REPORT

HEALTH INSURANCE COMMISSION (REFORM AND SEPARATION OF FUNCTIONS) BILL 1997

1. THE INQUIRY

1.1 The Health Insurance Commission (Reform and Separation of Functions) Bill 1997 was introduced into the House of Representatives on 27 June 1997. On 28 August 1997 the Senate, on the recommendation of the Selection of Bills Committee (Report No.12 of 1997), referred the provisions of the Bill to the Committee for report by 24 September 1997.

1.2 The Committee considered the Bill at a public hearing on 4 September 1997. Details of the public hearing are referred to in Appendix 2 The Committee received two submissions relating to the Bill and these are included as Appendix 1

2. THE BILL

2.1 The Bill has two main objectives:

- to separate Medibank Private from the Health Insurance Commission (HIC) and to create a new Medibank Private corporation; and
- to widen the role of HIC and allow it to take on additional functions, specifically health payment services and provision of health information.

2.2 The Government's aim in implementing these changes was outlined in evidence:

> The aim of the government in putting forward the bill to separate Medibank Private and the Health Insurance Commission was...to address the issue of the perception and reality of competitive neutrality, first. That is not to say that the government accepted that there was any real cause for concern. The arrangements that were made between the government programs side of the Health Insurance Commission and Medibank Private were as sensible and robust as could be desired. Nonetheless, there was a perception and a reality of being able to establish Medibank Private on a competitively neutral basis with other funds.
>
> But just as important-and perhaps more importantly-in terms of what the government was seeking to achieve by the separation was that both organisations...face significant challenges and opportunities, and they were seen to be best addressed by being the focus of single organisations, single managements and single boards...[1]

Medibank Private corporation

2.3 The Bill provides for the establishment and nomination of a company which is to be the company that will take on the functions of Medibank Private from the HIC. All of the share capital of the new company is to be owned by the HIC. After a period of transition, the shares will be transferred to the Commonwealth.

---

1 *Transcript of Evidence,* p.13.

2.4 The Bill provides that during the transition period:

- HIC is prohibited from transferring any of the shares in the nominated company and the company cannot issue shares to any other person;
- the nominated company must seek registration as a registered health benefits organisation under the *National Health Act 1953*;
- HIC's functions are extended to facilitate the transfer of Medibank Private to the nominated company; and
- HIC may enter into service arrangements with the nominated company, on a cost-recovery basis, to effect the separation.

2.5 The transfer of the business of Medibank Private to the company is to be through a scheme determined by the Minister. The scheme is to be notified in the Gazette and must provide for the transfer to take place on the fund-transfer day which is a day to be determined by the Minister. The scheme must provide that the transfer does not affect the continuity of a person's status as a contributor to the fund.

2.6 The Minister is to make declarations for the transfer of assets, contractual rights and obligations and liabilities from the HIC to the nominated company. Ministerial declarations are to be notified in the Gazette. Contracts between the HIC and a supplier of goods or services can be split by the Minister into two separate contracts so that certain rights and obligations can be transferred to Medibank Private and the remainder left with the HIC.

2.7 The Bill provides for the transfer of staff from the HIC to the nominated company:

- staff cannot be transferred any later than 12 months after the shares in the nominated company have been vested in the Commonwealth;
- staff must be employed by the nominated company on the same terms and conditions as they were immediately before the transfer; and
- accrued benefits and continuity of service are to be maintained.

The Bill does not preclude variations of staff conditions of service at a later date under any law, award, determination or agreement as would be the case under their existing employment.

2.8 The Bill also provides for the re-transfer, to the Commission, of employees who had originally transferred to the nominated company. Re-transfer provisions only apply during the transitional phase while the nominated company is owned by the HIC and for a period of 12 months after the transfer of ownership to the Commonwealth.

2.9 Other provisions of the Bill provide for:

- the exemption from State and Territory taxes in respect of matters necessary to carry out the separation;
- the transfer of records which relate to Medibank Private from the HIC to the nominated company;
- the transfer of pending legal proceedings to the nominated company where appropriate;

- the nominated company not to be taken to be a Commonwealth authority, a Commonwealth agency or instrumentality of the Crown; and
- complaints to the Ombudsman, Freedom of Information applications, applications to the Administrative Appeals Tribunal and complaints under the Privacy Act, which may have been or have been made prior to the fund-transfer day, and which relate to Medibank Private, to be completed.

