SUBMISSION TO THE PRODUCTIVITY COMMISSION'S DRAFT REPORT

CARING FOR OLDER AUSTRALIANS: INQUIRY INTO AGED CARE

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1. Introduction

As a well-established provider of retirement living, community care and residential aged care services, Australian Unity welcomes the opportunity to respond to the Productivity Commission's January 2011 draft report, *Caring for Older Australians*.

As we outlined in our previous submission, Australian Unity's Retirement Living business already represents a significant investment in the aged care sector and, with the right policy settings, it is our intention that we will continue to serve some of the most vulnerable people in our community through the delivery of innovative, flexible and high quality products and services. Given our participation in what are essentially three differently administered and legislated systems (retirement villages, aged care and community care), Australian Unity has witnessed first-hand many of the barriers preventing older people from accessing the level of accommodation and care they require, when they require it, and in the location and form they wish.

The Productivity Commission should therefore be congratulated for their thoughtful consideration of a range of innovative yet integrated strategies that will enhance consumer choice and reinvigorate the aged care sector. The Commission has responded to the overwhelmingly unanimous message emerging from initial consultations: the aged care industry as it currently stands, is no longer sustainable for providers, for governments, and most importantly, for consumers.

To deliver the care that people deserve, meaningful change must occur as a broad-ranging package of reform. Selective adoption of the recommendations presented in the draft report may further destabilise the industry and compromise further service delivery.

2. The Context of Reform

In this submission, Australian Unity offers a number of specific comments on elements of the draft recommendations, but it is intended they be read in the broader context of the following observations (both new and re-stated):

- Wellbeing can be measured through robust tools such as the Australian Unity Wellbeing Index.
- Loneliness is associated with increased incidence of mortality and morbidity, including Alzheimer's disease, and therefore the setting of care

delivery must seek to minimise the personal and financial cost of age-related isolation.

- A reformed system must be robust and comprehensive enough to absorb the future increase in demand for aged care services, as the number of people aged 65 and over surges in the next 20 years.
- The proposed Australian Seniors Gateway Agency must be able to manage the multi-disciplinary care streams required by the increasing prevalence of multiple, complex health and neurodegenerative conditions, and early consideration should be given to broadening service delivery opportunities for sub-acute, restorative and rehabilitative services, funded on a case payment system.
- The legislative and funding environments must be flexible enough to cater to the consumer demand for increased choice, flexibility and service range (including the availability of service delivery in the home and the conversion of residential aged care places to community based care, but not discounting the ongoing importance and role of residential aged care).
- Frameworks for accommodation and care costs must recognise the financial limitations of some older people (many who rely on the age pension) with the ability of others to pay for a higher level of accommodation and hotel-type services.
- Further consideration should be given to the removal of distorting barriers for consumers to adopt retirement village/age friendly housing options.
- There needs to be a greater consideration of the capital requirements of the sector under each of the Commission's proposals in order to support the redevelopment of out-dated infrastructure as well as the growing demand for accommodation and care services.
- A revised system must address the shortage of an appropriately trained workforce to support the needs of an ageing population, as well as transitional arrangements that enable the migration of a proportion of aged care workers from residential care to home-based care (as low level residential care is replaced with care in the home).
- Further consideration of the consequences of the projected shortage and ageing of unpaid carers on the delivery models of the future is warranted, given the compounding effect this has on the dependency ratio and workforce requirements.
- The sequence of reforms must allow adequate periods of adjustment, with a corresponding public education campaign around consumer co-payments, quality of service provision and pricing of services.

3. Overcoming Barriers to Reform

Most of the areas on which Australian Unity wishes to make specific comment are best characterised as the 'overlap territories' between the retirement living, aged care and community care settings, that is:

- the delivery of community care services into retirement villages;
- the benefits of co-locating retirement villages and residential aged care;
- respite, transition care and restorative programs that support people to return to their homes.

