



14 May 2020

TO: ALL PRIVATE HEALTH INSURERS

COVID-19: PRUDENT CONSIDERATIONS RELATED TO DISRUPTION OF HEALTH SERVICES

This letter sets out APRA's expectations for private health insurers given the current economic and social impacts of COVID-19, including APRA's views on the application of the capital framework.

COVID-19 has fundamentally altered the economic outlook in Australia and globally. Beyond the current sharp contraction in activity, the outlook for the local and global economy is highly uncertain and there are material downside risks that could well extend far beyond the immediate health crisis. The need for private health insurers, and the financial system in general, to be sufficiently resilient to withstand current and future stresses is therefore critical.

Private health insurers have an important role to play in supporting the wellbeing of their policyholders. Private health insurers should support their policyholders' access to medical services and respond appropriately to customers facing hardship. APRA acknowledges the announcements made by private health insurers to support policyholders to-date.

APRA is liaising with other government bodies, including the Department of Health (DoH) and the Australian Competition and Consumer Commission (ACCC), on the effects of COVID-19 on the industry. DoH has recently written to private health insurers seeking information to monitor the implementation of undertakings to policyholders.

APRA acknowledges that private health insurers are particularly affected by uncertainty around the impact of actions to suspend certain elective surgeries, and disruption to general medical services from social distancing measures. APRA recognises that timeframes for resumption of medical services, the level of policyholder demand and capacity within the medical system as restrictions are lifted are also uncertain. These considerations are critical for private health insurers in calculating their Capital Adequacy Requirement and conducting liability valuations for financial statements.

Over recent years, APRA has expressed increasing concern that factors affecting the sustainability of private health insurers are becoming more acute. The impacts of COVID-19 may intensify the risks posed to insurers by the twin challenges of declining affordability and adverse selection.

Although claims are expected to be reduced in the short term, the prudential soundness of private health insurers will depend on claims over the medium and longer term. APRA expects private health insurers to demonstrate how they have considered a medium-term view (over 6-18 months) of the risks that are posed to profitability, solvency and membership as services resume. It is vital that private health insurers are prudent in their approach to determining claims volumes and timing to ensure that the industry remains prudently capitalised and can continue to meet its commitments to policyholders.

Private health insurers may experience a catch-up period in claims as the resumption of services expands. In light of this, APRA expects that private health insurers will consider how procedures deferred from the current period may result in a higher volume of claims in future periods. In completing June 2020 Financial and Capital returns, APRA expects private health insurers to demonstrate how they have considered the uncertainty caused by the disruption of COVID-19 to policyholder's access to health services.

Private health insurers and their auditors should consider guidance published by ASIC¹ on the financial reporting and audit implications of COVID-19. FAQ #6 of ASIC's guidance specifically addresses the accounting treatment by private health insurers for a backlog of procedures.

APRA also expects private health insurers will demonstrate their consideration of other risks that arise due to COVID-19 in determining their Capital Adequacy Requirement as at 30 June 2020. Relevant risks would include the unknown timing for future procedures and resumption of services, likely changes to premiums, expected costs of the various financial relief measures insurers have publicly announced and the risks posed by changes in membership numbers and demographics due to economic pressures.

In light of the economic uncertainty caused by COVID-19 and the specific impact on health services leading to heightened uncertainty for private health insurance business, APRA anticipates an increase in the Capital Adequacy Requirement for private health insurers. Consistent with the matters set out in this letter, and ASIC's guidance, APRA expects private health insurers will carefully consider both the immediate period and a longer-term impact of a backlog of procedures on projections of profitability; and the level of uncertainty related to any projections or estimates.

APRA will continue to engage with industry and other stakeholders to understand the timeframes and likely claims patterns as the resumption of medical services expands, to ensure the impacts of any backlog are prudently managed. Where APRA considers private health insurers have not undertaken a prudent calculation of the Capital Adequacy Requirement, it will consider prudential capital adjustments to ensure sound capital positions for the protection of policyholders.

This letter should be shared with all board members.

If you have any questions on matters raised in this letter, please contact your APRA supervisor.

Yours sincerely

Geoff Summerhayes
Executive Board Member

¹ <https://asic.gov.au/regulatory-resources/financial-reporting-and-audit/covid-19-implications-for-financial-reporting-and-audit-frequently-asked-questions-faqs/#q6>