COMPAS

WORKERS COMPENSATION AND OH&S NEWSLETTER

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In this Issue

Bad Policy Decisions Marr WorkCover Performance

The new Minister for WorkCover, John Della Bosca, could be forgiven for thinking that he has inherited a poisoned chalice. Not only has the WorkCover system run into massive debt, it has been plagued by a succession of bad policy decisions and now fails to meet its own objectives.

Workers compensation is an employer funded social welfare system set up to provide genuinely injured workers with reasonable benefits at an affordable cost.

The Government's own inquiry into the WorkCover system (Grellman 1997) and most other observers have recognised that major structural change is needed if the system's objectives are to be met.

Over the last decade a number of vested interests have been allowed to influence the way that the system operates to collect premiums and pay claims and scheme liabilities now exceed assets by more than $2 billion. These vested interests are predominantly scheme stakeholders such as employers, unions and insurers but successive Governments have also been receptive to submissions from service providers such as lawyers and doctors and changes to bring the scheme under control are long overdue.

One of the system changes that must be made is to align all of the financial incentives which operate within the system, another is to change the dispute resolution mechanism. Changes are needed in the way that claimant and employer fraud is dealt with, estimated to cost the system at least $400 million each year. The benefit structure is a hotchpotch of statutory entitlements and common law and desperately needs to be realigned to match the system's objectives. Over-servicing by provider organisations is rife and seemingly uncontrolled.

But even if all of the changes are made, the underlying poor performance of NSW employers in risk management will continue to bring the system down. Changes are urgently needed in the manner by which workplace safety is regulated to raise standards to those enjoyed in Europe and the USA.

Delaying change is irresponsible and bad policy. The deficit of fund assets over liabilities continues to grow as a result and NSW employers of the future will suffer when the bill finally must be paid.

Premiums Unrepresentative of Risk Exposure

The succession of bad policy decisions over WorkCover is not restricted to the Carr Government. The Coalition began the rot when it first fixed premiums for political purposes. To give it its due, the WorkCover Board has advised its various Ministers that artificially fixing premiums is bad policy and should be discontinued, yet none have heeded that advice. NSW now has a system with accumulated debts of over $2 billion, all of which will have to be repaid by future NSW employers.

According to the Auditor General①, the WorkCover debt will rise to $3 billion by 2004 whilst ever the system remains unchanged. If this does eventuate, rating agencies will no doubt take another look at NSW credit worthiness.

The Government has been convinced that NSW employers could not afford premium rates higher than an average of 2.8% of wages. This of course is a nonsense because so few NSW employers actually pay the average rate. Many employers, (construction firms, meat processors, manufacturers etc) pay up to 30%, conversely, most industries pay less.

Citing a comparison of the average costs of workers compensation in other States, employer lobby groups conveniently ignore the facts that legal costs, employer premium avoidance schemes and cost shifting to the Federal Social Security system are significant influences on scheme costs. These influences exist in other jurisdictions to a greater or lesser extent than they do in NSW and valid comparisons of scheme costs are extremely difficult.

In 1999 - 2000 the average cost of the Victorian system was 1.9% of wages②. Victoria has an employer excess on claims of 10 days, low statutory benefits, no common law, limited legal costs and it shifts much of its costs to the Federal system. NSW has an employer excess on claims of 5 days, significant employer premium avoidance, high benefits, common law and massive legal costs. Continuing to collect less in premiums than is paid out in claims through artificially pegging the average premium rate at 2.8% is irresponsible and simply bad policy.

Common Law Claims Explosion

When the WorkCover system was established in 1987, access to common law action was abolished. In changes made in the early 1990s common law was reintroduced but access was modified with the intention of filtering out all but the seriously injured cases. Thresholds were set which included a 33% impairment before an action could commence. In another example of bad policy, this threshold was reduced to 25% by the then Minister for Industrial Relations, John Fahey.

When the current NSW Government capped the Statutory WorkCover Benefits for permanent injuries at $100,000, it obviously did not consider the ramifications of this cost cutting exercise. These ramifications have manifested in a significant growth in the number of common law claims.

Insurance industry sources have indicated that common law claims grew by 25% in 1999 and at December represented 16% of claims costs up from 12% in May.

