The Health Insurance Authority
Workshop on Risk Equalisation

Private & Confidential for HIA members
Discussion paper only

2nd May 2002
## Agenda

<table>
<thead>
<tr>
<th>Agenda Item</th>
<th>Time</th>
</tr>
</thead>
<tbody>
<tr>
<td>Introduction and objectives</td>
<td>2.00</td>
</tr>
<tr>
<td>Reminder of responses received</td>
<td>2.05</td>
</tr>
<tr>
<td>Case study - risk equalisation in New York State</td>
<td>2.50</td>
</tr>
<tr>
<td>Presentation of “interventionist” criteria</td>
<td>3.20</td>
</tr>
<tr>
<td>Presentation of “non-interventionist” criteria</td>
<td>3.40</td>
</tr>
<tr>
<td>Perspective of a potential new entrant</td>
<td>4.00</td>
</tr>
<tr>
<td>Break</td>
<td>4.10</td>
</tr>
<tr>
<td>Presentation of outline draft implementation criteria</td>
<td>4.20</td>
</tr>
<tr>
<td>Authority discussion leading to agreed outline criteria</td>
<td>4.50</td>
</tr>
</tbody>
</table>
Reminder of responses received
Responses Received

- Advisory group (former members)
- BUPA
- Competition Authority
- Health Boards and ERHA CEO’s group
- IMO
- Ray Kinsella, UCD
- Royal & Sun Alliance restricted membership undertaking
- Society of Actuaries
- Vhi
- Vhi members advisory council
Advisory Group (former members) Response

- Unfunded liability emphasises the need for stability
- The greatest threat to stability is medical inflation
- Medical inflation is best dealt with by increasing competition
- However, effective competition cannot exist in a market with community rating without RE, because
  - The new competitor will either make windfall profits by setting their price just below that of the incumbent or cause instability by setting a very low price; and
  - The incumbent will not be in a position to compete on price
- A predatory spiral can cause serious instability very quickly
- If risk profiles differ significantly RE should be introduced
- RE should be based on age and gender only
BUPA Response

**Competition**
- In discussions with DoHC, DG Competition and DG Market about State Aid and other issues
- Competition issues are paramount to discussion regarding RE
- Competition is good for the consumer
- Competition makes the market more stable
- Stability is brought about by efficient practices and good management
- RE encourages claims, hospitalisation and payments to consultants

**Community Rating**
- Community rating is protected by legislation and does not need RE
- Community rating should not be an objective in itself but a public policy instrument to shape the market
- True community rating does not exist. This is price as a % of salary or fixed entry level price
- Pre-existing conditions, waiting periods, group discounts etc. impede community rating
- Subsidy from low cover plans to high cover plans
- Inability to differentiate by price will cause prices to rise
## BUPA- Circumstances Where RE Is Not Needed

<table>
<thead>
<tr>
<th>Windfall profits</th>
<th>Insurer going out of business</th>
</tr>
</thead>
<tbody>
<tr>
<td>• If a company is making windfall profits, competitors must go after those profits - it’s a sign to compete</td>
<td>• Sustained losses by one insurer is a sign of instability but may mean the insurer has to change</td>
</tr>
<tr>
<td>• Others cannot sit back and accept the situation - must change their products/prices to win this business</td>
<td>• DETE has experience of when to intervene (e.g. PMPA, ICI)</td>
</tr>
<tr>
<td>• An insurer cannot “allow itself” be left with a high risk profile</td>
<td>• HIA must investigate reasons why losses are arising</td>
</tr>
<tr>
<td>• Cannot restrict profit margins of companies, not competition if everyone is making the same profit margin</td>
<td>• Consumers could benefit from an inefficient insurer going out of business</td>
</tr>
<tr>
<td>• BUPA is not making windfall profits and RE would make BUPA’s business unviable</td>
<td>• Thresholds cannot be used - no insurer on brink of collapse in 1998</td>
</tr>
<tr>
<td></td>
<td>• There are examples of companies adapting to changing situations</td>
</tr>
</tbody>
</table>

© 2002 Andersen. All rights reserved.
BUPA- Circumstances Where RE Is Not Needed

Predatory pricing
- Could only be a temporary strategy
- Current prices cannot be significantly undercut/not a reality
- Existing insurers must find ways to respond
- People will not necessarily opt for cheapest price
- Inertia means people would be slow to move
- Renewals mean business doesn’t transfer quickly
- Might not adversely affect consumers

Large movement of older people to one insurer
- Must reassess the business plan
- Reassess control on cancer treatments, heart treatments etc.
- Redesign plans
- Design new plans
- Vhi membership has aged but profitability has increased
- “not a pricing problem, just a lot of work”

Responses received
BUPA- Circumstances Where RE May Be Needed

• “…Risk equalisation has no role to play in Ireland in protecting consumer interests.”

