

## WILL THE GOVERNMENT'S PROPOSED INSURANCE REFORM INCREASE THE HEALTH INSURANCE COVERAGE OF OLDER AUSTRALIANS?

### Jeromey Temple

*This article examines the impact of the Coalition Government's proposed increase in the private hospital insurance rebate for people aged 65 and over. It concludes that the increased rebate is only likely to benefit those already insured. Most people aged 65+ who are not insured are drawn from the ranks of the less affluent. The rebate will do little to overcome the financial problems they face in affording private health cover.*

In the previous issue of *People and Place*,<sup>1</sup> I examined the factors associated with the private health insurance coverage of older Australians (aged 55 years and over). The key conclusion from this article was that subgroups of the elderly, such as those in lone-person households, those on low incomes and the overseas born, would face difficulties in accessing elective surgery in a timely manner due to their poor insurance coverage.

Currently, the Federal government provides a 30 per cent rebate on private health insurance premiums. This is available to any Australian citizen, and is not income tested. Since the publication of my previous paper, the Federal government proposed (in August 2004) that this 30 per cent insurance rebate be increased to 35 per cent for persons aged 65-69, and to 40 per cent for persons aged over 70, at a cost of \$445.5 million over four years. The Minister for Health and Ageing, Tony Abbott, says that this policy will reward older Australians who currently have health insurance and will encourage a greater number of older persons to purchase health insurance.<sup>2</sup> The Prime Minister, John Howard, has argued that the new extended rebate will take pressure off the public health care system. Further, the government argues that the rebate will benefit a broad cross section of the elderly, thus constituting a

'safety net for older Australians'.<sup>3</sup>

In reply, the Labor Party, the Democrats and several Independent senators argue that the extended rebate will not increase the affordability of health insurance for older persons who do not already have it, and say that they will block the reforms in the Senate.<sup>4</sup> In response, the insurance industry has supported the new initiative and urged the Labor party to pass the reforms. For example, Michael Roff, executive director of the Australian Private Hospitals Association says: 'Some have made the bizarre assertion that older Australians who cannot afford health insurance get no benefit from the government's newly enhanced incentive ... Even more of them [older persons] will be able to afford hospital cover'.<sup>5</sup> Similarly, Russell Sneider, Chief Executive of the Australian Health Insurance Association, argues that the additional rebate will reduce 'stresses on the hospital system' and enable more persons aged 65 and over to 'either keep their private health insurance or take out cover'.<sup>6</sup>

Taken with the findings from my previous paper in *People and Place*, the purpose of this current article is to examine the likelihood of this new rebate increasing the insurance coverage of older Australians and to ask whether these reforms will benefit a broad cross section of the elderly.

**WILL THE POLICY INCREASE THE INSURANCE COVERAGE OF OLDER AUSTRALIANS SUBJECT TO LIFETIME HEALTH COVER?**

The effect of the new rebate cannot be considered in isolation from the Lifetime Health Cover policy. Lifetime Health Cover, introduced in July 2000, restructured the age component of community rating<sup>7</sup> in the Australian health insurance market. All persons aged over 30 who remained uninsured after July 2000 had their future insurance premiums subject to a two per cent surcharge for each year of age that they remain uncovered. Between July 1999 and July 2000, a person of any age could join a health insurance fund and remain exempt from this surcharge, so long as they remain covered for the rest of their life.<sup>8</sup> For example, a person aged 40 who purchases health insurance for the first time in 2004 is now subject to a 20 per cent surcharge on their current and future premiums ((40-30)\*2%). If this same person delays purchasing health insurance for a further 10 years, the surcharge will grow to 40 per cent ((50-30)\*2%) and so on.<sup>9</sup> The Lifetime Health Cover surcharge is capped at a maximum loading of 70 per cent. All persons born before July 1934

are exempt from the Lifetime Health Cover surcharge.

