LEGISLATIVE COUNCIL GENERAL PURPOSE STANDING COMMITTEE No. 1
OUTLINE OF INSURER PERFORMANCE MEASURES AND SCHEME OUTCOMES THAT THE PERFORMANCE MEASURES ARE DESIGNED TO ACHIEVE

This outline has been prepared in order to help the Committee understand the Performance Measures for Insurers and the Scheme outcomes that the Performance Measures are designed to achieve.

This information supplements relevant Insurer Guidelines, and the report of the PricewaterhouseCoopers (PwC) Review of Insurer Remuneration Arrangements (the PwC report), which have already been provided to the Committee.

This summary is divided into parts A and B concerning arrangements for the 2000/01 and 2001/02 remuneration years respectively.

Historically, insurer performance has been measured across various aspects of the Scheme including claims management, injury management and return to work, credit control, accounting, and data quality.

Insurers earned remuneration under a fee package that was determined by WorkCover each year and authorised under section 197 of the 1987 Act. This fee package had 3 components: -

- base service fees allocated to insurers on a market share basis to cover the routine processing of claims and premiums;

- performance fees paid for achieving Scheme benchmarks performance measures for claims/injury management, premium assessment, debt collection, data quality; and

- investment management fees.

It is understood that the Committee will be considering investment management as part of its final report. WorkCover therefore intends to provide details of insurer investment performance measures during the final stage of the Committee's inquiry.

<u>Part A: Outline of Performance Measures for Insurers for the 2000/01 period and Scheme Outcomes that the Performance Measures are designed to achieve:</u>

There are 15 performance measures for the 2000-01 remuneration year.

Measures 1 to 13 are based upon a self-assessment by each insurer of their performance. WorkCover conducts spot check audits on self-assessment results to ensure they were accurate and reported in accordance with the measurement requirements.

For the 2000/01 remuneration period measures 14 and 15 and the tail liability reduction measure are independently assessed by the Scheme's actuary.

Insurers are issued with a statistically appropriate random sample of policies or claims by WorkCover for each specific measure. The insurer then conducts an assessment of their performance based upon the samples supplied and reports their results to WorkCover.

The insurer remuneration package is designed to promote the timely lodgement of self-audit results. Specific provisions relating to timely lodgement include:

- self-audit results are required to be lodged within 3 months from date of issue of audit sample;

- non-lodging insurers after 3 months will be formally advised (including to the insurer's CEO) by WorkCover that they have a further 1-month to lodge results. Failure to do so will result in no performance fees being paid regardless of self-audit results and a financial penalty equivalent to 2% of the insurer's monthly base fee allocation; and

- WorkCover and an insurer (or insurers) may agree on an extension of time for lodgement of results if reasonable grounds for non-lodgement within the 3 month timeframe exist. Extensions are to be agreed before the 3 month deadline (and/or within the further 1 month deadline) and will not be open ended.

Insurers are expected to lodge results of self-audits, regardless of whether they qualify for a performance payment. Refusal or continuing failure to lodge self-audit results can attract ongoing financial penalties.

Individual benchmarks are set for insurer performance against each measure. These benchmarks determine the level of remuneration that insurers stand to receive, ranging from 100% to 0% of the performance fee.

The assessment of insurer performance against performance measures for the 2000/01 remuneration period is currently being finalised, in part, because of concerns raised by WorkCover and insurers regarding the availability of appropriate data from the Workers Compensation Resolution Service, which was meant to be used for assessment purposes.

Many of these performance measures are long-term and dependent on data that takes time to mature. The PwC report indicated that, in particular, long-term performance measures cannot be evaluated during or immediately after the policy/fund period, but are based on late-emerging results, which must mature before their final values can be estimated with any certainty.

Despite the long-term nature of some of these measures, WorkCover is conscious of the need to expedite data collation and analysis of insurer performance. At the Committee's Scheme Design Forum on 15 March 2002 the General Manager of WorkCover indicated that the need to integrate information technology and data management systems throughout the Scheme has become acute.

The General Manager also outlined WorkCover's current strategies to achieve this objective including:

<u>Strategy 1. Customer Contact</u>

Investment in new modern communication infrastructure and customer contact systems focused on customers needs. This will allow easy access to WorkCover services and electronic lodgment and follow up of claims.

Strategy 2. Reporting Channels

Investment in technology that supports decision-making, business intelligence and makes management information accessible. Typically, this strategy involves establishing an enterprise wide data warehouse giving WorkCover analytical processing and data-mining facilities.

Strategy 3. Business Operations

Investment in modern integrated administrative and business operations systems that support single inquiry view of information stored on enterprise platforms.

Strategy 4. Infrastructure, Business Continuity, Gosford Relocation

Investment in modern technology infrastructure to support the business functions and operations of WorkCover.

To help the Committee gain an insight into the range of performance by individual insurers, results for the 1999/00 remuneration period are therefore provided.

Individual Insurer Performance

To comply with the disclosure requirements of the workers compensation legislation WorkCover requested individual insurers to provide their consent to the release of details concerning their performance.

WorkCover did not receive the requisite consent from all insurers until 4 April 2002. Insurers have consented to details of their performance being provided to the Committee subject to a number of conditions.

Insurers would like to highlight that the information relating to the 1999/00 remuneration year is the latest year with information relating to all the remuneration measures. Insurers have indicated that they think it is important that the Committee understands that it is now over 20 months past the end of the assessment period, which in turn convened 12 months earlier.

Insurers have indicated that data for the 1999/00 remuneration period may give a misleading impression of the current performance of an insurer and that the information at best can be considered as “lead indicators” of the performance of individual insurers.

Insurers have also indicated that care needs to be taken to ensure that any information published is not capable of being used to encourage inappropriate market behaviour from other parties involved in the Scheme. Insurers have therefore requested that the names of individual insurers be replaced with a pseudonym. The names of the 8 insurers have therefore been replaced with the letters A to J.

WorkCover intends to provide details on the performance of the remaining insurers once the requisite consent has been received.

Underpinning the 2000/01 performance measures are the below incentives:

Bonus Fees

Bonus fees are paid to good performers (ie above 90% performance levels) out of the remaining pool of performance fees allocated for each measure after all performance fees have been paid. WorkCover has modified the scale of bonuses paid out of the remaining pool to increase payouts to good performers, especially those over 95%.

Achievement Fee

An achievement fee is payable to reward insurers who achieve a high standard of performance across all performance measures. A $2m pool is available and payment is limited to 20% of total bonus paid for that insurer. This payment is over and above any bonus fees paid.

