

The Chair
Finance and Administration Committee
Parliament House
George Street
BRISBANE QLD 4000

By email: fac@parliament.qld.gov.au

3 September 2012

Dear Mr Michael Crandon MP,

OPERATION OF QUEENSLAND'S WORKERS' COMPENSATION SCHEME

The Insurance Council of Australia (ICA)¹ is pleased to contribute to the Finance and Administration Committee inquiry into the Operation of Queensland's Workers' Compensation Scheme. Please find attached our submission to the inquiry for your consideration.

Our workers' compensation insurer members do not currently operate in the Queensland's Workers' Compensation Scheme. We would like however to provide the inquiry with our members' views on two items of the inquiry:

- The performance of the scheme in meeting its objectives under section 5 of the Act;
- WorkCover's current and future financial position and its impact on the Queensland economy, the State's competitiveness and employment growth.

The Insurance Council and its members look forward to working with the Finance and Administration Committee's inquiry on the workers' compensation scheme in Queensland to enhance its balance between the protection of injured workers whilst ensuring affordability of premiums for employers.

If you have any questions or comments, please do not hesitate to contact Vicki Mullen, General Manager Consumer Relations and Market Development on (02) 9253 5120 or vmullen@insurancecouncil.com.au.

Yours sincerely



Robert Whelan
CEO & Executive Director

¹ The Insurance Council of Australia is the representative body of the general insurance industry in Australia. Our members represent more than 90 percent of total premium income written by private sector general insurers. Insurance Council members, both insurers and reinsurers, are a significant part of the financial services system. June 2012 Australian Prudential Regulation Authority statistics show that the private sector insurance industry generates gross written premium of \$37.5 billion per annum and has total assets of \$118.2 billion. The industry employs approx 60,000 people and on average pays out about \$115 million in claims each working day.

Insurance Council members provide insurance products ranging from those usually purchased by individuals (such as home and contents insurance, travel insurance, motor vehicle insurance) to those purchased by small businesses and larger organisations (such as product and public liability insurance, professional indemnity insurance, commercial property, and directors and officers insurance).



Operation of Queensland's Workers' Compensation Scheme

**Submission by Insurance Council of Australia to
the Finance and Administration Committee**

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Introduction

The Insurance Council of Australia (ICA) provides the following submission to the Finance and Administration Committee concerning the Inquiry into the Operation of Queensland's Workers' Compensation Scheme (Inquiry).

Aside from self-insurers, the Queensland workers' compensation scheme (Queensland Scheme) sits entirely within the control of Government, including regulation, insurance operations, dispute resolution, information collection, scheme-wide return to work and rehabilitation programs and applications for self-insurance. As such our workers' compensation insurer members currently have no involvement in the Queensland Scheme.

However, it is an important part of the ICA's strategic blueprints to promote harmonisation of the benefits and scheme design for workers' compensation insurance so that injury management and compensation systems operate on a stable, predictable, affordable and consistent basis, for the benefit of employers, injured workers and their families. The ICA believes that such schemes can be effectively delivered by the private market with appropriate regulatory oversight.

Various compulsory compensation scheme reviews in Australia and overseas have examined the issue of whether such schemes are more efficient and effective when underwritten by governments (public monopoly schemes) or private insurers. The arguments for and against the involvement of private insurers as underwriters of compulsory compensation schemes are varied and complex.

However, the ICA submits that a leading analysis is set out in the Productivity Commission's Report of 2004 for its inquiry into National Workers' Compensation and Occupational Health and Safety Frameworks as follows:

The literature does not provide a powerful case for either public monopoly or competitive private provision of workers' compensation insurance. However, the Commission considers that, on balance, private provision is preferred on grounds that: private capital is directly at risk; competition in the marketplace is likely to generate incentives for efficiency and innovation; and there is greater transparency of any governmental influence over premiums. Further, the risk of private insurer failure can be reduced by prudential regulation. However, even in competitive schemes, the Commission notes that pressure can be applied to governments as funders of last resort in the case of significant market failure.¹

It is worth noting that the prudential regime for general insurers in Australia has been significantly strengthened in the last decade. The prudential regime will be strengthened again with significant new requirements coming into effect from 1 January 2013. As a result private insurers are required to hold more than sufficient capital to ensure that a privately underwritten scheme is fully funded.

