Australian Government

Department of Health and Ageing

Committee Secretary
Senate Economics Committee
Department of the Senate
PO Box 6100
Parliament House
CANBERRA ACT 2600

Dear Secretary

Thank you for the opportunity to provide a written submission to the Senate Economics Committee's inquiry into the Fairer Private Health Insurance Incentives bills.

Please find attached the Department of Health and Ageing submission to this inquiry.

Yours faithfully

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9 June 2009

Department of Health and Ageing Submission to the Senate Economics Committee Inquiry into the Fairer Private Health Insurance Incentives Bills
9 June 2009

1) Why has the Government decided to means-test the private health insurance rebate?

The Government is rebalancing the suite of policies supporting private health insurance – so that those with a greater capacity to pay for their own private health insurance do so.

Consistent with the Government's commitment to maintaining the balance between public and private health systems, high income earners will receive less in Government payments for their private health insurance, but will face an increase in costs should they opt out of their hospital cover.

Across the tax and payments system the largest benefits are provided to those on lower incomes – except for private health insurance. These changes are consistent with the principle underpinning the tax and transfer systems – the greatest support should be provided to those on lower incomes.

Spending on the private health insurance rebate is growing quickly and expected to double as a proportion of health expenditure by 2046-47.

Singles
Without reform, the Treasury estimates that in 2010-11 approximately 14 per cent of single tax filers will have incomes of greater than $75,000, but this group would receive about 28 per cent of the total PHI rebate paid to singles. Under the new reforms, this group is estimated to receive about 12 per cent of the total private health insurance rebate paid to singles.

Couples/Families
By 2010-11, about 12 per cent of couples/families are expected to have incomes above $150,000 but this group would receive about 21 per cent of the total private health insurance rebate paid to members of couples/families. Under the new reforms, this group will now be estimated to receive about 9 per cent of the total private health insurance rebate paid to couples/families.

2) Impact on the private health insurance industry

It is estimated that 99.7% of people with private health insurance hospital cover will retain their insurance. This represents 2.2 million single adult policyholders and 2.4 million couple/family policyholders (note dependents are not included).

Over the last decade several incentive measures have been introduced to encourage people to purchase private health insurance. These are the rebate (including the higher rebates for older Australians), Lifetime Health Cover and the Medicare Levy Surcharge.

The most effective component of the existing incentive structure, Lifetime Health Cover, will remain in place. This increases the premiums for hospital cover for people who do not take out insurance until later in life by 2% for each year they are aged over 30.

The Government is also increasing the Medicare Levy Surcharge for higher income earners. For many above average and higher income earners, it will be more expensive to drop their health insurance than to keep it, even with the lower (or nil) government rebate.

Out of all forms of private health insurance cover (hospital only cover, combined hospital and general treatment (ancillary) cover and general treatment only cover), it is expected that around 40,000 people will drop some form of private health insurance. The anticipated breakdown of people who will drop their cover is:

- 25,000 people who had either hospital or combined cover are estimated to drop all of their cover;
- 10,000 people who had combined hospital and general treatment cover are estimated to drop their general treatment cover only; and
- 5,000 people with general treatment cover only are estimated to drop their cover.

It is important to note that individuals earning $75,000 or less and couples and families earning $150,000 or less will not experience any change, with the existing 30%, 35% and 40% rebates continuing to apply:

Age	**Under 65**	**65 – 69**	**70 and over**
Earning $75,000/ $150,000 or less	30%	35%	40%

The additional costs to higher income earners with private health insurance will be more than offset by the tax cuts in July 2009 and July 2010. For single income earners, the following table compares the average increase in the cost of premiums with the value of the tax cuts in 2010-11:

Income	**Private Health Incentive Tier**	**Net tax cut**	**Average PHI increase**	**Annual amount taxpayer better off by**
75,000	N/a	$450	$0	$450
80,000	1	$450	$167	$283
90,000	1	$750	$167	$583
100,000	2	$1,050	$333	$717
110,000	2	$1,350	$333	$1,017
120,000	2	$1,650	$333	$1,317
130,000	3	$1,950	$500	$1,450
140,000	3	$2,250	$500	$1,750
150,000	3	$2,550	$500	$2,050
160,000	3	$2,850	$500	$2,350
170,000	3	$3,150	$500	$2,650
180,000	3	$3,450	$500	$2,950
200,000	3	$3,450	$500	$2,950
250,000	3	$3,450	$500	$2,950

It is possible for there to be a case where the tax cut is not greater than the rebate loss, but for that to happen the affected individual would have to have a taxable income in the $70,000 – $80,000 range ($450 per annum tax cut) but also an income for rebate/surcharge purposes of greater than $120,000 (to lose the $500 per annum rebate on an average single premium). This would only occur in rare cases where the person has very substantial reportable fringe benefits, salary sacrificed superannuation contributions, etc. that are not included in taxable income but are included in rebate/surcharge income (adjusted taxable income).

3) How will the changes impact on premiums?

The Government does not anticipate that this measure will flow on to increased premiums. As it is expected that 99.7% of people with private health insurance hospital cover will retain their insurance, there would be very little increase in premiums due to people dropping their insurance. Any drop in membership levels would also lead to a drop in claims against the insurer.

Similarly, the Government does not anticipate significant additional administrative costs to insurers. The private health insurers are well managed, with low management expense ratios compared with other types of insurance, and this will continue to be the case.

The Government has examined the impact on insurers of the introduction of two additional rebate levels in 2005 (when the higher rebates for older Australians were introduced.) Additional administrative costs associated with the introduction of the two additional rebate levels were not reported in insurer rate change applications for 2005 as a reason for premium increases, and average management expenses decreased in the years following the introduction of the additional rebate levels.

