

## **Appendix 5**

# **Auditor-General's Report to Parliament 2001**

## **Volume 7**

### **WorkCover Scheme**

### **Statutory Funds**

## WorkCover Scheme Statutory Funds

The WorkCover Scheme Statutory Funds consist of separate funds maintained by individual licensed insurers as a requirement of the *Workers Compensation Act 1987*. WorkCover has prepared the results and financial position of the Scheme Statutory Funds (the Scheme) in accordance with the requirements of Australian Accounting Standard AAS 26 'Financial Reporting of General Insurance Activities' based on audited returns provided by the licensed insurers. The Scheme financial statements are included by way of Note (Note 26) to the WorkCover Authority financial statements.

### KEY ISSUES

#### WorkCover Scheme Results

The operating results of the Scheme for the last seven years have been:

Year ended 30 June	2001 \$m	2000 \$m	1999 \$m	1998 \$m	1997 \$m	1996 \$m	1995 \$m
Underwriting loss	(1,359)	(390)	(167)	(1,166)	(953)	(760)	(594)
Other income(a)	242	387	205	280	618	249	272
Total loss/excess of income over expenditure	(1,117)	(3)	38	(886)	(335)	(511)	(322)

(a) Other income represents the net result of investment and other income, and other operating expenses.

The WorkCover Scheme had a loss of \$1,117 million in 2000–01, compared to a loss of \$2.7 million in 1999–2000. This very significant increase resulted mainly from the increase in the Outstanding Claims Provision. WorkCover's actuaries have stated that claims costs have increased mainly because of:

- ◆ the recognition of a 35 per cent per annum historical underlying growth rate in common law numbers in the actuarial modelling. This growth rate is net of the observed acceleration in reporting of common law claims. The actuaries assume this is due to the uncertainty surrounding future access by workers to common law
- ◆ an increase in the number of future commutations, based on an observed increase in commutation settlements over the last six months to 30 June 2001.

The accumulated deficit of the Scheme, represented by the excess of liabilities over assets, as at 30 June 2001 is \$2,756 million (\$1,639 million in 2000).

The WorkCover actuaries' projection of the Scheme deficit is that it will grow from \$2,756 million to around \$5,468 million by June 2006, assuming no change in current premium rates. They state that they have made no explicit allowance for the effect of any prospective changes to the Scheme structure. This would include changes introduced in Parliament in June 2001 but not passed at the time of the actuaries' projections.

The actuaries' report shows that the estimated breakeven premium rate for the Scheme for 2000–01, as a percentage of wages, would have been 3.06 per cent. This compares to the actual collected rate of 2.7 per cent. The breakeven rate going forward is estimated to be 3.13 percent of wages, gross of GST.

### Scheme Reforms

The *Workers Compensation Legislation Amendment Act 2001* (the Act) was assented to on 17 July 2001. It amends the *Workers Compensation Act 1987* and its companion Act, the *Workplace Injury Management and Workers Compensation Act 1998*. The Act makes extensive reforms to claims procedures, dispute resolution, commutation, lump sum compensation, and common law damages.

The main aim of the Act is to reduce the high rate of disputes surrounding workers compensation claims and to quickly, and at less cost, resolve those disputes. Key features of the Act are the establishment of a Workers Compensation Commission, a new Claims Advisory Service, streamlined and simplified procedures for claims processing and the development of objective guidelines for measuring permanent impairment. The new Workers Compensation Commission will replace the Workers Compensation Resolution Service and is expected to operate from January 2002.

After negotiations with stakeholders, the Government agreed to defer certain aspects of the reform agenda, namely the common law issues, which were referred to a judicial inquiry headed by Justice Sheahan. Justice Sheahan issued his report on 31 August 2001, making the following recommendations:

- ◆ common law actions available to workers against employers be limited to economic loss damages, which should remain 'capped' and calculated only to age 65
- ◆ only workers assessed to have 'whole person' impairment of 20 per cent or more should be entitled to make a common law claim for economic loss damages
- ◆ as soon as the Scheme's financial position permits, there should be a reinstatement of indexation of benefits, and the maximum amount recoverable be increased gradually to \$250,000 and indexed thereafter
- ◆ common law actions for employment injuries be dealt with normally by the District Court, but without juries
- ◆ compliance with a pre-litigation process aimed at early and cost-effective settlement of the claim, is to be a condition precedent to commencing proceedings for common law damages
- ◆ a range of procedural reforms and new rules regarding legal costs.

The reforms relating to permanent impairment of workers were deferred pending discussions with stakeholders, and the development of guidelines for the assessment of permanent impairment. The *Workers Compensation (Further Amendment) Bill 2001* has recently been released and was expected to be introduced into Parliament in late November 2001. The Bill gives effect to the Sheahan recommendations and addresses the permanent impairment criteria.

