



Commissioner Patricia Scott
Disability Care and Support
Productivity Commission
GPO Box 1428
Canberra City ACT 2601

By email: disability-support@pc.gov.au

16 May 2011

Dear Ms Scott

**PRODUCTIVITY COMMISSION INQUIRY INTO DISABILITY CARE AND SUPPORT –
Insurance Council’s Submission to the Draft Report**

The Insurance Council of Australia refers to our earlier submissions dated 12 August and 21 September 2010 and welcomes the opportunity to provide further feedback to the Productivity Commission’s inquiry into Disability Care and Support (Inquiry) following the release of the release of the Productivity Commission’s Draft Report into Disability Care and Support (Draft Report) in February 2011.

We enclose our submission to the Inquiry in response to the Draft Report which, in line with our earlier submissions, broadly supports the aims and recommendations of the Productivity Commission to establish the National Disability Insurance Scheme (NDIS) and the National Injury Insurance Scheme (NIIS) to oversee disability care and support for people with a significant or catastrophic disability on a lifetime basis.

Our submission discusses the ways that the general insurance industry can be of assistance to decision makers in ensuring that both proposed agencies operate on an efficient and effective basis.

The insurance industry is keen to remain involved through ongoing engagement with the Productivity Commission and looks forward to discussing further the issues raised in our submission with you.

Yours sincerely

Robert Whelan
Executive Director & CEO



Disability Care and Support – Productivity Commission Draft Report

Submission by Insurance Council of Australia

Insurance Council of Australia Limited
ABN: 50 005 617 318
Level 4, 56 Pitt Street
SYDNEY NSW 2000
Phone: +612 9253 5100
Fax: +612 9253 5111

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Contents

INTRODUCTION..... 3

NATIONAL DISABILITY INSURANCE SCHEME 4

NATIONAL INJURY INSURANCE SCHEME 5

 1. “Managed” Private Sector Underwriting..... 7

 2. Private Sector Underwriting with mitigation of frequency/severity risk through premium mechanism 8

 3. Private underwriting with capped insurer cover and price adjustment mechanism 9

 4. Government Underwriting with Insurer Case Management 10

 5. A “Two Tier” System for Catastrophic & Non Catastrophic Risks 10

 Summary 11

CATASTROPHIC MEDICAL ACCIDENTS 11

CONCLUSION 13

INTRODUCTION

The Insurance Council of Australia (ICA) welcomes the release of the Productivity Commission's Draft Report into Disability Care and Support (Draft Report) in February 2011 and is pleased to contribute further to the Productivity Commission's Inquiry into Disability Care and Support (Inquiry) to examine the feasibility, costs and benefits replacing the current system of disability services with a new national disability care and support scheme.¹

In line with our earlier submissions, the ICA broadly supports the aims and recommendations of the Productivity Commission (PC) to establish two agencies/entities to undertake disability care and management into the future as follows:

- The National Disability Insurance Scheme (NDIS)
- The National Injury Insurance Scheme (NIIS)

The PC confirms that the recommended NDIS will be a federally provided system of high quality care and support for all Australians who currently suffer from a significant disability. In contrast, the aim of the NIIS is to federally co-ordinate a series of State based insurance schemes to provide lifetime care and support for people who suffer a catastrophic injury on a no-fault basis.¹

The ICA submits that the general insurance industry can be of assistance to decision makers in ensuring that both proposed agencies operate on an efficient and effective basis. Accordingly, the ICA does not propose addressing the individual recommendations in the Draft Report but rather will seek to inform the PC of the potential of private insurance capacity to meet the PC objectives.

We would however, wish to take this opportunity to refer to a specific request for information contained in the Draft Report arising from the discussion in Chapter 16 as follows:

The Commission seeks feedback on the benefits and risks of requiring nationally consistent disclosure to an appropriately charged body responsible for monitoring and publicly reporting trends in legal fees and charges paid by plaintiffs in personal injury cases.²

The ICA supports the principle of nationally consistent disclosure of legal costs and any initiatives which are designed to provide injured people with timely access to injury management and compensation that is focussed on optimal health and work outcomes.

We draw to your attention an example of this procedure currently in place in the Dust Diseases Tribunal in NSW where legal practitioners are required to provide notice to the Tribunal of the costs charged in a matter within 30 days of the settlement of the claim.³

We submit, however that further consideration of the mechanism for data collection be made in due course. We anticipate that there will need to be a common data set that is

¹ Productivity Commission's Draft Report into Disability Care and Support (Draft Report) Vol 1, Overview pp2-3.

