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Interactions between Income Systems

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Interactions between income systems

Lisa Simpson & Raewin Davies

Abstract

This paper expands on a previous paper authored by Davies and Gould, titled, "How system design impacts the funding mix for people injured in accidents," presented to the Accident Compensation Seminar in 2011. This paper explored the interaction of welfare and injury schemes' income replacement benefits. In recent years, there has been a significant increase in claims through life insurance, particularly attached to superannuation schemes. We explore the interaction between welfare, salary continuance, TPD benefits and other injury scheme benefits for injured persons.

Keywords: Lisa Simpson, Raewin Davies, income systems, welfare, benefit design, 2015, behavioural economics, Injury Schemes Seminar

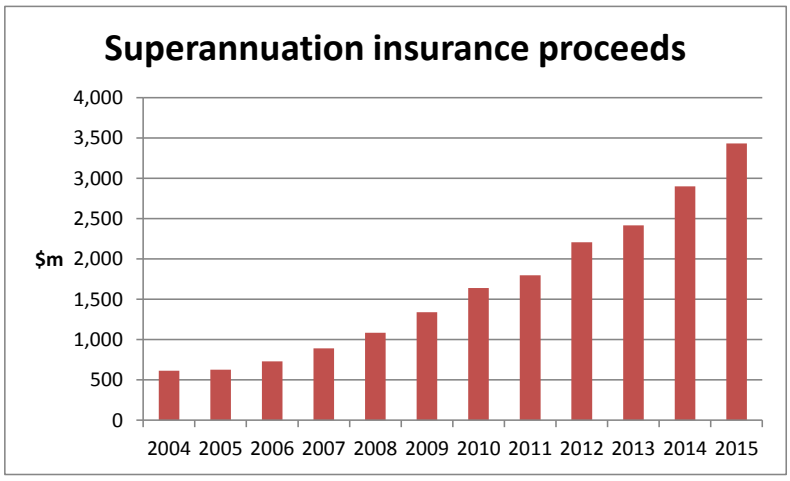
1 Introduction

This paper builds on the previous analysis carried out in 2011 which explored the impact of scheme design on the funding mix for injured persons. The sources of funding mix adopted in the 2011 analysis included:

- Individual savings, including personal savings, private insurance and spousal income
- Government, including Centrelink, Medicare and Public Hospitals; and
- Compulsory insurance, namely compensation schemes for workers compensation and CTP.

Since the time of the 2011 paper, there has been an increase in claims through superannuation funds, as shown in the following graph:

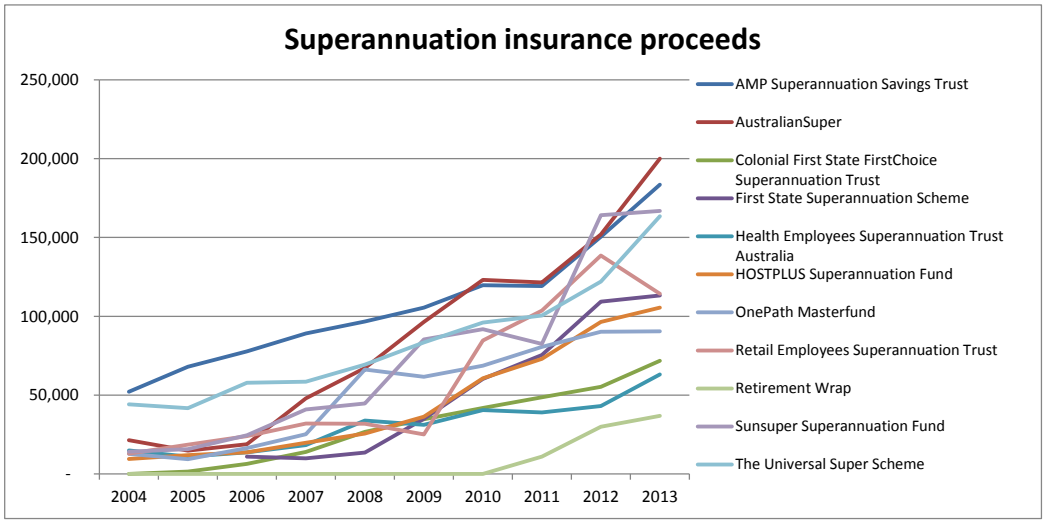
Figure 1: Claims through superannuation.



Source: APRA Quarterly Superannuation Performance June 2015

Superannuation insurance payouts are increasing at around 17% p.a. The payouts of nearly $3.5b in 2015 compare with $6.0b in workers' compensation. The following graph shows the experience for the 10 largest funds, showing that the trend is strong across many of them.

Figure 2: Claims through superannuation, by fund



Source: APRA Superannuation Fund Level Profiles and Financial Performance June 2013

Insurance payouts are available as both salary continuance and total and permanent disablements. Anecdotally, it is the lump sum TPD benefits driving much of the increase. Using the REST superannuation fund as an example, the automatic, default TPD cover is $64,500, with the option to purchase additional cover. TPD benefits can have long reporting delays, of some years. Access to insurance benefits is widely promoted through plaintiff solicitor firms, a number of which have now set up new divisions focussing on TPD claims in particular:

Figure 3: Plaintiff firm advertising

Maurice Blackburn Lawyers WE FIGHT FOR FAIR

Total and permanent disability claims (TPD) You're eligible for a TPD lump sum payment if you can show you're not able to do your normal job or any other work related to your training and experience. That doesn't mean you're unfit for all work – just the work that fits your skills and experience. For example, a bad back that stops you from working in your normal construction job allows you to make a TPD claim, even if your doctor says you're still fit for office work.

The increasing trend in claims through superannuation raises the question about the drivers of this behaviour. The following questions come to mind:

1 Are people choosing to claim through superannuation rather than through workers compensation or other compulsory insurance? If so, is this related to compulsory schemes' changes in benefit design, or other

factors? Are there any insights from jurisdictional comparisons which can add insight to this question?

2 What has been the impact of the GFC on this experience? Given that people's private savings were impacted through the GFC, did this prompt injured people to make different decisions about the funding mix for their injuries?

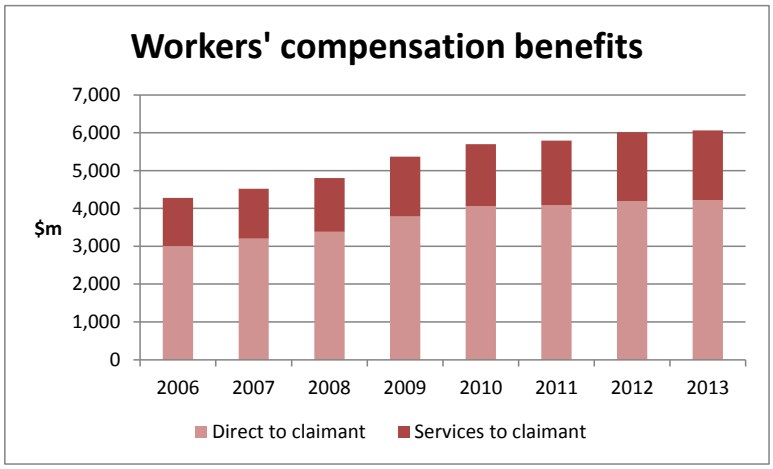
3 What insights can we glean from behavioural economics to understand the drivers of the funding mix for injuries? Are there any intergenerational differences which can explain the emerging trends?

This paper explores these questions in more detail. We start with a review of recent trends in workers' compensation benefits, to determine whether they are the same as those observed in the superannuation environment, or different.

2 Trends in Workers compensation benefits

Firstly, we examine the trends in total workers' compensation payments nationally.

Figure 4: Workers' compensation benefits



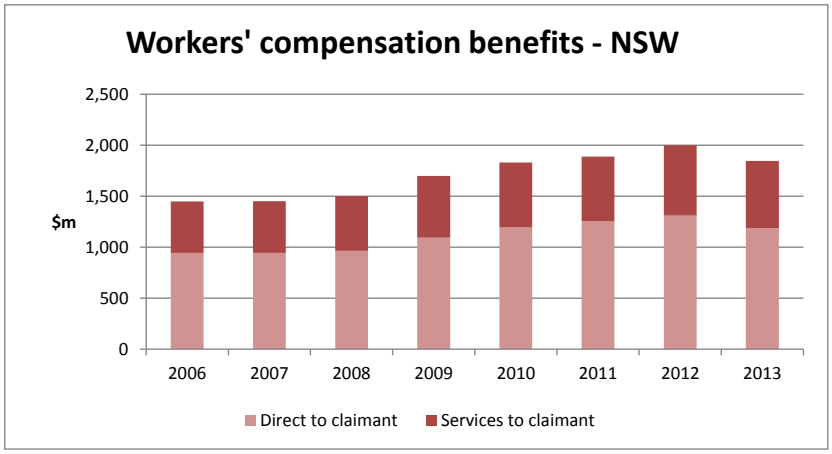
Source: Comparative Performance monitoring report, Safework Australia, 2015

Workers' compensation benefits have grown by around 5% p.a. over the period shown. However, growth rates over the period from 2007-2010 were somewhat higher. Anecdotally, injuries which occurred during the GFC were associated with longer durations, potentially due to difficulties in arranging suitable return to work duties for injured workers. There was also an increase in stress related claims during the GFC, which appear to have now stabilised at a higher proportion of total claims.

