*Your health is all that matters.*

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6 June 2013

Committee Secretary
Senate Standing Committees on Community Affairs
PO Box 6100
Parliament House
Canberra ACT 2600
Australia

Dear Committee Secretary,

Please find attached a copy of HBF's January 2013 submission to the Senate regarding the Private Health Insurance Amendment (Lifetime Health Cover Loading and Other Measures) Bill 2012 in support of our submission to the Private Health Insurance Legislation Amendment (Base Premium) Bill 2013. We are providing this as supporting documentation as we believe both Bills and our comments should be considered in the context of each other.

With regard to the Lifetime Health Cover Loading Bill, we have had continuing contact with the relevant government departments in an attempt to obtain greater clarification and address our concerns. To date however, there has been little written clarification provided.

One particular area of concern is the notice period required to give to members in relation to direct debits. Consequently, we request that the effective implementation date of the LHC Bill be postponed to provide sufficient time for the detail to be clarified, changes to be implemented effectively and appropriate notice to be provided. This may only be a short period but sufficient to address the issues.

Yours sincerely

Rob Bramsby
Managing Director

16 January 2013

Mr Gerry McInally
A/g Secretary
Standing Committee on Community Affairs
Legislation Committee
PO Box 6100
Parliament House Canberra 2600

Dear Mr McInally

**Submission on Private Health Insurance Amendment Bill**

Thank you for the opportunity to provide input to the Senate Inquiry into the Private Health Insurance Amendment (Lifetime Health Cover Loading and Other Measures) Bill 2012.

HBF is a not-for-profit company that insures the health of nearly 900,000 members in Western Australia. Nearly 48,000 of these members are subject to Lifetime Health Cover loading and in the interests of these members and the wider WA community we would like to raise several areas of concern regarding this proposed legislative change.

***Lifetime Health Cover (LHC)***

Removing the Australian Government Rebate on private health insurance (Rebate) from the LHC portion of premiums will have significant negative effects on private health insurance members subject to loading.

If the Rebate does not apply to the LHC loading proportion, the premium payable will increase, in some cases substantially. Tens of thousands of WA members will see their premiums rise by hundreds of dollars per year. Many of these are older Australians on fixed incomes who will be subjected to considerable financial stress by the proposed changes. In the current economic climate, this will mean that for many members private health insurance will become unaffordable and they may choose to cancel their health insurance and rely on an already overstretched public hospital system, to the detriment of the community as a whole.

Further, the financial considerations are likely to affect the products selected by members with a limited budget. For example, an older person with a high LHC loading may, for financial reasons, select a product designed for a younger demographic that excludes certain procedures. The impact of this is twofold; firstly, upward premium pressure on the lower price point products and secondly, the individual will have to rely on the public health system where their treatment is excluded on their product.

Health fund members who have taken out health cover despite knowing that they will be subject to LHC loading of up to 70% have done so on the understanding that the government has committed to paying the Rebate on their loading for the ten year penalty period. Removing the Rebate when these members are partway through their ten year period can only be regarded as a breach of good faith on the part of the government. HBF believes that if this measure is to be introduced it should apply only to those who take out health cover in the future and that current health fund members should be exempted.

***Administrative areas requiring clarification***

It is estimated that approximately one million Australians are subject to LHC loading, however the government has not detailed any major communication strategy to notify affected members of the removal of the Rebate from their loading. This means that private health insurers will be left to communicate the negative effect of these changes to their members.

The difficulties of such a communication are compounded by the fact that insurers have already been required to make substantial changes to tax information provided to members and the ATO files we submit for this financial year. Given we are still awaiting the ATO requirements for the tax changes and clarification around the application of any loading removal, there is an extremely limited timeframe and it is difficult to prepare an appropriate message for our members.

From an administrative perspective, clarification is required as to how any removal of Rebate from loading would be applied. Earlier discussions indicated that the removal of Rebate from the LHC loading portion of the premium may be different to how we apply rebate tiers to payments (ie: based on period of cover rather than just the date the payment is made). Prompt clarification of the manner in which the Rebate removal is to be applied would be appreciated, as it will assist funds in making necessary amendments to their systems.

