The Auditor-General
Audit Report No.42 2005–06
Performance Audit

Administration of the 30 Per Cent Private Health Insurance Rebate Follow-up Audit

Australian Taxation Office
Department of Health and Ageing
Medicare Australia

Australian National Audit Office

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Canberra ACT
25 May 2006

Dear Mr President
Dear Mr Speaker

The Australian National Audit Office has undertaken a performance audit in the Australian Taxation Office, Department of Health and Ageing, and Medicare Australia in accordance with the authority contained in the *Auditor-General Act 1997*. I present the report of this audit and the accompanying brochure to the Parliament. The report is titled *Administration of the 30 Per Cent Private Health Insurance Rebate Follow-up Audit.*

Following its tabling in Parliament, the report will be placed on the Australian National Audit Office's Homepage—http://www.anao.gov.au.

Yours sincerely

Steve Chapman
Acting/Auditor-General

The Honourable the President of the Senate
The Honourable the Speaker of the House of Representatives
Parliament House
Canberra ACT

AUDITING FOR AUSTRALIA

The Auditor-General is head of the Australian National Audit Office. The ANAO assists the Auditor-General to carry out his duties under the *Auditor-General Act 1997* to undertake performance audits and financial statement audits of Commonwealth public sector bodies and to provide independent reports and advice for the Parliament, the Government and the community. The aim is to improve Commonwealth public sector administration and accountability.

For further information contact:
The Publications Manager
Australian National Audit Office
GPO Box 707
Canberra ACT 2601

Telephone: **(02) 6203 7505**
Fax: **(02) 6203 7519**
Email: **webmaster@anao.gov.au**

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Audit Team

Wendy Michaels
Andrew Morris
Fran Holbert

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Abbreviations

ANAO	Australian National Audit Office
ATO	Australian Taxation Office
Finance	Department of Finance and Administration
Health	Department of Health and Ageing
Health fund	Registered Health Benefits Organisation
HIC	Health Insurance Commission, the predecessor organisation to Medicare Australia
IMAS	Information Matching and Analysis System
IPS	Incentive Payments Scheme
IT	Information Technology
PBS	Portfolio Budget Statements
PHIAC	Private Health Insurance Administration Council
PHIIA	*Private Health Insurance Incentives Act 1998*
PHIIS	Private Health Insurance Incentive Scheme
PRS	Premiums Reduction Scheme
Rebate	30 Per Cent Private Health Insurance Rebate
REP	30 Per Cent Rebate Enhancement Project conducted between March and September 2003 in what is now Medicare Australia
SLA	Service Level Agreement
SSPA	Schedule to the Strategic Partnership Agreement

Summary and Recommendations

Summary

Background

1. The Australian Government subsidises the cost of private health insurance premiums for Australians. The subsidy is a financial incentive designed to make private health insurance more affordable and support the mix of public and private health care that makes up Australia's health care system.

2. The Government introduced a 30 Per Cent Private Health Insurance Rebate (the Rebate) on 1 January 1999.[1] The Rebate provides for a reimbursement, or discount, of 30 per cent of the cost of private health insurance cover, and is available to all Australians who are eligible for Medicare and who are members of a registered[2] health benefits organisation (health fund)—regardless of their level of private health insurance cover, income or type of membership.

3. The 31 March 2006 quarterly figures from the Private Health Insurance Administration Council reported that Australia's 38 health funds provided over 10 million Australians with private health insurance cover (43.1 per cent with hospital cover). In the first few years after 1 January 1999, the proportion of the Australian population with private health insurance (hospital cover) increased by more than ten percentage points, but has remained relatively stable in recent years.

4. The Government's investment in the Rebate since 1999–2000 has almost doubled, with government agencies involved in administering the Rebate expecting expenditure to exceed $3 billion in 2005–06.

5. Three Australian Government agencies are involved in the administration of the Rebate. The Department of Health and Ageing (Health) determines private health insurance policy and the Australian Taxation Office (ATO) and Medicare Australia administer the Rebate in accordance with the *Income Tax Assessment Act 1997* and the *Private Health Insurance Incentives Act 1998*, respectively. In 2004–05, Medicare Australia made over 94 per cent of the total Rebate payments (amounting to approximately $2.7 billion).

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[1] Changes to the *Private Health Insurance Incentives Act 1998*, introduced from 1 April 2005, increase the Rebate from 30 per cent to 35 per cent for people aged 65 to 69 years, and to 40 per cent for people aged 70 years and over.

[2] A fund registered under Part IV of the *National Health Act 1953*.

6. The Australian National Audit Office (ANAO) audited the administration of the Rebate in 2001–02 in order to assess the effectiveness of Australian Government agencies' administration of the Rebate. Audit Report No.47 2001–02, *Administration of the 30 Per Cent Private Health Insurance Rebate*, made six recommendations addressing: Federal Budget estimates; financial controls; and performance information for the Rebate. Agencies agreed with all of the recommendations with the exception of Recommendation No.6, which Health agreed to with qualification.

7. Given the magnitude of the Australian Government's expenditure under the Rebate, and the widespread access to the Rebate in the Australian community, the ANAO conducted a follow-up on agencies' implementation of the 2001–02 audit report recommendations.

Follow-up audit objective

8. The follow-up audit assessed the extent to which the ATO, Health and Medicare Australia had implemented the six recommendations from the 2002 audit. The audit also looked at:

- the implementation of some of the major suggestions for improvement in the original audit; and
- the current validity of some of the positive major findings from the original audit.

9. The ANAO wrote to the ATO, Health and Medicare Australia when the follow-up audit started, requesting their initial assessment of the implementation status of the original audit recommendations, and evidence supporting those assessments.

10. The ANAO's methodology for the audit then involved the audit team interviewing relevant staff in the three agencies and analysing relevant agency files and documents. The ANAO met with the Private Health Insurance Administration Council, the Private Health Insurance Ombudsman, and the Australian Health Insurance Association (industry representative body). The ANAO also conducted telephone interviews with three health funds. The majority of the audit fieldwork was carried out between September and December 2005.

Overall conclusion

11. The ANAO concluded that the ATO, Health and Medicare Australia have acted upon the recommendations contained in Audit Report No.47 2001–02 and, overall, the administration of the Rebate is currently being undertaken effectively.

12. The ANAO was informed that, in 2003, Medicare Australia spent $501 000 on a seven month project to address the recommendations of the previous ANAO audit and worked with the ATO and Health on implementing the joint recommendations.

13. Table 1 summarises the ANAO's assessment of agencies' progress in implementing the six recommendations made in 2002. The ANAO found that three of the recommendations have been fully implemented, and the other three substantially completed. The relevant agencies are continuing to work towards full implementation of the three recommendations that have been substantially completed.

Table 1

Summary of ANAO's 2006 assessment of agencies' progress in implementing recommendations from Audit Report No.47 2001–02

Audit Report No.47 2001–02 recommendations[A]	ANAO assessment of the implementation status in 2006	Reference in this report
Recommendation No.1 To ensure that Health's budget estimates in relation to the Private Health Insurance Rebate continue to be soundly based, the ANAO recommends that Health review its budget estimates approach with a view to effectively utilising available data relating to private health insurance premium growth and participation.	**Fully implemented**	**Chapter 4** Para. 4.8
Recommendation No.2 The ANAO recommends that the Health Insurance Commission (HIC)[B] review its Premiums Reduction Scheme (PRS) registration procedures to ensure that: (a) they comply with the *Private Health Insurance Incentives Act 1998*; (b) all eligible PRS applicants are registered; and (c) health funds are fully informed of their responsibilities in respect of the registration process.	**(a) Fully implemented** **(b) Fully implemented** **(c) Fully implemented**	**Chapter 2** Para. 2.7 Para. 2.12 Para. 2.15
Recommendation No.3 The ANAO recommends that HIC ensure arrangements for PRS reimbursements have adequate financial controls, including: (a) requiring health funds to support their claims with data on the policy details of each health fund member for whom a PRS reimbursement is claimed (line-by-line data); (b) implementing pre- and post- payment checks and a systematic audit programme to help ensure the validity and accuracy of claims, with post-payment checks conducted on a timely basis; and	**(a) Fully implemented** **(b) Substantially implemented**	**Chapter 2** Para. 2.22 **Chapter 2** Para. 2.50

Audit Report No.47 2001–02 recommendations[A]	ANAO assessment of the implementation status in 2006	Reference in this report
(c) undertaking reconciliations of PRS payments made in 1998–99, 1999–2000 and 2000–01 against line-by-line data to provide assurance that health funds have correctly calculated their PRS reimbursement claims, identify claiming irregularities that require further investigation, and assist HIC in targeting future audit activity.	**(c) Fully implemented**	**Chapter 2** Para. 2.72
Recommendation No.4 Pending any change in policy and related legislation for the Incentive Payments Scheme, the ANAO recommends that HIC strengthen financial controls surrounding the Scheme.	**Fully implemented**	**Chapter 3** Para. 3.31
Recommendation No.5 The ANAO recommends that HIC and ATO review their data exchange arrangements to ensure that ATO obtains timely access to the data it requires to undertake adequate data matching checks for inappropriate multiple claiming under the Private Health insurance Rebate.	**Substantially implemented**	**Chapter 3** Para. 3.65
Recommendation No.6 The ANAO recommends that Health and HIC develop clear performance indicators and standards in relation to Private Health Insurance Rebate payment accuracy by HIC (i.e. the extent to which eligible people receive a rebate of the correct amount).	**Substantially implemented**	**Chapter 4** Para. 4.26

Note: (A) Agencies agreed with all of the 2001–02 audit report recommendations with the exception of Recommendation No.6, which Health agreed to with qualification.

(B) At the time of the 2001–02 audit, Medicare Australia was known as the Health Insurance Commission (HIC).

Source: ANAO analysis.

Key findings

Premiums Reduction Scheme Administration (Chapter 2)

Premiums Reduction Scheme registration procedures (Original Recommendation No.2)

14. The original audit found that Medicare Australia was not complying with some parts of the *Private Health Insurance Incentives Act 1998* (PHIIA) for Premiums Reduction Scheme (PRS) registration notifications and variations.[3] This meant that Medicare Australia was not able to enforce the Rebate eligibility criteria set out in the PHIIA. The ANAO concluded, however, that given the broad nature of the eligibility criteria, the total payment to ineligible persons was unlikely to have been material in financial statement terms.

15. The ANAO's follow-up audit in 2005–06 found that Medicare Australia has fully implemented Recommendation No.2 of the original audit as:

- the agency's current PRS registration processes comply with relevant sections of the PHIIA;
- eligible PRS applicants are being registered; and
- health funds are fully informed of their responsibilities in respect of the registration process.

Premiums Reduction Scheme reimbursements to health funds (Original Recommendation No.3)

16. The ANAO found in the 2001–02 audit that a number of weaknesses existed with Medicare Australia's pre-payment checks and only very limited post-payment reconciliation checks were in place for PRS reimbursements to health funds. This finding gave little assurance that health funds were correctly calculating their PRS claims for reimbursement. The ANAO concluded that the shortcomings with the PRS registration processes and database affected Medicare Australia's financial controls for the PRS pre- and post-payment checks and audit and compliance activity.[4]

17. The ANAO's follow-up audit in 2005–06 found that Medicare Australia now has generally adequate financial controls for PRS reimbursements, as Medicare Australia:

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[3] Australian National Audit Office 2002, *Administration of the 30 Per Cent Private Health Insurance Rebate*, Audit Report No.47 2001–02, ANAO, Canberra, p. 14. This report is referred to as the 'original audit' in the current audit.

[4] Australian National Audit Office, op. cit., p. 41 and pp. 50–51.

- requires health funds to support their Rebate claims for each health fund member with line-by-line data;
- has implemented a range of pre- and post-payment checks and a systematic audit programme; and
- undertook adequate reconciliations of PRS payments made in the period January to June 1999, and the 1999–2000 and 2000–01 financial years against line-by-line data. In addition, the monthly reconciliations of PRS payments against line-by-line data Medicare Australia introduced for subsequent financial years have strengthened the financial control framework for PRS payments.

18. However, the ANAO has also identified a number of areas within the PRS reimbursement process where Medicare Australia could further improve its financial controls. In particular, the ANAO recommends that Medicare Australia should further treat the risk of overpayments to health funds, resulting from health fund members' dishonoured premium payments, by reviewing and updating a number of the current control mechanisms (see Recommendation No.1, paragraph 2.38).

19. Overall, the ANAO considers that Medicare Australia has substantially completed implementing Recommendation No.3 of the original audit.

