On 8 August 2011, the Australian Government announced the release of the Productivity Commission’s final report into Caring for Older Australians (28 June 2011).

The final report follows the Commission’s draft report released in January 2011 for public comment and largely maintains the recommendations of the draft report together with a number of new recommendations.

The government announced its intention to consult for a 2 month period before rejecting or accepting the recommendations. In a joint release on 8 August, it was stated that, ‘The government will develop its response to the report’s recommendations guided by four overarching principles:

• First, every older Australian has earned the right to be able to access quality care and support that is appropriate to their needs, when they need it.
• Secondly, older Australians deserve greater choice and control over their care arrangements than the system currently provides.
• Thirdly, funding arrangements for aged care need to be sustainable and fair, both for older Australians and for the broader community.
• And finally, older Australians deserve to receive quality care from an appropriately skilled workforce.”

The Minister for Mental Health and Ageing, Mark Butler, said the recommendations in the report will be considered as part of the government’s broader ageing agenda.

This summary provides an overview of the key recommendations, the recommended timeline for implementation and includes brief commentary on the implications for aged care operators.

Key elements of the recommendations for aged care providers

What we know

Until the government completes its consultation period and determines whether to adopt all or any of the recommendations, no further guidelines on the proposed frameworks will be known. However, there is an undeniable need to shift from the current aged care system, which is seen to be unsustainable, complex and inequitable - and the Productivity Commission’s final report provides the direction in which this change is likely to occur.

The establishment of a single integrated system predicated on consumer choice is the foundation to the fundamental redesign of the current aged care system enabled by the following four key pillars:

• Australian Seniors Gateway Agency
• Australian Home Credit Scheme
• Australian Aged Care Commission
• Australian Age Pensioners Savings Account.

Action needs to be taken now by aged care providers to prepare for this change, regardless of the timing of implementation. The direction set out in the report means fewer restrictions on supply, increased competition between providers, increased accountability and greater public transparency with more older Australians choosing to receive services in their homes, and those entering residential aged care facilities being frailer and older on entry. A greater commitment to consumer choice and control over the types of services they will receive will also require a more flexible service system and challenge service providers to develop innovative, responsive yet efficient models of support and care.

What we don’t know

Critically, whilst the report makes 58 recommendations, the government is yet to agree and announce which recommendations it will adopt, so a significant degree of uncertainty remains as to the extent of change and impact on the sector and aged care providers.

Elements that require confirmation are:

• which of the proposed reforms will be adopted by the government
• transition plan and timing
• infrastructure that the government will establish to support the reforms
• extent of regulation on bond payments and periodic payments.

Main elements of the proposed reforms impacting aged care providers at a glance

A summary of the implications of the proposed reforms for operators, both positive and negative, is set out below. The other many recommendations impacting individuals, the community and government have not specifically been included.

<table>
<thead>
<tr>
<th>Proposed reform</th>
<th>Implications for operators</th>
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<tbody>
<tr>
<td><strong>Funding</strong></td>
<td></td>
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<tr>
<td><strong>Australian Seniors Gateway</strong> and capacity to pay testing</td>
<td>✓ Greater clarity for residents and standardisation of the entry process</td>
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<tr>
<td></td>
<td>✓ Those with capacity to pay make a larger contribution to the cost of care</td>
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<td></td>
<td>× Operators may have to provide a more standardised offering through the Gateway</td>
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<td>and so may have less flexibility to offer differentiated services and may have less</td>
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<td></td>
<td>ability to market direct to residents</td>
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<tr>
<td><strong>Separate policy settings for accommodation, living expenses and care costs</strong></td>
<td>✓ Those with capacity to pay make a larger contribution to the cost of care, living</td>
</tr>
<tr>
<td></td>
<td>expenses and accommodation</td>
</tr>
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<td></td>
<td>× Operators may have less ability to factor in their different cost models into the</td>
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<tr>
<td></td>
<td>standardised pricing required to be offered through the Gateway</td>
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<tr>
<td><strong>Removal of distinction between high care, low care and extra service</strong></td>
<td>✓ Improves capacity to meet high care, with bonds now able to be charged</td>
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<td></td>
<td>✓ Bonds will more accurately reflect the cost of providing the facilities</td>
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<td>× Potential preference for periodic payments may reduce the take-up of bonds</td>
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<td></td>
<td>resulting in a need for all operators to find new sources of capital</td>
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<td></td>
<td>× Possibility that government may charge for the guarantee of bond repayments</td>
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<td><strong>Removal of caps on the number of community care packages and bed licences</strong></td>
<td>✓ Better ability to respond to local demands regardless of the type of care</td>
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<td></td>
<td>× Increased financial risks from opening up of the market and the loss of value in</td>
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<td>existing licences, requiring higher rates of return in compensation</td>
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<tr>
<td><strong>Australian Age Pensioners Savings Account Scheme</strong></td>
<td>× May prove a disincentive for residents to pay the bonds as opposed to utilising this</td>
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<tr>
<td></td>
<td>scheme and making periodic payments to operators</td>
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<tr>
<td><strong>Australian Age Care Home Credit Scheme</strong></td>
<td>× May prove a disincentive for residents to drawdown these loans to pay the bonds</td>
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<tr>
<td></td>
<td>as opposed to making periodic payments</td>
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<tr>
<td><strong>Minimum allocation of supported places to reflect regional requirements and</strong></td>
<td>✓ Allow providers to pursue more innovative residential care models</td>
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<tr>
<td>costs</td>
<td>× The level of subsidy will need to sustain the commercially viable provision of</td>
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<tr>
<td></td>
<td>supported accommodation</td>
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<tr>
<td><strong>Inclusion of the share of the principal residence in the Supported Place tests</strong></td>
<td>✓ Should ensure allocation of supported places to only those in need</td>
</tr>
<tr>
<td><strong>Australian Aged Care Commission review and recommendations</strong></td>
<td>✓ Realistic prices, subsidies and indexation will ensure a sustainable industry</td>
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<td></td>
<td>✓ Greater industry confidence in the price setting process</td>
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</tbody>
</table>
Main elements of the proposed reforms impacting aged care providers at a glance (continued)