***Incentives Payment Scheme (IPS)***

Whilst HBF recognise that the majority of members receive their Rebate as a direct reduction of their premium, the move to cease the Incentives Payment Scheme (IPS) will impact a proportion of members. Members who do not lodge an income tax return and are not registered to receive their Rebate as a reduced premium will have no mechanism to receive their Rebate. The same situation applies if a member has nominated a tier lower than what they are entitled to and needs to claim the difference.

The introduction of rebate tiers has meant that some members are making the decision not to register for the Rebate as a reduced premium, particularly those who are unsure of their projected income. Those members who do not lodge a tax return will have no method to receive the Rebate if the IPS is ceased.

HBF would suggest that, if the IPS is ceased, there should be other provisions to ensure these members are not disadvantaged and can still receive their Rebate entitlement.

It is understood that the approximately 6,000 people claiming the Rebate via the Incentives Payment Scheme will receive a letter from the government notifying them that this option is ceasing from 1 July 2013. Since they are unable to retrospectively receive the Rebate as a premium reduction and not all may submit a tax return, we would like clarification of any transitional arrangements. For example, will a member be able to claim under the IPS after 1 July 2013 for payments made (and covering a period) prior to that date? If not, what solutions are proposed?

Thank you once again for the opportunity to provide a submission on behalf of our members.

Yours sincerely

Rob Bransby
Managing Director

6 June 2013

Committee Secretary
Senate Standing Committees on Community Affairs
PO Box 6100
Parliament House
Canberra ACT 2600
Australia

Dear Committee Secretary

**Private Health Insurance Legislation Amendment (Base Premium) Bill 2013**

Thank you for the opportunity to provide input to the Senate Inquiry into the proposed Private Health Insurance Legislation Amendment (Base Premium) Bill 2013.

HBF is a not-for-profit company that insures the health of over 900,000 members (55.8% of the market) in Western Australia.

Our focus as the dominant health insurer in WA is to:

- Ensure access to quality services when needed (we have contracts with 38 Private hospital providers in WA – more than any other major fund);
- Keep the cost of premiums affordable (with the lowest premium increase in April 2013 of any major fund); and
- Keeping the difference between benefits paid and fees charges by providers to a minimum (we cover more hospital related charges in WA than any other major fund).

With regards to the proposed legislative changes, HBF have reviewed the legislation in terms of the potential to:

- Support the objectives of the Australian Government Rebate i.e. maintain an appropriate balance between public and private health care by providing support to those that choose to pay for private health insurance;
- Drive competition; and
- Provide transparency and ease of access for consumers.

In this context, we have a number of concerns relating to the above mentioned Bill, as well as the changes to Lifetime Health Cover which have recently been passed, including:

- **Timing** – if LHC is to be applied from July 1 2013, there is a very short timeline to make system changes, notify members and most importantly provide the appropriate notice period for changes to direct debits.
- **Impacts on affordability** for consumers, highlighting a potential 1.12% increase in premiums by 2016 (on top of the normal yearly increases);
- **Price elasticity**, indicating that healthy, low claiming members are more likely to down-grade or drop their cover;
- Issues of **under-insurance,** increasing pressure on the public health system, and creating disillusionment with PHI;

- **The exponential increase in the complexity** of private health insurance offerings when you compound all the recent changes based on income, age and now CPI.
- **A severe lack of detail** in the legislation making assessments about implementation impossible at this stage (this includes any clarity on tax statements, new products, new entrants to the market etc.)
- **The cost of implementation** (which ultimately impacts our premium increases) and the ongoing administration issues associated with the legislation; and
- **The basis for indexation** - complications around indexing the rebate at a product level and the dilution of competition if its applied at an industry level.

In response to these concerns, we recommend:

- Postponing the effective implementation date of the Lifetime Health Cover (LHC) loading amendments to provide sufficient time for the detail of both bills to be clarified, changes to be implemented effectively and appropriate notice to members be provided.
- Using the Health CPI as the basis for indexation as opposed to the All Groups CPI;
- Utilising the state based CPI instead of the weighted average of the 8 capital cities;
- Indexing the rebate at a fund level rather than product or industry level to maximise competition; and
- Deregulation of the private health insurance premium increase process now that the government has a diminishing and capped interest in any future increases.