• Proposed measures of market stability
  – When consumers stop buying insurance due to market features
  – When old age policyholders exit the market in significant numbers
  – When an insurer is threatened with financial collapse

• Does instability threaten the interests of consumers?

• Intervention should be as a last resort, implemented only in exceptional circumstances and where other interventions will not work

• HIA should publish basis of recommendations but no aggregate data unless sufficient number of competitors

  “Better management normally solves the issue”
Competition Authority Response

- “Given the overriding importance attached to…community rating, some system of risk equalisation is likely to be necessary.”
- Clarified that they believe a reserve power is absolutely necessary and implementation at some stage is likely to be necessary
- A range of issues makes the health insurance market unattractive to new entrants
- Recommend removal of threshold 2
- Competition is the best protector of consumer interests
- “Any risk equalisation scheme should be as supportive of competition as can be practically achieved”
Health Boards and ERHA CEO’s Group

- Data supplied to HIA must be accurate, timely and independently verified
- RE scheme should take account of
  - Rural/urban mix
  - Level of community care and other services
  - Level of health insurance cover
  - Accuracy of data
  - Impact of Treatment Purchase Fund
  - Impact of readmission rates
  - Smaller hospitals
  - Rates of payment for paybeds
  - Risk of patients being diverted to other hospitals
Irish Medical Organisation

- Very supportive of community rating
- Preferred risk selection may lead to “a spiraling of costs with a rapid deterioration in the financial position of those insurers with poorer risk profiles”
- Without RE, open enrolment is unenforceable
- RE should be at statutory minimum levels rather than level of plan most subscribed to
- RE “must not penalise efficiency and compensate inefficient operators”
“It is difficult to see any circumstances in which risk equalisation should be implemented………”

“In all instances in which the arguments for implementing risk equalisation have been advanced….there are less damaging, more proportionate and more easily enforceable alternatives.”

RE would be damaging to competition and market development

Other forms of intervention can ensure market stability “specifically Conduct of Business arrangements”

“…..a decision by the Authority on whether to implement risk equalisation would have to be informed by the likely response of the Commission.”

The argument that a new insurer will attract younger members assumes the incumbent is unable or unwilling to respond
• Consumer interests are best captured by considering impact on insurers
• RE would “almost certainly have a profoundly negative effect on the consumer”
• The possibility of RE prevents new competition entering
• Use of a “minimum four player” indicator would reduce uncertainty and encourage market entry
Royal & Sun Alliance RMU

• The Royal & Sun Alliance plan would be unviable with RE due to administration and cost burden
• Not necessary because do not compete in the health insurance market
• Suggest option of permanent exclusion
• DoHC proposed that permanent exclusion would remove right to open enrolment
• Suggest this as unfair, must receive all members under open enrolment
• Deterrent to younger people joining the scheme - adverse effect on finances
Now is an opportunity to remove community rating above minimum level
– hard to justify on general good grounds
– would reduce unfunded liability
– do now whilst most members have low cover

Instability can come from
– the market failing to secure young new members (RE cannot help)
– or failure of an insurer to attract sufficient good risks (unlikely)
– therefore, “can be argued that the stability argument alone would not justify risk equalisation”

Market incentive is to be a price follower - do not want to attract other insurer’s high risk lives

Important for overall market stability that insurers have an incentive to attract new low risk members
Society of Actuaries

- Recommend age and gender only system
  - no sharing of achievements in reduced length of stay, reduced costs, reduced incidence of claims
  - difficult to obtain information on health status
  - need a remaining incentive to attract low risk members

- Recommend prospective system
  - HIA publishes age and gender rates for minimum benefits
  - HIA publishes community rate for minimum benefits
  - Transfer is difference between these rates for each member