The two per cent surcharge has decreased the affordability of health insurance for those born after 1934, and this has important implications for the new rebate. To illustrate this argument, Table 1 displays the premiums payable for hospital insurance by date of birth and date of insurance purchase. The base premiums are for a lone person purchasing hospital cover. The table uses a base insurance premium of \$1300 as an example. This value is similar to a number of hospital insurance policies available in the marketplace that enable treatment as a private patient in a public hospital, and involve payment of no excess.<sup>10</sup>

As can be seen in Table 1, the effect of the Lifetime Health Cover exemption for people born before July 1934 is clear. Under the current system a person born in January 1934 purchasing insurance for the first time in 2005 would pay \$910 for this insurance policy after the 30 per cent rebate. With the introduction of the 40 per cent rebate, the insurance premium drops to \$780, a saving of \$130.

Private health insurance will be considerably more expensive for a person born one year later in 1935 who attempts

**Table 1: Annual insurance premiums under the current and proposed rebate system, 2005**

Year Born	Age in 2005	Base Premium \$	Purchased Insurance		Base Premium Plus Surcharge \$	Premium After 30% Rebate \$	Premium After New Rebate \$
			Before July 2000 (Amnesty Period)	After July 2000 (After Amnesty)			
1932	73	1300	n.a	n.a	1300	910	780
1933	72	1300	n.a	n.a	1300	910	780
1934	71	1300	n.a	n.a	1300	910	780
1935	70	1300	-	70% max	2210	1547	1326
1936	69	1300	no surcharge	-	1300	910	845
1937	68	1300	-	70% max	2210	1547	1437
1937	68	1300	no surcharge	-	1300	910	845
1950	55	1300	-	50%	1950	1365	1365
1950	55	1300	no surcharge	-	1300	910	910

Source: Author's calculations

to purchase health insurance for the first time in 2005. Aged 70 in the year 2005, they are subject to the maximum 70 per cent Lifetime Health Cover surcharge. The base premium for this person is increased from \$1300 to \$2210 after the surcharge. Under the current 30 per cent rebate system, this person pays \$1547 per annum for their hospital insurance policy. Under the new rebate system, the person pays \$1326. To be clear, this 70 year old pays \$546 more per annum than the 71 year old for exactly the same insurance policy due to the Lifetime Health Cover exemption rule, even with the new rebate.

In contrast, a person born in 1937 who had purchased health insurance before July 2000 pays no Lifetime Health Cover surcharge. After the current 30 per cent rebate this person (who will be aged 68 in 2005) pays \$910 per annum. Under the proposed system, the person is entitled to a 35 per cent rebate, decreasing the annual insurance premium by \$65 to \$845. A person of the same age attempting to purchase health insurance for the first time in 2005 will face a premium of \$1436.50 for exactly the same insurance policy.

The Lifetime Health Cover surcharge affects persons of all ages, not just the elderly. A person aged 55 who, for the first time, has decided to purchase health insurance, will be subject to a 50 per cent surcharge ((55-30)\*2%). As this person is younger than 65, the government's proposed reforms of August 2004 do not affect them. After the 50 per cent surcharge and less the 30 per cent rebate, this person faces a premium of \$1365. A person of the same age who had purchased health insurance prior to July 2000, pays a net premium of \$910 for the same insurance policy.

The key point is that older persons, who would like to purchase health insur-

ance for the first time at some point after July 2000, face a much higher premium than those older persons who already had health insurance before that date. In fact, due to the Lifetime Health Cover surcharge, any person in the former position born between 1935 and 1940 will be subject to the maximum 70 per cent surcharge in the year 2005. This means that an additional five per cent or 10 per cent rebate for the uninsured will only have a small effect at the margin.

An important consideration is what rebate would enable an uninsured person to purchase the same health insurance policy at the same price as an insured person in 2005? That is, what rebate might encourage an uninsured person to buy health insurance?

We can define the rebate required (RR) at age  $i$  as:

$$RR_i = 1 - \frac{NP_i^{INS}}{SP_i^{UN}}$$

where:

NP is the Net Premium for an insured person of age  $i$ , that is the out-of-pocket premium paid by an insured person.

SP is the after Surcharge Premium for an uninsured person of age  $i$ . This is the base premium plus the Lifetime health cover surcharge, but before the rebate.

