



Australian Government

Australian Government Actuary

**Fifth report on the costs of the
Australian Government's
Run-Off Cover Scheme for
midwife professional indemnity
insurers**

2014-15 financial year

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TABLE OF CONTENTS

1. INTRODUCTION	1
2. BACKGROUND	3
2.1 Midwife professional indemnity insurance	3
2.2 Brief history of private midwife insurance in Australia — the lead-up to the Midwife Professional Indemnity Scheme	4
2.3 What is the Run-Off Cover Arrangement?.....	5
3. DATA	7
3.1 Data collection	7
3.2 Data verification	7
3.3 Eligible midwives.....	7
3.4 Claims eligible for Run-Off Cover Commonwealth contributions	8
3.5 Run-Off Cover Commonwealth Contributions	8
3.6 Run-Off Cover support payments	9
4. FINANCIAL MANAGEMENT OF THE RUN-OFF COVER SCHEME	11
4.1 Future liabilities of the Run-Off Cover Scheme	11
4.2 Notional Account.....	12
4.3 Actuarial management.....	15
APPENDIX 1: RUN-OFF COVER SUPPORT PAYMENTS	17
APPENDIX 2: ELIGIBLE PRACTITIONERS AND RUN-OFF COVER SCHEME CONTRACTS	18
APPENDIX 3: RUN-OFF COVER SCHEME CLAIMS	19
APPENDIX 4: METHODOLOGY, ASSUMPTIONS AND UNCERTAINTY	20

1. INTRODUCTION

1.1 This report has been prepared to comply with certain requirements of the *Midwife Professional Indemnity (Commonwealth Contribution) Scheme Act 2010*. Section 48 of the Act provides for a report on aspects of the Midwife Professional Indemnity Scheme (the Scheme) to be tabled each year in Parliament. The report is required to contain a statement of the:

- number of persons eligible for the Run-Off Cover component of the Scheme (ROC Scheme) as set out in subsection 31(2) of the Act;
- total Run-Off Cover Commonwealth contributions (ROC Commonwealth contributions) paid by the Commonwealth during the financial year;
- total Run-Off Cover support payments (ROC support payments) paid to the Commonwealth during the financial year; and
- projected Commonwealth's liabilities in relation to amounts of Run-Off Commonwealth contributions in future financial years.

1.2 This is the fifth report that has been prepared under section 48 of the *Midwife Professional Indemnity (Commonwealth Contribution) Scheme Act 2010*. It relates to financial year 2014-15.

2. BACKGROUND

2.1 MIDWIFE PROFESSIONAL INDEMNITY INSURANCE

2.1.1. Midwife professional indemnity insurance covers privately practising midwives for their professional negligence.¹

2.1.2. All privately practising midwives in Australia are now required to purchase professional indemnity insurance from private sector underwriters² under National Registration and Accreditation arrangements.

2.1.3. For the period covered by this report, Medical Insurance Australia Pty Ltd (MIGA) was the only underwriter that provides Government-supported midwife professional indemnity cover to eligible registered midwives. This insurance will not, however, cover the planned delivery of babies outside of a hospital. As a result planned home births are excluded.

2.1.4. Midwife professional indemnity claims are initiated by, or on behalf of, patients against midwives. A very low number of claims of professional negligence might be expected each year in relation to private midwifery practice in Australia. However, in percentage terms, there could be substantial variation from one year to the next. The small population of privately practising midwives makes it difficult to project the number of midwife professional indemnity claims with any precision.

2.1.5. The cost to the insurer of midwife professional negligence claims would be expected to be highly variable since the claims relate to bodily injury. The cost of a midwife professional negligence claim to the insurer is made up of damages which are payable to the plaintiff, any of the plaintiff's legal costs which the insurer is obliged to pay, and the insurer's own costs of defending and managing the claim. There is very limited data available to make any meaningful projections about the size of claims. However, similar to professional indemnity claims against doctors, the overall cost of claims against midwives is likely to be dominated by a small number of large claims.