Under Performance Penalty

This measure was introduced for the 2000/01 remuneration period. The 2000/01 remuneration package was designed to ensure that the base fee funds insurer functions to an adequate standard across all activities, in conjunction with performance fees to encourage and reward performance that is better than acceptable.

Historically, some insurers have under performed in some areas with their performance below a satisfactory standard. The performance measures (whilst not covering all facets of the insurer's operations) represent key areas and outcomes that are critical to the Scheme achieving its financial and service delivery objectives.

Consequently, it is not appropriate for insurers to under perform in critical areas that would cause adverse impacts on the Scheme without incurring a financial penalty. Insurers who perform below an adequate standard are required to pay a penalty based on the extent of under performance in that performance measure. This system is commonly referred to as 'clawback'.

The under performance penalty payment will be calculated by applying a progressive percentage to the performance fee capable of being earned for that measure – for example if an insurer achieves a 55% result then a penalty of 40% of that performance fee is payable. In other words, instead of earning a performance fee, if an insurer significantly under performs in that measure, a penalty is incurred.

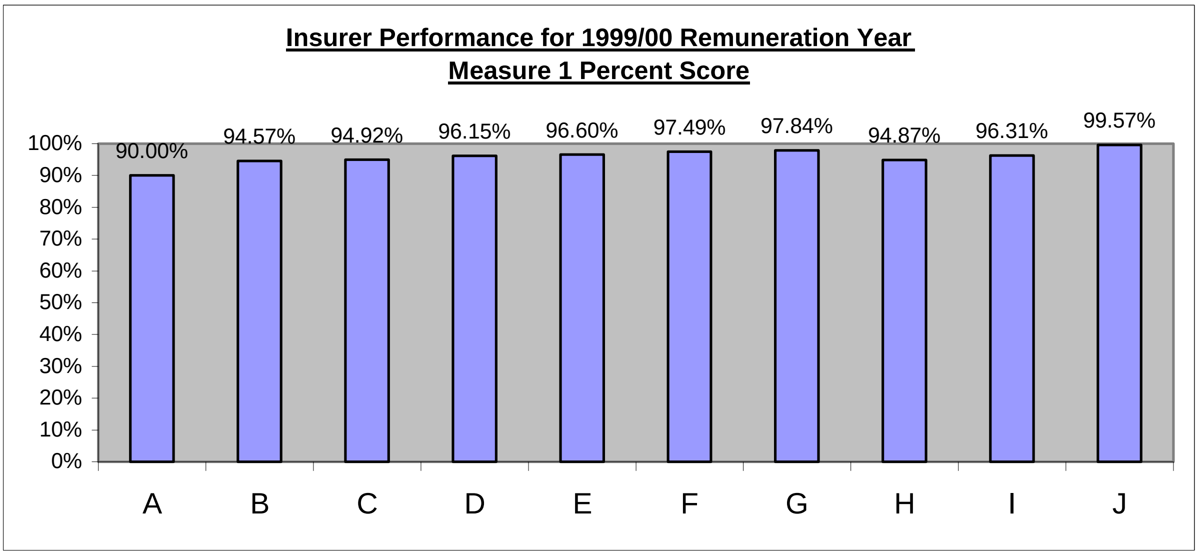
Measure 1 – Correct Tariff Applied to Employers Policies

This measure is designed to ensure that insurers are applying the correct industry classification codes to policies.

Objective

The desired Scheme outcome is that:

- correct premiums are being charged in order to maintain scheme income and ensure equity for all employers; and
- the premium is identical regardless of which insurer issues a policy.

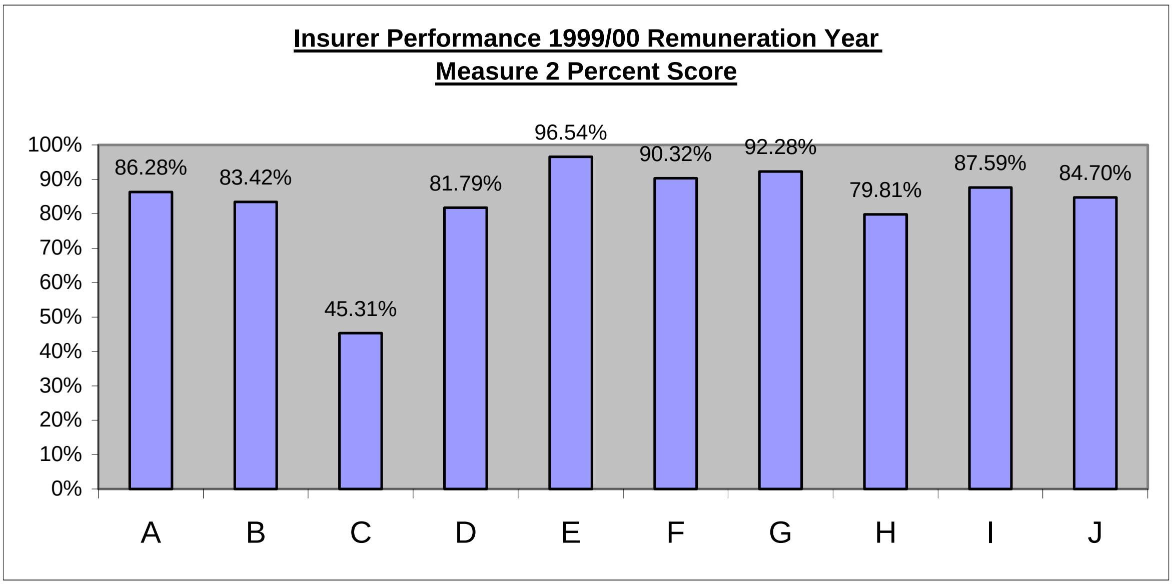


Measure 2- Correct Claims Estimating

This measure is designed to ensure that insurers apply correct claims estimates for premium calculation purposes.

Objective

The desired Scheme outcome is that correct premiums are charged to maintain scheme income and ensure equity for all employers.