In 1995 common law claims represented approximately 2% of the total.

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NOTES

① Auditor General's Report to Parliament 1999 Vol 3 Page 500

② Heads of Workers Compensation Authorities Comparison of Workers Compensation Arrangements in Australian Jurisdictions January 2000

Common Law Claims Explosion

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Minister Della Bosca made much of the changes he introduced to cut the costs of Greenslips, one of which was to modify the operation of common law. The effect of this change makes common law action for motor vehicle accident claims now less attractive compared with workers compensation common law. This is already expected to shift actions involving work related motor vehicle accidents (either journeying to and from work or at work) into the workers compensation jurisdiction. The explosion in the numbers and costs of common law claims for whatever reason (political interference or claimant behaviour) puts further financial pressure on the workers compensation system by adding to the already massive deficit.

The employment sector most likely to be hardest hit by the explosion in common law is the Government itself and therefore the taxpayers of NSW. A very worrying trend is the emergence of a growing number of common law claims for psychological (stress) injuries. The Government employment sector is where the majority of stress claims occur as could be expected, with employment involving public service in Health, Police, Child Welfare and Education.

The Government has been advised to raise the impairment threshold for common law claims back to 33% but has so far failed to act. Changing the threshold however is unlikely to control the costs of common law claims. What is needed is the introduction of a system of structured settlements of claims with annual reviews. This would be fairer to the injured worker as they are less able to fritter away an award, and fairer to the compensation payer as they can ensure that the disability in question is ongoing and warrants support.

Aligning the Financial Incentives

The single change needed to have the greatest effect on the financial operation of the workers compensation system is to apply financial incentives to all participants which encourage improved performance. Currently, incentives are applied to employers via the premium methodology, but these are grossly flawed by the rating system and its cross subsidies. Incentives are applied to claimants via the benefits structure being linked to early return to work but these are frustrated by the antics of the Compensation Court and recalcitrant employers. Incentives are applied to insurers via their remuneration structure but again these are ineffective and in many cases unachievable by insurers.

Not only is the WorkCover system charging a lower premium rate than represented by the risk, but cross subsidies are rife. The current system uses a rating methodology developed originally in 1917, and even though the Government's own 1997 inquiry recommended that a new rating system be introduced, nothing has yet eventuated. The cross subsidisation in the system means that safe employers pay for their unsafe competitors and whilst the unsafe employers continue to get away with not paying for their poor performance, they will never lift their game.

The mechanism which would provide the necessary incentives has already been determined and was contained in legislation introduced into the Parliament in 1998. It involves the transfer of the workers compensation risk

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Aligning Financial Incentives

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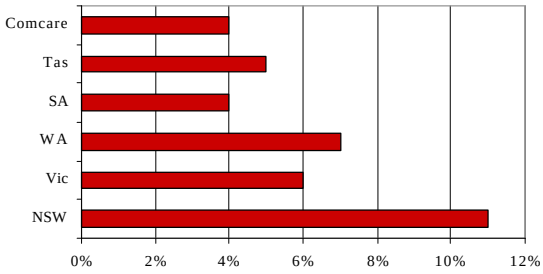
to private insurers through a controlled system of competitive underwriting. The system proposed would have meant that insurers take the risk rather than WorkCover and a new rating system would be introduced which would remove cross subsidies.

By deferring private insurance since 1998 the Government has cost NSW employers over $500 million. This is bad for the economy and plainly a bad policy decision.

Legal Costs Highest in NSW

Another bad policy perpetuated by Governments is the entrenchment of the legal profession in the WorkCover system. Cynics might say that this has a lot to do with many WorkCover Ministers being lawyers themselves. NSW WorkCover is a no fault scheme, yet it has the highest involvement by the legal profession of any Australian workers compensation jurisdiction①. To give the legal involvement context, insurance companies are paid up to $180 million (approximately 9% of system costs) each year to administer the system, doctors are paid $160 million, lawyers are paid $240 million②.

LEGAL FEES AS % OF ALL PAYMENTS



Rather than fix the dispute resolution mechanism by introducing binding medical panels and the like, the Government introduced another layer of lawyer involvement when it set up the Workers Compensation Resolution Service.