Our submission firstly provides our comments in relation to the financial performance of the Queensland Scheme in the light of the state's current economic conditions. This gives rise to our detailed discussion of the benefits of an alternative private market model that could

¹ Productivity Commission, *inquiry into National Workers' Compensation and Occupational Health and Safety Frameworks Report 2004*, p323

deliver a competitive workplace accident scheme in Queensland. We believe that this would be consistent with the Queensland Scheme's objects to treat workers and their dependents fairly and balance fair benefits with reasonable costs for employers and the community².

In particular the ICA submits that:

- innovation by the private sector in risk rating premiums can improve fairness to employers and is likely to drive changes in employer's risk behaviour as a response to price signals;
- discipline by the private market may also deliver improved effectiveness in controlling claim payments (to be limited to appropriate amounts to only those that are entitled); and
- regulatory powers are likely to be more effectively used in relation to the private sector.

Our submission will highlight the conclusions of a recent report prepared on the performance of the ACC Scheme in New Zealand³ (ACC Stocktake Report) which we believe provides the most recent and comprehensive analysis of the arguments for and against private underwriting.

According to the ACC Stocktake Report, the long term stability and viability of accident compensation schemes is better served by the private sector which can deliver:

- *immunisation from political processes that may reduce Scheme stability and inhibit the pursuit of improved value for money for levy payers;*
- *consumer choice, so that levy payers can respond directly to poor service, inefficient pricing and a lack of innovation;*
- *a wide range of specialist underwriters and service providers who are likely to provide better service in niche markets, including those serving particular ethnic and socioeconomic groups in society;*
- *the transparency that is associated with private providers, including explicit equity capital and reserves to provide a buffer against short-term variations in financial performance.*⁴

Finally, we will provide you with a discussion of some of the most effective features of scheme design that can deliver scheme stability and good health outcomes for injured workers. These views derive from long-standing experience that our members have in underwriting compulsory State and Territory compensation schemes.

As a result the ICA's submission will provide further detail on the issues surrounding two of the matters the motion required the Committee to consider, namely:

- The performance of the scheme in meeting its objectives under section 5 of the Act;
- WorkCover's current and future financial position and its impact on the Queensland economy, the State's competitiveness and employment growth.

² Workers' Compensation and Rehabilitation Act 2003, section 5

³ Accident Compensation Services in New Zealand: The Performance of the ACC Scheme and Opportunities for Improvement. Final report prepared for the Minister for ACC by the Steering Group for the Stocktake of ACC Accounts. 30 June 2010

⁴ ACC Stocktake Report, p5

1. Financial Performance of Queensland's WorkCover Scheme

The Queensland Commission of Audit - Interim Report into Queensland's Financial Position, Public Sector Service Delivery and Infrastructure Program - June 2012 (Interim Report) identified risks from Government Owned Corporation's in terms of the need for potential future contributions from Government to prop up balance sheets.

For many years, Queensland managed its State finances and borrowings better than most. However, due to increased total government gross debt Queensland's AAA credit rating was downgraded during 2009/10. The Interim Report quoted S&P *Queensland's budgetary performance is [now] the weakest of all the Australian States.*⁵

While WorkCover Queensland is a standalone statutory body within the Queensland government, it has also suffered deteriorating financial security - with its funding ratio falling from 183% at June 2007 to 112% by June 2011⁶.

The average 2012/13 WorkCover Queensland premium rate is expected to be \$1.45 for every \$100 of wage roll. While this is an increase from 2009/10 levels (\$1.15) it remains insufficient to fully cover the costs of the Queensland Scheme. (WorkCover reports a breakeven premium of \$1.49 is required to fully fund 2012/13 costs.) The ICA submits that this situation would be far less likely to arise under a privately underwritten scheme. The ACC Stocktake Report suggested that a private insurance model would

*...promote greater transparency in community understanding of the true (actuarially fair) cost of providing accident compensation benefits. Changes in the claims experience of each line of compulsory insurance would be reflected more quickly and more transparently in the premiums charged.*⁷

The Interim Report recommended government examine commercial assets and the total government balance sheet. The ICA would support such a review should it extend to examining the risk and return associated with the sale of WorkCover Queensland to private sector insurers. We believe that moving workers' compensation outside the government sector would be an excellent symbol of a return to superior fiscal management. It would also, according to the ACC Stocktake Report *(t)ransfer the burden of risk-bearing for unforeseen contingencies and unfunded liabilities arising in the future from current levy payers and the Crown to shareholders of the private insurance companies.*⁸

In addition to balance sheet risk, the Interim Report identified that Queensland public sector employee numbers had increased 40% since June 2000 and average wages had increased 16.7% compared to the national public sector average of 12.7% over that same period. While WorkCover Queensland employees are funded by WorkCover premiums, transferring this workforce to the private sector is one small step that government could execute to containing public sector workforce numbers and wage roll going forward.