- Many barriers to entry in the Irish market
  - size of market
  - investment required relative to size of market
  - dominant position of Vhi, its ownership, regulatory position and lack of commercial mandate
  - uncertainty regarding RE
“We believe that the longer term interests of the consumer and of the market would be served by the introduction of a limited form of risk equalisation now, both in terms of the intrinsic market effects and by establishing certainty on the issue”

- Reasons
  - “Either risk equalisation is a concomitant of community rating etc. or it is not….Why there should be linkages to ex post market outcomes is not clear” - conclude that it is a concomitant
  - RE would not cause market instability
  - RE would not inhibit competition
  - Uncertainty should be eliminated

- Recommend introduction of unfunded lifetime community rating
- Recommend removal of Vhi from Dept of Health, a commercial mandate and reserves compliant with DET&E standards
Vhi Response

Windfall profits

• Vhi’s average claim is c. 3.5 times BUPA’s - most meaningful criterion to use. Vhi does not favour thresholds.

• BUPA windfall profits have taken €60m from the system giving a 3% price increase

• BUPA’s underwriting profit margin is more than 50%

• Adamant that RE transfers to Vhi would lower prices. Government controlled pricing reinforces this. Profit margin unchanged. Will always price to maximise volume.

• Community rating is the distortion, not RE
Community Rating

- The low risk community has become separated from the high risk community - subsidisation removed ("communities rating")
- Open enrolment is not sufficient protection for the high risk community
- Community rating should not provide a reason to transfer insurers
- Few new benefits have arisen for the high risk community

Insurer going out of business

- Vhi’s business is not sustainable without RE
- Need for RE has been masked by economic boom
- Dramatic slowdown in young new members will cause rapid deterioration in Vhi finances
- "cash in cash out" business increases speed of deterioration
- Stability is insurers not being in financial difficulty and prices increasing at a reasonable rate
Vhi Response

Competition

- BUPA has not attracted new people to the market - feature of economic boom
- More competition has not entered because buying Vhi is easier than greenfield
- Community rating without RE favours one competitor over another
- Absence of RE has caused BUPA to overpay providers. They can make uneconomic deals to gain a marketing advantage because they do not incur claims.
- Consumer’s interest is served by “delivery of equity between all consumers regardless of where they purchase their private health insurance”
- BUPA has been able to make benefit improvements due to windfall profits. Lines between high cover plans and low cover plans have become blurred. Plan B is more expensive than it should be due to benefit improvements.
- Cherry picking will happen because the regulatory system encourages it
- Believe in facilitating real competition, not preferred risk selection!
Vhi Response

- Preference is for utilisation to be used but do not believe there are significant differences within age bands - could do age and gender only subject to review
- Favour publication of industry information for the benefit of consumers
Vhi Members’ Advisory Council

- Additional premium burden of 3% is unacceptable
- 85% of the insured population is paying more than they should
- This group is mostly older and has been contributing to health insurance for longer
- RE is necessary to sustain community rating - its absence causes “major inequity”.
- RE is necessary to ensure new insurers are discouraged from cherry picking
- Lack of certainty over RE has contributed to lack of entry of new insurers to the market - a barrier to entry
- Implementation of the scheme will result increase confidence from insurers and further entrants
Summary of Positions

Non-interventionist

- Ray Kinsella
- BUPA

Interventionist

- Competition Authority
- Vhi
- Advisory Group (former members)
- Society of Actuaries in Ireland
Healthcare Market - Prior to NYHCRA

- Empire BCBS was the dominant healthcare payor in NYS
- Several upstate regional BCBS plans
- Empire controlled 90% of the hospital based business
- Hospital reimbursements based on per diem rates derived from empire experience
- Empire paid hospitals the per diems less a “discount” to compensate empire for being the “carrier of last resort”
- Empire’s book of business was composed of
  - Large employer group experience-rated business
  - Mid-size employer group community-rated business
  - Small employer group community-rated business
  - Individual “direct payment community-rated business
Healthcare Market - Prior to NYHCRA (Cont.)

