Australian Government
Department of Health

Meeting Brief
MB18-001264 Version (1)
Date sent to MO: 26/03/2018

To: Minister Hunt

cc: Minister Wyatt

Subject:

Minister Hunt …..…… **Date:** / /

Comments:

Contact Officer:	s22(1)(a)(ii)	Director, Funding Reform Section, Funding Policy and Prudential Branch	s22(1)(a)(ii)
Clearance Officer:	James Benson	A/g Assistant Secretary, Funding Policy and Prudential Branch, Residential and Flexible Aged Care Division	Ph: (02) 6289 8796 Mobile: s22(1)(a)(ii)

Date / Time: Tuesday 27 March 2018 / 11:00am-12:00pm

Location: M1.41, Parliament House

Purpose: s22(1)(a)(ii)

s22(1)(a)(ii)

Key Issues:

1. The Government is actively progressing work on long-term reform of residential aged care funding.

s22(1)(a)(ii)

Key Stakeholder Engagement:

- The current focus of the Government's residential aged care funding reform agenda is the Resource Utilisation and Classification Study (RUCS) currently being undertaken by the Australian Health Services Research Institute (AHSRI) at the University of Wollongong which commenced in March 2018. This comprehensive study is due to be completed around the end of 2018.

- Any decision on residential aged care funding reform will follow the completion of the RUCS, and extensive consultation with the sector.

Sensitivities:

- Residential care profitability results for the sector have declined over the 12 month period to December 2017 based on analysis by StewartBrown. The slow-down in ACFI growth and increasing cost pressures will be putting pressure on the sector, for the lower performers in particular. Media reports of cut backs to staffing highlight the sensitivities. Residential care profitability results for 2017 are provided at Attachment B.

s22(1)(a)(ii)

Attachments:

Attachment A Key discussion points (Meeting Brief)
Attachment B Residential Care Profitability – StewartBrown Results.
Attachment C Attendees Biographical details.

Attachment A
(Meeting brief)

Key discussion points and background

1. Residential Aged Care Funding Reform

- Work is underway to investigate alternative approaches to determining residential care funding that delivers more stable funding arrangements.
- The Government has been engaging with the sector on the development of this longer-term reform.

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Key Discussion Points

- Following higher than anticipated growth in Aged Care Funding Instrument (ACFI) expenditure, the Government announced a number of measures in 2015-16 and 2016-17 to control and mitigate growth.
- The Government is actively progressing work on long-term reform on residential care funding. The aim of this work is to develop a more stable and sustainable funding system that provides more stability and certainty for the sector and Government and better supports the delivery of quality care.
- The current focus of the Government's residential aged care funding reform agenda is the RUCS currently being undertaken by AHSRI which will commence in March 2018. This comprehensive study is due to be completed around the end of 2018.
- The RUCS is a landmark study which will provide a solid evidence base on what drives relative care costs in residential aged care, both at the resident level and facility level, essential to help inform Government decision making on reform options.
- Undertaking a RUCS was a key recommendation of AHSRI's report "Alternative Aged Care Assessment, Classification System and Funding Models Report". This report was commissioned by the Government to explore alternative options and tools for residential care funding arrangements, and was published in April 2017.
- The RUCS is designed around the recommended blended fixed/variable funding option identified in AHSRI's report, but will also provide an evidence base for all future funding reform options.

- In addition, the Government also commissioned a review of the existing ACFI tool, the "Review of the Aged Care Funding Instrument" by Applied Aged Care Solutions (AACS). This report examines options for significant amendments to ACFI to make it more contemporary and robust. This report was led by Richard Rosewarne, the designer of the current ACFI, and was published in October 2017.

- Any decision on residential aged care funding reform will follow the completion of the RUCS, and extensive consultation with the sector.

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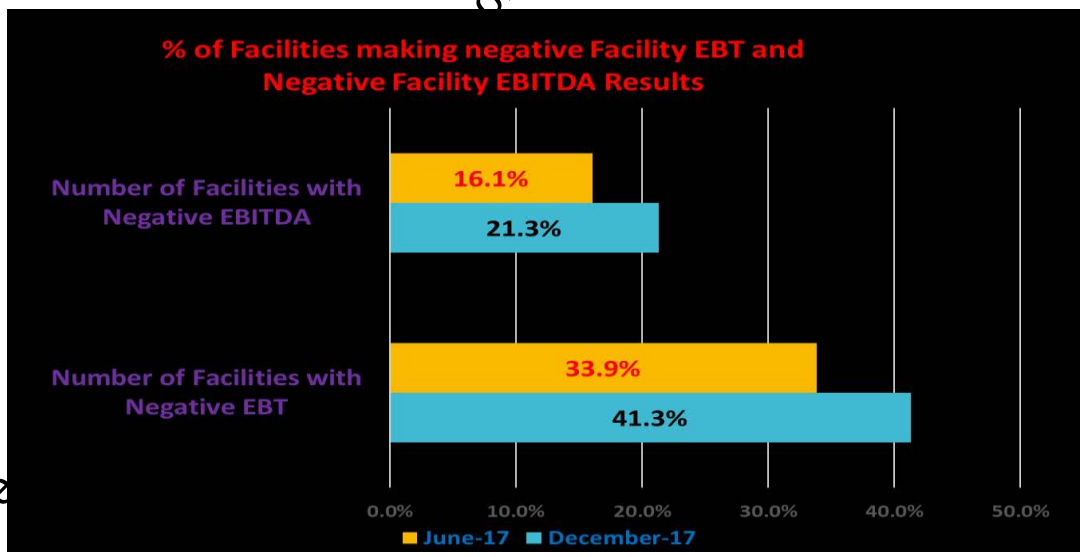
Attachment B

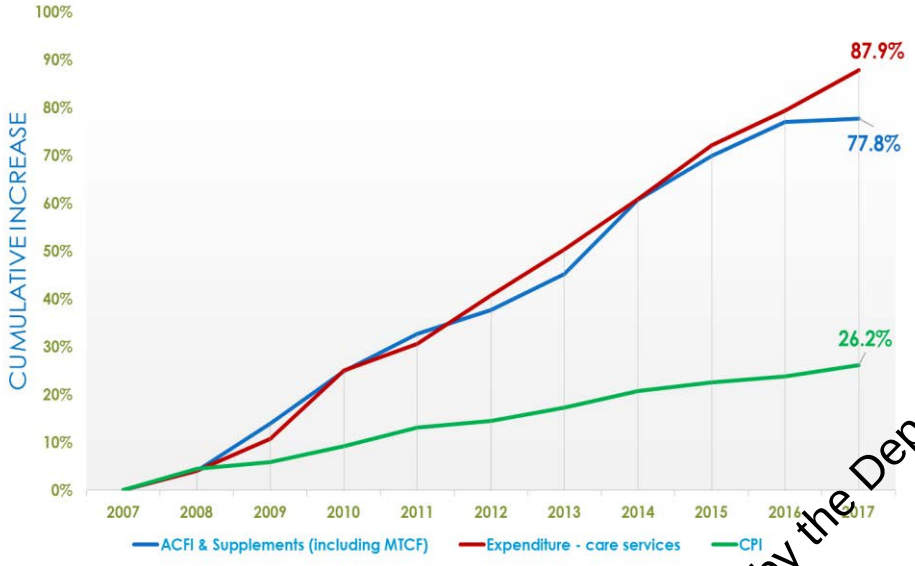
Residential Care Profitability

StewartBrown Results

- Financial Results for the sector have declined over the past 12 months based on analysis by StewartBrown.
- The latest StewartBrown report covers the period to December 2017. Key findings are:
  - The ACFI indexation freeze and other ACFI changes have decreased revenue growth (ACFI revenue growth has largely been flat) which has fallen behind growth in wage and other expenses resulting in reduction in earnings/profit;
  - A common performance measure is EBITDA (earnings before interest, tax, depreciation and amortisation). Facility EBITDA has continued to noticeably reduce:
    - From $9,404 per resident per annum (prpa) at Dec 16 to $8,397 (June 17) and $7,071 (Dec 17);
    - More facilities reporting negative EBITDA (21% of facilities compared to 16% at June 17);
  - Another measure is Net Profit Before Tax / Earnings Before Tax.
    - 41% are now recording negative NPBT/EBT compared to 34% at June 17. See chart.