Of course, changes to benefits are also a factor in the total payments experience. These can be examined more closely by looking at the experience of individual states.

In NSW, the growth is spasmodic, with strong increases in 2009 through to 2012, then a fall in 2013, as shown in the following graph.

Figure 5: Workers' compensation benefits – New South Wales

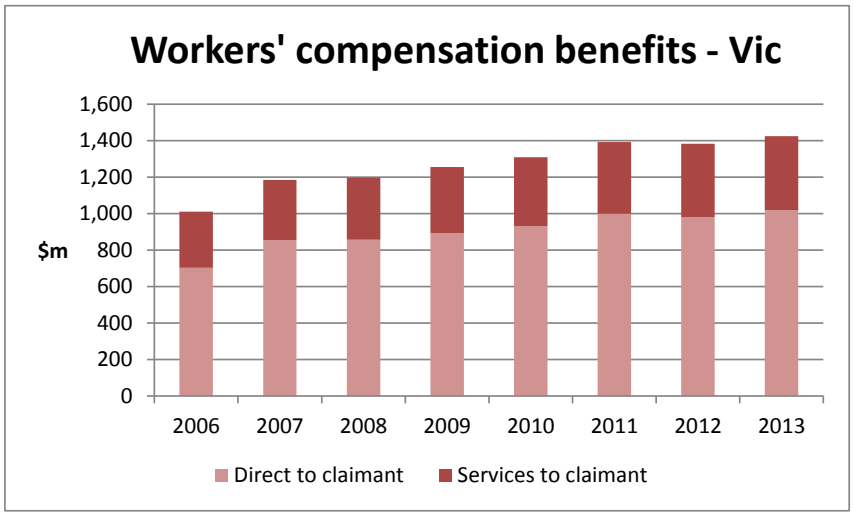


Source: Comparative Performance monitoring report, Safework Australia, 2015

A notable part of the reduction relates to the removal of journey claims from the NSW scheme in 2012, along with tightening up the eligibility for ongoing medical and treatment costs and limiting the number of impairment assessments. Some of these benefit reforms have recently been unwound. I discuss these changes further in section 4 below.

In Victoria, benefits increased sharply in 2007, with slower growth through to 2011, then a fall in 2012. The 2011 experience was impacted by the Hanks reforms, which increased weekly compensation and death lump sum amounts. Again, the GFC had the impact of increasing durations on benefit, but also reducing claim frequency.

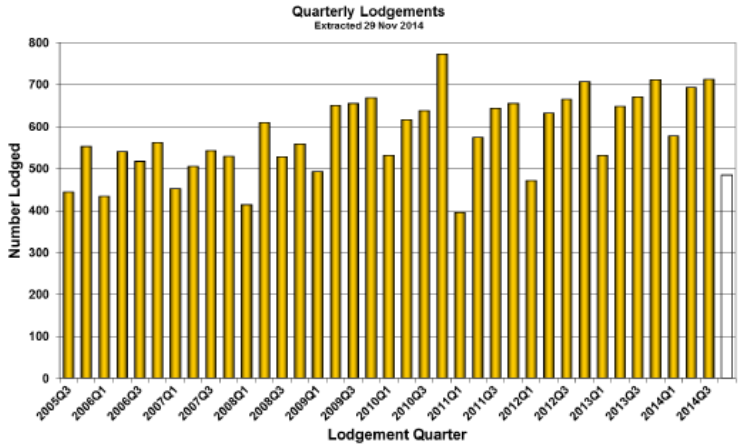
Figure 6: Workers' compensation benefits - Victoria



Source: Comparative Performance monitoring report, Safework Australia, 2015

Despite the apparent stability in payment levels in the Victorian scheme, there is a trend towards increasing numbers of common law lodgements, as shown in the following graph:

Figure 7: WorKSafe Victoria Common law lodgements

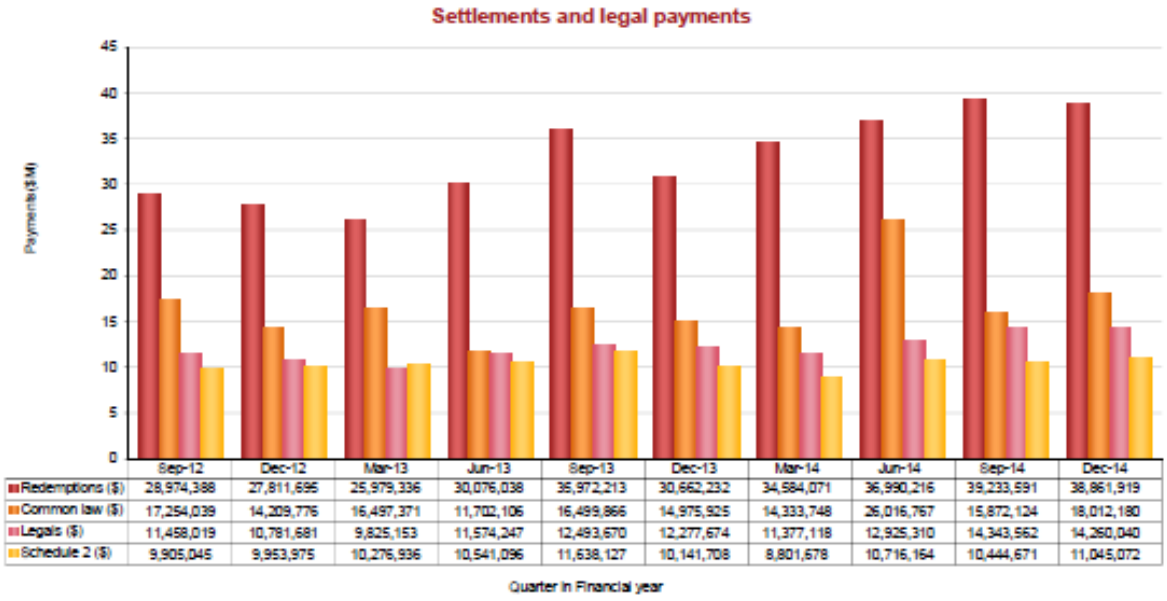


** Note: 2014Q4 represents only 2 months of data

Source: https://www.worksafe.vic.gov.au/__data/assets/pdf_file/0010/157816/LLG-Key-Issue-Paper-12-December-2014.pdf

Similar increasing common law trends can be observed in the ACT and WA workers compensation schemes, when examining payment trends:

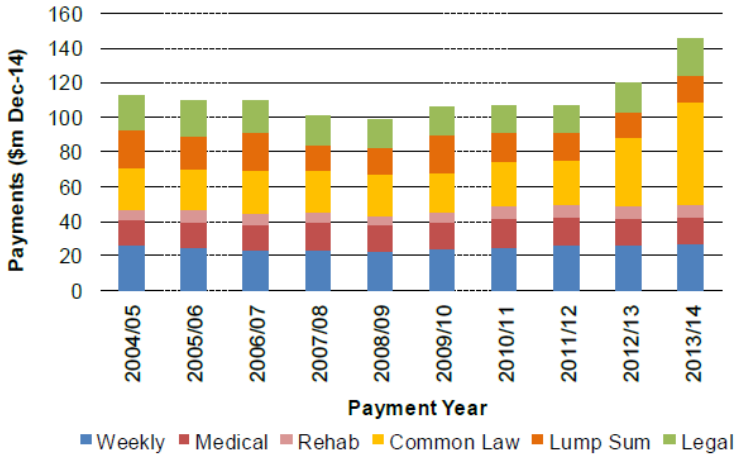
Figure 8: WorkCover WA payment trends



	Sep-12	Dec-12	Mar-13	Jun-13	Sep-13	Dec-13	Mar-14	Jun-14	Sep-14	Dec-14
Redemptions ($)	28,974,388	27,811,695	25,979,336	30,076,038	35,972,213	30,662,232	34,584,071	36,990,216	39,233,591	38,861,919
Common law ($)	17,254,039	14,209,776	16,497,371	11,702,106	16,499,866	14,975,925	14,333,748	26,016,767	15,872,124	18,012,180
Legals ($)	11,458,019	10,781,681	9,825,153	11,574,247	12,493,670	12,277,674	11,377,118	12,925,310	14,343,562	14,260,040
Schedule 2 ($)	9,905,045	9,953,975	10,276,936	10,541,096	11,538,127	10,141,708	8,801,678	10,716,164	10,444,671	11,045,072

Source: WorkCover WA Quarterly performance Monitoring December 2014

Figure 9: ACT Workers Compensation payment trends



Source: ACT Workers Compensation, Review of Scheme Performance to June 2014, Finity

In summary, there is evidence of growth in common law benefits through a number of schemes, consistent with the trend towards increasing superannuation TPD benefits, but at a lower level of growth. It is possible that changes to scheme design are impacting the relative rate of growth between workers' compensation common law utilisation levels, and may also be influencing injured workers' choice to claim through superannuation. We explore recent scheme changes in the next section.