Table 2, shows the rebate required to allow people who do not have health insurance to purchase it at the same price as a person who had purchased insurance prior to July 2000. Instead of a rebate of 40 per cent, a person aged 70 in 2005 would require a rebate of 64.7 per cent to purchase health insurance at the same price as a person aged 70 who already holds it. A person aged 51 would require a rebate of 57.75 per cent to buy health insurance at the same price as a person of

**Table 2: Lifetime Health Cover surcharge, rebate offered and rebate required for uninsured persons to reduce costs to the level of those required to pay the surcharge, 2005**

Age	Lifetime Health Cover surcharge	Proposed rebate offered %*	Rebate required %**
73	n.a	40	n.a
72	n.a	40	n.a
71	n.a	40	n.a
70	70	40	64.7
69	70	35	64.7
68	70	35	64.7
67	70	35	64.7
66	70	35	64.7
65	70	35	64.7
64	68	30	64.3
63	66	30	63.9
62	64	30	63.4
61	62	30	63.0
60	60	30	62.5
59	58	30	62.0
58	56	30	61.5
57	54	30	61.0
56	52	30	60.5
55	50	30	60.0
54	48	30	59.5
53	46	30	58.9
52	44	30	58.3
51	42	30	57.8

Source: Author's calculations

\* Existing 30 per cent rebate plus the new rebate for people aged 65-69 and 70+

\*\* Rebate required for a previously uninsured person to buy insurance at the same price as an insured person

the same age who already has insurance. As this person qualifies for the 30 per cent rebate, not the extended rebate, this represents a shortfall of 27.7 percentage points. Clearly I am not proposing that such a policy should be implemented, but the calculation does point to the inequity faced by many Australians, both old and young, who desire to purchase health insurance. Although the Lifetime Health Cover provided a one-year grace period (July 1999 to July 2000) in which a person of any age could purchase health

insurance and remain exempt from the surcharge, it is likely that a large number of people simply did not have the funds to purchase health insurance during this time frame. If the grace period had been extended over a longer period, it might have helped more people purchase health insurance, and avoid the two per cent surcharge.

**WILL THE POLICY INCREASE THE INSURANCE COVERAGE OF OLDER AUSTRALIANS WHO ARE EXEMPT FROM LIFETIME HEALTH COVER?**

As people aged 71 and over in 2005 are not subject to the Lifetime Health Cover surcharge, the 40 per cent rebate may have a different effect upon their propensity to purchase health insurance. A key question then is did the initial 30 per cent rebate increase the insurance coverage of those aged over 65?

Several analysts have examined the effectiveness of the Private Health Insurance Incentives Scheme, the Private Health Insurance Incentives Act and Lifetime Health Cover on the health insurance coverage of the Australian population. Butler has argued that the effect of the 30 per cent rebate was small in comparison to the introduction of Lifetime Health Cover.<sup>11</sup> Frech et al. also point out that the 30 per cent rebate did increase health insurance coverage, but report that the effect was small.<sup>12</sup> Manners has suggested that the 30 per cent rebate was not as successful as it could have been as it was not financially attractive for low income earners, but does note that no gap insurance<sup>13</sup> may

have improved the operation of the 30 per cent rebate.<sup>14</sup> Quinn's study concludes, that: 'even a generous rebate seems small compared to the effective prices faced by many Australians'.<sup>15</sup> The long run effectiveness of such a costly subsidy has also been questioned, given the potential for health care price inflation to make the subsidy ineffective.<sup>16</sup>

Research has shown that the uptake in health insurance due to the Private Health Insurance Incentives Scheme and the 30 per cent rebate has not been uniform across the population. Using taxation data, Smith found that about half of the Federal government's expenditure on the 30 per cent rebate went to the highest 20 per cent of income earners, and almost 75 per cent of the Federal funding for the 30 per cent rebate goes to the top 40 per cent of income earners.<sup>17</sup> A possible explanation is the high level of self insurance<sup>18</sup> in the population. Vaithianathan has shown that prior to the reforms in 1997, many wealthier families were opting out of private health insurance coverage and becoming self insured. When the tax disincentive in the Private Health Insurance Incentives Scheme was introduced and then the subsequent Private Health Insurance Incentives Act 30 per cent rebate, a large number of wealthier people switched from self-insurance to private health insurance.<sup>19</sup> More generally, Wilcox argued that, since income is highly associated with health insurance, it is not surprising that middle and upper income households benefited more from the 30 per cent rebate than lower income households.<sup>20</sup> Hall et al. have pointed out that a large proportion of Federal funds were simply directed to high income earners who already held insurance before the reforms.<sup>21</sup>

