Chapter 2

Demutualisation of private health insurers

2.1 Schedule 1 of the bill provides relief from capital gains tax (CGT) for private health insurance policyholders when their insurer converts from a mutual not-for-profit operation into a for-profit insurer. The CGT exemption applies both to policyholders who receive shares and those who receive a cash payment.

2.2 The amendment in Schedule 1 has particular currency in light of the merger of MBF with BUPA Australia Group and MBF's demutualisation on 16 June 2008. NIB demutualised in October 2007. The demutualisation of health insurance funds follows a number of demutualisations of building societies and insurance companies.[1]

2.3 The MBF demutualisation entitled MBF's policy holders to a cash payment for the disposal of certain membership rights. Division 9AA and Schedule 2H of the *Income Tax Assessment Act 1936* provide a tax exemption for capital gains from demutualisations of life insurers, general insurers and some other mutuals.[2] However, many policyholders of health insurers are not captured under the Act's definition of 'members'.[3] This bill will extend the capital gains tax exemption to all private health insurance policyholders.

2.4 The ATO notes on its website:

> Until the proposed new law is enacted, there is some uncertainty about what amount, if any, should be included in your tax return as a result of the demutualisation. In light of this uncertainty, the Tax Office will allow you to lodge your 2007/2008 tax return without including any capital gain from the receipt of cash from the MBF demutualisation at this stage. The Tax Office and MBF will let you know what amount (if any) to include in your tax return and how to do this at a later time.[4]

2.5 If the bill is passed, MBF policyholders who received a cash payment in June 2008 will not be liable to pay CGT on this sum, and nor will future beneficiaries of demutualisations. The cost to revenue is estimated at around $2 million in 2009-10

---

1 Better known examples include Colonial Mutual, AMP and St George. See 'Demutualisation in Australia', *Reserve Bank of Australia Bulletin*, January 1999, pp 1-10.

2 *Explanatory Memorandum*, p. 5.

3 The Hon. Chris Bowen, Minister, Competition Policy and Consumer Affairs, *Second Reading Speech*, 26 June 2008.

4 Australian Taxation Office, 'Demutualisation of MBF', http://www.ato.gov.au/individuals/content.asp?doc=/Content/00147168.htm.

and $1 million in following years.[5] This amount would obviously vary with the number of funds which demutualise in coming years, which is hard to predict.

2.6 The demutualisation of a private health insurance fund is clearly of financial benefit for existing policyholders. However past policyholders, who have also contributed to building up the fund's reserves, will not receive any benefit. Taxpayers in general have also contributed to the reserves of the health insurance funds through the very generous subsidies given to private health insurance funds, such as the 30 per cent rebate and the exemption from the Medicare levy surcharge. This suggests there is an argument that at least some of the windfall gains accruing to those people who happen to be policyholders at the time of demutualisation should be returned to the community by making the gains taxable.

2.7 The Government has argued that this taxation exemption 'is intended to facilitate the demutualisation of private health insurers'. Demutualisation contributes to the spread of share ownership in the community. It allows the entity concerned to raise external capital more readily, which may enable it to expand or diversify its operations. Arguably, the accountability arrangements pertaining to a listed company are stronger than those applying to a mutual association.

5 *Explanatory Memorandum*, p. 5.