Institute of Actuaries of Australia

**HEALTH PRACTICE COMMITTEE**

**Information Note: Private Health Insurance – Rebate Means Testing**

**August 2011**

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## 1. Information Note status and purpose

1.1 This Information Note was prepared by the Health Practice Committee of the Institute of Actuaries of Australia ("Institute"). It does not represent a professional standard or practice guideline of the Institute.

1.1 The purpose of this Information Note is to bring to the attention of Institute members the considerations and potential impact arising from the Federal Government's proposal to means test the 30% rebate on private health insurance ("PHI") contributions, when providing advice to private health insurers.

1.2 Feedback on this Information Note from Institute members is encouraged and should be forwarded to the Health Practice Committee at: peter.lurie@au.pwc.com

## 2. Legislative background

2.1 The Labor Government announced its intention to means test the rebate in the 2009/10 Federal budget. Under the changes proposed at the time, individuals/couples who earn above the income threshold for the Medicare Levy Surcharge ("MLS") would be eligible for a reduced (or no) rebate, but would face an increased MLS for not holding a qualifying PHI hospital product.

2.2 When introduced to the Senate in September 2009 and again in November 2009, the legislation failed to pass on both occasions. However, in the 2011/12 Federal Budget, the Government announced that it would once again attempt to pass legislation to means test the rebate. Since the Budget announcement in May 2011, the Government introduced the three "Fairer PHI Incentive Bills" legislation to Parliament with a proposed commencement date of 1 January 2012.

2.3 The table below summarises the changes in the 2011/12 financial year:

| | | | Current | | Proposed | |
|---|---|---|---|---|---|---|
| | **Income Tier** | **Taxable income per annum** | **Rebate Level** | **Medicare Levy Surcharge %** | **Rebate Level** | **Medicare Levy Surcharge %** |
| Singles | Non-tier | Less than $80,000 | 30% | 0.00% | 30% | 0.00% |
| | Tier 1 | $80,001 to $93,000 | 30% | 1.00% | 20% | 1.00% |
| | Tier 2 | $93,001 to $124,000 | 30% | 1.00% | 10% | 1.25% |
| | Tier 3 | $124,001 or more | 30% | 1.00% | 0% | 1.50% |
| | | | | | | |
| Families | Non-tier | Less than $160,000 | 30% | 0.00% | 30% | 0.00% |
| | Tier 1 | $160,001 to $186,000 | 30% | 1.00% | 20% | 1.00% |
| | Tier 2 | $186,001 to $248,000 | 30% | 1.00% | 10% | 1.25% |
| | Tier 3 | $248,001 or more | 30% | 1.00% | 0% | 1.50% |

2.4 The above applies to members under 65 years of age. For members 65 to 70 years of age, the rebate is 35% with proposed means tested tiers 1 to 3 of 25%, 15% and 0%. For members age 70 years and older, the rebate is 40% with proposed means tested tiers 1 to 3 of 30%, 20% and 0%.

2.5 As shown, the income thresholds for couples and families with one child are double the individual threshold. The thresholds for families with more than one child increase by $1,500 for each additional child.

## 3. Impact of proposed changes

3.1 The proposed legislation changes the financial incentives with respect to PHI for individual policyholders earning above $80,000 a year (or families earning over $160,000), which may cause some policyholders to consider downgrading their PHI cover or lapsing. For example, the rebate for policyholders in income tier 1 decreases without any increase in the MLS. Policyholders in income tiers 2 and 3 will experience an increase in premium as the rebate is reduced, or face an increase in the MLS if they lapse.

3.2 The extent to which the proposed changes will impact membership and coverage is unknown. Any significant change in the structure or balance of the various incentives and penalties supporting Community Rating has the potential to lead to structural and/or behavioural changes to current and future membership of health insurers.

## 4. Considerations for members

4.1 Institute members should consider these changes in relation to their specific client, including their potential impacts and the likelihood of those impacts, when providing advice in relation to private health insurance.

4.2 The underlying drivers to consider include:

- the potential for policyholders to move to lower premium products;
- the potential for an initial increase in policyholder lapses and/or ongoing reduction in new policyholders joining;
- the likelihood that those lapsing and downgrading would generally have more favourable claims experience, and that some of these policyholders may also make claims immediately prior to lapse/downgrade; and
- lapses and product downgrades by policyholders not directly affected by the rebate means test, in response to higher premium increases that may result from worsening claims experience caused by the first round of lapses and downgrades.

4.3 Resulting from these drivers, impacts to consider include (amongst others):

- the likely impact on future health insurer profitability and premium rate increases;
- impact on solvency and capital adequacy requirements, available net capital and any increased risk margins required;
- impact of changing policyholder profiles on premium income, claims experience, drawing (claim) rates, risk equalisation, management expense ratios etc; and
- impact on capital management plans, investment strategy and risk appetite.

4.4 If any Institute member is in doubt about the appropriate approach to advising their clients in these matters, they should consult with another suitably experienced actuary or a member of the Health Practice Committee.