3 Changes in injury scheme benefit design

There have been a number of trends with injury schemes' benefit changes in recent years:

1) Introducing thresholds, or tightening of existing thresholds for access to common law benefits. (eg WorkCover Queensland, SA MAC, RTW SA)
2) Limiting the period for which income replacement benefits are payable. (eg NSW WorkCover, RTW SA)
3) Increasing focus on early intervention and rehabilitation.

These changes have been introduced in light of the trends within each scheme, which can then flow on to changes in utilisation of other income systems. I explore each of these changes in turn.

3.1 Common law thresholds

The following table shows the current thresholds applicable to common law benefits for workers compensation and motor liability schemes across the country. Of these, Queensland workers compensation, SA motor and workers compensation and NSW Workers compensation have all undergone recent changes:

Table 1: Common law thresholds for schemes

State	Motor Liability	Workers Compensation
QLD	ISV for general damages	ISV for general damages
		Current >5% DPI for any damages
NSW	10% WPI For Pain and Suffering	15% DPI for damages
VIC	Narrative test or >30% WPI	Narrative test or >30% WPI
ACT	None	None
SA	> 10% ISV for NEL, Voluntary services and	> 30% WPI for economic loss only
	> 7% ISV for loss of earning capacity	>5% for NEL and Economic loss statutory lump sums
WA	> 5% for NEL	> 15% PWPI for damages
NT	Not available	Not available
TAS	None	> 20% WPI

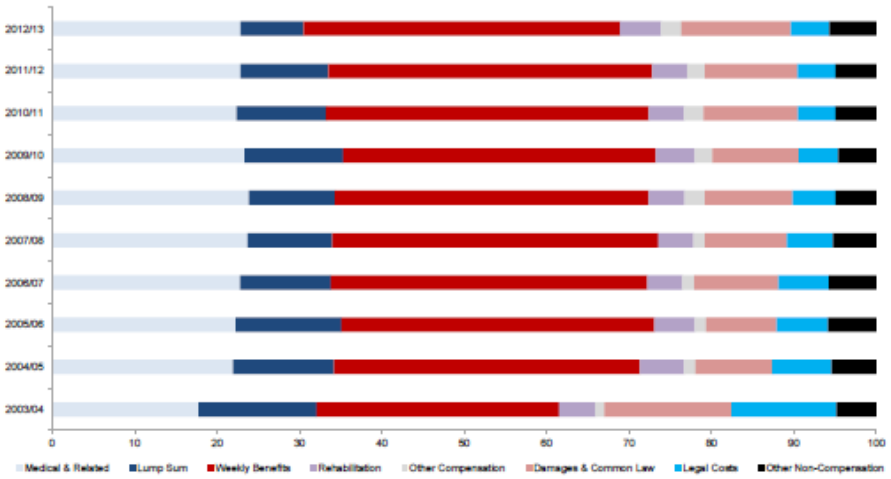
Source: Respective scheme websites

The following case studies illustrate the impact of recent changes in thresholds.

NSW

NSW WorkCover tightened the eligibility for work injury damages in 2012, by stipulating that a single impairment assessment be carried out. Previously, injured workers were having multiple impairment assessments over time, as the nature of their injury changed, which resulted in more injured workers accessing work injury damages over time. Payment trends are shown below with damages and common law increasing over time as shown in the light pink.

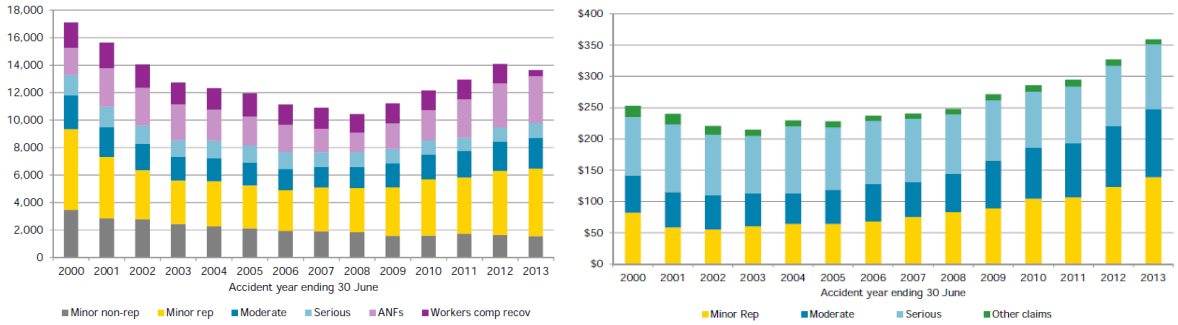
Figure 10: NSW WorkCover payment trends



Source: NSW WorkCover Statistical bulletin 2013

Although not a recent reform, the NSW CTP scheme was significantly changed in 1999, when thresholds were introduced for pain and suffering, designed to reduce the number of minor claims. There have also been further benefit reforms throughout the 2000s, with the expansion of the accident notification form benefits, and the introduction of the LTCS. The removal of journey claims from the NSW WorkCover scheme has also impacted the NSW CTP experience. These changes are explored in the following graphs:

Figure 11: NSW CTP trends in claim numbers and cost per policy



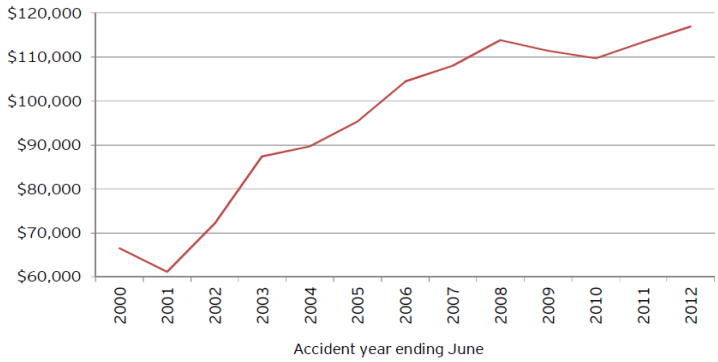
Source: EY Selected indicators of the performance of the NSW CTP Scheme to 2013

The graph to the left shows that there was a steady reduction in the number of claims with minor injuries with legal representation over the accident years to 2006. The total almost halved from approximately 5,900 in 2000 to 3,200 in 2002 and then grew to 4,500 in 2012.

This experience from 2006-2012 was accompanied by a small reduction in the number of claims with minor injuries which were not legally represented. Numbers of claims arising from more severe injuries, which would usually be legally represented, do not show strong trends.

The changes in numbers of minor severity claims which have legal representation can be explained by examining the average claim size experience for those claims. The following graph shows the averages by accident year for such claims.

Figure 12: NSW CTP average claim size trends for minor represented claims



Source: EY Selected indicators of the performance of the NSW CTP Scheme to 2013

The graph shows that the average claim sizes have increased significantly over the last 10 years.

What is not shown is that the comparative average claim size for accidents which occurred prior to the 1999 legislative reforms would have been much higher, as there was no threshold for access to general damages. Therefore, it is likely that the large reduction in numbers of claims with legal representation with minor injuries was due to the lower average damages for minor injuries under the changed legislation in the early 2000s.

In summary, it was less economically attractive for injured road users with minor injuries to bring a claim under the CTP scheme in the early 2000s, and it was less economically attractive for solicitors to represent such injured parties. It is likely that the low average damages amounts made the solicitor client fees too low to be economically attractive for plaintiff firms.

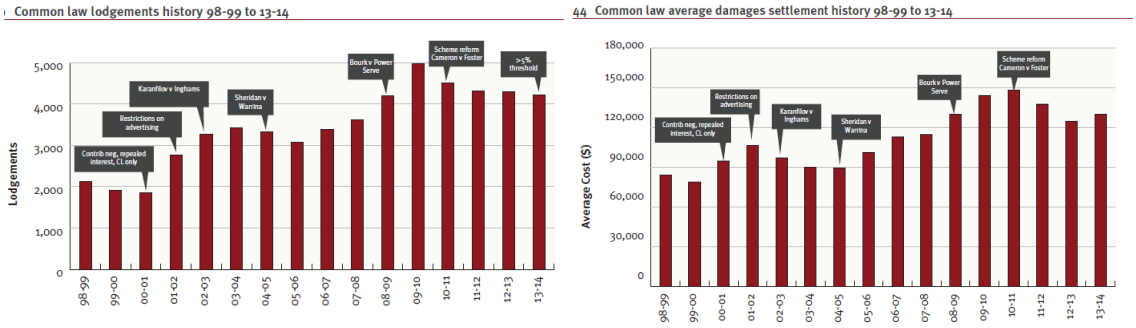
Over time, the increase in average damages for minor injuries has been driven by the increased utilisation of care benefits and superimposed inflation in other heads of benefit. The increase in numbers of legally represented claims coincides with the increase in damages.

These trends illustrate the linkage between changes in benefit levels and scheme utilisation.

Queensland

WorkCover Queensland has undergone a number of benefit reforms, and the common law experience in particular has been impacted by a number of precedents. In 2011 there was a change to link general damages to an Injury Scale Value, consistent with the Queensland CTP scheme. Further reforms in October 2013 introduced the requirement for a greater than 5% degree of permanent impairment for access to common law. This threshold has now been unwound, with retrospective application for injuries after January 2015. The following charts show the recent reducing trend in lodgements from the most recent two reforms. Average damages have also trended downwards due to the introduction of a scale and also due to WorkCover's litigation approach of holding to initial offers.

