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Significant cost savings by abolishing private health insurance rebates

New research from the University of Melbourne shows that abolishing the 30 percent rebate on private health insurance could potentially yield significant cost savings to the Australian Federal Government.

A recent Melbourne Institute working paper by Dr Terence Cheng investigates the effects of removing subsidies for private health insurance on public sector expenditure for hospital care. The paper predicts that shifting patients from private to public hospitals would cost an extra \$1.38 billion per year. This figure is a fraction of the \$3 billion the government spent on subsidising private health insurance in 2004-05.

Dr Cheng says these findings indicate that the cost of the subsidy program is considerably higher than the cost of the expected increase in hospital use. "These results suggest that eliminating private health insurance subsidies could potentially yield substantial public sector savings," he said.

The findings are based on a simulation analysis that applies microeconomic models to survey data from the Household, Income and Labour Dynamics in Australia study. It considers how removing the rebates would influence the decision on whether to purchase private health insurance. It also predicts changes in insurance status and the effect on the use of hospital care by patients.

Dr Cheng says that the analysis shows that abolishing the private health insurance rebate is likely to result in a reduction of the number of people with private health insurance coverage.

"Our predictions suggest that coverage among the population aged 25 years and over would fall by 6 per cent, from 50 percent to about 44 percent. This would result in an 11.1 percent and 7.8 percent drop in the number of private admissions for day and overnight hospital care respectively," says Dr Cheng.

According to Dr Cheng the findings have important ramifications for the federal government's attempt introduce means-testing for private health insurance rebates.

"Research suggests that the introduction of means-testing of private health insurance rebates will result in only a small number of individuals dropping cover. This is because the Medicare Levy Surcharge provides a strong incentive for high income individuals to buy private health insurance and avoid paying more in taxes."

"There is evidence internationally of persistent behaviour in the decision to purchase health insurance in that people who are already insured are likely to choose to remain insured," says Dr Cheng.

Working Paper 26/11 can be downloaded from the Melbourne Institute website at:

www.melbourneinstitute.com/miaesr/publications/default.html

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