



Institute of Actuaries of Australia

# IMPLEMENTING LEGISLATIVE REFORM: THE SOUTH AUSTRALIAN STORY

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# **IMPLEMENTING LEGISLATIVE REFORM: THE SOUTH AUSTRALIAN STORY**

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### **Abstract - Implementing Legislative Reform: the South Australian Story**

To discuss the process and management of recent legislative reform of the South Australian workers compensation scheme and its resultant benefits. To provide some lessons learnt in the implementation of legislative reform as a method of altering scheme design.

On Tuesday 17 June 2008 an Act was passed by the South Australian Parliament significantly amending the *Workers Rehabilitation and Compensation Act 1986*. This Amendment Act, which was based on the recommendations within the Clayton-Walsh Review, followed considerable discussion, debate and dissent. Relations with stakeholders were strained and WorkCoverSA was under pressure to implement and bed down the legislative reform. Whilst the journey to the passing of the Amendment Act was interesting, the process of implementing legislative change was revealing.

For WorkCoverSA to deliver the changes as quickly as possible, whilst managing the risks of implementation and allowing sufficient time for the establishment of key systems and consultation, a staggered implementation plan was developed. A dedicated implementation team was established to keep the myriad of changes on track.

Although WorkCoverSA's independent actuary has stated that it will take several years for the full effects of legislative reform to be observed and reflected in our claims liability valuation, the Amendment Act requires the Government to instigate an independent review of the impact of the program of legislative reform as soon as practicable after 31 December 2010.

Implementation of such significant legislative reform has taken up considerable time and concerted effort. There have been difficulties along the way and the timetable for implementation became increasingly demanding, yet the commitment and belief remains that without these changes the scheme would become unsustainable. WorkCoverSA remains committed to improving the Scheme's performance in the long term through improving return to work. It is too early to see the financial and return to work benefits of legislative reform but WorkCoverSA is confident that the anticipated financial and cultural benefits will be realised.

**Key words:** scheme design, legislative reform, implementation, benefits realisation.

## **1. Introduction**

WorkCoverSA is a statutory authority which administers a compulsory no fault workers compensation scheme in South Australia. The primary objective of the scheme is to rehabilitate and return injured workers back to safe employment and the community.

It is funded by levies collected from employers, generating revenue to pay for all expenses within the scheme.

WorkCoverSA administers two Acts of Parliament: the *Workers Corporation Act 1994*, which establishes the Corporation and the Board and sets out their functions and powers; and the *Workers Rehabilitation and Compensation Act 1986*, which establishes the compensation and rehabilitation scheme and sets out the rights and obligations in relation to injured workers and employers.

On 17 June 2008, the South Australian Parliament passed the *Workers Rehabilitation and Compensation (Scheme Review) Act 2008* (the Amendment Act). This made significant legislative changes to the *Workers Rehabilitation and Compensation Act 1986* and thus to the WorkCover Scheme.

A number of provisions within the Amendment Act were suspended “until dates to be fixed by subsequent proclamation”. The majority of these sections have since been proclaimed on 2 October 2008, 1 January 2009, 1 April 2009 and 1 July 2009.

As at 1 July 2009, most of the Amendment Act has commenced and the implementation of the changes by WorkCover is well underway. Benefits are being seen through the early indicator statistics and through financial improvements in the scheme.

## **2. The need for change**

The South Australian Workers Rehabilitation and Compensation Scheme had largely remained unchanged since it began operation in September 1987.

By 2006, the almost 20 year old Scheme had been modified from time to time, however, the fundamental structure of the Scheme, and how it delivered its objectives in South Australia’s changing social and economic environment, had not been reassessed.

Other jurisdictions have regularly updated and reviewed their schemes’ legislation in line with changes to business, social, environmental and scheme costs.

Over a number of years the South Australian scheme had been under-performing on important indicators, including return to work rates for injured workers, the development of a lump sum culture and, the level of employer levies.