Role of the HIC

2.10 The Bill provides for the functions of the HIC as follows:

- Medicare functions - substantially unchanged
- service delivery functions - enables the HIC to enter into service arrangements with a Commonwealth authority for the provision of services to that authority and the HIC may receive payment for the services so provided;
- spare capacity functions - the Minister may approve the provision by HIC of services or facilities on a commercial basis to any person. The provision of these services or facilities must either utilise the HIC's spare capacity or relate to a designated matter including a matter related to external affairs or the executive power of the Commonwealth; and
- additional functions - three functions conferred by the *Health Insurance Commission Act 1973*, conferred by regulation and conferred by written delegation of the Minister.

2.11 The Bill also allows the States and Territories to confer powers and functions on the HIC. With the approval of the Minister the HIC may perform those functions and exercise those powers.

3. ISSUES

Competitive neutrality

3.1 In his second reading speech, the Minister stated that:

> Through the separation, the Government will ensure that Medibank Private cannot be perceived to have any competitive advantage over other private health funds through its association with Medicare or other government programme functions of the HIC.[2]

3.2 The issue of competitive advantage of Medibank Private has often been raised. Matters such as co-location with Medicare which results in 'free' advertising of Medibank Private and the ability to lease or own prime commercial sites at a significantly lower cost than other funds were given as examples of this advantage. Two inquiries have commented on Medibank Private's competitive advantage. First, the 316th Report of the Joint Committee on Public Accounts stated:

> The Committee is not persuaded by evidence to the Inquiry that cross subsidisation occurs of Medibank Private by Medicare. It notes further that the HIC, Medibank Private and Medicare are subject to audit by the ANAO. The

---

2 Minister for Health, second reading speech.

> auditing process includes scrutiny of the cost apportionment and asset rental systems. Were instances of cross subsidisation to be noted by the audit process they would be reported by the ANAO to the Parliament. In the absence of such reports the Committee has been unable to substantiate allegations of cross subsidisation.[3]

3.3 In February 1997, the Industry Commission reported on private health insurance. The Commission found:

- Medibank Private appears to have played a ‘catalytic role in intensifying competitive pressure in the industry;
- Medibank Private appears to derive significant market advantages unavailable to other insurers through its co-location with Medicare; and
- there are governance and competitive neutrality principles associated with the relationship between HIC and Medibank Private. The Commission found that Medibank Private had lower management costs per members than some other funds but it was unsure if this was due to ‘a statistical artefact, genuinely higher technical efficiency or cost shifting to Medicare’.[4]

3.4 In evidence the Australian Health Insurance Association (AHIA) noted that there had been much concern about ‘one-stop shopping in joint Medicare and Medibank Private offices, which has led to the perception of commercial advantage, whether real or not’.[5] The AHIA also stated that as a result of the separation ‘there will be a level playing field. The fact that we are not competing with an organisation which, in our view - and I acknowledge it is disputed - is receiving a special advantage by virtue of its association with the Medicare program’.[6]

3.5 The AHIA also submitted that separation of the HIC and Medibank Private was ‘a welcome step towards restoring genuine competition between a Government owned registered benefits organisation and non-Government operators’.[7] The AHIA stated Medibank Private had received cost advantages through co-location with Medicare and Medibank Private ‘has been able to artificially undercut [other private health funds]’.[8] These cost advantages included:

- that funds advanced by the Government for establishment costs did not attract interest payments;
- a capacity to reduce or conceal administration costs below industry norms by virtue of sharing costs with taxpayer funded activities;
- the existence of a captive tenant arrangement which allowed the Commission to invest in property which is funded by the taxpayer;

---

3 Joint Committee of Public Accounts, Report 316, *The Administrative and Financial Relationship between Medicare and Medibank Private*, AGPS, Canberra, 1992, p.15.

4 Industry Commission, *Private Health Insurance,* Report No 57, AGPS, 1997, pp.358-9.

5 *Transcript of Evidence*, p.2.

6 *Transcript of Evidence*, p.3.

7 Submission No.2, p.1 (AHIA).

8 *Transcript of Evidence*, p.4.