• Other carriers, primarily large mutual life insurers like met life and prudential offered “wrap around” medical coverage
• Healthcare market was stable in product and cost variations
• Empire’s book was self-sufficient based on reasonable level of premium
• No competitive pressures
• No legislative issues to “stir” the mix
Healthcare Market - Competitive Changes

- Medical costs began to escalate with double digit medical trends
- Empire premium rates began to increase to keep pace
- Legislative pressures to keep rate increases under control
- Empire’s margins began to come down
- Competitors began to offer “comprehensive” plans including hospital coverage
- Empire’s hospital discount began to lose its competitive advantage
- Competitors began to “cherry pick” the better employer group risks using selective marketing in a community-rated market
Healthcare Market - Competitive Changes

- Empire’s pool began to worsen, especially the mid-size pool
- Empire’s ability to “underwrite” the large employer groups, primarily the “national” groups began to be lost
- Empire’s small group and individual “risk” pools began to reach “unmanageable” levels
- Empire’s community premium rates began to increase causing regulatory and public pressures
- Uninsured population began to increase causing additional legislative pressures
- Empire’s financials began to exhaust their surplus reserves
- Empire was placed on “warning” status by the BCBS assoc.
- For-profit HMOs entered the market
Healthcare Market - NYHCRA Implementation

• New York Healthcare Reform Act of 1993
  – Direct pay market changes
  – Demographic pooling mechanism
  – Specific medical condition pool
  – Hospital deregulation (even playing field)
  – GME/indigent pools
• Empire became one of many healthcare players, including AETNA, CIGNA, and united healthcare
• Large mutual life carriers exited the healthcare market
• Market dominated by the “for-profit” HMOs
• Empire licensed as an HMO to compete
Healthcare Market - Post NYHCRA

• Healthcare market has leveled and stabilised
• Empire’s financials have improved
• Empire has petitioned the legislature for “for-profit” status
• Managed care has keep costs relatively flat and controlled
• Recent public and provider support for managed care has changed to adversarial in nature
• Double digit medical costs are the norm
• Demographic pool has “lapsed” with no replacement
• GME/indigent pooling remains in place (minimal impact)
• SMC pooling remains (minimal impact)
• Consolidations in the healthcare market
Presentation of “interventionist” criteria
Basis of “Interventionist” Case

- BUPA has attracted a significantly younger profile of members
- This enables them to make windfall profits
- Which seriously damages Vhi’s profit and loss account……and therefore increases prices for Vhi’s members
Scenario - BUPA Trades off Claims for Profit

Pool of resources

- Community rated premium
- Tax relief
- Interest on reserves

- Claims
- Expenses
- Profits
- Additions to reserves
- Tax on profits

Interventionist case
Scenario - Vhi Trades off Premium for Claims

Community rated premium

Tax relief

Interest on reserves

Pool of resources

Claims

Expenses

Profits

Additions to reserves

Tax on profits
Scenario - Loading of Profit and Premium
(Total Claims Unchanged)
Average Vhi Claims Cost by Age Band

Source: Vhi
Age Distribution of Membership

VHI actual
BUPA estimate

Key income zone
Key loss zone

Source: Vhi

© 2002 Andersen. All rights reserved.
Estimate of Average Claim Per Member

Source: BUPA estimate derived from Vhi estimates of age distribution of BUPA membership and Vhi average claim for each age group.
Distribution of Average Claim by Age Band

Source: Calculated from Vhi average claim for each age group, Vhi data on age distribution of members and Vhi estimates of age distribution of BUPA members
Estimated Effect of BUPA Profits on Consumer

<table>
<thead>
<tr>
<th></th>
<th>Per member</th>
<th>Total*</th>
<th>Assumptions</th>
</tr>
</thead>
<tbody>
<tr>
<td>Average premium</td>
<td>€295</td>
<td>€72m</td>
<td>Data provided by BUPA</td>
</tr>
<tr>
<td>Average claim</td>
<td>(€155)</td>
<td>(€38m)</td>
<td>50% of VHI’s average claims</td>
</tr>
<tr>
<td>Expenses</td>
<td>(€56)</td>
<td>(€14m)</td>
<td>Data provided by BUPA</td>
</tr>
<tr>
<td>Normal profit margin</td>
<td>(€35)</td>
<td>(€7m)</td>
<td>Assumed at 12%</td>
</tr>
<tr>
<td>=Windfall Profit</td>
<td>€49</td>
<td>€13m</td>
<td>Equates to 2.4% of VHI premium income</td>
</tr>
</tbody>
</table>