Prior to the process of legislative reform, significant changes to the management of the scheme were commissioned, including the appointment of a new WorkCover Board, the appointment of a principal legal provider and the appointment of a sole claims agent.

WorkCoverSA's unfunded liability at 30 June 2006 was \$694 million and the analysis provided to the Board indicated that without rapid and significant improvement in return to work rates and a movement away from a lump sum culture, the Scheme could not expect the funding position to improve within a reasonable time frame.

A major factor to WorkCoverSA's growing unfunded liability was the increased length of time people remained on the scheme. Long term claims involving payment of income maintenance ('weekly claims') represented nearly 30% of all ongoing WorkCover claims and a very significant part of its claims liability. This was reflected in the return to work rate based on industry collected statistics. For 2005/2006, the return to work rate in South Australia, as measured by Campbell<sup>1</sup>, at 78% was the lowest of the Australian jurisdictions and compared with the national average of 87%.

All of these factors combined to make it clear that the Scheme needed to undergo significant change to deliver a fair, sustainable and fully funded scheme with return to work as its critical focus.

### **3. WorkCover Board proposal**

In 2006 the WorkCover Board reviewed other rehabilitation and compensation schemes in Australia and New Zealand to gauge where the South Australian legislation was out of alignment, particularly where there was evidence of better return to work performance. The WorkCover Board identified that there was an opportunity to make changes to the Scheme to improve return to work outcomes without undermining the achievement of a reasonable balance between the interests of employers and workers or the provision of fair compensation for work-related injuries.

Following this review, in November 2006 the WorkCover Board made recommendations to the SA Government for legislative change to enable the Scheme to improve the return to work rate in South Australia, to restructure levy rates, to minimise legal costs through disputation and to reduce disputes over opinions of medical experts.

The proposals were formed with the view that substantial increases in the return to work rate could be achieved by the significant curtailing of the entitlement to negotiate redemptions, the effective combination of strong claims management, including rehabilitation services and employment placement, and properly timed and targeted financial (dis)incentives for injured workers who have capacity to return to work.

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<sup>1</sup> Campbell: HWCA Australia & New Zealand National Report 2005/2006 located [http://www.hwca.org.au/reports\\_rtw.php](http://www.hwca.org.au/reports_rtw.php)

The proposed changes also dealt with other matters which the WorkCover Board considered deterred return to work such as dispute procedures and disputes over medical issues, as well as reforming the payment structure for non-economic loss to bring them into line with other jurisdictions.

The WorkCover Board's proposals for change included:

- reducing initial weekly income maintenance payments to injured workers and further reducing those payments after 13 weeks to 75% of the worker's average weekly payments
- changing the two year work capacity review to limit income maintenance to an eligible injured worker to a maximum of 75% of the workers average weekly earnings and to cease income maintenance to workers who have not returned to work to their assessed capacity
- capping entitlements to medical expenses to 12 months after cessation of income maintenance
- increasing the maximum payment to injured workers for non-economic loss from \$219,425 (including the supplementary payment) to \$363,660
- removing arbitration and appeals to the Full Bench of the Workers Compensation Tribunal as part of an expedited dispute resolution procedure and allowing appeals to the Supreme Court on matters of law only and by leave of the Court
- appointing independent medical panels in lieu of the Tribunal to make final and binding determinations about disputes over medical questions, including the nature of the injury, the capacity for work, assessment of suitable employment, assessment of the degree of permanent impairment and loss
- limiting solicitors' capacity to charge injured workers and making solicitors personally liable for costs incurred as a result of fault or failure by the solicitor
- ceasing income maintenance until disputes are resolved with arrears and interest paid to the worker where the dispute is resolved in favour of the worker
- decreasing the period of notice required to an injured worker over the cessation of income maintenance in the first year of the claim period
- increasing the period of notice required to an injured worker over the cessation of income maintenance in the second and subsequent years of the claim period
- raising the 7.5% levy cap to 15% to limit the cross subsidisation of higher risk industries by lower risk industries
- increasing the minimum levy from \$50 to \$200 and removing the requirement on employers to register and pay the levy where annual employee remuneration is less than \$10,000
- requiring the levy to be paid in advance, not in arrears
- strengthening controls over participation as a self insurer where businesses have restructured corporate arrangements or otherwise downsized.