The WCRS was intended to conciliate claims disputes and keep them out of the Courts. Claimants and insurers should have been able to appear before an impartial arbiter who would have assisted an agreed resolution of the dispute.

The Government decided that before Court action could commence every disputed claim must go before the WCRS and of course it wasn't long before lawyers inserted themselves into the process at around $2,500 a time. So far, the WCRS has been able to successfully conciliate less than 20% of the matters referred to it. Typically WCRS considers over 2,500 disputed claims each month and rejects half because they are unsuitable for conciliation or add unbearably to WCRS's workload. Of the remaining 1,000 or so claims only 500 are resolved at conciliation.

Much of the $240 million paid to lawyers each year could be paid to injured workers and take some of the financial pressures off the system. This will only be possible if the Government introduces a dispute resolution mechanism which does not rely on the Courts and will be the most difficult of the changes to achieve.

NOTES

① Source - PwC

② Source - NSW Workers Compensation Statistical Bulletin 1997/98, WorkCover Annual Report 1999

WorkCover Fraud

In the USA the National Association of Insurance Commissioners estimate that 10% -20% of all insurance claims are fraudulent. The California State Compensation Insurance Fund estimates that fraud accounts for up to 25% of workers compensation costs.

In a survey conducted by the Insurance Council of Australia, one in four Australians admitted to knowing someone who had committed a fraud on an insurance company. Insurers are fair game - workers compensation in NSW is regarded as insurance.

Employee Fraud

The incidence of staged claims in NSW workers compensation is believed to be very low. Insurers claim to be assiduous in determining liability and in recent times there have been very few if any prosecutions for fraudulently staging a claim.

But fraud means obtaining a benefit by false representation and like it or not, any claimant who exaggerates the extent of his/her injury is guilty of fraud. Whilst there is no empirical evidence to prove the extent of fraud by exaggeration, it is widely estimated within the workers compensation insurance industry to represent at least 10% of claims costs, ie $200 million each year.

Insurers and other stakeholders have recommended scheme reforms to the Government which address the fraud by exaggeration issue. These recommendations have largely been ignored.

In workers compensation, the anecdotal evidence is that many doctors are, or have been guilty of aiding and abetting fraud through exaggeration. Most don't see it that way, they are acting on their judgment which is based on a combination of factors.

Some however, appear to have done so deliberately in order to maintain their business relationship with their patient. The workers compensation system does not hold the doctors accountable, they are never pursued through the Courts because exaggeration of a symptom is very hard to detect.

To be fair to the doctors, they are in an invidious position when they see a workers compensation patient. Much of their diagnosis is history based, they only have the claimant's side of the story to go by. In many injuries (stress, sprains, strains) there may be no signs of injury whatsoever, the doctor only has symptoms to go by and these are in the hands (minds) of the claimant.

Insurers and other stakeholders have recommended ways of minimising the potential for fraud by exaggeration. Developing treatment protocols is one of the best. Best practice protocols for various injuries are developed using evidence-based medicine. These are used by GPs in their management of claimants and the compensation payer audits treatments against the protocols and monitors recovery times against those expected. Some of these protocols have been in place in South Australia and Victoria for a number of years.

What is more common in workers compensation is fraud through non-disclosure. In these cases, claimants recover either partially or fully but do not tell their doctor, they lie about the extent of their disability. Insurers claim that they constantly monitor a claimant's progress towards recovery and return to work using medical and physical surveillance.

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Employee Fraud

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In many cases, concealing the extent of the disability is part of a legal strategy, recovery will affect the size of an award so that there is little motivation to return to work in litigated claims.

Every opportunity to prosecute claimants found to be defrauding the system is taken and widely publicised. For some examples of cases of successful fraud prosecutions, visit the WorkCover web site at www.workcover.nsw.gov.au.

Employer Fraud

A major incidence of fraud, is that which is committed each year by employers who deliberately under declare the wages paid to employees thereby avoiding paying their full premium. In one industry alone (Construction) under declaration is admitted by peak industry bodies to be at least 30%. In the wider employer community fraud by under declaration is believed to be at least 10% of the total premium ie. $200 million each year.

