

# **FAMILY FIRST**

## **Dissenting Report**

### **Provisions of the Medibank Private Sale Bill 2006**

1.1 FAMILY FIRST believes the government is selling out Australian families by selling Medibank Private. Profits should not come before families.

1.2 Private health insurance is important to Australian families, where take-up rates are highest among couples who have children.

1.3 Private health insurance has become an essential service for these families, who want access to quality hospitals at affordable prices. Private health cover gives families a sense of security and peace of mind.

1.4 The Government is partly responsible for this situation. It has forced many Australians into private health insurance by offering discounts on cover and punishing families with higher fees if they sign up later on.

1.5 FAMILY FIRST believes the needs of Australian families must always come first.

1.6 Instead, the government has turned its back on families by selling our largest health insurer, Medibank Private.

1.7 The needs of the market are more important to the Government than the needs of families.

1.8 The sell-off of Medibank Private is yet another example of the Government's so-called 'family-friendly' policies being nothing more than 'market-friendly'.

1.9 A privatised Medibank Private would first and foremost have to make money for its shareholders - lots of money. Its top priority would be profits – delivering maximum returns to shareholders. This would lead to increased premiums and reduced services.

1.10 Australian families are already struggling and they would be worse off with a privatised Medibank Private motivated solely by profits and the bottom line.

1.11 The Government announced in September that it would sell Medibank Private by share market float in 2008.<sup>1</sup> That was a mistake.

1.12 The Government should ditch its plans to sell Medibank Private.

1.13 The Government should retain ownership of Medibank Private for the public good, to ensure affordable health insurance and quality health services for Australian families.

1.14 The Government continues to have a legitimate role as owner of a not-for-profit Medibank Private to ensure that the company focuses on the needs of its members rather than just profits.

### **Focus on the needs of members**

1.15 FAMILY FIRST wants the best for Australian families, and families would be worse off if Medibank Private is sold as its sole focus would then be profits rather than the needs of its members.

1.16 Medibank Private members want good quality health cover at the lowest possible prices. In October, Medibank Private announced a record \$200 million profit which " ... has been achieved while keeping the member at the centre of our strategies."<sup>2</sup> But as a company controlled by shareholders, the shareholders would take precedence over members. This would mean fewer services for members, and higher fees.

1.17 International studies validate FAMILY FIRST's concerns that members would be worse off. A recent OECD (Organisation for Economic Co-operation and Development) report into private health insurance found that, in general, for-profit medical insurers tend to be more motivated by profit and satisfying the interests of shareholders, while not-for-profit health insurance funds are in general terms more member and community focused.<sup>3</sup>

1.18 Medibank Private is not a mutual fund, but as a not-for-profit government-owned business it has characteristics similar to a mutual of putting members' interests before profits or shareholders.

1.19 It was reported that comparisons of mutual funds with profit making insurers found that mutuals were able to offer more to their members.

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1 *Medibank Private to be Floated in 2008*, Media Release: Senator Nick Minchin, Minister for Finance, 12 September 2006.

2 *Membership growth drives record result for Medibank*. Media Release, Medibank Private, 5 October 2006.

3 The OECD Health Project, *Private Health Insurance in OECD Countries*, OECD, 2004.

A 1999 study by global insurance giant Swiss Re concluded that in the health insurance sector, mutuals were generally more efficient than for-profit companies, enabling them to offer their members a better premium-to-payments ratio. And in a 2001 survey of 97 insurance companies in Western Europe, the International and Co-operative Mutual Insurance Association found that mutuals were more efficient and had lower premiums relative to claims payments.<sup>4</sup>

1.20 Dr John Deeble, a former commissioner in the Health Insurance Commission over the 14 years that the Commission managed Medibank Private, explained:

We always interpreted our task as one of giving standard private cover at affordable prices. We were not there to make profits; we were there to provide a service to people at the lowest price that we could do that at, but also not just to operate as a commercial operation which maximised its market but to be concerned with the quality of the health care that people got as well ... [I]t was not just a business to make money for government; it was established to provide a service.<sup>5</sup>

1.21 Another health fund argued that shifting the focus from the needs of members is less efficient:

Our view where a shareholder is placed above a member, as could happen in a for profit health fund, policies in regard to claim payments would become more focussed towards the stakeholder return than the outcome for the member, which in our view is not efficient or competitive.<sup>6</sup>

1.22 FAMILY FIRST has a fundamental disagreement with the Government over the aims of Medibank Private. The objective of Medibank should be to provide a service to consumers at the best possible price – not to make as much profit as it can. As health insurance has become an essential service to many Australian families, there is a legitimate role for government to provide these services to satisfy customers rather than profits.

### **Privatisation, efficiency and cutting benefits**

1.23 A report by CRA International, commissioned by the Department of Finance, found that Medibank Private was efficient, but "... has scope to increase efficiency by a further 5 to 7 per cent to match the efficiency of the better performing open health funds."<sup>7</sup>

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4 Breusch, J, 'The prognosis is uncertain', *Australian Financial Review*, 13 September 2006, p.61.