These proposals were provided to the South Australian Government at the end of 2006, and in March 2007 the Government announced a review of the Scheme, which would include a review of the WorkCover Board's Recommendations.

#### **4. Clayton-Walsh Review**

The Government, with the support of the WorkCover Board commissioned two independent experts to review and report on the proposals of the Board, to consult with employee and employer organisations and make recommendations to Government about the adoption of the proposals and any modifications or alternatives to those proposals.

The two independent reviewers were: an independent research consultant working in accident compensation and injury prevention - Alan Clayton, and an actuary and partner at PricewaterhouseCoopers - John Walsh.

The terms of reference of the review stated that any changes to the Scheme should be directed towards three objectives, namely:

1. Injured workers should receive fair financial and other support that should be delivered efficiently to enable the earliest possible return to work.
2. The average employer levy rate should be reduced from 3.00% and contained within the range of 2.25% to 2.75% by July 1, 2009.
3. The scheme should be fully funded by the earliest possible date.

After extensive analysis and stakeholder consultation, including a supplementary list of (predominantly technical) proposals provided by the WorkCover Board, the Clayton-Walsh report was provided to the Government at the end of 2007.

The 65 Clayton-Walsh recommendations reflected a large proportion of the November 2006 WorkCover Board proposals as well as additional legislative, non-legislative and policy recommendations.

Alan Clayton stated at the time, that “If the full range of recommendations set out in this Report were to be implemented, South Australia will retain its position as the fairest workers compensation scheme in the country.”

The recommendations included:

- maintaining weekly payments at 100% of pre-injury average weekly earnings with a step down to 80% after 13 weeks
- the adoption of a modified work capacity test for injured workers on weekly payments at two and a half years after the injury occurred
- increasing the maximum in the lump sum payment for non-economic loss for injuries to \$400,000
- a maximum payment of \$400,000 for death arising from a work injury, with counselling to be available to family members of the deceased
- larger employers must appoint accredited rehabilitation and return to work coordinators
- forming an inspectorate within WorkCover to ensure employers are supported to meet their obligations to assist injured workers to return to work
- the establishment of a Return to Work fund to fund rehabilitation and return to work programs and initiatives
- the establishment of a Code of Workers’ Rights
- the establishment of a WorkCover Ombudsman to investigate complaints about the handling of claims and systemic issues within the Scheme.

There were a number of other recommendations relating to the determination of medical disputes, provision for increased legal costs, arbitration arrangements and other matters all directed towards the efficient handling of claims and resolution of disputes.

It was anticipated that had the initiatives in the report been undertaken, in accordance with the terms of reference, the scheme would have been fully funded within five to six years, with a reduction of the average levy rate in the range of 2.25% to 2.75% from 1 July 2009.

The report was tabled in Parliament on 26 February 2008, and the *Workers Rehabilitation and Compensation (Scheme Review) Amendment Bill 2008* (the Bill) was subsequently introduced in Parliament on 28 February 2008, reflecting the recommendations of the Review.

The *WorkCover Corporation (Governance Review) Amendment Bill 2008* was introduced on the same day, proposing amendments and new sections including those with regards to Ministerial Directions, Delegations, Auditing of accounts and Charters and Performance Statements.