Incentive Payments Scheme and Tax Offset Administration (Chapter 3)

Incentive Payments Scheme administration (Original Recommendation No.4)

20. The 2001–02 audit found that Medicare Australia assessed the risks[5] and adequacy of the financial controls for the Incentive Payments Scheme (IPS), but did not take action for some time to address these issues because of the relatively low total value of the IPS payments and the possibility that the IPS option would be abolished on cost-benefit grounds. However, in 2000 Medicare Australia did recover funds from individuals for incorrect IPS payments. At the time, the ANAO concluded that the financial controls for the IPS could be further strengthened by Medicare Australia.

21. The ANAO's follow-up audit in 2005–06 found that Medicare Australia adequately administers the IPS, as it:

[5] A December 1998 Medicare Australia risk assessment concluded that there was a high/very high risk of forged health fund receipts; multiple payments; and payments for ineligible policies. There was also a risk that double dipping would occur by claiming through the IPS and the Tax Offset or PRS Rebate options. Australian National Audit Office, op, cit., p. 54.

- has introduced a pre-payment control linking the IPS claims system to PRS data held in the same system;
- has revised the format and introduced a certification process for health funds' IPS receipts; and
- is providing adequate training to Medicare operators processing IPS payments.

22. Therefore, the ANAO considers that Medicare Australia has fully implemented Recommendation No.4 of the original audit.

Data matching between Medicare Australia and the ATO (Original Recommendation No.5)

23. The ATO relies on data provided by Medicare Australia and the health funds to identify incorrect Rebate Tax Offset claims. Medicare Australia is required to provide annual line-by-line data to the ATO by 28 September each year. The ATO requires health funds to provide line-by-line data for each financial year by 30 November.

24. The original audit found that Medicare Australia did not comply with s. 19–15 of the PHIIA, which required it to provide the ATO with the data necessary for the ATO to conduct adequate data matching checks.[6] Initially, this was because the legislation did not permit Medicare Australia to obtain relevant data from health funds in order for Medicare Australia to comply with s. 19–15. After December 1999, the legislation was amended to require health funds to provide this data. However, Medicare Australia decided not to implement the systems necessary to provide the ATO with the data prescribed in s. 19–15. An effect was that for the Rebate's first two and a half years, arrangements were not adequate to detect people inappropriately claiming the Rebate through more than one delivery channel.

25. The original audit suggested that Medicare Australia and the ATO should investigate the scope for streamlining the exchange of data between health funds and Australian Government agencies to reduce the administrative burden on health funds.

26. The ANAO considers that Medicare Australia and the ATO have substantially completed implementing Recommendation No.5 of the original audit. The two agencies have agreed data exchange protocols that provide the ATO with access to the data necessary to detect inappropriate Rebate claims.

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6 Australian National Audit Office, op. cit., p. 19.

27. However, the data exchange protocols require health funds to provide data to both Medicare Australia and the ATO, but this might not be providing a net benefit to the Australian Government. Furthermore, the ATO's main compliance tool used to identify potential overpayments associated with the Rebate excluded many potential audit cases in 2002–03 because the data supplied to the ATO by Medicare Australia was different to the data provided to the ATO by the health funds.

28. The ANAO also considers that it is important that the ATO proceeds with planned refinements of the business rules affecting its compliance processing of the Rebate to improve debt identification in subsequent years. Consequently, the ANAO recommends that Medicare Australia and the ATO resume discussions about streamlining data collection (see Recommendation No.2, paragraph 3.59).

Budget Estimates and Performance Information for the Rebate (Chapter 4)

Budget estimates of the Rebate (Original Recommendation No.1)

29. The original audit found that Health adopted a reasonable approach to preparing Rebate Federal Budget estimates. Health's assumptions were reasonable and based on an adequate level of analysis.[7]

30. However, the audit noted that with the accumulation of data on the impact of Lifetime Health Cover,[8] Health was in a position to enhance its estimates model through an analysis of the factors underlying private health insurance premium growth (including health funds' income and costs and Medicare hospital statistics), trends in private health insurance participation among different demographic groups post-Lifetime Health Cover, and the relationship between private health insurance premium growth and participation rates.

31. The ANAO considers that Health has fully implemented Recommendation No.1 of the original audit given that Health has extensively reviewed its Budget estimates methodology, trialling various models that included the available private health insurance data. However, in the end, the

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7 Australian National Audit Office, op. cit., pp. 16–17.

8 Lifetime Health Cover is an Australian Government initiative that started on 1 July 2000 and was designed to encourage people to take out hospital insurance earlier in life, and to maintain their cover. People who delay taking out hospital cover will pay a two per cent loading on top of their private health insurance premium for every year they are aged over 30 when they first take out hospital cover. See the Department of Health and Ageing website for more details at <http://www.health.gov.au>.

existing model proved more accurate than the revised models and was retained by Health. This model proved to be reasonably accurate for most years since the original audit, but considerably underestimated Rebate costs in 2004–05. Health is continuing to work with Finance to improve the accuracy of the model.

Performance indicators of Rebate payment accuracy (Original Recommendation No.6)

32. The original audit assessed the adequacy of performance information for the Rebate. It found that Health developed a sound basis for assessing Medicare Australia's, and the ATO's, overall administrative performance for both internal management and external reporting purposes.[9]

33. While overall performance information was considered sound, the original audit found that the claim processing accuracy indicator for Medicare Australia did not appropriately address accuracy. Above all, the Schedule for the Rebate under the Strategic Partnership Agreement did not provide clear standards in relation to the accuracy of processing by Medicare Australia (that is, paying the correct person the correct amount).

34. The original audit also noted that the performance indicators in the Health-ATO agreement were adequate given the respective roles and responsibilities of the agencies. As reported in the original audit, the ATO indicators were, however, inadvertently omitted from Health's *2001–02 Portfolio Budget Statements* (PBS). Health intended to include broad agency performance measures, consistent with measures set out in Health's Service Level Agreement with the ATO, in the next Health Annual Report and PBS.

35. The ANAO's follow-up audit in 2005–06 found that Health and Medicare Australia have substantially completed Recommendation No.6 of the original audit.

[9] Australian National Audit Office, op. cit., p. 21.

Recommendations

36. The ANAO identified further opportunities for improvement in agencies' administration of the Rebate and made two recommendations that address improving:

- the ATO's and Medicare Australia's data exchange arrangements; and
- Medicare Australia's risk management and audit programme for the Rebate.

Agency responses

Australian Taxation Office

37. The Second Commissioner of Taxation provided the following summary response to the audit findings.

> The Tax Office agrees with the recommendation.
>
> Recent work with Medicare Australia, regarding data exchange requirements for the Private Health Insurance Rebate, indicates that the need for health funds to provide data to both the Tax Office and Medicare Australia could be removed with effect from the 2006–07 year.
>
> Subject to Medicare Australia including some additional information currently provided by the health funds and the health funds agreeing to this process, the requirement for health funds to provide the information to the Tax Office will be removed.

Department of Health and Ageing

38. The Secretary of the Department of Health and Ageing provided the following summary response to the audit findings.

> The Department of Health and Ageing welcomes the findings of the ANAO follow-up audit, in particular the overall finding that the administration of the rebate is currently being undertaken effectively.
>
> The report confirms that the recommendation from the earlier audit report, *Administration of the 30 Per Cent Private Health Insurance Rebate* (Audit Report No.47, 2001–02), that the Department review its budget estimates approach for the rebate, has been fully implemented.
>
> The earlier audit report recommended that the Department and the HIC (now Medicare Australia) develop clear performance indicators and standards in relation to the rebate payment accuracy. The Department agrees with the

current report's finding that the performance indicator agreed between the Department and Medicare Australia, as part of the Business Practice Agreement (BPA), has the potential to enable both agencies to better track payment accuracy. It is anticipated that the BPA will be in place by 1 July 2006 which will then render the recommendation from the earlier report fully implemented.

Medicare Australia

39. The Chief Executive Officer of Medicare Australia provided the following summary response to the audit findings.

> Medicare Australia welcomes the assurance provided by the ANAO that Medicare Australia has acted upon the recommendations contained in the original report and, overall, the administration of the rebate is currently being undertaken effectively. Medicare Australia agrees with the two ANAO recommendations and has taken action in response to each.

Recommendations

Recommendation No.1

Para. 2.38

The ANAO recommends that Medicare Australia further treat the risk of overpayments of the Private Health Insurance Rebate to health funds, resulting from health fund members' dishonoured private health insurance premium payments, by reviewing and updating:

(a) the Private Health Insurance Rebate's 2002 *Risk Management Plan;*

(b) the annual Private Health Insurance Rebate audit programme; and

(c) the Private Health Insurance Rebate *Processing Manual for private health funds* to include specific advice to health funds about processing refunds to Medicare Australia resulting from dishonoured premium payments.

***Medicare Australia's response*:** Agreed.

Recommendation No.2

Para. 3.59

The ANAO recommends that Medicare Australia and the Australian Taxation Office review their data exchange requirements for the Private Health Insurance Rebate, to determine the net benefit of both agencies continuing to collect annual data from the health funds. If this benefit is negative or low, the agencies should examine options to rationalise the collection of this data.

Australian Taxation Office's response: Agreed.

Medicare Australia's response: Agreed.

Audit Findings and Conclusions

1. Introduction

This chapter describes the Rebate, outlines the original audit findings and explains the follow-up audit approach.

Background

1.1 The Australian Government announced a 30 Per Cent Private Health Insurance Rebate (the Rebate) initiative as part of the *Tax Reform: not a new tax, a new tax system* package in August 1998 for introduction on 1 January 1999.[10]

1.2 The Rebate is a financial incentive aimed at: 'easing the burden on Medicare and the public health system and giving more Australians greater choice and access to private hospitals'.[11]

1.3 Table 1.1 shows the three ways to claim the Rebate, and the Australian Government agency responsible for administering each option. The Rebate can be paid in different ways during a financial year, but not for the same period of insurance cover.

Table1.1

Rebate payment options and responsible agencies

Rebate payment option	Responsible agency	Total payment in 2004–05
Premiums Reduction Scheme: Premium reduction through a private health insurance fund	Medicare Australia	$2 700 million
Tax Offset: Tax rebate in an annual tax return	Australian Taxation Office	$160 million
Incentive Payments Scheme: Direct payment from Medicare offices	Medicare Australia	$2.3 million

Source: Department of Health and Ageing, and Medicare Australia, 2005.

1.4 All Australians who are eligible for Medicare and who are members of a registered health benefits organisation (health fund) are eligible for the

[10] For every dollar an individual contributes to their private health insurance premium, the Australian Government returns 30 cents. Changes to the *Private Health Insurance Incentives Act 1998*, introduced from 1 April 2005, increase the Rebate from 30 per cent to 35 per cent for people aged 65 to 69 years, and to 40 per cent for people aged 70 years and over.

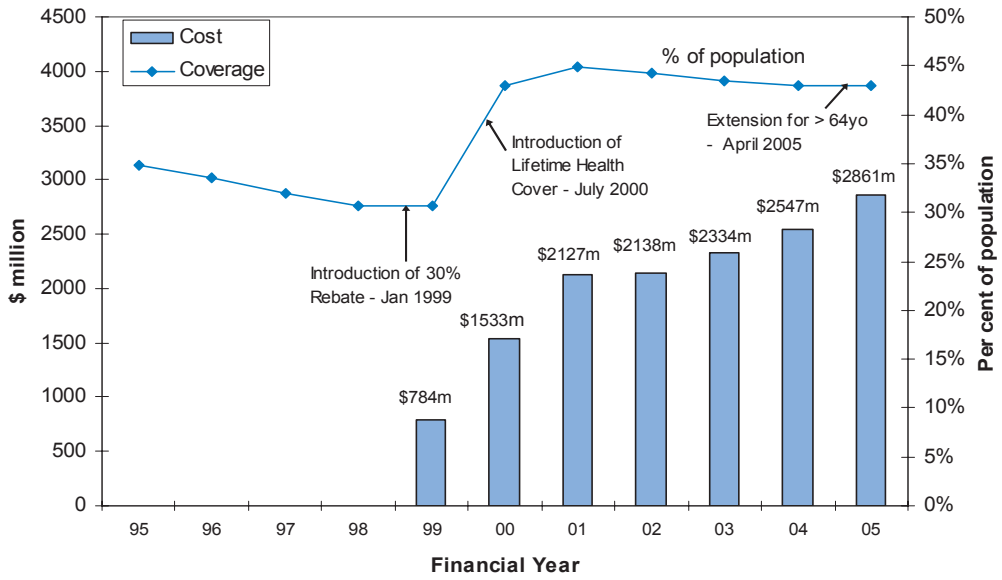
[11] Department of Health and Ageing, *Building a healthier system* [Internet]. Department of Health and Ageing, Canberra, 2004, available from <http://www.health.gov.au> [accessed 21 July 2005].

Rebate. In May 2006, 38 health funds operated in Australia, with over ten million Australians covered by some form of private health insurance. The six largest health funds accounted for nearly 80 percent of the national coverage.