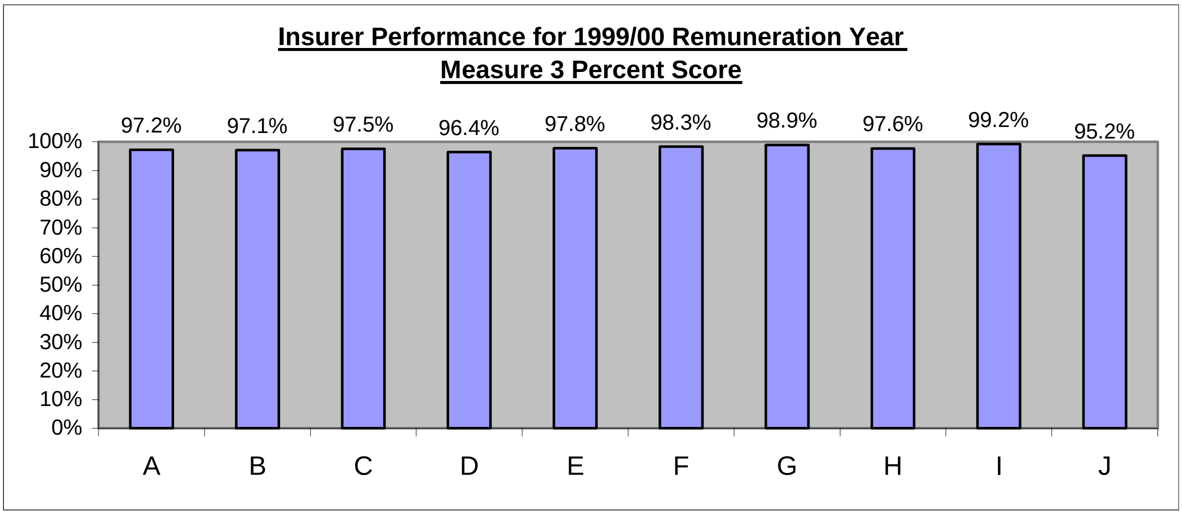


Measure 3 – Ratio of Debt to Gross Written Premium

This measure is designed to ensure that insurers identify overdue/unpaid premiums 'debts' and undertake appropriate debt recovery actions.

Objective

The desired Scheme outcome is to ensure that premium collection is optimised.

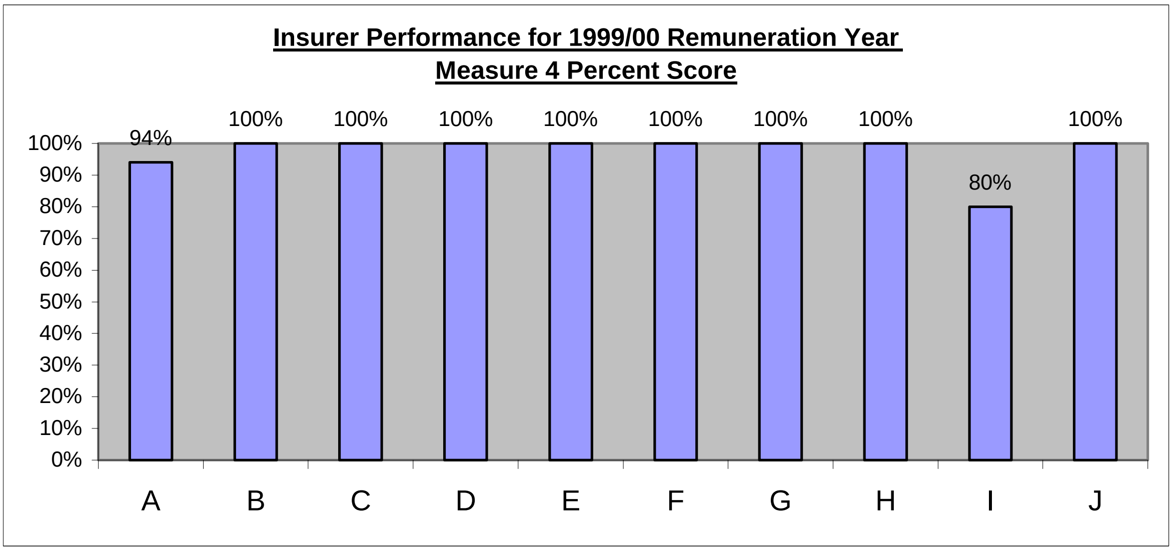


Measure 4 – Data Quality Reporting Standards

This measure is designed to ensure that insurers provide high quality claims/policy data.

Objective

The desired Scheme outcome is to ensure that high quality claims/policy data is compiled in order to enable sound decisions to be made about the Scheme.

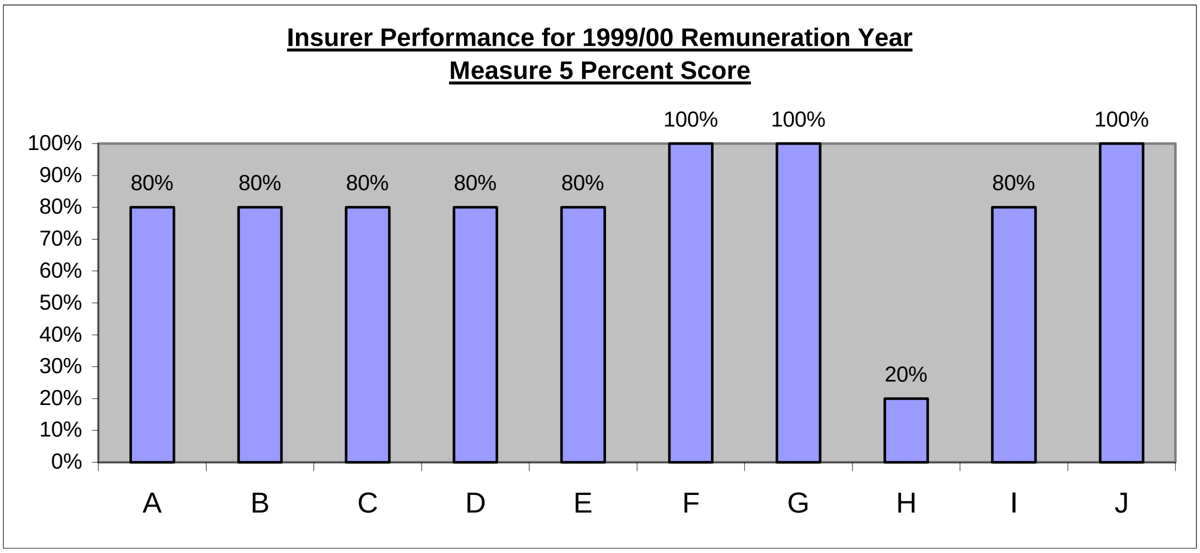


Measure 5 – Reconciliation of Accounting Returns

This measure is designed to ensure that insurers provide high quality accounting returns.

Objective

The desired Scheme outcome is to ensure that high quality accounting returns are compiled in order to enable sound decisions to be made about the Scheme.