- a capacity to share staff and resources in co-located shopfronts; and
- Ministerial approval to transfer moneys between States to maintain solvency levels in the early years of the introduction of Medicare.

3.6 The AHIA also asserted that the joint operation has allowed Medibank Private over the years to generate a surplus that may not have existed if its accounts had been free-standing and not based on the cost sharing formula determined by the minister of the day. The AHIA provided the examples of where it believed Medibank Private had enjoyed a benefit from cost sharing with Medicare:

- *audit fees and payments to Commissioners*: these two costs had both decreased for Medibank Private following the establishment of Medicare;[9]
- *salaries*: using industry average staff ratios, the AHIA suggested that Medibank Private's salary bill should be $13 million (39%) greater;
- *occupancy*: the AHIA suggested that Medibank Private should have paid an additional $34 million in occupancy costs in 1994-95;
- *asset utilisation*: the AHIA suggested that Medibank Private should have paid an additional $14 million in asset utilisation costs in 1994-95.

3.7 In its submission, the Community and Public Service Union (CPSU) disputed the claim that Medibank Private enjoyed a competitive advantage and noted that the Industry Commission had found that the HIC is the largest health insurer with the lowest management costs. Further, the HIC had access to significant economies of scale due to its size and market presence in every State and Territory. The CPSU also stated that the cost apportionment arrangements operating with Medibank Private and Medicare are fair with the Minister's determination on apportionment being made in consultation with Treasury and being acceptable to the Auditor-General. Further:

> This has shown that the cost apportionment guidelines between the two sectors of the Health Insurance Commission do not give a financial advantage to one side of the organisation or the other. We would strongly argue that the statutory cost apportionment guidelines which currently apply do provide the level playing field that the private industry is so concerned about.[10]

3.8 In response to the evidence received from the AHIA, the HIC noted that when Medibank Private first came into the market there were major disadvantages as the organisation did not have knowledge of the private health insurance industry, it was not a household name and it had no infrastructure.

3.9 The HIC also responded to the AHIA's claims that Medibank Private had received advantages from the Government. It was noted that Medibank Private was granted $11 million in compensation for a payment of $13.8 million to Medibank Standard in the 1970s to reimburse benefits for members who had incorrectly claimed. At the same time,

---

9 Submission No.2 p.2 (AHIA).

10 *Transcript of Evidence*, p.7.

other private funds had been reimbursed for such repayments. However, Medibank was disadvantaged as it did not get the $2.8 million difference.[11]

3.10 In regard to the cost apportionment matters raised by the AHIA, the HIC stated that both Anutech and accountants KPMG had examined the cost apportionment principles and found them to be a 'fair and equitable distribution of costs incurred by the HIC'.[12] In regard to the claim that Medibank Private had been able to transfer reserves between State operations, the HIC noted that the National Health Act allowed all funds that operate in more than one market to transfer reserves and that Medibank Private was not the only fund which had taken advantage of these provisions.[13]

3.11 A further matter that was raised before the Committee was that of the possible future privatisation of Medibank Private. The CPSU stated that it and its members saw the legislation as a first step toward privatisation of the organisation.[14] While the AHIA noted that it had never asked for Medibank Private to be privatised.[15] In response, Dr Loy, DHFS, stated that it was not the Government's aim to 'privatise' Medibank Private. The Government:

> wanted this legislation to ensure that government ownership of Medibank Private was embedded in the legislation. That is not to tie down the hands of any future government or any future parliament...But the government, having made a commitment in the election context, was anxious to ensure that the legislation ensured that government ownership of Medibank Private remained.[16]

Consumer interest

3.12 The CPSU stated that the consumer interest would not be served by the separation of Medibank Private and the HIC. It noted there will be a significant reduction in the number of retail outlets available to the public for Medibank Private business, with the present number of outlets where Medibank Private business can be conducted dropping from 270 to approximately 70.[17] As a result not only would prospective customers of the private health insurance industry suffer, but also current policy holders would be disadvantaged and 'might possibly be pushed out of the private sector health insurance market altogether'.[18] The CPSU concluded that 'we do not understand the rationale for this legislation. It is going to be highly disruptive to the careers of our members. I do not think the taxpayer or the public will be any better off. It is arguable that they will be worse off.'[19]

3.13 The AHIA noted that if:

---

11 *Transcript of Evidence*, p.20.