*assumes 245,000 members
**“Worst Case” Estimated Effect of BUPA Profits on Consumer**

<table>
<thead>
<tr>
<th></th>
<th>Per member</th>
<th>Total*</th>
<th>Assumptions</th>
</tr>
</thead>
<tbody>
<tr>
<td>Average premium</td>
<td>€295</td>
<td>€72m</td>
<td>Data provided by BUPA</td>
</tr>
<tr>
<td>Average claim</td>
<td>(€62)</td>
<td>(€15m)</td>
<td>20% of VHI’s average claims</td>
</tr>
<tr>
<td>Expenses</td>
<td>(€56)</td>
<td>(€14m)</td>
<td>Data provided by BUPA</td>
</tr>
<tr>
<td>Normal profit margin</td>
<td>(€35)</td>
<td>(€7m)</td>
<td>Assumed at 12%</td>
</tr>
<tr>
<td>=Windfall Profit</td>
<td>€49</td>
<td>€36m</td>
<td>Equates to 6.6% of VHI premium income</td>
</tr>
</tbody>
</table>

*assumes 245,000 members
Conclusion

Absence of RE means prices are at least 2.4% higher than required
Effect of Absence of RE on Vhi

• Vhi has been successful in attracting new business
  – 33,000 new members in 2000
  – 780 new group schemes

• This new business is mostly in the key income zone (age 19 to 29)

• This level of new business is not expected to continue due to a slowdown in market growth
Effect of Loss of Members in Key Age Group

<table>
<thead>
<tr>
<th></th>
<th>Age band 19-29</th>
</tr>
</thead>
<tbody>
<tr>
<td>Average premium</td>
<td>€350</td>
</tr>
<tr>
<td>Average claim</td>
<td>(€132)</td>
</tr>
<tr>
<td>=Average marginal surplus</td>
<td>€218</td>
</tr>
<tr>
<td>x Number of members</td>
<td>273,600</td>
</tr>
<tr>
<td>=Total marginal surplus</td>
<td>€59.6m</td>
</tr>
<tr>
<td>Reduction in surplus for 10,000 lost members</td>
<td>€2.2m</td>
</tr>
<tr>
<td>Extra price increase required</td>
<td>0.4%</td>
</tr>
</tbody>
</table>
Example of Criteria for “Interventionist” Case

• Implement RE when market equalisation percentage reaches 4.5%.
• This indicates that one insurer’s average claim size, is less than 60% of the average claims of other insurers.
• This can be made subject to the HIA being satisfied that this difference mainly arises due to differences in age profile and health status (i.e. not differences in claims management or levels of cover)
• Allows wide scope for a difference in average claims, which is more than sufficient allowance for start up expenses and normal profit taking
Presentation of “non-interventionist” criteria
Some Opening Thoughts

“Above all, do no harm”
(Hippocratic Oath c. 400 B.C.E.)

“When the only tool you have is a hammer, every problem begins to resemble a nail”
(Abraham Maslow)

“To benefit the common good by facilitating a competitive health insurance market whilst preserving community rating, open enrolment and lifetime cover”
(HIA Vision)
Introduction

• RE payments can only help consumers by addressing one problem, a destructive spiral of market exit and entry caused by predatory behaviour
• RE is ineffective against other problems and may harm consumers interests
• This presentation sets out what is meant by predatory behaviour in this context and how RE payments can address the problem
• The presentation continues with an analysis of the effect of RE payments in other circumstances
• Concludes on the type of criteria needed
Predatory Behaviour 1

Community rating with a single insurer

Average Claim + OH + margin = premium €500
Average Claim €400

© 2002 Andersen. All rights reserved.
Predatory Behaviour 2

“Healthy Competition” with a new entrant

- New entrant will make “windfall profits” if it attracts lower risk members precisely because it is bona fide community rating
- An inefficient firm can be driven out of the market. Other can insure all comers at its current premium. Little damage to consumers / “community rating”.

© 2002 Andersen. All rights reserved.
Predatory behaviour by a new entrant

- New entrant undercuts incumbent, but only because it has a better risk profile
- Incumbent has to raise premiums so driving consumers out of market or to new entrant, to the extent that new entrant accepts them
- Incumbent could be driven out of market. New entrant then forced to leave or raise premiums. Consumers face fluctuating premiums and no assurance of future cover
Predatory Behaviour 4

• RE may address the problem by making the incumbent viable and keeping them in the market. RE payments, which would cease if the incumbent left the market, may make it worthwhile to stay. In addition a predatory new entrant pursuing this type of strategy would be unlikely to be able to afford RE payments (unless they cease predatory pricing).