² Draft Report, Vol 1, p69

³ Clause 95 Dust Diseases Tribunal Regulation 2007

captured across all jurisdictions and classes for ease of reporting and analysis.

In the following sections this submission will explore the ways in which insurers can assist the NDIS and NIIS to achieve their aims in the following areas:

- The operation of the NDIS
- The risk principles governing NIIS schemes
- The PC's specific requests for information concerning medical accidents.

NATIONAL DISABILITY INSURANCE SCHEME

The ICA understands that the NDIS is expected to cover the full range of disability supports and to operate on an “insurance” or “case management” model. The scheme, we believe, is designed to be customer centred allowing the disabled and their carers to flexibly provide for their care and support according to their preferences (but always subject to participation goals). Personal plans are envisaged together with disability assistance “brokering” whereby the disabled engage professional advisers or disability support organizations to assist them in developing care plans that maximize disabled/carer welfare and maximize the opportunity for mainstream participation.

The PC recommends that one of the services provided by the NDIS will involve:

Case management, local coordination and development, which are broad services, including individual or family-focused case management and brokerage (disability support organisations), as well as coordination and development activity within a specified geographical area. They aim to maximise people's independence and participation in the community.⁴

The ICA's Further Submission to the PC dated 17 September 2010 highlighted a number of ways in which the insurance industry can assist the proposed NDIS through its extensive experience with active case management. In particular, the insurance industry make use of the principles of commercial insurance to focus on the “total cost” over the life of the claim and not just individual cost elements. As such, insurance case management promotes measures which aid the recovery of injured persons thereby reducing costs to the compensation scheme as a whole.

The enormity and sheer scale of the NDIS (estimated by the PC to be have a gross cost of \$12.5 billion and with 359,000 people under the age of 65 receiving some form of assistance)⁵ raises the potential for supply side inflation as providers seek to maximise returns arising from the additional flow of funds into disability care arrangements. Furthermore, and as the PC itself envisages, the additional flow of funds into the NDIS will introduce new entrants into disability care services, with the resultant effects on effective care coordination and supply side management. In other words, the NDIS will require extensive and careful oversight of care services to ensure the ongoing viability of the scheme and to minimise care supply side inflation.

The insurance industry contends that the NDIS would be well served by utilising the

⁴ Draft Report, Vol 1, Overview p 21
⁵ See Draft Report, Volume 2 at 14.1

services of the insurance sector in active case management. Moreover, the scale of the NDIS implicitly dictates that case management be contested to ensure that costs are reduced and care managed effectively. In this regard, the absence from the Draft Report of a role for the private insurance sector as active care management agents in the NDIS should be reassessed.

The insurance industry is also in a unique position to provide the NDIS with an alternative means to oversee provider management of disability services. At present, the insurance industry currently provides such type of assistance in a range of schemes including the workers compensation schemes in NSW and Victoria. As the insurers do not themselves provide care and support services, they are independent of any particular care and support or service regime and are not rewarded on the basis of arranging a particular service. This approach allows insurers to effectively focus on a total cost management approach at the same time as maximising health benefits (and return to active participation) for the person requiring disability care and support.⁶

As organisations operating as outsourced managers of care providers, private sector insurance participants are subject to commercial practices such as benchmarking, performance management and tendering processes. The ICA submits that these arrangements provide a solid commercial footing for injury management and moreover provide scope for the establishment of a contestable market for the NDIS to control the costs of the scheme as a whole.

With this in mind, and notwithstanding the Draft Report recommends that the NDIS operate on a “funder/provider” basis with contestable markets for disability supports, the ICA contends that the Final PC Report would be improved with the explicit inclusion of the scope for NDIS to make use of private sector insurance/agent providers in the management of claims.

NATIONAL INJURY INSURANCE SCHEME

The NIIS proposal is designed to provide fully funded care for catastrophic injuries on a no fault basis for motor vehicle accidents, medical, criminal and general accidents with the expectation that the first phase of its development be for no fault motor and medical injuries from 2013 and for remaining injuries by 2015.

The ICA understands that some of the scheme's key factors include:

- Primary funding through insurance premiums and, where appropriate, to include experience and risk-rating to help prevent injury
- A structured federation of separate, State-based schemes.