More detail is provided in our submission below and our earlier submission on the Private Health Insurance Amendment (Lifetime Health Cover Loading and Other Measures) Bill 2012 (attached).

## 1. Current Situation

Currently, the Government supports consumers of private health insurance by providing a set rebate percentage (based on age and income) regardless of the type of policy held. The current rebate structure supports those consumers that pay for private health insurance in addition to their Medicare rebate and has significantly contributed to the current high levels of private health insurance participation (54.3%[1]) and a good balance between public and private care.

## 2. Proposed Legislative Changes

The changes that have recently been passed by the Legislative Assembly and which are soon to be considered by the Senate, propose to index the rebate by the lower of CPI or the premium charged by the private health insurer.

Assuming health fund increases will be greater than CPI (as has been the case historically due to health inflation), the result is a gradual reduction of government support via the rebate.

[1] As at June 2012

## 3. Impacts of the Proposed Legislative Changes

### 3.1. Affordability

#### 3.1.1. Expected increase to member contributions

The proposed changes to the rebate are expected to drive the overall health insurance price upward. HBF analysis indicates that a hospital and ancillary product combination with the average premium increase in April 2013 will be significantly impacted by the legislative changes. Based on recent CPI trends, we estimate that by 2016, members will be paying an extra $1.57 (1.12%) a week[2] (equating to $81.50 per year for a single policy or $163 for a family policy) on top of their normal yearly increases.

1.12% a week (or $163 per annum) may seem insignificant, however 3.4 million Australians with private health insurance live in households with incomes less than $35,000 per year[3], and this increase could be enough to render private health insurance unaffordable for many.

#### 3.1.2. Price elasticity and sensitivity

The legislative changes are likely to lead to those consumers who are more price elastic (typically the young and healthy) dropping private health insurance completely or downgrading their cover. This would result in increased upward pressure on premiums due to a deterioration of the risk pool.

There has been a general trend of members opting for higher excess products over the past year as the income testing of the rebate has come into effect. This is evidenced by a 3.2% decrease in our Top Hospital with $0 excess polices, and an increase of 5.2% in our Top Hospital and $200 excess policies. This trend is also consistent within our Intermediate Hospital product offerings.

The complication of tiered rebates and rebate indexation will make it difficult for consumers to accurately forecast the cost of their health cover over a year. HBF finds that consumers behave in an overly conservative way in confusing situations, which can reflect in lower levels of insurance purchased as more members choose cover based on affordability rather than cover which suits their health needs.

#### 3.1.3. Under - insurance

One of the consequences of people purchasing health insurance based on price is under-insurance. In this instance, while we may have a large number of people holding health insurance policies (possibly just to avoid the Medicare Levy Surcharge), the insurance will not cover their needs resulting in disillusionment with private health insurance or reliance on public hospital services despite them having private health insurance.

**Recommendation**

HBF's recommendation is not to pass the proposed amendments in the current form. More consultation and consideration is required to ensure the negative impacts on the private health insurance industry and the public health system, are minimised.

[2] Prices based on HBF Top Hospital with $0 excess and Extra Essentials products, with the same increase per year as April 2013, and an indexation rate of 2.2% per year.

[3] Private Healthcare Australia: Private Health Insurance - Debunking the Myths

### 3.2. Ability to implement the legislative changes

#### 3.2.1. Complexity to consumers

Private health insurance is incredibly complex to consumers[4]. The industry already experiences a barrier for new entrants for this reason. Explaining pricing with rebate indexation will further confuse and potentially isolate consumers.

Ipsos research[5] shows that 44% of people without private health insurance "just don't even think about it because it is too complex and confusing" and that 66% of people who made inquiries about private health insurance in 2010 were deterred from proceeding due to the complexity.

Existing complexities in private health insurance include:

- Income testing of the Rebate (recently introduced and still being understood)
- The Medicare Levy Surcharge
- Lifetime Health Cover Loading, which can apply to an individual as one amount or to a policy at different amounts (where two adults on a policy have one or more LHC loadings applied) and is then removed after a continuous ten years.

The combination of all these complex features make it extremely difficult and costly to administer in such a way that makes it simple for the consumer to understand.