2.1.6. The professional indemnity claim process can be long. Years can elapse between the date of a negligent incident and the date that legal action against the midwife is initiated. It is not unusual for claims to take a number of years to finalise after they have been initiated. Using the medical indemnity claim process as a guide for these claims, the whole process could be expected to take more than five years for a single claim. The ultimate cost of a claim will depend significantly on economic and judicial conditions prevailing at the time the claim is finalised (paid), rather than at the time of the relevant incident or the time that the claim is made.

1 Midwife professional indemnity insurance can also cover other costs such as those associated with appearing at coronial inquiries.

2 On the other hand, many employed midwives practising solely in a public hospital will be indemnified by their employer against negligence.

2.1.7. All of these factors make midwife professional indemnity insurance difficult for an insurer to accurately assess the cost of the product. It is hard to forecast claim numbers and claim sizes reliably. Moreover, much of the cost is likely to relate to a small minority of the claims, which adds further uncertainty.

2.2 BRIEF HISTORY OF PRIVATE MIDWIFE INSURANCE IN AUSTRALIA — THE LEAD-UP TO THE MIDWIFE PROFESSIONAL INDEMNITY SCHEME

2.2.1. Historically, midwife professional indemnity cover was only available to Australian midwives practising in public or private hospitals. There was no professional indemnity product offered by insurers to privately practising midwives.

2.2.2. There are a number of reasons for this. The main reasons are that privately practising midwives represent a small potential premium pool and there is a lack of accurate and up-to-date data on likely claims cost.

2.2.3. The Australian Government's 2008 Maternity Services Review aimed to improve maternity care in Australia by providing greater choice and access to maternity services by Australian women and their families, and by supporting the maternity services workforce. One of the recommendations adopted was providing Government supported professional indemnity insurance to eligible and qualified midwives from 1 July 2010. Under a contract with the Government, MIGA will provide such professional indemnity insurance.

2.2.4. MIGA will pay the first \$100,000 of each eligible claim; plus 20 cents in the dollar for claims costs between \$100,000 and \$2 million. The Government will contribute the remaining 80 cents in the dollar for claims costs between \$100,000 and \$2 million (that is, Level 1 Commonwealth contributions) and will meet the full costs of claims over the \$2 million threshold (that is, Level 2 Commonwealth contributions).

2.2.5. These arrangements have reduced the net claims cost and the degree of claims cost uncertainty for the contracted midwife professional indemnity insurance provider, both of which, in turn, improve premium affordability for midwives.

2.2.6. All midwife professional indemnity insurance is provided on a 'claims-made' basis. Consequently, midwives have to maintain insurance in order to remain covered against claims that might emerge, even if they are no longer practising. This form of insurance cover is known as run-off cover. Put simply, run-off cover provides insurance protection for midwives who have ceased practice. The potential delay between a pregnancy or birth-related incident and a claim for damages highlights the need for midwives to maintain run-off cover after ceasing practice.

2.2.7. Similar to the Australian Government's Run-Off Cover Scheme for doctors, the Midwife Professional Indemnity Scheme also requires eligible insurers³ to provide run-off cover to eligible midwives who have ceased private practice. The Run-Off Cover component of the Scheme (ROC Scheme) is intended to be broadly cost neutral to taxpayers on a present value basis.

2.2.8. This report covers the ROC Scheme as required under section 48 of the Act. It does not cover the Commonwealth's liabilities in relation to Level 1 and Level 2 Commonwealth contributions.

2.3 WHAT IS THE RUN-OFF COVER ARRANGEMENT?

2.3.1. The Midwife Professional Indemnity Scheme facilitates the provision of free professional indemnity insurance cover to particular groups of midwives who have ceased private practice.