### Financial Viability of the Scheme

The large increase in the deficit of the Scheme was a cause of concern after the relative stability over the past two years. However we did not issue a qualified audit opinion in respect of the going concern basis of the Scheme because:

- ◆ the Scheme as at 30 June 2001 had nearly \$6 billion in investments. Based on claims payment experience, this should be sufficient to ensure that claims can be paid as and when they fall due for a number of years
- ◆ the legislation allows for funding of the Scheme deficit by the levying of a contribution on employers as part of future premiums
- ◆ the Government's reform initiatives outlined earlier are expected to reduce Scheme costs.

### *WorkCover Scheme Statutory Funds*

### Control of the Scheme

As we have reported over a number of years, the Scheme does not form part of the whole-of-Government financial report. Our view is that the Scheme Statutory Funds are controlled by the State under the definition of control in Australian Accounting Standard AAS 24 "Consolidated Financial Reports". We believe the Government has the capacity to dominate decision-making in relation to the financial and operating policies of the Scheme, partly because it has the legislative power to give policy directions and it has the ability to set premiums and to determine the range of benefits under the Scheme.

Last year, and again this year, we qualified the Independent Audit Report on the Total State Sector Accounts because the assets and liabilities of the Scheme Statutory Funds have not been consolidated into those Accounts.

### Parliamentary Committee

On 28 June 2001 the Legislative Council resolved that General Purpose Standing Committee No. 1 address various workers compensation issues. The Council's resolution gave the Committee the following functions:

- ♦ to monitor the financial position of the workers compensation scheme under the Workers Compensation Act 1987 and the Workplace Injury Management and Workers Compensation Act 1998
- ♦ to monitor and review the implementation and operation of the Workers Compensation Legislation Amendment Bill 2001 (No 2), as finally passed by the Parliament
- ♦ to investigate and report on the efficiency of the operation of the workers compensation system and the administration of the WorkCover Authority, and
- ♦ to monitor the impact on premiums of the bill.

The Committee has issued a first interim report outlining background information, but is yet to make any recommendations.

### Abridged Statement of Financial Performance

Year ended 30 June	2001 \$'000	2000 \$'000
<b>REVENUES</b>		
Net earned premiums	1,958,099	1,906,246
Investment income	451,220	528,057
Other income	<u>15,936</u>	<u>12,494</u>
<b>TOTAL REVENUES</b>	<b><u>2,425,255</u></b>	<b><u>2,446,797</u></b>
Net claims incurred	3,317,434	2,296,616
Insurers management fees	160,903	134,654
Other expenses	<u>64,024</u>	<u>18,267</u>
<b>TOTAL EXPENSES</b>	<b><u>3,542,361</u></b>	<b><u>2,449,537</u></b>
<b>OPERATING DEFICIT</b>	<b><u>(1,117,106)</u></b>	<b><u>(2,740)</u></b>

*WorkCover Scheme Statutory Funds*

**Abridged Statement of Financial Position**

At 30 June	2001 \$'000	2000 \$'000
Current assets	1,700,839	1,600,027
Non-current assets	<u>4,742,464</u>	<u>4,717,292</u>
<b>TOTAL ASSETS</b>	<b><u>6,443,303</u></b>	<b><u>6,317,319</u></b>
Current liabilities	2,907,206	2,317,830
Non-current liabilities	<u>6,292,000</u>	<u>5,638,286</u>
<b>TOTAL LIABILITIES</b>	<b><u>9,199,206</u></b>	<b><u>7,956,116</u></b>
<b>NET LIABILITIES (ACCUMULATED DEFICIT)</b>	<b><u>(2,755,903)</u></b>	<b><u>(1,638,797)</u></b>

Assets consist mainly of current investments, \$1,355 million (\$1,330 million in 2000) and non-current investments of \$4,510 million (\$4,469 million). Investments are mainly fixed interest securities, \$1,895 million (\$1,891 million), Australian equities, \$1,095 million (\$1,131 million), bank and non-bank bills \$1,087 million (\$1,058 million) and CPI Bonds \$865 million (\$814 million).

The major components of the outstanding claims liability of \$8,631 million (\$7,432 million) were: weekly benefits, 11.4 per cent (15.1 per cent); commutations, 21.0 per cent (22.3 per cent); legal costs, 19.3 per cent (19.0 per cent); and common law claims, 27.1 per cent (18.8 per cent).

The outstanding claims liability is an actuarially determined amount and is subject to considerable uncertainty.