Competition in the Private Health Insurance Market

Executive Summary

January 2007

The Competition Authority
An tÚdarás Iomaíochta

EXECUTIVE SUMMARY

Context of the Report

1. The Competition Authority undertook this analysis of competition in the private health insurance market following a request by the Minister for Health and Children, in a press release of 23rd December 2005, to the Competition Authority and the Health Insurance Authority, to report *"on further measures to encourage competition in the health insurance market and the strategy or strategies which might be adopted in order to create greater balance in the share of the market held by competing insurers"*.

2. The analysis was undertaken in the context that Ireland's public policy objective in private health insurance is intergenerational solidarity – whereby the young subsidise the old by paying the same prices for private health insurance, despite the lower risk they represent to health insurers. The concept of intergenerational solidarity is underpinned by the following principles:

   a. **Community Rating** – unlike all other insurance products in Ireland, health insurers must charge all customers the same price for the same level of cover regardless of age, gender and the current or likely future state of their health.[1]

   b. **Open Enrolment** – all applicants for private health insurance must be accepted by a health insurer.

   c. **Lifetime Cover** - all consumers are guaranteed the right to renew their policies (irrespective of factors such as their claims history).

   d. **Minimum Benefits** – health insurers are required to cover a particular set of treatments and procedures, and to cover all public hospitals.

   e. **Risk Equalisation** – this system aims to neutralise differences in health insurers' costs that arise due to variations in the risk profile of their customer base. Risk equalisation results in cash transfers from health insurers with lower risk profiles to health insurers with higher risk profiles.

3. The Competition Authority does not assess the necessity, proportionality or appropriateness of these principles but their effects on competition are analysed, and measures to promote competition within this framework are identified. The report does not purport to tackle issues in the public health system, or to analyse how it affects the private health insurance market.

4. Since the Minister's request there have been a number of significant developments that may lead to a fundamental change in the structure of the Irish private health insurance market. Specifically, BUPA Ireland announced, on 14th December 2006, its intention to withdraw from the Irish market and has ceased accepting new members. Thus various potential future scenarios exist for the Irish private health insurance market and there is much uncertainty.

[1] Ireland's requirement of Community Rating is "unfunded", meaning that there is no fund built up over the lifetime of an insured person to cover their expected claims cost. Instead, the money contributed by all insured persons is pooled by each health insurer and the cost of claims in any given year is taken from the pools.

5. The Competition Authority concluded in December 2006 that it could best pursue its statutory objective of promoting competition by reporting in an independent capacity, rather than in conjunction with the Health Insurance Authority.

6. It was considered that a separate report could be completed more speedily and that this was desirable due to the increased market uncertainty and change to the original impetus for the report. Nonetheless, much useful work was carried out jointly by both Authorities and much of the analysis and findings contained in this report were informed by the expertise of the Health Insurance Authority.

Key Findings

The Effect of Public Policy on Competition

7. Competition in private health insurance in Ireland is constrained by the combination of it being a voluntary system and founded on the concept of intergenerational solidarity. The legislative and regulatory framework designed to support this decision significantly limits the scope for competition in private health insurance; by definition, community rating, open enrolment, lifetime cover, the Minimum Benefit Regulations and risk equalisation prevent many of the key features of competition in insurance markets[2] from emerging in private health insurance. For example:

   - Health insurers cannot offer discounts to people with healthier lifestyles, such as non-smokers;
   - Health insurers cannot offer discounts to employers who have programmes for promoting employee health, such as free/subsidised health screening;
   - Innovation in private health insurance is limited as health insurers must continue to cover procedures that have been overtaken by more effective and efficient technologies until the Minimum Benefit Regulations are updated; and,
   - Health insurers are constrained in their ability to select the most efficient network of hospitals.

8. Moreover, insurance is all about risk and insurance companies compete through the effective management of risk. As health insurers in Ireland are not allowed to price their products according to the perceived risk presented by each customer, the basis upon which actuaries can assess private health insurance products and customers is fundamentally changed and this limits the basis upon which health insurers compete.

9. The legislative and regulatory limitations imposed on private health insurance in Ireland to enforce intergenerational solidarity thus encourage the prices and products of competing health insurers to converge. One cannot expect to see the kind of competition in private health insurance that consumers are used to in other insurance markets.

[2] Insurance markets here refers to private insurance (e.g. motor insurance and house insurance), rather than public insurance (PRSI).

Factors that Inhibit and Distort Competition in Private Health Insurance

10. The private health insurance market is also characterised by a number of other factors which tend to distort and dampen competition beyond the restrictions imposed by intergenerational solidarity.

11. First, the largest private health insurance provider, Vhi Healthcare, is not prudentially regulated as a health insurance undertaking.[3] This situation arises from Vhi Healthcare's continued exemption under Art. 4(c) of the 1973 EU First Non-Life Insurance Directive.[4] Without this exemption, Vhi Healthcare would have to be regulated by the Financial Regulator and would be legally required to have reserves far greater than its current levels and to establish subsidiary or sister companies for selling its non-health insurance products (such as travel insurance and contact lenses).[5] Thus Vhi Healthcare enjoys a regulatory advantage which allows it to compete in ways not available to other health insurers.