2.3.2. The rules for the Scheme appear in the *Midwife Professional Indemnity (Commonwealth Contribution) Scheme Act 2010* (the Act) and the *Midwife Professional Indemnity (Run-off Cover Support Payment) Act 2010* (ROCSPA). The principal elements of the Scheme are as follows:

- Under arrangement with the Commonwealth, MIGA is required to provide run-off cover to particular groups of midwives who have ceased private practice.
- The Act provides for the Commonwealth to make payments to the insurers to reimburse the costs associated with eligible run-off claims. These payments are known as ROC Commonwealth contributions.
- The Act also provides for the insurers to make payments to the Commonwealth to ensure that the Scheme is broadly cost-neutral to taxpayers on a present value basis. These payments are levied as a tax on insurers' premium income. In practice, the cost is met by a loading on midwives' professional indemnity insurance premiums. These payments are known as ROC support payments. The ROCSPA sets out the rules for calculating ROC support payments.

2.3.3. The Scheme provides for ROC support payments to be made by eligible insurers to the Commonwealth and for ROC Commonwealth contributions to be made by the Commonwealth to eligible insurers.

3 At the valuation date, MIGA was the only eligible insurer.

2.3.4. An important financial dynamic of the ROC Scheme is the timing mismatch between the payment of ROC support payments by an eligible insurer and the emergence, payment and reimbursement of professional indemnity claims of eligible midwives who are no longer in private practice. The first ROC support payments were received on 30 June 2011. The ROC Scheme applies to eligible professional indemnity claims that are first notified to eligible insurers on or after 1 July 2010. As a result of inherent delays in the claims process, it is to be expected that the level of ROC support payments will be greater than the level of ROC Commonwealth contributions for a number of years. This has been demonstrated in the experience of the Run-Off Cover Scheme for doctors. That is, in a cashflow sense, the ROC Scheme is immature. It will probably take many years to reach maturity when income from ROC support payments and expenditure on ROC Commonwealth contributions are of a similar order of size.

3. DATA

3.1 DATA COLLECTION

3.1.1. For the purpose of preparing this report, certain data was collected from MIGA by Department of Human Services (DHS) during late 2015 including:

- details of midwives who were identified as having become eligible for the ROC Scheme under subsection 31(2) of the Act before 30 June 2015;
- details of claims (including incidents) notified to MIGA by 30 June 2015 which might eventually become eligible for reimbursement under the ROC Scheme;
- details of ROC support payments;⁴
- actuarial estimates of that part of the future claims cost of incidents projected to be notified during the 2015-16 to 2018-19 financial years which is expected to be reimbursed under the ROC Scheme; and
- actuarial estimates of that part of the future claims cost of incidents occurring during 2015-16 which is expected to be reimbursed under the ROC Scheme.

3.1.2. Department of Health provided actuals and estimates of the number of midwives managing clinical setting births for the years from 2010-11 to 2019-20.

3.2 DATA VERIFICATION

3.2.1. The results in this report rely on information provided by MIGA and MIGA's actuaries as well as ROC support payment data and midwife eligibility data provided by DHS. Guidance was provided as to the nature of the data, calculations and information required. This information is regarded as the most suitable information available for the current purpose.

3.3 ELIGIBLE MIDWIVES

3.3.1. Midwives performing private practice become eligible for the ROC Scheme by means of permanent retirement at age 65 years or older, cessation of private practice for three years, death, permanent disability or maternity leave.

4 A database of ROC support payments is maintained by DHS.

3.3.2. Appendix 2 describes the test of eligibility for the ROC Scheme and the process of issuing and notifying compulsory run-off cover to eligible midwives. Eligible midwives are entitled to receive notification of the terms and conditions of compulsory run-off cover from MIGA. MIGA is also required to notify DHS of the details of the compulsory run-off cover provided.

3.3.3. There are inherent lags involved in notification of the details of eligible midwives to DHS. As a result, it will be possible only to estimate the number of midwives who have become eligible for the ROC Scheme at any time. For example, there will often be a delay between the time that a midwife becomes eligible for the ROC Scheme and the time when the insurer becomes aware of this. For all of these reasons, the numbers of eligible midwives reported by MIGA need to be treated with caution.