Currently there are a range of compensation schemes across Australia which provides a level of care and support for people catastrophically injured. Some of these are fault-based while others operate on a no-fault system.⁷ Depending on the individual scheme arrangements, private sector general insurance providers have differing roles and

⁶ ICA's Further Submission to the Productivity Commission (ICA Further Submission) dated 17 September 2010, p10

⁷ Draft Report, Vol 2, pp15.24 to15.28 including the comparison of coverage under different types of scheme in Figure 15.2

responsibilities.

While the PC recommends that these schemes remain under the control of each individual State it also recommends the establishment of a “national framework” with consistent and harmonised arrangements for such aspects as eligibility and assessment, minimum levels of support and scheme reporting (including actuarial reporting).⁸

The ICA refers to our further submission to the PC which canvassed in considerable detail the principles of commercial insurance.⁹ We submit that the benefits of commercial insurance to the NIIS, include:

- The potential to access private sector capital to cover future liabilities.
- The ability for governments to limit/share their risks and exposures to catastrophic injury.
- The ability to improve cost management and simultaneously optimise health outcomes, through early intervention and effective management of care and support.
- The ability to secure prudential certainty through compliance with fully funded scheme obligations.

The ICA notes that the NIIS has been recommended as federally coordinated set of State based arrangements and accordingly, the PC envisages each individual State to retain sovereignty of the final design of their own scheme. Nevertheless, the ICA contends that the Draft Report would be improved if the capacity of private insurance was expressly acknowledged and that a set of guiding principles to the States to this effect was developed as the States transitioned to the NIIS objectives.

In particular, we submit that the private insurance industry is adept at providing risk based compensable injury schemes and that further, private sector provision is adept at managing the underwriting the risks such schemes generate. The financial risks such a scheme will be subjected to include:

- **Frequency risk** – that is, the changes in the number of participants from year to year. For example, based on the current experience of the LTCS in NSW the level of participation is relatively small each year but is subject to considerable variation.¹⁰
- **Severity risk** – while all participants in the NIIS will be, by definition, catastrophically injured there is still likely to be a large variation in the degree of care and support required for individual participants which creates variation in cost from year to year. In the Draft Report the average catastrophic transport accident in the TAC is quoted at a cost of \$1.0 million while cost for a high level quadriplegic is \$5.6 million and for a paraplegic is \$0.9 million.¹¹

⁸ Draft Report, Vol 2, p16.1

⁹ See ICA Further Submission, p9

¹⁰ LTCSA Annual Report 2009-2010, pp15-17

¹¹ Draft Report, Vol 2, p15.7

- **“Normal” inflation risk** – by their nature, future NIIS liabilities are likely to be very long term and as a result they are more susceptible to inflation risk with minor increases in inflation having disproportionate effect on future liabilities.
- **Longevity and health risk** – given the long term nature of the NIIS, and the prospective medical environment remains uncertain; future medical developments may reduce liabilities, while others may have the opposite effect.
- **Superimposed inflation risk** – this represents the risk that costs under the NIIS may increase by more than “normal” inflation driven by changing attitudes to what constitutes a reasonable level of care and or poor provider management and cost containment.

The ICA contends that private sector providers are well equipped and able to respond to such underwriting risks in a cost effective and efficient manner. Moreover, the ICA suggests that the founding principles of the NIIS (and implicitly the principles that will guide State based negotiations on individual State based schemes) should explicitly acknowledge the capacity of private insurance markets in meeting the NIIS objectives.

The ICA acknowledges that individual State based scheme design will remain the prerogative of each individual State and that the NIIS envisages such State sovereignty. Nevertheless, as a basis of future development towards the NIIS, the ICA would welcome the opportunity for the States to engage with the private sector insurance industry to maximise scope for private sector provision. In other words, although the precise arrangements will remain the prerogative of the States, a common principle for the NIIS should be set going forward that does not *ex ante* seek to “crowd out” private sector capacity and to the contrary, works with private sector providers to ensure private capacity is strengthened.

To make the case for such guiding principles in the PC Final Report and to assist the States in advancing the transition to the NIIS, the ICA has examined several scheme design options for a future NIIS.¹²

These options have been developed with a view to ensuring each State’s scheme sovereignty is retained and range (depending on particular insurer appetite) from full underwriting, through some form of modified underwriting, to active case management. The ICA suggests that when considering their pathway to the NIIS, the States should be mindful of all options and engage with private sector providers on discussions. It should be noted that these options are provided for the purposes of general information and understanding and as a prerequisite, would require additional due diligence by the parties as States transition to their preferred NIIS arrangements.