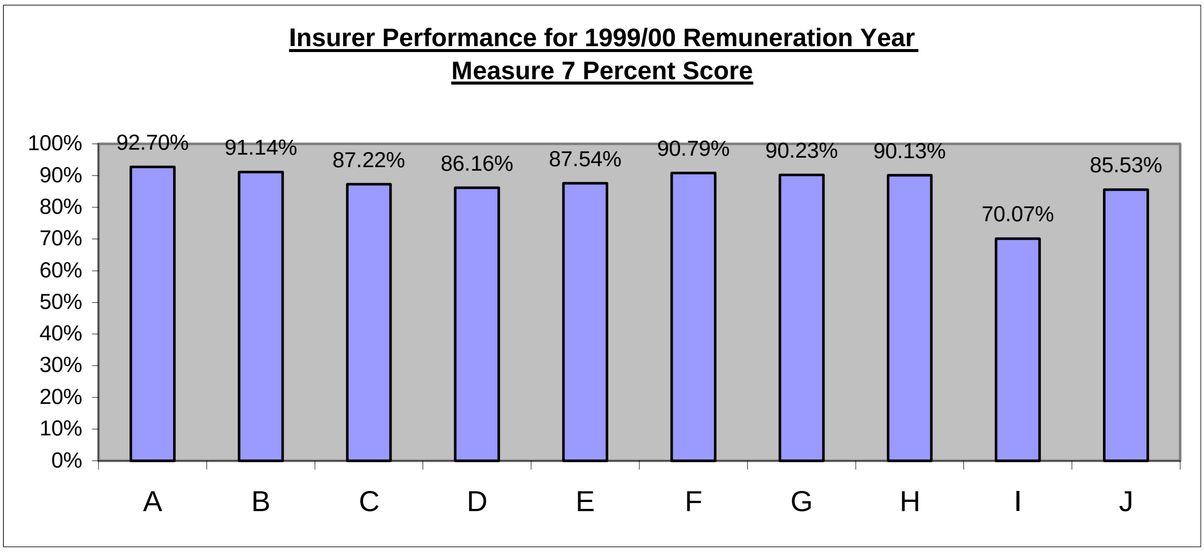
Measure 6 – Discontinued

Measure 7 – Payment of Continuing Benefits

This measure is designed to ensure that insurers make prompt payment of correct benefits to injured workers.

Objective

The desired Scheme outcome is to ensure that injured workers receive their appropriate entitlements promptly.



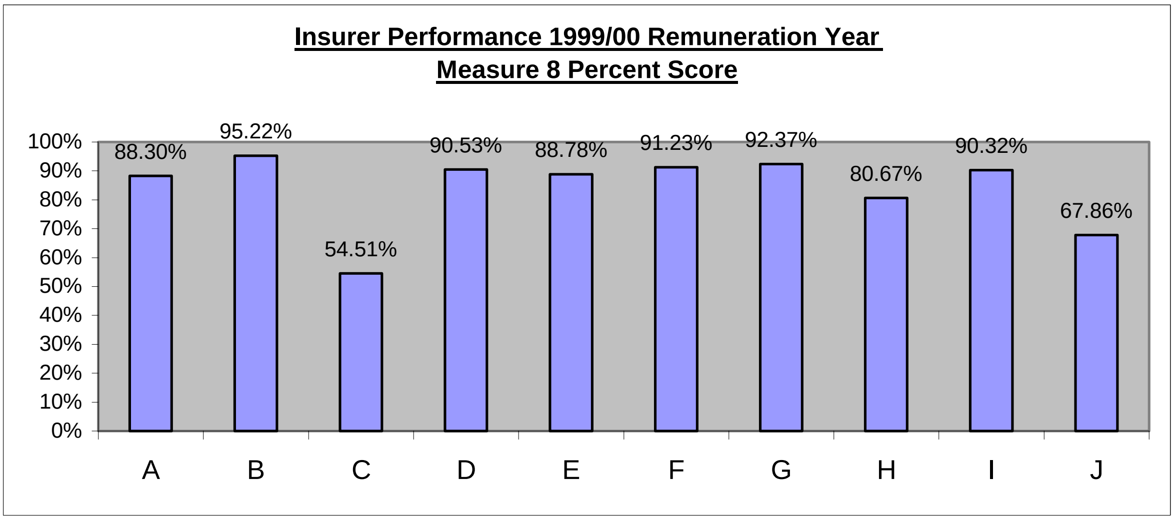
Measure 8 – Soundly Based Decisions

This measure is designed to ensure that insurers make sound decisions in relation to liability.

This measure also serves as a proxy indicator of an insurer's qualitative claim determination process.

Objective

The desired Scheme outcome is to ensure that insurers make appropriate decisions about the liability of claims.

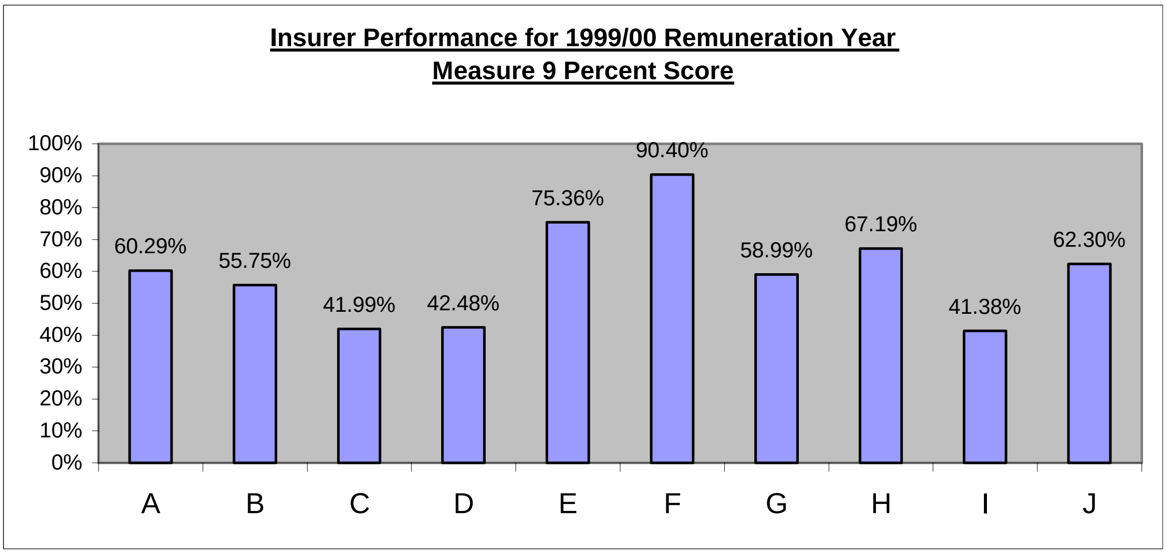


Measure 9 – Timely Offer of Section 66 Entitlements

This measure is designed to ensure that insurers make prompt payment of Section 66 (permanent impairment) benefits to entitled workers.