  - The impact of slow/flat revenue growth (blue line) and increasing costs (red line) can be seen in chart below. While this does not take into account other revenue sources (accommodation, fees, investment) which contribute to overall EBITDA it highlights the financial pressures.



Top Quartile v. the Rest

- The top quartile of providers in StewartBrown continue to return much higher results than the average but also show a decline in results:
    - From EBITDA of $18,943 prpa at Dec 16 to $18,285 (June 17) and $17,760 (Dec 17);
    - This highlights the variability across the sector with the better providers still returning good results. While their earnings have declined it has not been as marked as for the lower performers.

ACFA Results

- ACFA's latest report only covers year to 30 June 2016 (before the ACFI changes took effect). That showed:
    - 17% with negative EBITDA;
    - 31% with a negative net profit;
    - ACFA noted in that report that they expected financial results to deteriorate as the ACFI measures took effect.
- StewartBrown results reflect a survey and can be somewhat worse than the whole of sector ACFA results as StewartBrown predominantly covers not for profit providers who in general have lower financial results (and may not aim to maximise profit as much as for profit providers).
    - Nevertheless trends in StewartBrown data (such as reducing profit/EBITDA) are likely to be the same across the industry.
- Historically, based on ACFA figures, the percentage of providers having negative NPBT or EBITDA has been relatively stable (around 15-20% negative EBITDA and around 30-34% negative NPBT). Negative profit does not necessarily mean a provider is not able to continue operations. As noted above profit may not be the driving motive for providers in the not for profit sector and they may also finance their operations from other sources and being part of a broader group.

- There was an increase in providers with negative profit of around 4 percentage points (from 30% to 34%) when reductions to ACFI happened previously in 2012 but this proved to be temporary (helped in part by later reforms - higher accommodation supplement, roll-in of workforce supplement to subsidies etc - which were positive for the sector in the Living Longer Living Better package).

Commentary

- As noted in the Information Brief from January, the slow down in ACFI growth and increasing cost pressures will be putting pressure on the sector, for the lower performers in particular. Media reports of cut backs to staffing highlight the sensitivities.
- The reduction in profit/earnings continues to be evident in the StewartBrown analysis. How providers respond will depend very much on the management of the facility and other factors (parent entity support etc). The return to mostly full indexation from 1 July 2018 will also help but there are not the same revenue friendly reforms as helped restore profitability after 2012.

Australian Government
Department of Health

Meeting Brief

MB18-001467
Date sent to MO: 01/05/18

To: Minister Wyatt

s22(1)(a)(ii)

Contact Officer:	s22(1)(a)(ii)	*Director, Funding Reform Section*	s22(1)(a)(ii)
Clearance Officer:	*Nigel Murray*	*Assistant Secretary, Funding Policy & Prudential Branch*	Ph: (02) 6289 8796 s22(1)(a)(ii)

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Key Facts:

1. Following higher than anticipated growth in ACFI expenditure, the Government announced a number of measures in 2015-16 and 2016-17 to control and mitigate growth. This included changes to the ACFI tool and a full indexation freeze in 2017-18. While full indexation will apply from 1 July 2018 to the Activities of Daily Living and Behaviour elements of ACFI, there will be a 50 per cent indexation pause to the Complex Health Care Domain in 2018-19.

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Sensitivities:

- According to analysis by Stewart Brown, residential aged care financial performance results (earning before tax) have declined over the 12 month period to December 2017. This is attributed to a slow-down in ACFI growth and increasing cost pressures e.g. wage cost rises above inflation and price increases on equipment. Media reports of cut backs to staffing also highlight this sensitivity.

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- The Government notes these results on financial performance, and is undertaking the Resource Utilisation Classification Study to better understand the relative costs of the residential aged care system.

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1. The 2016-17 Budget changes to residential aged care funding

- The Australian Government is providing estimated funding of $18.6 billion in 2017-18 to support aged care consumers and the sector.
- Government spending on aged care will continue to grow over future years and is expected to reach over $22.3 billion by 2020–21. The Government is committed to having an aged care system that supports older Australians while ensuring aged care expenditure is affordable and sustainable.
- Due to a much higher than anticipated growth in funding claims, the Government increased funding estimates for residential aged care over the forward estimates by an additional $3.8 billion in light of higher than anticipated growth in funding claims. As a responsible fiscal manager, Government had to take action to ensure growth is sustainable. The 2016–17 Budget measures reduced the unexpected growth by
- $2 billion over the forward estimates.
- Funding to the residential aged care sector will continue to grow over the forward estimates.
- These measures do not change the requirements on providers to provide quality care to residents, with the *Aged Care Act 1997* setting out the responsibilities approved providers must meet including quality of care standards. The standards require aged care providers to ensure there are adequate numbers of appropriately skilled staff to meet the care needs of residents. These requirements are monitored by the Australian Aged Care Quality Agency in its assessment of an aged care home against the standards.

2. Residential aged care funding reform

- The Government is actively progressing work on long-term reform on residential care funding. The aim of this work is to develop a more stable and sustainable funding system that provides more stability and certainty for the sector and Government and better supports the delivery of quality care.
  The current focus of the Government's residential aged care funding reform agenda is the Resource Utilisation and Classification Study (RUCS) currently being undertaken by the Australian Health Services Research Institute (AHSRI) at the University of Wollongong which commenced in March 2018.
- This landmark study will provide a solid evidence base on what drives relative care costs in residential aged care, both at the resident and facility level, essential to help inform Government decision making on reform options.
- Any decision on residential aged care funding reform will follow the completion of the RUCS, and extensive consultation with the sector.

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MINISTERIAL INFORMATION REQUEST

MB18-002236
Date Sent to MO:<dd/mm/yy>

MINISTER: Ken Wyatt

s22(1)(a)(ii)

- The Government is committed to having an aged care system that supports older Australians while ensuring aged care expenditure is affordable and sustainable.

- Total Australian Government spending on aged care including residential aged care will continue to grow over future years and is expected to reach around $23.6 billion per year by 2021-22.

- Residential care providers have benefited from major reforms in recent years, including changes from 1 July 2014 including a 2.4 per cent increase in subsidies, the deregulation of accommodation payments and the higher rate of Government accommodation supplement.

- The Government is aware that while some providers are producing strong results, others are reporting losses and this was highlighted in the recent StewartBrown report.

- In 2016, due to a much higher than anticipated growth in funding claims, the Government increased funding estimates for residential aged care over the forward estimates by an additional $3.8 billion. As a responsible fiscal manager, the Government had to take action to ensure future expenditure growth was sustainable. In the 2016–17 Budget, the Government announced measures aimed to reduce future growth by $2 billion over the forward estimates.

- One of these changes included an indexation pause for all ACFI domains in 2017-18. The majority of indexation for the ACFI will return in 2018-19, which will increase funding for the sector.

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- The Department of Health has commissioned a residential aged care resource utilisation and classification study to empirically determine the characteristics of residents that drive residential care costs. The study will also design and test a new residential classification system and funding model. This study is due to be completed around December 2018.

- No decision has been taken by Government on reform options and any decision will follow further consultation with the sector.

Background:

<u>The Resource Utilisation and Classification Study (RUCS)</u>

The Government has commissioned reports on options for funding reform and commenced a landmark Resource Utilisation and Classification Study (RUCS) to determine a solid evidence base on what drives care costs in residential aged care, both at the resident level and facility level. The study, which is currently underway, and will be finalised around the end of 2018, will inform Government's consideration of funding reform options.

The study will:

- Identify those clinical and need characteristics of aged care residents that influence the cost of care (cost drivers);

- Identify the proportion of care costs that are shared across residents (shared costs) relative to those costs related to an individual's needs (variable costs);

- Develop a casemix classification based on identified cost drivers that can underpin a funding model that recognises both shared and variable costs;

- Test the feasibility of implementing this classification and funding model across the Australian residential aged care system.

