CHAPTER II

BACKGROUND TO THE ACT AND THE RISE OF THE LEVY SYSTEM

2.1 THE HISTORICAL BACKGROUND TO THE NEW ZEALAND ACCIDENT COMPENSATION ACT 1972

By the early sixties the existing avenues for recompense open to persons injured by accident had become inadequate and anachronistic. Under the heritage of an English common law system, an injured person could claim damages if he could establish negligence against the defendant. Any contributory negligence reduced the damages awarded proportionately. The fault principle as a basis for deciding who received compensation and how much, produced increasingly arbitrary and inequitous results. Many seriously injured persons received nothing, sometimes through lack of adequate witnesses, while others, with minor injuries, received large settlements. The expensiveness of litigation, the delays and suspense, the inherent disincentives to rehabilitation until settlement, together with the lottery-like awards of common law action became subject to increasing criticism.[1]

Workers who could not prove negligence were eligible to

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1. For a full discussion of the failures of the Tort system see N.Z. Royal Commission of Inquiry, Compensation for Personal Injury in New Zealand; Report, Wellington, Govt.Print., 1967, pp.42-77. Also T.G. Ison, The Forensic Lottery, Great Britain, The Trinity Press, 1967.

claim under the Workers' Compensation Act from their employers. However, this avenue provided only limited weekly recompense for most, and could only be claimed for work-related accidents. The benefits were income-related and set at 80% of average weekly earnings, but the ceiling imposed on such payments was low. In addition, there was a maximum period of six years for which weekly compensation was payable so that persons with more serious disabilities received no compensation after this period under the Act, despite need. For those injured in non-work accidents, where negligence action failed, the only remaining avenue was social security. This system provided flat-rate, means-tested benefits at a subsistence level.

In 1962, the late Sir Richard Wild, the then Solicitor-General, convened a committee on Absolute Liability. This provided the first airing ground for the problems of liability based on fault in motor vehicle accidents. Although no dramatic recommendations came from this committee, it was recognised that there were good arguments for the abolition of the common law action for damages for industrial injuries and road injuries in favour of a broad accident cover scheme.

After several years of further discussion, a Royal Commission was appointed, chaired by Mr Justice Woodhouse. The report, presented in 1967, was radical and based on five guiding principles:

(a) Community responsibility.

(b) Comprehensive entitlement.

(c) Complete rehabilitation.

(d) Real compensation.

(e) Administrative efficiency.[1]

Woodhouse envisaged a unified and comprehensive system for meeting losses arising from personal injury no matter where or how the injury might occur. The adversary system and the Workers' Compensation scheme were to be abolished and the philosophy of individual responsibility to disappear in favour of national responsibility. The level of compensation was to be such as to encourage effort and to recompense longer-term disability adequately. Thus short-term disability was to be compensated at a lower level, up to $25 for the first four weeks. Periodic payments would continue thereafter for life if necessary at 80% of tax-paid income, adjusted to keep pace with changes in the cost of living.

In 1969 a commentary on the Report was prepared by Government to set out the form, together with variants or alternatives of the scheme which Woodhouse suggested.[2] Then a select committee, chaired by the Hon. G.F. Gair, M.P., was appointed to hear submissions from interested parties, and to make recommendations as to the final legislation.[3] The recommendation of the Select Committee was that the Royal Commission's proposals be partially implemented by two no-fault, funded schemes, one for earners and the other for

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1. Royal Commission of Inquiry, Compensation for Personal Injury, p.39.

2. N.Z. House of Representatives, Personal Injury, A Commentary on the Report of the Royal Commission of Inquiry into Compensation for Personal Injury in New Zealand, Wellington, Govt. Print., 1969.

3. N.Z. House of Representatives, Report of the Select Committee on Compensation for Personal Injury in New Zealand. Wellington, Govt. Print., 1970.

victims of motor accidents.

After several more months of committee and drafting work, the complex legislative document itself appeared in September 1972. The Labour Government subsequently amended the Act in 1973 so that non-earners were also covered under a supplementary scheme. The process of grafting on of amendments has resulted in a piece of legislation of considerable obscurity, which is now seen in many quarters as in urgent need of complete redrafting.[1]

The final provisions of the Act depart significantly from the original Woodhouse proposals, both in the level of benefits and the financial underpinnings. Benefits are more generous than those proposed by Woodhouse, and the emphasis has been shifted, so that the principle of concentrating on longer-term disability has been diluted by the very favourable treatment given to short-term and minor disability.

