a three-year funding horizon, but is silent on the treatment of investment returns. Funding calculations therefore reflect a mix of Cabinet policy and agency practice.

through baseline efficiencies. Lower baselines could prompt more explicit consideration of choices and trade-offs in spending decisions.



...and reviewing the way that funding requirements are calculated

Officials and independent actuaries agree that the funding policy for this account should be reviewed. Areas for review are likely to include:

- the use of a three-year funding horizon, which makes funding estimates more volatile (by comparison, Ministers have recently agreed a 10-year horizon for ACC's levy-funded accounts);[5]
- the use of risk-free discount rates (rather than forecast investment returns) to estimate asset values and claim costs in out years. This is likely to over-estimate funding requirements. Table 3 below shows what requested appropriations at Budget 2015 would have been if forecast investment returns were used.

We understand MBIE plans to review the funding policy for this account later in 2015.

Table 3: Estimated appropriations using forecast investment returns

$ million	2015/16	2016/17	2017/18	2018/19	2019/20
Current baseline	1,091	1,205	1,310	1,417	N/A
Using forecast investment returns	1,205	1,278	1,360	1,447	1,514
Difference	114	73	51	30	N/A

Helen Anderson, Senior Analyst, Health, 04 917 6307
Ben McBride, Manager, Health, 04 917 6184

5 We understand that the move from a three-year to a 10-year funding horizon could increase estimated appropriations (though it would reduce volatility in funding estimates once implemented). We will consider this as part of the funding policy review.