When debate commenced on the Bill on 1 April 2008, the Government introduced amendments to the original Bill as a result of consultation undertaken after the tabling of the original Bill on 28 February 2008. These amendments, which were incorporated in the Bill, included:

- reducing weekly payments to 90% (instead of 80%) after 13 weeks with a further adjustment to 80% after 26 weeks
- allocating \$15 million to a Return to Work Fund, to fund initiatives helping retraining, rehabilitation and return to work programs and initiatives
- enabling the WorkCover Ombudsman to review a decision to cease weekly payments during a dispute where the decision is unreasonable
- streamlining the Workers Compensation Tribunal by removing the arbitration process
- retaining the 7.5% levy cap instead of the proposed 15%
- increasing the WorkCover Ombudsman's powers to ensure that employers meet their obligation to provide suitable employment for injured workers
- not proceeding with the proposal to provide lump sum payments for psychiatric disability
- providing the WorkCover Ombudsman with a role in reviewing certain decisions
- increasing the minimum notice period for cessation of payments from 7 to 14 days
- providing in the Regulations the formula that determines the fees for employers exiting the scheme
- including a provision in the Bill that clarifies that medical questions will be referred to medical panels

After significant debate the Bill was passed on 17 June 2008 with an amendment requiring the Minister for Industrial Relations to appoint someone to carry out a review of the legislative changes "as soon as practicable after 31 December 2010".

The majority of the Amendment Act commenced on 1 July 2008 along with supporting regulations and documents published in the South Australian Government Gazette.



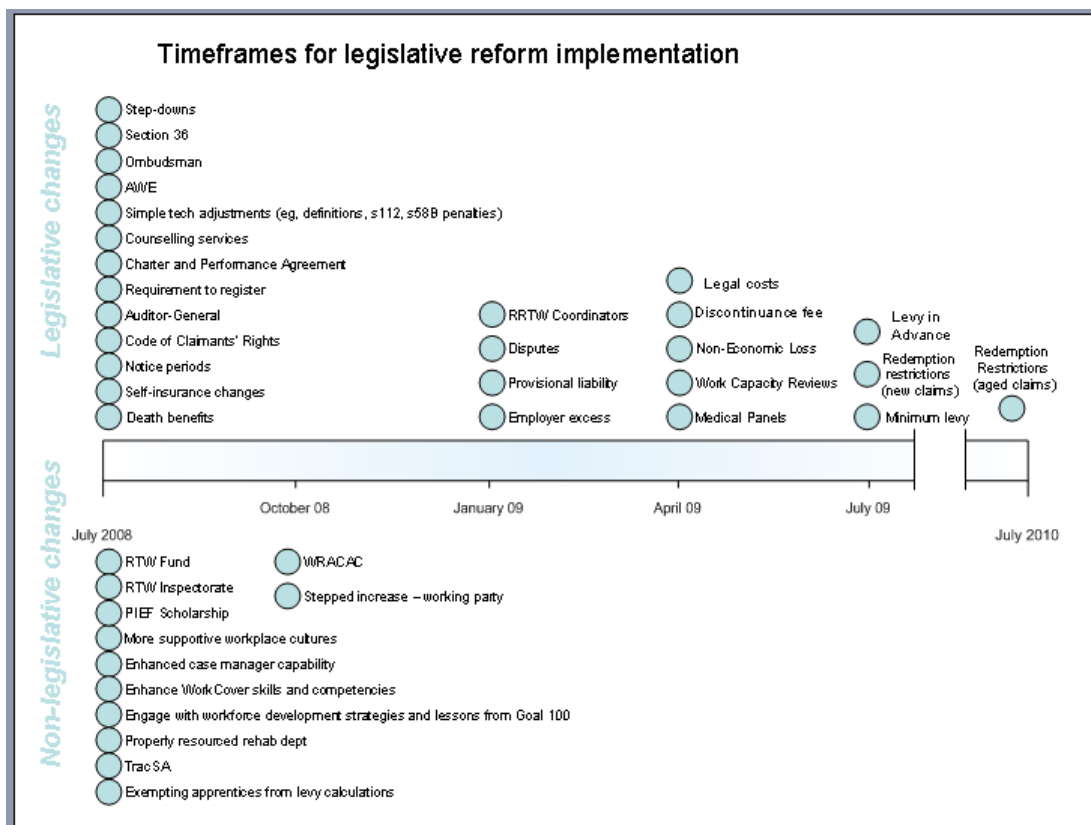
Full details and explanations of the changes are available on WorkCoverSA's website at [www.workcover.com/Home/Aboutus/WorkCoverSA/ChangestotheWorkCoverScheme](http://www.workcover.com/Home/Aboutus/WorkCoverSA/ChangestotheWorkCoverScheme).