12. Second, there are many barriers to new health insurers entering the Irish market. Some of these barriers to entry relate to the peculiarities of private health insurance and are unavoidable. The current climate of uncertainty regarding Risk Equalisation and BUPA Ireland's stated intention to exit the market also make the Irish private health insurance market less appealing. One barrier to entry is the market position of Vhi Healthcare in terms of its legacy as a State-owned former monopoly and its regulatory advantage. A less significant barrier is the large legacy network of salary deduction schemes that Vhi Healthcare built up as the former incumbent monopoly provider of private health insurance. Inertia on the part of employers makes it difficult for other health insurers to build up a similar network.

13. Third, although the process of switching health insurer is simple and straightforward, some consumers have an incorrect perception that the process is difficult and cumbersome. Certain practices by health insurers also discourage consumers from switching health insurer in response to a more competitive offering, for example tying private health insurance and travel insurance products.

14. Fourth, it is difficult for consumers to compare and contrast private health insurance policies. This makes it difficult for consumers to know which health insurer's product best meets their needs and inhibits competition.

15. Fifth, the Minimum Benefit Regulations, in their current form, hinder innovation in product design and the development of limited cover plans.

Key Recommendations

16. The Competition Authority makes 16 recommendations in this report for promoting competition in the private health insurance market in Ireland. In particular, the Competition Authority recommends:

    - Vhi Healthcare's exemption from prudential regulation should be ended as soon as possible so that it becomes subject to the legal solvency requirements and corporate structuring rules that apply to other health insurers in Ireland;

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[3] Vhi Healthcare is regulated by the Financial Regulator in its capacity as an insurance intermediary, for the sale of travel insurance and dental health insurance for example.

[4] The European Commission recently announced that it has decided to *"send Ireland a formal request to submit its observations on the continued legality of the exemption of the Irish Voluntary Health Insurance Board (VHI) from certain EU rules on non-life insurance."* European Commission press release, 24th January 2007.

[5] Vhi Healthcare is currently statutorily prevented from establishing subsidiaries.

- A package of measures should be introduced to provide consumers with useful and timely information to enable them to consider alternative private health insurance products, and to promote consumer awareness of the ease of switching health insurer;

- Vhi Healthcare should discontinue its practice of cancelling its MultiTrip Travel Insurance when its members switch health insurer;

- The Minimum Benefit Regulations should be modernised and the Health Insurance Authority should be allowed to approve limited cover plans, to allow more innovation in the market;

- The Health Insurance Authority should conduct an information campaign to inform employers about how to set up multiple salary deduction mechanisms;

- The Health Insurance Authority should be given wider powers to enforce the Health Insurance Acts and formally assigned the function of promoting the interests of consumers; and,

- The Health Insurance Authority should undertake a full cost benefit analysis of what would be required to move to a prospective Risk Equalisation System and the Minister for Health and Children should clarify the exemptions from Risk Equalisation that apply.

17. These measures will promote competition in private health insurance, within the limits of intergenerational solidarity, regardless of how the market structure evolves.

The Commencement of Risk Equalisation Transfers

18. The Competition Authority finds that once Risk Equalisation transfers commence, the average price of private health insurance will increase regardless of the level of competition in the market. This is because the market is currently distorted by Vhi Healthcare's ability to reduce its level of reserves to compete with BUPA Ireland's and VIVAS Health's prices, which are in turn facilitated by their more favourable risk profiles. The commencement of Risk Equalisation transfers, and the impending requirement on Vhi Healthcare to increase its reserves to meet the Financial Regulator's requirements, will inevitably lead to price increases in private health insurance in Ireland.

19. The commencement of Risk Equalisation transfers is also likely to strengthen Vhi Healthcare's market power and allow it to increase its prices above competitive levels and sustain those prices for a significant length of time.

20. At the time of writing, it is extremely difficult to make predictions about the future of the private health insurance market and competition in the market given the speed at which events are unfolding.

21. Eventually, the uncertainty surrounding Risk Equalisation and BUPA Ireland's declared exit will dissipate. Vhi Healthcare's regulatory advantage will be ended. Thus the likelihood of new health insurers entering the market to compete with Vhi Healthcare will be somewhat improved.

22. Ireland may wish to consider more fundamental measures to promote competition. These measures could involve, for example, one or a combination of: structural solutions (e.g. splitting Vhi Healthcare into a number of competing insurers, and perhaps a one-off "Grey PHI" consisting of consumers over a certain age), privatisation, and a review of intergenerational solidarity and the manner in which that objective is pursued.

23. Whether such fundamental measures are desirable or not depends on the trade-offs between the actual value added by the principles governing private health insurance, which effectively control prices and redistribute risk, against the loss in consumer welfare caused by those same principles which by their nature prevent the emergence of a more normal competitive market.

