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Tax Laws Amendment (Medicare Levy Surcharge Thresholds) Bill 2008

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Portfolio: Treasury

Commencement: On Royal Assent

Links: The relevant links to the Bill, Explanatory Memorandum and second reading speech can be accessed via BillsNet, which is at http://www.aph.gov.au/bills/. When Bills have been passed they can be found at ComLaw, which is at http://www.comlaw.gov.au/.

Purpose

The purpose of the Bill is to increase the Medicare levy surcharge thresholds on annual taxable income from $50 000 to $100 000 for individuals, and from $100 000 to $150 000 for families and couples. The Bill proposes amendments to the *A New Tax System (Medicare Levy Surcharge—Fringe Benefits) Act 1999* and the *Medicare Levy Act 1986* (MLA 1986).

Background

An outline of the Medicare levy and surcharge

When Medicare was introduced in 1984 the scheme was part-funded by the imposition of a Medicare levy, originally set at 1 per cent of taxable income, with a low income cut-off threshold below which no levy was payable. In 1995 the Medicare levy was increased to its current level of 1.5 per cent of taxable income.

The Medicare levy surcharge (MLS) is an additional one per cent surcharge on taxable income imposed on 'high-income' earners who do not have private hospital insurance, currently set at $50 000 for individuals and $100 000 for couples and families. The MLS was introduced by the former Howard government in 1996 as part of a package of reforms to address declining private health insurance membership.[1] The Medicare levy thresholds,

1. In an attempt to stabilise the level of coverage of private health insurance in Australia, the Howard government announced in the 1996 Budget a two-pronged strategy which offered means-tested subsidies for people with private health insurance and a penalty through the Medicare levy for higher income earners without private health insurance. The incentives

below which no Medicare levy is payable, are regularly adjusted to take account of increases in the Consumer Price Index (CPI). Changes to the current threshold amounts are proposed in a separate bill, the *Tax Laws Amendment (Medicare Levy and Medicare Levy Surcharge) Bill 2008*. However, the MLS threshold amounts have remained unchanged since they were first applied in 1997. This Bill proposes increases to the MLS thresholds from $50 000 to $100 000 for individuals, and from $100 000 to $150 000 for families and couples. There is no proposal to regularly adjust the thresholds in future years to take account of CPI.

As well as amendments to the MLA 1986, the Bill proposes similar amendments to reportable fringe benefits provisions in the *A New Tax System (Medicare Levy Surcharge—Fringe Benefits) Act 1999.* This is to ensure that individuals will not swap their cash salary for fringe benefits and avoid or reduce their liability for the MLS. The amendments will apply to the 2008–09 year of income and subsequent years.

The Medicare levy and surcharge only partially fund the total cost of Medicare. In 2006–07 the levy and surcharge raised around $7.2 billion in revenue, while the cost of Medicare for the same period was $17.2 billion.[2]

Basis of policy commitment

This measure was officially announced in the 2008–09 Budget.[3]

Committee consideration

The Bill passed the House of Representatives on the 29 May 2008. At the time of writing it has not been referred to a committee.

Position of significant interest groups/press commentary

The proposed changes to the MLS have generated considerable attention and debate. The Assistant Treasurer, the Hon. Chris Bowen, maintains that the proposed increases in the MLS thresholds 'will help reduce financial pressure on many working families' and casts

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and levy were contained in the *Private Health Insurance Incentives Bill* and the *Medicare Levy Amendment Bill (No. 2) 1996* introduced in December 1996. Subsequently the means-tested incentives were replaced with the 30 per cent private health insurance rebate in 1999.

2 Hon. P. Costello, *Final Budget Outcome 2006-07*, p. 3 and p. 88.

3. See the Hon. Wayne, (Treasurer), *Increasing the Medicare Levy Thresholds*, media release, Parliament House, Canberra, 13 May 2008. The measure was first announced by the Treasurer the Hon. Wayne Swan on the 10 May 2008, 'Doorstop Parliament House, Canberra', Transcript, 10 May 2008.

the measure as providing consumers with 'real choice'.[4] However, opponents of the measures argue the proposed changes will lead to declines in private health insurance membership, financial pressure on private health insurance premiums and strain the public hospital sector.

Some have argued—notably the Federal Opposition Health spokesman, the Hon. Joe Hockey, the Australian Health Insurance Association (AHIA) and the Australian Medical Association (AMA)—that the proposed increases to MLS will lead to a mass exodus of members from private health insurance and place a greater strain on the public hospital sector, particularly on public hospital waiting lists.[5] They argue that holders of private health insurance will abandon their private health insurance cover and instead rely on public hospitals to meet their health needs, thus adding significant strain to the already overstretched public sector.

