Are the health funds' bubbles bursting?

By Graham Middleton, BA, MBA

"Ancillary members... sacrifice 22 cents in the dollar for the privilege of having 52% of their ancillary treatment paid for by the ancillary insurer..."

Health funds' business models are flimsy, with heavy churn rates of policies, complaints by the public and ancillary cover being widely questioned as offering poor value for money.

Dentists have become used to health funds interfering in clinical decision-making by changing rules and as at least one ADA branch puts it:

- Showing a lack of procedural fairness towards dental practitioners;
- Threats of de-recognition that would prevent a dentist's patients from receiving rebates from health funds;
- Intimidatory behaviour by funds in their practitioner audits; and
- Refusal to rebate GP dentists for supposed specialist procedures.

I have received many emails from dentists about these and other health fund related matters.

Boa constrictors

Health funds' tactics are akin to those of boa constrictors, which quietly slither up to unsuspecting animals and then, ever so gently, wrap their coils around them; gradually tightening their embrace. Eventually they kill their prey and swallow it.

The dental profession laid down with health funds in a cooperative manner many years ago, only to see whole geographic areas dominated by funds which became ever more aggressive in their manner towards dentists and their practices; ultimately claiming that policy-holders are their clients rather than dentists' patients, with the funds actively encouraging patients to switch from dentists which they could not persuade to become preferred providers, often implying that the patient's regular dentist was inferior, i.e. "is not on our preferred list".

Dental practice goodwill

Ultimately, if sufficient Australians sign up for ancillary health insurance cover, the funds will become more powerful, thereby eroding the goodwill value of dental practices. What would practices be worth if health fund action resulted in the majority of treatment being done in almost all practices under health fund rules?

Current ADA President speaks out

Recently ADA President Rick Olive has exhibited signs of going where his predecessors and the national CEO have previously been reluctant to venture, by attacking the funds for their paltry rebates and systematic skimming of ancillary premiums.

There is little doubt that there has been a significant conflict of interest among ADA office bearers concerning health funds over many years. Silence has descended following calls for declarations of conflicts of interest.

The two great issues facing Australian dentistry in the past 20 years have been:

1. The explosion of dental numbers through the huge increase in Australian dental school places and dentists being included in the category of migrants designated as filling skilled shortages in Australia; and
2. The substantial inroads of the private health insurers.

It now seems likely that dentistry is to be removed from the skilled immigration list, but four additional dental schools opened in recent years and enlarged classes in others, together with the surplus of dentists who have already migrated, will continue to flood the dental market with dentists surplus to need for years to come.

With respect to private health insurers, the issue of funds profiteering from ancillary tables at the expense of dentists and dentists' patients has been widely known for many years. It is good to see the current ADA President raising important issues concerning ancillary health insurance.

Funds exhibiting weakness

Between February 2012 and December 2014, it is reported that 1,576,409 health insurance policies were dumped and a further 985,211 downgraded, with the industry regulator reporting just 5.4 million policies with hospital cover at 31 December 2014. The proportion of the population having health insurance has remained steady, so it is apparent that the comparators have caused a huge churn rate, with more expensive policies being dumped in favour of policies in other funds with cheaper options.

Huge health insurance churn

It's also apparent that since 17 March 2015, when the above was reported in *The Australian*, there has been a lot more activity on behalf of comparators, including significant television advertising and letterboxing. It seems likely that with large premium increases applying from 1 April 2015 onwards, many more health insurance policyholders will have taken comparators' advice to transfer to cheaper policy cover and that this activity is continuing.

Also noted are the banding together of the mutual funds under a joint heading of "members' own" to combat:

- BUPA, which remits its profit to its UK parent; and
- ASX listed Medibank Private and nib, which have to satisfy shareholders as to profitability by paying sufficient dividends.

It is unlikely that BUPA, Medibank and nib can offer sufficient additional value to members compared to mutual funds to compensate members for funds' profits being directed to the UK parents in the case of BUPA or to shareholder dividends in the case of Medibank Private or nib, whereas mutual funds put all of their profits back into fund reserves to benefit members.