4) How will the changes impact on insured people?

Treasury estimates that 2.3 million people will be affected by the changed rebate levels. This is the number of people covered by private health insurance hospital policies where the policy holder will receive a lower rebate or no rebate after the changes, and comprises:

- 630,000 singles;
- 490,000 couples (980,000 people); and
- 690,000 dependents.

It is estimated that 7.4 million people will continue to be covered by private health insurance hospital policies with the full 30%, 35% or 40% rebates, comprising:

- 1.6 million singles;
- 1.9 million couples (3.8 million people); and
- 2.0 million dependents.

5) How will the changes impact on people without private health insurance?

Treasury estimates that the changes to the Medicare Levy Surcharge will affect around 130,000 higher income earners who currently do not have private health insurance (the

number of people in Tiers 2 and 3 who currently pay the Medicare Levy Surcharge):

	TIER 1	TIER 2	TIER 3
Singles Couples	$75,001–$90,000 $150,001-$180,000	$90,001-$120,000 $180,001-$240,000	$120,001 or more $240,001 or more
All ages	1.0%	1.25%	1.5%
Number of affected people without PHI	Nil (no change to current surcharge liability)	90,000	40,000

The affected 130,000 people will have to pay an increased Medicare Levy Surcharge, unless they purchase appropriate private health insurance. These people may decide to buy private health insurance rather than pay additional tax, which would offset any decrease in participation as a result of this measure.

6) How will the changes impact on public hospitals and dental services?

The small number of people who do drop out of private health insurance will not result in a significant additional burden on public hospitals.

Ipsos *Health Care and Insurance Australia 2007* survey data indicate that around 35% of people require hospital treatment in a two year period. As Treasury estimates up to 40,000 people will drop out of a form of private health insurance, Australian public hospitals as a whole may see a rise in demand of around 8,000 people in a two year period. The increase in public patients would be around 0.1% of the usual public hospital workload (4.7 million admissions per year or more than 9 million admissions over a two year period).

At the Council of Australian Governments' (COAG) meeting in November 2008, the Commonwealth agreed to provide $64 billion over five years to the States and Territories for State health systems and national health partnerships. This included an additional $22 billion in funding largely for public hospitals, covering the costs of an additional 350,000 emergency department presentations and an additional 370,000 hospital admissions over four years.

Over a two year period when public hospitals could expect to see an extra 8,000 people who have dropped their private health insurance as a result of this measure, the additional Commonwealth funding would provide for an additional 175,000 Emergency Department presentations and 185,000 public hospital admissions.

It is not expected that there will be any impact on public dental services or waiting lists associated with people dropping their general treatment (ancillary) cover, which usually provides insurance for the costs of dental services.

Public dental services are only provided to pensioners and health care concession card holders. It is very unlikely that a person earning over $75,000 a year or a member of a couple/family earning over $150,000 a year would be eligible for public dental services.

7) How will the changes impact on private health insurers' costs?

To enable people to continue to claim the rebate as an upfront premium reduction from their insurer, insurers will need to be able to adjust their rebate reduction schemes provided to their members to reflect the changed rebate levels. The insurers' systems currently allow for four different rebate levels (0%, 30%, 35% and 40%).

From 1 July 2010, insurers' systems will need to be able to recognise an additional four rebate levels (10%, 15%, 20% and 25%). This may involve changes to computer systems and additional administrative staff to deal with rebate level elections by their members.

In 2005, insurers implemented changes to deal with an additional two rebate levels, when the higher rebates for older Australians were introduced from 1 April 2005. At that time, no insurer sought an increase in premiums as a result of increased administrative costs or management expenses attributed to the additional rebate levels.

In fact, insurers' management expense ratios dropped from 9.9% in 2003-04 to 9.5% in 2004-05 immediately following the introduction of the additional rebate levels, and dropped again to 9.4% the following year (2005-06). On the basis of this experience, the Government does not anticipate significant additional administrative costs to insurers. The Government will allow insurers to decide how often they allow their members to change their rebate level elections.

The Government will assist insurers in preparing for the introduction of the new rebates, by preparing standard rebate election forms and guidance material for insurers to use.

8) How will the changes be implemented?

The changes will start on 1 July 2010. People will continue to be able to receive their rebate in three ways:

- as an up-front premium deduction made by the insurer;
- by claiming the rebate as a refund at a Medicare office by presenting a premium receipt; and
- by claiming the rebate through a tax return at the end of the financial year.

When claiming the rebate as a premium deduction or through a refund at Medicare, a person will need to nominate a premium rebate level that they are entitled to based on their 'adjusted taxable income'. If people over-estimate their income, they will receive a rebate 'refund' through their tax return for that year. If people under-estimate their income, they will incur a rebate 'debt' through their tax return that year. This will be recoverable as a normal tax debt.

There will be no requirement for insurers or Medicare Australia to collect information about people's income, or to check the accuracy of a person's rebate nomination. If a person claims the incorrect rebate level, this will be identified when the person completes his or her tax return for that year. People will be required to repay any rebate they claimed and were not entitled to, or will be repaid the correct rebate by the ATO if the rebate they claimed was too low.

9) How will the Government tell people about the changes?

Funding for a general communications campaign about the changes has been provided to the ATO through the budget. This campaign will be conducted during 2009-10 in the lead up to the changes starting on 1 July 2010.

The communications campaign will be coordinated by the Australian Taxation Office, with support from the Department of Health and Ageing. The Department will focus on assisting industry to implement the changes, through the development of information and guidance material and standard forms.

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