9 June 2009
Committee Secretary
Senate Standing Committee on Economics
PO Box 6100
Parliament House
Canberra ACT 2600

Dear Secretary,

**Re: Inquiry into the Fairer Health Insurance Incentives Bill 2009 and two related bills**

Bupa Australia appreciates the opportunity to make this submission to the Senate Economics Committee's inquiry into the *Fairer Health Insurance Incentives Bill 2009* and related bills. We trust the submission will be of assistance to the committee, and would be pleased to further elaborate on the content of the document or provide additional information at the committee's request.

**Background to Bupa Australia**

Bupa Australia is the largest privately managed health insurance group in Australia, with a combined market share of around 28%. We have a significant presence in all States and Territories and support the health care needs of around 3 million Australians through a range of trusted brands including HBA, MBF and Mutual Community.

As part of the international Bupa Group, we draw upon the strength and expertise of a recognised global leader in the health and care sector. Bupa provides health insurance to more than 10 million people in over 190 countries. It also provides wellness, aged care and other health and financial services to millions more customers around the globe.

The Bupa Group is driven by a collective vision of *"Taking care of the lives in our hands"* with the goal of helping people live longer, healthier, happier lives. Bupa is a company limited by guarantee – it does not have shareholders and all profit is reinvested in the provision of better care facilities and services to benefit Bupa's customers and the communities in which Bupa operates.

Since 2002, Bupa has invested more than $4 billion in Australia's health and care sector, acquiring and building our health and aged care businesses in this market. In Australia, Bupa is also one of the largest private operators of aged care facilities, providing care for more than 4,000 elderly Australians through Bupa Care Services Australia.

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**Background to Australia's Private Health Sector**

*Role and participation*

Australia has a health system that is the envy of the world, one of the key tenants of its success is its mixed public/private model. The private sector plays an integral role in the health system, complementing and substituting public services to improve choice and access to health care for all Australians. The private sector's role in alleviating pressure on the public system is vital to improving wait times and access for the uninsured population. Therefore, it is important to the long term sustainability of the Australian mixed health system that the private sector remains viable, attractive and affordable for all customers.

The importance of the private sector in relieving pressure on the public system has been recognised and supported by Federal Governments over the past decade via three main initiatives; the Private Health Insurance Rebate, Lifetime Health Cover (LHC) and the Medicare Levy Surcharge (MLS). These support mechanisms were designed to promote long-term stability and growth in private health insurance (PHI).

These three initiatives, working together, have resulted in sustained growth in private health insurance membership since 2000 to its current level, where 44.6% of Australians have hospital cover and more than 51% have some form of PHI. These initiatives are strongly interrelated and changes to any one of them has the potential to impact adversely on the current and future level of PHI membership, which would place greater pressure on Australia's public health system.

More than 11 million Australians currently hold some form of private health insurance with private health insurers contributing more than $10.3 billon to Australia's health economy in 2007/08. As pressures on government expenditure for all social services increase, the private sector will become an even more important support to government in coping with the increased demand for health services.

*The impact of Community Rating on pricing*

Australia's PHI industry is underpinned by the principle of Community Rating, which requires that insurers charge the same premiums to customers irrespective of health status, age (other than age at entry under LHC), race, gender or claims history. The average risk of the insured population is therefore borne across all customers in the sector and any change to that average risk is shared financially across all remaining insured people.

With average hospital utilisation increasing as people get older, age is a major factor in determining the risk that premiums need to cover. Generally speaking, an increase in average age of just 1 year across the insured population requires around a 5% increase in premiums, before taking into account any growth in hospital or medical costs.

**Overview**

Bupa Australia actively encourages and contributes to discussion around review of Australia's Healthcare system and is supportive of moves to improve access, affordability and quality across the entire health sector.

We are concerned however, that the changes proposed in the Fairer Health Insurance Incentives Bill 2009 (the Bill) work against, rather than enhance, affordability and access to the Australian health system.

These proposed changes will impact directly and indirectly on all of our three million customers and on an additional eight million other Australians who currently have PHI. They also have the potential to reduce participation levels in the sector, which in turn would place additional pressure on an already straining public health sector, adversely impacting all Australians.

Although the proposed means test is promoted as a targeted initiative directed at higher income earners, the impact from the change will ultimately be felt hardest by middle and lower income earners.