The relative size and relationships of these environments is illustrated by the following schematic:

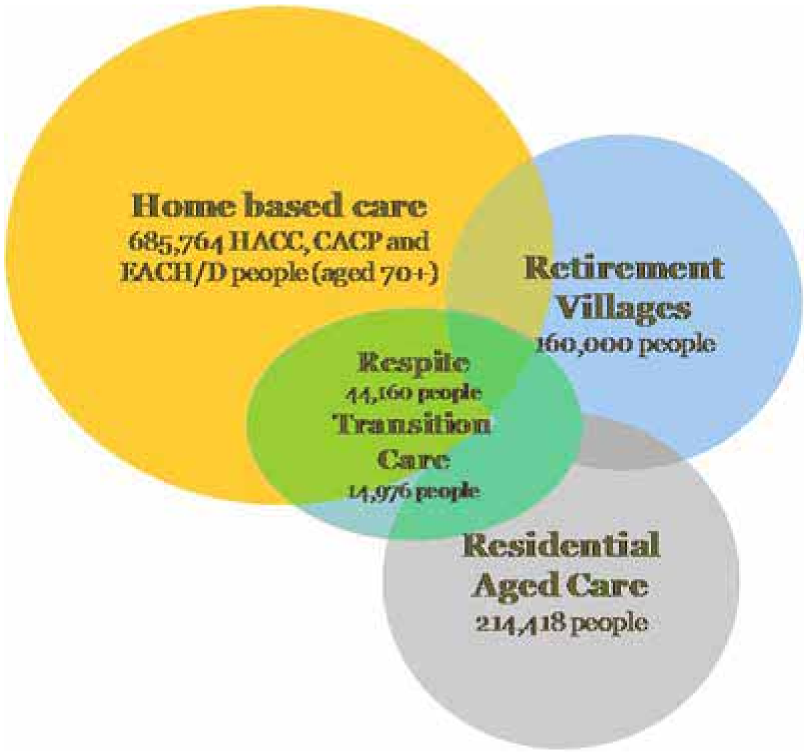

Figure 1: Accommodation and services for seniors (figures as at 30 June 2010)

3.1 Age-friendly housing and retirement villages

It is encouraging that the Productivity Commission acknowledges the role of age-friendly housing and retirement villages in accommodating older Australians, as described in draft recommendations 10.1 to 10.5 of the report. The legislative considerations facilitating more coordinated housing and planning strategies as well as a national regulatory approach to retirement villages and home maintenance systems are well detailed.

Australian Unity would like to reinforce the wider range of synergies and benefits offered by a more integrated approach to age friendly accommodation and service delivery, given that a significant growth in the overlap of these two sectors would deliver efficiency gains as well as socio-economic benefits. We also note that approximately one third of residents in Australian Unity villages receive some form of in-home care and anticipate that this proportion will continue with the increasing age of residents.

Heightened wellbeing

The individual and community benefits of living in a retirement village are demonstrable.

Australian Unity's annual resident survey, which is founded on the disciplines of the Australian Unity Wellbeing Index,[1] reveals that residents in retirement villages have significantly higher wellbeing compared to the general population aged over 65 years. Our data revealed that residents in Australian Unity villages rated their personal wellbeing at 80.3 points in 2009, compared with a like demographic sample of people living outside retirement villages (who scored 77 points). The Deakin University researchers noted this was statistically significant. Such a result is noteworthy, given that village residents reported a significantly reduced satisfaction with their health status compared with the control sample. These findings therefore highlight the importance – and the impact – of well designed and flexible accommodation and care services that focus on improving the quality of life of residents.

One of the key drivers of wellbeing is social inclusion. Combating loneliness not only generates personal, mental and emotional benefits, but a substantial body of scientific evidence demonstrates that it is also correlates with reduced mortality and morbidity rates.[2] The underpinning services and community infrastructure typical of many retirement villages offer residents a valuable range of options for social activity and personal contact, in addition to health enhancement programs, lifestyle activities and broader community connection.

Service efficiencies

Retirement villages in Australia increasingly cater to an older, frailer demographic with escalating care needs. A recent Grant Thornton–Retirement Village Association survey reveals that, on average, residents are entering

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[1] <www.australianunity.com.au/wellbeingindex>. See also the submission made to this Inquiry on behalf of the Australian Unity Wellbeing Index.

[2] Julianne Holt-Lunstad and others, 'Social Relationships and Mortality Risk: A Meta-analytic Review', *Library of Science, Medicine*, 7 (2010), 1–20; Reijo S. Tilvis and others, 'Suffering from Loneliness Indicates Significant Mortality Risk of Older People', *Journal of Aging Research* (2011), 1–5; Robert S. Wilson and others, 'Loneliness and Risk of Alzheimer Disease', *Archive of General Psychiatry*, 64 (2007), 234–40.

retirement villages at an older age, staying for shorter periods of time and are increasingly demanding assistance with their care needs.[3] Australian Unity's own data backs up this observation: the average age of our incoming retirement village residents (both singles and couples) is 77, which has risen from 75 over the past four years alone, while at least 30 percent of our residents currently receive some form of home-based care.