Figure 13: WorkCover Queensland common law trends



Source: Workers' Comensation Regulator Statistics Report 2013-14

It is likely that the introduction of thesholds in the workcover scheme has resulted in a shift to other income systems, such as insurance through superannuation, as observed in the trends shown in section 1. It is not possible to be definitive as to the relationship between the changes in the workers' compensation scheme and superannuation trends, as the APRA regulated funds report on a national consolidated basis.

With the unwinding of the 5% DEPI threshold for access to common law, it would be anticipated that some of the superannuation trends may reverse in Queensland. Furthermore, there would be an expected impact on welfare trends.

South Australia

The South Australian MAC scheme introduced thresholds for access to different heads of benefit for injuries post 1 July 2013. Restrictions on plaintiff legal fees for smaller claims were also introduced, to reduce the number of minor claims.

The South Australian WorkCover scheme introduced common law for the first time, but only for those with greater than 30% WPI. Statutory lump sums are also available for non-economic loss and economic loss for those greater than 5% impairment levels.

It is again hypothesised that the changes in access to common law in these schemes in South Australia will result in changes to welfare utilisation, and potential further impact on superannuation insurance benefits.

We examine welfare trends further in section 5 below.

3.2 Income benefit period limitations

The 2012 WorkCover NSW reforms also limited the benefit period for weekly compensation to five years for those with impairment less than 20%, and introduced work capacity reviews which act to cease benefits after 130 weeks if the injured work has capacity to work.

Similar work capacity reviews were added to the SA WorkCover Scheme, which has been successful in reducing the number of injured workers continuing on benefits at longer durations. There have been a number of reductions in liability estimates resulting from this change.

Such limitations to income benefit periods are included in most schemes, bringing them closer together in terms of benefit design over time. At the same time, there has been an increased focus on early intensive return to work. Together, these can be seen to act as a "carrot and stick" mechanism. Anecdotally, it is considered that one of the key decision points where injured persons seek out a plaintiff solicitor is at the time that their income benefits cease. Increasing rates of disputation have been observed to coincide with increasing rates of lodgement at common law. Although it is difficult to prove causation, these trends can be observed across a number of schemes which seemingly gives weight to the hypothesis.

3.3 Intensive early intervention

Although return to work is stated as the key strategic goal of all workers compensation schemes, there has been an ongoing increased focus towards improving outcomes nationally.

One example is the South Australian WorkCover Scheme, which has undergone significant changes, focussed on return to work and early rehabilitation. The scheme is rebranded "Return to Work," which illustrates the significance of the changes. Mobile case managers are delivering a face to face service with injured workers and employers to overcome any barriers to return to work.

WorkSafe Victoria have developed an agent incentive measure based on return to work performance six months after injury. This index measure resulted in improved return to work outcomes over the latest agent contract period.

It would be anticipated that these trends and initiatives would result in lower overall compensation paid through injury schemes and lower utilisation of common law benefits over time. There may be offsetting increases in welfare utilisation, particularly the disability support pension. We look at welfare trends further in section 5 below.

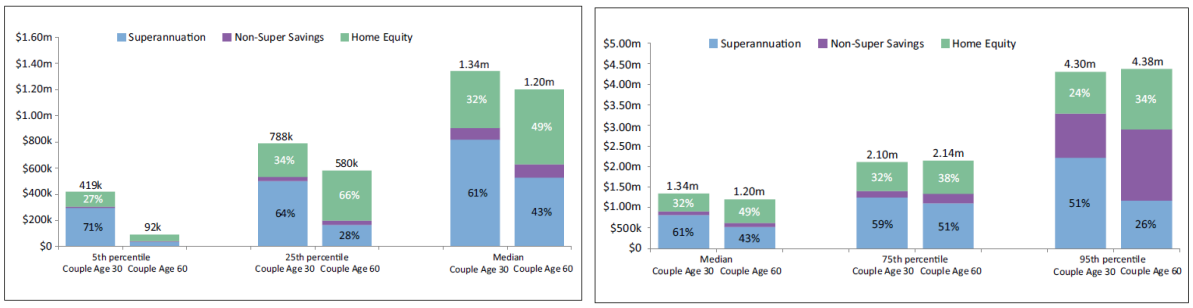
4 Intergenerational differences

When considering income systems and the choices made by injured workers and motorists in respect to compensation, it is also instructive to consider intergenerational differences. This has been explored in the IAAust's white paper titled, "For Richer for Poorer, Retirement Incomes" published in 2015.

One of the key differences between generations is the extent of their superannuation savings compared to their other forms of saving. The introduction of the superannuation guarantee charge in 1994 coincided with the time that Generation X commenced full time employment. Therefore, as a proportion of their overall wealth, generation X will have much higher levels of superannuation savings than generations before them at the same point in their careers, and lower investment in housing and other forms of wealth. Conversely, older workers will have higher savings in their dwellings and other wealth and less superannuation as a proportion of their overall wealth.

The following graph illustrates the projected sources of wealth at age 65 for different cohorts of 30 year old and 60 year old couples.

Figure 14: Sources of wealth at age 65



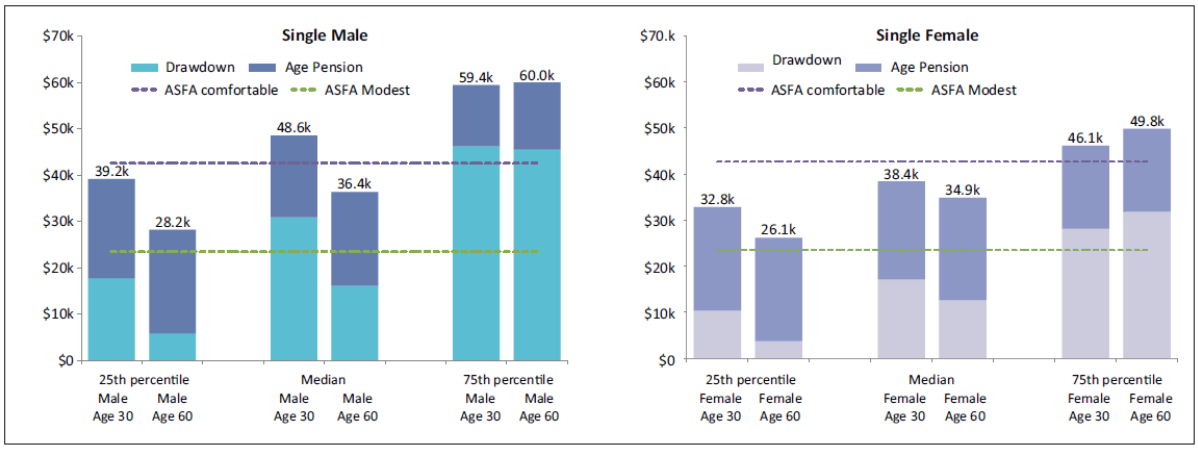
Source: Actuaries Institute: For Richer, for Poorer, Retirement incomes

The graphs illustrate projected amounts of household wealth and sources of that wealth.

Considerations of sources of personal wealth and interactions with welfare and other income systems are important in terms of decision making. It is instructive for those working within injury schemes to consider the demographics and other characteristics of their clients when seeking to understand their choices. For example, clients approaching retirement may still have adult children at home, may still have a mortgage and may be seeking to support their children to enter the housing market. In such a situation, they may prefer lump sum sources of income over ongoing periodic payments, to discharge debts and help family.

The following graph shows the projected sources of income from superannuation savings compared to age pensions, for single males and females for different wealth percentiles.

Figure 15: Sources of wealth at age 65



Source: Actuaries Institute: For Richer, for Poorer, Retirement incomes

The graphs illustrate the expected sources and amounts of income in retirement and compare these to amounts estimated to provide a "modest" or "comfortable" retirement, as defined by the Association of Super Funds of Australian.

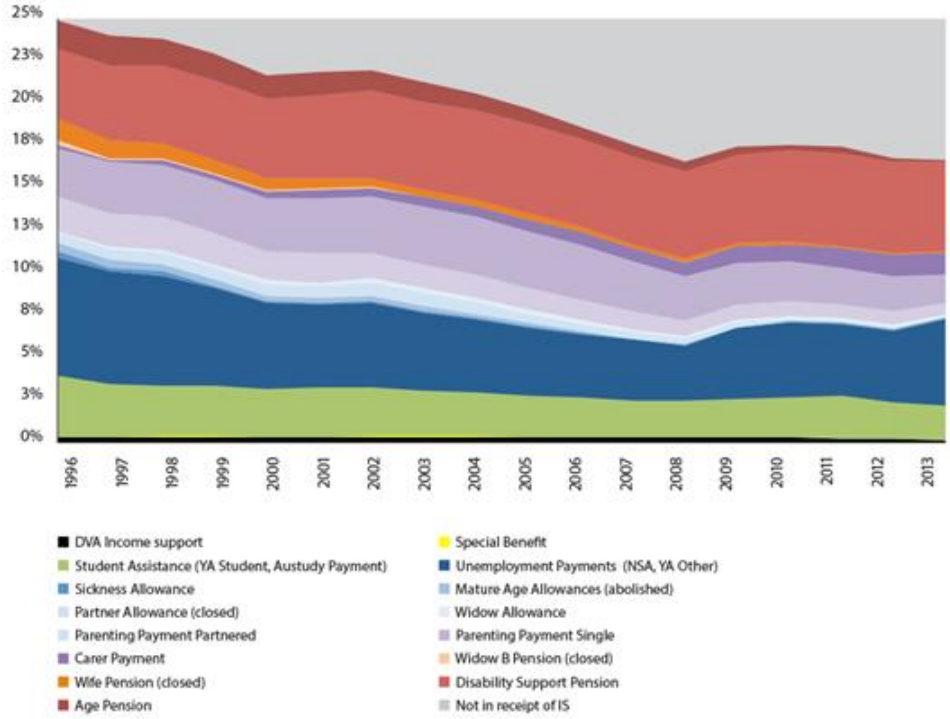
All else being equal, the lower an individual's superannuation savings, the more important the age pension becomes as a source of income. In such circumstances, the Centrelink preclusion period which arises after receipt of common law damages for economic loss becomes more significant in decision making processes. This preclusion period is calculated based on a notional weekly amount, and represents the number of weeks before someone is able to receive any Centrelink income benefits.