<table>
<thead>
<tr>
<th>Proposed reform</th>
<th>Implications for operators</th>
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</thead>
<tbody>
<tr>
<td><strong>Care and support</strong></td>
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<tr>
<td>Improved access to aged care and community services</td>
<td>✓ Simplified information, assessment and referrals processes available at a regional level</td>
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<td></td>
<td>✓ Providers able to market low intensity services directly to potential customers</td>
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<tr>
<td>In-reach services and cost-reflective sub-acute services</td>
<td>✓ Allows providers to deliver a more flexible range of care services and diversify their</td>
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<td>client and revenue bases</td>
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<td><strong>Quality of care</strong></td>
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<tr>
<td>Quality and Outcomes data set</td>
<td>✓ Improve accountability for government subsidies received</td>
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<td></td>
<td>× Over regulation may not provide increased quality</td>
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<tr>
<td>End-of-life care</td>
<td>✓ Care providers to receive appropriate case mix payments for delivering palliative and</td>
</tr>
<tr>
<td></td>
<td>end-of-life care</td>
</tr>
<tr>
<td><strong>Workforce issues</strong></td>
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<tr>
<td>Improvement employment conditions</td>
<td>✓ Increased ability to pay competitive wages to nursing and other care staff where</td>
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<td></td>
<td>scheduled prices for aged care take into account these costs</td>
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<td></td>
<td>✓ Ability to attract employees with improved pay and career paths</td>
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<tr>
<td><strong>Regulatory institutions</strong></td>
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<tr>
<td>Reporting requirements</td>
<td>✓ Streamlined reporting mechanism will reduce unnecessary costs</td>
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<td></td>
<td>✓ Reduce significant disclosure burden</td>
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<td></td>
<td>✓ Free up resources to find missing residents</td>
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</table>
Possible timeline for the introduction of the proposed reforms

The final report provides an implementation plan, summarised below, as follows:

0 to 2 years
Stage 1

- Establishing the Australian Aged Care Commission and the Australian Seniors Gateway Agency
- Remove the distinctions between low and high care, and between ordinary and extra service
- Require residential aged care facilities to offer and publish periodic accommodation charges and accommodation bonds
- Remove regulated accommodation bond retention amounts
- Introduce price monitoring for residential accommodation
- Increase the number of community care places by 20%
- Increase the supported resident accommodation supplement progressively to a level commensurate with the cost of an approved supported resident place
- Introduce the Australian Age Pensioners Savings Account scheme
- Conduct a public benchmarking study of aged care costs
- Increase the release of data, information and research findings
- Introduce a temporary assistance package for small residential providers.

Within 2 - 5 years
Stage 2

- Introduce the new model of care assessments and service entitlements
- Create the formal entitlement based aged care system, together with the block funded community support services
- Finalise the major regulatory changes
- Introduce the new co-contribution and lifetime stop-loss funding arrangements
- Introduce the Australian Aged Care Home Credit Scheme
- Set care prices and accommodation charge for supported residents
- Gradually increase the quantity of residential places by 10%-20%
- Introduce measures to improve the quality of aged care services, including the promotion of transparency and accountability
- Continuing the increase in the number of community care places
- Implement the Commission’s remaining recommendations

5 years and beyond
Stage 3

- After 5 years, remove supply restrictions in both residential and community care
- Commission a public review
What does this mean for aged care providers?

The business issues for aged care providers associated with the proposed reforms for the aged care sector for Australia include:

- costs to business
- shift in provider funding models
- impacts on business models
  - increased competition
  - increased transparency
- workforce and training
- accounting issues
- importance of robust reporting systems.