Minister	**Ken Wyatt**
PDR Number	**MB18-002236**
Issue	**MIR - Minister Wyatt - Maksymow Corro**
Contact Officer	s22(1)(a)(ii)
Clearance Officer	**Nigel Murray** **(02) 6289 8796** s22(1)(a)(ii)
Division/Branch	**Residential and Flexible Aged Care**

Adviser/DLO Comments:

Return for Redraft ☐

Australian Government
Department of Health

Meeting Brief

MB18-004537
Date sent to MO:17/10/18

To: Minister Wyatt
s22(1)(a)(ii)

Contact Officer:	s22(1)(a)(ii)	Director Aged Care Quality and Regulatory Reform Branch	s22(1)(a)(ii)
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s22(1)(a)(ii)

3. Aged care funding

- Total Australian Government spending on aged care including residential aged care will continue to grow over future years and is expected to reach around $23.6 billion per year by 2021-22.
- The current focus of the Government's residential aged care funding reform agenda is the Resource Utilisation and Classification Study being undertaken by the Australian Health Services Research Institute at the University of Wollongong. The study will provide a solid evidence base on what drives relative care costs in residential aged care, both at the resident and facility level, and is essential to help inform decision making on reform options.
- Further details on residential aged care funding are at Attachment D.

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Aged care funding

- The Government is committed to supporting a sustainable high quality residential care sector. That is why the Government is continuing to actively progress work on reform options for residential aged care funding.
- The Resource Utilisation and Classification Study is progressing well and is set to be completed around the end of the year.
- No decisions have been taken by Government on residential aged care funding, and any decision will follow further consultation with the sector.
- The Government is aware of the findings of the StewartBrown report and that while some providers are producing strong results, others are reporting losses.
- The residential care sector is funded via subsidies paid under the Aged Care Funding Instrument and the majority of these subsidies have returned to indexation from 1 July 2018 increasing funding for the sector.
- Rural and remote providers are provided additional funding over and above Aged Care Funding Instrument (ACFI) subsidies through a Viability Supplement.

ATTACHMENTS

Attachment D: Aged Care Funding and other issues

Attachment D

Aged Care Funding and other issues

Residential aged care funding

- Due to a much higher than anticipated growth in funding claims, the Government increased funding estimates for residential aged care over the forward estimates by $3.8 billion. As a responsible fiscal manager, Government had to take action to ensure growth is sustainable. The 2016–17 Budget measures were aimed at reducing the unexpected growth by $2 billion over the forward estimates, leaving a net increase in funding to the sector of $1.8 billion. The measures included changes to the ACFI tool and indexation freezes.
- ACFI expenditure was below budget in 2017-18, and, if current trends continue, will be below budget in 2018-19.
- The sector is likely to view growth below budget forecasts as the changes having a deeper impact than Government had intended.
- In addition, in the 2018-19 Budget, the Australian Government announced additional funding of $40 million for infrastructure investment in regional, rural and remote aged care.

Summary of StewartBrown Aged Care Financial Performance Survey

- The June results show a further deterioration in results (i.e. the proportion of facilities reporting a loss) since the March quarter, continuing the previous trend. Profitability also increases in metropolitan areas compared to regional and remote areas.
- These results reflect cost increases (largely wages) continuing to exceed revenue growth (particularly with the ACFI indexation freeze still in place in the June quarter, though indexation mostly returned from 1 July).
- 45% of facilities in their survey group now reporting a loss. This is up from 43% at the March quarter and 34% at 30 June 2017.
    - As noted previously, there has historically been around 1/3 of providers making a loss.
    - Using the other common performance measures of Earnings Before Interest Tax Depreciation and Amortisation (EBITDA) there are 21% reporting negative EBITDA. This is no change from March but up from 14% at 30 June 2017.
- Inner Regional at 47% making a loss compared to 36% at 30 June 2017 (23% negative EBITDA now versus 13% at 30 June 2017).
- Outer Regional and Remote at 63% making a loss compared to 52% at 30 June 2017 (38% negative EBITDA now v. 25% at 30 June 2017)
- The top 25% continue to report much better results, though these have also seen a decline.
    - Top 25% have average net profit of $10,637 per resident per annum versus $810 for sector in total.
- Metro areas have average net profit per resident of $1,507 versus $246 for inner regional and a loss of $2,336 for outer regional and remote.
- Stewart Brown have added analysis predicting results for the 2018-19 year. These predictions show that results will continue to deteriorate in 2018-19 but not at the same rate as in 2017-18 (reflecting that indexation is returning but still running below the expected wage costs growth going forward).

QB18-000316

Date QTB created: 18 September 2018
Last Updated by Department: 16 October year
Last Updated by Adviser: day month year

AGED CARE FUNDING REFORM

BUDGET

	2012-13 (ACTUAL) ($m)	2017-18 (ACTUAL) ($m)	2018-19 (BUDGET) ($m)	2019-20 (BUDGET) ($m)	2020-21 (BUDGET) ($m)	2021-22 (BUDGET) ($m)	Total 2018-19 to 2021-22 ($m)
TOTAL AGED CARE FUNDING	**13,327.5**	**18,086.68**	**19,764.5**	**21,103.1**	**22,185.4**	**23,602.7**	**86,655.7**
INCREASE IN SPEND OVER PREVIOUS PERIOD			**SEE NOTE**	**1,338.6**	**1,082.3**	**1,417.3**	
GROWTH (%)			**SEE NOTE**	**6.8%**	**5.1%**	**6.4%**	

Note: Figures will be included once forward estimates have been set at MYEFO.

KEY POINTS

- The Government is not planning any changes that would reduce funding to aged care.
- Annual funding will increase to record levels by $5.5 billion over the forward estimates from $18.1 billion in 2017-18 to $23.6 billion in 2021-22.
- The Australian Government is providing record aged care funding of $19.8 billion this year, of which $15.2 billion is residential and home care.
- Aged care spending has increased by an average of more than 6% each year.
- That is, on average, $1 billion of extra support for older Australians each year. We are adding an additional 13,500 residential aged care places and 775 short term restorative places.
- Based on the latest data, in 2017-18, the average Australian Government payment (subsidy plus supplements) for a permanent resident in residential care was $66,000 per resident; this compares to $53,100 in 2012-13, which was Labor's last full financial year. This is an increase of $12,900 per resident or 24.3%.
- Since the last budget we are delivering 20,000 new high level home care packages to support senior Australians to remain at home longer.
- By 2021-22, over 74,000 high level home care places will be available, an increase of 86 per cent on 2017-18.

- Over $100 million investment in mental health services for ageing Australians in the community and in residential aged care, consisting of:
    - A $20 million trial to improve mental health services for Australians over 75 years of age.
    - $82.5 million in new mental health services for people with a diagnosed mental disorder living in residential aged care facilities.
- On 12 September 2018 we announced an additional $16 million to police quality in aged care.
- We are also bringing forward $90 million this financial year to support quality in residential aged care and aged care capital works in regional, rural and remote Australia.
- The Government is also examining options for a more stable, certain and efficient residential care funding tool to replace the current Aged Care Funding Instrument (ACFI), which has been recognised by the independent Aged Care Financing Authority as no longer being contemporary, as inefficient, too subjective and lacking stability in outcomes.
- Development of a new funding tool is being led by the University of Wollongong who will provide a report to the Government by the end of this calendar year. Any new tool adopted by Government will involve a better and more efficient way of allocating the funding pool – the Government is not considering any options that would reduce the funding pool.

KEY FACTS AND FIGURES

Table 1. Average Australian Government payments (subsidies plus supplements) and cumulative increase since 2012-13 for each permanent residential care recipient, 2012-13 to 2017-18

	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18*
Average payment	$53,100	$56,100	$60,200	$63,400	$65,500	$66,000
Cumulative increase since 2012-13		$3,000	$7,100	$10,300	$12,400	$12,900

* preliminary - subject to change

IMPACT ON REGIONAL AUSTRALIANS

- Any new funding tool will examine the costs being incurred by facilities in regional Australia to allow these costs to be better reflected in funding outcomes.