5 Trends in welfare

Relatively, favourable economic conditions over the past two decades, combined with an enhanced participation focus in the income support system, have led to a reduction in the extent to which the Australian working age population is in receipt of income support.

The percentage of the working age population receiving income support peaked in 1997 at 24.9 per cent, before falling to 16.6 per cent in the 2008, rising to 17.6 in 2010 following the Global Financial Crisis and then easing back to 16.7 per cent in 2013. This is shown in the graph below.

Figure 16: Percentage of working age (16–64 years) population receiving income support



Source: A New system for better employment and social outcomes. McClure report

With increases in the age pension eligibility age, we are seeing more people on disability support pension over time. Women had their eligibility age increased by six months every two years from 60 to 65 starting in 1995 and finishing in July 2013.

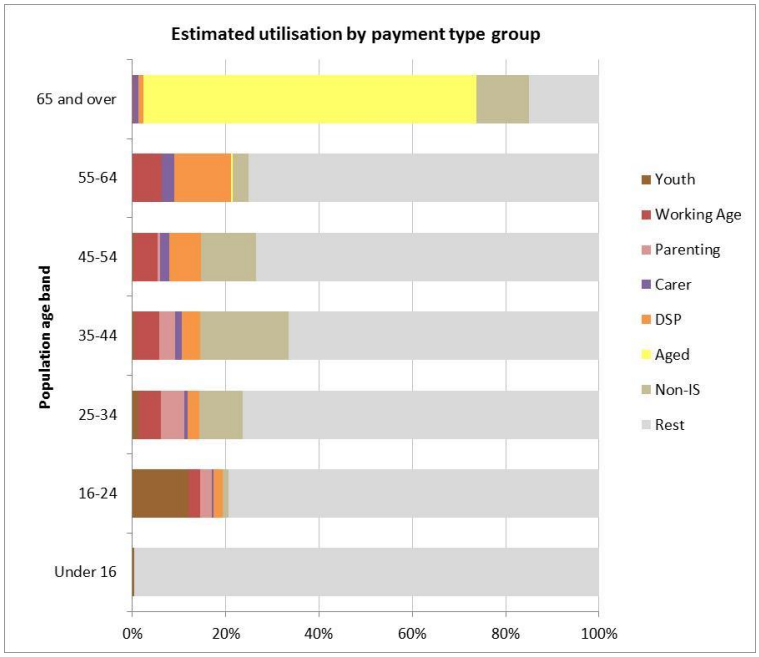
There is a clear interaction from the aging population, later access to aged pensions, later access to superannuation and the resulting impact on DSP utilisation. This would be anticipated to impact workers compensation utilisation trends for the 55-65 year old group in particular.

The trends in utilisation of welfare during the GFC are similar to the trends in workers compensation payments over the same period. The welfare trend during the GFC was driven by increasing unemployment benefits and continued strong utilisation of the DSP. We explore some of these utilisation results further in the next section.

5.1 Utilisation of welfare

The following graph illustrates the utilisation of welfare by payment type and age group in Australia.

Figure 17: Utilisation of welfare by payment type and age group

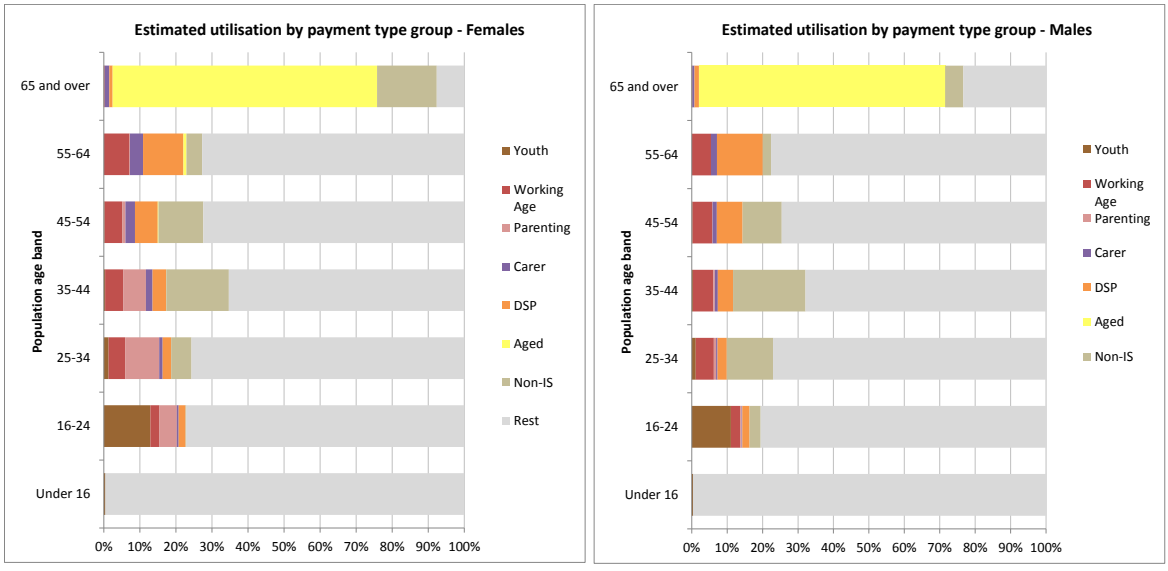


- Youth = Abstudy, Austudy and Youth Allowance
- Working age = Partner allowance, Newstart Allowance, Sickness Allowance, Special benefit, Widow allowance
- Parenting = Parenting payment single and partnered
- Carer = Carer payment
- DSP = disability support pension
- Aged = age pension, Wife pension (partner on aged and disability pensions)
- Non income support = Pensioner concession card, carer allowance, Seniors health card, Family tax benefits A&B

Source: Department of Social Services statistical overview 2013, Australian Census population data

The following graphs break down the total picture into the experience for men and women separately.

Figure 18: Utilisation of welfare by payment type, age group and sex.



Source: Department of Social Services statistical overview 2013, Australian Census population data

Welfare recipients are slightly higher as a proportion of the population for women at all ages. Most notable difference is in the 65 plus group, where 73.3% of women are receiving the pension compared to 69.5% of men. There are 15% more women than men in this category. It reflects the difference in assets and longevity of women compared to men. The non-income support benefits for this group reflect the pensioner concession care and seniors health card. Again, utilisation of these benefits is higher for women.

Conversely, there is a higher utilisation of the disability support pension at all ages by men rather than women.

At the youngest ages, parenting payment is normally received by the mother. We have tried to only count welfare recipients once, and therefore if the mother is receiving parenting payment she is usually also receiving family tax benefits, and hence we do not count that twice. For males, given that few men receive the parenting payment, then they are counted as receiving the family tax benefit at younger ages.