5 Dr Deeble, *Committee Hansard*, 3 November 2006, Canberra, p.29.

6 Westfund, *Submission 10*.

7 CRA International, *The Impact of Privatisation of Medibank Private on Private Health Insurance Premiums*, 21 October 2006, p.1.

1.24 But this report has not gone unchallenged. The Australian Medical Association questioned the scope for extra efficiencies:

We doubt that Medibank Private has fully exploited the scope for scale efficiencies. Were they to manage as efficiently as BUPA (the most efficient of the large funds), they could save some \$30 million per annum in management expenses. The report by CRA International (CRAI) argues that Medibank Private could achieve efficiency gains of 5 to 7%. Based on 2004-5 figures, that would imply cutting costs (management expenses and benefits paid) by between \$127 and \$178 million per annum. It is simply not possible to cut nearly \$180 million out of management expenses of \$238 million. Such cuts in costs would necessarily require cuts in benefits paid.<sup>8</sup>

1.25 It was argued that the CRA report focused on profits at the expense of benefits for members:

They have defined 'efficiency' as profit making. You will make a higher profit obviously if you can get your costs down. They have phrased it in such a way that people would believe that this relates to administrative expenses. But when you actually go through and see what they are saying, they are not talking about that. The seven per cent has got to come out of benefits ... [T]he only way they can get a higher gross margin and a higher net margin that is feasible is to pay less out in benefits. Is that a gain in efficiency for the members?<sup>9</sup>

1.26 The AMA points out that "the CRAI report cites MBF as a more efficient fund than Medibank Private on the grounds that MBF pays lower benefits."<sup>10</sup>

1.27 The issue comes back again to a fundamental disagreement over what the overall objectives of Medibank Private should be – to make a profit or to serve members. FAMILY FIRST believes that Medibank Private's main objective should be to serve members.

### **Premiums are likely to rise**

1.28 The Government argues that privatising Medibank Private will put downward pressure on premiums.

1.29 FAMILY FIRST believes this is nonsense, as there is already competition between health insurance funds. Privatising Medibank Private will in fact put extra upward pressure on premiums.

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8 Australian Medical Association, *submission 8A*.

9 Dr John Deeble, *Committee Hansard*, 3 November 2006, Canberra, p.38.

10 Australian Medical Association, *submission 8A*.

1.30 The Australian Medical Association argued that a privatised Medibank Private would face the extra pressure of having to make more money for shareholders:

Our concern is that, in order to get that return on the investment another entity would make to buy out Medibank Private, there are only a few ways that they can do it. One is to gain huge efficiencies in management, and we are not convinced that there are huge efficiencies to be gained. The other one is to reduce benefits. The problem with that is that may lead to a loss of membership of the fund. Another way to do it is to increase the income into the fund. There is a limit to how much can be done with non-premium income. There might be some efficiencies there in terms of investing money more wisely, but it would be hard to see a fund like Medibank Private not already effectively investing its assets. The conclusion is that premiums would probably have to go up as a result of the sale.<sup>11</sup>

1.31 Dr Deeble argues that privatisation would not make the health fund more competitive and that private ownership is not the best way to hold down costs:

Under the present proposals for a float, nothing significant would change. Despite conventional wisdom and convictions, there is no Australian evidence that private ownership and for-profit status has produced any efficiency gains sufficient to offset the higher cost of private capital; and good reason to believe that non-profit status, not the incentives of private ownership, has been the largest controlling influence on premiums.<sup>12</sup>

1.32 In addition, for-profit health funds have to earn more than other funds just to cover tax:

To give a return on funds, a for-profit fund has to earn 30 per cent more because it pays 30 per cent tax. In principle it is as simple as that. It is the tax exempt status of the non-profit funds which has kept premiums down, not the profit incentive of the for-profit ones.<sup>13</sup>

1.33 An extra pressure which may help increase premiums is people's reluctance to change funds, in the same way people are unlikely to change banks because of the hassle.

1.34 Medibank Private argued that health insurance is a competitive market:

... [P]eople do compare products and people do switch. They now have full portability. Those dynamics of competition are at their most intense now than they have ever been in the history of private health insurance in Australia.<sup>14</sup>

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11 Dr Yong, Australian Medical Association, *Committee Hansard*, 3 November 2006, Canberra, p.16.

12 Dr John Deeble, *submission 5*.

13 Dr John Deeble, *Committee Hansard*, 3 November 2006, Canberra, p.31.

14 Mr Morphy, Medibank Private, *Committee Hansard*, 3 November 2006, Canberra, p.61.

1.35 But Dr Deeble argued that people tended not to switch health funds despite differences in premiums:

... [health insurance] is not very price elastic at all. I can tell you that, in 15 years or so on that board, we could be five or 10 per cent or more above or below our competitors with no effect on our contributor membership at all.<sup>15</sup>

People make a decision on their health insurance membership when they join. There is, or there has been in all that time, almost no transfer between institutions on the basis of price. Also, all of the funds make it extremely difficult—and this is ordinary commercial practice which does not only apply to health funds, it applies to almost every other product—or almost impossible to compare prices directly because that is not what they want them to do.<sup>16</sup>

1.36 It is tempting for health funds to increase premiums to boost profits for shareholders.

### **Important role of government ownership**

1.37 There is a variety of views about what should happen to Medibank Private. Some have argued it should be "... sold to the right buyer, creating the right market structure " rather than floated on the share market.<sup>17</sup>

1.38 The Australian Medical Association would support the Government selling Medibank Private if it became a mutual, rather than a company floated on the stock exchange.<sup>18</sup>

1.39 But the best way to ensure families can afford health insurance is for the government to be a player in the sector to keep everyone honest.