1.5 Figure 1.1 shows the percentage of Australians with private health insurance hospital cover and the total amount of Rebate payments made to health funds by the Government over the period 1999 to 2005.

Figure 1.1

Private health insurance hospital coverage and Australian Government Rebate payments to the health funds, 1995 to 2005 financial years



Source: Department of Health and Ageing, and Private Health Insurance Administration Council, 2005.

1.6 In the first few years after 1 January 1999, the proportion of the Australian population with private health insurance (hospital cover) increased by more than ten percentage points, but has since remained relatively stable in recent years. The Australian Government's investment in the Rebate since 1999–2000 has almost doubled, with Australian Government agencies involved in administering the Rebate expecting expenditure to exceed $3 billion in 2005–06.

The original audit

1.7 The objective of the original audit,[12] tabled in May 2002, was to determine the effectiveness of Australian Government agencies' administration of the Rebate. The audit scope included examining the Federal Budget estimates process, financial controls, roles and responsibilities of the agencies and performance information. The agencies involved in the original audit were: the ATO, Department of Finance and Administration (Finance), Health, the Health Insurance Commission (HIC)[13] and the Department of the Treasury.

Original audit conclusions

1.8 The ANAO concluded that, faced with the complexity and significant scale of the task of implementing the Rebate, the agencies had implemented the scheme in time to allow eligible persons to receive the Rebate from the Australian Government's announced commencement date of 1 January 1999. The HIC had only six weeks to implement systems to support the Rebate, while the ATO had only a few days to draft legislative amendments required to support the premium reduction option.

1.9 The original audit made six recommendations, covering Budget estimates, financial controls and performance information. The HIC and the ATO agreed to implement the recommendations relevant to them, as did Health with the exception of one that the Department 'agreed with qualification'.[14]

The follow-up audit

Audit objective

1.10 The objective of the follow-up audit was to assess the extent to which the ATO, Health and Medicare Australia have implemented the recommendations from the original audit. The audit also looked at the

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[12] Australian National Audit Office 2002, *Administration of the 30 Per Cent Private Health Insurance Rebate*, Audit Report No.47 2001–02, ANAO, Canberra, p. 13. This report is referred to as the 'original audit' in the current audit.

[13] Direct references to the original audit use the name 'Health Insurance Commission' (HIC). However on 1 October 2005 the HIC became a prescribed agency under the *Financial Management and Accountability Act 1997* and a statutory agency under the *Public Service Act 1999*, under the Department of Human Services. On that date, the HIC was also renamed 'Medicare Australia' and performs all the functions and provides all the services that were performed by the HIC. The agency's new name is used throughout the follow-up audit where appropriate.

[14] Recommendation No.6, relating to improving performance monitoring and reporting.

implementation of some of the major suggestions for improvements from the original audit and the current validity of some of the positive major findings made in that audit.

Audit methodology

1.11 The ANAO wrote to the ATO, Health and Medicare Australia when the follow-up audit started, requesting their initial assessment of the implementation status of the original audit recommendations, and evidence supporting those assessments.

1.12 The ANAO then interviewed relevant staff in the agencies and analysed relevant agency files and documents. The ANAO met with the Private Health Insurance Administration Council, the Private Health Insurance Ombudsman, and the Australian Health Insurance Association (industry representative body). The ANAO also conducted telephone interviews with three health funds. The majority of the audit fieldwork was carried out between September and December 2005.

1.13 The audit considered the findings of Audit Report No.20 2005–06 *Regulation of Private Health Insurance by the Private Health Insurance Administration Council*. Additionally, the audit took into account the introduction of a 35 and 40 per cent Rebate in 2005 and the establishment of the Department of Human Services on 26 October 2004,[15] and the transition of the

[15] In October 2004, the Finance and Administration Portfolio was expanded through the creation of a new Department of Human Services, which brought together six agencies that in total administer $80 billion of human services each year. Medicare Australia is one of the six agencies. Matters dealt with by the Department include monitoring and management of service delivery relationships involving Medicare Australia. In announcing the creation of the Department of Human Services, the Prime Minister, the Hon John Howard MP, said: 'The new department will ensure that the development and delivery of government services is placed under strong ministerial control with clear lines of responsibility through the Secretary. The new department will ensure that the Government is able to get the best value for money in delivery with an emphasis on continuous service improvement and a whole of government approach.' Available from <http://www.pm.gov.au/news/media_releases/media_Release1134.html>, Media release, 22 October 2004 [accessed 24 March 2006].

HIC into Medicare Australia as part of the Australian Government's response to the Uhrig Report.[16]

1.14 The audit was conducted in accordance with ANAO auditing standards at a cost to the ANAO of $290 000.

Acknowledgements

1.15 The ANAO would like to thank Medicare Australia's management and staff for the high level of professional support and cooperation provided to the ANAO throughout the audit process. Medicare Australia staff were involved in implementing five of the six audit recommendations from 2002. The ANAO would also like to express appreciation to the ATO and Health for their contribution to the audit.

Structure of report

1.16 The three remaining chapters in this report are as follows:

- Chapter 2: Premiums Reduction Scheme Administration;
- Chapter 3: Incentive Payments Scheme and Tax Offset Administration; and
- Chapter 4: Budget Estimates and Performance Information for the Rebate.

[16] In November 2002, the Australian Government appointed Mr John Uhrig AC to identify ways in which corporate governance might be improved and to provide the Government with options for increasing accountability and ensuring high levels of performance. The Government released its response to the Uhrig Report, *Review of the Corporate Governance of Statutory Authorities and Office Holders*, on 12 August 2004. As part of the implementation of the Government's response to the Uhrig Report, the *Human Services Legislation Amendment Act 2005*, amended the *Health Insurance Commission Act 1973* and established Medicare Australia, to replace the Health Insurance Commission (HIC). While the HIC was established with a governance board and covered by the *Commonwealth Authorities and Companies Act 1997*, Medicare Australia became a prescribed Agency under the *Financial Management and Accountability Act 1997*, and a statutory agency under the *Public Service Act 1999*, on 1 October 2005, without a governance board.

2. Premiums Reduction Scheme Administration

This chapter examines agencies' progress in implementing recommendations made by the ANAO in the original audit for the Premiums Reduction Scheme (PRS) option of the Rebate. The original audit recommended that agencies give priority to implementing these recommendations. Recommendation No.2 focused on the PRS registration procedures and Recommendation No.3 on PRS financial reimbursements to health funds.

30 Per Cent Rebate Enhancement Project

2.1 Medicare Australia's major response to the original audit was a *30 Per Cent Rebate Enhancement Project* (REP), which started in March 2003 and finished in September 2003 at a total cost of $501 000. The REP contained eight objectives designed to improve the administration of the PRS and IPS. Medicare Australia developed the objectives in consultation with the major Rebate stakeholders[17] and created a separate project for each objective.

2.2 Medicare Australia's *Post-Implementation Review* of the REP project management process and a *Project Closure Report*, both completed in September 2003, concluded that the REP had met its objectives. Medicare Australia has not formally evaluated the Rebate systems since this time.

2.3 The success of the REP largely determines the status of implementation of Recommendation No.s 2–4 of the original audit, which are assessed in this chapter and Chapter 3. Therefore, this chapter closely examines the success of the REP in meeting its objectives.

Premiums Reduction Scheme registration procedures

Findings of the original audit

2.4 The original audit found that Medicare Australia was not complying with some parts of the *Private Health Insurance Incentives Act 1998* (PHIIA) for PRS registration notifications and variations.[18] This meant that Medicare

[17] The major Rebate stakeholders consulted by Medicare Australia were: health funds; health funds' software providers; the ATO; Health; the Private Health Insurance Administration Council; and the Australian Health Insurance Association.

[18] Australian National Audit Office, op. cit., p. 14.

Australia was not able to enforce the Rebate eligibility criteria set out in the PHIIA. The ANAO concluded at the time that, given the broad nature of the eligibility criteria, the total payment to ineligible persons was unlikely to have been material in financial statement terms.

Original Recommendation No.2

The ANAO recommends that HIC [Medicare Australia] review its Premiums Reduction Scheme registration procedures to ensure that:

(a) they comply with the *Private Health Insurance Incentives Act 1998*;

(b) all eligible Premiums Reduction Scheme applicants are registered; and

(c) health funds are fully informed of their responsibilities in respect of the registration process.

Original HIC [Medicare Australia] response: The HIC [Medicare Australia] **agreed** with the recommendation. The HIC [Medicare Australia] commented that initiatives were actioned to address deficiencies noted in relation to the PRS including: setting up a working group to review the *Private Health Insurance Incentives Act 1998* and draft appropriate amendments; implementing a new claiming procedure in February 2002 to improve the PRS registration process; and informing health funds of their responsibilities at every opportunity.

Findings of the follow-up audit

Compliance with the Private Health Insurance Incentives Act 1998

2.5 Medicare Australia established a Rebate Working Group[19] in 1998 to consider potential policy, legislation and operational matters. This group considered the ANAO's original audit recommendations, including the need to comply with the requirements of the PHIIA.

2.6 Table 2.1 summarises the changes Medicare Australia made to its administration of the PRS registration process to ensure that it complies with the PHIIA. Medicare Australia implemented these changes as part of the REP.

[19] The Rebate Working Group was comprised of members from all of the major stakeholders listed at footnote 17.

Table 2.1

Medicare Australia's compliance with the registration and registration variation processes in the *Private Health Insurance Incentives Act 1998*

Section of the PHIIA	Medicare Australia's compliance in 2002	Medicare Australia's compliance in 2006	Date of effect of the change
s.11-25			
Medicare Australia notifies applicants within 14 days of a decision to refuse a registration or deeming provisions apply.[A]	✗	✓	September 2003
s.19-2(2)			
Medicare Australia notifies applicants in writing of a decision to refuse registration.	✗	✓	September 2003
s.11-45(2)			
Medicare Australia notifies health funds of variations to the registration database.	✗	✓	September 2003
s.11-5(4)			
Medicare Australia notifies health funds of new registrations.	✗	✓	September 2003

Notes: (A) Section 11-25, PHIIA, states that a person is registered if Medicare Australia does not give notice of refusal within 14 days after receiving advice from a health fund of an application for registration.

Source: ANAO Audit Report No.47 2001–02, *Administration of the 30 Per Cent Private Health Insurance Rebate*, Figure 3, p. 43, and ANAO analysis 2006.

2.7 Based on the findings listed in Table 2.1, the ANAO considers that Medicare Australia has taken reasonable steps to implement Recommendation No.2(a) of the original audit report and is now complying with the PHIIA for PRS registrations and variations.

Registering eligible applicants for the Rebate

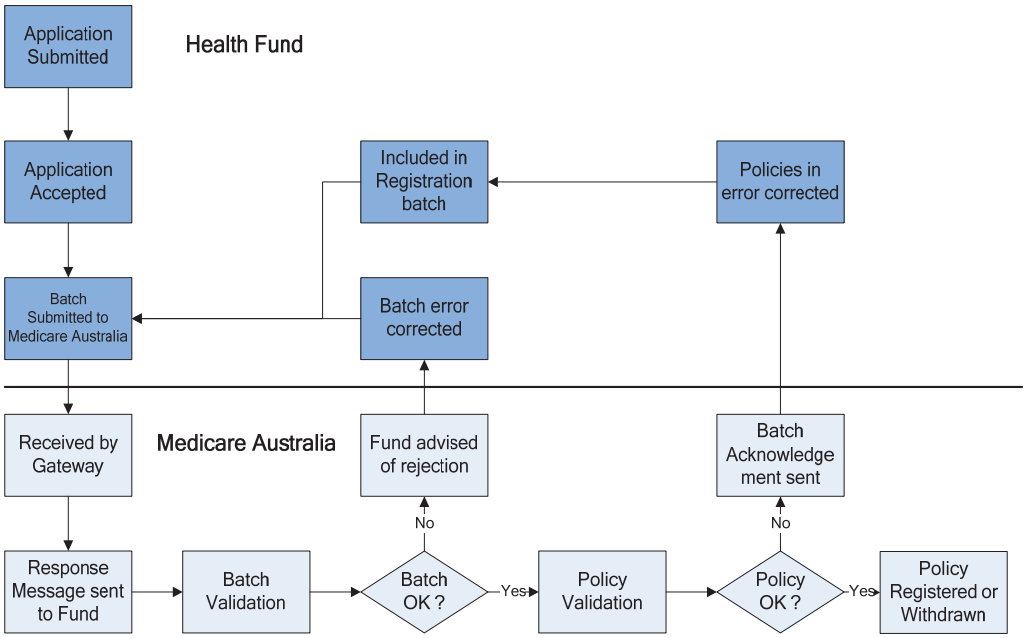
2.8 The original audit found that Medicare Australia's PRS registration database was not accurate and up-to-date.[20] As a result, Medicare Australia was not able to implement adequate controls to ensure that it was making appropriate Rebate payments.