1. “Managed” Private Sector Underwriting

Under this option, private insurers would underwrite all the financial risks associated with the NIIS coverage and provide care and support benefits to NIIS participants for life. The Government (through the relevant NIIS Authority) would serve as the premium collector and claimant allocator. An example of this type of model is the operation of the first two years of the NSW CTP scheme (1989/90 and 1990/91) where policies were allocated to insurers based on agreed market shares (although the premiums were set by Government).

¹² Finity Consulting *NIIS – Underwriting Options* discussion paper available for review on request.

Although it is apparent that this approach would ensure that NIIS liabilities are not retained on a given government's balance sheet, the approach does contain challenges. In particular, it is not clear that the model represents "pure" private sector underwriting given the potential mismatch between premium collection and liability risk. Further, in the early years of such a model, pricing may be somewhat speculative with scheme designers need to carefully assess the potential of the affordability of premiums. Lastly, the capital obligations of such a model need to be carefully assessed by scheme designers. A proposal of this type remains capital intensive with the resultant implications for cost, access to scarce capital and prudential supervision.

The insurance sector contends that notwithstanding that such a model is *potentially* available for consideration, it remains to be seen whether there exists private insurance appetite to transition to such an approach. As mentioned above, careful consideration and review (including due diligence) would be a required as part of the assessment of this model.

2. Private Sector Underwriting with mitigation of frequency/severity risk through premium mechanism

This option would operate in a similar way as in the first option however insurers would establish a schedule of prices on a per claimant basis relating to the type and severity of injury. Insurers then receive a "deposit" premium at the start of the insurance year based on their allocated market share and the expected number of claimants. At the end of the insurance year a premium adjustment is calculated based on the actual number of claimants allocated to the insurer and the type of injury. The relevant NIIS Authority may then need to collect additional premiums in the following insurance year if total net adjustment premiums payable exceed any withheld premiums.

An example of this type of adjustment is workers compensation schemes which have deposit and adjustment premiums for a subset of large employers depending on claims experience and total wages paid during the year.

Under this option, frequency/severity risk is shared between government and private insurers given the scope for adjustment premiums in the event of more adverse experience. Nevertheless, there is still a significant severity risk borne by insurers in this option as it may take a number of years for the actual severity of a claimant to become apparent.

This option provides certain advantages to both governments and insurers. It is likely to give insurers greater certainty about premium collection relative to risk especially in the earliest scheme years when there will be significant uncertainty about the number and severity of NIIS claimants. It also provides an advantage to governments as it is likely to reduce the annual volatility for small jurisdictions or small market shares.

Nevertheless, there remain considerable potential disadvantages including:

- It will require significant capital for insurers which will need to be reflected in pricing.
- There may also be an insurer solvency risk to Government given the very long term nature of the liabilities.¹³

¹³ This is of course subject to APRA's licensing and prudential requirements of insurers

- As noted above, scheme designers will need to carefully balance the cost of capital implications on affordability and any government objectives in this regard.

A variation of this approach is also available for consideration. For example, it remains possible for an insurer to commute their outstanding liabilities for an NIS participant after a specified number of years to the government. A penalty could apply to the insurer for early commutation. Although the benefits of a commutation arrangement remain broadly in line with the thrust of this option (i.e price certainty), additional due diligence would be required to ensure alignment with government priorities for the scheme.

3. Private underwriting with capped insurer cover and price adjustment mechanism

This option is comparable to the second option with the addition of a cap on the insurer's liability for a participant of a particular payment total after which the Government is liable. (A variation on this option could be for the Government to take 50% of the cost over a certain threshold).

An example of this option has been in operation in the USA State of Michigan since 1978. The Michigan Catastrophic Claim Association (MCCA) operates as a reinsurer to private insurers for the lifetime care and support needs of people catastrophically injured in motor vehicle accidents.

Michigan provides unlimited lifetime medical and care for victims of motor accidents on a no fault basis. The insurance is underwritten by private insurers and the lifetime care component is reinsured with the MCCA. Claims continue to be handled by the insurer for the life of the claim, and the MCCA reimburses the insurer for costs in excess of \$480,000 per claimant (the deductible for 2011).