Private Health Insurance in Ireland – Facts and Figures

24. The entire population of Ireland can avail of public care in public hospitals.[6] The main function of private health insurance in Ireland is to cover private secondary medical care in hospitals.

25. Since access to healthcare is guaranteed under the public health system, the role of private health insurance is to offer consumers a greater choice of treatments and facilities, higher standards of accommodation during treatment, and potentially shorter waiting times for treatment.

26. Around 50% of the population of Ireland has private health insurance – about 2 million people. This is quite a high penetration rate; in the UK, for example, which also has a universal public healthcare system but a *risk-rated* private health insurance market, around 10% of the population have private health insurance. Overall, the demand for private health insurance has increased with Ireland's economic growth.

27. BUPA Ireland entered the Irish private health insurance market in 1997[7] to compete with the State owned Vhi Healthcare, which had held a monopoly position for 40 years. BUPA Ireland steadily grew its market share to 20% in 2004, when VIVAS Health entered the market.

28. By September 2006, VIVAS Health had a market share of 3%, BUPA Ireland had a 22% market share, and Vhi Healthcare had 75% of private health insurance consumers.

29. It remains to be seen how the announcement by BUPA Ireland, in December 2006, that it intends to exit the market will affect relative market shares.

30. Private health insurance prices have been rising. Medical inflation has been running at much higher levels than elsewhere in the economy and this has been passed through to consumers of private health insurance.

[6] There is a daily charge of €60 up to an annual maximum charge of €600. Thirty percent of the population qualify for a medical card and are exempt from the €60 charge.
[7] Technically BUPA Ireland entered in 1996 but it began accepting business in 1997.

How Health Insurers Compete

31. Health insurers compete through product innovation and price competition. When it entered the Irish market in 1997, BUPA Ireland sought to differentiate its products from Vhi Healthcare, for instance by offering cover for alternative therapies. In 2004, VIVAS Health introduced a wide range of options for consumers, with cover for services which Vhi Healthcare and BUPA Ireland do not provide, such as tooth whitening and laser eye surgery. VIVAS Health also introduced some targeted marketing for certain occupational groups (e.g. nurses and teachers).

32. Vhi Healthcare responded to this competition, sometimes pre-emptively, by introducing its own innovations; in particular, complementary products such as travel insurance, dental insurance, and health clinics.[8] These are just some of the product innovations that have been introduced since Vhi Healthcare's monopoly ended in 1997.

33. When BUPA Ireland entered the market, it initially priced its products about 10% below comparable Vhi Healthcare plans. Since then, annual price increases by BUPA Ireland have been very similar in magnitude to Vhi Healthcare's, thereby maintaining this 10% price differential.

34. When VIVAS Health entered the market in October 2004, it initially priced its plans more than 10% below comparable BUPA Ireland products and more than 20% below comparable Vhi Healthcare products. The price differential between VIVAS Health and the other health insurers has increased in the last two years.

35. Competition in the private health insurance market in Ireland has led to the steady decline of Vhi Healthcare's share of the overall market and a corresponding steady gain by BUPA Ireland and later VIVAS Health.

36. As overall demand for private health insurance in Ireland has been growing, Vhi Healthcare's customer base has remained static, despite its declining share of the market.

37. Since BUPA Ireland entered the market approximately 10% of private health insurance consumers have switched health insurer.

38. Switching occurs mainly in the younger age cohorts, with "cost savings" by far the most commonly cited reason for switching. Thus newer health insurers tend to attract younger more profitable customers, and while Vhi Healthcare's overall market share may have been declining, it has retained a higher share of older and thus less profitable consumers. Many consumers have not switched because they are satisfied with their current provider or they see no point in switching.

Vhi Healthcare's Regulatory Advantage

39. Private health insurance is highly regulated, by a complex web of regulations, legislation and regulatory institutions including EU Directives, Irish health insurance legislation, the Minister for Health and Children, the Health Insurance Authority and the Financial Regulator.

[8] Ordinarily the Financial Regulator does not permit health insurance undertakings to sell other insurance products directly but Vhi Healthcare is not regulated by the Financial Regulator and is actually prevented from establishing subsidiaries under its legislative framework.

40. In 1992, the EU enacted the Third Non-Life Insurance Directive which, in effect, prescribed that Ireland must allow any health insurance company which is authorised in another EU Member State to offer health insurance in Ireland.

41. The existing framework of EU Directives and Irish health insurance legislation and regulations has led to each health insurer in Ireland being regulated differently:

    - Vhi Healthcare is exempt from prudential regulation (but must obtain the approval of the Minister for Health and Children in certain aspects of its business);

    - BUPA Ireland is an intermediary for a UK health insurance undertaking (BUPA Insurance Ltd); and,

    - VIVAS Health is the only health insurance undertaking in Ireland regulated as such by the Financial Regulator.