2.9 Figure 2.1 is a diagram of the current PRS system. All registration notices confirming, rejecting or withdrawing registrations are processed and transferred automatically between the health funds and Medicare Australia.

[20] Australian National Audit Office, op. cit., pp. 43–44.

Figure 2.1

Premiums Reduction Scheme overview diagram



Source: Medicare Australia, December 2005.

2.10 Medicare Australia's usual business practice now is to do same day processing of new applications for registration, and to electronically notify health funds of a successful or unsuccessful registration within 24 hours of an application being received.

2.11 The ANAO found that, as at 1 November 2005, the PRS registration database was working, routine system checks were in place and there was no backlog of data errors waiting to be corrected by Medicare Australia. Health funds the ANAO interviewed during audit fieldwork confirmed the overall reliability of the PRS system, including its capacity to maintain an accurate registration database.

2.12 Therefore, the ANAO is satisfied that Medicare Australia is processing and registering the PRS applications sent by health funds, and so has fully implemented Recommendation No.2(b).

Informing and educating health funds

2.13 The original audit found that Medicare Australia did not adequately monitor registration processes to confirm that health funds understood and fulfilled their registration responsibilities.[21]

2.14 The ANAO found in 2005 that Medicare Australia had:

- issued health funds with several versions of a detailed Rebate *Processing Manual for private health funds*;
- held regular Rebate Working Group meetings and education seminars with health funds;
- regularly emailed advice to the health funds on technical and general Rebate matters; and
- provided Rebate Help Desk facilities from September 2003 for health funds, their members and software vendors, and Medicare branches.

2.15 The ANAO considers that Medicare Australia is taking appropriate and comprehensive steps to inform and educate health funds about their responsibilities for the PRS registration process. The ANAO, therefore, concludes that Medicare Australia has fully implemented Recommendation No.2(c) from the original audit.

Conclusion

2.16 The ANAO considers Medicare Australia has fully implemented Recommendation No.2 of the original audit as:

- the agency's current PRS registration processes comply with relevant sections of the PHIIA;
- eligible PRS applicants are being registered; and
- health funds are fully informed of their responsibilities in respect of the registration process.

[21] Australian National Audit Office, op. cit., p. 41.

Premiums Reduction Scheme reimbursements to health funds

Findings of the original audit

2.17 The ANAO found in the 2001–02 audit that a number of weaknesses existed with Medicare Australia's pre-payment checks and only very limited post-payment reconciliation checks were in place for PRS reimbursements to health funds. This finding gave little assurance that health funds were correctly calculating their PRS claims for reimbursement. The ANAO concluded that the shortcomings with the PRS registration processes and database affected Medicare Australia's financial controls for the PRS pre- and post-payment checks and audit and compliance activity.[22]

Original Recommendation No.3

The ANAO recommends that HIC [Medicare Australia] ensure arrangements for PRS reimbursements have adequate financial controls, including:

(a) requiring health funds to support their claims with data on the policy details of each health fund member for whom a PRS reimbursement is claimed (line-by-line data);[23]

(b) implementing pre- and post- payment checks and a systematic audit programme to help ensure the validity and accuracy of claims, with post-payment checks conducted on a timely basis; and

(c) undertaking reconciliations of PRS payments made in 1998–99, 1999–2000 and 2000–01 against line-by-line data to provide assurance that health funds have correctly calculated their PRS reimbursement claims, identify claiming irregularities that require further investigation, and assist HIC [Medicare Australia] in targeting future audit activity.

Original HIC [Medicare Australia] response: The HIC [Medicare Australia] **agreed** with the recommendation. The HIC [Medicare Australia] also advised that the financial controls for PRS reimbursements had been strengthened by: introducing a new monthly claiming system in February 2002 for health funds to support their claims; implementing pre- and post-payment checks and an audit programme for health funds; and conducting reconciliations for payments made to health funds in 1998–99, 1999–2000 and 2000–01.

Findings of the follow-up audit

Line-by-line data for each health fund member

2.18 Health funds claim Rebate reductions for their members monthly from the Australian Government by electronically submitting a summary claim to Medicare Australia. Medicare Australia requires health funds to send line-by-line payment details for all of the policies used in calculating the claim.

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[22] Australian National Audit Office, op. cit., p. 41 and pp. 50–51.

[23] 'Line-by-line data' refers to the health funds sending Medicare Australia a single line of data for each health fund member they are claiming a Rebate for. The single line of data contains information about the fund member and their policy details.

2.19 The line-by-line data requirement was expanded and strengthened by Medicare Australia in September 2003 as part of the REP to include details of the membership, cover and claim types.

2.20 Medicare Australia uses the monthly line-by-line data as a before and after payment reconciliation of health funds' claims. The data is electronically reconciled with the PRS registration database and used to identify any unregistered policies that health funds are claiming the rebate for.

2.21 Since the original audit, Medicare Australia has only needed to withhold a monthly payment once from a health fund because it did not meet the reporting obligations for line-by-line transmissions.

2.22 By introducing requirements for, and monitoring, line-by-line data from health funds, the ANAO considers that, Medicare Australia has met the intention of and fully implemented Recommendation No.3(a) of the original audit.

Pre-payment checks

2.23 The ANAO found that Medicare Australia has expanded its pre-payment checks and now uses examples of pre-payment checks suggested by the ANAO in the original audit, for example, checking that:

- health funds' monthly summary claims equal the sum of the individual premium reductions listed in the line-by-line data;
- health funds only claim for registered members; and
- there are no overlapping periods of cover.[24]

Post-payment checks

Risk management

2.24 Medicare Australia developed the following risk management plans for the Rebate:

- *Risk Management Plan* for the Rebate (2002); and
- *Risk Management Plan* for the REP (2003).

Additionally, Medicare Australia's *Fraud Control Plan* 2002–05 identified the misappropriation of Rebate scheme funds as having a 'high' level of risk.

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[24] Australian National Audit Office, op. cit., pp. 47–48.

2.25 However, the Rebate's *Risk Management Plan* has not been formally reviewed or updated since 2002. The ANAO also found that the Rebate's *Risk Management Plan* did not contain all of the risks identified by Medicare Australia in 2000 as being relevant to the administration of the PRS. The risk that was omitted (treatment of cancelled and lapsed policies) is discussed in the following section.

Treatment of cancelled and lapsed policies

2.26 Medicare Australia's Audit Committee papers for September 2000 contain an internal audit report finding for the Rebate that: 'No policies or procedures have been issued to Funds participating in the 30 per cent Rebate premium reductions scheme to refund rebates claimed on cancelled or lapsed policies'. The internal audit report identified that Medicare Australia was exposed to a risk that health funds may not be refunding over-claimed rebates for lapsed or cancelled private health insurance policies.

2.27 Medicare Australia discussed the business rules for cancelled and lapsed policies with health funds during Rebate Working Group meetings prior to September 2000. Medicare Australia further proposed, in response to the September 2000 internal audit report finding, to address the issue by sending policy guidelines to health funds by the end of November 2000. However, no written policies or procedures were issued to health funds to guide their processing of cancelled and lapsed policies.

2.28 Reducing or eliminating the risk of overpayments not being returned by the health funds should have been part of Medicare Australia's risk management strategy for the PRS.[25]

2.29 The risk of overpayments was realised in June 2005 when the largest of the health funds, Medibank Private Limited (MPL), informed Medicare Australia that a discrepancy had been identified by MPL relating to refunds of the Rebate for dishonoured direct debit contribution payments dating back to the start of the Rebate in 1999.

2.30 MPL advised Medicare Australia that, due to a software programming error, the health fund's electronic systems had not automatically refunded (in subsequent monthly claims) any Rebate amounts that were correctly claimed

[25] In June 1999 and October 2000, Medicare Australia's Audit Committee considered a similar risk for the IPS that, after a Rebate refund has been paid through a Medicare office, a fund member might terminate their private health insurance policy or the member's payment is rejected by a dishonoured cheque, debit or credit card payment. In this case, the fund member is responsible for repaying the overpaid Rebate amount to the Australian Government. Improvements made by Medicare Australia to the IPS systems after the original audit report have treated this risk.

as being for current MPL memberships in a particular month, but the premium payments were later dishonoured by the member's financial institution. The problem occurred in MPL between January 1999 and June 2005.

2.31 MPL made an offer of $10.8 million to Medicare Australia in June 2005 in full and final settlement of the matter with the Australian Government for the period January 1999 to June 2005. Medicare Australia accepted the offer and in September 2005 received the payment of $10.8 million from MPL.

2.32 Medicare Australia surveyed all of the health funds during October and November 2005, in respect of the 2004–05 financial year, to see if a similar problem was occurring or was possible in other funds. An Outcome Report produced from the dishonoured payments survey found that 65.5 per cent of all health fund member contributions nationally are paid by credit card or direct debit. The report concludes that: 'Based on the information received from each of the health funds there does not appear to be a widespread systemic issue with the processing of dishonoured payments'. Health funds' survey responses to Medicare Australia indicated that they are refunding any Rebate overpayments through the monthly claim process. Medicare Australia assessed the issue that arose in MPL as being a 'one-off', which has been addressed by MPL.

2.33 Medicare Australia advised the ANAO that the scope of its current annual Rebate audit programme of health funds does not include specific consideration of the potential that rebates may be claimed against policies where the payments are subsequently dishonoured. Medicare Australia's recent survey Outcome Report recommends that Medicare Australia continue to monitor the treatment of dishonoured payments by health funds, including adjusting the annual Rebate audit programme, and carrying out a follow-up survey at the end of 2006. Medicare Australia further advised the ANAO in March 2006 that it plans to amend the Rebate *Processing Manual for private health funds* to include details of the processes to be followed for cancelled and lapsed policies.

2.34 The guidance provided by Medicare Australia to the health funds on the Auditor's Certificate required each year under subsection 16–5(7) of the PHIIA is broad enough to encompass this issue. However, it does not specifically require any sign-off that rebates have not been claimed against any policies where the payment was subsequently dishonoured.

2.35 In this context, Medicare Australia observed to the ANAO that, while the scope of its annual audit programme did not include specific examination

of this issue, ANAO, as MPL's auditor, also did not identify the problem with the fund's system in the context of preparing the annual Auditor's Certificates for MPL. The ANAO notes that the certificates were prepared in accordance with Australian Auditing Standards and this issue was not material from a financial reporting perspective.

2.36 Medicare Australia was aware of the risk of dishonoured payments occurring for the PRS since September 2000 and could reasonably have been expected to act to lessen those risks. The fact that Medicare Australia proposed a treatment for the risk in September 2000 indicated that the agency considered the risk to be unacceptable without mitigation (see paragraph 2.27).

2.37 The ANAO considers that the risk treatment initially proposed by Medicare Australia for cancelled or lapsed private health insurance policies might not have been adequate on its own to successfully reduce the risk of overpayments. A complementary audit programme, assessing health funds' processes for dishonoured payments, would provide increased assurance to Medicare Australia.

Recommendation No.1

2.38 The ANAO recommends that Medicare Australia further treat the risk of overpayments of the Private Health Insurance Rebate to health funds, resulting from health fund members' dishonoured private health insurance premium payments, by reviewing and updating:

(a) the Private Health Insurance Rebate's 2002 *Risk Management Plan;*

(b) the annual Private Health Insurance Rebate audit programme; and

(c) the Private Health Insurance Rebate *Processing Manual for private health funds* to include specific advice to health funds about processing refunds to Medicare Australia resulting from dishonoured premium payments.

Medicare Australia's response

2.39 **Agreed.** Medicare Australia is currently reviewing and updating the Private Health Insurance Rebate's Risk Management Plan to include the risk of dishonoured payments from health funds with the mitigation being inclusion of an audit process in the revised Private Health Insurance Rebate audit programme.

2.40 Medicare Australia's annual Private Health Insurance Rebate audit programme is currently being reviewed by an external consultancy to determine whether it covers all necessary aspects of health fund operation including adequate processes for the handling of dishonoured payments.

2.41 Medicare Australia is currently reviewing and updating the Private Health Insurance Rebate Processing Manual to ensure that health funds are fully aware of the procedures to be adopted where dishonoured premium payments occur and which require the refund of claim amounts to Medicare Australia.

Audit programmes

Annual audit certificates

2.42 Medicare Australia, under s. 16–5(7) of the PHIIA, requires health funds to provide a written audit certificate from a registered company auditor stating the correctness of their PRS accounts and records in a financial year. The original audit found that Medicare Australia relied heavily on these audit certificates to make up for limitations in the agency's pre- and post-payment checks.

2.43 The ANAO found in November 2005 that Medicare Australia had not reviewed the adequacy of the scope of the health funds' independent audit certificates since their introduction.