Similarly, over 70 percent of operators surveyed by Grant Thornton considered the provision of on-site services a "critical priority" for the majority of residents, while more than three quarters believed there was scope to provide greater levels of care support in their villages.[4]

If the demand for care in retirement villages is latent, it is arguable that the relative efficiencies of delivering services into this setting over the broader home-care sector make it an obvious target for a greater role in aged care service delivery. As participants in the 2003-04 Retirement Villages Care Pilot, Australian Unity was able to provide personalised care services that had high preventative healthcare and social support benefits, such as brief daily visits to support medication management, which also highlighted the sense of social isolation experienced by the resident and meant that lifestyle activities and socialisation could be offered – and personal wellbeing enhanced. The co-location of residents on a single retirement village site provides staffing efficiencies, minimal travel requirements and importantly, service flexibility as resident needs change over time. Retirement village units are also more easily adaptable home environments since they are typically built to meet universal housing design guidelines, including larger bathrooms with grab rails and wheelchair accessibility. As such, they facilitate a longer suitability of that home as an appropriate environment to "age-in-place".

Infrastructure benefits

Age friendly housing and retirement villages can also play a more significant role in broader planning, community and health infrastructures. Not only will support of retirement-village-style downsizing result in a greater level of private housing availability for young families within established suburbs, but the more efficient and tailored delivery of support services possible in higher density living could lower the rate of cost inflation (via more efficient service delivery and lower costs of house adaption) and reduce demand on acute health services (by lowering morbidity rates through reduced loneliness).

Removing disincentives for seniors

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[3] *Retirement Living: Industry Trends & Prospects* (January, 2011), p. 4.

[4] *Retirement Living: Industry Trends & Prospects*, p. 11.

The Productivity Commission has gone some way to acknowledging some of the challenges ageing Australians face in meeting their accommodation and care costs by suggesting that the facilitation of equity release from the family home could provide the incentive for better socio-economic outcomes. The Pensioner Bond Scheme and Aged Care Equity Release Scheme are two ways in which older people could more effectively access associated care and support, but the Commission could go further in facilitating easier access to retirement villages and their broad-ranging benefits.

One cohort of ageing Australians who received little recognition in the draft report are those residents currently residing in serviced apartments. In addition to fully funding their own accommodation cost, these people also pay for much of their own care. Many of these residents would be eligible for low care residential support but choose to live outside a 'hostel' or 'nursing home'. The shortage of community care packages means that, despite meeting assessment criteria, these residents do not have access to government-subsidised services. This results in a low demand for serviced apartments and frequently, residents have difficulty in selling these apartments when they move to residential care, further penalising people who are willing self-fund their accommodation and care costs. Under a more equitable system, which could be implemented quickly, anyone dwelling in an approved form of seniors' accommodation meeting assessment criteria should be eligible for subsidised care services.

Removing disincentives for operators

Retirement villages (or similar) typically cost more to construct, have slower sales rates and experience slower, lower development returns than experienced in other forms of residential community development. Despite their community benefits, therefore, it is more difficult to secure the necessary debt funding to construct new villages or redevelop ageing stock.

To compound this, the recent draft ruling issued by the Australian Tax Office (ATO) regarding the treatment of GST in retirement village developments and on sale, provides a further disincentive to invest in seniors' accommodation. The below table starkly illustrates the current distortion:

	High Care RACF	Low Care RACF	Serviced Apartments	ILUs
Charitable operators	GST free	GST free	GST free	GST free
Non-charitable operators	GST free	GST free	GST free	**Input taxed**

In addition to suppressing vitally needed new investment in affordable and appropriate housing for the aged, the current ATO draft ruling places a question mark over future investment in existing villages, including the upkeep of facilities, due to the valuation for tax purposes on sale being dramatically higher than actual transacted pricing. The promulgation of this draft ruling suppresses village development and further, may herald a significant decline in the value of a resident's main asset.

Consideration should instead be given to recognising the resource efficiency retirement villages provide to the aged care sector and the social benefits to residents. Consumers, taxpayers and the broader health system would best be served by an elimination of tax disincentives for retirement village construction. This could include:

- removing the GST distortion on the construction of retirement villages co-located with serviced apartments or residential aged care facilities;
- removing GST for those stand-alone villages offering affordable housing in an equivalent value of the GST revenue foregone. For example, $3.5m in foregone GST on development could provide ten affordable housing units.

Due to the lower development returns, retirement operators find it difficult to compete with other developers in acquiring in-fill land, which ironically is located in established suburbs where older people generally live and wish to remain. Requiring a socio-economic assessment is undertaken on the appropriate uses of excess government land prior to disposal, with consideration of local social and aged housing requirements, would support the industry to develop the volume of housing necessary to meet the forthcoming demand of the ageing population.