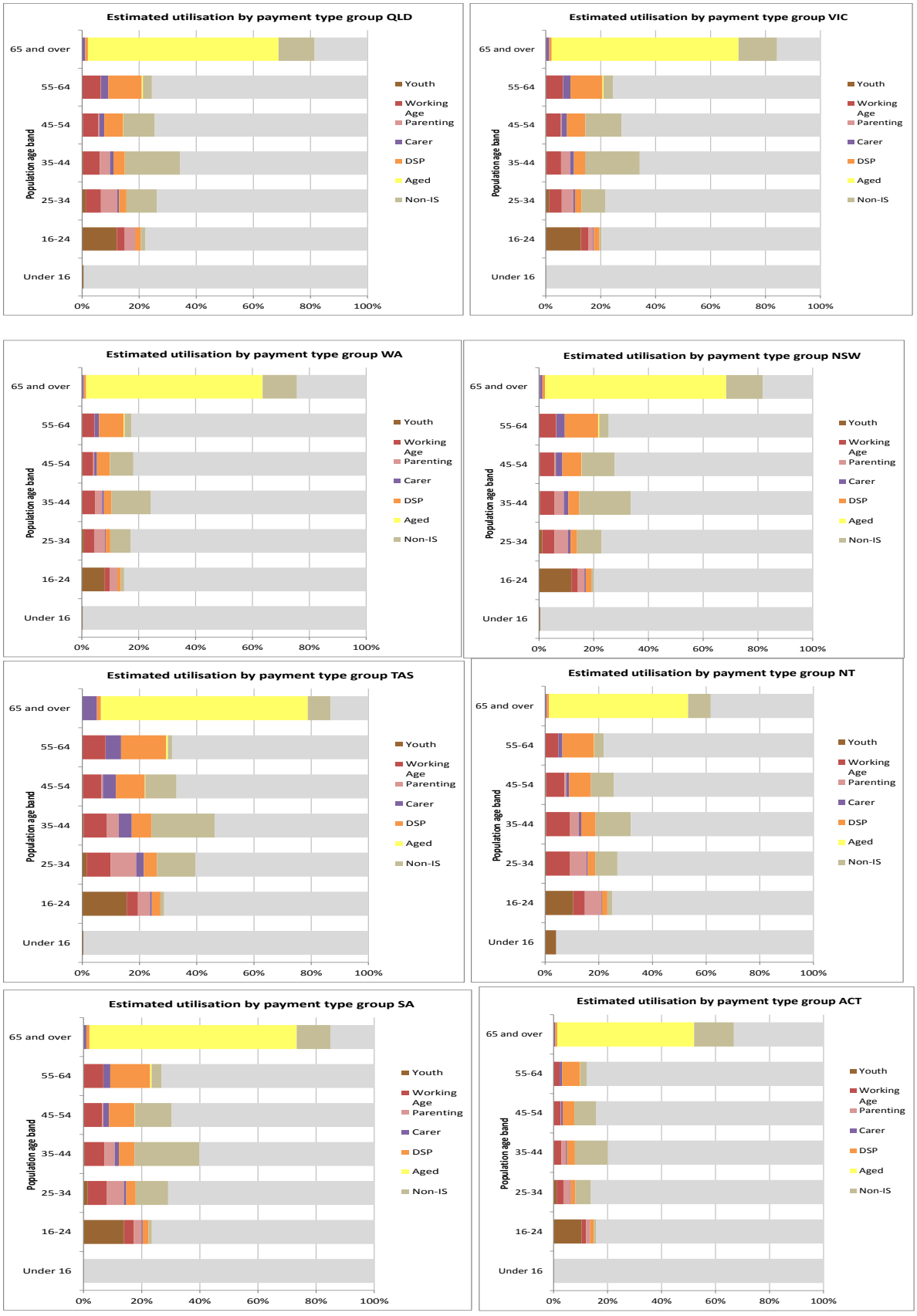
A higher proportion of women than men are receiving youth benefits.

A higher proportion of men than women are receiving Newstart and other working age allowances. This trend is reversed in the 55-64 year age group, where the addition of the "widow allowance" means that 7.1% of women receive these benefits compared to 5.4% of men.

So what does this mean in terms of interactions with other systems? Overall, between 20-30% of people of working age are receiving some sort of welfare payment, with the highest proportion in the 35-44 year bracket. Therefore, welfare payments would be expected to play an important role in decision making processes for people navigating income systems.

Next we examine whether there are any differentials by state, in light of changing benefits available through injury schemes. It would be anticipated that states with lower benefits available through injury schemes would have a correspondingly higher utilisation of welfare benefits, or other income systems.

Figure 19: Utilisation of welfare by payment type, age group and State.



Source: Department of Social Services statistical overview 2013, Australian Census population data

Firstly, looking at the disability support pension, across the board by age group, Tasmania has the highest utilisation, followed by South Australia. This phenomenon is likely to be strongly driven by the economies of each state. Tasmania and SA have the highest unemployment rates at 7.6% and 7.3% respectively, as shown in the following table. The order of the other states varies a little by age.

Table 3: Ranking of DSP utilisation compared to unemployment rates by state

	Unemployment rate Persons	Ranking Unemployment	Ranking DSP utilisation to age 45	Ranking DSP utilisation age 45-55	Ranking DSP utilisation age 55-65
TAS	7.60	1	1	1	1
SA	7.30	2	2	2	2
QLD	6.73	3	4	5	5
VIC	6.07	4	5	6	7
WA	6.03	5	8	7	6
NT	5.57	6	3	3	4
NSW	5.35	7	6	4	3
ACT	3.93	8	7	8	8

Source: Australian Bureau of Statistics, Department of Social Services statistical overview 2013

Up to age 45: Queensland, Victoria and NSW are grouped pretty closely together in that order, followed by ACT and WA. Qld unemployment is higher at 6.73%, followed by Victoria at 6.07% and NSW at 5.35%. Interestingly WA's unemployment at 6.03% ranks it fifth, but it is ranked eighth in its utilisation of DSP for younger age groups, but 6th for older age groups.

ACT has 4% unemployment, which is usually referred to as "full employment" and it consistently ranks lowest in utilisation of DSP. There is also the impact of household wealth, which is also high in the ACT, as shown in figure 20.

For those aged 45-65, NSW moves up to 3rd or 4th place in utilisation of DPS. Interestingly, Victoria drops down to 7th rank in DSP utilisation, with decreasing rank for each age group. This could be linked to WorkSafe's weekly compensation benefit structure, which enables seriously injured workers to receive compensation to age 65. However, NSW's WorkCover benefits have been similar until the recent past, and NSW has the opposite trend, moving up the ranks in utilisation of DSP with age.

Working age welfare payment utilisation follows the pattern by unemployment rate, with the exception of the NT, which tops the utilisation despite having relatively low unemployment. The following table details the results:

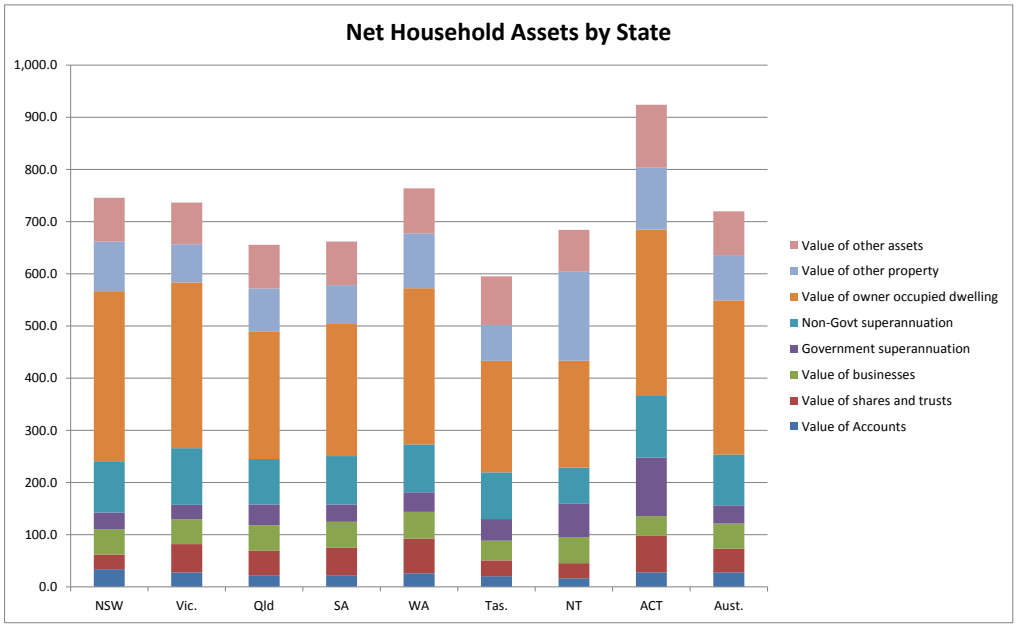
Table 4: Ranking of benefit utilisation compared to unemployment rates by state

	Ranking Unemployment	Ranking Working age welfare utilisation age 25-34	Ranking Working age welfare utilisation age 35-44	Ranking Working age welfare utilisation age 45-55	Ranking Working age welfare age 55-65
TAS	1	2	2	2	1
SA	2	3	3	3	2
QLD	3	4	4	5	4
VIC	4	5	5	6	5
WA	5	7	7	7	7
NT	6	1	1	1	6
NSW	7	6	6	4	4
ACT	8	8	8	8	8

Source: Australian Bureau of Statistics, Department of Social Services statistical overview 2013

Similar patterns are observed for other welfare. Youth support is also topped by TAS and SA but Victoria is in third place, followed by Queensland and NSW. The aged pension is also topped by TAS, and SA, then QLD, Victoria, NSW, WA, NT and ACT. The rankings for aged pension utilisation are most likely driven by relative household wealth, which is illustrated in the following figure. Wealthier states have less reliance on the aged pension.