2.2 BENEFITS UNDER THE ACT

The provisions dealing with compensation are set out in Part VI of the Act. In summary, they allow for broad coverage of medical and hospital expenses and other associated expenses as well as earnings-related compensation. From Table 1.1 it can be seen from total expenditure for the year ended March 1978, of $103 million, $44 million was paid in

1. For a detailed description of the legislative history of the Act and the significance of subsequent amendments, see a recent contribution by G. Palmer, 'Accident Compensation in New Zealand: The First Two Years'. The Social Welfare State Today, ed. G. Palmer. Trentham, Wright and Carman Ltd., 1977, pp.165-529.

TABLE 1.1

Accident Compensation Commission

SUMMARY OF INCOME AND EXPENDITURE

	1978				1977			
	Earners' Fund	Motor Vehicle Fund	Supplementary Fund	Total	Earners' Fund	Motor Vehicle Fund	Supplementary Fund	Total
	$	$	$	$	$	$	$	$
Income—								
Gross levy revenue	79,457,887	22,248,201	...	101,706,088	71,897,204	21,530,409	...	93,427,613
Investment income	9,067,770	6,113,496	...	15,181,266	5,677,347	3,776,012	...	9,453,359
Other	...	...	10,902,016	10,902,016	...	...	7,504,796	7,504,796
Total income	88,525,657	28,361,697	10,902,016	127,789,370	77,574,551	25,306,421	7,504,796	110,385,768
Expenditure—								
Earnings related compensation, or loss of potential earnings, payable to injured persons	39,031,179	5,223,677	48,544	44,303,400	35,503,779	4,160,991	5,121	39,669,891
Earnings related compensation or remarriage grants, payable to dependants ...	3,392,502	1,724,249	...	5,116,751	2,442,960	1,130,842	...	3,573,802
Funeral expenses and dependants allowance	610,348	684,640	209,938	1,504,926	714,225	467,426	95,782	1,277,433
Non-economic loss	11,836,838	3,899,091	2,374,027	18,109,956	6,148,402	2,160,435	1,063,406	9,372,243
Medical treatment	6,594,108	647,050	5,558,678	12,799,836	6,176,715	402,735	4,578,851	11,158,301
Hospital treatment	1,608,518	198,018	496,090	2,302,626	1,314,002	157,943	443,858	1,915,803
Dental treatment	1,267,179	213,263	640,150	2,120,592	1,085,730	180,035	423,296	1,689,061
Conveyance for medical attention ...	909,602	173,524	407,566	1,490,692	605,705	133,867	164,131	903,703
Rehabilitation—aids, training and grants...	113,676	93,946	12,713	220,335	79,276	80,030	8,715	168,021
Other expenditure	412,591	383,507	416,404	1,212,502	407,679	346,939	333,001	1,087,619
Total compensation and medical expenditure	65,776,541	13,240,965	10,164,110	89,181,616	54,478,473	9,221,243	7,116,161	70,815,877
Revenue collecting agency fee	2,491,237	1,024,161	...	3,515,398	2,267,375	1,019,777	...	3,287,152
General fund transfer	7,043,840	2,321,081	737,906	10,102,827	5,086,596	1,763,672	388,635	7,238,903
Total expenditure	$75,311,618	$16,586,207	$10,902,016	$102,799,841	$61,832,444	$12,004,692	$7,504,796	$81,341,932

SOURCE: REPORT OF ACCIDENT COMPENSATION COMMISSION, 31 March 1978.

House of Representatives E19, 1978, p.16.

earnings-related compensation to injured persons, $45 million was paid as compensation to dependents, medical, hospital and dental expenses, transportation, rehabilitation and compensation for non-economic losses. The later item, non-economic losses, refers to lump-sum assessments made under section 120 for loss of enjoyment of life, pain and suffering.[1] These cases are discretionary and can pose difficult questions for the Commission in terms of setting precedents, and providing cases for review decisions. Such settlements are not made until at least two years have elapsed so that a particular medical condition has a chance to stabilise. For this reason, only latterly has this item been significant in the accounts. The figure for 1978 is $18 million. The remaining 13.6 million dollars is accounted for by administration expense, expenditure on accident prevention, and payment to agencies who act as revenue collectors for the Commission.