Medibank CEO sounds off

CEO George Savvides sounded off in *The Age* on March 20, complaining that state governments and their public hospital administrators were harvesting patients with private health insurance so they could bill their insurers for medical cover given in the public system.

Mr Savvides claimed that the rate of growth in members' claims coming from public hospitals had been 50% higher than the growth in claims for patients treated in private hospitals. He expressed concern that patients in public hospitals were not being properly informed about the potential consequences of using their insurance in that way. The article didn't explain what the potential consequences were.

Given the huge churn rate in health insurance policies being cancelled and replaced by cheaper alternatives or downgraded, it seems as though Mr Savvides may be preparing Medibank Private Ltd for a potential profit downgrade. Given that all of this would or should have been known to Mr Savvides before Medibank Private Ltd's recent float, it appears to be a variation of the old game of CEOs blaming their predecessors. It also displays a weakness in the health insurance fund business model.

> "There is a real danger that the health funds realising the weakness in their business models, as demonstrated by the comparators' churn rate, will become ever more tenacious in their tactics concerning dentists and dental patients... It is time for the ADA to become much more active in bringing health insurers to account..."

Elsewhere, Mr Savvides complained about the government's downgrading of the rebates paid to private health insurance during the term of the previous Labor government. This was certainly well known before the Medibank Private Inital Public Offering and further highlights the weakness of Medibank Private's business model.

Medibank Private received approval to lift its premiums by 6.59% against the health fund average fee premium hike of 6.18%. As these increases were well above the rate of inflation, it added impetus for members to check whether there were cheaper options within their own fund or whether they should switch to another fund.

It is clear that the health funds are suffering with respect to health insurance cover. It has long been known that they sought to partially paper over this weakness by persuading the public to take ancillary (general) insurance cover and rationing the benefits offered under ancillary policies.

They were able to manipulate benefits in order that they could provide a guaranteed profit in the ancillary cover business which, in the case of mutual funds, was then held in fund reserves to subsidise hospital cover insurance, which at times came dangerously close to a loss-making situation. However, this approach showed scant respect for ancillary benefits members, particularly those who had ancillary benefits but not hospital cover.

The 22% skim

Recently the ADA president has publicly identified the skim as representing 22% of ancillary cover, again raising the serious question of "why do members choose to belong to ancillary benefits tables?"

This in turn reveals a serious weakness in health funds' business models. Since health fund administrative costs are 8.5% on average, ancillary benefit contributions are getting back on average 78% in claim rebates, paying 8.5 cents in the dollar administratively for the privilege of having their money recycled and contributing 13.5 cents per dollar to somebody else's pocket; it sounds like a great deal to avoid.

High income earners don't need ancillary cover to escape the tax surcharge, requiring only hospital insurance. Furthermore, the hospital cover could be one with the lowest cost options.

Choice says 'drop it'

Consumer group Choice's spokesman, Tom Godfrey, has indicated that people would be better off keeping the premiums in their bank accounts and paying their own ancillary health bills. He advised that if you are struggling with the April 1 health fund price hike, you should consider dropping your extras (ancillary) cover.

PHIAC chief says extras cover is "irrational"

In a candid assessment, Private Health Insurance Administration Council (PHIAC) Chief Executive Shaun Gath was quoted in *The Advertiser* (30/3/2015) saying that extras cover was an irrational purchase and "probably doesn't make sense". However, funds "spend a lot of money advertising it".

96% vs 52%

The relatively recent Medibank Private prospectus indicated at figure 2.8 on page 16 that whereas 96% of hospital fees were covered (by hospital cover) only 52% of extras were paid by health insurers; meaning that 48% of extras are paid for by patients out of their own pocket. This again begs the question as to why have ancillary health insurance at all, when the rebates are on average paltry, 22% of members' contributions are skimmed off the top and even the PHIAC CEO says it's an irrational purchase?