To summarise, those on high and medium incomes were far more likely to benefit from the 30 per cent private health

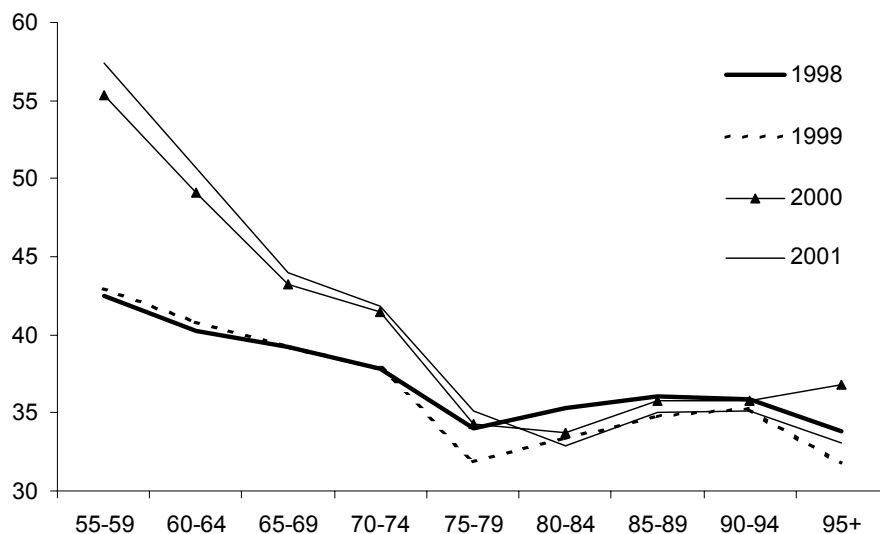
insurance rebate, while the policy had little effect in inducing a large number of low income earners to purchase health insurance.

The influence of the recent insurance reforms on the older population has been small. I have found that, for persons aged over 55, an age grading effect exists such that the increase in health insurance decreases with age.<sup>22</sup> This effect is shown in Figure 1. As can be seen, there was little change in the percentage of the population covered by health insurance for persons aged over 70 between 1998 and 2001. The lack of responsiveness of those aged over 70 to the insurance reforms indicates that the 30 per cent rebate had little effect on their propensity to purchase health insurance. Given that it is middle and upper income earners who predominantly benefited from the 30 per cent subsidy, it is unlikely that those older persons born before 1934, and not subject to the Lifetime Health Cover rules, will increase their coverage given an additional subsidy of five per cent.

#### **WILL THE POLICY BENEFIT A BROAD CROSS SECTION OF THE ELDERLY?**

A key justification made for the recent insurance reforms is that, by improving health insurance coverage of the population, pressure will be taken off public hospitals and waiting times for elective surgery will decrease.<sup>23</sup> However, since the implementation of recent reforms, there is little evidence to suggest that waiting lists have been reduced. Drawing upon National and State level data, Hurley et al. find that waiting lists for public hospitals have remained relatively stable over the period 1995 to 2001.<sup>24</sup> Birrell et al., however, find that, for surgical procedures, there is actually a trend to increased, rather than decreased,

**Figure 1: Percentage with health insurance by age, 1998 to 2001**



Sources: Private Health Insurance Administration Council, 'Statistical trends—membership and benefits', 2004; Australian Bureau of Statistics, 'Estimated resident population—Australia', 2004

waiting times.<sup>25</sup> Supporting both the Hurley and Birrell et al. observations, Deeble argues: 'Some bottlenecks remain and they tend, unfortunately, to have most impact in a few specific services, mostly surgical, which are used by older people with the least ability to use private alternatives'.<sup>26</sup> Hurley et al. have also argued: 'Both theory and evidence indicate that creating a parallel private sector can actually increase wait times when providers can work simultaneously in both the public and private sectors'.<sup>27</sup>

The issue of waiting times is important given the recent shift to elective surgical procedures being performed in the private, rather than public, hospital system. With the future supply of surgeons in the public health care system becoming increasingly uncertain, Birrell et al. foresee a situation in which 'surgery is generally available for the more affluent and for those with the

foresight, means and willingness to make the required financial sacrifice'.<sup>28</sup> That is, holding health insurance will become increasingly important for older persons requiring elective surgery. Those older persons who are subject to the full 70 per cent surcharge may find it difficult to access surgery in a timely manner, given their lack of insurance coverage.