As for the basis of determining relevant earnings for compensation, the Commission has discretionary power to decide what constitutes the earner's normal, average weekly earnings. The maximum relevant earnings on which compensation is assessed has been $300.[2] For the major classes of recipients, the benefits are as follows :

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1. A maximum of $7,000 is payable under section 119 for actual permanent loss or impairment of bodily function and a further $10,000 under section 120 for pain and suffering, loss of enjoyment of life. For quantum of awards made in specific cases see A.C.C. Report vol.3, no.4, Sept., 1978, pp.1-3 and no.5, Nov.1978, pp.1-4.

2. From April 1, 1979, this maximum will become $360; see the A.C.C. Annual Report, 1978, p.10.

Earners: The employer is liable to pay 100% of lost wages exclusive of overtime for the first week of incapacity, if the accident is a 'work' accident.[1] Thereafter, the Commission pays 80% of lost wages, subject to the maximum mentioned above. Injuries to the self-employed and injuries to an employee outside his employment do not qualify for any first week compensation, but after the first week, earnings-related compensation is payable by the Commission.

When injury results in permanent incapacity, the Commission is required to assess the nature and extent of such disability and determine the amount of long-term earnings-related compensation payable under section 114.[2] Other sections of the Act allow for provisions to be made for low earners and potential earners. In addition to earnings-related compensation, the victim may also be eligible for a lump-sum assessment.

Non-earners: In general, no periodic payment is made, except in cases such as when loss of potential earnings is allowed. Lump sum assessments are made and constituted approximately one quarter of all expenditure from the Supplementary Fund, 1978. The other major category of expenditure for this group is medical expenses.

The Self-employed: The Commission have experienced difficulty in some cases in establishing a fair measure of earnings-loss for the self-employed. If the injured person's income is not affected by his non-participation in the business, no earnings-related compensation is payable. The Commission has no discretion to adjust figures, where tax incentive deductions have artificially reduced assessable income. However, a minimum annual levy is set at $36, which allows a minimum basis for compensation. The payment of a levy by the self-employed is not then a contractual arrangement whereby compensation is automatically paid when incapacity occurs. This and other problems, such as the criterion upon which such medical events as heart attacks can be classified as injuries for the self-employed, have made the position of this group rather ambiguous.

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1. For definitions of what constitutes a 'work' accident, see the Act, Part III, sections 84-90.

2. An award made under this section cannot be revised downwards if the disabled person's earning capacity improves. This provision has been made so that the incentive to rehabilitate will not be affected. Assessments made under this section require that the claimants' medical condition has stabilised, and all efforts have been made towards rehabilitation.

2.3 SOURCES OF FINANCE

There are three main schemes operating under the Act, all separately funded and self-contained.

The Earners' Scheme: Income is derived from differential levies placed on employers according to the degree of risk in the industrial activity and based on wages paid. Levies are not paid on individual wages in excess of $15,600 which corresponds to the maximum wages on which compensation is assessed.[1] The self-employed also contribute to this fund at the flat rate of 1% up to $15,600 irrespective of occupation.

The Earners' Fund is used to pay all earnings-related compensation, lump-sum assessments, medical expenses and other related expenses for all accidents, work or non-work to earners. An exception is made for motor vehicle accidents which are not identified as work accidents. These are met under the motor vehicle scheme.

The Motor Vehicle Scheme: Contributions to this scheme come from levies on motor-vehicle owners and take the place of third party insurance premiums. Each class of motor vehicle has a different levy.

The Supplementary Scheme: This is funded by an appropriation from Parliament and meets all payments to persons who do not have cover under the other two schemes.

Transfers are made from each of these three funds to the General Fund from which is met all administration expense and expenditure on accident prevention.

