TAYLOR FRY

09 April 2018

Neil Singleton
Insurance Commissioner
Office of the Insurance Commissioner
By email: Neil.Singleton@treasury.qld.gov.au

Dear Neil,

Scheme performance

Please see attached for the Executive Summary of our report titled, "Scheme Performance: Scheme delivery and affordability", dated 09 April 2018.

If you have any questions, please do not hesitate to contact us.

Yours sincerely,

Richard Brookes
Fellow of the Institute of Actuaries of Australia

Peter Mulquiney
Fellow of the Institute of Actuaries of Australia

1 EXECUTIVE SUMMARY

1.1 Introduction

This report presents two measures of Scheme performance over time:

» Scheme delivery, defined as the proportion of Scheme premiums eventually paid as claimant benefits
» Scheme affordability, defined as the Scheme premium expressed as a proportion of average weekly earnings.

1.2 Definition

Scheme delivery

In simplified terms, when a premium is paid by the policyholder, it is invested and subsequently used to fund payments to various parties, the main ones being:

» Payments to claimants
» Payments to legal representatives of claimants and defendants
» Levies of various types
» Acquisition, claims management and reinsurance expenses
» Insurer profit.

We have defined the Scheme delivery index as the ratio of projected ultimate payments made to or in respect of claimants, adjusted for investment returns, to the corresponding underwritten premium. Payments to or in respect of claimants include payments made to legal representatives of those claimants. We have excluded payments by the nominal defendant, the nominal defendant levy, and the NIISQ levy from our calculations.

On advice from MAIC, we have included Trustee Administration Fees in claimant benefits.

In our previous reports on Scheme delivery, the Scheme delivery index was measured on a Class 1 equivalent basis. That is, it was calculated on a basis that assumed that all vehicles were class 1. For the current report, on MAIC's request, Scheme delivery has been assessed on an all classes basis.

Scheme affordability

Scheme affordability is shown as the highest filed Class 1 premium expressed as a proportion of Queensland full-time adult persons ordinary time weekly earnings as declared by the Australian Bureau of Statistics. This is consistent with the *"affordability index"* as calculated by MAIC in accordance with the *Motor Accident Insurance Act 1994*. The affordability index is defined as 45 per cent of Queensland full-time adult persons ordinary time weekly earnings declared by the Australian Statistician in the original series of the statistician's average weekly earnings publication most recently published. A comparison of the highest filed premium with the affordability index has been regularly reported in MAIC's annual report over a number of years.

1.3 Methodology

Scheme delivery

The main technical difficulty in the calculation of the Scheme delivery index is the projection of ultimate payments. We have done this using the same models we use to estimate recent risk premiums in our regular advice to MAIC. In particular, the calculations for this report are very similar to those underlying our report on retrospective profit (subsequently referred to as the “Retrospective Profit Study”) and so our calculation of the Scheme delivery index is subject to the same assumptions and uncertainties inherent in that advice.

Given the definition of the Scheme delivery index, we are required to split each component of premium into claimant benefits and delivery costs. Table 1.1 shows the split of premium.

Table 1.1 **Claimant benefits and delivery costs**

Claimant benefits	Delivery costs
Aids and appliances	Insurer investigation costs
Past and future care including home care	Defendant legal costs
Past and future economic loss	Administration costs and other expense costs
General damages	Reinsurance and acquisition costs
Home and vehicle modifications	Insurer’s claim handling expense
Plaintiff legal costs	Insurer’s profit margin
Hospital, pharmaceutical and medications	Statutory Insurance Scheme levy
Pre-approved costs and rehabilitation	Queensland Transport administration fee
Funeral expenses	
Trustee’s administration costs	
Trustee’s sanction fees	
Recoveries	
Hospital and emergency services levy	

We have assumed that the costs and profit are incurred at the level assumed by MAIC.