Objective

The desired Scheme outcome is that injured workers receive their appropriate entitlements promptly.

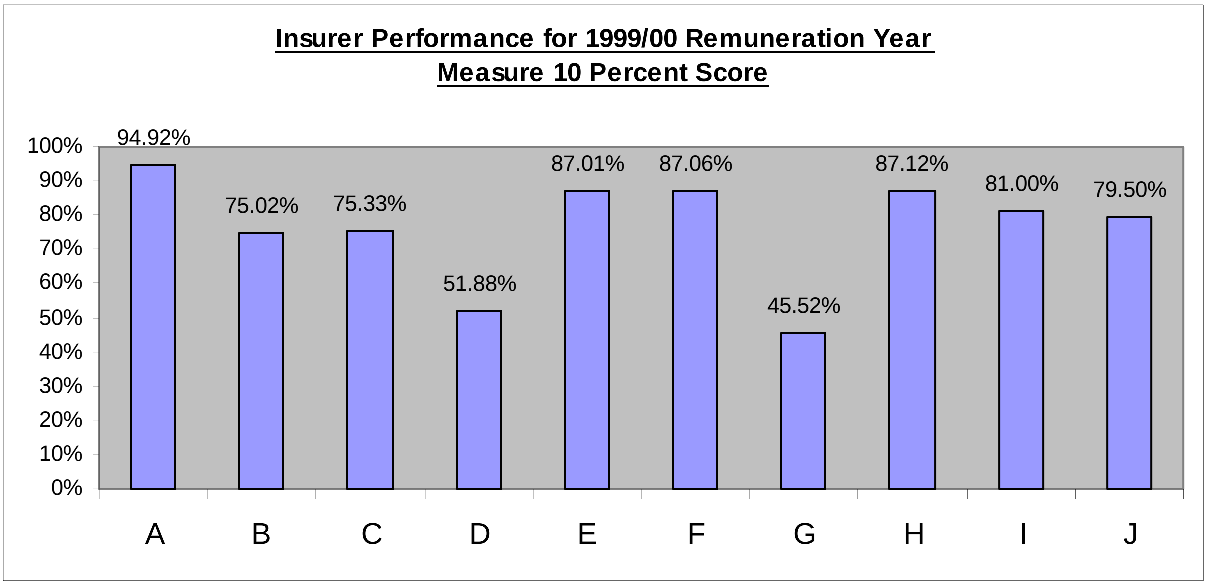


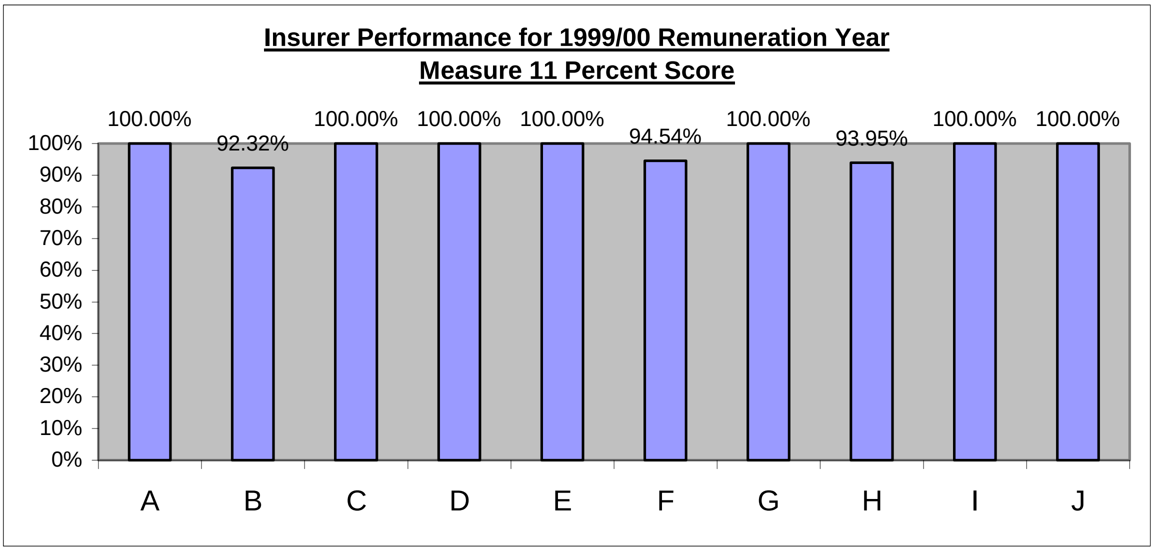
Measures 10 – Proactive Injury Management
Measure 11 – Review of Injury Management Plans

These measures are designed to ensure that insurers proactively manage injuries and conduct regular reviews of injury management outcomes.

Objective

The desired Scheme outcome is that injuries are treated promptly and appropriately and that injured workers can return to sustainable work as quickly and safely as possible.