3.3.4. According to the eligibility data provided by DHS, there were no eligible midwives⁵ as at the valuation date.

3.4 CLAIMS ELIGIBLE FOR RUN-OFF COVER COMMONWEALTH CONTRIBUTIONS

3.4.1. MIGA is entitled to reimbursement from the Australian Government for the costs of claims which:

- are first notified to MIGA on or after 1 July 2010;
- relate to an incident which occurs or occurred on or after 1 July 2010;
- relate to a midwife who is eligible under the ROC Scheme at the date of notification,⁶ and
- meet the other requirements for 'payable claims'.⁷

3.4.2. As at 30 June 2015, MIGA has not identified any claim as potentially being eligible for the Scheme.

3.5 RUN-OFF COVER COMMONWEALTH CONTRIBUTIONS

3.5.1. ROC Commonwealth contributions are the payments made by the Australian Government to MIGA as reimbursement of the costs of eligible claims.

5 That is, no midwives were eligible for the Run-Off Cover component of the Scheme.

6 Refer paragraph A.2.1.

7 Refer paragraph A.3.2.

3.5.2. If a claim is eligible for Level 1 or Level 2 Commonwealth contributions, then the amount of the ROC Commonwealth contribution is reduced by the amount of the Level 1 or Level 2 Commonwealth contribution.

3.5.3. No ROC Commonwealth contributions were made during 2014-15.

3.5.4. The Commonwealth's own administration costs are funded separately and so are not considered in this report.

3.6 RUN-OFF COVER SUPPORT PAYMENTS

3.6.1. ROC support payments are paid to DHS in the form of an annual lump sum imposed as a tax on MIGA from 1 July 2010 under the ROCSPA.

3.6.2. The amount of ROC support payments is calculated using a method set out in the ROCSPA. Appendix 1 describes the calculation in detail. Very briefly, it is based on:

$$\text{Applicable rate} \times (\text{premium income less taxes and charges}) \div (1 + \text{applicable rate}).$$

3.6.3. In 2014-15, the applicable rate was 10 per cent.

3.6.4. In total, \$23,569 ROC support payments were received during the 2014-15 financial year.

3.6.5. In order to provide full transparency for midwives, MIGA is required to attribute ROC support payments to individual policyholders. Each premium notice specifies the amount that has been included in the policyholder's invoice to meet MIGA's ROC support payment obligations. All amounts are reported to DHS, which maintains a record of each practitioner's total run-off cover credit. Interest is applied to this balance annually at the short term bond rate in accordance with section 44 of the Midwife Professional Indemnity Act.

3.6.6. Division 4 of the Midwife Professional Indemnity Act provides for certain payments, should the Scheme ever be wound up without alternative arrangements being put in place. Thus, midwives who were still practising at the time of the wind up of the ROC Scheme would be entitled to have an amount not exceeding their total run-off cover credit paid to their nominated professional indemnity provider. Midwives who were eligible for the ROC Scheme at the time of its wind up would not be entitled to any refund but would continue to be covered for any future claims that might emerge.

4. FINANCIAL MANAGEMENT OF THE RUN-OFF COVER SCHEME

4.1 FUTURE LIABILITIES OF THE RUN-OFF COVER SCHEME

4.1.1. The estimation of the Commonwealth's liabilities under the ROC Scheme in future years is an inherently imprecise process. The operation of the ROC Scheme is likely to be characterised by a small number of claims of highly variable size. It is not possible to predict the costs of the ROC Scheme with a high level of confidence. For example, the presence of even a single large claim in any given year would be expected to have a substantial effect on the total amount of ROC Commonwealth contributions for that year.

4.1.2. The liabilities of the ROC Scheme could be measured in a number of ways. It is normal for insurance-type liabilities to be measured on either a 'notified' or an 'occurrence' basis. On a notified basis, new liabilities would accrue to the Scheme as new claims were notified. On an occurrence basis, new liabilities would accrue to the Scheme at the time of the occurrence of the incidents which were expected to give rise to professional indemnity claims which would attract a ROC Commonwealth contribution.