2.44 Medicare Australia discussed the scope of the health funds' independent audit certificates with health funds at a Rebate Working Group meeting in March 2006.

Medicare Australia's annual Rebate audit programme

2.45 Since 2001–02, Medicare Australia has received further reassurance about the validity and accuracy of health funds' PRS claims by carrying out its own Rebate audit programme using a Medicare Australia internal audit team. These audits are designed to measure:

- the reliability of health funds' PRS claiming, by testing registration accuracy and validity; and
- the accuracy of the health funds' monthly claim calculations.

2.46 All health funds were audited by Medicare Australia by 30 June 2002 and the health funds are now being audited again over the course of a three to four year cycle, at a rate of approximately 12 health funds per year.

2.47 The ANAO's analysis reveals the following major findings from Medicare Australia's audit programme from 2001–02 to 2004–05:

- of the claimed memberships (which were reviewed by the Medicare Australia audit team at health funds' offices), the number of claims that were not recorded in Medicare Australia's registration database fell from 2.1 per cent (with a value of $2.5 million) in 2001–02 to 0.19 percent (with a value of $24 016) in 2004–05;
- health funds' calculation of the Rebate amounts were found to be: 'performed correctly, accurately and consistently', in 2001–02, and, with minor exceptions that were not financially material, the same finding applied to the next three years;
- each year health funds were not able to produce some of the sampled Rebate application forms they are required to keep for five years to verify a member's existence and Rebate payment preference—in 2001–02 this was 7.6 per cent, which fell to a low of 0.3 per cent in following years, before rising to 5.9 per cent in 2004–05; and
- Medicare Australia's annual audit programme reports concluded that the potential financial risk the PRS was exposed to was low from 2001–02 to 2003–04, but rose to moderate in 2004–05 (as a result of the rise in the proportion of Rebate application forms that the health funds were not able to produce).

2.48 Medicare Australia advised the ANAO in February 2006 that, in addition to discussing the audit findings with each health fund as the audits are done, the agency had responded to the *2004–05 Audit Programme Report* findings by starting an audit of Rebate application forms in six health funds.

2.49 Medicare Australia has a systematic audit programme in place for key elements of the PRS. Health funds the ANAO interviewed said Medicare Australia's auditors gave useful feedback on the findings during their audit process. However, as recommended at paragraph 2.38, there is the potential to improve the effectiveness of the audit programme further by reviewing Medicare Australia's *Risk Management Plan* for the Rebate.

2.50 Therefore, the ANAO considers that while Medicare Australia has substantially completed Recommendation No.3(b) of the original audit there remains further action that should be undertaken to fully implement that part of the recommendation as set out in Recommendation No.1 of this report at paragraph 2.38.

Receiving and storing Rebate application forms

2.51 The financial risk for the Rebate system increases if health funds are not able to produce to Medicare Australia PRS registration application forms, because there is a risk that health funds could claim the Rebate for a fictitious member.

2.52 An increasing use of Internet and telephone-based applications for private health insurance policies means that there can be a delay in health funds receiving a member's signed application for the Rebate.

2.53 Health funds the ANAO interviewed considered the Rebate application form process to be inconvenient for their members and would prefer to accept a new member's verbal (or electronic) request for the PRS option, without the need to ask members for a further hard copy of the application.

2.54 Health funds also incur costs for either storing the forms in hard copy or scanning the forms for electronic storage for five years as required by the PHIIA.[26]

2.55 However, for the reason noted in paragraph 2.51, the signed PRS registration application forms are an important element of the control framework for the Rebate. Accordingly, the ANAO considers that if changes are made to the registration system, the financial control mechanisms for the Rebate will need to be reassessed as appropriate.

Private Health Insurance Administration Council audit certificates

2.56 The Private Health Insurance Administration Council (PHIAC)[27] is responsible for monitoring and reporting on the effectiveness of the Australian Government's premium reduction initiatives. Under s. 82L of the *National Health Act 1953*, health funds registered with PHIAC to participate in the Rebate must provide PHIAC with details relating to the Rebate, including a statement by an auditor as to whether the health fund has complied with the provisions of the PHIIA during a financial year.

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[26] Section 11–50(2) of the PHIIA enables health funds to store Rebate registration forms in hard copy, or electronically with the approval in writing of the Medicare Australia Chief Executive Officer.

[27] The PHIAC is an independent statutory authority and the specialised prudential regulator for the private health insurance industry. The PHIAC publishes information from the health funds in an annual report tabled in the Federal Parliament. Private Health Insurance Administration Council, *Operations of the Registered Health Benefits Organisations 2003–04 Annual Report* [Internet]. Private Health Insurance Administration Council, Canberra, 2004, available from <http://www.phiac.gov.au> [accessed 5 September 2005].

2.57 Health funds send the same annual audit certificate they send to Medicare Australia to PHIAC, which reviews the audit certificates for inconsistent or unexpected findings. While PHIAC can, and has, published the details of health funds receiving a qualified audit certificate in its annual report on the operation of the health funds, it has no legislative basis for taking any action to follow-up on the findings.

2.58 PHIAC named two health funds in 2003–04 and three health funds in 2004–05 that had received qualified audit certificates, of which three of the health funds were named because they were unable to produce completed and signed Rebate application forms for all participating members.[28] This reporting is consistent with the findings of Medicare Australia's annual Rebate audit programme.

2.59 Medicare Australia also monitors PHIAC's reports and acts promptly to resolve any differences or shortcomings found in health funds' activities during the independent audit process.

2.60 The ANAO suggests that, in future, Medicare Australia consider applying the penalty provisions of s. 18–5(1)(d) of the PHIIA (recovery of 150 per cent of a payment) for health funds that are repeatedly found to be unable to produce registration application forms on request. Given the Rebate was introduced in 1999, a disincentive for poor record keeping and non-compliance with the PHIIA may be necessary if Medicare Australia's existing education activities with the health funds are not able to halt or reverse emerging trends with Rebate application forms.

2.61 In March 2006, Medicare Australia acknowledged the ANAO's suggestion in paragraph 2.60 and advised that the penalty provisions would be applied on a case-by-case basis and outlined several examples of when funds would or could be penalised under s. 18–5(1)(d).

Debt management

2.62 Medicare Australia was reviewing its *Debt Recovery Plan* 2003, for the PRS and IPS, in early 2006. The ANAO noted that relevant sections in the plan did not match current Rebate practice for debt recovery.

2.63 In February 2006, Medicare Australia was using a monthly unregistered claims report to assist with the recovery of incorrectly paid

[28] Private Health Insurance Administration Council, op. cit., pp. 30–31, and Private Health Insurance Administration Council, *Operations of the Registered Health Benefits Organisations 2004–05 Annual Report,* Canberra, 2005, p. 22.

Rebate funds. The report is automatically sent to any health funds with unregistered claims, after the monthly payment process has been completed. This is designed to assist health funds to identify any unregistered claims and either refund the amount or register the policy.

2.64 The Rebate *Processing Manual for private health funds* states that: 'If the policy is not successfully registered, Medicare Australia will seek recovery of claims made within three months of the claim date'.[29] The ANAO found that Medicare Australia sends the health funds a *Debt Recovery Details Report* for all unregistered claims older than three months and most debts are then recovered as refunds through the monthly line-by-line data.

2.65 From June 2002 to 1 November 2005, Medicare Australia formally recovered money from health funds three times, outside the monthly recovery processes, due to health funds over-claiming the Rebate. During this period, Medicare Australia has not applied s. 18–5(1)(d) of the PHIIA, which enables 150 per cent of a payment to be recovered.

2.66 The health funds which the ANAO interviewed during audit field work advised that they were receiving the monthly unregistered claims report from Medicare Australia, as required, as part of their regular electronic transactions and found the reports useful.

Annual PRS reconciliation

2.67 In the original audit, Medicare Australia and Health acknowledged that post-payment checks, based on line-by-line data, were required to verify the accuracy of payments made to health funds.[30] The ANAO recommended at that time that Medicare Australia reconcile PRS payments made in 1998–99, 1999–2000 and 2000–01 as a key post-payment control.

2.68 The ANAO verified in 2005 that Medicare Australia had reconciled health funds' monthly summary claim data and supporting line-by-line data with the total Rebate claimed from the start of the Rebate in January 1999 to June 1999, and for 1999–2000 and 2000–01.

2.69 After June 2001, Medicare Australia replaced the annual financial reconciliation process for the PRS with monthly reconciliations, which the ANAO considers is a stronger financial control.

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[29] Medicare Australia, March 2005, *Federal Government 30% Rebate on private health insurance. Processing Manual for private health funds*, Version 3.2, p. 14

[30] Australian National Audit Office, op. cit., p. 49.

2.70 Medicare Australia advised the ANAO that the current pre- and post-payment financial controls, such as the requirement for health funds to provide line-by-line data to support their claims for payment and the Rebate audit programme, also contributed to making an annual financial reconciliation process redundant. Medicare Australia also advised the ANAO that it monitors the monthly payments to identify any pattern over time of claiming irregularities. Findings from these reviews are used to guide Medicare Australia's audit activity in the health funds.

2.71 The ANAO considers that monthly checks are timelier than an annual process and should enable Medicare Australia to act more quickly on any overpayments to health funds.

2.72 The ANAO considers that Medicare Australia has fully implemented Recommendation No.3(c) of the original audit report.

Conclusion

2.73 The ANAO concludes that Medicare Australia has generally adequate financial controls for PRS reimbursements, as Medicare Australia:

- requires health funds to support their Rebate claims for each health fund member with line-by-line data;
- has implemented a range of pre- and post-payment checks and a systematic audit programme; and
- undertook adequate reconciliations of PRS payments made in the period January to June 1999, and the 1999–2000 and 2000–01 financial years against line-by-line data. In addition, the monthly reconciliations of PRS payments against line-by-line data Medicare Australia introduced for subsequent financial years have strengthened the financial control framework for PRS payments.

2.74 However, the ANAO has also identified a number of areas within the PRS reimbursement process where Medicare Australia could further improve the financial controls. In particular, the ANAO recommends that Medicare Australia further treat the risk of overpayments to health funds, resulting from health fund members' dishonoured premium payments, by reviewing and updating a number of its current control mechanisms (see paragraph 2.38).

2.75 Overall, the ANAO considers that Medicare Australia has substantially completed implementing Recommendation No.3 of the original audit.

3. Incentive Payments Scheme and Tax Offset Administration

This chapter examines agencies' progress against recommendations made by the ANAO in the original audit for the IPS and Tax Offset options of the Rebate.

Incentive Payments Scheme administration

Findings of the original audit

3.1 The original audit found that Medicare Australia assessed the risks[31] and adequacy of the financial controls for the IPS. Because of the relatively low total value of the IPS payments and the possibility that the IPS option would be abolished on cost-benefit grounds, Medicare Australia did not take action for some time to address these issues. Medicare Australia did, however, recover funds from individuals for incorrect IPS payments in 2000. The ANAO concluded that the financial controls for the IPS could be further strengthened by Medicare Australia.

Original Recommendation No.4

Pending any change in policy and related legislation for the Incentive Payments Scheme, the ANAO recommends that HIC [Medicare Australia] strengthen financial controls surrounding the Scheme.

Original HIC [Medicare Australia] response: The HIC [Medicare Australia] **agreed** with the recommendation. The HIC [Medicare Australia] also commented that IPS controls had been strengthened, including implementation of enhanced procedures to check for duplicate claims against the PRS system.

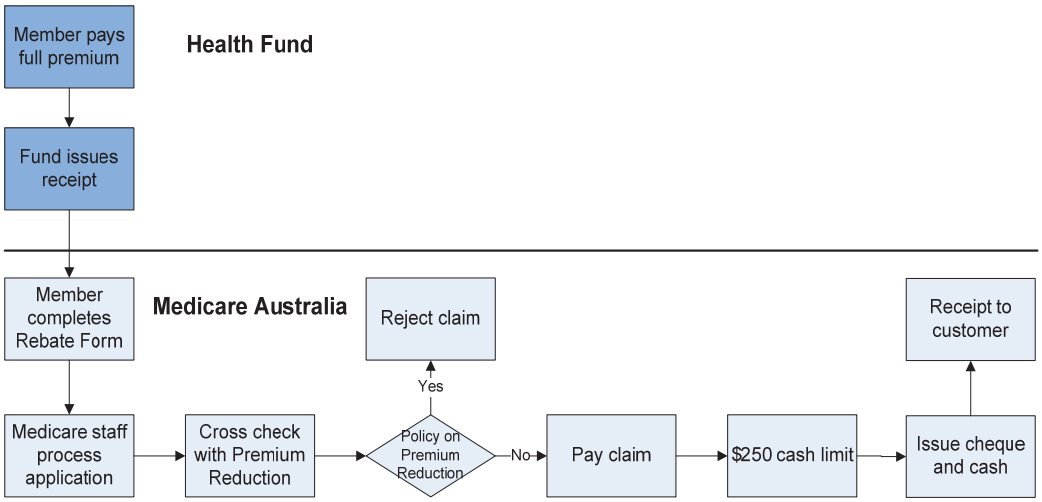
Findings of the follow-up audit

3.2 The original audit suggested a number of changes that could be made to strengthen the administration of the IPS (see Figure 3.1 for a diagram of the current IPS claims system).