⁵ Queensland Commission of Audit Interim Report June 2012, p4

⁶ WorkCover Annual Reports

⁷ ACC Stocktake Report, p6

⁸ ACC Stocktake Report, p5

2. Improved Pricing (price signals to influence risk behaviour)

The ICA submits that appropriate risk identification and experience rating of workers' compensation premiums is a desirable outcome for employers and the community. The ACC Stocktake Report noted that:

...experience rating is socially desirable in that it has the effect of focusing the attention of employers on improving safety and reducing accidents. It provides employers with relatively strong incentives because privately underwritten markets respond very quickly to changes in claims experience by adjusting the premium range set.⁹

We believe that a competitive private insurance market fosters innovative risk identification and pricing responses. A single government insurer continuing indefinitely with pricing which does not cover the scheme's liabilities is likely to create inefficient cross-subsidies. Over the course of their investigation, the Steering Committee concluded that ACC levies contained *inefficiently high levels of cross-subsidisation that are affecting financial performance and value for money.*¹⁰ The ICA submits that a private insurer by contrast has a strong incentive not to tolerate loss making business balanced with a commercial requirement to not set prices too high. Thus, we believe that participation by the private insurance market in workers' compensation is likely to improve individual risk rating and drive improvements in safety, incidence rates and rehabilitation and return to work outcomes. Risk and experience rating are economically and socially desirable in that they have the effect of focusing the attention of employers on improving safety and reducing accidents.

3. Improved Effectiveness

Private market insurers are subject to stakeholder forces that ensure real financial discipline is adhered to. Shareholders or other owners expect returns to be made. APRA expects that solvency will be sufficient to cover claimant and policyholder obligations to a very high degree of certainty. These and other balancing tensions safeguard against unsound financial management and ensure that schemes are fully funded.

The ICA submits that private insurers' capital positions are likely to be more stable than public sector insurers. Therefore there is a lower risk of retrospective premium adjustments to post fund eroded solvency and substantial legislative amendment under a private market model of delivery of workers' compensation insurance.

The ACC Stocktake Report suggests that private markets would introduce *...disciplines... precluding the adoption of partially-funded premium levels in response to any extension of benefits or deterioration in claims experience or rehabilitation rates...*¹¹

We submit that a private market model for delivery of workers' compensation would bring

⁹ ACC Stocktake Report, p 113

¹⁰ ACC Stocktake Report, p 125

¹¹ ACC Stocktake Report, p 6

with it more stable funding for the underwriters, at least no greater premium volatility and potentially lower premiums – as indicated in the ACC Stocktake Report.

The evidence available to the Steering Group does not suggest that premiums will rise as a result of the introduction of competitive private delivery, since the margins required to provide insurers with a return on capital are modest compared to the improvements in the efficiency of premium-setting, and the improvement in accident and rehabilitation rates that could be expected with private delivery.¹²

The ACC Stocktake Report goes further suggesting that competitive private delivery of compulsory insurance would be likely to:

...allow competition between insurers and specialist service providers to focus the performance of the compulsory insurance system on investment in accident prevention and rehabilitation in part through the creation of a wider range of options for the use of discounts for investment in accident prevention and experience rating to impact on the premiums actually paid.¹³

The ICA believes that better outcomes for injured workers would result from private insurer involvement in underwriting the Queensland Scheme.

4. Improved Regulation and Governance

The ICA supports strong regulation of both workplace health and safety and workers' compensation insurance operations. We believe that a co-ordinated approach to regulation of these functions should lead to improved workplace injury incidence rates, return to work and rehabilitation outcomes.

The ICA argues that a government regulator can be more effective in dealing with the private sector. Guiding insurer behaviour and effective scheme management as a whole is better served by an arrangement whereby the government - through the Workers' Compensation Regulatory Authority (trading as Q-COMP) - regulates the private sector.