4.1.3. Under the occurrence model, liabilities are recognised more quickly than under the notified model. The occurrence model is more consistent with the notion that the Scheme is ongoing. Accordingly, the occurrence model will be adopted for this purpose. The liabilities of the ROC Scheme will therefore be taken as the present value of future ROC Commonwealth contributions which relate to relevant pregnancy or birth-related incidents which occurred before the effective date of valuation.

Assumptions

4.1.4. We have relied on a set of assumptions set out in Appendix 4. They are the same assumptions as those used for the January 2016 Forward Estimate. One of the key assumptions, that is, the number of midwives managing clinical setting births from 2010-11 to 2019-20, is provided to us by the Department of Health, and it has been updated this year. The other assumptions are developed jointly by the Department of Health and this office, and they have not been changed since our last report.

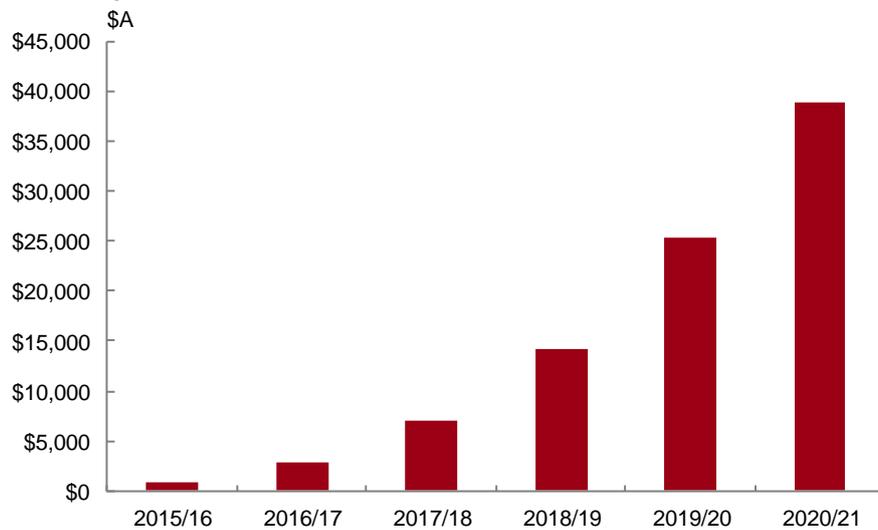
Projected Run-Off Cover Commonwealth contributions

4.1.5. This section sets out projections of ROC Commonwealth contributions for the next 7 financial years. The projections should be regarded as indicative only, and they are based on the assumptions described above. Table 1 below sets out the projections, which are illustrated in Figure 1. The Scheme is not expected to become mature in a cashflow sense for many years. The payments projected below are in nominal dollars and have not been discounted to current dollar values.

Table 1: Projected Run-Off Cover Commonwealth contributions

Year ending 30-Jun	Projected ROC Commonwealth contributions
2016	\$784
2017	\$2,900
2018	\$7,074
2019	\$14,210
2020	\$25,363
2021	\$38,888

Figure 1: Projected Run-Off Cover Commonwealth contributions



4.2 NOTIONAL ACCOUNT

4.2.1. The Scheme must be managed over a long time frame. As discussed previously, ROC Commonwealth contributions are likely to be 'lumpy' in nature and immature in size for many years. ROC support payments will be received well in advance of ROC Commonwealth contributions. As a result of the payment timing mismatch and the expected volatility in the ROC Commonwealth contribution pattern, it is appropriate to have a system which enables proper tracking of the financial flows over time. Accordingly, a ROC notional account (the Notional Account) is maintained.

4.2.2. It is important to appreciate that the ROC notional account is not an official Government account. Rather, it is a device established for the sole purpose of facilitating equity between midwives and other taxpayers.

4.2.3. The Notional Account is credited with:

- ROC support payments; and
- notional interest.