Bupa Australia is committed to keeping health care affordable for our customers. In that aim, we cannot support the proposed changes to the PHI rebate. Our concerns with the proposed changes are wide-ranging and include;

- Although changes are promoted as a targeted initiative directed at "high income earners," the financial cost any reduced participation or downgrades will adversely impact premiums for ALL PHI customers. In addition, the income level at which the rebate reduction commences impacts middle income families – not just the extremely wealthy.
- Customers in tiers 1 and 2 (the lower income tiers) will be subject to premium increases significantly higher than the increase in the MLS.
- The group of people most immediately at risk of either downgrading or leaving are younger people who experience below average claims history. These people have traditionally accounted for the majority of new customer sales and provide a subsidy to overall risk which will have to be funded by premium growth for all PHI customers if they leave the sector.
- There is still no information available on the expected start-up and ongoing cost of administration for insurers and our customers.
- Given we have yet to experience our first end of tax year following changes to the MLS, there has not yet been an opportunity to fully assess the impact those changes will have on the private health sector. We believe that the industry should not be required to shoulder further change until the impact of the MLS can be assessed.

- The PHI rebate continues to represent good value for Government, with every dollar invested generating an additional $2 in privately funded revenue to support the costs of delivering health in Australia.

**Impact of proposed changes to the PHI Rebate**

*Direct customer impact*

Proposed changes to the PHI rebate will directly impact more than 100,000 of our customers holding singles cover and more than 160,000 couples or families covered by Bupa Australia products. On average, we estimate that almost one in five Bupa customers will be impacted directly by the proposed changes. Industry-wide, the Treasury estimates more than 2 million people will be directly affected by the proposed changes.

The cost increases are very significant for customers, with increases of up to 66.7% for those who currently receive a rebate from the government but whose eligibility will change under the proposed changes.

A summary of the cost increase for customers is outlined in the following table:

| **Age** | **Percentage cost increase for customers as a result of the proposed rebate changes** | | |
|---|---|---|---|
| | Tier 1<br>*Singles $75,001 – $90,000*<br>*Families $150,001 – $180,000* | Tier 2<br>*Singles $90,001 – $120,000*<br>*Families $180,001 – $240,000* | Tier 3<br>*Singles $120,0001 +*<br>*Families $240,001 +* |
| Under 65 Years | 14.3% | 28.6% | 42.9% |
| 65 – 69 Years | 15.4% | 30.8% | 53.8% |
| 70+ Years | 16.7% | 33.3% | 66.7% |

*Source: Table developed from figures in KPMG PHI Industry Update*

Under the proposed system, reductions in the level of rebate start for single people earning more than $75,000 and couples/families earning more than $150,000 per year. Many of our customers earning incomes in this bracket would consider themselves “middle income” earners, as opposed to “wealthy” Australians. This is especially the case at the lower end of the tier, considering recent changes to the definition of income for tax and benefit purposes will mean that people who would, under previous definitions, not have been affected by the proposed changes will now be impacted.

In difficult economic times, customers in this income tier in particular will face a range of competing financial interests for a relatively inflexible budget.

More concerning however, as indicated in the table below, is that for the lower income tiers the cost of PHI premiums under the proposed changes will increase at a much greater rate than the MLS they would be liable to pay should they drop their PHI. Customers in Tier 1 face an increase in premiums without any change at all to their current MLS.

Any claims that MLS changes are designed as a 'stick' to better incentivise PHI and to prevent people from changing or dropping their cover under the new rebate structure are not supported by the table below. The majority of customers impacted by the proposed PHI rebate changes will face premium increases higher than any change to the MLS.

| Average Single (Pre Rebate) | | | $1,813 | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| Income | Current Rebate | Premium Cost | MLS now | Future Rebate | Premium Cost | MLS Then | Change in Premium | Change in MLS |
| $75,000 | $544 | $1,269 | $750 | $544 | $1,269 | $750 | $0 | $0 |
| $75,001 | $544 | $1,269 | $750 | $363 | $1,450 | $750 | $181 | $0 |
| $90,000 | $544 | $1,269 | $900 | $363 | $1,450 | $900 | $181 | $0 |
| $90,001 | $544 | $1,269 | $900 | $181 | $1,632 | $1,125 | $363 | $225 |
| $120,000 | $544 | $1,269 | $1,200 | $181 | $1,632 | $1,500 | $363 | $300 |
| $120,001 | $544 | $1,269 | $1,200 | $0 | $1,813 | $1,800 | $544 | $600 |
| $250,000 | $544 | $1,269 | $2,500 | $0 | $1,813 | $3,750 | $544 | $1,250 |