The MCCA charges a 'per vehicle' levy that is collected by the insurers and passed to the MCCA. The current levy is \$143.09 per vehicle and the MCCA currently has an investment fund of approximately \$12 billion. The levy is set each year based on the estimated lifetime cost of catastrophic claims for the year, and is adjusted up or down to correct past over- or under-funding.¹⁴

The degree of sharing of the inflation and longevity risk between the government and insurers would depend on the size of the cap employed. The higher the cap applied the more risk that is retained by insurers.

This option provides several advantages to both insurers and governments:

- It is less capital intensive with a cap on individual losses for insurers.
- The insurers have the incentive to contain costs and so drive innovation in case management (if the threshold is high enough).
- It lessens government liabilities that would otherwise apply in the case of a full public sector underwriting model.

However there remain some disadvantages under this option. There may not be any incentive for insurers to contain costs once a claim exceeds the particular threshold. In

¹⁴ More details can be found at the MCCA's website www.michigancatastrophic.com

addition the capital intensity of the product may make the price of premium unattractive to government.

4. Government Underwriting with Insurer Case Management

Under this option the government underwrites the pool and insurers operate as case managers tendering for case manager roles and being remunerated based on performance against a number of measures. Examples of this model are NSW WorkCover, SA WorkCover, WorkSafe Victoria, SA CTP and the Treasury Managed Fund scheme in NSW.

The government retains the underwriting risk in this option. There may be a small sharing of this risk with the insurer case managers depending on the remuneration structure.

There are several advantages to this option. It represents a minimal risk for insurers while at the same time ensuring that they have the incentive to contain costs through remuneration arrangements. It also represents a minimal insurer solvency risk to government. Nor do governments need to establish case management capabilities under this model.

However there are also several disadvantages to this model which include:

- The full liabilities and capital remain on the government balance sheet.
- The tendering process may be complex, extended and expensive.
- There is not the same level of link between performance and remuneration for insurers as in an underwriting model.

5. A “Two Tier” System for Catastrophic & Non Catastrophic Risks

Consistent with the approach taken in this submission to consider the broad spectrum of options for private general insurance, the ICA includes for completeness the current scheme in operation in NSW. The NSW CTP scheme involves a system under which risks are “tiered” according to their severity. “Tier One” claims are defined as catastrophic and managed separately on a first party basis by the statutory Lifetime Care & Support Scheme. The remaining “Tier Two” claims are privately underwritten in an independent scheme under third party arrangements.

Given the now medium term operation of the NSW LTCS, the relative advantages and disadvantages of the NSW model are well known to decision makers and further, have been subject to considerable review by policy makers.¹⁵ It is also noted that the Draft Report references the LTCS approach and highlights its potential application.

Nevertheless, the extension of catastrophic claims segregation to other motor accident schemes in other States and to other compensable schemes (for example, workers compensation) requires careful assessment and appraisal and we urge detailed consultation with private sector general insurers in this regard.

¹⁵ See for example NSW Legislative Council Law & Justice Committee, Review of Life Time Care & Support

Summary

The ICA respectfully suggests that these options prove a useful starting point for consideration by the States and Territories when developing their NIIS arrangements. Further, we submit that the insurance industry has the flexibility to participate in discussions over a range of particular State scheme arrangements and according to each State's objectives.

Unfortunately, the Draft Report does not provide guiding principles for the States in transitioning to their NIIS arrangements. The ICA submits that a principle that ensures that private sector insurers be engaged in advance of State settlement of their NIIS arrangements would be a valuable addition to the PC Final Report.

Moreover, the ICA contends that the States would benefit explicitly from the knowledge and resource of the private sector insurance industry in developing their NIIS arrangements. As shown above, private sector insurers have the capability to assess underwriting risk and to work with the States in developing models/approaches that meet a given set of objectives. It is the view of the insurance industry that future discussions concerning the NIIS would be advanced in partnership with private sector insurance providers and that the States should be encouraged to facilitate, where appropriate, arrangements to this end.

CATASTROPHIC MEDICAL ACCIDENTS

The Draft Report set out several "*Requests for Information*" for the response of relevant stakeholders. Two of these relate to the medical indemnity sector of the insurance industry. The first question seeks feedback on any practical interim funding arrangements which can be put in place as part of a transfer of catastrophic medical accidents to the NIIS. The second question asks for the industry's view on what should be the appropriate criterion to define the coverage of medical accidents under the NIIS.