In support of these arguments the AHIA and the AMA both point to separately commissioned research which, they claim, casts doubt on Treasury advice that 485 000 people would drop their private health insurance, and result in a net saving to government of $299 million.[6] The AHIA claims that their research shows that around 613 000 people would need to drop their insurance in order to meet the forecast savings, meaning that some 900 000 Australians would then become solely reliant on the public system.[7]

Separately, the AMA points to research it commissioned from Access Economics. While not forecasting numbers who will drop their cover—on the basis that knowledge of the price elasticity of demand for private health insurance was insufficient—the research

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4. Hon. Chris Bowen, 'Second reading speech: Tax Laws Amendment (Medicare Levy Surcharge Thresholds) Bill 2008', House of Representatives, *Debates*, 27 May 2008, p. 46.
5. Australian Medical Association (AMA), '*Budget private health changes will hurt'*, media release, AMA, Barton, ACT, 14 May 2008, http://www.ama.com.au/web.nsf/doc/WEEN-7EM4EC, accessed on 19 May 2008; Australian Health Insurance Association (AHIA), '*Hundreds of thousands to join public hospital waiting lists'*, media release, AHIA, Deakin, ACT, 10 May 2008; Danielle Cronin, '*Medicare changes could push up private health fees*', Canberra Times, 13 May 2008, p. 6.
6. Hon. Wayne Swan (Treasurer), 'Address to the National Press Club', media release, Canberra, Parliament House, Canberra, 14 May 2008; see also Budget estimates on savings contained in Australian Government, 'Part 1: Revenue Measures' *Budget Paper no. 2: Budget Measures 2008-09*, Commonwealth of Australia, Canberra, p. 33.
7. Australian Health Insurance Association, '*Treasury figures show an additional 900,000 Australians will rely on the public hospital sector'*, media release, 17 May 2008; the research was undertaken by Price Waterhouse Coopers.

questions the forecast savings from the measure, which is described as 'highly implausible'.[8]

However, claims of a mass exodus from private health insurance and the negative consequences for the public hospital system have been questioned by others, including by some in the private sector.

The Australian Private Hospitals Association (APHA) is not convinced that the changes will lead to an exodus of members. It argues that the high quality and value that private health insurance offers 'outweighs' any small financial benefits to be gained from member dropping their private cover, and still sees private health insurance membership 'growing strongly' in the next few years.[9] Some in the private sector point to the importance of other factors driving private health insurance membership, such as rising incomes and disillusionment with the public hospital sector.[10]

In an indication that longer-term damage to private health insurance is not envisaged by all in the sector, the proposed acquisition by health insurer BUPA Australia of its competitor MBF remains on-track, despite the announced changes to the MLS.

Others outside the private health sector have argued that other measures—notably Lifetime Health Cover and the 30 per cent private health insurance rebate—play a greater role in the decision to purchase private health insurance than does the MLS. They point to the continuation in the decline in private health insurance membership after the introduction of the MLS in 1997, with this only being arrested when these other measures were introduced in subsequent years.[11]

It is further argued by some proponents of the MLS changes that those who purchase private health insurance in order to avoid the 'penalty' of the MLS tend to be young and healthy and purchase the cheapest product available, often with high co-payments. These members tend to have low rates of hospital use, and in any case rely on the public system in order to avoid the high co-payments that they would be subject to if they used their private health insurance. In any case the higher premiums faced after the age of 31 also act as a disincentive for young people considering abandoning their cover. Therefore, it is

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8. Access Economics, '*Health and the 2009-09 Federal Budget: Report by Access Economics Pty Limited for the Australian Medical Association*', May 2008.

9. Australian Private Hospitals Association, '*Don't risk waiting list lottery—private hospitals urge*', media release, 11 May 2008.

10. NIB Chief Executive, Mark Fitzgibbon, as reported in J. Breusch, 'Industry mulls Labor surcharge shake-up', *Australian Financial Review*, 22 November 2007, p. 17.

11. L. Russell, 'Unclear bill of health in extra sticks and carrots', *Canberra Times*, 13 May 2008, p. 13.

argued, their opting out of private health insurance will have minimal impact on public hospital utilisation rates, and pubic hospital waiting lists.[12]

Opponents of the changes also argue that the proposed changes will lead to higher private health insurance premiums.[13] It is argued that as young healthy members drop their private health insurance this will lead to pressure on health insurance premiums, as health insurers seek to offset the impact of the loss of this revenue stream. In particular, those health insurers that target younger healthy members—that is, those who are likely to drop their membership—are likely to face the greatest financial pressures. Health insurer NIB (the only publicly listed health insurer), has specifically targeted younger members, but has already seen the impact of the proposed increases to the MLS thresholds, with its share price dropping significantly following the announcement.[14] This loss of younger members it is argued, may lead to a 'snowballing effect' as higher insurance premiums turn people against private health insurance which then leads to more premium rises to offset these losses, creating premium inflation.[15]