[31] A December 1998 Medicare Australia risk assessment concluded that there was a high/very high risk of forged health fund receipts; multiple payments; and payments for ineligible policies. There was also a risk that double dipping would occur by claiming through the IPS and the Tax Offset or PRS Rebate options. Australian National Audit Office, op, cit., p. 54.

Figure 3.1

Incentive Payments Scheme overview diagram



Source: Medicare Australia, December 2005.

3.3 Based on Medicare Australia's assessment in late 2000 of the IPS,[32] the ANAO examined the following parts of the IPS system during the follow-up audit:

- pre- and post-payment checks using the IPS Information Technology (IT) system;
- health funds' receipts; and
- training for Medicare staff that process IPS claims.

3.4 The *30 Per Cent Rebate Enhancement Project* (REP) in 2003 focussed on the IPS IT system and receipt processes. The ANAO also examined the total payments and administration costs for the IPS option in 2005–06.

Pre-payment check

3.5 An electronic linkage between the IPS and PRS systems was introduced by Medicare Australia in October 2003 to produce an immediate notification of an attempt to process an IPS claim that has already been claimed for the same period under the PRS.

[32] Australian National Audit Office, op. cit., p. 55.

3.6 The current *IPS Direct Payments Manual,*[33] for use by Medicare operators processing IPS claims, details reject reason codes for instances when the IPS IT system does not calculate a Rebate amount.[34]

Post-payment checks

3.7 Medicare Australia developed an *IPS Duplicate Payment/Overlapping Periods Report* as part of the REP. However, the report has not functioned correctly since October 2003 and produces unreliable results. The problem is listed on a Medicare Australia *30 Per Cent Rebate Priorities List* for action.

3.8 Therefore, if Medicare operators identify an apparent IPS/PRS payment overlap they will usually ring the Medicare Australia national office Rebate team to check. The Rebate team keeps an informal record of the inquiry. If a duplicate payment is made in error the Rebate team is contacted again and a manual file fix is made in the electronic system to resolve the issue.

3.9 Medicare Australia also uses an annual data reconciliation process with health funds as a post-payment check for the IPS, as well as the ATO's annual data matching (see paragraph 3.33).

Debt management

3.10 Medicare Australia advised the ANAO in December 2005 that it had taken action to recover three debts for the IPS since May 2002. The amounts recovered ranged from $30 to $315.

3.11 Given the low incidence of IPS overpayments, and evidence of appropriate debt recovery action, the ANAO considers that Medicare Australia's debt management for the IPS is adequate.

Health fund receipts

3.12 In April 2003, Medicare Australia started a project, under the REP, to introduce a standard IPS receipt process for health funds. Medicare Australia worked with private health insurance industry representatives to increase the

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[33] The IPS Manual has detailed instructions for Medicare office staff on the operation of the IPS IT system and explains the steps and controls that are in place to accurately process a valid IPS claim. If a Medicare operator is unsure about any of the processing steps, the IPS Manual advises them to contact the Rebate Help Desk.

[34] Medicare Australia, March 2005, *IPS Direct Payments Manual,* Version 2.0, p. 31.

information requirements (member details, cover and receipt information) and standardise the format of health fund IPS receipts.[35]

3.13 The receipt is designed as a financial control for Medicare offices to make sure that: 'Claims that do not contain all of the required data elements will be rejected.'[36] The first receipts were introduced in September 2003, with the receipts being reformatted and recertified by Medicare Australia in 2005 to take account of the introduction from 1 April 2005 of a 35 per cent Rebate for people aged 65 to 69 years and a 40 per cent Rebate for people aged 70 years and over. Figure 3.2 shows an example of a current IPS standardised receipt for the 30, 35 and 40 per cent Rebates.

[35] The format for a health fund's IPS receipt is certified by Medicare Australia as meeting the standards required for Medicare Australia to process and pay claims for the IPS. Electronic copies of the health funds' receipts are made available to all Medicare Australia staff that process Rebate claims. This is to reduce the possibility of members submitting fraudulent receipts and also to increase the operator's ability to accurately assess eligible claims.

[36] Medicare Australia, May 2003, *30 per cent Rebate Enhancement Project. Business Requirements*, Version 1.1, p. 12.

Figure 3.2

Certified health fund receipt for the Incentive Payments Scheme

Receipt for Federal Government Rebate on Private Health Insurance Incentive Payments Scheme		
Health Fund Information		
Health Fund ID		
Fund Name		
Members Details		
Given Names		
Surname		
Cover Information		
Membership ID		
Membership Type		
Cover Type		
		Receipt Information
	Receipt Start Date	
	Receipt End Date	
	Date or FY Premium Paid	
Rebate Type	SPE Indicator (Y or N)	Premium per Rebate Type
30%	**N/A**	
35%		
40%		
	Amount of Premium Paid	
The premium paid for this policy, as shown above, has not been reduced by the federal government Rebate		

Source: Medicare Australia, December 2005.

3.14 Health funds interviewed by the ANAO said that they found certifying IPS receipts with Medicare Australia was a straightforward and low cost process.

3.15 The ANAO considers that Medicare Australia has successfully revised the health fund receipt process.

Training for Medicare operators

3.16 The REP identified that one of the largest problems to emerge from the IPS system was the occurrence of duplicate registrations which, in part, occurred due to data entry errors made by Medicare operators.

3.17 Medicare offices infrequently process IPS payments (approximately one customer per week).[37] The IPS Manual, Rebate Help Desks, a Reference Suite (documents on Medicare Australia's Intranet) and regular circulars are available to support Medicare operators' processing of IPS receipts.

3.18 The ANAO considers that the training provided to Medicare operators for the IPS appears to be adequate, given the low financial risk for the IPS, but encourages Medicare Australia's national office to monitor the level of data errors made by Medicare operators so that more support can be provided if needed.

Risk management

3.19 Medicare Australia's Rebate *Risk Management Plan*, 2002, identifies overpayments to policyholders through the IPS as a low risk. The rating is based on an assessment by Medicare Australia that:

> The financial cost of duplicates is expected to be low, since the total Rebate paid in cash is a low proportion of the total amount paid, and the duplicate rate is expected to be low.[38]

3.20 The ANAO found that Medicare Australia has acted to reduce the risk of fraud or error for the IPS. The ANAO also notes that, while total payments under the IPS have fluctuated both in absolute and proportional terms compared to the PRS payments from 2002–03 to 2004–05, the IPS remains the smallest of the three payment categories under the Rebate (see Figure 3.3).

Cost of the Incentive Payments Scheme option

3.21 The original audit found that Medicare Australia and Health were discussing:

> the possibility of Health recommending to the Government that the IPS be abolished on cost-benefit grounds. Total cash payments under the IPS accounted for $4.3 million, or 0.2 per cent of the private health insurance rebate payments administered by HIC [Medicare Australia], in 2000–01.[39]

3.22 In December 2005, Medicare Australia provided the ANAO with figures for the PRS and IPS payments made by Medicare Australia for the financial years from 2002–03 to 2004–05 (see Figure 3.3).

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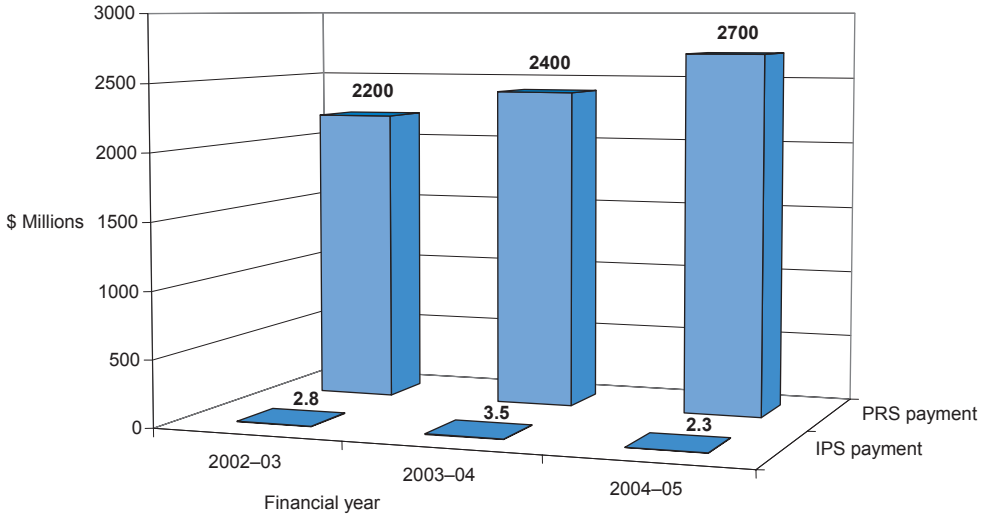
[37] Medicare Australia, September 2003, *30 Per Cent Rebate Enhancement Project Risk Management Plan*, p. 7.

[38] Medicare Australia, 2002, *30 Per Cent Rebate on Private Health Insurance Risk Management Plan*, p. 11.

[39] Australian National Audit Office, op. cit., p. 19.

Figure 3.3

Rebate payments from 2002–03 to 2004–05



Source: Medicare Australia, December 2005 and ANAO analysis.

3.23 Figure 3.3 illustrates that private health insurance policyholders, eligible to receive the Rebate, prefer to access the Rebate through an up-front deduction on their policy's premium—the PRS option. This preference has increased since the Rebate was introduced in January 1999.

3.24 Private health insurance industry stakeholders, with whom the ANAO consulted during November-December 2005, advised that health funds would prefer that the Rebate offered only two options to consumers—the PRS and Tax Offset.

3.25 Currently, Medicare Australia and the health funds are maintaining two separate Rebate systems for the PRS and IPS incorporating: IT systems and support; processing documentation and training; records storage; and financial controls.

3.26 The ANAO was advised by health industry stakeholders that there are costs for the health funds associated with creating and maintaining IT software to support two separate systems. Industry stakeholders also considered that there would be savings if the IPS system was no longer available and could be turned off without the need for further change.

Cost of the Private Health Insurance Incentive Scheme

3.27 The Rebate was introduced in 1999 to replace the Private Health Insurance Incentive Scheme (PHIIS) that operated from 1 July 1997. The PHIIS was income-tested and the amount of PHIIS benefit a person was entitled to depended on the type of policy and the number of people covered rather than the cost of the policy.[40]

3.28 When the Rebate was introduced in January 1999, 1.3 million PHIIS participants were automatically entitled to the Rebate.[41] Section 4–10 of the PHIIA applied natural justice principles by making sure that no one was disadvantaged under the Rebate, by requiring health funds to calculate and pay to previous PHIIS participants the greater of the two benefit entitlements—the PHIIS benefit or the 30 per cent Rebate.

3.29 The ANAO's analysis of the available evidence indicates that in 2006 the 'better off under PHIIS' rule is providing a relatively small benefit to a limited number of people. The number of health fund members receiving a PHIIS benefit is decreasing over time as the value of the 30 per cent Rebate increases relative to the value of the PHIIS benefit.

3.30 Medicare Australia informed the ANAO that most of the PHIIS registrations have now expired, but IT system changes mean that the exact number of ongoing registrations is unknown. PHIAC's annual reporting on the operation of the health funds notes that: 'The PHIIS has now been largely superseded by the 30 per cent Rebate'.[42] However, potentially, a small number of health funds are still:

- running separate PHIIS and Rebate systems;
- performing a dual calculation of benefit entitlements for PHIIS members; and
- providing two types of tax statements for their customers.

Conclusion

3.31 Medicare Australia adequately administers the IPS, as it:

- has introduced a pre-payment control linking the IPS claims system to PRS data held in the same system;

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[40] Australian National Audit Office, op. cit., p. 12.

[41] ibid., Footnote 6, p. 30.

[42] Private Health Insurance Administration Council, 2004, op. cit., p. 30.

- has revised the format and introduced a certification process for health funds' IPS receipts; and
- is providing adequate training to Medicare operators processing IPS payments.

3.32 Therefore, the ANAO considers that Medicare Australia has fully implemented Recommendation No.4 of the original audit.

Data matching between Medicare Australia and the ATO

Findings of the original audit

3.33 The ATO relies on data provided by Medicare Australia and the health funds to identify incorrect Rebate Tax Offset claims. Medicare Australia is required to provide annual line-by-line data to the ATO by 28 September each year. The ATO requires health funds to provide line-by-line data for each financial year by 30 November.