12 *Transcript of Evidence*, p.20.

13 *Transcript of Evidence*, p.21.

14 *Transcript of Evidence*, p.7.

15 *Transcript of Evidence*, p.5.

16 *Transcript of Evidence*, p.14.

17 *Transcript of Evidence*, pp.6-7.

18 *Transcript of Evidence*, p.7.

19 *Transcript of Evidence*, p.13.

> Medibank Private has not been subsidised by a conjoint operation with Medicare, there is no reason why its costs would increase. If the assertions that there has been no subsidisation are true, there will be no change. If our assertion that there has been subsidisation is true, it is a problem for Medibank Private, but at least the taxpayer no longer subsidises that operation.[20]

3.14 The HIC responded to the CPSU's concerns about office closures by noting that Medibank Private business was not distributed evenly across the Medicare network. Medibank Private would be targeting where it opens an office or where it uses another form of distribution strategy to address the needs of its members in the area. Further, it was noted that more people are moving to direct billing and that in dealing with hospitals, health funds were making more direct payments to hospitals and in some instances co-payments were also being made at the time of a members hospital visit. The HIC also noted that a significant proportion of members contributions were made by group payments, that is through employers' payroll deduction schemes, rather than by cash over the counter.[21]

3.15 The HIC responded to the AHIA by stating that separation will not be the cause of premium increases. Further, Medibank Private had been successful as it had not diversified from its core business like some other private health funds.[22]

3.16 In evidence, it was also noted that there were some disadvantages to Medibank Private of co-location with Medicare. For example, customer service was constrained as Medibank Private customers had to queue with Medicare customers before being served. Mr MacDougall, General Manager, Medibank Private, also noted that Medibank Private would have more freedom to act after the separation such as expanding its distribution network through other organisations. This had not happened in the past, 'but a separate entity out there will allow it to establish a primary distribution network to enable it to deliver customer service and then look at how it can expand that distribution network throughout Australia'.[23]

---

20 *Transcript of Evidence*, p.4.

21 *Transcript of Evidence*, p.18.

22 *Transcript of Evidence,* p.21.

23 *Transcript of Evidence*, p.19.

Staffing

3.17 In his second reading speech, the Minister stated that:

> Staff affected by the transfer will be treated fairly. Where an employee is transferred under these provisions, their terms and conditions of employment and other rights and entitlements defined in the Bill, have been preserved.

3.18 The CPSU in its submission to the Committee, raised two areas of concern. The first matter related to mobility rights of staff. The CPSU noted that the Bill gives the Minister power to forcibly transfer staff from the HIC to the new company, thus 'the power could be exercised *against* the expressed wishes of a staff member'.[24] In evidence it was stated that approximately one-quarter of staff (1,200 people) are dedicated to Medibank Private work and will be required to staff the new company.[25] The Union suggested that less than 1,200 wished to transfer to the new company.

3.19 The CPSU noted that it had been advised by the HIC that legal advice had indicated that in order for some conditions of employment to be preserved, the Minister must have the power to transfer employees to the company. The CPSU argued that if this is the case, 'in order to counter-balance the Minister's unfetted power, HIC employees must be given the right to freely transfer between the Health Insurance Commission and Medibank Private'.[26] It also noted that staff turnover was not high, with many members building a career on a mixture of Medicare and Medibank work.

3.20 The CPSU also raised the matter of the Minister's power to re-transfer staff from the company to the HIC and pointed to two major concerns:

i. The re-transfer arrangements are only available to staff for a period of 12 months from the date of separation. The CPSU considered that this period was too short and should be extended to three years to reflect the 'standard' that applies in the Australian Public Service when employees are transferred from the Service to a statutory authority.

ii. Re-transfer is predicated on the agreement of the Minister or his/her delegate. The CPSU was of the view that an employee should have a re-transfer right to counter-balance the Minister's power to forcibly transfer in the first instance.

3.21 The CPSU also noted that while it was stated that staff would be transferred with all terms and conditions, legislation based conditions of employment were not picked up. This included maternity and long service leave. Following representations by the union, the HIC has agreed to incorporate the long service leave and maternity leave into the HIC award.[27]

---

24 Submission No.1, p.2 (CPSU).

25 *Transcript of Evidence*, p.10.