Insurers are required by the WorkCover Authority to audit their customers to ensure that the correct wages are paid but a strong legislative force does not support these audits. The rate of detection of fraud by under declaration is low and the fines applied by the Courts are inconsequential. Anecdotally, many employers deliberately run the risk on non-insurance of workers compensation because the penalties when detected and prosecuted are much less than the premium avoided.

A perfectly legal employer mechanism used to avoid paying a premium which represent the risk, is setting up a trust to take advantage of loopholes in the workers compensation legislation. Another legal means is to split the employer into a number of smaller companies and thereby take advantage of the Two Times Rule.

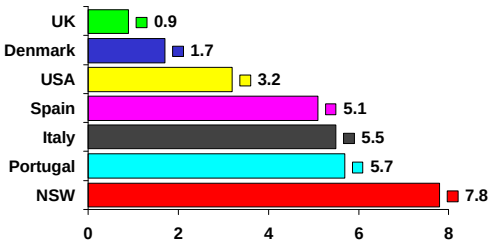
The Government has been aware of these and other premium minimisation schemes for a number years but has so far been reluctant to close all of the loopholes.

NSW Injury Prevention Record

NSW has an unenviable record when it comes to work related fatalities. On average we kill 3.4 workers each week in work related accidents. Our fatal injury incidence rate per 100,000 employees stands at 7.8, in the UK it is 0.9.

In NSW 270 employees are permanently disabled every week. Each year 6,500 are so badly injured that it takes over 6 months for them to fully recover from their work related injury.

FATAL INJURIES PER 100,000 EMPLOYEES



Source: NSW Statistical Bulletin 1997-98
UK Health and Safety Executive

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Sadly all too few employers are responsible for these appalling injury statistics.

It has been estimated that about 450 employers in NSW are under-performing by at least 20% compared to the average for their industry. There are approximately 320,000 employers in NSW covered by WorkCover, the poor performers represent 0.15% of the numbers yet account for an estimated 20% of the costs.

The WorkCover Authority has identified the poor performers and has recently implemented a strategy to force them to lift their game, the problem being that the process is amazingly slow.

Medical Practitioners Frustrate Injury Management

The Nominated Treating Doctor is the gatekeeper in the early return to work of an injured employee because the evidence of an injury needed to lodge a workers compensation claim is usually in the form of a medical certificate. It is the injured worker's responsibility to provide a medical certificate which conforms to the legal and other requirements.

The workers compensation medical certificate should be completed fully and legibly. Obviously decisions to accept or reject a medical certificate should be tempered with realism. If there is little doubt about the nature and circumstances of the injury, or the injured worker returns directly to work, then an incomplete certificate could be overlooked.

Doctors are notorious for their refusal to communicate with employers about their patients and many seek to hide behind the veils of patient confidentiality, the medical system per se or they are ignorant of their role in workers compensation.

The Workplace Injury Management and Workers Compensation Act and the NSW Medical Board have given employers some powerful tools to use when dealing with the medical profession for workers compensation purposes.

The NSW Medical Board has published a set of guidelines for doctors to use when issuing medical certificates, and the Act now requires medical practitioners to provide specific information for workers compensation purposes.

For example, the Medical Board Guidelines state that "The certificate should be legible, and should not contain abbreviations or medical jargon.

The Guidelines published by WorkCover clearly indicate that it is not the role of the doctor to decide what duties a patient can or can not do. The doctor's role is to determine the restrictions which would apply if the worker returned to work on altered (suitable) duties and to facilitate that return.

Employers should not hesitate to contact the treating doctor to clarify issues. Doctors are paid to provide telephone advice as part of the claims cost. They are also fully compensated for completing the WorkCover Medical certificate properly. In the past, doctors have been allowed to get away with frustrating the return to work process or not fully cooperating.

Where the treating doctor refuses to cooperate with the injury management process the employer should advise him/her that his/her conduct will be reported to the NSW Medical Board or WorkCover. The employer must then report the doctor to the appropriate authority.

Rating Bureau Premium Rates Comparisons

The most recent Rating Bureau Premium Methodology was deemed to be approved by the WorkCover Board in late June 2000. The Rating Bureau is required to develop a premium system which would be used in the event that private insurance is ever introduced. The table below shows a comparison between the WorkCover premium rates and those which would be used by private insurers to calculate a premium under the proposed controlled competitive insurance system.

