The case for a PAYG ACC

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Three points

1. Cost of ACC is the benefits paid; not premiums collected
2. Government is currently hostage to accounting standards
3. Pure PAYG preferable: short-term smoothing would give needed certainty
Point 1: Cost of ACC is benefits paid

- Pre-funding does not change the cost of the ACC’s expected benefits
- The ‘cost’ is the amounts actually paid – driven by the benefits
- Pre-funding changes the **incidence** of the cost; not the actual cost
Point 2: Hostage to accounting standards

• Pre-funding and reporting standards are essential for private providers

• Two main reasons:
  1. Security of contractual ‘entitlements’:
     • A provider may disappear
     • So NZ IFRS 4 requires disclosure
     • But the government will never disappear
  2. Paying for the liabilities that accrue today
     • Intergenerational equity for private policy holders
     • Owners and markets need to know profits
     • Owners need a return on investment
     • But the government has the power to tax

• So, why pre-fund?
Point 2: Hostage to accounting standards

• If pre-funding is a good idea, what about:
  – Future health spending?
  – Superannuation?
  – Future spending on education, defence, police?
  – Or anything else?

• The accounting standard NZ IFRS 4 has no place in the government’s balance sheet

• The government is not an ‘insurer’

• The accountants should be told to re-write NZ IFRS 4
Point 2: Hostage to accounting standards

... and they may well do just that:

“Consultation Documents
The XRB plans to issue two Consultation Papers relating to the proposed new accounting standards framework...[including] Accounting Standards Framework for General Purpose Financial Reporting by Public Benefit Entities.”

• Earliest “announcement will be made will be towards the end of August 2011.”

External Reporting Board, here
Point 3: A PAYG ACC

• The actuary’s basic job – to calculate next year’s premiums

• Answers are based on a mixture of:
  – **Experience**: actual claims, assets, investment returns, people data, accident rates etc.
  – **Assumptions** (‘guesses’): future experience of existing claims, new claims, future premiums, investment returns, interest rates etc.

• NPV ‘future liabilities less future income’

• Compare with assets

• Adjust difference through premiums now or over time
Point 3: A PAYG ACC

- Role of actuarial calculations for private insurers:
  a) Ensure ‘solvency’ now or over a period
  b) Monitor equity between groups of employers/employees/policy holders
  c) Assess provider’s profitability for owners/markets

- **Solvency** irrelevant to ACC
- ‘User pays’ more relevant than **equity** for ACC
- **Profitability** irrelevant to ACC
Point 3: A PAYG ACC

- Alternative based on PAYG principles
- Can be occupation/employer/pay/motor vehicle specific (as now)
- Add up the expected payouts in 2012/13
- Set a 2012 levy to recover those
- For more certainty, use a 3-5 year smoothing
- 2012 levy will be somewhat less than now
- $12.8 billion of assets no longer needed
Point 3: A PAYG ACC

- Advantages of PAYG
  - Removes uncertainty of investment returns
  - Avoids worry about actuarial ‘guesses’ that must ‘work’ over very long periods
  - Simple to administer and monitor
  - Easy to understand
  - Lowers political risk

- Everything else the government does is PAYG
- The actuary can then retire
- If ACC partially privatised, premiums on that business must be calculated as now (still no need for a fund)
None of this need affect benefits

- We have only discussed how to pay for the ACC ...
- ... not what the ACC should pay for
- Today’s employers/employees/individuals/car owners should pay for today’s costs – not yesterday’s or tomorrow’s
- They must decide benefits/costs
- Tomorrow’s employers/employees/individuals can decide their own benefits/costs
A thought:

'Business model': A reverse-engineered, retrofitted abstraction of reality, accurate after the fact, because of the fact..

*The Management Contradictionary*