42. This means that the three health insurance providers are competing subject to differing regulatory restraints. For example:

    - Vhi Healthcare is not subject to any solvency requirements;

    - BUPA Ireland's underwriting is subject to UK solvency requirements; and

    - VIVAS Health's solvency requirements are set by the Financial Regulator.

43. This inconsistency distorts competition in private health insurance.

44. The Minister for Health and Children has already indicated her intention to legislate for Vhi Healthcare to be obliged "*to attain the level of reserves necessary to achieve authorisation as an insurer within six years*." The Competition Authority recommends that this timeframe be shortened and Vhi Healthcare's exemption from regulation as a health insurance undertaking removed as soon as possible.

45. The Competition Authority further recommends that this review should consider methods for Vhi Healthcare to build up its reserves to appropriate solvency requirements other than the accumulation of surplus through premium increases.

46. Vhi Healthcare should also be obliged to establish sister companies (or subsidiaries) to carry out its non-health insurance activities, as it would have to do if it was regulated by the Financial Regulator.

The Health Insurance Authority

47. The Health Insurance Authority was established in 2001 and is responsible for monitoring the operation of health insurance legislation, including associated regulations. Its powers of enforcement are very limited, however, and it does not have the explicit function and power of promoting consumers' interests as other sectoral regulators, such as the Financial Regulator, do.

48. If the Health Insurance Authority believes, for example, that a health insurer's product has the potential to undermine community rating, or that the information a health insurer provides to consumers is misleading, it has only the draconian power to de-register the health insurer or sometimes no power at all. The Competition Authority recommends that the Health Insurance Authority be given the powers to:

- Direct that a health insurer alter its practices or its products to comply with the provisions of the Health Insurance Acts or regulations, and to provide for appropriate sanctions; and
- Promote the interests of consumers.

49. Giving the Health Insurance Authority these powers will allow it to better protect consumers and promote competition by ensuring that the information consumers receive is accurate and useful, and that private health insurance products available in Ireland comply with the law.

Barriers to New Health Insurers Entering the Market

50. A wide range of obstacles to entering the Irish private health insurance market have been identified by stakeholders and potential entrants:

- The irretrievable cost of building a trustworthy brand (although this would be less for a recognised provider of other forms of insurance);
- Private health insurance is a highly regulated and specialised form of insurance and so specialist knowledge is required and commercial freedom limited;
- Vhi Healthcare's legacy position as a former monopoly and State-owned entity, its regulatory exemptions and large market share;
- Risk Equalisation and the associated uncertainty around its commencement; and,
- Access to salary deduction mechanisms.

51. It is clear from the views of potential market entrants that the single greatest barrier to entry is the position of Vhi Healthcare in the market, whereby its legacy advantages are, in part, perpetuated by a favourable regulatory regime.

52. A less significant barrier is the large legacy network of salary deduction schemes that Vhi Healthcare built up as the former incumbent monopoly provider of private health insurance. Inertia on the part of employers makes it difficult for other health insurers to build up a similar network.

53. The Competition Authority recommends that the Health Insurance Authority should conduct a campaign to make employers aware of their ability to set up multiple salary deduction mechanisms.

Barriers to Existing and Future Health Insurers Competing

54. For competition in any sector to work it is important that consumers are able to choose the supplier which offers them the best product or service for their needs. For products such as private health insurance, which involve ongoing contracts, consumers must be able to switch their health insurer when they are offered a more suitable or more competitive product than their existing plan.

55. The actual process of switching health insurer is simple and straightforward. Research indicates that 98% of switchers were "satisfied" or "very satisfied" with the switching process.

56. Switching is inhibited because consumers find it difficult to make comparisons between different private health insurance products in the first instance and because there is an incorrect perception that switching is difficult or may lead to a loss of cover. There is also a certain amount of consumer inertia – 14% of private health insurance consumers surveyed said that they would never switch insurer.

57. The Competition Authority recommends a package of measures to promote better information for consumers to enable them to switch health insurer where appropriate.

    - Health insurers should be obliged to provide prescribed information to consumers regarding the switching process and comparing private health insurance plans, both at point of sale and renewal; and,

    - The Health Insurance Authority should draft a Switching Code for health insurers detailing their duties during the switching process.

58. These recommendations will bring the private health insurance market into line with recent reforms in markets for other financial products such as motor insurance and bank current accounts. They will aid any new health insurers in attracting customers from existing providers.

59. One further market feature that inhibits switching is Vhi Healthcare's practice of linking its private health insurance products to its travel insurance products. If a customer of Vhi Healthcare decides to switch his/her private health insurance to another health insurer, and that customer has also purchased a Vhi MultiTrip travel insurance product, Vhi Healthcare also cancels the travel insurance.

60. This practice forces Vhi Healthcare customers to research alternative travel insurance products as well as alternative private health insurance products when they are considering switching. Switchers who wish to avoid gaps in their travel insurance cover are forced to switch both products at the same time. This practice discourages Vhi Healthcare customers from switching to alternative health insurers by creating unnecessary inconvenience. This should cease immediately.