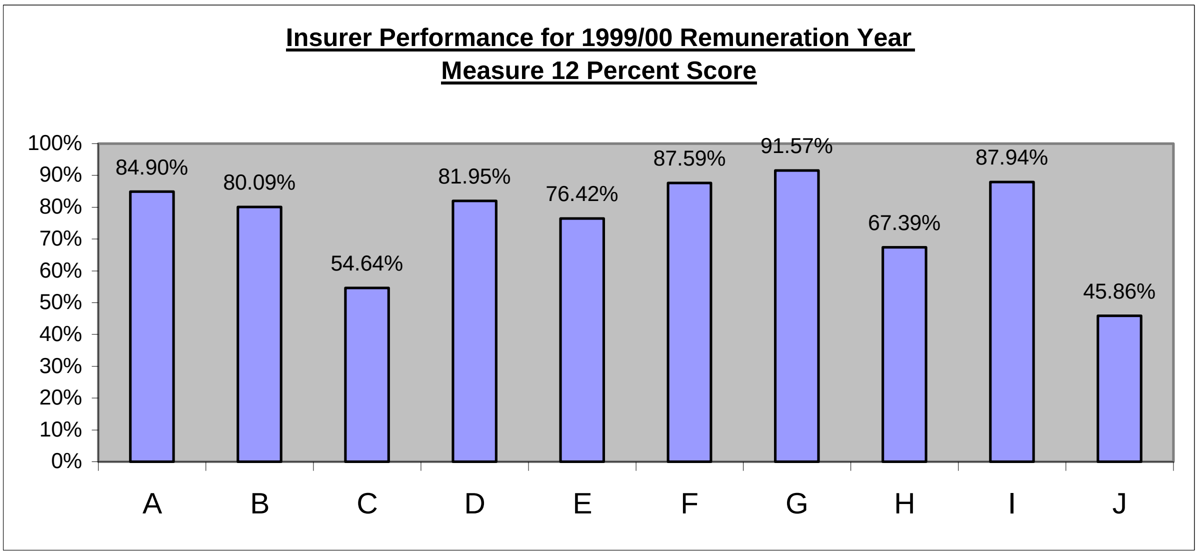


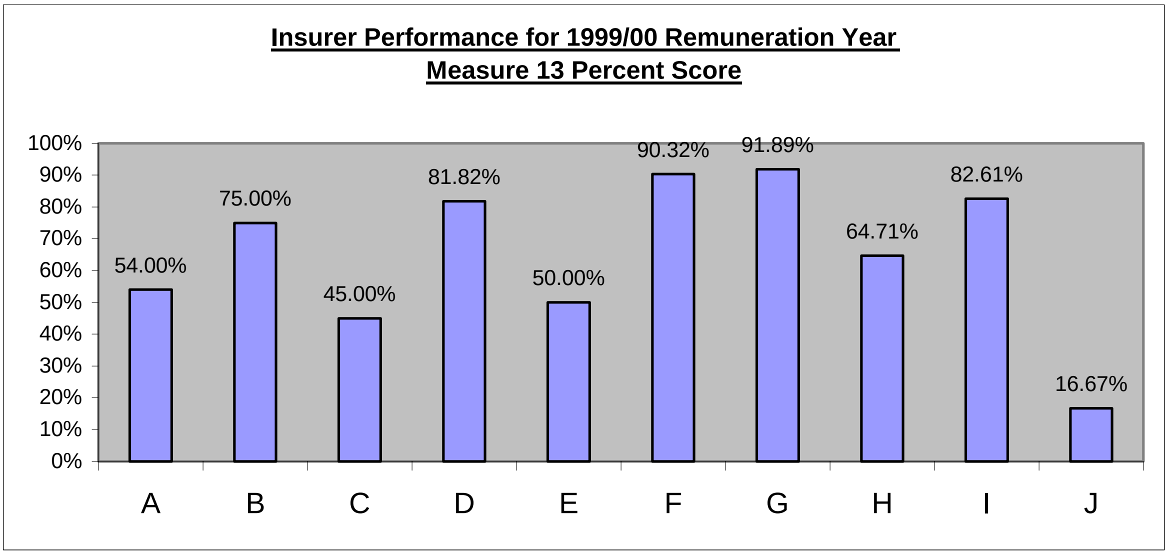
Measure 12 – Injury Management – 21 Day Rule Applied Correctly
Measure 13 – Injury Management – 42 Day Rule Applied Correctly

These measures are designed to ensure that insurers comply with claims handling procedures for paying correct benefits to entitled workers and make timely decisions on liability issues.

Objective

The desired Scheme outcome is to ensure that injured workers receive their initial entitlements promptly.





Measures 14 and 15

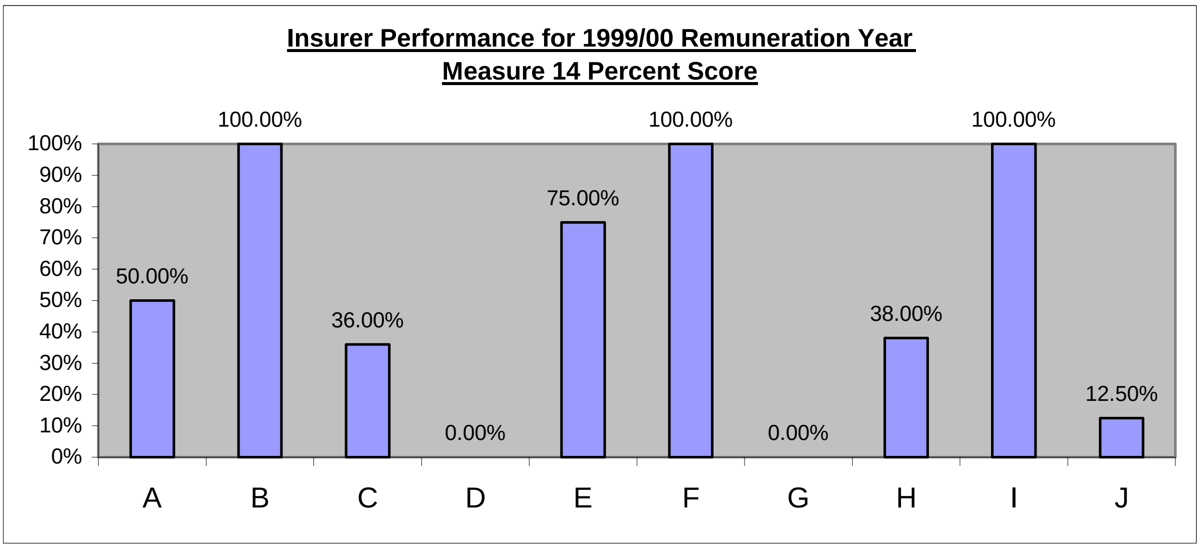
These measures deal with short-term (4 weeks claim duration) and long-term (26 weeks claim duration) injury management.