#### 3.2.2. Complexity of Administration

Our initial high level review of the amendment indicates the level of development required will be substantial and rival those associated with implementing the Rebate Tiers last year, which for HBF alone was over $2 million. These changes are also likely to have flow-on effects to other processes and Government agencies like the Department of Human Services and the Australian Taxation Office.

With the amendment to index the rebate entitlement, the ATO will potentially have to hold details of the base premiums for each fund at an individual product level which will change year on year.

This is in addition to the administratively complex changes currently being made for this financial year to cater for income testing that was introduced 1st July 2012 and the LHC changes proposed for 1st July 2013.

**Recommendation**

We would urge further consideration to the Base Premium Bill to find a way to simplify as far as possible without diminishing competition. Our recommendations are included below.

### 3.3. Approach to Indexation

The legislation currently states that the rebate will be indexed at the product subgroup level.

We believe this method could become unnecessarily complex as consumers migrate between and within products with unintended consequences such as:

a) Complexity and changing rebates when consumers change products within a fund

[4] Ipsos Health Care and Insurance Australia Report 2011
[5] Ipsos Health Care and Insurance Australia Report 2011

b) Product profitability and transition. Many insurers may have products that require price correction over the next few years to reduce product cross subsidisation. A transition period to assist this is currently not mentioned, resulting in the potential for a product to lose a substantial part of the rebate in a once off adjustment. We do not believe this is the intention of the legislation.
c) The rebate that would apply to new products.

**Recommendation**

HBF recommend a fund based approach to indexation. Applying the indexed rebate at a fund level would be a much simpler method for reducing the Government's expenditure on the rebate. This will incentivise funds to keep their overall premium increases to a minimum, to protect the amount of rebate their members receive whilst still encouraging competition between funds. There will also be greater transparency for members as each fund will have a set rebate percentage across all of their product offerings.

As a not for profit fund, HBF intends to continue to have lower premium increases relative to our competitors and retain as much of the rebate as possible. We believe we can be a positive competitive force and influence the market to keep premiums and increases low. An industry approach to indexing would remove this.

The example below illustrates how the rebate for a low increase fund would differ based on a fund model versus an industry model. As you can see there is a 1.6% difference in the rebate amounts in only a few years.

| Fund Based | Apr-13 | Apr-14 | Apr-15 | Apr-16 |
|---|---|---|---|---|
| CPI | 2.50% | 2.50% | 2.50% | 2.50% |
| Fund 1 - Rate Increase | 3.75% | 3.75% | 3.75% | 3.75% |
| *Rebate Percent | 30.0% | 29.6% | 29.3% | 28.9% |

| Industry Based | Apr-13 | Apr-14 | Apr-15 | Apr-16 |
|---|---|---|---|---|
| CPI | 2.50% | 2.50% | 2.50% | 2.50% |
| Industry Average Rates | 5.60% | 5.60% | 5.60% | 5.60% |
| *Rebate Percent | 30.0% | 29.1% | 28.2% | 27.3% |

*Source: HBF Modelling 2013.*
** Rebate Percent = 30% - (fund increase - CPI) x 30%.*