The Earners' and Motor Vehicle Schemes are 'funded', i.e. sufficient money must be invested in any one year to cover all future payments for accidents which occured in that year. The Commission has experienced two major problems with the funded approach. Firstly, it is difficult to make accurate

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1. The Accident Compensation (Prescribed Amounts) Order 1978 increased this maximum to $18,720 as from 1 April 1979.

actuarial calculations because of lack of statistics pertaining to impaired life mortality rates. Secondly, the provisions of the Act allow adjustment of earnings-related compensation to accommodate inflation and higher levels of earnings. The size of the fund required depends then on the real rate of interest. Inflation has been at very high levels during the past four years, but the Commission have been only able to invest in secure, relatively low-interest investments. The Chairman, Mr K. Sandford, has expressed serious doubt that the balance in the Earners' Fund will be sufficient to meet future liabilities.[1] This raises the prospect of several alternatives; the levies could be raised, the level of benefits and other expenditure reduced, or the shortfall made up in the future when and if the deficiency occurs.

2.4 THE RISE OF THE LEVY SYSTEM

The present system of financing accident compensation has its roots back in the old Workers' Compensation Schemes. Prior to these, the attitude was that the worker should look out for himself and bear the whole burden of any accidental misfortune. A few were lucky enough to successfully claim against their employer under common law.

Bismark was the first politician to recognise the res-

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1. The return averaged 8.28% during 1976-7 and improved to 10.35% in 1977-78. Report of the Accident Compensation Commission for year ended 31 March 1978, p.20. The annual rate of increase of the consumer price index has been above 11% since mid-1974 and was 16.9% in 1976, New Zealand Official Yearbook 1977, p.608.

ponsibility of employers towards their employees for accidents arising out of their employment and from his influence came Workers' Compensation Acts in Germany and then most Western countries in the late nineteenth century.[1] The New Zealand Workers' Compensation Act 1900, modelled on the British Act, was based on the principle that regardless of fault, employers must share some of the losses of employees who had work-related accidents. The injured party also had recourse through the courts if he could prove negligence. Very early on, the theory of occupational risk emerged which asserted that each industry should bear the costs of its own occupational risks. In this connection, Lloyd George is attributed with the saying 'The cost of the product should bear the blood of the working man'.

Under the New Zealand Workers' Compensation Act 1956 - an Act which consolidated previous legislation - a complicated system of 137 separate occupational classifications existed, upon which employers paid premiums ranging from $0.05 to $9.50 per $100 wages paid.[2] The Act was administered by the Workers' Compensation Board who determined the rates of levies from the claims experience of particular classes of occupations. These were maximum rates, but the Board was empowered to impose penalty levies on firms whose accident records were significantly worse than others in the same class.

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1. For a detailed account of the history of these Acts see H. Somers and A. Somers, Workmen's Compensation, Prevention, Insurance and Rehabilitation of Occupational Disability. New York, John Wiley, 1954.

2. See J.W. MacDonald, Law Relating to Workers' Compensation, 4th ed., Wellington, Butterworths, 1968.

When Woodhouse examined this system he accepted the idea that because compulsory premiums levied on all employers to pay for compensation and negligence if proven, were built into the cost of the industry and became part of the price paid for the product, that it was in the end the community who pays anyway.[1] Thus the principle of finance through employer contributions was accepted, but the desirability of differential levies was felt to be less clear.

In Britain, twenty years earlier, the differential levy system, and the adjustment of levies to reward or penalise firms whose record differed from the average was abandoned. A report, commissioned in 1941 under Sir William Beveridge[2] favoured a pooling of risks at a fixed flat rate, apart from a special levy on employers engaged in industries scheduled as hazardous.

The principle of broad risk pooling was based on recognition of the interdependence of all industry. This community of interest was seen to apply to employees as well as employers, thus a case was made for employee contributions. It was also believed that a visible contribution from employees would be likely to foster worker involvement in safety administration and put the brake on workers' unreasonable demands.

The government of the day accepted the principle of

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1. He went on to expose the fallacy of having separate, lesser benefits for those injured in non-work accidents or disabled from sickness. After all the community itself was ultimately paying. This view involves a considerable simplification of the way in which taxes on industry can be passed on, see discussion Chapters 3 and 5.

2. Sir W. Beveridge, Report of the Interdepartmental Committee on Social Insurance and Allied Services Cmd. 6404 H.M.S.O. 1942.

interdependence in total, rejecting Beveridge's suggestion of a special levy on hazardous industries.[1] These special levies would have fallen on certain important industries, e.g. mining and shipping, which face foreign competition and the imposition of extra cost was thus felt to be undesirable. Also, the government were not persuaded that a scheme of merit rating in these industries had in the past induced any extra improvements in safety. It was decided that safety could be more readily promoted by development of safety standards and establishments of joint bodies of workers and employers.

