Sustainable Financing of Aged Care Capital Expenditure: Stakeholder Perspectives

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Costs in residential aged care

- Costs associated with living in residential aged care
  - Care costs - mostly funded by the Australian Government through the Aged Care Funding Instrument (ACFI)
  - Daily living expenses – paid by the residents – mostly from the single aged pension
  - Accommodation costs
    - Residents with low means – supported by the government through accommodation supplement – income and means tested
    - Partially supported and non-supported residents pay themselves
    - housing is the consumer's responsibility

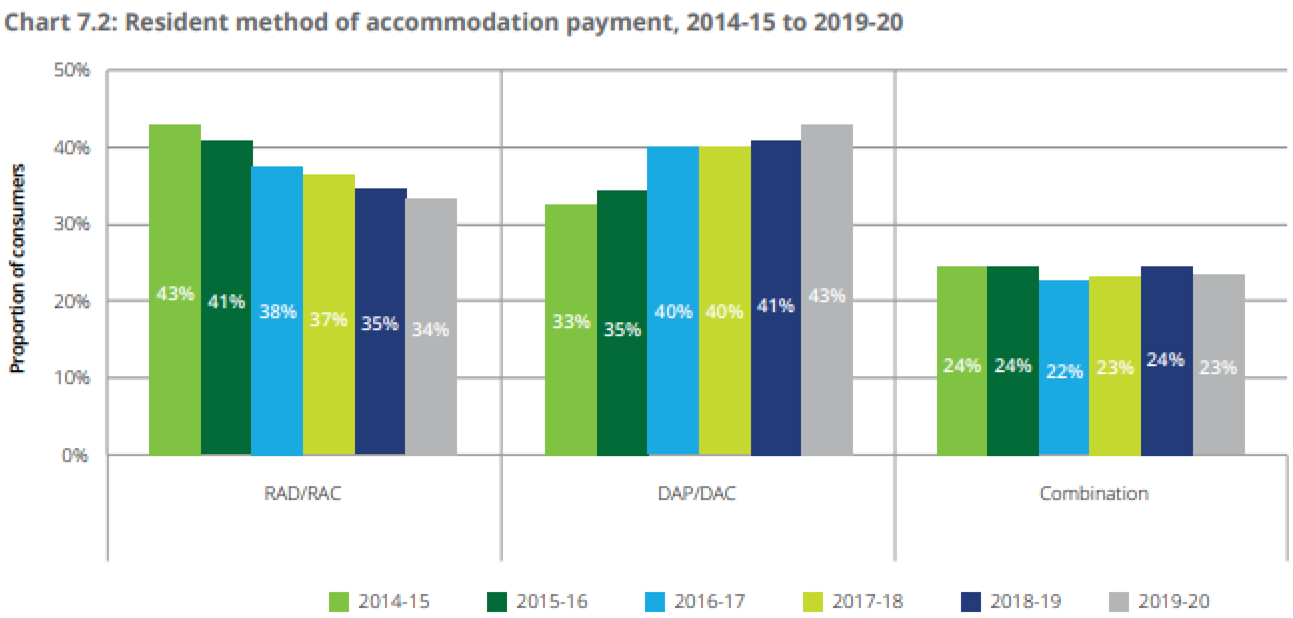
Accommodation costs

- Australia has a unique capital financing system for residential aged care accommodation
- When a resident enters aged care, they pay their accommodation through:
  - A refundable accommodation deposit (RAD) – lump sum payment
  - A daily accommodation payment (DAP) – a rent styled payment
  - Or a combination of both
- RADs are used to fund capital expenditure
  - Significant refurbishment and develop new facilities
  - Total value held by providers $30.2b (2018-19)
- Capital expenditure is also funded through equity, commercial debt, donations, endowments and capital grants

Background

- 1997: Accommodation bonds introduced to increase investment in nursing home stock
- 2013: Living Longer Living Better (LLLB) reforms
- 80,000 new beds are required to meet demand over the next decade (projected by ACFA)
    - Refurbishment and rebuilding current stock
    - Combined total investment of $51billion: this will require a substantial increase in RAD balances

RAD vs DAP



Source: ACFA, 2021

- In recent years, there has been a shift away from RADs to DAPs
- Providers have no choice over whether a resident pays a RAD
- This has left them exposed to a reduction in RADs given this shift

Conflicting views

- Conflicting views on the role of RADs in residential aged care:
  - The Royal Commission into Aged Care Quality and Safety recommended
    - Phasing out of RADs for new residents
    - For government to assist providers to transition away from RADs
    - Establishing an aged care accommodation capital facility
  - Aged Care Financing Authority
    - No obvious and immediate alternative funding models to RADs
    - A system offering RADs and DAPs to consumers are appropriate
  - Residential Aged Care Accommodation Framework
    - Seek to clarify whether a viable alternative capital financing mechanism exists
    - Framework to commence from 1 July 2024