QB18-000316

Date QTB created: 18 September 2018
Last Updated by Department: 16 October year
Last Updated by Adviser: day month year

IF ASKED

If asked about funding cuts to ACFI

- ACFI growth in 2014-15 and 2015-16 was around 2 percentage points higher than predicted.
- As a result Government made estimates variations at MYEFO 2015 and Budget 2016-17 which increased estimated residential care expenditure over the forward estimates by around $3.8 billion.
- The growth in estimated funding in 2015-16 could not be attributed to natural growth in frailty alone.
- A natural growth in frailty would occur gradually over time and not lead to claiming growth in certain parts of one domain of ACFI (the complex health care domain) alone.
- Rather increases in funding claims would have been spread more evenly within the complex health care domain and more evenly spread across the other areas of ACFI (activities of daily living and behaviour domains).
- The Government announced measures at MYEFO 2015 and Budget 2016-17 to mitigate the impact of this higher growth. These included changes to the ACFI tool and indexation freezes. The impact of these measures was to reduce growth by $2 billion over the forward estimates. Overall, growth still increased by $1.8 billion.
- The Government's approach in 2016-17 was consistent with that taken by the then Government in 2012 when unanticipated growth in ACFI funding claims also led the then Government to pause indexation for a year and make changes to the ACFI tool (to address concerns of 'over claiming' under the tool) to constrain growth to more sustainable levels – largely the same actions taken by the Government in 2016-17.
- In 2012 ACFI changes and an indexation pause resulted in a $1.1 billion saving.
- The 2016-17 changes to the ACFI tool focused on changes to the Complex Health Care (CHC) domain as that had been where the highest growth in claims had been occurring.
- Funding paid to providers is not 'earmarked' for particular residents but is pooled by providers and then used in the most efficient way to deliver the quality of care to all residents required by Quality Standards. Changes to CHC should not directly reduce care for any individual resident.

- At the time of the ACFI changes the Government also significantly increased the viability supplement:
    - $102.3 million over four years was provided in the 2016-17 Budget to target the viability supplement more effectively to the areas of greatest need.
    - In addition, the viability supplement was increased by $2.12 per care recipient per day from 1 July 2017 at a cost of $19.3 million over 4 years.

If asked about payments by ACFI domain

- The following table details average ACFI payments by domain from 2012-13 to 2017-18.
- The average funding for ACFI has increased each year in aggregate summing together all 3 domains.
- The ACFI changes commenced from 1 July 2016 (the MYEFO ACFI changes took effect from 1 July 2016 and the Budget changes took effect from 1 January 2017).

Table 2: Average Australian Government payments by ACFI domain for permanent residential care recipient, 2012-13 to 2017-18

	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18*
Average ACFI payment	$46,100	$48,000	$56,800	$60,700	$62,600	$62,700
- **ADL**	$25,400	$26,200	$30,500	$32,100	$33,100	$33,500
- **BEH**	$7,700	$7,900	$9,200	$9,700	$10,000	$10,100
- **CHC**	$13,000	$13,900	$17,100	$18,900	$19,500	$19,100

Note: ACFI expenditure in 2014-15 includes rolling in of the Conditional Adjustment Payment (equivalent to 8.75% of the basic subsidy) and the one-off 2.4% increase to subsidies due to the redistribution of the Workforce Supplement. This contributes to large growth in expenditure in that year that is not attributable to ACFI claiming.

Options for reforming ACFI

- Two reports were commissioned to examine options for reform to the funding tool.
- One report was from Applied Aged Care Solutions which looked at options to amend but retain the ACFI tool.

- The option for a new tool being considered by Government is that put forward by the University of Wollongong and is being informed by a detailed Resource Utilisation and Classification Study (RUCS) which is currently well under way. The University's option does not involve any reduction to the funding pool but rather a more efficient and effective and stable tool for allocating the funding pool. The University's report is due at the end of the calendar year.

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Cleared by: Deputy Secretary	Dr Margot McCarthy	Work Phone: 02 6289 1479	Mobile Phone s22(1)(a)(ii)

In-depth Analysis of Winners and Losers Post 2016-17 ACFI Measures

Real growth (note: all dollars are in 2017-18 values) in the ACFI has slowed down considerably since the introduction of the 2016-17 growth deterrent measures.

At national level, the average ACFI recorded nil growth in 2017-18 over 2016-17 and an annualized growth of 1.1% since the introduction of the measures (see Table 1a). If viability supplement (VS) were to be distributed among all providers (which is not the case), the annualized growth since the introduction of the measures rises to 1.2%. What the latter demonstrates is that Government expenditure per Residential care recipient rose annually by 1.1% prior to VS and by 1.2% post VS.

VS per resident increased by close to 50% (48.6%) nationally since the introduction of the measures. However, this translated to only 0.2% increase in the national average subsidies (see Table 1a). VS for eligible providers increased by 41% and this translated to 0.4% increase in their subsidies (see Table 1b). On average VS contributes an additional $2.00 per resident day for eligible providers (see Table 1b and Figure 1)

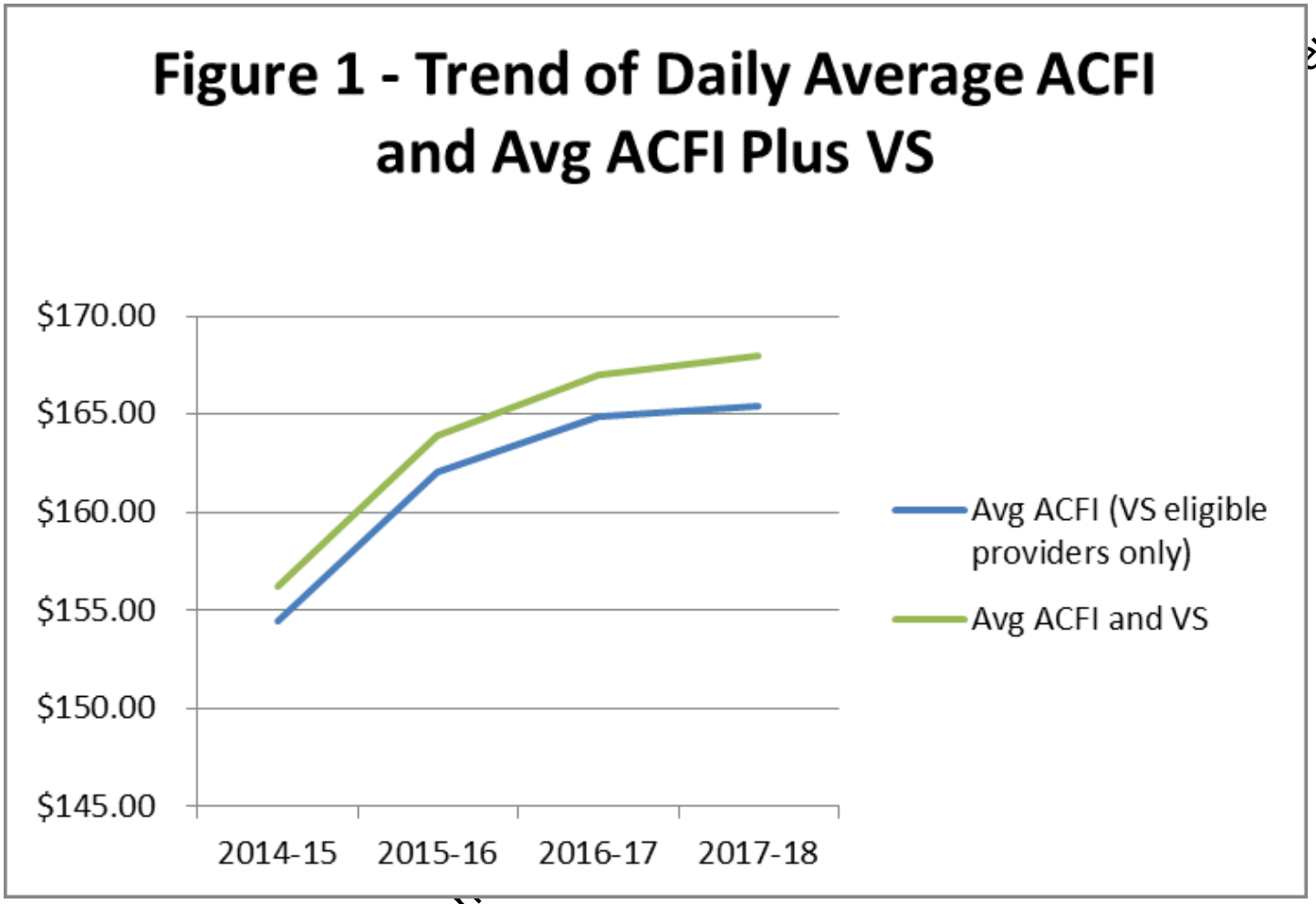
In as much as no growth was recorded in the national average ACFI in 2017-18, some providers still made a gain, while others suffered a loss. This paper seeks to measure those gains and losses and assess whether specific characteristics could be attributed to winners and losers. In other words, it would look at whether specific groups were disproportionately disadvantaged/advantaged relative to others. Emphasis will be on providers/services receiving viability supplement.