While the impact of reforms to the private health insurance sector introduced by the former Howard government in 2007 are yet to be fully gauged, these were designed to improve the attractiveness of private health insurance by enabling health insurers to offer more flexible and innovative products, such as Broader Health Cover.[16] These reforms are intended to enable insurers to respond effectively to the broader challenges they are likely to face in coming years, including an ageing population, increases in chronic disease prevalence and expensive new technologies. Some insurers have responded with new products, but there has been criticism that in areas such as palliative care, there is little product choice.[17] It remains to be seen whether any loss of members due to changes to the MLS, will prompt health insurers to offer a wider range of innovative products in order to maintain their attractiveness to consumers.

Although a stated intent of the proposed increases to raise the MLS thresholds is to bring them into line with those income thresholds that applied in 1997[18], there is no proposal to

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12. Ian McAuley, 'Higher thresholds for the Medicare surcharge—a welcome reform', *Crikey*, 14 May 2008.
13. Access Economics, op cit.
14. John Breusch, 'Funds' figures do the talking', *Australian Financial Review*, 29 May 2008, p. 7.
15. Access Economics, op cit.
16. For more detail of these reforms see Amanda Biggs and Luke Buckmaster, 'Private Health Insurance Bill 2006: Bills Digest', Parliamentary Library Bills Digest No. 81 2006-07.
17. Clare Pirani, 'Insurance yet to meet the demand for palliative care', *The Australian*, 8 september 2007, p. 28.
18. Hon. Chris Bowen, op. cit.

regularly adjust the MLS thresholds in line with increases in the CPI in future years, as is done with the Medicare levy thresholds.

Financial implications

The revenue implications over the forward estimates are provided in the Explanatory Memorandum. The government is expected to forego income tax revenue of $660 million over the forward estimates, due to the increased income tax thresholds that are proposed for the MLS. The Budget also forecasts a decrease in expenditure of some $959.7 million, from a reduction in the 30 per cent private health insurance rebate, due to an expected decline in private health insurance membership over the period.[19] Overall the government forecasts a net saving of some $299 million from this measure.

As noted previously, these estimates over the forecast period 2009–2012, have been questioned by the AHIA and the AMA.

Main provisions

Schedule 1—Singles and families income thresholds

Items 1 and **2** proposes to amend the reportable fringe benefits threshold provisions contained in subsections 6(1) and 6(2) of the *A new Tax System (Medicare Levy Surcharge—Fringe Benefits) Act 1999*, so that the family income threshold amount is increased from $100 000 to $150 000, and for each dependent child the income threshold increases by $1 500.

Item 3 proposes to amend the reportable fringe benefits threshold provisions contained in paragraph 12(1)(a) of the *A new Tax System (Medicare Levy Surcharge—Fringe Benefits) Act 1999*, so that for individuals the income threshold amount is increased from $50 000 to $100 000.

Item 4 proposes to repeal the meaning of 'family surcharge threshold' contained in section 3A of the *Medicare Levy Act 1986*, and replaces it with a new section with the family surcharge threshold amount for a year of income increased from $100 000 to $150 000.

Item 5 proposes to amend subsection 8(B)(2) of the *Medicare Levy Act 1986*, so that for unmarried individuals without dependents the Medicare levy surcharge threshold is increased from $50 000 to $100 000.

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19. Australian Government, 'Part 1: Revenue Measures' *Budget Paper no. 2: Budget Measures 2008-09*, Commonwealth of Australia, Canberra, p. 33.

Item 6 proposes to amend subsection 8E(2) of the *Medicare Levy Act 1986*, so that for individuals who are beneficiaries of trust income the threshold is increased from $50 000 to $100 000.

Item 7 specifies that these amendments would apply to income tax assessments for the 2008–09 financial year and later years of income.

Concluding comments

The Bill proposes amendments to increase the income threshold amounts above which taxpayers without appropriate private health insurance are liable to pay the Medicare levy surcharge. These thresholds have remained unchanged since 1997. The proposed income threshold amount for individuals is $100 000, and for families and couples it is $150 000.

The proposed changes have been contentious because of concerns that this will lead to an exodus of members from private health insurance, because those taxpayers on incomes below these thresholds will no longer be liable for the surcharge. Critics are concerned that such an exodus of membership will have negative consequences for health insurance funds, increase pressure on premium rises and adversely impact on the public hospital sector. However, others argue that the changes are unlikely to lead to these outcomes.

The government argues that the changes to the thresholds will ease cost of living pressures on families on modest incomes.

Members, Senators and Parliamentary staff can obtain further information from the Parliamentary Library on (02) 6277 2514.