• In addition, the presence of a RE scheme may prevent anyone from attempting such a strategy.

• To achieve this all that is required is a RE scheme triggered by evidence of predatory behaviour that would not be sustainable by an insurer bona fide community rating driving other insurers out of the market.
RE to Address “Windfall Profits” 1

- Normal competition will reduce the problem of two “communities” with different risk profiles and premium set for higher risk profile
Once an insurer has decided to stay in the market RE receipts do not affect the demand conditions it faces. It will not decrease its premiums.

RE receipts may even increase premiums.
Conclusion

- RE payments are only useful where a predatory spiral has started.
- Where there is no danger of market exit, RE has no benefits for consumers and may even harm them.
- Suggested criteria are the signs that a predatory spiral is starting.
Example Criteria for “Non-interventionist” Case

- Implement RE if market has become unstable due to predatory behaviour and there is a danger of market exits.
- Possible warning signs are:
  - A community rated price existing in the market that is not sustainable for the market as a whole
  - Significant loss of policyholders by an insurer, say loss of 10% of members in any year
  - Downsizing of the market, say 5% per annum decrease in number of consumers in market in any year
  - Exit of old age policy holders, say 5% of insurer’s >60 members drops out in any year
  - Significant change in age profile of an insurer’s membership
- These are only warning signs - qualitative work required
- Ideally this criteria would never be met and RE would be a reserve power bringing stability to the market
Perspective of a potential new entrant
Perspective of a Potential New Entrant

• Advantages of the market to a new entrant
  – “Cherry pick” the better risk
  – Underwriting skills/experience
  – Acquisition of current player (well capitalised)
  – Well known healthcare player

• Disadvantages of the market to a new entrant
  – Not well known in the market
  – Initial expense to develop provider network (reimbursement rates)
  – Marketing and sales (start-up costs)
  – Administrative services (local or other)
  – Community rating restrictions
Presentation of outline draft implementation criteria
Health Insurance (Amendment) Act, 2001

- “….Include in that report a recommendation by it that the minister ought or ought not (as it considers appropriate having regard to the best overall interests of health insurance consumers) to exercise the power hereafter mentioned…”

- “The best overall interests of health insurance consumers includes a reference to the need to maintain the application of community rating across the market for health insurance and to facilitate competition between undertakings.”
Defining Consumer Interests

- Community rating
- Facilitation of competition
- Value for money
- Comprehensive cover
- Quality private health services
- Choice of products

- Product enhancements
- Choice of insurer
- Financial security of insurers
- Financial security of providers
- Good customer service
- Quality of information

For all health insurance consumers!
Draft Criteria for Implementation

A. Effectiveness Test

B. Consumer Test

C. Materiality Test

D. Competition Test

Decision on factors affecting consumer interest that will benefit by implementation of RE and reduce list to relevant consumer issues

Identify any elements of consumer interest from A that are not currently being served in the market

Test whether the distortion in the market is material

Balance the benefit to the consumer of implementation with any negative effect on competition
**A: Effectiveness Test**

**No direct positive effect**
- Choice of insurer
- Comprehensive cover
- Quality private health services
- Choice of products
- Product enhancements
- Quality of information
- Good customer service
- Financial security of providers

**Possible positive effect**
- Value for money
- Community rating
- Facilitation of competition

**Positive effect**
- Financial security of insurers
A: Effectiveness Test

**No direct positive effect**

- Choice of insurer
- Comprehensive cover
- Quality private health services
- Choice of products
- Product enhancements
- Quality of information
- Good customer service
- Financial security of providers
A: Effectiveness Test

Possible positive effect

- Value for money
- Community rating
- Facilitation of Competition
A: Effectiveness Test

Positive effect

- Financial security of insurers
A: Effectiveness Test
Consumer Interests Addressed by RE

Reduced list of relevant consumer issues that RE can address
• Value for money (and facilitation of price competition)
• Community rating
• Financial security of insurers

For all health insurance consumers!
B: Consumer Test
Identify Current Issues

Signal

- The existence of a predatory spiral

Which may be evidenced by…..