Looked at critically, the Australian health insurance industry faces hospital costs which rise a lot faster than inflation, as an ageing population draws heavily on medical skills to provide procedures which weren't available to previous generations. This rising cost leads to premium rises above the rate of inflation, which in turn is fuelling the activities of comparator businesses, which are churning policies to cheaper alternatives and earning themselves substantial commissions in the process.

Desperate advertising

The funds advertising for ancillary members indicate that they are desperately trying to make up for the weakness in their hospital cover arrangements by attracting new ancillary members, who will sacrifice 22 cents in the dollar for the privilege of having 52% of their ancillary treatment paid for by the ancillary insurer. It all adds up to a very shaky business model.

Complaints about private health insurance rise

The Private Health Insurance Ombudsman's annual report shows a big increase in complaints about exclusions and restrictions in the 2014 financial year compared to the prior year. Overall, the ombudsman received 3,427 complaints in 2013/14, a 16% increase.

Complaints about the oral advice funds provided to their members were up 40%, while high level complaints requiring intervention by the ombudsman were up 28%. BUPA attracted 1,040 complaints, 400 more than Medibank Private.

The danger for dentists and patients

There is a real danger that the health funds realising the weakness in their business models, as demonstrated by the comparators' churn rate, will become ever more tenacious in their tactics concerning dentists and dental patients.

It is time for the ADA to become much more active in bringing health insurers to account. While it is welcome, we can predict that the recent complaint to the ACCC by the ADA will be met with determined resistance and obfuscation by the health insurers. They may try and knock it out by arguing that it's not correctly framed under the relevant legislation; or use legal tactics which will delay and obfuscate the issue. The ADA will have to become resolute enough to press the issue continuously over a period of time.

It is desirable that the ADA not rely on its own data but have the PHIAC data examined forensically by one of the large accounting groups in order that its utterances carry as much weight as possible.

Typical of dentists' comments is one received from a dentist of 30 years, who says:

"My experience is that my practice base has been stealthily eroded in recent years by the hijacking of health funds with ADA's tacit support."

While the ADA stance may be changing, it is yet to be proven that it can do this on a sustained basis. Certainly over many years, it has been seen by its membership to have been insufficiently active on the members' behalf in this area or in relation to health funds changing rules.

Received from an oral and maxillofacial surgeon:

"I'm not sure whether you are aware that two major private health funds are now refusing to cover hospital admissions for patients with top benefit cover if they are having dental implants without any other treatment (such as tooth extraction or bone grafts). This is on the grounds that dental implant treatment, even for someone with no teeth at all and having 8-10 implants placed in a lengthy surgical procedure, is cosmetic!"

That comment would have related to hospital cover tables, but there are also many observations of dentists indicating

that health funds change the rules with respect to the classifications of the treatments that they will rebate.

It does seem that Jane and Joe Public pay their premiums only to find out at a later date that what they thought they were covered for is not the case.

Conclusion

All of the above indicates that while the health funds are likely to be even more tenacious with respect to the way that they interact with dentists and dental patients, their own business models have substantial weakness.

About the author

Graham Middleton personally has been advising dentists on strategic, practice management, valuation and conflict resolution processes for 27 years, the last 20 as a founding partner and director of Synstrat Management Pty Ltd and Synstrat Accounting Pty Ltd. He was once a regular army officer, and later Director Human Resources Manager, Attorney General's Department of Victoria. He is considered an expert on dental practice valuation and practice performance benchmarking. He has spent many years advising dentists in respect of their business and financial strategy and measuring their practice and financial performance. He is the author of Synstrat Dental Stories, the Synstrat Guide to Practice Management, 50 Rules for Success as a Dentist and Buying & Selling General & Specialist Dental Practices. He is a long-term contributor to the Australasian Dental Practice magazine. The Synstrat Group is an independent data-based organisation providing management, benchmarking, valuation, financial and accounting services to the dental profession. Synstrat Management Pty Ltd is a Licensed financial services company. Both Synstrat companies are owned by the same directors who work within the Synstrat Group. For more info, call (03) 9843-7777, Fax: (03) 9843-7799, email dental@synstrat.com.au or see www.synstrat.com.au.

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