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SUPPLEMENTARY SUBMISSION TO STANDING COMMITTEE ON LAW AND JUSTICE

Buying in to the LTCS Scheme

The Parliament has recently passed the Motor Accidents (Lifetime Care and Support) Amendment Bill 2009. It is this Bill that creates the opportunity for recipients of lump sum compensation from accidents occurring before the introduction of the LTCS scheme to buy into the scheme.

The reading speeches in support of the 2009 Bill indicated that this new measure would be fully funded. In other words, the cost of buying in would be the real commercial cost of providing a lifetime of care.

Prior to the passage of the bill the legal profession provided a submission to the Parliament pointing out that if those receiving lump sum compensation were charged a proper commercial rate then they would not be able to afford to buy in. Their compensation would be inadequate to cover the commercial cost of their future care. The reason for this was the 5% discount rate used by the Motor Accidents Compensation Act 1999.

The Discount Rate

In calculating an award for damages the court is required to use a discount rate of 5%. The discount supposedly represents the financial benefit to the recipient in having an upfront lump sum to cover future costs. A discount rate is usually calculated by reference to:-

Investment return - inflation - tax paid.

The legal profession has been shown some early modelling from the LTCS Authority – their "costs calculator". They have assumed a 6% return on investment and 4% inflation – a net discount rate of 2%.

An accident victim receiving a lump sum calculated at a 5% discount rate is not going to be able to afford the LTCS Authority buy-in calculated at 2%. Take the following examples: -

a) If care, treatment and the like cost $5,000 per week and the claimant/purchaser has a life expectancy of a further 30 years then the damages awarded (at 5%) will be $4.1 million. The buy in price charged by the LTCS Authority (at 2%) will be $5.9 million. There is a $1.8 million between the compensation recovered and the buy in price.

b) If the participant is a child who has a further 50 years to live then the differential is even more stark. At $5,000 per week the child will

receive $4.9 million in compensation. The LTCS Authority buy in price will be $8.3 million, a gap of $3.4 million.

It has been long understood that accident victims run out money. It is not necessarily because they spend it foolishly. A 5% discount rate chronically over estimates the return on funds invested. The common law discount rate in Australia (devised by the High Court) is 3%. In England the discount rate is even lower. The LTCS Authority have calculated that a proper commercial discount rate is 2%.

Having a 5% discount rate means that accident victims are not properly compensated. The accident victim subsidises the motor accident scheme and the price of green slips. The discount rate used by the motor accident scheme should be 2% or 3%. The Ipp review of personal injury law recommend 3%.

With regards the buy in provision, the maths is fairly simple – either the Authority does not charge on a fully funded basis or accident victims cannot afford to buy into the scheme using their lump sum compensation.