**Costs to business**

Aged care providers will need to understand their cost structures to separate what it costs to provide care services and accommodation facilities, inclusive of their respective costs of capital and any subsidisation of Supported Places, to ensure these services are appropriately priced and charged to residents in a transparent manner. In the event that the distinctions in care are removed, providers will have greater flexibility to charge an accommodation bond, albeit they will need to consider how to set the level of bond and the periodic payment alternative options to ensure they are in line with the new regulatory framework and also ensure an adequate return on capital is generated.

**Shift in provider funding models**

The combination of the changes to the resident payment structures along with the introduction of the Australian Age Pensioners Savings Account Scheme and the Australian Age Care Home Credit Scheme may see a disincentive arise for residents to pay the accommodation bonds as opposed to making periodic payments. Providers will need to understand the impact of these changes, as this may see a reduced capacity to repay bonds of current residents leaving the facilities and may require an increase in debt funding to both repay these bonds and support further facility upgrades and development of new facilities. It will be critical for operators to undertake detailed modelling and planning of the implications of these changes to ensure the sustainability of their funding and business models.

**Impacts on business models**

"Older Australians generally want to remain independent and in control of how and where they live; to stay connected and relevant to their families and communities; and be able to exercise some measure of choice over their care." This statement and the recommendations contained in the Productivity Commission report have potential to significantly impact the business models of residential aged care providers. Key factors providers of services should consider include:

- There will be more competition with the market shifting from being supply driven as the supply-side limits on bed licences, community care packages and other services are lifted.
- The current distinction between residential low and high care and between ordinary and extra service status will be removed,
- As more people are choosing to stay at home longer they will tend to be frailer and older residents when they enter care - shifting the demand side further to high care or community based care.

The opening up of supply and promotion of a more competitive market requires providers to consider the appropriateness of their business models and refocus on the strength of their management skills.

**Key actions for current providers:**

- determine how well you know the business operationally and where the potential efficiencies will come from
- determine cost drivers and the levers to be used to flex them as required
- determine the demand drivers for your services.
- consider the overlap of services currently being provided in the provider portfolio
- determine the impact of having a single gateway referral process into your services
- determine the need or desire to broaden or diversify service offerings e.g. into providing community based care, if not already. Consider strategies and risks of this need/desire for the business going forward.
- understand the increased financial risks from competition and any changes to existing business valuations.

The Productivity Commission’s final report sees competition as a “powerful incentive for providers to improve quality and efficiency, and to offer care solutions that best address the needs of individuals.”
**Workforce and training**

The sector is facing a significant shortage of quality nursing and other aged care related skills. To lift the quality of care provided and improve attraction and retention of the workforce, aged care providers should be:

- incorporating the implications of associated workforce costs due to recommended changes to wages to nursing and other aged care staff (together with the changes to pricing of services discussed above), in the financial modelling undertaken by the provider, taking into account appropriate staffing levels, skills mix and remuneration arrangements
- considering the cost and workforce impacts of the improvement in quality of vocational education and training in the industry
- developing well articulated career paths and better management skills in the organisation.

**Accounting implications**

Financial reporting for aged care providers will be impacted once the government adopts the recommendations and sets out a timeline for transition.

Under the Productivity Commissions’ model of government subsidies for aged care being more directly linked to people rather than places, this is likely to mean that existing bed licences held by aged care providers no longer provide future economic benefits, that is, if the concept of bed licences is removed. In this case, there is bound to be a transition scenario.

Once a known date for implementation of the new model is determined, the useful life of bed licences currently on the balance sheet of an aged care provider would need to be reconsidered, and amortised over the period of transition such that they have a nil value on full implementation. This may also mean that some bed licences could be impaired, particularly in the case where these bed licences have been purchased for consideration.

**Asset impairment testing**

Of immediate concern to aged care providers will be the potential impact on asset impairment testing for financial statement reporting purposes.

Although it remains uncertain if the recommendations will be adopted, management should now be considering the expected impact of the removal of bed licences on cash flow projections for assets and cash generating units.

Whilst it is likely that uncertainty will still exist in relation to adoption of these recommendations, management should make, and disclose, any significant assumptions required to allow a best estimate cash flow to be derived.

**Importance of robust reporting systems**

Reporting systems used to collect data for reporting of costs of care, accommodation and other services, will form the basis of management’s determinations of appropriate fees and charges. It is critical for providers to implement systems able to collect and store relevant data to be used for management analysis and reporting.

**Is your business ready for aged care reform?**

Aged care providers that prepare now will be better placed to respond to future reform announcements. Scenario planning of strategic implications of a framework that heads in the direction of the proposed reforms is critical to ensure a sustainable business to operate in this new environment.
Why select us

KPMG has extensive experience in the provision of practical solutions to business issues in the aged care sector.

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