61. The Minimum Benefit Regulations were established to give consumers a high degree of protection, given the complexities of private health insurance products, by obliging health insurers to cover certain procedures and hospitals.

62. The Regulations ensure that consumers do not inadvertently purchase private health insurance plans with insufficient cover. However, the Regulations also limit the extent to which health insurers can innovate and reduce the scope for the development of "limited cover plans". Limited cover plans are tailored, lower cost plans which, for example, cover a limited set of hospitals or do not offer maternity benefits.

63. The Competition Authority recommends that the system of minimum benefits should be simplified and updated, and that products offering limited cover should be permitted subject to prior regulatory approval by the Health Insurance Authority.

Vhi Healthcare's Buyer Power

64. The three health insurers in Ireland cover about 50 private medical facilities[9] and close to 2,000 hospital consultants. Private hospitals are heavily reliant on custom generated by private health insurers. Other sources of custom for private hospitals are the National Treatment Purchase Fund, restricted membership health insurance schemes or persons who pay for treatment out of their own pockets.

65. At the same time, private health insurance tends to lead to incentives to over-consume private healthcare, because the consumer is no longer paying the true cost of private healthcare. Over-consumption of healthcare pushes up the cost for all consumers. Thus health insurers seek ways to minimise the effect of this tendency towards over-consumption and their negotiating power over the private hospitals and consultants aids them in this regard.

66. With 75% of private health insurance consumers, Vhi Healthcare is by far the largest buyer faced by private hospitals. If BUPA Ireland's stated intention to exit the market results in there being only two health insurers in Ireland Vhi Healthcare's position will be further strengthened.

67. Vhi Healthcare's position affects contractual negotiations between private hospitals and other health insurers; Vhi Healthcare "sets the rules of the game". This does not give Vhi Healthcare a significant advantage in the private health insurance market, however, as other health insurers benefit from being able to replicate Vhi Healthcare's contract arrangements.

68. Vhi Healthcare's position also makes it a "gatekeeper" of significant importance. The OECD has found that *"Providers…. cannot afford not to have a contract with one insurer, given the concentration of the [private health insurance market] and their high dependence on income from privately insured patients".*[10] New private hospitals will find it difficult to prosper without securing Vhi Healthcare's custom. According to the OECD, the Irish private hospital sector is relatively underdeveloped, and most private treatments are still delivered in public facilities, in part because health insurers have not supported private hospital capacity increases.[11]

69. Vhi Healthcare's scale may enable it to negotiate better reimbursement rates, and thus lower premiums for its customers, but the measures taken by Vhi Healthcare to reduce reimbursement costs are those which any economically rational health insurer would be expected to exercise and do not rely exclusively on buyer power. Cost control measures, rather than buyer power, drive real efficiencies in the provision of private hospital services.

70. Financially prudent health insurers exercise caution in deciding which hospital facilities to cover. It is prudent for health insurers to refuse to cover medical facilities where there are justifiable concerns that such facilities would constitute unused surplus capacity; average costs fall as more capacity is used.

71. However, by virtue of its buyer power Vhi Healthcare has a significant influence over the level of private hospital capacity in Ireland. The Minister for Health and Children has recently announced a number of measures which will lead to an increase in the number of private hospitals in Ireland.

[9] Around half are in-patient hospitals which vary substantially in size; 20% are treatment or addiction centres; and the remaining 30% includes dental clinics, laser eye clinics, cosmetic surgery facilities, imaging facilities, diagnostics, pathology-related testing and respite care.
10 OECD (2004) p.38
[11] OECD (2004a), p.177

Risk Equalisation and Community Rating

72. Risk equalisation is a mechanism that aims to neutralise the effects of differing risk profiles across insurers. It aims to avoid the market instability that can arise if individual health insurers fail to attract a sufficient share of low risk consumers. Risk Equalisation by its nature limits competition.

73. The practice of risk adjustment and reimbursement started more than 30 years ago in the United States. Countries which have introduced a form of risk equalisation or cost reinsurance include Australia, Canada, New Zealand, Germany and the Netherlands.[12]

74. Ireland introduced legislation providing for Risk Equalisation in 1994; the current system came into effect in 2003. Risk Equalisation transfers under the Irish scheme will affect competition, both in terms of price and competition for different market segments.

75. Vhi Healthcare has stated that it cannot survive without Risk Equalisation transfers. BUPA Ireland has always maintained that it cannot make a profit under Risk Equalisation and that it would exit the market if it had to make Risk Equalisation transfers (which is has stated that it will now do). VIVAS Health has never objected to the existence of Risk Equalisation *per se* (though it believes Ireland's particular Risk Equalisation Scheme to be "draconian") and has recently reiterated its commitment to the Irish private health insurance market.