The Pensioner Bond Scheme, mentioned by the Commission on p. 173 of the draft report, is described as a scheme

> that would be available for age pensioners selling their homes. Under this arrangement any surplus funds from the sale of the home could be invested in the government scheme … It would offer an alternative (or supplement) to an accommodation bond and be exempt from the age pension assets test. Older Australians using this facility could draw upon it to fund their day-to-day living expenses and their aged care costs.

Australian Unity seeks clarification that such a product would be applicable to people entering retirement villages. The Aged Care Equity Release Scheme, described by the Commission on pp. 207–13 of the draft report, proposes a government-backed scheme to support sector funding.

Australian Unity recommends that such financial products, while appropriate for home-owners, are unsuitable for lease-hold tenure, such as commonly found in retirement villages.

The administrative cost arising from multiple providers seeking regular valuations on their equity security, being the independent living unit, and the possible consequences for village operator financing (particularly when multiple, varied valuations arise across the one unit type in the same village), suggests a cautionary approach is required in this setting.

Compounding this, however, is consequences such schemes could have in the affordable and/or regional segments of retirement village markets, where low property growth rates (or a decline in unit value) and deferred fees may already reduce the sum returned to the resident upon re-leasing. It would be a tragedy if operators avoided providing retirement accommodation in these markets for fear of adverse publicity, flowing from residents accessing equity release schemes.

3.2 Funding Mechanisms – Accommodation Bonds and Periodic Payments

The Productivity Commission identified that "pricing, subsidies and user co-contributions are [currently] inconsistent and inequitable" and that clients should "contribute in part to the cost of care (with a maximum lifetime limit) and meet their accommodation and living expenses (with safety nets for those with limited needs".

Australian Unity supports this shift to a 'user-pays' system of aged care, where those who can afford to pay, should do so.

Similarly, the recommendation to remove the distinction between residential high care and low care places and remove regulatory restrictions on accommodation payments, including the cap on accommodation charges in high care, is a necessary step to counter a system that currently stifles investment in residential care and bleeds capacity from the system.

Australian Unity has some concerns, however, regarding the potential flow-on effects for consumers and operators of the element of recommendation 6.4 that specifies that:

> the Government should require that those entering residential care have the option of paying for their accommodation costs either as: a periodic payment […]; a lump sum […]; or some combination of the above. To ensure that accommodation payments reflect the cost of supply … [the Government] should require that providers offer an accommodation bond that is equivalent to, but no more than, the relevant periodic accommodation charge.

The "cost of supply"

Although the purpose of publishing accommodation charges (and their bond equivalents) and linking both to the 'real' cost of supply appears to eliminate the possibility of providers charging 'super bonds', establishing the cost of supply could be more complex than simply an analysis of a provider's investment in physical infrastructure. Although accommodation charges/bond values set in a more open market would no doubt reflect the quality of accommodation stock, regional benchmarks and the segment of the population targeted (such as ethnically-specific services), there are less tangible costs to consider from a provider perspective:

- the additional costs of physical infrastructure and amenities that support the wellbeing of residents;
- replacement of building stock with superior product;
- associated debt financing and repayment of debt;
- return on equity (which is vital if new residential aged care development is to be supported by bank finance or other investment sources).

Furthermore, we have all experienced differential pricing in the hotel industry based upon perceived value, rather than costs, with, for example, harbour views adding substantially to the price of a room compared with lane-way or city views. It is therefore important that the 'real' cost of accommodation moves beyond simple input costs associated with the physical building structure and incorporates the quality of life and other 'outputs' generated from the built form.

Similarly, it is vital that governments continue to make capital grants or other forms of additional funding available to providers supplying certain care types, such as high level frailty, dementia and special needs such as mental health and homelessness, since these are market areas that will not easily be driven from a consumer choice, user pay or market competition perspective.

Bonds and periodic payments

In a 'user-pays' system, it is entirely reasonable that consumers have a greater choice of equitable accommodation payment systems. The choice between accommodation bonds, periodic payments or a mixture of the two therefore makes sense from a consumer perspective. However, suggestions of equity release products that can be used to fund care and accommodation needs via periodic cash releases could be read as encouragement of periodic payments over accommodation bonds: after all, what consumer would choose to pay an upfront bond with no rate of return, when they can invest their equity in a scheme with at least minimal returns and pay for their accommodation and care on a periodic basis?