Table 1a - Trend of National Average ACFI and Viability Supplement (VS) - All Providers

	2014-15	2015-16	2016-17	2017-18	2017-18 vs 2015-16	Annualized Post Mea Growth
Avg National ACFI	$ 159.70	$ 168.28	$ 171.93	$ 172.01	$ 3.74	$ 1.87
Avg VS (Shared among all Providers)	$ 0.57	$ 0.58	$ 0.68	$ 0.86	$ 0.28	$ 0.14
Avg Nat ACFI and VS	$ 160.27	$ 168.85	$ 172.61	$ 172.87	$ 4.02	$ 2.01
Avg ACFI annual growth		5.4%	2.2%	0.0%	2.2%	1.1%
Avg VS annual growth		1.2%	18.0%	25.9%	48.6%	21.9%
Aggregated annual growth		5.4%	2.2%	0.2%	2.4%	1.2%

Table 1b - Trend of Average ACFI and Viability Supplement - VS eligible Providers only

	2014-15	2015-16	2016-17	2017-18	2017-18 vs 2015-16	Annualized Post Mea Growth
Avg ACFI (VS eligible providers only)	$ 154.46	$ 162.07	$ 164.89	$ 165.40	$ 3.33	$ 1.67
Avg VS	$ 1.76	$ 1.85	$ 2.10	$ 2.61	$ 0.76	$ 0.38
Avg ACFI and VS	$ 156.22	$ 163.92	$ 166.99	$ 168.02	$ 4.09	$ 2.05
Avg ACFI annual growth		4.9%	1.7%	0.3%	2.1%	1.0%
Avg VS annual growth		5.2%	13.3%	24.4%	40.9%	18.7%
Aggregated annual growth		4.9%	1.9%	0.6%	2.5%	1.2%



Winners and Losers – Volume and Weight

Prior to the introduction of the measures in 2016-17, an average of 79% of providers used to record a positive growth in their average daily ACFI. This rose by 1 percentage point if VS were to be included (see Table 2a). The worst absolute loss in average ACFI revenue recorded by a provider prior to the measures was $30.44 (without VS) or $27.36 (with VS). s22(1)(a)(ii)

s22(1)(a)(ii)

Table 2a -Weight and Volume of Winners and Losers Before and After VS (Provider Level)

	Before Viability Supplement				After Viability Supplement		
	2015-16	2016-17	2017-18		2015-16	2016-17	2017-18
Winners	79%	67%	44%		80%	69%	48%
Losers	21%	33%	56%		20%	31%	52%
Minimum Annual Abs Growth	-$ 30.44	-$ 27.59	-$ 51.27		$ 27.36	-$ 27.59	-$ 51.27
Maximum Annual Abs Growth	$ 69.57	$ 76.89	$ 44.25		$ 69.57	$ 74.62	$ 46.27
Minimum Annual Growth Rate	-19%	-19%	-32%		-14%	-19%	-32%
Maximum Annual Growth Rate	105%	92%	53%		88%	89%	47%

Relative to their average ACFI revenue, the worst loss recorded by a provider prior to the measures was 19%. This grew significantly to 32% after the measures indicating that some providers lost about a third of their ACFI revenue.
The highest absolute gain in average ACFI revenue recorded by a provider prior to the measures was $69.57 (with and without VS). This dropped significantly to $44.25 (without VS) or $46.27 (with VS), indicating that the best performing provider (in ACFI growth terms) in 2017-18 received VS.

Relative to their average ACFI revenue, the highest gain recorded by a provider prior to the measures was 105%. This dropped significantly to 53% after the measures indicating that some providers doubled their ACFI revenue from year to year prior to the measures.

At service level, all of the above results tend to be amplified and this is mainly attributable to size (see Table 2b

Table 2b -Weight and Volume of Winners and Losers Before and After VS (Service Level)

	Before Viability Supplement				After Viability Supplement		
	2015-16	2016-17	2017-18		2015-16	2016-17	2017-18
Winners	80%	65%	47%		80%	66%	50%
Losers	20%	35%	53%		20%	34%	50%
Minimum Annual Abs Growth	-$ 37.75	-$ 35.43	-$ 57.65		-$ 37.75	-$ 35.37	-$ 51.36
Maximum Annual Abs Growth	$ 81.48	$ 86.49	$ 61.32		$ 81.48	$ 86.49	$ 198.50
Minimum Annual Growth Rate	-21%	-19%	-32%		-22%	-26%	-32%
Maximum Annual Growth Rate	105%	98%	58%		98%	98%	120%

Prior to the introduction of the measures, 80% of services were winners and 20% were losers after building in viability supplement (see Table 2C). Post measures 51% of services became losers. However 9% of all services (or 18% of all post-measures losers) were already losers before the measures were introduced. Interesting to look at are the 41% of all services that used to be winners prior to the measures and who became losers after the measures.

Table 2C - Distribution of Winners and Losers before And after the measures

	Post Measures		
Pre Measures	**Winners**	**Losers**	**Total**
Winners	39%	41%	80%
Losers	11%	9%	20%
Total	**49%**	**51%**	**100%**

SB18-000152

BRIEF

Budget Estimates 2018 - 2019

RESIDENTIAL CARE VIABILITY/PROFITABILITY

SUBJECT / ISSUE:

To summarise the financial performance of the residential sector as reported by The Aged Care Financing Authority (ACFA) and StewartBrown, and report on the work being undertaken to address residential aged care funding.

KEY POINTS

- ACFA's most recent annual report (July 2017) showed an improvement in the financial performance of residential care providers in 2015-16 (ACFA's next report is due in June 2018).
- The more recent StewartBrown survey results for December 2017 has shown that the profitability (average annual facility results) of residential care providers (predominantly comprising of not-for-profit providers) has decreased since June 2017.
- The return to indexation of the majority of the Aged Care Funding Instrument (ACFI) subsidies from 1 July 2018 will increase funding for the sector.
- The Resource Utilisation and Classification Study (RUCS) is currently being undertaken by the Univeristy of Wollongong to inform the next step in the residential aged care funding reform process.

KEY FIGURES

- The Government is the principal funder of aged care providing estimated funding of $18.6 billion in 2017-18. Government spending on aged care will continue to grow over future years and is expected to reach around $23.6 billion by 2021-22.

Key 2015-16 figures reported by ACFA in July 2017 report

- In 2015-16 total revenue increased by 8.6 per cent to $17.4 billion, while total expenses increased 8.1 per cent to $16.3 billion.
- Total Earnings before Interest, Taxes, Depreciation, and Amortisation (EBITDA) increased 11.8 per cent to $1,985 million, up from $1,776 million.
- Average EBITDA per resident per annum increased from $10,222 to $11,134 or 8.9 per cent, while the EBITDA margin increased to 11.6 per cent (11.2 per cent June 15).
- Top quartile EBITDA per resident per annum increased from $23,687 to

$25,254 or 6.6 per cent, while the EBITDA margin decreased slightly by 0.1 per cent to 23.8 per cent.

- 69 per cent of providers achieved a net profit, up from 68 per cent.
- Total Net Profit Before Tax (NPBT) increased from $907 million to $1,063 million, an increase of 17.2 per cent.

StewartBrown Key Figures – December 2017

- StewartBrown's December 2017 survey reported average residential facility Earnings Before Taxation (EBT) of $1,617 per bed per annum, compared to $3,236 in June 2017 (-50.0 per cent).
- The survey also reported top quartile residential facility EBT of $12,319 per bed per annum, compared to $13,102 in June 2017 (-6.0 per cent).
- They concluded that the combined consequences of the COPE freeze, ACFI amendments and ACFI downgrades have had a significant effect on financial performance. While ACFI has stabilised, staff costs have increased at a much higher rate than inflation.

IMPACT ON REGIONAL AUSTRALIANS

- Residential aged care homes in rural and remote Australia represent a higher proportion of the unprofitable homes in the sector. The Government continues to support the rural and remote sector with the Viability Supplement, new capital grants and the Aged Care Approvals Round.

