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Both sides failing the test on health

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IT is disingenuous to claim, as the government does daily, that its private health insurance changes, which seem set to get parliamentary approval this week, are a savings. And it is even more disingenuous to claim they will increase efficiency in our health system. Rather, they will increase costs while entrenching a two-tier health system that penalises the poor.

But that isn't the worst of it. For what the debate about these changes highlights is that neither the government nor the opposition have a coherent strategy for dealing with the challenges our health system faces.

Start with the government's claims. Yes, substantial amounts are spent on the PHI rebate. And, yes, as PHI coverage rises with income much of this spending goes to high-income households. But Julia Gillard's assertion that this amounts to forcing "a young apprentice to subsidise the private health insurance of a wealthy businessman and his family" is nonsense. For what is actually involved is churn, in which higher income earners, who account for the vast bulk of income tax payments, get some of those payments back as benefits. Given that, it might seem better to eliminate the rebate and reduce tax rates, securing a double dividend: improved incentives and lower administrative costs. But matters are not so straightforward.

After all, public hospital services are provided without a direct user charge. And private hospital cover competes, to some extent, with public hospitals. Absent a matching subsidy, its price, as reflected in PHI premiums, would consequently be inefficiently high. Therefore, reducing the rebate could distort choice between private and public hospitals and increase healthcare costs overall.

But, despite what it says, the government is not really proposing to reduce the subsidy to PHI: it is merely changing its form. Specifically, while means-testing would decrease the on-budget benefit to high-income households, the proposed rise in the surcharge increases the benefit those same households get, in the form of avoided tax payments, by taking out private cover. The government, in other words, is replacing a spending carrot with a no smaller, and for many households larger, tax stick.

It is precisely because the implied tax slug is so large that the government is right and the opposition wrong: a fall in PHI coverage is unlikely.

But two points follow.

First, to call the change a savings makes little sense. It is no more a savings than would be replacing direct government funding of roads with a requirement that all households over a certain income give \$500 to a private road building fund or pay a \$1000 tax fine. Clearly, such a measure would increase, rather than reduce, the total volume of resources government extracted from taxpayers; only accounting tricks could make it seem otherwise. This is, in other words, a tax hike not a spending cut.

Second, and even more important, the change from the carrot to a bigger stick is by no means neutral. It raises effective marginal tax rates, with all the distortions that creates. And, even worse, it will make high-income consumers less responsive to the price of private health insurance. For once the new surcharge is in place, even were PHI premiums to rise, taking out PHI and getting its benefits would still be cheaper than paying additional taxes and getting nothing in return.

That reduced price responsiveness creates incentives for increases in PHI premiums, probably by some 10 to 15 per cent above the levels that would otherwise have prevailed. Those increases will, in the long run, mainly go as higher incomes to health professionals in the private system, as increases in charges in that system will meet less price resistance. This will have two further effects.

First, as the public and private systems compete for health professionals, it will increase costs and reduce quality in the public system. Second, it will make PHI even less affordable for low-income consumers, ensuring that we truly do end up with two healthcare systems: one for the better off, who will be forced to have private cover, and one for those with lower incomes, who will have to rely on the public hospitals.

This is a strange outcome for a Labor government to seek. Not only is it inefficient but, as growing numbers of taxpayers move into the category where PHI is effectively compulsory, electoral support for the public system will erode, reinforcing the healthcare divide. And with all middle and upper income families covered by PHI, future governments, as they try to control healthcare outlays, will surely tighten access by those with private insurance to the public system, making the divide all the deeper.

The government's changes, therefore, set us on the path to a health system that is costlier and less equitable. But that is not to endorse our current arrangements. For those arrangements are themselves unsustainable, inequitable and inefficient. And the flaws are compounded by the silos they create between healthcare and aged-care, and its inability to provide adequately for disability, dental cover and mental health.

What would a better system look like? It would provide comprehensive, rather than uneven, coverage of major health risks. It would be genuinely universal. And it would give all Australians, rich or poor, a choice of insurer.

To achieve these goals, it would subsidise premiums for those whose low incomes or inherent risk profile imply insurance payments they could not afford. But those with high incomes and who were tolerable risks would face the full price signal taking out insurance involves. That would create incentives to shop around. And, to make those incentives all the more effective, such a system would ensure transparency in insurance premiums, provide certainty about the charges to which consumers would be exposed and reduce the barriers consumers face to changing insurer.

These are hardly small changes from the current situation. That they involve myriad difficulties is obvious. But the Rudd government's National Health and Hospital Reform Commission was right to endorse them as a long-term direction we need to take.

That Labor has instead opted for a policy that lacks any overall coherence is not to its credit. But Labor's error cannot let the opposition off the hook. Its focus on defending the current system, rather than on elaborating a sensible alternative, is a wasted opportunity. For achieving sustainability, efficiency and equity in healthcare is perhaps the most complex challenge our nation faces. Let the opposition, in doing its duty of denouncing the manifest deficiencies in the government's proposals, show it is a challenge it can rise to.

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