3.34 The original audit found that Medicare Australia did not comply with s. 19–15 of the PHIIA, which required it to provide the ATO with the data necessary for the ATO to conduct adequate data matching checks.[43] Initially, this was because the legislation did not permit Medicare Australia to obtain relevant data from health funds in order for Medicare Australia to comply with s. 19–15. After December 1999, the legislation was amended to require health funds to provide this data. However, Medicare Australia decided not to implement the systems necessary to provide the ATO with the data prescribed in s. 19–15. An effect was that for the Rebate's first two and a half years, arrangements were not adequate to detect people inappropriately claiming the Rebate through more than one delivery channel.

[43] Australian National Audit Office, op. cit., p. 19.

Original Recommendation No.5

The ANAO recommends that HIC [Medicare Australia] and ATO review their data exchange arrangements to ensure that ATO obtains timely access to the data it requires to undertake adequate data matching checks for inappropriate multiple claiming under the Private Health Insurance Rebate.

Original HIC [Medicare Australia] response: The HIC [Medicare Australia] **agreed** with the recommendation. The HIC [Medicare Australia] commented that it was working with the ATO to design a new data exchange protocol and have agreed a rationalised approach for data collection involving a single data set that funds will provide to the HIC [Medicare Australia] by the legislated date of 30 September. The HIC [Medicare Australia] will add required information to the data and forward to the ATO by a date determined by the ATO.

Original ATO response: The ATO **agreed** with the recommendation. The ATO commented that ongoing discussions between the HIC [Medicare Australia] and the ATO, through the Interagency Steering Committee of the 30 Per Cent Private Health Insurance Rebate Process Improvement Project, has led to the formation of a working group to address data exchange issues. The ATO has appointed appropriate resources to the working group and will continue to liaise closely with the HIC [Medicare Australia] with a view to ensuring the ATO has timely access to data necessary to detect inappropriate Private Health Insurance Rebate claims.

3.35 The original audit suggested that Medicare Australia and the ATO investigate the scope for streamlining the exchange of data between health funds and Australian Government agencies to reduce the administrative burden on health funds.

Findings of the follow-up audit

Medicare Australia's and the ATO's review of Rebate data exchange arrangements

3.36 An Interagency Steering Committee, established in August 2001, involving the ATO, Health and Medicare Australia contributed to ensuring compatibility between the system requirements for the three main data collection mechanisms for the Rebate:

- reporting from Medicare Australia to the ATO—according to *Private Health Insurance Incentive Reporting by Health Insurance Commission Version 3.1;*
- reporting from the health funds to Medicare Australia—according to *Private Health Insurance Fund Information Reporting for the Federal Government 30% Rebate Version 4.0;* and
- reporting from the health funds to the ATO—according to *Private Health Insurance Fund Information Reporting Version 3.1*.

3.37 The committee's work resulted in each of these specifications asking for virtually the same information and each of the data elements addressing virtually the same requirements.

Timing of Medicare Australia's transfer of data to the ATO

3.38 Section 19–15 of the PHIIA requires Medicare Australia to provide the necessary information to the ATO within 90 days after the end of the financial year—that is, before 28 September each year.

3.39 The ATO confirmed that Medicare Australia had provided this data on time since the original audit for the 2002–03 and 2003–04 financial years. Medicare Australia did not meet the legislative timing for supplying Rebate data to the ATO for the 2004–05 financial year.

3.40 The ATO advised Medicare Australia in September 2005 that corrections were needed to the data from the previous year before proceeding with lodging the 2004–05 data. Accordingly, the agencies agreed that Medicare Australia would lodge the 2004–05 data with the ATO on 15 November 2005. Medicare Australia met the agreed deadline. The ATO advised the ANAO that this later lodgement of the 2004–05 data did not affect any of the ATO's programmes.

3.41 Medicare Australia advised the ANAO that it expects to be able to meet the legislated timing requirements in coming years, now that it has corrected the data issues identified by the ATO.

Quality of Rebate data provided to the ATO by Medicare Australia

3.42 The key determinants of the quality of the data provided by Medicare Australia to the ATO are:

- the completeness of matching the identity of private health insurance fund members and taxpayers; and
- the extent to which the data is free of critical errors.

3.43 Medicare Australia and the ATO have worked together in recent years to improve the rate of matching between health fund data sent by Medicare Australia, and taxpayer identity.[44] The matching rates have been high for the latest two years. Table 3.1 illustrates that the ATO has matched around 95 per cent of the Rebate data provided by Medicare Australia to the ATO in 2002–03 and 2003–04 at the high or medium confidence level that there is an accurate match.

[44] Matching is carried out using the reported name, address and date of birth for contributors and dependants who are partners of the contributors.

Table 3.1

Results of the ATO matching of Tax File Numbers to Rebate data provided by Medicare Australia 2002–03 and 2003–04, percentage of records

Year	2002–03[A] (%)	2003–04[B] (%)
High	74	78
Medium	20	18
Low	2	2
No Match	3	2
Total	100	100

Note: (A) Results as at 15 February 2005.
(B) Results as at 28 September 2005.
Source: Data provided by the ATO, 24 October 2005.

3.44 Rebate data provided by Medicare Australia (and the health funds for that matter) is acceptable to the ATO for compliance testing if it is free of critical errors.[45] The proportion of matched records with critical errors has been relatively low for the latest two years—around six per cent for 2002–03 and one per cent for 2003–04 tax assessments.

Adequacy of the data to allow the ATO to control payment of the Rebate via the Tax Offset option, and the quality of that control

3.45 The ATO commented that, together with data provided directly by the health funds, it has sufficient data to carry out the required compliance checks. That is, the ATO can check whether people requesting the Rebate via the Tax Offset have been paid the Rebate via the PRS or the IPS, and are claiming the correct amount of Rebate.

3.46 Table 3.2 shows the results of the ATO's compliance activity. The value of debt raised for 2000–01 and 2001–02 exceeded $5 million, and affected around five per cent of all people claiming the Tax Offset. However, in 2002–03, the value of debt raised reduced to around $750 000, affecting less than one per cent of all people claiming the Rebate through the tax system. The amount of debt raised averaged around $2 per Tax Offset claimant in 2002–03, compared to around $15 for the previous two years.

[45] Examples of critical errors are when the values reported in the 'Type of cover' or 'Type of policy' fields of the Membership data record do not coincide with the allowable values for these fields as stated in the reporting specifications.

Table 3.2

Results of ATO compliance activity regarding the Rebate, 2001–02 to 2003–04

Year	2000–01	2001–02	2002–03	2003–04
Number of Tax Offset claims	450 578	394 546	352 901	308 813
Number of potential overpayments identified	25 499	18 752	76 165	na [A]
Number of overpayment letters issued	25 499	18 752	2 609	na
Number of debts raised	22 221	17 745	1 999	na
Value of debts raised	$6 765 688	$5 266 593	$752 004	na
Debts raised per claim	5%	4%	1%	na
Average value of debt per debtor	$304	$297	$376	na
Average value of debt per claim	$15	$13	$2	na

Note: (A) Data for 2003–04 was being processed in March 2006.
Source: Data provided by the ATO, November 2005.

3.47 The ANAO found that there is no data available that clearly identifies the main causes of the large reduction in Rebate Tax Offset debts in 2002–03, compared to previous years.

3.48 The ATO advised the ANAO that the likely main cause is a lower incidence of over-claiming due to people previously served debt notices not re-offending because they are better educated about the scheme. The ATO also acknowledges that the introduction of a new IT compliance system impacted on its compliance activity for that year.

3.49 In May 2005, the ATO introduced the Information Matching and Analysis System (IMAS), as the main compliance tool to identify overpayments associated with the Rebate (and other payments) for the 2002–03 financial year. IMAS is a fully automated system with options that can be set to isolate individuals from further assessment of overpayments, according to a range of selection criteria.[46]

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[46] Examples of the selection criteria are:

- low quality spouse identity match;
- tax file number exists in Medicare Australia record, but not in health fund record (ATO unable to match the two records); and,
- Medicare Australia advised cover different to health fund cover.

3.50 When IMAS was introduced, the ATO deliberately chose to isolate cases where there was a lower confidence of matching or data integrity. The ATO advised the ANAO in March 2006 that: 'This was a precautionary approach to ensure understanding of the outputs of the new system'. This approach resulted in a lesser number of 'best available' cases being selected for audit and a decreased number of overpayment letters being issued for 2002–03.

3.51 The ANAO considers that this precautionary approach is likely to have contributed to the reduction in the debts raised for the 2002–03 tax year, of over $4 million compared to the previous year.

3.52 The ATO further advised the ANAO in March 2006 that:

> All available cases (for the Rebate in 2002–03) were actioned and the appropriate business rules to mitigate exposure to incorrect taxpayer contacts were applied. These business rules are regularly refined and it is expected that an improvement in case identification and creation will occur in subsequent years.

3.53 The ANAO supports the ATO reviewing the business rules for IMAS. If the results show that the exclusions currently applied inappropriately reduce the number of 'best available' cases that are likely to result in debts, then the ATO should provide guidance to the case selection staff about the future use of the exclusions.

Streamlining the provision of Rebate data between Medicare Australia and health funds

3.54 As set out in the HIC's [Medicare Australia's] response to the original audit, and as a comment in the August 2002 HIC [Medicare Australia] Audit Committee report, the HIC [Medicare Australia] did intend to agree:

> a rationalised approach for data collection involving a single data set that Funds will provide to HIC by the Legislated date of 30 September. HIC will add required information to the data and forward to ATO by a date determined by ATO.

3.55 Medicare Australia advised the ANAO in October 2005 that changes were required to the legislation (specifically, s. 19–15 of the PHIIA) before it could alter the content or timeliness of the data it and the health funds provide. The proposed legislative amendment, which did not proceed due to competing

legislative priorities, was to allow Medicare Australia a further 30 days to prepare Rebate data for the ATO. The ANAO considers that streamlining the current data sets would also involve the health funds providing all of the required data to Medicare Australia, and not having to provide any data directly to the ATO. Providing Rebate data to the ATO is not mandatory and the Commissioner could decide not to ask the health funds to provide such data.[47]

3.56 Currently, the only difference in health funds reporting to the ATO compared to Medicare Australia reporting to the ATO is that the Medicare Australia data includes the amount of the Rebate paid (or premium reduced). Thus, the Medicare Australia data is more comprehensive than the health funds' data. The main value of the health funds reporting to the ATO is to provide the opportunity for cross-checking, which could improve the compliance systems.

3.57 However, as reported in paragraph 3.50, the ATO's current approach to a discrepancy in data between Medicare Australia and health funds is to isolate that record from further investigation into possible incorrect payments. While this may reduce the number of letters to taxpayers sent out that wrongly identify possible overpayments, it is also likely to reduce the number and value of overpayments identified and ultimately recovered.

3.58 The ANAO discussed streamlining data requests with three health funds and other stakeholders as part of audit fieldwork. These funds stated that providing both data sets was not ideal, but were not sure how much additional cost was involved in sending the data to the ATO. The funds would like to provide only one set of data, but would be concerned if this required future system changes and costs for them. While it may be possible to reduce the amount of data sent to both Medicare Australia and the ATO, health funds generally were wary of changes to the current data requirements and were not actively asking for any changes.

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[47] Section 264BB(1) of the *Income Tax Assessment Act 1936* states that the Commissioner *may* require a health fund to provide information.

Recommendation No.2

3.59 The ANAO recommends that Medicare Australia and the Australian Taxation Office review their data exchange requirements for the Private Health Insurance Rebate, to determine the net benefit of both agencies continuing to collect annual data from the health funds. If this benefit is negative or low, the agencies should examine options to rationalise the collection of this data.

Australian Taxation Office's response

3.60 **Agreed.** Recent work with Medicare Australia, regarding data exchange requirements for the Private Health Insurance Rebate, indicates that the need for health funds to provide data to both the Tax Office and Medicare Australia could be removed with effect from the 2006–07 year.

3.61 Subject to Medicare Australia including some additional information currently provided by the health funds and the health funds agreeing to this process, the requirement for health funds to provide the information to the Tax Office will be removed.

3.62 An initial meeting with Medicare Australia representatives on 22 March 2006 developed a strategy to progress the matter further.

Medicare Australia's response

3.63 **Agreed.** Medicare Australia has recently held discussions with the ATO. Both organisations have agreed that there is duplicate effort related to the provision of annual rebate data from health funds. From the 2007 reporting period, health funds will be required to send one data set, which provides all policy details to which the 30 per cent Rebate Premiums Reduction Scheme applies, to Medicare Australia who will add its own data, on policies processed under the Incentive Payments Scheme, and onforward to the ATO for processing.