The Rating Bureau makes no allowance for the added costs an insurer would incur in a competitive market place and a factor of 20% - 25% might be used for guidance.

NOTES

① WCA refers to the industry rate which applied in that policy year

② Y2K includes the effects of A New Tax System estimated to be approximately 12%

③ This is the % change of Y2K over Y1999

④ ANZSIC is a Standard Industrial Classification System which enables industries to be classified under 17 broad headings and further broken down into more than 500 industry segments

⑤ The Rating Bureau developed a differential rating system dependent on the size of the employer. The Medium employer (between $10,000 and $500,000 premiums) rate is shown here

Industry	Tariff Rate	WCA 1991 ①	WCA 1998	WCA 1999	WCA 2000 ②	% INC ③	ANZSIC Code ④	RB MR ⑤
Abattoirs	501	8.40	13.36	13.36	15.02	12	2111	20.10
Aged Care Hostels	515	1.15	5.57	5.57	7.19	29	8721	4.70
Barber Shops	540	0.80	1.58	1.82	2.35	29	9526	2.30
Biscuit Mfg	546	3.10	2.77	2.41	2.71	12	2163	4.10
Building	568	5.60	9.36	9.36	10.52	12	4111	5.20
Butchers	573	2.60	7.36	6.40	8.27	29	5121	8.00
Car Sales	786	0.80	1.82	1.82	2.35	29	5311	1.50
Carrying, Carting	583	4.60	8.36	8.36	9.4	12	6110	6.00
Child Care Services	595	0.55	1.58	1.82	2.35	29	8710	3.00
Cleaning	603	2.60	7.36	8.36	10.52	26	7866	9.50
Clothing	607	2.60	3.66	4.21	5.44	29	2241	3.60
Councils	621	3.10	5.57	4.84	5.44	12	8113	4.70
Doctors	641	0.25	0.79	0.79	1.02	29	8621	0.60
Dry Cleaners	644	2.10	4.21	4.84	6.26	29	9521	4.70
Engineering (Heavy)	760	5.60	8.36	8.36	9.4	12	2741	6.70
Engineering (Light)	914	4.21	4.21	4.21	4.73	12	2759	5.50
Engineering (n.o.c.)	657	3.80	6.40	6.40	7.19	12	2949	3.30
Financial Institutions	666	0.25	0.52	0.52	0.58	12	7321	0.30
Foundries (Ferrous)	675	6.90	10.36	10.36	11.64	12	2712	4.10
Furniture Mfg	682	3.1	6.40	6.40	8.27	29	2929	4.70
Hospitals	708	2.60	3.66	3.66	3.57	- 2	8611	2.80
Hotels	710	1.70	2.77	2.77	3.57	29	5710	3.30
Ministers of Religion	784	0.65	1.04	1.04	1.35	30	9610	0.90
Paper Converting	808	2.60	3.66	3.66	4.11	12	2411	3.10
Printing	833	1.40	2.41	2.41	2.71	12	2412	2.60
Prof: Equipment Sales	835	N/A	1.38	1.38	1.17	- 15	4612	0.60
Quarries	838	3.10	7.36	6.40	7.19	12	1411 20	9.40
Residential Care Servs	842	N/A	1.82	2.09	2.71	30	8722	3.90
Retail Shops	847	1.40	2.77	3.18	3.57	12	5111	6.50
Sawmilling	862	8.40	15.36	15.36	17.26	12	2311	13.10
Schools	614	0.55	1.58	1.38	1.55	12	8422	0.90
Stevedoring	893	3.80	5.57	4.84	5.44	12	6621	4.20
Tailors	902	1.70	2.77	2.77	3.57	29	2249	3.80
Tobacco Mfg	913	1.70	2.41	2.09	2.05	- 2	2190	0.90
Undertaking Services	923	2.60	4.84	4.21	4.11	- 2	9524	2.40
Welfare Organisations	945	0.25	1.58	1.82	2.35	29	8729	2.90
Wine Making	947	3.80	3.66	3.66	4.11	12	2183	3.90
Woodworking n.o.c.	955	3.80	6.40	6.40	7.19	12	2329	5.90