## 4. CPI Considerations

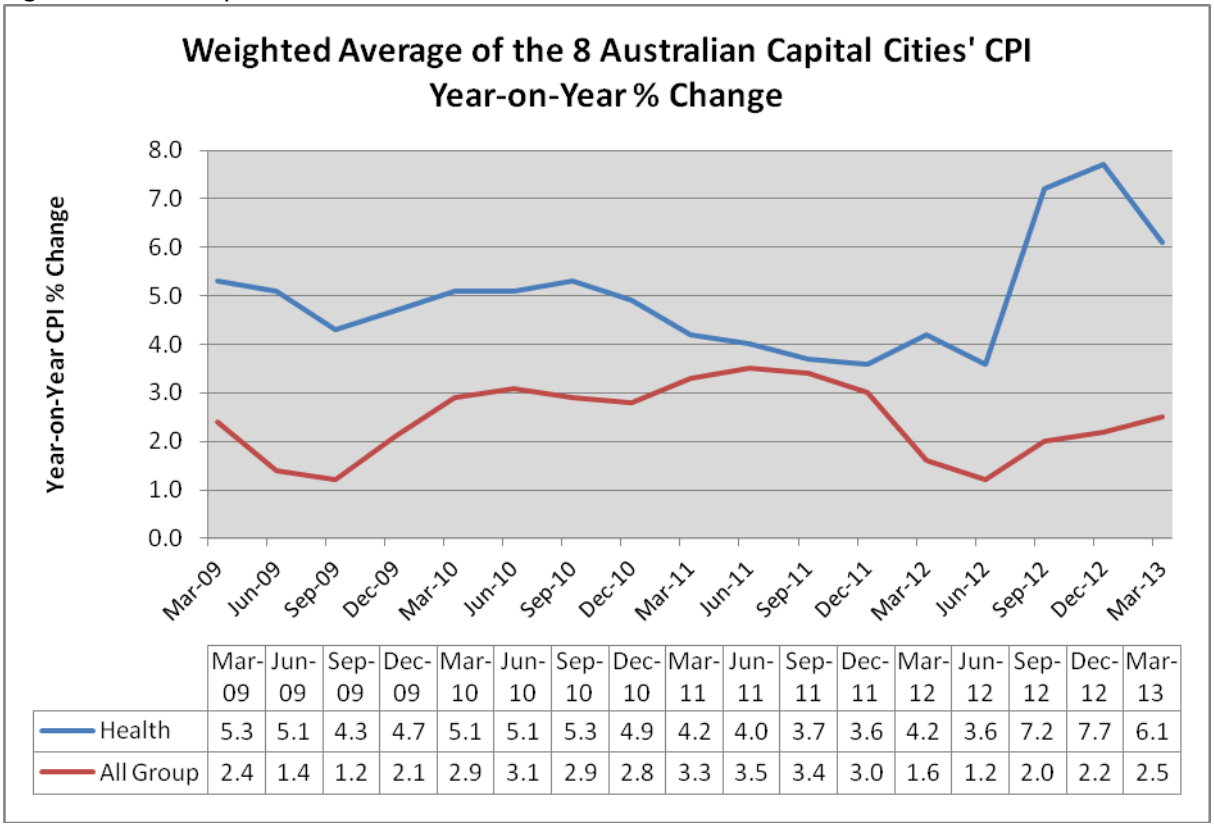
### 4.1. All Group CPI vs. Health CPI

The legislation states that the Consumer price index (CPI) percentage change will be based on the All Groups Consumer Price Index number, being the weighted average of the 8 capital cities. As a not-for-profit health fund, the premium increase that HBF requests is the minimum necessary to cover for the increase in hospital and medical costs.

Figure 1 illustrates the difference in All Group and Health CPI. Health CPI historically has always been above All Group CPI. Over recent years, the Health CPI has been above All Group on average by 4.8%, most notably from Sep-12 to Mar-13. The latest figures published by ABS state that "Over the

twelve months to March quarter 2013, the health group rose 6.1%, mainly due to rises in medical and hospital services (+9.3%)"[6].

Figure 1 – All Group vs. Health CPI




| | Mar-09 | Jun-09 | Sep-09 | Dec-09 | Mar-10 | Jun-10 | Sep-10 | Dec-10 | Mar-11 | Jun-11 | Sep-11 | Dec-11 | Mar-12 | Jun-12 | Sep-12 | Dec-12 | Mar-13 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Health | 5.3 | 5.1 | 4.3 | 4.7 | 5.1 | 5.1 | 5.3 | 4.9 | 4.2 | 4.0 | 3.7 | 3.6 | 4.2 | 3.6 | 7.2 | 7.7 | 6.1 |
| All Group | 2.4 | 1.4 | 1.2 | 2.1 | 2.9 | 3.1 | 2.9 | 2.8 | 3.3 | 3.5 | 3.4 | 3.0 | 1.6 | 1.2 | 2.0 | 2.2 | 2.5 |

*Source: Australian Bureau of Statistics – 6401.0 Consumer Price Index, Australia*

HBF's average premium increase over the past 10 years is 5.25% (the industry average is 5.88%) with a Health CPI average of 5.2%, indicating that our increases have been kept to a minimum and to ensure solvency. If premium increases are to be benchmarked against the All Group CPI instead of Health CPI, many private health insurance consumers will be impacted in April 2014, as all health funds are likely to require a premium increase greater than All Group CPI to remain sustainable. This additional cost to consumers is likely to challenge the affordability of private health insurance for many members, ultimately putting further pressure onto the public healthcare system.