In addition to more effective regulation of the scheme, the ACC Stocktake Report identified the benefits that private insurance within compulsory insurance markets brings to internal governance and monitoring discipline. The Steering Committee notes that these arrangements:

...will benefit from the expertise and technology of the private sector in the delivery of accident compensation services. The retention by the government of the power to determine the scope of, and benefits provided by, the ACC Scheme, and to enforce compulsion in the payment of levies, is sufficient to deal with the legitimate interests of the Crown in the ACC scheme.¹⁴

¹² ACC Stocktake Report, p 5

¹³ ACC Stocktake Report, p6

¹⁴ ACC Stocktake Report, p143

The ICA believes that the above statement would be supported by a clear statement of the intentions and objectives of legislation under which the private sector must meet its obligations.

To that end, and in the context of comparison to scheme arrangements in other Australian jurisdictions, the ICA submits that key objectives of reducing the number of the workplace accidents and disease, and promoting prompt return to work outcomes are not addressed as explicitly in the objectives of the Queensland legislation as they are in the legislation of other jurisdictions. We believe that one of the key tenets for the success of workers' compensation schemes is that objectives of legislation are clearly laid out in plain language and in that way can be monitored and measured against.

It may be worthwhile revising the objectives of the Workers' Compensation and Rehabilitation Act to specifically address return to work and injury prevention. The ICA notes that recommendation 5.1 of the 2010 Structural Review states that *Return to work and rehabilitation should be a primary object of the WCRA*.

5. Features of Scheme Design

The ICA's members do not operate in the Queensland Scheme. However we would like to provide the Inquiry with the benefit of our members' experience in other workers' compensation schemes across Australia. ICA members underwrite the workers' compensation schemes in Western Australia, the Northern Territory, Tasmania and the ACT. They also operate as scheme agents for the workers' compensation schemes in NSW and Victoria.

As a result of this experience the ICA submits that the following scheme design features are most likely to enhance scheme stability and effectiveness, and to deliver fair levels of benefits to injured workers:

- **A competitive market** – This requires moving away from the sole underwriter and/or sole service delivery model. A competitive market is likely to encourage timely innovative practices to achieve scheme outcomes and to identify and respond in a timely fashion emerging issues;
- **An appropriate balance** between premium affordability for employers and levels of benefits to injured workers;
- **Early access for injured people to medical treatment and rehabilitation** – early medical and rehabilitation intervention is vital to achieve safe, durable return to work. The success of this component does depend on the ability of employers, workers, medical, rehabilitation service providers and insurers to work closely together to achieve scheme outcomes. Incentives or enhancements to encourage this focus are vital.
- **A focus by all scheme service providers on health outcomes** (rather than a focus on maximising compensation) – this requires focussing the culture on work capacity as opposed to work incapacity. The success of this component requires various strategies. First, the ability of the insurer to provide strategies to assist employers to prevent work injuries in the first place. If an injury does occur, then timely medical and rehabilitation intervention with the aim of early return to suitable duties. As stated previously, for this to be successful, this does require close and meaningful collaboration between employers, workers, medical, rehabilitation advisors and insurers.
- **A framework that inhibits volatility** and reduces friction costs such as legal fees, and superimposed inflation;

- **Access to a rapid and cost effective dispute resolution process;** and
- **Permanent impairment thresholds** to provide a reasonable balance between access to common law benefits for the most seriously injured and scheme affordability for employers. We believe that unrestricted access to common law benefits is not conducive to early medical and rehabilitation intervention and early return to work. We submit that this is the result of the focus spent on proving fault and seeking damages would be better utilised in focussing on medical and rehabilitation intervention and early return to suitable duties.

The ICA submits that the overall success of a workers' compensation scheme in respect to the above points is dependent on scheme design that promotes and links workplace safety, a culture of work capacity as opposed to work incapacity with collaborative and meaningful work between employers, workers, medical, rehabilitation service providers and insurers to return workers to early, safe and durable work.

With the Australian employment market constantly changing, businesses need to be competitive in order to be able to grow across national jurisdictional borders. Increasingly, workers will need to follow employment opportunities. With this in mind, we believe that the Queensland Scheme will need to encourage business competitiveness and growth and the placement of workers in suitable positions, where they arise. The ICA submits that by harmonising key aspects of the Queensland Scheme with other jurisdictions, this will reduce barriers to businesses from the multi-jurisdictional regulatory burden of complying with multiple state and territory workers' compensation laws.

Conclusion

The ICA recommends that the Queensland Government considers the introduction of competitive delivery of Queensland's workplace accident insurance by the private market for:

- enhanced regulatory effectiveness
- more efficient and effective execution of Queensland Scheme objectives;
- improved social and financial outcomes; and
- addressing financial risks associated with the Government balance sheet and public sector workforce.