4.2.4. Notional interest is credited to the Notional Account to ensure that midwives derive the proper benefit of the time value of money since ROC support payments are received by DHS well in advance of any ROC Commonwealth contributions being made by DHS. Notional Interest is applied at the short term bond rate for consistency with section 44(4a) of the *Midwife Professional Indemnity (Commonwealth Contribution) Scheme Act 2010*, which requires interest of the short term bond rate to be applied to the total run-off cover credit balances of individual midwives.

4.2.5. The Scheme 'operates after' the Level 1 and Level 2 Commonwealth contributions. The Level 1 Commonwealth contribution meets 80 per cent of the excess between \$100,000 and \$2 million, the Level 2 Commonwealth contribution meets the excess above \$2 million. The following table sets out the funding sources for a ROC claim which costs \$2.5 million.

Table 2: Funding sources for a \$2.5 million claim which is eligible for the Run-Off Cover Scheme

Funding source	Amount
Level 2 Commonwealth contribution	\$500,000
Level 1 Commonwealth contribution	\$1,520,000
Run-Off Cover Scheme	\$480,000

4.2.6. The Act provides for payment of a midwife's total run-off cover credit, should the Scheme ever be wound up without alternative arrangements being put in place. Thus, in this event, the accumulated ROC support payment balance would become a liability of the Scheme. At the same time, since the Scheme liabilities are being measured on an occurrence basis, some of the liabilities of the Scheme would be released, partially offsetting this impact. However, for the purpose of this report, the Scheme has been assumed to be ongoing and the whole amount of the accumulated ROC support payments has been taken to be available to meet relevant ROC Commonwealth contributions.

4.2.7. The liability estimates given in this report are central estimates. In broad terms, this means that they are intended to be equally likely to be too high or too low. In particular, it is not intended that the liability estimates contain any margin for risk. Funding considerations for the Scheme are not the same as for private sector insurance arrangements. The objective here is to manage the funding over the long term. Since substantial volatility in the liability estimates is likely from time to time, periods of surplus and periods of deficit in the Notional Account might be expected. However, given the long funding time horizon that is appropriate for the Scheme, a short term deficit in the Notional Account is not a cause for concern. As a result of this, there is no strong reason to maintain a risk margin in the liability estimates.

4.2.8. Table 3 below sets out the cashflow statement of the Notional Account for 2014-15.

Table 3: Cashflow statement of the Notional Account 2014-15

Income	
ROC support payments (received 30 June 2015)	\$23,569
Notional interest	\$1,035
Expenses	
ROC Commonwealth contributions	\$0
Net cashflow	\$24,604

4.2.9. Table 4 below sets out the balance sheet of the Notional Account as at 30 June 2015.

Table 4: Balance sheet of the Notional Account as at 30 June 2015

Assets	
Cash as at 1 July 2014	\$50,596
Net cashflow	\$24,604
Total	\$75,200
Liabilities	
Incurred but not yet notified	\$42,387
Total	\$42,387

4.2.10. The Notional Account as at 30 June 2015 has disclosed an estimated surplus of about \$33,000. Note again that no account has been taken for possible payments to midwives under division 4 of the Act, should the Scheme be wound up without alternative arrangement being put in place. Based on the data provided by DHS, this amount is around \$75,000 as at 30 June 2015. Generally, the estimated surplus position should be regarded as highly uncertain.

4.2.11. Finally, it is appropriate to provide a benchmark projection of the liabilities of the Scheme. A simple model was developed within this office for the purpose of projecting future liabilities under this Scheme. The table below sets out estimates of the liabilities at the end of each of the next five financial years. The numbers are very small, and there is very substantial uncertainty in these estimates. In effect they are based on an assumption of significantly less than one ROC claim per year up until at least 2017-18. It will be clear that the presence or absence of even a single ROC claim in any year would mean that the actual experience will turn out to be very different from the projected experience.