The Prime Minister has stated on several occasions that these reforms will assist a broad cross section of the elderly.<sup>29</sup> Although it is true that many older Australians with health insurance are on low incomes, results from my previous paper show that lone females, lone males, those aged over 75, those who are born overseas or living in regional areas, and those with low retirement incomes have a substantially lower probability of holding health insurance in old age.<sup>30</sup> The government's own Industry Commission

inquiry into health insurance also hypothesized that, in old age, those on low income and who are widowed have a low propensity to purchase health insurance.<sup>31</sup> It is these groups of older Australians who will continue to be locked out of health insurance and who will not reap the benefits of the new reforms due to the Lifetime Health Cover surcharge.

This poses important equity questions for the Australian health care system — those with health insurance are able to jump the public sector queue and obtain timely care. Those without health insurance must queue.

### CONCLUSION

For persons born after 1934, the suggested reforms will do very little to encourage health insurance purchase by people who do not already have insurance due to the heavy surcharge they face: up to 70 per cent. Persons born before 1934 were largely unresponsive to the recent health insurance reforms. Given that past research has shown that it is those on middle and higher incomes who benefited and were encouraged to take up health insurance by the 30 per cent rebate, it is unlikely that an extra five per cent or 10 per cent rebate will encourage health insurance among those aged over 70 — especially those in advanced old age and on restricted incomes. There may be some small effect at the margin for persons with well above average retirement incomes.

Nonetheless, an additional five per cent rebate for persons aged 65-69 and 10 per cent for those aged 70 and over will increase the affordability of health insurance for those older persons who currently hold health insurance, in the short run. Whether savings of up to \$200 per annum as cited by the government will enable older persons to maintain their health insurance requires further analysis. Recent

cohort analysis shows that, between 1997 and 2002, male age cohorts born before 1927 are slowly dropping out of health insurance.<sup>32</sup> This effect, however, does not appear to occur for females. It is possible that the higher life expectancy of females, combined with bequest transfers from their husbands is a potential explanation for this finding. A further issue to consider is the long run effectiveness of such a subsidy. As suggested earlier, increases in the price of health insurance undermine the effectiveness of insurance subsidies in improving affordability and stabilizing insurance membership. Further, recent research suggests that insurance companies themselves are creating insurance products to separate young healthy low risk consumers from higher risk elderly consumers, who must pay a higher premium.<sup>33</sup> Clearly, this is against the concept of community rating and 'Lifetime Health Cover' more specifically and decreases the affordability of health insurance for all older persons.

The \$445.5 million dollars spent to fund the proposed subsidy offers no relief to those older persons who, due to the Lifetime Health Cover surcharge, cannot buy private health insurance. If the government's goal is to increase affordability of health insurance, they should first address the problem of older persons who are faced with high surcharges under Lifetime Health Cover. Although Lifetime Health Cover has been crucial in increasing the level of private health insurance, consideration needs to be given to those persons who, even with the 30 per cent rebate, could not afford to purchase it. With the added burden of the Lifetime Health Cover surcharge, health insurance is now unattainable for many. As such, older persons without health insurance are left to queue in the public sector for elective surgery. So long as the two per

cent Lifetime Health Cover surcharge exists, the Federal Governments suggested policy reform is far from being a 'safety net for older Australians'.

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- <sup>8</sup> Once insurance is purchased, persons are entitled to a 24 month period of absence. For each 365 days after the 24 month period, the person is subject to the two per cent surcharge.
- <sup>9</sup> 'Loading for late entry', Lifetime Health Cover Web Site: <http://www.health.gov.au/privatehealth/lhc/consumers/elements.htm> Date Accessed: 23/08/04.
- <sup>10</sup> Australian Consumers' Association 'Health insurance 2004—Compare a policy tool', <http://www.choice.com.au/> Accessed 23/08/04. The value, however, is largely insignificant in illustrating the effect of the proposed rebate and Lifetime Health Cover. The excess is an amount charged by the health insurance fund for claiming hospital benefits. By paying a higher premium, consumers can limit or reduce to zero the excess payable for a hospital stay.
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