Figure 20: Net household assets by state



Source: Australian Bureau of statistics

ACT is the richest state/territory, followed by WA, NSW, Victoria, NT, Qld, SA and Tasmania. This series is directly the reverse of the Pension utilisation series, with the exception of the NT. NT has a lower average age for those above 65: 71.9 compared to 74-75 in other states, so possibly a higher proportion are still working in

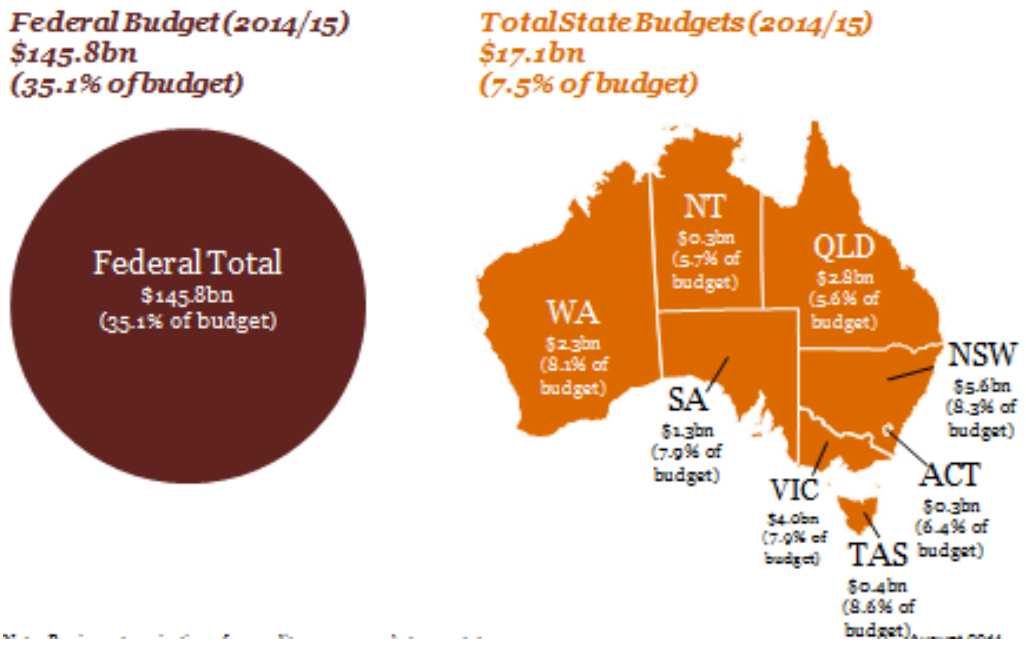
that cohort. Also, those over 65 only represent 6.5% of the population in the NT, compared to 15-17% in other states.

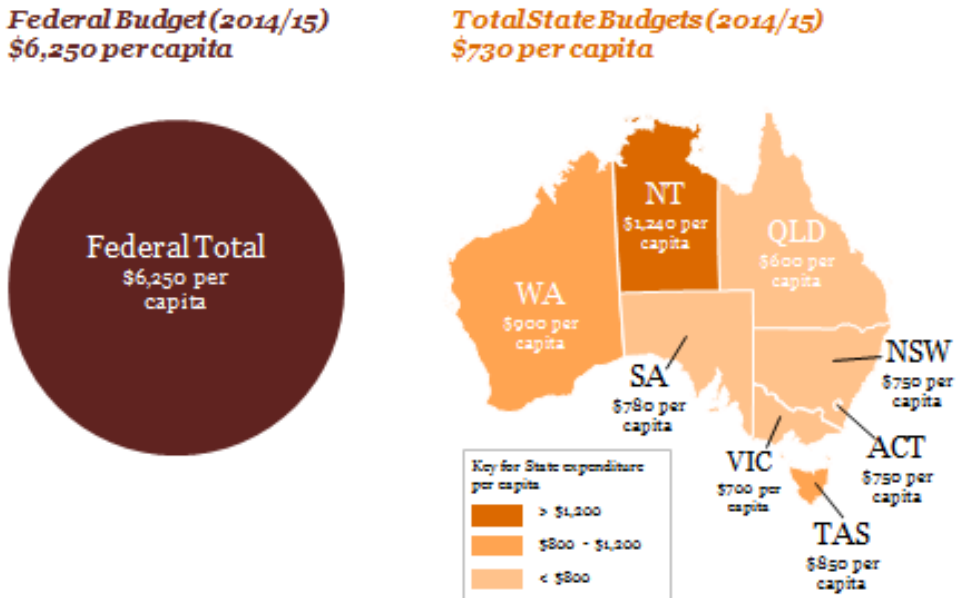
In summary, there is no definitive relationship between welfare utilisation and the relative generosity of benefits provided through injury schemes. Welfare utilisation seems more closely driven by employment and household wealth. The relative size of the payments made through injury schemes compared to welfare payments is also small. For example, the total paid in DSP in 2012/13 was $15Bn, to 822,000 participants. By comparison, total workers compensation payments were $6Bn. To explore this further, we look next at the aggregate welfare expenditure per capital in each state.

5.3 Welfare and social services expenditure by state

Comparing the proportion of each state's budget allocation to welfare and social services, the totals vary from 5.6% in Queensland up to 8.6% in Tasmania. The order of the percentage of each states budgets devoted to welfare and social services is TAS, NSW, WA, SA, VIC, ACT, NT and QLD. The following graphics illustrate the size of the welfare budget in each state, and per capital and the corresponding figures from the Federal budget.

Figure 21: Welfare budgets and per capita amounts





Source: PwC research

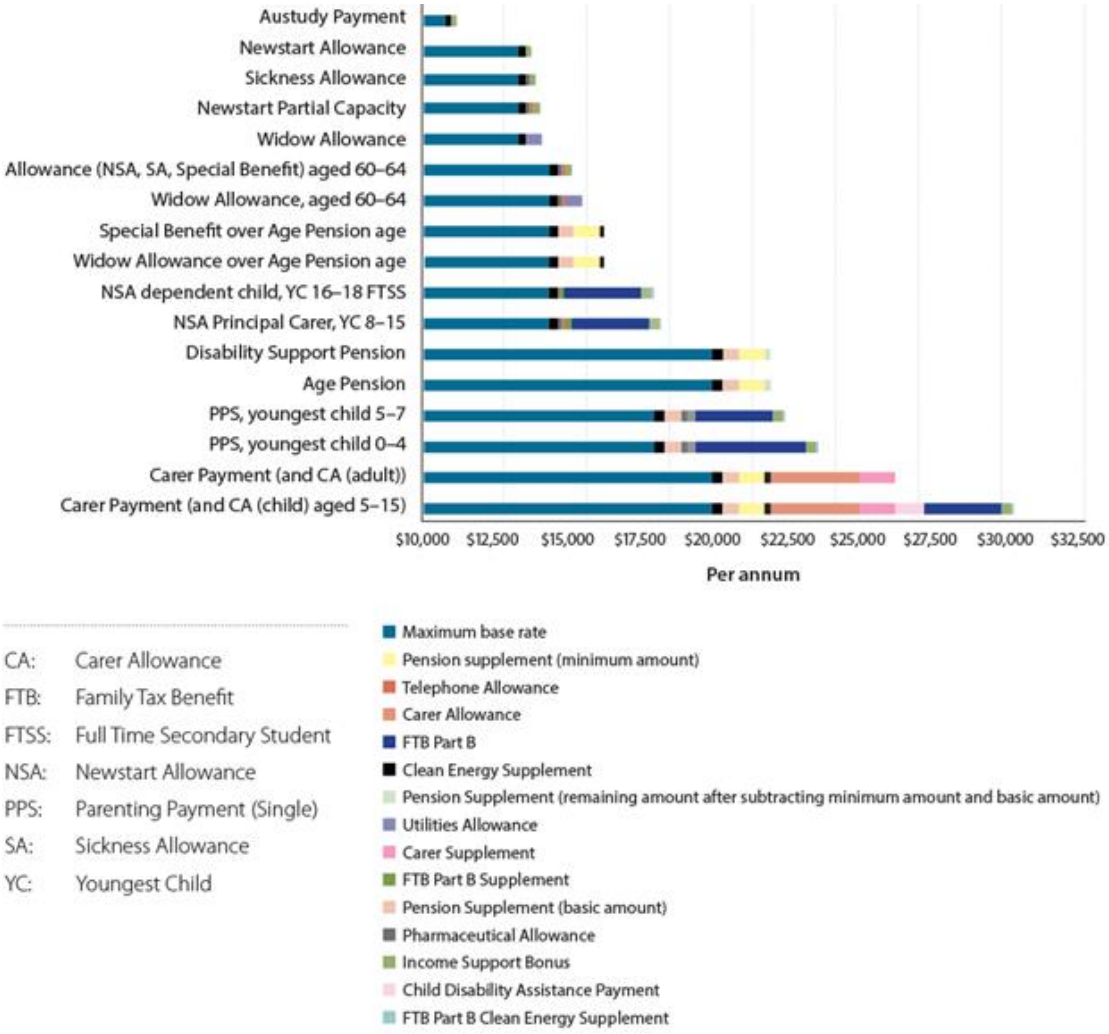
The Federal government supports roughly eight times the level of welfare expenditure per person compared to that of each state. The Federal government is responsible for the delivery of Centrelink benefits, whereas the states provide benefits such as housing and other support services.

The difference in expenditure can be a function of the demographic differences in each state, along with the difference in wealth profiles of the residents and the relative generosity of supports provided as well as the cost of delivering those supports. These factors will also impact the choice of income systems. In order to illustrate the impact of different factors on the utilisation of different income systems, we now explore some case studies.

6 Case Study

The following graphic shows the amount per recipient of the various income support payment available through Centrelink.