- A community rated price existing in the market that is not sustainable for the market as a whole
- Significant loss of policyholders by an insurer, say loss of 10% of members in any year
- Downsizing of the market, say 5% decrease in number of consumers in market in any year
- Exit of old age policy holders, say 5% of insurer’s >60 members drops out in any year
- Significant change in age profile of an insurer’s membership
B: Consumer Test
Identify Current Issues

Issue of Value for money
And Facilitation of Competition based on price

Signal

- Prices being too high due to separation of communities resulting in windfall profits
- And evidence that RE payments will be passed on to consumers as lower premium

Which may be evidenced by….

- An insurer’s average claim being less than 60% of the other insurers’ average (and is not reflected in premiums)
- Evidence that payments will be passed on to consumers as lower premium may be provided by
  - Not for profit status
  - Information from the insurer on passing on of payments
  - Any price controls existing
  - Any evidence that competition based on price will improve
B: Consumer Test
Identify Current Issues

Issue of Community rating

Signal

• Lack of intergenerational solidarity, i.e. separation of high risk and low risk communities across the market

Which may be evidenced by….

• Windfall profits
• A predatory spiral
C: Materiality Test

Materiality of Distortion

- Materiality test is reached when market equalisation percentage reaches 4.5%
- This indicates a wide difference (c. 60% ratio) in average claims between insurers and incorporates the materiality of each insurer’s business
D: Competition Test
Balance Implementation With Competition 1

- At this stage of the decision the authority has found that consumer interests are being harmed, that RE would address this harm and that the issue is material.
- However, RE may also have a detrimental effect on competition and hence on consumer benefit. The two effects on consumer benefit will have to be balanced.
- For example, one commentator regards this as very important and feels that RE should only be considered if there are at least four competitors in the market.
- Two questions to ask:
  - Will RE affect the level of competition
  - What impact will any reduction of competition have on consumers
D: Competition Test
Balance Implementation With Competition 2

• RE can hinder competition in three ways:
  – Driving a competitor out of the market
  – Preventing a competitor from competing vigorously
  – Discouraging potential new entrants

• This assessment will be easier when you have actual return information, however best estimate now would be:
  – RE would not drive BUPA out of market
  – RE would not affect BUPA’s incentives to compete
  – RE would make Ireland a less attractive market for new entrants

• If this assessment is correct, RE would not reduce the number of competitors but would make further entries less likely. This could be a negative effect on competition.
## Competition Test

### Balance Implementation With Competition 3

<table>
<thead>
<tr>
<th>Competition promotes</th>
<th>Competition may harm</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Value for Money</td>
<td>• Community rating</td>
</tr>
<tr>
<td>• Choice of Insurer</td>
<td>• Financial security of insurers</td>
</tr>
<tr>
<td>• Comprehensive cover</td>
<td></td>
</tr>
<tr>
<td>• Quality private health services</td>
<td></td>
</tr>
<tr>
<td>• Choice of products</td>
<td></td>
</tr>
<tr>
<td>• Product enhancements</td>
<td></td>
</tr>
<tr>
<td>• Quality of information</td>
<td></td>
</tr>
<tr>
<td>• Good customer service</td>
<td></td>
</tr>
<tr>
<td>• Financial security of providers</td>
<td></td>
</tr>
</tbody>
</table>
Draft Criteria for Implementation

A. **Effectiveness Test**
   - Decision on factors affecting consumer interest that will benefit by implementation of RE and reduce list to relevant consumer issues

B. **Consumer Test**
   - Identify any elements of consumer interest from A that are not currently being served in the market

C. **Materiality Test**
   - Test whether the distortion in the market is material

D. **Competition Test**
   - Balance the benefit to the consumer of implementation with any negative effect on competition
Draft Risk Profile Weight

• Propose 0% weighting to utilisation at outset
• This eliminates any potential criticism that RE results in sharing of efficiencies between insurers
• If HIA observes material differences in claims within age bands, the source of this difference should be further investigated by the HIA
• If the HIA finds that the source of these differences is health status, then a risk profile weight should be introduced
• The appropriate level of risk profile weight depends on the findings of the HIA on the source of differences within age bands