| Average Family Premium (Pre Rebate) | | | $3,626 | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| Income | Current Rebate | Premium Cost | MLS now | Future Rebate | Premium Cost | MLS Then | Change in Premium | Change in MLS |
| $150,000 | $1,088 | $2,538 | $1,500 | $1,088 | $2,538 | $1,500 | $0 | $0 |
| $150,001 | $1,088 | $2,538 | $1,500 | $725 | $2,901 | $1,500 | $363 | $0 |
| $180,000 | $1,088 | $2,538 | $1,800 | $725 | $2,901 | $1,800 | $363 | $0 |
| $180,001 | $1,088 | $2,538 | $1,800 | $363 | $3,263 | $2,250 | $725 | $450 |
| $240,000 | $1,088 | $2,538 | $2,400 | $363 | $3,263 | $3,000 | $725 | $600 |
| $240,001 | $1,088 | $2,538 | $2,400 | $0 | $3,626 | $3,600 | $1,088 | $1,200 |
| $500,000 | $1,088 | $2,538 | $5,000 | $0 | $3,626 | $7,500 | $1,088 | $2,500 |

| Example of a Family Premium | | | $5,000 | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| Income | Current Rebate | Premium Cost | MLS now | Future Rebate | Premium Cost | MLS Then | Change in Premium | Change in MLS |
| $150,000 | $1,500 | $3,500 | $1,500 | $1,500 | $3,500 | $1,500 | $0 | $0 |
| $150,001 | $1,500 | $3,500 | $1,500 | $1,000 | $4,000 | $1,500 | $500 | $0 |
| $180,000 | $1,500 | $3,500 | $1,800 | $1,000 | $4,000 | $1,800 | $500 | $0 |
| $180,001 | $1,500 | $3,500 | $1,800 | $500 | $4,500 | $2,250 | $1,000 | $450 |
| $240,000 | $1,500 | $3,500 | $2,400 | $500 | $4,500 | $3,000 | $1,000 | $600 |
| $240,001 | $1,500 | $3,500 | $2,400 | $0 | $5,000 | $3,600 | $1,500 | $1,200 |
| $500,000 | $1,500 | $3,500 | $5,000 | $0 | $5,000 | $7,500 | $1,500 | $2,500 |

CHANGE IN PREMIUMS HIGHER THAN CHANGE IN MLS

PREMIUM COST HIGHER THAN MLS

*Source: Australian Health Insurance Association*

*Impact on Premiums*

Research conducted by the AHIA indicates that around one million customers are likely to downgrade or drop their cover as a result of the proposed changes. People with significant claims or high utilisation of health services are the least likely to change their cover as a result of price increase or other changes. The group of people most immediately at risk of either downgrading or leaving are younger people who experience below average claims history.

The industry is already feeling the impact of significant downgrades in customer cover over the past 6 months as economic pressure increases. The proposed changes to the rebate will simply exacerbate that affect.

The price increases from these proposed changes are significant and they will impact middle income singles families as well as wealthier ones. Under the proposed changes, customers in the first tier will be especially challenged in relation to price elasticity.

Downgrades, including customers dropping extras cover, are a very real risk for the industry and for the broader health sector. Moreover, customers can choose to drop extras cover without any MLS implications and in many cases, can similarly downgrade their hospital products without any MLS impact.

According to surveys assessed by the AHIA, around 41% of PHI customers indicated they would downgrade their cover and 36% stated they would drop their ancillary cover should their premium increase by around 25%.

If this was to occur, it would affect Australia's health sector in two ways.

1) It would cause an increase in premium for entire privately insured community as it is not only age mix but also product mix which helps maintain affordability under a community rated system, This in turn would force a larger number of people to have to consider either downgrading or dropping cover in response to changes in price.

2) It would significantly increase pressure on the public system, as people with downgraded or no cover will have rely more heavily on the public sector for those services they have either cancelled or chosen to accept a large excess for.