76. BUPA Ireland and VIVAS Health have to date been able to price below Vhi Healthcare due to their more favourable risk profile and hence lower average claims. Prior to BUPA Ireland's declared intention to exit the market, the Competition Authority concluded that the commencement of Risk Equalisation transfers would, in the short run, have likely led to a sharp rise in BUPA Ireland's prices. This effect would tend to lead to a narrowing of the price differential between Vhi Healthcare and BUPA Ireland. This is due to the neutralising effect Risk Equalisation transfers have on risk profile asymmetry; all health insurers will have to carry a share of the cost of all risks.

77. The commencement of Risk Equalisation transfers and the subsequent narrowing of price differentials could have numerous effects. First, BUPA Ireland's most price-sensitive consumers would be likely to discontinue cover completely. Second, switching from Vhi Healthcare would become less likely and, if BUPA Ireland's prices increased by as much as it estimated, switching to Vhi Healthcare would have become more likely. Each of these effects imply a consolidation of Vhi Healthcare's market position.

78. VIVAS Health is exempt from Risk Equalisation transfers until October 2007; the price differential between VIVAS Health and Vhi Healthcare will then also narrow.

79. Overall, price competition will be significantly reduced in the short term and the scope for price competition in the future will remain limited. Risk Equalisation transfers will reduce the competitive pressure on Vhi Healthcare.

[12] Though in many of these countries, private health insurance is mandatory.

80. Risk Equalisation transfers also change health insurers' incentives to compete across different market segments. In the absence of Risk Equalisation transfers, health insurers have an incentive to target low risk customers, typically younger customers, who are more profitable in a community rated market. Risk Equalisation attempts to eliminate advantages from competing for low risk customers only.

81. There is no perfect Risk Equalisation system, however, and health insurers may still try to improve their position by attracting less risky customers. They may succeed because young people generally switch more readily and healthier people may also switch more readily.

82. Nonetheless, Risk Equalisation should improve competition for older and more risky customers, although the considerable inertia of this segment will make it more difficult for other health insurers to attract this custom.

83. Finally, Risk Equalisation discourages new health insurers from entering the Irish market. Though new health insurers are exempt from Risk Equalisation transfers for three years, they are likely to be net contributors to the Risk Equalisation system as they tend to win custom from younger and healthier individuals.

Vhi Healthcare's Market Power

84. Market power allows a health insurer to set prices above competitive levels or reduce the quality of its products below what would be the norm in a competitive market. It can also reinforce barriers to entry and slow down the rate of innovation.

85. Once Risk Equalisation payments commence, Vhi Healthcare's market power will increase significantly. This is the case regardless of whether BUPA Ireland exits the market.

86. Vhi Healthcare's market power stems from a combination of factors:

- Vhi Healthcare's very large share (75%) of a market which has very few health insurers;
- Vhi Healthcare has been able to maintain prices above its competitors for comparable plans, and Risk Equalisation transfers would allow it to profitably raise its prices;
- Though Vhi Healthcare did respond to competition from BUPA Ireland and VIVAS Health by introducing innovations and new products, the commencement of Risk Equalisation transfers will reduce the competitive pressure on Vhi Healthcare to attract and retain price-sensitive consumers;
- The competitive threat from new health insurers entering the market is low due to the high barriers to entry; and,
- Private health insurance customers, including group schemes, have little or no countervailing buyer power when dealing with Vhi Healthcare.

87. Before Risk Equalisation was triggered, Vhi Healthcare had some market power but BUPA Ireland and VIVAS Health imposed a significant competitive constraint on the behaviour of Vhi Healthcare. The commencement of Risk Equalisation transfers will substantially weaken this competitive constraint and increase Vhi Healthcare's market power. Vhi Healthcare is likely to be able to profitably increase its premiums above competitive levels for a sustained period of time.

88. The Competition Authority also finds that once Risk Equalisation transfers commence, the average price of private health insurance will increase regardless of the level of competition in the market. This is because the market is currently distorted by Vhi Healthcare's ability to reduce its level of reserves to compete with BUPA Ireland's and VIVAS Health's prices, which are in turn facilitated by their more favourable risk profiles. The commencement of Risk Equalisation and the impending requirement on Vhi Healthcare to increase its reserves to meet the Financial Regulator's requirements will inevitably lead to price increases in the market.

Potential Further Measures to Promote Competition

89. At the time of writing, it is extremely difficult to make predictions about the future of the private health insurance market and competition in the market given the speed at which changes are occurring.

    - Eventually, the uncertainty surrounding Risk Equalisation and BUPA Ireland's declared exit will dissipate;
    - The implementation of the Competition Authority's recommendations should reduce barriers to entry and provide more scope for effective competition between health insurers; and,
    - The longer VIVAS Health is in the market the more valuable and trusted its brand will become.

90. Regardless of how the structure of the private health insurance market evolves, Ireland may wish to consider more fundamental measures to promote competition. These measures could involve, for example, one or a combination of: structural solutions (i.e splitting Vhi Healthcare into a number of competing insurers, and perhaps a one-off "Grey PHI" consisting of consumers over a certain age), privatisation, and a review of intergenerational solidarity.