Figure 22: Centrelink income support payments



Source: A New system for better employment and social outcomes, page 45. McClure Report

Average annual amounts for disability support or aged pensions are about $22,000 including all of the supplements available. Parenting payments are a little higher.

Family tax benefit A and B can be $11k p.a. in addition to the benefits shown, and these benefits are income tested. In addition to income support, recipients are also able to receive a concession card, which gives discounts on healthcare and other expenditure. This card is perceived to be very valuable by recipients.

The total welfare benefits compare to an average of about $45,000 p.a. in weekly compensation for injured workers.

Therefore, it would appear at first glance that injured workers would stay with workers compensation if they can. However, the total benefit package including Family tax benefit and concession card might make the comparison more even.

Based on the WorkSafe Victoria model, we explore an illustrative example as to how welfare and common law might interact. Take an example of a 60 year old with $45,000p.a. in average wages. The present value of $45,000 for 6 years using the 6% p.a. as per the legislation, results in a total of $221,000 for economic loss. If we allow an extra $100,000 for pain and suffering, this brings total common law damages to $321,000.

We have then used Centrelink's on-line calculator to determine the preclusion period, which is the time before someone can receive any income benefits after they have received common law damages including economic loss components. This calculator assumes that 50% of the claim is for economic loss. Under our example, the exclusion period is 171 weeks or 3.3 years, based on 50% of compensation at $940.20 per week.

In reality, injured workers would be unlikely to earn 6% p.a. on their common law damages. If we assume a discount rate of 1.5% p.a. then the total of $221,000 is really only 5.2 years of benefits at $45,000 per annum. If we consider that the injured worker may have had to pay say $50,000 of their compensation to their solicitor, the total economic loss component could represent 4.0 years of compensation.

This example illustrates the interactions and economic considerations in pursuing common law compared to welfare benefits. However, it is not clear that workers are aware of these considerations when pursuing common law claims, given the complexity of the comparisons involved.

It is our understanding that benefit exclusionary period do not apply to superannuation TPD amounts received. These amounts are treated more in the nature of a capital loss, and are part of means testing for various Centrelink benefits. This could explain the relatively large rise in insurance claims through superannuation compared to damages claims through workers compensation.

Alternative compensation paths for the injured worker, with varying access to Centrelink, and to TPD and common law, are examined below. We have also reduced the benefits for assumed legal fees:

Worker profile:	
Pre-Injury earnings	$45,000
Centrelink benefit	$22,000
Current age	60
Years to retirement	6

		Option 1	Option 2	Option 3	Option 4	Option 5
Lump sum benefits						
Economic loss		$0	$0	$221,280	$221,280	$221,280
Pain and suffering		$0	$0	$0	$100,000	$100,000
TPD		$0	$65,000	$0	$0	$65,000
Total lump sum		$0	$65,000	$221,280	$321,280	$386,280
Legal fees		$0	$10,000	$50,000	$50,000	$60,000
Centrelink exclusion period	(weeks)	-	-	118	171	171
	(years)	-	-	2.3	3.3	3.3
Compensation and welfare benefits to retirement						
Year 1		$22,000	$77,000	$171,280	$271,280	$326,280
Year 2		$22,000	$22,000	$0	$0	$0
Year 3		$22,000	$22,000	$16,214	$0	$0
Year 4		$22,000	$22,000	$22,000	$15,714	$15,714
Year 5		$22,000	$22,000	$22,000	$22,000	$22,000
Year 6		$22,000	$22,000	$22,000	$22,000	$22,000
Total payments		$132,000	$187,000	$253,493	$330,994	$385,994
Average payments p.a.		$22,000	$31,167	$42,249	$55,166	$64,332
		Health care card provides additional benefits				

For an injured worker nearing retirement, the possibility of accessing a lump sum through either the TPD or the common law route, together with Centrelink payments and health care cards benefits, is an attractive option economically. The lump sum gives the worker the ability to pay down the mortgage, or assist children with education costs and the like. With the no-win no-fee solicitor agreements available, workers can readily commit to pursuing lump sum benefits. In the next section, we examine the factors which may be driving behaviours of injured persons.

7 Behavioural Economics

The field of behavioural economics can shed light on the changing trends within income systems. When considering scheme design for injury schemes, or product design for insurance policies, it can be useful to apply the following behavioural lenses.

Firstly, those designing or working in insurance and injury fields often think that people operate from the perspective of Citizen 1. In other words, everyone brings time, attention and ability to all of their interactions with an injury scheme. People plan their lives carefully, and only take into account the facts when making decisions, thinking through the information provided in a rational manner. People are only interested in outcomes which impact them, and operate in a selfish fashion.

Table 5: Behaviours assumed vs reality

Citizen 1	Citizen 2
Time, attention and ability	Limited time, attention and ability
Planner	Present biased
Just the facts	Presentation matters
Personal outcomes, selfish	Social considerations
Rational computer	Looks for cues to take shortcuts

Source: PwC Behavioural economics team

In reality, quite the opposite is true and people behave more like Citizen 2: people have limited time, attention and ability. When dealing with complex injury schemes or insurance products, they do not read the complex and voluminous legalistic documentation provided to them, such as product disclosure statements or many of the standard letters from injury schemes, such as those detailing eligibility decisions.

People are biased towards present outcomes, and use heuristics or other clues to take short cuts in their decision making processes. They also take into account social considerations, rather than operating purely in a selfish manner. Lastly, the way information is presented makes a significant difference in the way people process that information and make decisions.

The following table details other elements of decision making processes from a behavioural economics perspective:

Table 5: Behavioural elements of decision making

Present bias	Weight present day costs and benefits vastly higher than those in the future – even for small delay
Vivid Future	See our future self as a different person – need to see future vividly
Commitment Devices	People might set up future scenarios to lock themselves into difficult behaviours
Channel Effects	The more specifically people plan the more likely to follow through (who, when, where, how)
Deadline Effects	Response to scarcity and possibility of missing out

Reciprocity	Pay from our own pocket/effort to return good gestures (disproportionately)
Punishment	Pay from our own pocket/effort to punish negative gestures (disproportionately)

Anchors	What is a suggestive level or amount that behaviour is adjusted towards?
Messenger	Who is telling us to act – do we like them and do they carry authority?
Primes	What idea, image or emotion is spilling over from one moment into the decision moment?
Defaults	What is the pre-set or do-nothing selection? Choices will tend to end up here more often than not
Affect and Statistics	What emotions are re-weighting statistics?
Norms	We look to what is normal and what others are doing
Heuristics	What back-pocket shortcuts will the human decision maker use to decide when in novel, complex or time-pressured environments?

Source: PwC Behavioural economics team

From an income systems perspective, there are a number of potentially relevant behavioural lenses which impact decision making processes:

- People tend to prefer lump sum compensation rather than on-going periodic payments. There is a perceived inconvenience of having to engage with an injury scheme over a long period of time. However, it is likely that "present bias" also makes the idea of a lump sum more attractive than ongoing payments, especially when we consider that the lump sum is often economically significantly less than the person might receive if they were to stay on periodic benefits. This is particularly the case where the discount rate used for calculating lump sum compensation is high relative to current market rates of return.

- Deadline effects have often been observed in injury schemes, such as the impact of statutes of limitations or implementation dates for changes to benefits. These often cause a rush of claims as people rush to avoid potentially missing out.

- The concept of "punishment" and going out of one's way to punish someone for perceived injustice is very likely involved in the choice of pursuing common law damages. Indeed, injured workers who feel like they have not been treated well by their employer may seek to pursue common law as a form of retribution. ISCRR published research which shows that fault status is an important predictor of functional and quality of life indicators for those injured in road accidents. The perceived injustice of being in an accident where someone else was at fault has an impact on that person's recovery and cost of claim.

- Anchors play a significant role in behaviours. For example, if people are told the maximum amount of compensation available up-front before pursuing damages, they tend to compare the amount they receive unfavourably with this maximum and feel disappointed.

- The messenger effect can be strong with plaintiff solicitor firms who are seen to be on the side of the injured person, advocating for them and taking the risk of the success of the claim through a "no win no fee" arrangement. This effect can be further enhanced through shared stories of successful outcomes through advertising.

8 Conclusion

It is not possible to determine the causes of the trends in claims through superannuation schemes for TPD and income protection policies from analysis of available data alone. At the same time this trend has been emerging, we have also observed some increasing trends in utilisation of common law benefits across a number of injury schemes.

Both of these trends could be impacted by a number of factors, including:

- Changes to benefits within injury schemes, including limiting periods of weekly compensation;
- Changing demographics and changes to welfare, including age pension eligibility rules, combined with the impact on household savings resulting from the GFC; and
- The growth in the plaintiff solicitor market, and increases in advertising of their services.

Behavioural economics can also bring insights into the behaviours of injured workers when making decisions regarding their choices between different income systems.

For those managing injury schemes, it is important to consider the interactions between systems when considering changes to benefits, or designing new claims management approaches.

In an ideal world, income systems would be designed considering the impacts on lifetime income from all potential sources using an investment approach. Such an approach would model the interactions between systems, with the aim of identifying those at risk of poor outcomes and designing interventions or changes to systems to improving outcomes. Such lifetime investment models are gaining popularity in a range of jurisdictions, such as the New Zealand Ministry of Social Defence's model of welfare utilisation.