**Recommendation**

HBF recommend amending the proposed legislation to use the Health CPI percentage change to index the rebate. The Health CPI directly relates to the cost of health care and therefore is analogous to the cost increases to health providers, health insurers and consumers alike.

### 4.2. State based variations

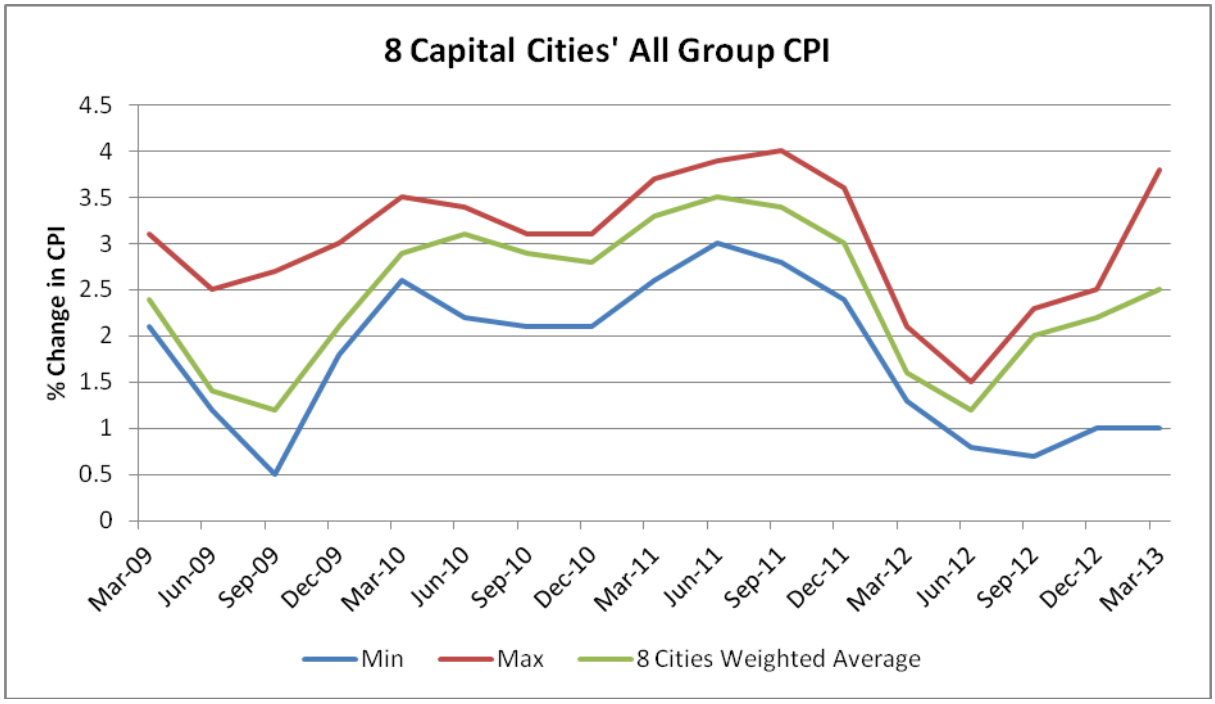
Using the All Group CPI weighted average of the 8 capital cities is a concern due to the varying CPI rates across states. The March 2013 All Group CPI percentage change of the 8 capital cities shows ranges from 1% in Hobart to 3.8% in Darwin, with the weighted average of the 8 cities at 2.5%. Therefore, health funds that are focused in specific states will be disadvantaged from using the weighted average.

[6] ABS 6401.0 – CPI, Australia, Mar 2013. Weighted average of eight capital cities. Percentage change from previous quarter. 24 Apr 2013

For example, if the majority of the health fund's members are based in Darwin, even if the fund is to have a premium increase on par with the state's All Group CPI at 3.8%, it would still be 1.3% above the weighted average of the 8 capital cities' All Group CPI at 2.5%.
On the other hand, if the majority of the health fund's members are based in Hobart, the fund would have more flexibility to work around with the premium increase since Hobart's All Group CPI is 1% compared to the weighted average of 2.5%.