Table 5: Projected liabilities

Year ending 30-June	Liability	New accrual	Interest cost	Payments
2015	\$42,387			
2016	\$83,363	\$39,216	\$2,543	\$784
2017	\$145,308	\$59,843	\$5,002	\$2,900
2018	\$229,009	\$82,057	\$8,718	\$7,074
2019	\$322,331	\$93,791	\$13,741	\$14,210
2020	\$423,712	\$107,404	\$19,340	\$25,363

4.3 ACTUARIAL MANAGEMENT

4.3.1. Regular review of the costs and notional assets of the Scheme will allow the ROC support payment rate to be adjusted from time to time, if necessary. Consideration of that rate is beyond the scope of this report. This report has described a framework for the valuation of Scheme liabilities and established the Notional Account. It is intended that the valuation and accounting framework be applied at each future annual review of the Scheme.



Peter Martin FIAA
Australian Government Actuary
15 June 2016

APPENDIX 1: RUN-OFF COVER SUPPORT PAYMENTS

A.1.1 ROC support payments are paid to DHS in the form of an annual lump sum imposed as a tax on each insurer (currently MIGA is the only insurer) from 1 July 2010.

A.1.2 The amount of ROC support payments is calculated as a percentage of premium income received from contributing midwives. The calculation rules are set out in the ROCSPA and regulations. The tax imposed on each insurer is the applicable percentage of the insurer's premium income (section 7) for the applicable contribution year ending on 30 June or an alternative date specified in the regulations (section 5).

A.1.3 Under section 7, an insurer's premium income for the purpose is the sum of all of the premiums paid to the insurer for midwife professional indemnity cover provided for eligible midwives by contracts of insurance with the insurer, reduced according to the formula:

Premium income equals

Net premium — Net premium x Applicable percentage ÷ (1 + Applicable percentage)

A.1.4 Net premium is calculated according to section 7 as follows:

- sum of all premiums paid to the insurer during the operation of the Scheme for midwife professional indemnity cover provided for eligible midwives;
- minus the amount of GST payable (subsection (2)(a)) and the amount of stamp duty payable (subsection (2)(b)) in relation to the premiums; and
- plus/minus other payments specified in the regulations.

A.1.5 For premium payments relating to 2014-15, the applicable percentage is specified in the regulations as 10 per cent for all insurers, and thus the ROC support payment will be calculated as net premium x 10 per cent ÷ 1.10.

APPENDIX 2: ELIGIBLE PRACTITIONERS AND RUN-OFF COVER SCHEME CONTRACTS

ELIGIBLE PERSONS

A.2.1 Eligible persons are those who fit one or more of the following eligibility categories at the time the claim (or incident) is first notified to the eligible insurer (section 31(2) of the *Midwife Professional Indemnity (Commonwealth Contribution) Scheme Act 2010*):

- a person aged 65 years or older who has permanently retired from private practice as an eligible midwife;
- a person who has not engaged in private practice as an eligible midwife at any time during the preceding three years. (Note: unlike other categories, eligibility does not occur immediately upon ceasing practice);
- a person who has ceased the person's practice as an eligible midwife because of maternity;
- a person who has ceased the person's practice as an eligible midwife due to permanent disability; and
- a legal representative of a deceased person who had been an eligible midwife.

A.2.2 Eligible midwife means a person who:

- is licensed, registered or authorised to practice midwifery by or under a law of the Commonwealth, a State or a Territory; and
- meets such other requirements (if any) as are specified in the Rules.

PROVISION AND NOTIFICATION OF COMPULSORY RUN-OFF COVER

A.2.3 Under an arrangement in force with the Commonwealth, MIGA is required to notify eligible midwives of their entitlement to run-off cover and then to provide that cover to them.

APPENDIX 3: RUN-OFF COVER SCHEME CLAIMS

A.3.1 The legislation defines claims broadly. Claims need not involve legal proceedings. Claims may include civil claims for negligence, administrative proceedings, disciplinary proceedings (including those performed by a professional body) and inquiries or investigations into conduct (subsection 5(1) of the *Midwife Professional Indemnity (Commonwealth Contribution) Scheme Act 2010*).