91. Whether such fundamental measures are desirable or not depends on the trade-offs between the actual value added by the principles governing private health insurance, which effectively control prices and redistribute risk, against the loss in consumer welfare caused by those same principles which by their nature prevent the emergence of a more normal competitive market.

92. When considering fundamental measures, the following factors must be taken into consideration:

    - A structural solution may cause some administrative duplication initially but this would not be major and could certainly be overcome by selling "baby Vhi"s to experienced (health) insurance undertakings;
    - Structural solutions may require the destruction of the Vhi Healthcare brand;

- The effect on health insurers' ability to negotiate with private hospitals and hospital consultants;

- All options would need to be researched in terms of their feasibility, legal requirements, costs and benefits to find the most appropriate package of measures;

- Private health insurance is inextricably linked to (perceptions of) Ireland's public health system – any changes to one will affect the other.

LIST OF RECOMMENDATIONS

The Competition Authority makes 16 recommendations to improve competition in the Irish private health insurance market. A number of these recommendations concern the structure and regulation of Vhi Healthcare. The Authority recommends addressing Vhi Healthcare's market position by means of legislative and regulatory measures (Recommendations 1-5).

In a Press Release of December 23rd, 2005, the Minister for Health and Children announced that the recommendations arising from this Report would *"inform the drafting of the Bill that will provide for the conversion of VHI into a PLC"*. Accordingly, dates have not been allocated against each Recommendation, as is the Competition Authority's normal practice. Instead, some Recommendations (1, 2, 3, 6, 7, 9, 10, 12, 13 and 16) are designed to be accommodated as part of the upcoming Bill mentioned in the Minister's Press Release, while others (Recommendations 4 and 5) are contingent on the earlier recommendations.

Recommendation 1 **Require Vhi Healthcare to establish subsidiary or sister companies for activities other than health insurance**	**Action By**
Vhi Healthcare should be obliged to provide non-health insurance services in the same manner as other insurers. Accordingly, the Minister should allow and oblige Vhi Healthcare to establish sister companies (or subsidiaries) to carry out non-health insurance activities.	**Minister for Health and Children**

Recommendation 2 **Reassess the requirements placed on Vhi Healthcare to meet the Financial Regulator's reserve requirements**	**Action By**
Vhi Healthcare's solvency reserve requirements should be reassessed. • The proposed six-year timeframe allowed for Vhi Healthcare to attain the necessary level of reserves to be regulated as an insurance company should be reviewed. • Consideration should also be given to reducing the level of solvency reserves required of Vhi Healthcare prior to the conclusion of the "Solvency 2" process. • Consideration should be given by the Minister to methods of permitting Vhi Healthcare to raise capital by means other than the accumulation of surplus.	**Minister for Health and Children**

Recommendation 3 **Remove the requirement for Vhi Healthcare to seek Ministerial approval for premium increases**	**Action By**
The requirement for Ministerial approval for Vhi Healthcare premium increases under S.3 of the Voluntary Health Insurance (Amendment) Act, 1996 should be abolished.	**Minister for Health and Children**

Recommendation 4 **Regulate Vhi Healthcare as an insurance undertaking once it has reached the required reserves**	**Action By**
Vhi Healthcare should be subject to prudential regulation in its capacity as an insurance undertaking by the Financial Regulator when it has reached the level of reserves required by the Financial Regulator.	**Financial Regulator**

Recommendation 5 **Remove Vhi Healthcare's exemptions from the EU Non-Life Directives**	**Action By**
Vhi Healthcare's exemptions from the First and Third EU Non-Life Directives should be abolished. Once Vhi Healthcare has received authorisation as an insurance company from the Financial Regulator by reaching the required level of reserves, removal of these exemptions by the institutions of the EU should be sought by the Minister for Health and Children.	**Minister for Health and Children**

Recommendation 6 **Provide the Health Insurance Authority with wider powers to enforce the Health Insurance Acts**	**Action By**
Legislation should be brought forward to amend the Health Insurance Acts and provide that the Health Insurance Authority has the power to direct that a health insurer alter its practices or its products to comply with the provisions of the Acts or regulations thereunder; and is granted the power to apply appropriate sanctions.	**Minister for Health and Children**

Recommendation 7 **Assign the Health Insurance Authority the function of promoting the interests of consumers**	**Action By**
Legislation should be brought forward to amend the Health Insurance Acts to assign to the Health Insurance Authority the function of promoting the best interests of consumers.	**Minister for Health and Children**

Recommendation 8 **Employers should be made aware of their ability to set up multiple salary deduction mechanisms**	**Action By**
The Health Insurance Authority should conduct an information campaign to employers who provide employees with the option of paying their health insurance via salary deduction to inform them of the ease with which multiple salary deduction mechanisms can be set up.	**HIA** **2007**

Recommendation 9 **Implement a Switching Code for private health insurance**	**Action By**
The Health Insurance Authority should draft a Switching Code for health insurance which would, in a brief, clear and definitive manner, detail the duties and obligations of health insurers during the switching process, as well as the rights of consumers.	**HIA** **2007**