Given the complex nature of some of the amendments and associated implementation work, as well as later than expected passage of the Amendment Act, WorkCover developed a staggered implementation plan aimed at striking a balance between:

- delivering the changes as quickly as possible
- managing the risks of implementation
- allowing sufficient time for the establishment of key systems
- enabling consultation to take place with stakeholders on certain items.

The staggered implementation of legislative reform has worked well and has allowed WorkCover, Employers Mutual and other Scheme partners and stakeholders to work together to appropriately implement the changes.

A graphic detailing the implementation plan is below:



## **5. Financial Implications – Benefits Realisation Plan**

Prior to the release of the Clayton-Walsh Review and the Bill, an initial estimate of the likely financial benefits from legislative reform was completed by Scheme's actuary, Finity. The major elements of reform were also costed by PricewaterhouseCoopers (PwC) as part of the Clayton Walsh review in

line with the earlier approach taken by the Scheme actuary, with PwC's assessment of future benefits more aggressive in some respects than Scheme's actuary's original estimate.

From these estimates WorkCover developed a Benefits Realisation Plan that identified key elements of the package that impact on Scheme savings and liability release, as well as other critical milestones and decision dates (for example, levy rate decisions). The Benefits Realisation Plan was designed to assist with:

- outlining what is necessary for a successful implementation of the reforms
- providing evidence to the Scheme actuary to achieve liability release
- making decisions on the levy rates
- reporting on the progress made with implementation.

In June 2008 the Board endorsed the approach outlined for the development of the benefits realisation plan. In September 2008 the Board also agreed that two targets - total scheme funding ratio and actuarial release were the critical success indicators and would be reported in WorkCoverSA's strategic plan.

Since then further work has been undertaken on establishing a set of operational measures and targets that underpin the benefits realisation plan that will be used as lead indicators to track progress. This will ensure we get the earliest possible indication on whether key assumptions are supported and expected outcomes are being met.

### **Benefits Realisation Plan Model**

In modelling the expected financial benefits of the reforms, Scheme actuary used three different scenarios and applied these to both current and future claims. The three scenarios being:

‘Minimal change’ – allows only for the direct impacts of the scheme reform package (eg a reduction in income maintenance payments due to the new step-downs) i.e. this scenario did not allow for impacts which relied on changes in claimant behaviour

‘Target’ – the central scenario which in addition to the direct impacts of the reforms required ‘cultural change’ (i.e. improved return to work outcomes) to improve performance to this level

‘Optimistic’ – represents scheme outcomes which are more favourable than the ‘target’ scenario

It was agreed to use the ‘target’ scenario as the appropriate basis for developing the Benefits Realisation Plan and three year strategic targets. The comparison point for the pre-June 2008 accidents is the June 2008 valuation and for future accidents the pre-reform valuation (December 2007) has been used.

Achieving the target scenario will deliver an ultimate valuation release of \$155million on pre-June 2008 claims, and provide an ongoing annual saving of around \$120million (24%) in the scheme's future claims costs. Achieving this result would mean the cost of a new accident year will be 2.25% of

wages (a total reduction of 0.50% from the current level). It should be noted that these figures are based on the information available as at 30 June 2008. The Scheme's results to 30 June 2009 and in particular the impact of the global financial crisis will result in some variation to these figures particularly in relation to the Scheme's funding position.