3.64 Medicare Australia and the ATO have already agreed on the changes required, which are now being documented. Health funds were given a brief overview, in March 2006 at an industry workshop, of the future changes to reporting requirements.

Conclusion

3.65 The ANAO considers that Medicare Australia and the ATO have substantially completed implementing Recommendation No.5 of the original

audit. The two agencies have agreed data exchange protocols that provide the ATO with access to the data necessary to detect inappropriate Rebate claims.

3.66 However, the data exchange protocols require health funds to provide data to both Medicare Australia and the ATO, but this might not be providing a net benefit to the Australian Government. Furthermore, the ATO's main compliance tool that identifies potential overpayments associated with the Rebate excluded many potential audit cases in 2002–03 because the data supplied to the ATO by Medicare Australia was different to the data provided by the health funds.

3.67 The ANAO considers that it is important that the ATO proceeds with planned refinements of the business rules affecting its compliance processing of the Rebate to improve debt identification in subsequent years. Further, the ANAO recommends that Medicare Australia and the ATO resume discussions about streamlining data collection, with a view to ending the requirement for funds to provide data directly to the ATO.

4. Budget Estimates and Performance Information for the Rebate

This chapter outlines Health's implementation of Recommendation No.1 of the original audit, about approaches to Federal Budget estimates of the Rebate, and Health and Medicare Australia's development of clear performance indicators of Rebate payment accuracy to satisfy Recommendation No.6.

Budget estimates of the Rebate

Findings of the original audit

4.1 The original audit found that Health adopted a reasonable approach to preparing Rebate Federal Budget estimates. Health's assumptions were reasonable and based on an adequate level of analysis.[48]

4.2 However, the audit noted that with the accumulation of data on the impact of Lifetime Health Cover,[49] Health was in a position to enhance its estimates model, in particular, through an analysis of the factors underlying private health insurance premium growth (including health funds' income and costs and Medicare hospital statistics), trends in private health insurance participation among different demographic groups post-Lifetime Health Cover, and the relationship between private health insurance premium growth and participation rates.

Original Recommendation No.1

To ensure that Health's budget estimates in relation to the Private Health Insurance Rebate continue to be soundly based, the ANAO recommends that Health review its budget estimates approach with a view to effectively utilising available data relating to private health insurance premium growth and participation.

Original Health response: Health **agreed** with the recommendation. Health commented that it had developed, and would introduce, a revised estimate model, which incorporates a capitation-based approach to private health services and benefits paid.

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[48] Australian National Audit Office, op. cit., pp. 16–17.

[49] Lifetime Health Cover is an Australian Government initiative that started on 1 July 2000 and was designed to encourage people to take out hospital insurance earlier in life, and to maintain their cover. People who delay taking out hospital cover will pay a two per cent loading on top of their private health insurance premium for every year they are aged over 30 when they first take out hospital cover. See the Department of Health and Ageing website for more details at <http://www.health.gov.au>.

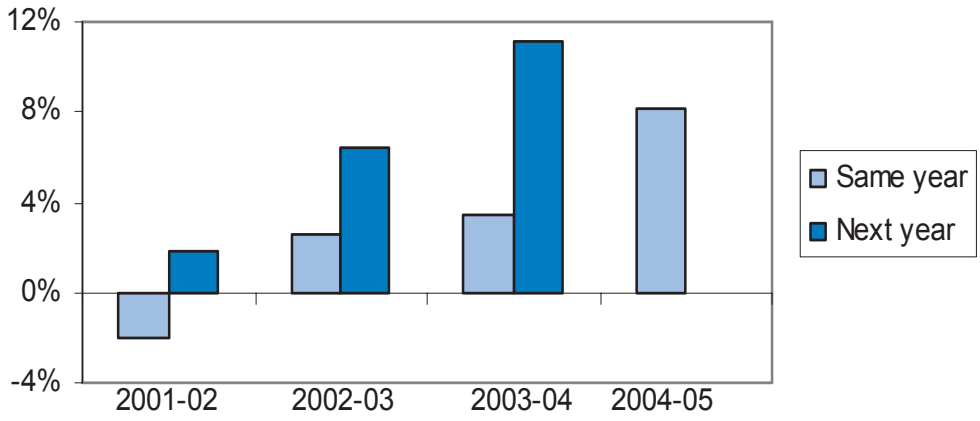
Findings of the follow-up audit

Accuracy of Rebate Budget estimates in recent years

4.3 The ANAO compared Health's estimates of the cost of the Rebate with the final outcome for the Budget and Additional Estimates processes for 2001–02 through 2004–05. Figure 4.1 shows that Health's Budget estimates for the Rebate were within five per cent of the actual Budget outcome for the first three of these years.

Figure 4.1

Accuracy of Health's Budget estimates, 2001–02 to 2004–05



Source: Information provided by Department of Health and Ageing, November 2005.

4.4 The final Budget outcome for 2004–05 was eight per cent, or over $200 million, higher than the Budget estimate in that year. Health explained that the increase in expenditure, compared to the Budget estimate, was mainly due to:

- the introduction from 1 April 2005 of the (35 and 40 per cent) Rebate for older Australians; and
- a higher than anticipated premium rise for health funds.

4.5 The ANAO acknowledges the difficulty of accurately estimating the cost of the Rebate, especially in years when significant Budget measures are introduced, such as 2004–05.

Health's Budget estimates model

4.6 Since the original audit, Health has continued to use the same model for estimating the cost of the Rebate. Consistent with Recommendation No.1 from the original audit, Health trialled alternative models. However, these models have not been adopted as they have been less accurate than the existing model.

4.7 Health and Finance initiated discussions in September 2005 about whether improvements can be made to the Rebate model to address Health's underestimates of Rebate costs in recent years.

Conclusion

4.8 The ANAO considers that Health has fully implemented Recommendation No.1 of the original audit given that Health has extensively reviewed its Budget estimates methodology, trialling various models that included the available private health insurance data. However, in the end, the existing model proved more accurate than the revised models and was retained by Health. This model proved to be reasonably accurate for most years since the original audit, but considerably underestimated Rebate costs in 2004–05. Health is continuing to work with Finance to improve the accuracy of the model.

Performance indicators of Rebate payment accuracy

Findings of the original audit

4.9 The original audit assessed the adequacy of performance information for the Rebate. It found that Health developed a sound basis for assessing Medicare Australia's and the ATO's overall administrative performance for both internal management and external reporting purposes.[50]

4.10 While overall performance information was considered sound, the original audit found that the claim processing accuracy indicator for Medicare Australia did not appropriately address accuracy. Above all, the Schedule for the Rebate under the Strategic Partnership Agreement did not provide clear standards in relation to the accuracy of processing by Medicare Australia (that is, paying the correct person the correct amount).

[50] Australian National Audit Office, op. cit., p. 21.

Original Recommendation No.6

The ANAO recommends that Health and HIC [Medicare Australia] develop clear performance indicators and standards in relation to the Private Health Insurance Rebate payment accuracy by HIC [Medicare Australia] (that is, the extent to which eligible people receive a rebate of the correct amount).

Original Health response: Health **agreed with qualification** to the recommendation. Health commented that it would incorporate into its strategic agreement and regular reporting arrangements with the HIC [Medicare Australia] some agreed high level performance indicators on administrative accuracy which are determined and used by the HIC [Medicare Australia] to meet other statutory and internal reporting requirements.

Original HIC [Medicare Australia] response: The HIC [Medicare Australia] **agreed** with the recommendation. The HIC [Medicare Australia] commented that the HIC [Medicare Australia] and Health have an agreed Schedule to the Strategic Partnership Agreement that details reports to be provided to Health and timeframes for reporting. The HIC [Medicare Australia] will consider the incorporation of appropriate performance indicators into the Schedule to the Strategic Partnership Agreement.

4.11 The original audit also noted that the performance indicators in the Health-ATO agreement were adequate given the respective roles and responsibilities of the agencies. As reported in the original audit, the ATO indicators were, however, inadvertently omitted from Health's *2001–02 Portfolio Budget Statements* (PBS). Health intended to include broad agency performance measures, consistent with measures set out in Health's Service Level Agreement (SLA) with the ATO, in the next Health Annual Report and PBS.

Findings of the follow-up audit

4.12 Health and Medicare Australia did not include an indicator of payment accuracy in the Schedule to the Strategic Partnership Agreement (SSPA). Health advised the ANAO that it has included an indicator of the accuracy of Rebate payments in a draft of the Business Practice Agreement, which was sent to Medicare Australia on 24 February 2006 for consideration.

4.13 The Business Practice Agreement will form part of a proposed Memorandum of Understanding between Health and Medicare Australia that will underpin the relationship between the two organisations, following Medicare Australia's move to the Human Services portfolio in October 2004. The Business Practice Agreements will be similar to the Schedules under the former Strategic Partnership Agreement, and are scheduled to be in place by 1 July 2006.

4.14 Table 4.1 illustrates the proposed indicator of the accuracy of Rebate payments contained in the draft Business Practice Agreement.

Table 4.1

Proposed indicator of Medicare Australia payment accuracy

Indicator	Source of performance information
The amount paid by Medicare Australia for claims calculated incorrectly by the funds (as identified in the annual audit programmes) is less than 0.5 per cent of the total amount paid to the funds covered by the annual health funds audits.	Annual report on health fund audits conducted by Program Review Division, Medicare Australia.

Source: Department of Health and Ageing, May 2006.

4.15 The ANAO considers that the performance indicator that Health and Medicare Australia are contemplating, as part of the Business Practice Agreement, has the potential to enable both agencies to better track and report on payment accuracy.

4.16 While the precise indicator has not yet been agreed, a suitable indicator is likely to be included in a key reporting mechanism by 1 July 2006. The ANAO considers, therefore, that Health and Medicare Australia have substantially completed Recommendation No.6 of the original audit.

Coverage of Rebate payment accuracy by the ATO in the Health and Ageing Portfolio Budget Statements and Annual Reports

4.17 The ANAO checked whether Health had included in its recent PBS and Annual Reports, indicators of payment accuracy relating to the ATO's processing of the Rebate Tax Offset programme. Health omitted these indicators from its 2001–02 PBS.

4.18 The ANAO found that Health included indicators of payment accuracy relating to the ATO's processing of the Rebate Tax Offset programme in its PBS for 2002–03, 2003–04, and 2004–05. Thus, it addressed the shortcoming identified in the original audit for those years. Health also reported against this indicator in its respective Annual Reports, stating that it met the required standards in all three years.

4.19 As part of a broader rationalisation of PBS performance indicators undertaken by the Department in 2005–06, Health again left this indicator out of its 2005–06 PBS. This issue is discussed below.

Coverage of Rebate performance information in the Health and Ageing Portfolio Budget Statements and Annual Reports

4.20 As reported earlier, the original audit found that Health developed a sound basis for assessing Medicare Australia's and the ATO's overall performance in administrating the Rebate, for both internal management and external reporting purposes. Reporting for internal management and cross-government purposes was through the Schedule to the Strategic Partnership Agreement (SSPA) with Medicare Australia and the Service Level Agreement (SLA) with the ATO. External reporting of this performance was mainly through the extensive set of indicators contained in Health's PBS and reported in its associated Annual Report.

4.21 The ANAO checked whether Health maintained this sound basis for assessing Medicare Australia's and the ATO's overall performance in administrating the Rebate.

4.22 The ANAO found that Health's monitoring through the SSPA and the SLA has continued virtually unchanged since the original audit to January 2006. Health improved monitoring of payment accuracy for Medicare Australia through the annual audits of Rebate payment accuracy undertaken by Medicare Australia.

4.23 The ANAO also found that Health continued its comprehensive external reporting of Medicare Australia's and the ATO's overall performance in administrating the Rebate, from 2001–02 through to 2004–05 in its PBS and respective Annual Reports. However, this reporting was substantially changed in Health's 2005–06 PBS.

4.24 In October 2005, Health advised the ANAO that the Department reviewed its performance management framework:

> to improve and reduce the number of performance targets that we report on in the PBS and Annual Report. Previously the Department had approximately 500 low level targets that did not allow us to report in a particularly meaningful way. That is, they were generally focused on process rather than on the achievement of outcomes. As part of the review, Budget Branch asked divisions to develop a small number of broad, high level targets for Administered Items, which were directly aligned with their Budget Related Expenditure items.

4.25 The ANAO understands the reasoning for this approach and considers that many of the indicators dropped for the 2005–06 PBS did represent low level targets that did not assist meaningful reporting. The ANAO also noted Health's advice that the Rebate indicators are consistent with other indicators in the PBS.

Conclusion

4.26 The ANAO considers that Health and Medicare Australia have substantially completed Recommendation No.6 of the original audit.

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Acting/Auditor-General

Canberra ACT
25 May 2006

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