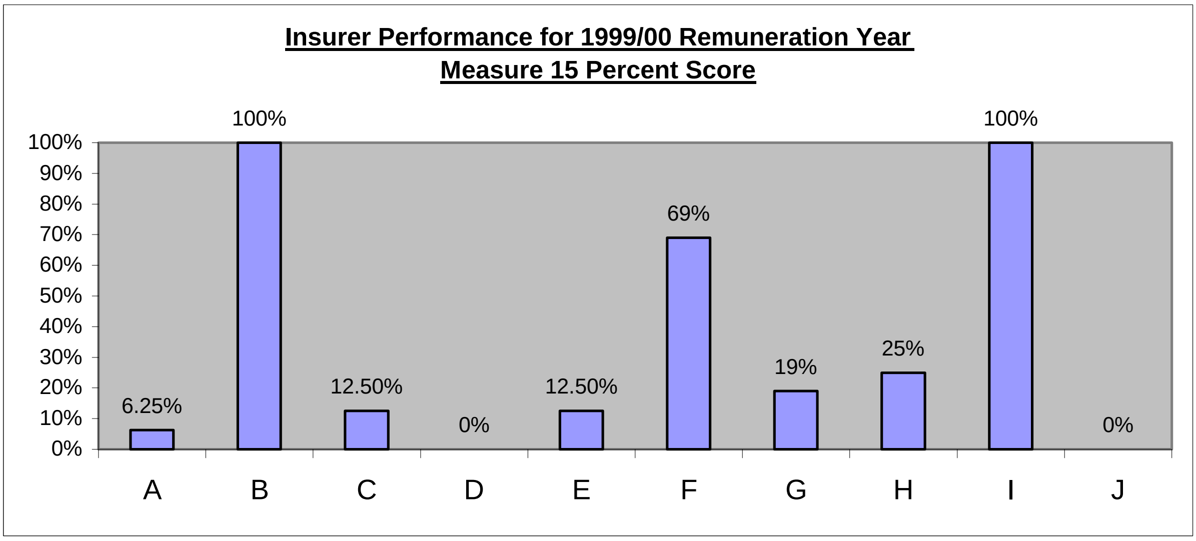
Insurers are measured against return to work benchmarks which require continuous improvement relative to historical performance.

Adjustments are made to benchmarks to allow for variation in industry and claims mix.

Objective

The desired Scheme outcome is to ensure that that insurers manage short-term and long-term claims efficiently and effectively and that injured workers return to sustainable work as quickly and safely as possible.





8% tail liability reduction fee

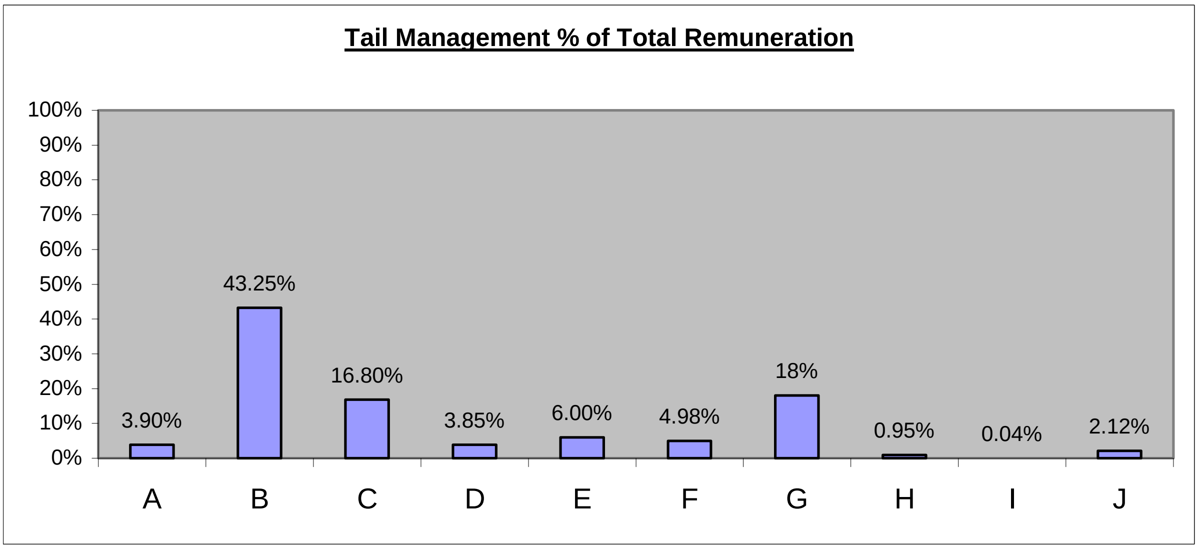
Insurers are paid an additional amount of 8% of the direct cost savings they make in the management of their long-term claims (claim duration of more than 104 weeks).

The savings for the 1999/00 period were assessed by the Scheme's actuary and were subject to peer review by the insurers' nominated actuary (Pricewaterhouse Coopers). The tail measure is open-ended in terms of available remuneration.

This measure is outcomes based and represents one of the most important drivers within the new remuneration arrangements. WorkCover is therefore redesigning this measure for the 2001/02 remuneration period (see below).

Objective

The desired Scheme outcome is to ensure that that insurers manage long-term claims efficiently and effectively and that injured workers return to sustainable work as quickly and safely as possible.



Part B: Outline of Performance Measures for Insurers for the 2001/02 period and Scheme Outcomes that the Performance Measures are designed to achieve:

Historically insurers have performed better in some performance areas than in others. Whilst it is difficult to rate the overall performance of insurers, their performance on average has been found to be of a mediocre standard.

In part, the level of insurer performance has been attributed to the financial incentives under the insurer remuneration arrangements.

It was in this context that in late 2000 WorkCover commissioned PricewaterhouseCoopers (PwC) to conduct a review of insurer remuneration arrangements (the PwC report).

The scope of the PwC review was to examine existing remuneration structures and develop and recommend new arrangements that will:

- provide adequate remuneration for licensed insurers to achieve the Scheme's social and financial objectives;
- ensure that remuneration arrangements are more closely aligned to Scheme objectives;
- ensure that remuneration levels correspond to performance;
- be simple and transparent; and
- minimise the risk of gaming and other aberrant behaviour.

The main conclusions from the PwC report were:

- insurers are currently performing poorly and profitability is low;
- significant investment by insurers in staff and resources (mainly IT systems) is necessary for improved performance;
- insurer management will not invest unless they can see they have a realistic opportunity to achieve an appropriate level of return on their investment, and
- WorkCover will not provide extra remuneration unless it is as a result of a substantial improvement in performance.

The PwC review recommended short-term and long-term performance measures. In general PwC recommended that performance measures be limited to those that have a direct impact on the financial performance of the Scheme or are of greatest importance to final outcomes.

In June 2001 the WorkCover Board approved in-principle PwC's proposed new insurer remuneration package for the 2001/02 remuneration period.

The new remuneration arrangements also complement the implementation of the 2001 legislative reforms including provisional liability and the establishment of the Workers Compensation Commission.

The key element of the new package is to provide insurers with a stronger incentive for improving their performance in delivering Scheme outcomes. Underpinning these performance measures is the performance fee component that stands at nearly 50% for the 2001/2002 period.