Scheme affordability

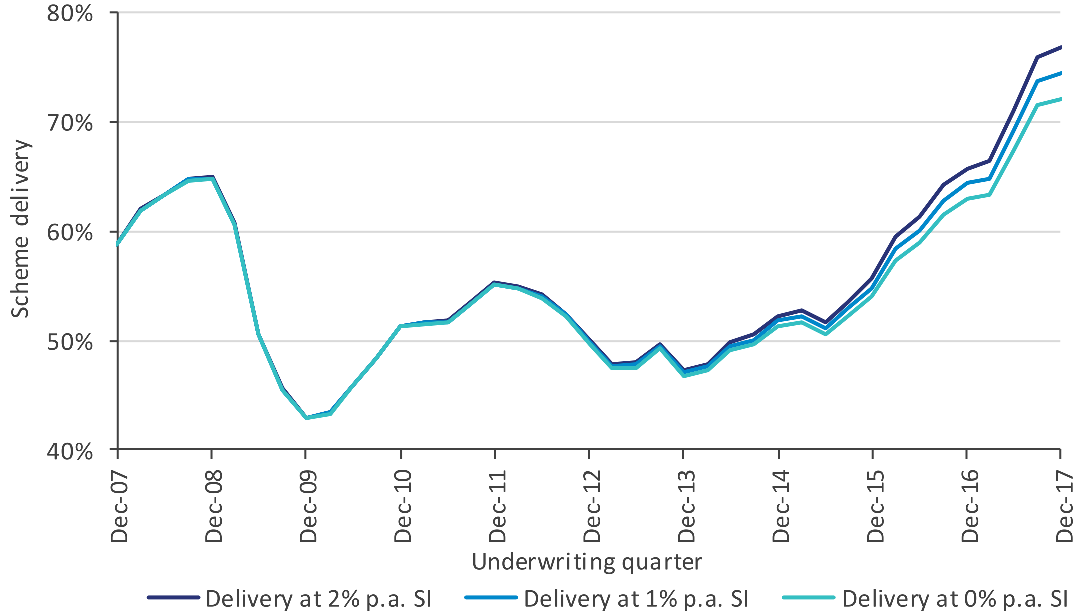
We have used the same methodology as shown in MAIC’s annual reports, which is consistent with the *Motor Accident Insurance Act 1994.*

1.4 Results

Scheme delivery

As shown in Figure 1.1 below and consistent with the Retrospective Profit Study, the Scheme delivery index is calculated under three superimposed inflation scenarios.

Figure 1.1 Scheme delivery across all vehicle classes



Superimposed inflation is generally an indicator of cost pressures in the Scheme. To the extent that it results in increased benefit payments to claimants, superimposed inflation will increase the Scheme delivery index but decrease Scheme affordability.

Table 1.2 shows the projected average break-up of the underwritten premium over various periods for the 1% future finalisation period superimposed inflation scenario.

Table 1.2 Scheme delivery with the 1% p.a. superimposed inflation scenario

Period	Claimant benefits			Delivery costs				
	Claim payments	**Levies**	**Total**	**Claim payments**	**Levies**	**Other costs**	**Profit**	**Total**
Most recent 2 years	59.3%	6.2%	**65.5%**	4.7%	2.9%	7.8%	19.2%	**34.5%**
Most recent 3 years	55.0%	5.9%	**60.9%**	4.3%	2.8%	7.5%	24.5%	**39.1%**
Most recent 5 years	50.2%	5.6%	**55.9%**	3.9%	2.8%	7.0%	30.5%	**44.1%**

Note: We assume that the reduction in costs for the claims transferred to NIISQ from 1 October 2016 is equal to our latest estimate of costs covered under NIISQ. This is different to the "NIISQ-offset" applied at premium setting. For policies underwritten before 30 September 2016, we have assumed that the reduction in cost of claims transferred to NIISQ is imperfectly offset by the amount of premium clawed back from insurers where the inconsistency arises from the difference between the previous and current estimate of costs covered by NIISQ.

Scheme affordability

Figure 1.2 shows the affordability index and highest filed premium as a proportion of AWE. For policies underwritten from 1 October 2016 we present the highest filed premium including and excluding the NIISQ levy because the claims that are covered by NIISQ do not belong to the CTP scheme.

The highest filed premium has never breached the affordability index. Scheme affordability has improved from a level of 39% of average weekly earnings in December 2004 to a level of about 24% including the NIISQ levy or 18% excluding the NIISQ levy, for the December 2017 underwriting quarter.

Figure 1.2 Highest filed premium and affordability index for Class 1 as proportion of AWE