Subject Matter Lead:	Nigel Murray, Assistant Secretary, Funding Policy Branch	Work Phone 02 6289 8796	Mobile Phone s22(1)(a)(ii)
Cleared by:	Jaye Smith, Acting First Assistant Secretary, Residential and Flex ble Aged Care Division	Work Phone 02 6289 4522	Mobile Phone s22(1)(a)(ii)

Australian Government
Department of Health

Information Brief

MB18-000199
Date sent to MO: 19/01/2018

To: Minister Wyatt

Subject: VIABILITY OF RESIDENTIAL AGED CARE SERVICES

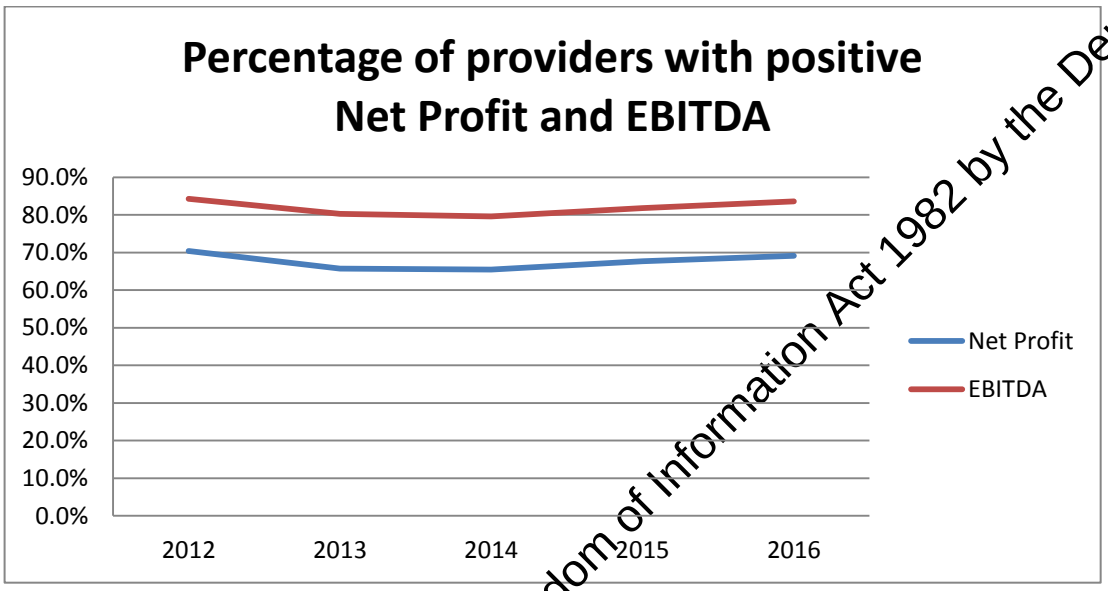
Minister Wyatt ..... **Date:** / /			
Comments:			
Contact Officer:	s22(1)(a)(ii)	*Financial Analyst, Funding Policy & Prudential Branch , Residential & Flexible Aged Care Division*	s22(1)(a)(ii)
Clearance Officer:	*Margot McCarthy*	*Deputy Secretary, Aged Care, Sport and Population Health Group*	Ph: (02) 6289 1479 s22(1)(a)(ii)

Key Issues:

1. Your Office requested a brief on the viability of residential aged care services and any information on the number of potentially vulnerable facilities.
2. Information and aggregated analysis on the financial performance of residential care services is available from the Aged Care Financing Authority (ACFA) annual reports (which use the annual financial reports that all providers are required to lodge with the Department as its information source) and quarterly private sector surveys, such as the StewartBrown quarterly performance surveys, which are based on survey data from 33% of facilities.
3. While the ACFA reports are more comprehensive in terms of covering the entire sector the StewartBrown reports are more timely (though are predominantly based on the generally lower performing Not for Profit sector). ACFA reference the StewartBrown results in their reports to provide commentary on more recent developments.

Profitability

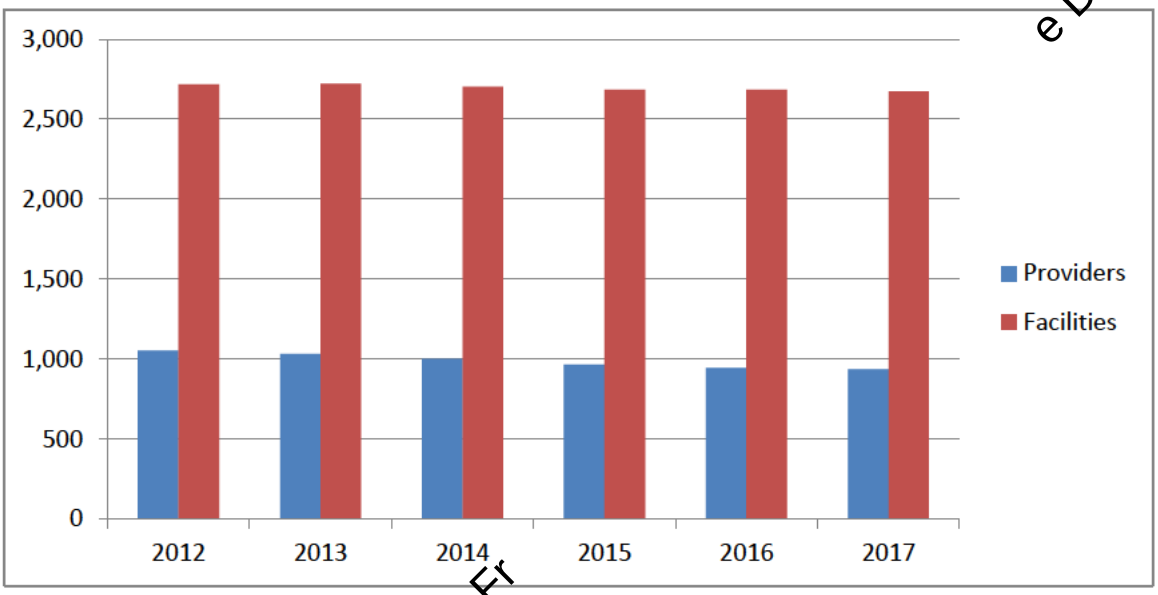
4. The most recent ACFA report covers the period up to 30 June 2016. This provides an indication of the aggregate performance of the sector over time. As can be seen in the chart below 69% of providers reported a net profit (blue line) for the 2015-16 year. The number recording a positive Earnings Before Interest, Tax, Depreciation and Amortisation (EBITDA) is higher (red line). EBITDA is commonly used in the sector as a measure of performance as it removes the potentially distortionary effects of different financing methods and accounting decisions on profit. The percentage recording a positive Net Profit and positive EBITDA has been reasonably consistent over time.



Impacts of Aged Care Funding Instrument (ACFI) changes

5. The chart above does not take into account the post 30 June 2016 changes to mitigate ACFI growth which reduced growth in ACFI funding in 2016-17 and 2017-18. More recent data from StewartBrown indicates these changes have contributed to a subsequent drop in performance.
6. In particular, ACFA noted in its most recent report that *"For the nine months to March 2017, StewartBrown reports that residential care providers have seen a decline in average results for the 2016-17 financial year-to-date as ACFI changes made to date have taken effect. StewartBrown has identified at this stage, cost management is the key differentiator between those provider facilities that continue to show stable results and those whose results have declined. StewartBrown results showed that average care results for the nine months to March 2017 were around 8 per cent lower than the results for 2015-16 and the facility EBITDA decreased by around 4 per cent over the same period. . . . the financial result reported by the StewartBrown survey population for the nine months to March 2017 could broadly reflect the trend experienced by the sector as a whole. However, the full impact of the 1 July 2016 ACFI changes and the progressive implementation of the other ACFI and indexation changes, together with the recent national wage case decision which increased minimum wages by 3.3 per cent, may be expected to contribute to a decline in financial performance over time"*.

7. StewartBrown reported that increases in costs for care labour and other operating expenses such as utilities and administration have been difficult to balance with slower growth in ACFI.
8. It can be expected that the number recording a net profit in 2016-17 is likely to fall from the 69%. It is of note that the changes made to ACFI are similar in magnitude to those made in 2012 when ACFI growth was previously an issue. It can be seen from the graph above that the number recording a net profit dropped from 70% in 2012 to 66% in 2013 when those changes took effect but then stabilised with the number making a profit growing gradually back up towards 70%.
9. There was also little change in the number of providers/services exiting the sector after the 2012 changes as can be seen in the chart below. In fact the slow but steady consolidation has also occurred in the more profitable years subsequent to 2012-13.