While stimulating more choice is, on the face of it, positive for the consumer, a consideration of the 'lifecycle' of the average residential aged care facility may prove otherwise. The majority of residential aged care facilities are built using some equity but largely rely on debt funding for construction.

Take a typical 100 place facility, for example (for the sake of simplicity, there are no concessional places).

Construction costs	$18 million ($180,000 per bed)
Land costs	$ 2 million
TOTAL	**$20 million**

This facility has been constructed with $15 million of debt and $5 million of operator equity.

Scenario 1

If all the places attract a $250,000 bond or a mix such that the average is $250,000:

Accommodation bonds	$25 million	
Less repayment principal and interest	($17.5 million)	
Less working capital required	($2.5 million)	
Return of equity	$5 million →	funds available to reinvest

Although not earning any return over the construction and fill period, $5 million of equity has been returned to the operator, which can then be used to contribute to the development (or redevelopment) of another facility or invest for a commercial return, with profits reinvested to improve service delivery.

Scenario 2

50 beds are bonded and 50 beds attract a periodic payment of $41 a day (being a bond equivalent of $250,000, index rate of 6%; therefore 50 beds at $15,000 = $750,000).

If debt finance for construction is secured, there would typically be a requirement to pay down the loan to value ratio from 75 percent to 25 percent, requiring debt to be reduced to $5 million.

Accommodation bonds	$12.5 million
Less repayment principal and interest	($12.5 million)
Less working capital required	($2.0 million)
Shortfall in funds requiring additional equity	($2.5 million)

There will be a continuing debt of $5 million, at 8% = $400,000 p.a. servicing cost.

Equity remaining in the facility would now be $7.5 million.

Therefore, the difference between additional periodic payments received and debt sourcing costs is $350,000. This represents less than 5% return on the $7.5 million equity (or it would take 20+ years to repay the equity to allow reinvestment in a new facility).

Under this scenario, additional equity is required; however, the inability to be able to return any equity to investors in the short term will severely restrict investment in the industry. Similarly, the additional returns provided by an increased periodic payment (under these assumptions) are not sufficient to provide a commercial return to potential investors or provide sufficient funds to reinvest in the business.

An environment of decreasing lump sum payments from bonds and increasing periodic payments is also likely to have an impact on the availability of debt finance to construct facilities. Given it will be difficult to forecast the mix of lump sum payments and periodic payments, financial institutions are likely to identify increased risks in developments and therefore reduce the level of funds they are willing to lend. This has the potential to further reduce availability of funding in an already difficult market.

Unless periodic payments provide a rate of return equivalent to other property sectors, any further decreases to existing accommodation bond pools will be enormously detrimental to the viability of aged care providers, regardless of the ability to take a bond on a 'high care' as well as a 'low care' place – and potentially lead to a decline in the number of residential aged care services and a narrowing of choice for the consumer.

A system that supports periodic payment over accommodation bonds will therefore amplify the issues already inherent (and articulated in Australian Unity's previous submission):

> In our experience … the cost to purchase land and build an aged care facility to meet the care needs of the community is more than the available accommodation bond income ... The ability to debt finance aged care development therefore reduces unless higher equity contributions are made. Higher equity contributions and a slow, long tail for equity return often renders development of new residential aged care facilities unviable as the return (if any) is not commensurate with the level of risk. A mismatch between low margins and high risk (both finance and construction) therefore renders this style of development unattractive to capital providers/ developers and impedes the supply of operational places in spite of the inherent demand.

In its most basic economic context, accommodation bonds ensure that providers can convert equity to capital in order to develop new facilities and improve their existing stock. Fewer bonds, albeit spread across more beds, will create a system in which debt is the primary source of funding – and there is no guarantee that debt will be readily available to providers.

Such an outcome places enormous pressure on an assumption that the banking sector – or other capital markets, including superannuation funds or private capital – will choose to invest in aged care development in the future. Already, an array of not-for-profit and for-profit providers have indicated an ongoing lack of confidence in their ability to secure appropriate levels of increased debt funding for new or redevelopment activities,[5] and in order to stimulate wider investment, the rate of return on equity would need to be above 10%.

4. Transition Arrangements

In light of the above points, careful consideration should be given to the phasing of industry reform. The aged care sector has indicated a willingness to adopt a comprehensive package of reforms broadly in line with the draft report. Consultation by the Productivity Commission with the industry has been high, which is to be applauded, and effective transition will require a continued engagement with all stakeholders.

March 2011

[5] Deloitte, *Annual Survey into the Australian Aged Care Industry 2010*, pp. 7–8.