Research aims

- Previous literature on aged care financing has focused on:
  - Consumer choice between RADs and DAPs (Abiona, Yu, Woods, & van Gool, 2020; Cutler et al., 2021)
  - Care costs (Fine & Chalmers, 2000; Sherris, 2021)
  - Several government initiated inquiries explored specific components of accommodation payments
- Our study aims to evaluate:
  - the role of RADs in the residential aged care sector
  - the potential impact from a significant reduction in RAD balances on the sector’s sustainability
  - Identify possible government policy responses

Method

- Use qualitative methodology
    - Ability to provide rich descriptions of complex phenomena
    - Illuminate the experience and interpretation of event by stakeholders
- Grounded theory
    - Used to develop a theory grounded in the behaviour, words and actions of those being studies (Goulding, 2020)
    - Involves iterative process, interrelated planning, data collection/analysis and theory development (Vollstedt & Rezat, 2019)
- This study follows the general principles of grounded theory (Corbin & Strauss, 2008)
    - Modified practical approach in carrying out analysis

Data

- Purposeful sampling to start the sampling process
  - Identified and recruited a wide range of stakeholders of interest with experience and knowledge
- 14 stakeholder interviews (60 minutes)
  - 6 lenders, 3 peak provider representatives, 2 peak consumer representatives & 3 valuers
- 5 focus groups (90 minutes)
  - 23 providers based on size of RAD balances, number of beds, ownership type
- Provider survey
  - Online survey of 300 providers (representing 35% of all approved providers)

Analysis method

- Used inductive constant comparative method
  - Analysed and coded the transcripts using Nvivo
    - Decomposed into small components to identify categories and concepts
    - Systematically categorised and compared themes to find patterns of data
    - Iterative process until themes became more developed to form unified explanations of the research questions

Themes: Use of RADs

- Access and uses of RADs vary by provider
  - Depends on provider preferences, characteristics, debt and liquidity level, and location of facilities
  - Uses include:
    - Invest into capital to avoid paying commercial debt
    - Repay bank debt and acquire land
    - Generate income through term deposits
- Preferences for RADs vary by providers
  - Preferences are mostly determined by desire to undertake capital expenditure
  - Some prefer a mixture of RADs and DAPs to reduce operational and capital investment risks

Themes: Advantages of RADs

- RADs represent a low-cost loan for many providers
  - Allow providers to access cheaper debt compared to commercial debt
    - at rates lower than the Maximum Permissible Interest Rate
    - MPIR is the government set interest rate used to calculate DAP on a specific RAD value, used to determine equivalence between RAD and DAP
    - MPIR is currently around 4%
  - Increases opportunity for providers to access commercial debt not otherwise obtainable
    - Provider's ability to attract RADs = capacity to repay debt
  - Allowing them to undertake significant capital expenditure

Themes: Risks associated with RADs

- RADs can create a volatile capital structure
  - RADs are a current liability but are used to finance capital expenditure which is a non-current asset
  - Requires continual monitoring and management
  - Significant reduction in RADs can create solvency risk
  - Provider's capital expenditure, liquidity and solvency are exposed to shifting consumer preferences away from RADs
- RADs incur administrative costs for providers
  - Smaller operators may struggle understanding prudential and compliance requirements
  - Providers with RAD balances must ensure they remain liquid to repay RADs to exiting consumers

Themes: Disadvantages of RADs

- The choice between RADs and DAPs is not well understood by consumers
  - Complex financial decision – impacts on assets and income
  - Some providers may try to manipulate the choice towards RADs
- RADs may impose barriers to entry for equity investment
  - Limited public information available on how RADs are treated
  - RADs not understood by international investors given they are unique to Australia
- No viable alternative to RADs currently exist
  - Not enough lending capacity from banks to substitute RADs
  - Lack of equity investment due to low profitability and uncertainty in the sector
  - Real estate investment trusts (REITs) are common overseas but current market does not generate enough yield for healthcare REITs to work in Australia

Reduction in RAD balances

- A reduction in RAD balances would impact on providers differently depending on their reliance on RADs
    - Benefit those not undertaking capital expenditure
    - Negatively affect providers mostly using RADs for capital expenditure
- Whether the government should intervene should depend on the size and timing of the reduction
- Any liquidity problems from significant reduction in RADs can lead to facility closures and consumer distress
- Australia government is responsible for consumers accessing residential care

Policy interventions

- Government can enforce liquidity and capital adequacy requirements on residential aged care providers
- Create a more viable market for equity investment or REITs
  - Greater return on investment required
- Remove RADs from aged care financing
  - As recommended by the Royal Commission
    - Phase out by 2025, government establish a capital facility

Policy interventions

- Accommodation capital facility
  - Government to guarantee providers' commercial debt
    - Increasing a bank's ability to lend to providers
  - Develop loan facility for providers to access capital
    - If providers cannot obtain commercial debt or equity
    - Funded by government's access to cheap debt via their AAA credit rating
    - Providers can invest surplus RADs back with higher returns
    - Creating risk pooling amongst providers
- Stakeholders' view: RADs can only be removed if there is a stable alternative, detailed transition plan and over long period of time

Thank you

For more information on this presentation, or the Macquarie University Centre for the Health Economy (MUCHE), please contact:

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