26 Submission No.1, p.2 (CPSU).

27 *Transcript of Evidence*, p.9.

3.22 The CPSU concluded that the separation of staff 'will be highly disruptive and lead to unwarranted effects on staff careers unless there is a genuine choice for staff whether to stay with HIC or transfer to Medibank Private Ltd'.[28]

3.23 The second matter raised by the CPSU was the separation of assets and staff. The CPSU noted that the HIC proposes to contract many operations and administrative arrangements, such as computer processing of claims and some corporate operations, between HIC and Medibank Private. The CPSU was of the view that 'once Medicare Private establishes itself, these contractual arrangements may cease, thereby leaving HIC with potentially redundant staff'.[29]

3.24 In evidence, Mr A Kelly, Manager, Employee Relations, HIC, informed the Committee that an enterprise agreement had been reached and that staff were being invited to indicate their preference as to whether or not they wished to join Medibank Private. While the HIC could not guarantee that staff would receive their preference, the HIC had, where possible, undertaken to 'maximise those preferences for them'.[30] Where a person did not receive their preference, there would be an opportunity for review.

3.25 Mr Kelly also stated that the HIC believed that the 12 month time limit for re-transfer was 'a fair and reasonable time limit' and that people would know within that time whether or not they wished to continue employment with Medibank Private.[31] In addition to the re-transfer provisions, Mr Kelly informed the Committee that a 'job swap' arrangement had been set up. Under this arrangement, if a person in the HIC wished to move to Medibank Private and a person in Medibank Private wished to move back to the HIC, then with agreement of both organisations such a swap could take place. This option would also be available for a 12 month period.

3.26 The Committee was also informed that the HIC did not expect that there would be any need for staff redundancies as the workload would not change. There was in fact, some expectation that the work of Medibank Private would expand and increase following the separation.[32]

3.27 In relation to terms and conditions, Mr Kelly noted that the legislation provides for those moving to Medibank Private to bring across the same terms and conditions they enjoyed with the HIC. Other Commonwealth legislation which covers such matters as workers' compensation issues, occupational health and safety issues will be recognised. Mr Kelly also stated that discussions are being held with the Department of Workplace Relations and Small Business in regard to long service leave and maternity leave. He stated 'while we have not secured a guarantee there, what we have undertaken with the CPSU is that we will use a pick-up clause in our award to cover both Medibank Private and also HIC' to ensure these provisions apply.[33]

---

28 Submission No.1, p.3 (CPSU).

29 Submission No.1, p.3 (CPSU).

30 *Transcript of Evidence*, p.15.

31 *Transcript of Evidence*, p.16.

32 *Transcript of Evidence*, p.17.

33 *Transcript of Evidence*, p.16.

Financial aspects

3.28 In evidence, the AHIA stated that on separation, there should be an appropriate allocation of assets between the HIC and Medibank Private. The AHIA stated that it 'would strongly argue that Medibank Private should only obtain those which can genuinely be attributed to its marketplace operations, which we suspect will be very difficult to identify'.[34]

3.29 The HIC stated that in the existing structure, parts of the assets are owned by Medibank Private and parts by Medicare. The HIC 'will transfer for a value that proportion that belongs to Medibank Private clearly to Medicare, because it required that post-separation Medibank Private is establishing its own network'.[35] In relation to buildings owned by Medibank Private, the Committee was informed that HIC is currently paying market rental based on proportional use. Medibank Private will retain ownership of these properties following separation and the agreements for HIC tenancy will be through a normal commercial lease.

3.30 The HIC noted that the legislation allows for some service agreements to be split between Medibank Private and the HIC. The object of this is to allow the organisations to manage costs such as information technology costs. The sharing will continue for a number of years to allow time for the other organisation to determine what sort of technology strategy it would like and to manage the costs of that strategy.[36]

4. RECOMMENDATION

4.1 The Committee reports to the Senate that it has considered the Health Insurance Commission (Reform and Separation of Functions) Bill 1997 and **recommends** that the Bill proceed.

Senator Sue Knowles
Chairman

September 1997

---

34 *Transcript of Evidence*, pp.1-2.

35 *Transcript of Evidence*, p.22.

36 *Transcript of Evidence*, p.22.