Achieving the target scenario will require significant improvement in front-end return-to-work outcomes that will arise as a behavioural response to the new legislative and operational tools available to WorkCover and Employers Mutual. A 25% improvement (prior to the work capacity 'test' at 130 weeks) in the number of active weekly claims for the 2009/10 and 2010/11 accident years are required to achieve this scenario. However, it will take some years before the savings can be fully recognised and specifically four to five years before the ultimate outcomes on new accident years are known with confidence. However, at each future scheme valuation a degree of recognition will be given based on the progress made towards the expected outcomes.

Assuming the target scenario is achieved and a constant future levy rate of 2.75% for 2009/10 and beyond, full funding of the scheme can be achieved within the next 5 to 10 years – a period of at least six years from the 30 June 2008 valuation, all other things being equal.

### **Early indicator statistics**

In March 2009, the WorkCover Board released WorkCoverSA's half-year results to 31 December 2008.

Declining stock markets and an unprecedented reduction of interest rates resulted in WorkCover posting a net loss of \$313 million for the half-year to 31 December 2008, resulting in the unfunded liability increasing to \$1.3 billion. (ie 51.7% funded). On a positive note, underlying claim experience provided an actuarial release in the six months of approximately \$50m, however this was more than offset by the other impacts noted above. As a result, the average levy rate was not reduced to 2.75% as was the aim of the Government at the time of announcing the Clayton Walsh review.

WorkCover is currently tracking a number of lead indicators to monitor the effectiveness of the overall implementation of the legislation.

Whilst it is too early to report on the progress of some of the lead indicators (for example, the recently implemented work capacity reviews), WorkCover has provided a summary table of the progress of some early indicators:

| <b>Indicator</b>                            | <b>Comments</b>                                                                                                                                                                                                                      |
|---------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Early injury reporting                      | Approximately 40% of workplace injuries recorded in June 2009 were reported within 5 days from the date of the accident. This was a significant improvement compared to the same period last year (19%).                             |
| Early claim decision (registered employers) | The average (median) number of days for a claim to be determined (including provisional liability decision) has reduced from 7 days in 2007-08 to 4 days in 2008-09, allowing for payments and claim management to initiate earlier. |

| Indicator                     | Comments                                                                                                                                                                                                                                                                                                                                                                                                                                            |
|-------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Substantiated complaints      | Whilst there were significant changes to the Scheme during the course of the 2008-09 financial year, the number of substantiated complaints was almost the same as last financial year (i.e. there was a 1% reduction in the number of substantiated complaints), and in particular have reduced toward the end of the financial year.                                                                                                              |
| Dispute numbers               | There has been a 28% reduction in the number of disputes lodged relating to average weekly earnings and weekly payment calculations for the year ending 30 June 2009 compared to the same period last year.                                                                                                                                                                                                                                         |
| Continuance rate (early exit) | As at 30 April 2009 the number of claims continuing to receive income maintenance at 4 weeks has remained roughly the same despite the introduction of the employer excess waiver. Hence the risk that these additional claims will stay longer on the Scheme does not appear to have been realised – over time it is expected that the impact of earlier claim management intervention will begin to reduce the number of claims reaching 4 weeks. |
| Lump sum payments             | Too early to asses the overall impact.                                                                                                                                                                                                                                                                                                                                                                                                              |

In addition to this the latest Campbell<sup>2</sup> measurement of return to work has reflected a significant improvement in South Australia.

In summary, it is too early to identify any sustained improvements in the performance of the scheme. The major structural and legislative reforms of the South Australian Scheme have now been done. For the reforms to have effect, significant cultural and return to work change needs to occur. Driving improved return to work through the changes described and case management is a key priority, for all South Australians.

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<sup>2</sup> Campbell: HWCA Australia & New Zealand National Report 2008/2009 located at [http://www.hwca.org.au/reports\\_rtw.php](http://www.hwca.org.au/reports_rtw.php)