1.40 If the Government no longer has a financial interest in the industry, how long will it be before its role of regulating premiums will become nothing more than a rubber stamp?

1.41 Dr Deeble argues that:

... MPL's presence affirms the broader public interest in private health insurance. I have always believed that Medicare is a national system of health care financing which includes the private sector and its insurers, not just a Commonwealth scheme of benefits for medical care and public hospital treatment. The two parts are complementary in ways which go

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15 Dr John Deeble, *Committee Hansard*, 3 November 2006, Canberra, p.29.

16 Dr John Deeble, *Committee Hansard*, 3 November 2006, Canberra, p.29.

17 Mr Francis Sullivan, 'Health insurers need competition', *Australian Financial Review*, 6 September 2006, page 63.

18 *Committee Hansard*, 3 November 2006, Canberra, p.16.

beyond the market place, although there are vested interests with a reason to argue otherwise.<sup>19</sup>

1.42 It was also argued that:

Poor co-ordination between the public and private provision of health care is a major, and justified, criticism of the Australian system and I see the continuing emphasis on separating them even further as our major policy mistake ... [B]ut the whole thrust of these proposals is to move Medibank Private Limited further away from the health service sector and into the more general finance industry. If the largest fund does so, others would probably follow. Integration would then be even less likely.<sup>20</sup>

1.43 Private health insurance is important to Australians. More than one in two adults have made the financial sacrifice to take out insurance, with the largest rates of private health insurance among couples with children. However, two thirds of those who do not have health insurance say it is because it is too expensive.<sup>21</sup> Given the significant government subsidies for health insurance, it is vital that the government continue to ensure access to private cover is affordable and accessible to as many Australians as possible.

### **Demutualisation has been bad for consumers**

1.44 There have been cases in the broader insurance industry where organisations that have been demutualised and made into for-profit companies have not appeared to serve their members well.

1.45 When the NRMA (National Roads and Motorists' Association) was demutualised in 2000 and removed as the leading premium-rebating insurer, others in the industry rejoiced. It became a management-focused company intent on delivering to shareholders ahead of policyholders.

1.46 In 2003 it was reported that NRMA members "... with 'basic care' membership [for road service] will have their fees hiked by 23 per cent or \$12.50 to \$67.50 while 'premium care' customer fees will jump by 33 per cent or \$34.60 to \$140 ..."<sup>22</sup>

1.47 Former NRMA board member Richard Talbot criticised the price hikes, saying:

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19 Dr John Deeble, *submission 5*.

20 Dr John Deeble, *submission 5*.

21 Australian Bureau of Statistics, *Private Health Insurance: A snapshot, 2004-05*, 22 November 2006, Catalogue 4185.055.001.

22 Belinda Tasker, 'NRMA to introduce hefty fee increases', *The Canberra Times*, 24 April 2003, p.19.

Members were told just two years ago that, after demutualisation, the road service would be in a stronger financial position ... Now they find, instead of a \$20 million annual profit for 2003 [forecast at the time of demutualisation], we have massive losses ...<sup>23</sup>

1.48 It was also commented that:

Any student of demutualisation or reorganisation of insurance companies over the past two year would notice the only consequence which is certain is that the remuneration of senior management immediately improves ... Benefits to customers – that's a less certain prospect as any AMP (or NRMA) shareholder might agree.<sup>24</sup>

1.49 While not a mutual, the sale of Medibank Private will follow the same path. Rewarding shareholders will be the top priority, which will be at the expense of members and their needs.

## **Conclusion**

1.50 The Government is selling out Australian families by selling Medibank Private. Profits should not come before families.

1.51 If the Government is serious when it claims to care about Australian families, it should ditch its plans to sell Medibank Private which will lead to higher premiums and reduced services.

1.52 Australian families will be worse off if Medibank Private is sold and the financial bottom line dictates decisions.

1.53 Families are already struggling to make ends meet and they will suffer further from a privatised Medibank Private.

1.54 The needs of families must always come first. For this reason, FAMILY FIRST calls on the Government to admit it has made a mistake and retain ownership of Medibank Private to ensure quality health cover at the lowest possible premiums.

**Senator Steve Fielding**  
**Leader of the FAMILY FIRST Party**  
**FAMILY FIRST Senator for Victoria**

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23 Anthony Hughes and Kate Askew, 'Now the NRMA lemon puts the squeeze on members', *The Sydney Morning Herald*, 4 March 2003, p.1.

24 Jack Waterford, 'Milking a cash cow leaves us feeling sick', *The Canberra Times*, 5 April 2006, p.17.