Note: Japara consolidated 36 provider identifications into the 1 provider identification in 2016-17. The graph above has not been adjusted to reflect this administrative adjustment

Failure to make a profit does not necessarily mean a provider is not viable

10. Headline figures such as profit numbers do need to be treated with some caution as they will not always reflect the ongoing viability of a business, particularly for the Not for Profit sector. Failure to make a profit does not mean a provider is necessarily at risk of failure, it may reflect a different approach to their business.
11. ACFA commented on this in page 103 of their most recent report

Operating performance continues to vary across provider ownership type, remoteness location and provider scale. The following commentary provides analysis across the segments of providers. Overall, for-profit providers have continued to outperform the not-for-profit and government providers in terms of EBITDA margin and Net Profit margin (Charts 9.8 and 9.9). However, this variable needs to be considered carefully because providers in the not-for-profit and government sectors often have different business motives, business models and funding sources and often operate in areas affected by the impacts of location and facility size. ACFA notes commentary from the not-for-profit sector that the generally lower operating financial results may be consistent with their community or religious missions. They may fulfil their charters in a range of ways that might be difficult or inappropriate in a more commercial environment

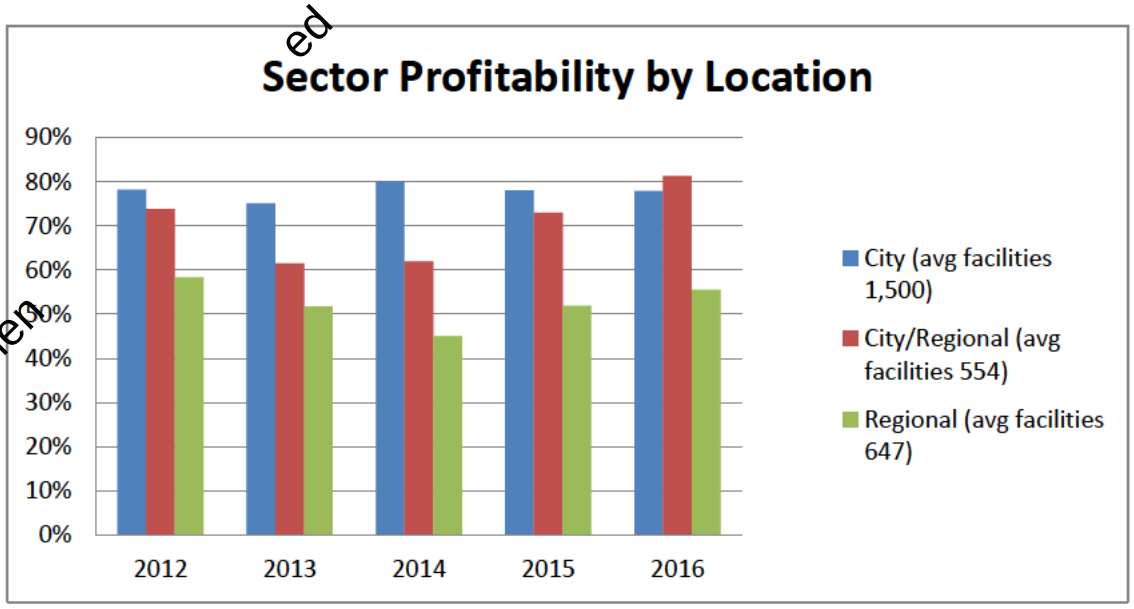
where investors are seeking returns. Specifically, not-for-profit providers may choose to invest in or expend funds on amenities and services for which they are not funded through regulated sources. Not-for-profit providers may be enabled to do this through a range of funding pathways and tax benefits, including payroll tax relief, income tax exemptions and tax deductible donations. However, where these costs are not covered by such incremental revenue, the comparatively lower EBITDA for many not-for-profit providers may be the product of the delivery of additional "community benefits" or "social impacts" or returns which are not recognised in the annual financial accounts.

12. ACFA has also noted regularly in its reports that the sector results are quite diverse with those in the top quartiles performing well, indicating that even with the same levels of Govt funding (or slowdowns in funding) some providers will always perform better and cope better than others reflecting better management and business models.

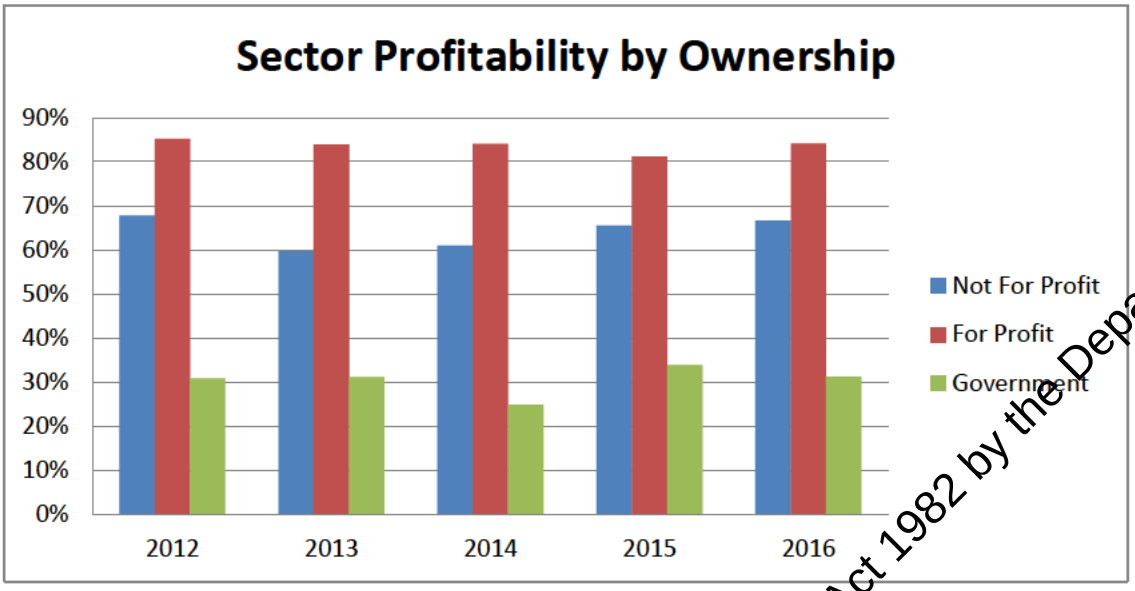
s22(1)(a)(ii)

Types of providers/facilities with typically lower financial results

18. Regional and remote providers make up a higher proportion of loss making providers as can be seen in the chart below. In 2016 55% of such providers had a net profit compared to nearly 80% for other providers. They incur higher costs, have lower occupancy rates and have sporadic funding streams which may result in lower profit margins for some providers. Government assistance through the viability supplement and support services such as the SDAP assists these providers.



19. For Profit providers typically outperform Not for Profits with Government providers having the lowest results as shown in the chart below.



20. While trends can indicate that some segments, such as rural and remote, and types of providers are more likely to have lower financial results, ACFA have noted that there is no one individual factor indicative of successful or conversely at risk providers. Not for Profit, rural and Government providers can be found in both the top 25% of performers and the lowest 25%. In its report "Factors Affecting the Financial Performance of Residential Care Providers" ACFA identified that strong disciplined management was a key factor to good performance while recognising that scale (more beds per facility), location, and ownership were indicators of performance.