Figure 2 shows the differences on the minimum, maximum and weighted average of the All Group CPI of the 8 capital cities. There is a significant difference creating inequity between states.

Figure 2 – 8 Capital Cities' All Group CPI




*Source: Australian Bureau of Statistics – 6401.0 Consumer Price Index, Australia*

**Recommendation**

The price of health care differs between states and the current private health insurance legislation recognises and incorporates this into the pricing structure of products offered over different states. In order to ensure this equity is maintained, HBF request consideration regarding the CPI rates in different states also being incorporated into any amendments.

## 5. Other Issues

### 5.1. Deregulation of Private Health Insurance Premiums

The indexation of the private health insurance rebate will gradually remove the rebate from consumers (assuming the historical gap between premium increases and CPI continues). The example above regarding fund based and industry based indexation demonstrates the impact of fixing the rebate to the CPI increase. It shows that the Government rebate is no longer dependent on the rate increase as it is fixed to CPI. In fact the higher the premium increase proposed by a fund (and the wider the gap with CPI), the faster a consumer loses their rebate.

**Recommendation**

Since the Government's rebate portion will be capped (to CPI) regardless of the premium increase, HBF strongly advocate for the deregulation of private health insurance premiums. This would not only help to increase market competition, but also reduce ambit claims and increase efficiency and innovation in areas such as product design. We do not suggest that PHIAC's prudential oversight of the funds is in any way removed, however the timing of premium increases may vary during the year.

### 5.2. Lack of detail in the legislation

Further to the goal of simplicity, we are concerned about the lack of clarity as to how the legislation will actually work, given an intended April 1, 2014 implementation date. The information provided to date does not provide the detail that would allow health funds to accurately develop complex system calculations in time. Significant gaps in information include:

1. The rebate that would be applied to new members to the industry.
2. The indexation that would apply when new benefits are added to increase the value of a product (the proposed changes provide a disincentive to do this)
3. The indexation that would apply if someone upgrades to a new product.
4. The base rate on which indexation would apply.

Whilst the legislation states that the base premium will be indexed by the lesser of the CPI percentage change or the change of the premium charged by the private health insurer at a product subgroup level, it does not specify a definition of the change of premium charged by the private health insurer.

For example, whether we use rate protected or non-rate protected premium increases at each product level. The rate protected and non-rate protected premium increase can vary by 1 to 2% depending on the number of prepayments.

The definition to be used of the percentage change of the premium will greatly impact the result of the amount of rebate that a member will lose, and it could potentially be the difference between retaining and losing the rebate (note that currently funds are not required to report rate protected figures at a product subgroup level).

### 5.3. Timing

The timeframes that funds will actually have to implement their new premiums and communicate these to members is challenging. The December 2013 CPI figures will not be available until around the 23rd January 2014. Under the new timetable introduced this year, the Minister will announce fund increases on 8th February 2014 leaving funds only a few weeks to accurately determine what portion of a member's premium will continue to receive the Government Rebate and include it in member communication.

**Recommendation**

There needs to be sufficient consultation to ensure the details of the legislation are adequately defined. The time frame needs to be examined jointly to ensure accurate and comprehensive explanation for consumers.

## 6. Summary

In light of the impact and consequences, discussed above, HBF propose to the Senate that the legislation be declined to allow further consultation. Failing this, we suggest at a minimum that the following modifications be applied to the Bill:

- Health CPI provides an appropriate indication of the cost of health insurance and therefore should be used to index the rebate.
- State based indexation allows room for state based CPI variations and takes into account the economic factors in each state. For that reason HBF recommends incorporating this change.
- Indexation at a fund level is simpler to implement, provides greater transparency for members and incentivises funds to keep premiums low. HBF does not support indexation at an industry level as funds who manage their business well and keep premium increases to a minimum will be penalised.
- Further information needs to be provided to clarify indexation requirements relating to new benefits, new entrants and new products.
- Deregulation of the private health insurance premiums is a logical next step to encourage competition given the Government's now capped exposure to premium increases going forward.

Thank you once again for the opportunity to provide a submission on behalf of our members.

Yours sincerely

Rob Bransby
Managing Director