These arrangements are designed to give insurers a financial incentive to invest in infrastructure and innovation that will enable them to deliver outcomes that are consistent with the Scheme's social and financial objectives.

For the 2001/2002 remuneration year insurer performance will be measured by a number of 'short term measures', a 'range of service measures' and 'outcome based measures'.

There are 18 performance measures for the 2001-2002 remuneration year. These include 10 service capability index measures, 5 short-term measures, and 3 outcome-based measures.

It is anticipated that the short-term measures and outcome-based measures will generally have a direct impact on the financial performance of the Scheme.

To ensure that insurers achieve optimum performance (across the whole range of short-term and outcome-based measures) their performance fees are based on their overall level of service (aggregated and given a value of between 0% and 100% under the 'service capability index').

These measures are subject to self-audit and/or independent audit review.

Service Capability Index (SCI) measures:

- Correct Claims Estimating (Modified 2000/01 Measure 2)
- Policy and Claims Data (Modified 2000/01 Measure 4)
- Reconciliation of Accounting Returns (Modified 2000/01 Measure 5)
- Payment of Continuous Benefits (Modified 2000/01 Measure 7)
- Timely offer of section 66 Entitlements (Modified 2000/01 Measure 9)
- Proactive Injury Management (Modified 2000/01 Measure 10)
- Timely determination of liability (Modified 2000/01 Measure 12)
- Complaints Handling (New Measure)

  The PwC report recommended that a new outcome-based measure be introduced to enable measurement of 'satisfactory service levels to clients' by 'measuring the level of valid complaints against each insurer over time and in comparison to their market share'.

  For the purposes of this measure a complaint is defined as an expression of dissatisfaction, by any party, which is conveyed to an insurer in writing or verbally with the expectation that it will be remedied by the insurer. This definition is consistent with the Insurance Council of Australia's General Insurance Code.

The Code is a self-regulatory code that aims to raise the standards of practice and service in the insurance industry. The Code was developed in anticipation of legislative changes to the Commonwealth *Insurance Act 1973* which require each authorised general insurer in Australia to adopt a Code of Practice approved by the Commonwealth insurance regulator.

Objective

The desired Scheme outcome is to ensure that insurers provide a satisfactory level of service to clients.

- Market Share Disputes (New Measure)

The PwC report highlighted that as many as ½ of the dispute applications made to the Workers Compensation Resolution Service arose because insurers failed to meet their obligations to inform claimants of a decision on liability within the appropriate timeframe.

The dispute market share measure calculates each insurer's portion of disputes in comparison to their market share.

This measure compliments the commencement of the 2001 legislative reforms including provisional liability and the establishment of the Workers Compensation Commission.

Objective

The desired Scheme outcome of the new market share disputes measure is to encourage open and timely communication and ensure that insurers make timely decisions.

- Paid Survey (New Measure)

The PwC report also recommended the implementation of a 'paid survey' measure to determine stakeholder satisfaction. PwC recommended that the parties that need to be surveyed are:

- injured workers;
- employers;
- medical providers and other providers including rehabilitation providers; and
- Workers Compensation Resolution Service Conciliators, Commissioners and Judges of the Compensation Court.

Because of significant operational changes arising from the commencement of the 2001 reforms (including provisional liability and the commencement of the Workers

Compensation Commission) it was not appropriate to implement this performance measure during the 2001/02 remuneration period.

It is expected that during 2002 WorkCover will conduct a base-line survey in order to develop a performance measure and remuneration structure, which will enable insurers to be paid according to their performance against that base line.

Short-term measures:

The actual amount of performance fees/bonus earned by an insurer for these measures will be subject to that insurer's SCI performance.

The 5 short-term measures are:

- Correct WIC Classification (Modified 2000/01 Measure 1)
- Ratio of Cash Collected to Gross Written Premium (Modified 2000/01 Measure 3)
- Soundly based decisions (Modified 2000/01 Measure 8)
- Review of Injury Management Plans (Modified 2000/01 Measure 11)
- Recoveries (New Measure)

  The new recoveries measure has been implemented for the period 1 January to 30 June 2002.

  This measure is designed to ensure that where appropriate, insurers recover the costs of claims from other sources. The most common sources of recoveries would be where a worker is injured and where another party (covered by a CTP or public liability insurance policy) is at fault.

  Historically, the management of recoveries has not been measured. WorkCover and the insurance industry have agreed that, to be fair measure of performance, remuneration should start at a point that is above the minimum target expected from insurers (based on the previous year's performance).

  Insurers will be paid $1 for every $4 recovered in excess of the minimum target. There is also a bonus pool (made up of fees not earned by other insurers), which will be distributed amongst insurers who recover more than their quota.

  Objective

  The desired Scheme outcome of the new recoveries measure is to ensure that that insurers achieve optimum recoveries in order to reduce the underlying costs of the Scheme.

Outcome-based measures:

The actual amount of performance fees/bonus earned by an insurer will be subject to that insurer's SCI performance (except tail management fees which are open ended).

The 3 outcome-based measures are:

- Tail Management (New 8% tail liability measure replacing the 2000/01 tail liability measure)

  This measure is one entirely outcomes based and represents one of the most important drivers within the new remuneration arrangements.

  WorkCover and insurers are therefore redesigning this measure for the 2001/02 remuneration period on the following basis:

  - actuarial approach has been maintained;

  - measure will assess two components separately, common law and the remainder; and

  - each component will be assessed on absolute and improved elements.

- Loss Ratio (New Measure)

  The PwC report recommended that an outcome-based loss ratio measure similar in concept to that in Victoria be introduced. PwC recommended however that a separate loss ratio for each policy year be used instead of a cumulative loss ratio.

  The PwC report also indicated that developing a fair performance measure was problematic.

  This measure is one entirely outcomes based and represents one of the most important drivers within the new remuneration arrangements.

  WorkCover and insurers are therefore currently developing a loss ratio performance measure on the following basis:

  - measure being totally outcomes based;

  - measure based over five years;

  - each fund year assessed separately;

  - the denominator will be the true premium that would be payable by an employer if the Scheme was fully funded;

  - claims cost will be balanced to the Scheme's actuarial assessment; and

  - insurers will receive a percentage of the savings achieved for the Scheme.

- Return to work (New return to work measure replacing 2000/01 measures 14 and 15)

  WorkCover and insurers are redesigning this measure for the 2001/02 remuneration period on the following basis:

- measure will be based on duration;
- claims included in the measure will be 3 – 5 years; and
- measure will aim to reward continuous improvement of claims reported on or after 1 January 2001.