A.3.2 A ROC claim is payable to an insurer under section 32 if:

- it relates to incident(s) that occurred on or after 1 July 2010;
- it relates to a person eligible under section 31(2) (see Appendix 2);
- it relates to incident(s) occurring in connection with the person's practice as an eligible midwife;
- the person has midwife professional indemnity run-off cover that indemnifies the person in relation to the claim; and
- the claim would be paid in the ordinary course of the insurer's business.

A.3.3 Where these criteria are met, the Commonwealth is liable to pay run-off cover indemnities regardless of whether the insurer has sought private reinsurance (section 71).

A.3.4 Applications for ROC Commonwealth contributions must be made to DHS (section 58 of the Act). They are paid by the CEO of DHS before the end of the month that immediately follows the month in which the eligible insurer applies for the indemnity (section 59).

A.3.5 If a Level 1 or Level 2 Commonwealth contribution is payable in respect of that payment, the amount of the run-off cover Commonwealth contribution is reduced by the amount of the Level 1 or Level 2 Commonwealth contribution (section 35(2)).

APPENDIX 4: METHODOLOGY, ASSUMPTIONS AND UNCERTAINTY

ASSUMPTIONS

Claim frequency

A.4.1 We have adopted the same assumption as that used for costing the Commonwealth's Level 1 and Level 2 contributions. That is, we have assumed an underlying claim frequency of 1.1 claims per 1,000 births for births in clinical settings. Although I do not regard this assumption as unreasonable, it is clearly subject to a high level of uncertainty.

Claim size

A.4.2 We have adopted the same assumption as that used for costing the Commonwealth's Level 1 and Level 2 contributions; that is, an average claim size of \$227,000 as at 2010. This might be expected to be broadly in line with the average size of claims against obstetricians. We have retained this assumption since we have no available experience data which would suggest it is unreasonable.

Number of midwives and number of births

A.4.3 We have assumed that midwives who manage births in clinical settings will manage 40 births each per annum. This assumption is the same as that used for costing of the Commonwealth's Level 1 and Level 2 contributions.

A.4.4 We have been provided with the actual and expected number of midwives managing clinical setting births from 2010-11 to 2019-20 by the Department of Health. Note that these are the registered practising midwives managing clinical setting births, not midwives who are eligible for the ROC Scheme.

Table 6: Number of midwives managing clinical setting births

Year	Number of midwives delivering babies in clinical settings
2010/11	24
2011/12	37
2012/13	67
2013/14	93
2014/15	114
2015/16	214
2016/17	314
2017/18	414
2018/19	455
2019/20	501

Economic assumptions

A.4.5 Professional indemnity claim costs are assumed to be increasing by 4 per cent per annum. This is intended to be neither optimistic nor conservative. However, over the medium term, it is conceivable that claim inflation could exceed this rate.

A.4.6 Claim payments were discounted at a rate of 6 per cent per annum. This rate provides consistency with the rate adopted in a number of similar contexts and therefore is suitable from a whole of government perspective.

Methodology

A.4.7 The model used for estimation of the future liabilities of the Scheme is based on a model developed within this office, which was used for the costs of the Level 1 and Level 2 Commonwealth contributions. The model assumes a gamma distribution of claim size which varies approximately along the lines as shown in the table below.

Table 7: Gamma distribution of claim size

Size of claim	Proportion of all claims (by number) less than upper bound of band
Up to \$100,000	71 per cent
Up to \$300,000	82 per cent
Up to \$500,000	87 per cent
Up to \$1,000,000	93 per cent

A.4.8 We have assumed that the ROC Scheme will pick up 6 per cent of the total amount of the net cost to the insurer, after the Level 1 and Level 2 contributions are made to the insurer. The model estimates the net cost to be around \$72,000 per claim that is, the ROC Scheme will pick up \$4,320.

A.4.9 Similarly, we have assumed that the ROC Commonwealth contributions will be 6 per cent of the estimated net payment that the insurer will pay, after the Level 1 and Level 2 contributions are made to the insurer.

A.4.10 The new accrual for each of the next eight years is calculated based on the assumptions above. The interest is credited each year to the opening balance of the liability.