Woodhouse found the British argument for non-differential levies appealing. The community of interest concept corresponded to the community responsibility premise of the Royal Commission's Report. The report recommended that instead of differential levies, a flat rate of 1% of wages should be paid by all employers. The self-employed were also to contribute 1%. Motor Vehicle owners and drivers would contribute a flat rate amount and all levies would be pegged. Any additional finance would come from general taxation.[2]

Of the principle of Community Responsibility, the Commission wrote :

> This first principle is fundamental. It rests on a double argument. Just as a modern society benefits

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1. U.K. Minister of Reconstruction, Social Insurance. Cmd 6551 H.M.S.O. 1941, pp.9-18. For the subsequent history of British experience of levies see Appendix I.

2. Royal Commission Report, p.188.

> from productive work of its citizens, so should society accept responsibility for those willing to work but prevented from doing so by physical incapacity. And since we all persist in following community activities, which year by year exact a predictable and inevitable price in bodily injury, so should we all share in sustaining those who become the random but statistically necessary victims. The inherent cost of these community purposes should be borne on the basis of equity by the community.[1]

For the Commission, the basis of equity was that the costs of accidents are reflected in the prices of goods which all buy. A change to a general system of taxation would be a continuing advantage to industry at the expense of the general taxpayer.[2]

The Commentary (1969) asked whether this was a consistent recommendation in that matters of community responsibility would normally be funded by general taxation. However, the general arguments of the Commission were accepted as pragmatic, except the argument pertaining to the rejection of differential rates. The Committee was persuaded that there was value in a system which would allow penalties and rebates in the cause of safety promotion and found the point cogent that 'the flat rate levy would amount to a tax on low risk occupations to subsidise the more hazardous.'[3]

In the third major document to appear in the debate, the Report of the Select Committee (1970), the view was

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1. Royal Commission Report, p.40.

2. Royal Commission Report, p.171.

3. Commentary, p.89. Throughout, the Ontario experience of merit and penal rating was influential. See Appendix I.

expressed that it was right in principle that premiums be proportional to the risks of accidents in each occupation and that a similar approach be followed as to premiums paid by the self-employed. The recommendation was that premiums be levied at similar rates and classifications as those under the Workers' Compensation Act 1956, but the number of classes reduced to about 15.

> This approach is part of normal economic policy whereby the market price of products and services incorporate their true costs without subsidies.[1]

The Select Committee recognised that it was stretching the user-pays principle a little in paying for non-work accidents from the Earners' Fund.[2] However, it theorized that employers should have a direct interest in the rehabilitation of injured workers, no matter where the accident occurs and therefore they hoped the proposal would be acceptable. Besides, it was expected that the abolition of the expensive adversary system, plus economies of administration should mean premiums would be little if any greater than under the old Act. The committee then made an entirely new and far-reaching recommendation which was also to ensure that the premium rates need not be increased; the employer was to be responsible for the first week payments for work accidents.

When the legislation was finally drafted the concept of differential levies was firmly established. The old Workers' Compensation levies were transposed with some

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1. Report of Select Committee, p.17.
2. Report of Select Committee, p.18.

new classifications added, and some compression of the rates, but roughly the same relative order maintained. The lowest rate was set at $0.25 and the highest, $5 per $100 of wages paid, and the self-employed were to pay a non-risk related flat rate of $1 per $100. Provision was made in the Act for penalty rates of levies up to 100% and rebates of up to 50%; however, this section was never used and is now replaced by a new amendment (see Appendix II).

2.5 CONCLUSION

The present form of the new Accident Compensation legislation can be seen to have evolved from a decade of intensive debate, proposals and counter-proposals. Most of the original principles enunciated by Woodhouse are still perceptible, but a variety of traditional, institutional, political and pragmatic factors have also been influential. The benefits and coverage are unique by world standards, but the methods chosen to finance the scheme are largely traditional, relying mainly on differential levies as under the Workers' Compensation Scheme and levies on motor vehicle owners as under the old third party insurance provisions.