Recommendation 10 **Provide consumers with prescribed switching information at point of sale and renewal**	**Action By**
Health insurers should be obliged by statute to provide prescribed information to consumers on their rights regarding switching and waiting periods as well as information to facilitate comparison and understanding of products and of their rights as consumers. Following consultation between the Health Insurance Authority, the insurers and others (e.g. National Consumer Agency), a prescribed format of documentation should be drawn up. Each insurer should be responsible for providing this documentation to consumers at point of sale and at renewal time. In the interim period, PHI firms should distribute the HIA's current pamphlet on consumer rights with renewal notices. This pamphlet should be replaced by the 'new' documentation when it is ready.	**HIA** **Health Insurers** **Annually** **Minister for Health and Children**

Recommendation 11 **Vhi Healthcare should cease cancelling travel insurance policies where a customer switches from Vhi Healthcare to another health insurer**	**Action By**
Vhi Healthcare should cease automatically cancelling the Vhi Healthcare MultiTrip travel insurance policies of customers who switch their PHI policy from Vhi Healthcare to another health insurer. Vhi MultiTrip travel insurance policies should remain active until the policy expiry date. Vhi Healthcare should be obliged to cover any claims which fall under the 'travel' element of the insurance policy, while the consumer's new health insurer should be obliged to cover any claims which fall under the consumers' health insurance policy. This recommendation would also apply to other health insurers should they decide to sell travel insurance products which are conditional on having private health insurance with them.	**Vhi Healthcare** **2007**

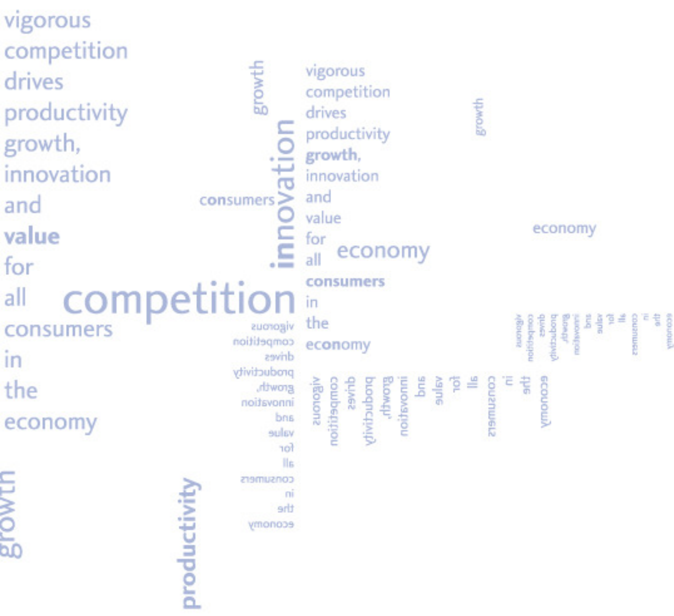
Recommendation 12 **The Minimum Benefit Regulations should be simplified and updated**	**Action By**
The Minister for Health and Children should amend the *Health Insurance Act, 1994 (Minimum Benefit) Regulations, 1996* in order to accomplish the following goals: • Simplify the system of minimum benefits • Remove restrictions on the PHI products which health insurers can offer, while maintaining an obligation to provide a certain minimum level of healthcare cover to any individual covered by a health insurance contract • Remove the fixed minimum monetary values • Specify benefits to be covered in non-monetary terms, if possible	**Minister for Health and Children**

Recommendation 13 **The Health Insurance Authority should be allowed to approve limited-cover plans**	**Action By**
If limited cover plans are found to be feasible and compliant with relevant legislation and with community rating, the Minister should amend the *Health Insurance Act, 1994 (Minimum Benefit) Regulations, 1996* to give the Health Insurance Authority responsibility for approving limited-cover plans proposed by health insurers. The key criterion for regulatory authorisation should be whether any such product could undermine community rating in the PHI market.	**Minister for Health and Children**

Recommendation 14 **The likely effect of the Health Status Weight on the scope for price competition in the market should be taken into account when investigating its introduction**	**Action By**
When investigating the introduction of the HSW the HIA, in addition to concluding that the material difference 'wholly or substantially' is attributed to variations in health status rather than efficiencies, should also take into account any likely effect that raising the HSW will have on scope for price competition in the market.	**Health Insurance Authority**

Recommendation 15 **Undertake a cost benefit analysis of moving to a prospective Risk Equalisation system**	**Action By**
Undertake a full cost benefit analysis of what would be required to move to a prospective Risk Equalisation system.	**Health Insurance Authority**

Recommendation 16 **Clarify eligibility for Risk Equalisation payment exemptions**	**Action By**
Legislation should be brought forward clarifying what type of companies are eligible for the limited exemption from the requirement to make returns and otherwise comply with the Risk Equalisation Scheme.	**Minister for Health and Children**



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