The ICA submits that issues concerning funding arrangements for medical accidents under NIIS may impact on the individual commercial arrangements of our members. We would however note that as the States move towards the implementation of a NIIS for medical accidents that there are no State based private medical practice medical indemnity schemes. As such we submit that the Australian Health Practitioners Regulatory Authority which regulates 10 groups of health professionals and collects registration fees could be taken into account when determining premium collection methods. Apart from these comments we are not in a position to provide any particular public feedback to the PC on this issue. Rather we understand that individual members may wish to deal directly with you to provide the assistance required.

The ICA understands that the PC wishes to introduce care and support for those who suffer a catastrophic outcome from a medical incident. However in relation to the second information request, the ICA submits that there are particular complexities involved in the definition of a "*medical accident*". Any definition which is based on the principle of no fault will necessarily result in a much larger class of claimants than the present negligence based regime.

In broad terms under the current law governing medical indemnity, damages are payable in the event of a negligent act or omission by a medical or health practitioner. However there are particular rules concerning the standard of care in place for various types of professional. In NSW for example, the definition of this standard is:

“A person practising a profession (a professional) does not incur a liability in negligence arising from the provision of a professional service if it is established that the professional acted in a manner that (at the time the service was provided) was widely accepted in Australia by peer professional opinion as competent professional practice.”¹⁶

One of the difficulties which arise in determining negligence is the identification of an event along a spectrum of expected but less than optimal outcomes of a particular medical procedure. Many forms of treatment are accompanied by known risks over and above any unexpected or unusual outcomes. Under the definition of negligence noted above, even a catastrophic outcome to a medical procedure may not arise from an act or omission which was not considered to be outside the scope of the established practice of the profession at the time. Difficulties may also arise if the medical treatment given arises from a compensable accident and questions are then raised as to which act (and scheme) may have resulted in the catastrophic disability.

The ICA refers to the Draft Report¹⁷ concerning the appropriate definition and offers the following comments in relation to the issues raised:

- **Known risks of medical treatment** – We submit that the question of whether the appropriate consent was obtained from patients will need to be taken into account when determining the scope of the definition.
- **Sufficiently unexpected or unusual** – We believe that the administrative expert panel should apply objective criteria to issues surrounding causation and whether an outcome reaches the level of “sufficiently” unexpected or unusual.
- **Genetic factors or underlying health condition** – We also believe that objective criteria be applied to this issue including the apportionment of the cause of the disability to genetic or underlying factors.
- **Possible exclusions** – The ICA submits that a significant degree of clarity will be required in determining any exclusions to the definition particularly concerning the basis on which procedures may be considered discretionary and how subsequent treatment of those discretionary procedures (for example if a correction is required) is dealt with.

While the ICA understands that determining the scope of the definition of medical accident is within the purview of the PC, we submit that the number of claims involved may increase significantly under a purely outcomes focussed (whether the patient now suffers from a catastrophic disability or not) definition. The definition which will ultimately be applied will need to be capable of being costed and differentiated from a claim made under the NDIS scheme. We submit that the clarity of this differentiation is essential to reduce any potential inefficiency in the operation of both schemes.

The ICA finally submits that a broad definition of medical accident to include not unexpected but suboptimal outcomes of medical procedures may also result in a significant

¹⁶ *Civil Liability Act 2002*, section 50(1)

¹⁷ Draft Report Vol 2, pp16.16-16.19

shortfall in funding arrangements which should be considered by the PC when determining the criterion to define a medical accident. Notwithstanding this, consistent with the views expressed above, the particular specifics of scheme design to include medical negligence will remain the preserve of the States and State government ongoing engagement with private sector providers will assist this process.

CONCLUSION

The insurance industry welcomes the release of the Draft Report and the reform arrangements proposed for disability care and support. In particular, the ICA welcomes the broad understanding in the Draft Report that disability care and support arrangements could be placed on a firmer footing by applying some of the processes observant under private sector and case management approaches.

In this regard, the ICA respectfully contends that the Draft Report could be further enhanced by making greater mention of the strengths of private insurance and in particular, the capacity of private sector insurance providers. As highlighted, private sector insurance providers can potentially play a large role in the NDIS.

As the PC develops its thoughts on the design of the NDIS and NIIS following the release of the Draft Report, the ICA hopes that the further material provided in response to the issues raised has been of assistance.