Another significant challenge for the industry is a substantial slowing of growth in recent times. Over the past 12 months (which covers the period of time since the MLS changes were announced) Bupa Australia's growth (quarter on quarter) has reduced consistently each quarter from a high of 0.8% to just a quarter of that, 0.2%, in the March 2009 quarter.

This is especially concerning given that younger people previously accounted for the majority of our new customer sales every year.

If these younger, healthier people leave the sector, downgrade or choose not to join as a result of the proposed PHI rebate changes, the subsidy they provide to the overall risk of the insured pool will instead have to be funded by premium growth for all insured Australians.

In addition to the cost and service pressure that this could potentially place on the public health system, it presents a significant equity and access issue for lower income families as well as those who are most likely to need to access health services.

PHI attracts customers across a diverse range of incomes. AHIA analysis of National Health Survey and PHIAC data indicates around 37% of Australian households with gross annual incomes of between $26,000 and $48,049 currently rely on private cover

The policies that support PHI in this country have improved the age mix of the insured population, keeping premiums lower and making it possible for those low-middle income families or individuals who value or need private cover, to choose it.

The proposed changes hit harder with the lower proposed income tiers (in terms of PHI increase vs MLS increase) than with the highest income tier. These are the tiers likely to contain younger people with fewer claims who are the greatest risk for retention in the face of increased cost.

The wealthiest Australians will always be able to afford PHI. Any additional pressure on premiums will hit low to middle income earners and fixed-income seniors hardest, which includes some of the people who are the greatest consumers of health services in this country.

**Administration – application and cost.**

There is still no detail around how the proposed changes will be administered nor how much administration and communication is likely to cost insurers. Certainly the cost of administering and reconciling these multiple tiers against 11 million people's annual income will be a mammoth task. We understand the bulk of this administration will be done by the Federal Government, primarily through the Australian Tax Office. Nonetheless, arrangements with insurers will likely remain in place to facilitate upfront rebate claiming as a premium reduction.

For the industry, the lack of clarity around administration of the scheme means the costs of start-up, systems, communication and ongoing administration of this far more complex proposed rebate scheme cannot be estimated. This is of considerable concern, as we are still unclear on the degree to which these costs could ultimately impact on our customers through their premiums.

The proposed changes will also serve to increase complexity for a very large number of PHI customers. To ensure this is managed as smoothly and effectively as possible, the Federal Government should commit to a significant annual consumer communications campaign, incorporating mailings and production of printed material and forms.

This will help to ensure that the cost burden associated with helping people understand and navigate the additional complexity does not rest with those same customers who already face significant premium increases as a result of the changes.

We are not clear whether Treasury has incorporated the costs for set up and ongoing administration of the proposed system into its savings calculation, but believe that, given the proposal has been promoted as an essential revenue measure of the 2009-10 budget, any true savings figure must also reflect associated costs.

**Timing of change**

Bupa Australia is concerned that this proposal comes at a time when there still has not been an opportunity for full or thorough assessment of the impact of the Medicare Levy Surcharge changes which were passed by the Parliament in November last year.

PHIAC figures show that the rate of growth in PHI membership since the changes were announced have dropped from a prior rate of 4% to just 2% in the March 2009 quarter. The industry has yet to experience the impact of the first 'end of tax year' since the MLS changes.

Bupa Australia strongly believes that no changes should be made that are likely to further affect the PHI industry until there has been an opportunity to fully assess and understand the impact of the global financial crisis and the MLS changes on current and future membership.

**Conclusion**

Bupa Australia's concern about the proposal in no way reflects a concern about the value of our products. PHI is a highly competitive industry, where product development, innovation and value have always played an integral part in an insurer's success or failure in the market. We continue to provide high quality, great value products and are proud of our success in this challenging environment.

The fundamentals that make PHI attractive remain unchanged: Choice of doctor, access to hospital and excellent care when you need it without the waiting lists that currently exist in the public system. Australians recognise and appreciate the value of this, with more than 56% of elective surgery conducted in the private system.

Moreover, there are also millions of lower-middle income singles and families not currently subject to the MLS who choose PHI because they recognise its value to them.

We believe that choice in healthcare should be an option for the broadest possible number of Australian families – not just the wealthy. This can not be achieved unless the private sector remains viable, attractive and affordable for all Australians.