

Meeting between Department of Health and APRA

16:00 to 17:30 – 25 July 2019
Level 12 - 1 Martin Place Sydney

Agenda for the meeting

- Role of APRA
- APRA's view of industry challenges & areas of focus
- Premium round

Discussion Points

1. Observations on the PHI industry
2. Pressures in the system – sustainability risks
3. APRA Capability review
4. Challenges on premiums

1) Department observations on the PHI industry

- Current reforms are insufficient to meet cost pressures and deliver affordable premium increases.
- Opportunities for additional reforms that have broad stakeholder consensus (insurers, private hospitals, doctors) limited.
- Service innovation in this market has traditionally been slow and overly reliant on government endorsement.
- There is significant diversity across funds in terms of engagement with the Department. Many large funds have an ongoing dialogue with the Department, but smaller funds seem far less inclined to engage with the Department. Further, the Department is aware of a general lack of sophistication for smaller insurers (lack of product diversity, 'simple' errors in their Rules, etc).

This document was released under the Freedom of Information Act 1982 by the Department of Health

2) Pressures in the system – sustainability risks

- In early June APRA released a letter to all private health insurers (PHIs) on sustainability risks, and expectations for PHIs to improve their resilience to deal with heightened sustainability challenges posed by declining affordability for policy holders and the impact of government policies to respond to pressures on the wider health system.
- The letter contains strong messages that APRA expects PHIs to be pro-active in taking actions to manage material industry risks.
- APRA signalled its concern about the resilience of PHIs to address sustainability risks in a public speech in February 2018. The letter increases the intensity messaging.
- APRA has assessed that actions by PHIs to-date are likely to be insufficient to build resilience to sustainability challenges in the long-term.
- APRA has no immediate concerns for the financial viability of any PHI, but the extent of these sustainability issues is likely to challenge business models for a number of insurers.
- The letter communicates that APRA will take a more assertive response via entity-specific supervisory action to protect policy holders where a PHI continues to take a passive approach to these risks.

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APRA'S SUPERVISION OF PHI AND RELATIONSHIP WITH THE DEPARTMENT OF HEALTH

The PHI industry has several features that create different challenges for APRA in carrying out its prudential supervisory role compared to its other regulated industries.

PHI is a part of Australia's health financing system. As such, the PHI industry is subject to a high degree of government regulation. Key external factors relevant to APRA's prudential mandate include:

- Government regulation of pricing and product features, including annual ministerial approval of premium increases, community rating and risk equalisation;
- Government incentives to encourage greater participation in PHI, particularly by younger people and those on higher incomes, including Lifetime Health Cover, the PHI rebate and the Medicare Levy Surcharge; and
- Government regulation or control over the price of some inputs, including the cost of medical prostheses.

These factors produce risks that are largely unique to the PHI industry. The affordability of PHI is declining as premium increases outpace wages growth in order to keep pace with rising healthcare costs and utilisation. This risks impacting participation rates at the same time as the average age of policyholders is increasing, placing further pressure on premiums and affordability.

Since taking over responsibility for prudential regulation of PHI in 2015, APRA has worked to substantially improve entity resilience in terms of capital, risk management and governance to address these viability risks. APRA has also focussed on recovery planning. The Panel agrees this is appropriate, noting the work on recovery planning faces similar capability issues as discussed in Chapter 3.

The extent of government regulation of PHI and policy influence over the PHI industry requires APRA to have an effective relationship with the DoH. APRA provides advice to the Department on the prudential sustainability of proposed premium changes. The direct link between premium changes and insurer viability means that APRA has an important role to play in this process. APRA should also have a sophisticated understanding of how PHI fits into the broader health system.

The Panel observes that APRA has a good working level relationship with the Department, with regular engagement on business as usual matters and an increasing appetite to engage on strategic issues. The relationship however is weak at more senior levels. For example, APRA does not have regular liaison meetings at senior levels with the Department, unlike its other key agency relationships. This is a risk for APRA in terms of its visibility of forthcoming political risks and its capability to work with the government to address urgent issues such as a failing entity. As part of its wider peer agency refresh, APRA should strengthen its engagement and relationship with the DoH at all levels of seniority.