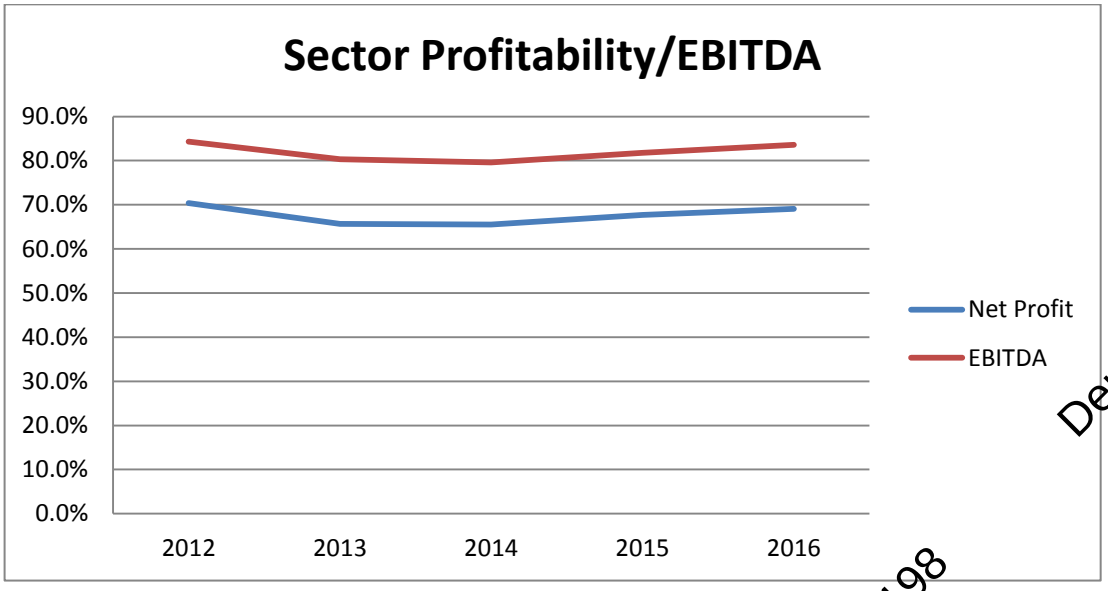
Commentary/Conclusion

21. It would be reasonable to summarise that the slow-down in ACFI growth and increasing wage pressures will be putting more pressure on the lower performers and so increasing the risk factor, but whether and to what extent vulnerable facilities may 'fall over' is difficult to say as this will depend very much on management of facility and other factors (parent entity support etc).
22. StewartBrown noted that *cost management is the key differentiator between those provider facilities that continue to show stable results and those whose results have declined.*
23. Temporary cuts to growth (such as indexation pauses) are also more likely to be measures that providers could cope with in the short term as opposed to permanent ongoing reductions in funding. The sector recovered from the 1 July 2012 ACFI changes without any significant increase in the number of providers going out of business.
24. Indexation is scheduled to return from 1 July 2018 (though the Complex Health Care component of ACFI will only be 50% indexed) which will help providers manage their financial position going forward.

Attachments

Attachment A – Sector profitability/EBITDA - 5 year trend
Attachment B – Sector provider and facility numbers – 5 year trend
Attachment C – Sector profitability/EBITDA by location – 5 year trend
Attachment D – Quartile analysis – 2016 EBITDA (per bed day) by location
Attachment E – Sector profitability/EBITDA by organisation type – 5 year trend

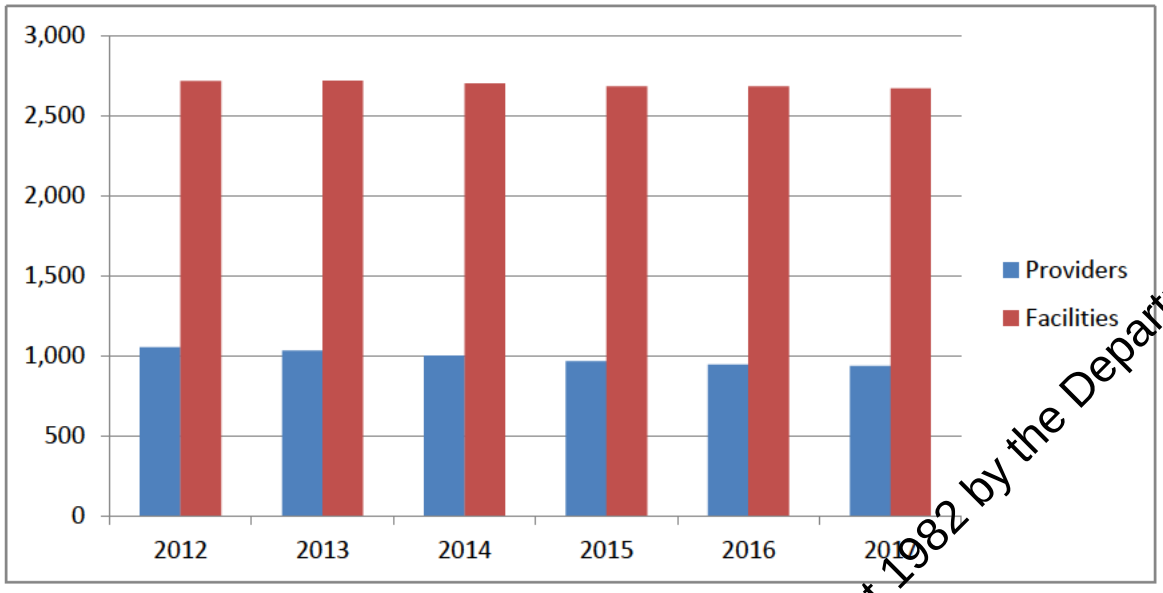
Attachment A – Sector profitability/EBITDA - 5 year trend



The above graph shows the trend line of the percentage of residential aged care providers that have reported profits and positive Earnings Before Interest Taxation Depreciation and Amortization (EBITDA) in the last 5 years.

After a decrease in profit following the ACFI changes in 2012, providers reporting profits have recovered from levels of 66% in 2013 to lift to almost 70% in 2016. This is likely to fall in 2016-17 and 2017-18 reflecting slow down in ACFI growth.

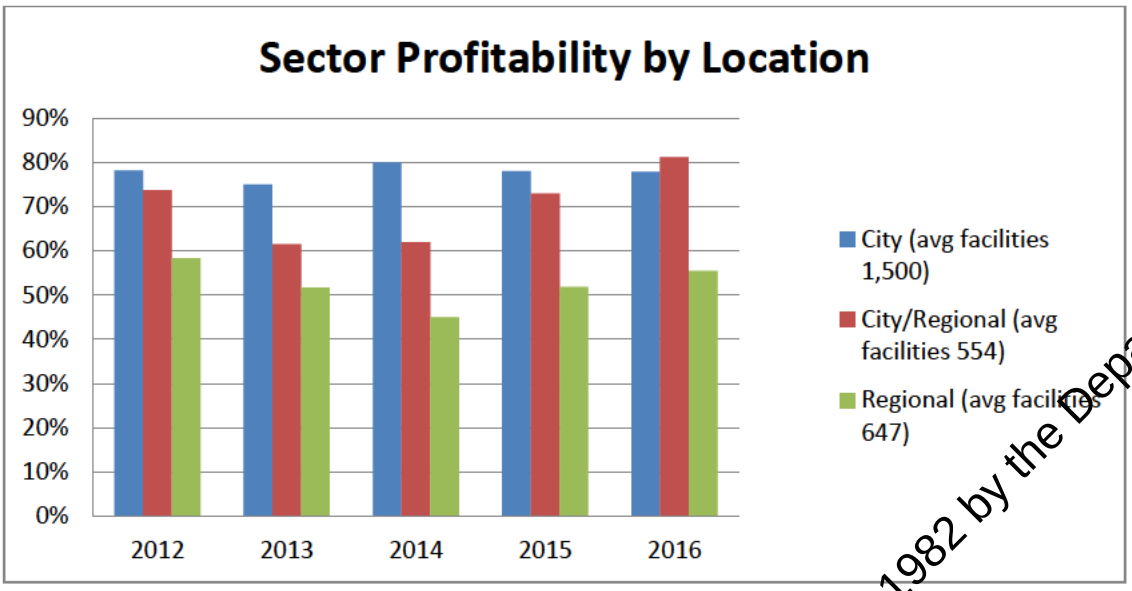
Attachment B – Sector provider and facility numbers – 5 year trend



Note: Japara consolidated 36 provider identifications into the 1 provider identification in 2016-17. The graph above has not been adjusted to reflect this administrative adjustment

The above graph shows the movement in providers and facilities from before and after the 2012 ACFI changes. It shows that over the 6 years there has been a consolidation of providers from 1,054 in 2012 to 902 in 2017, a decrease of 152. Facility numbers have also decreased gradually.

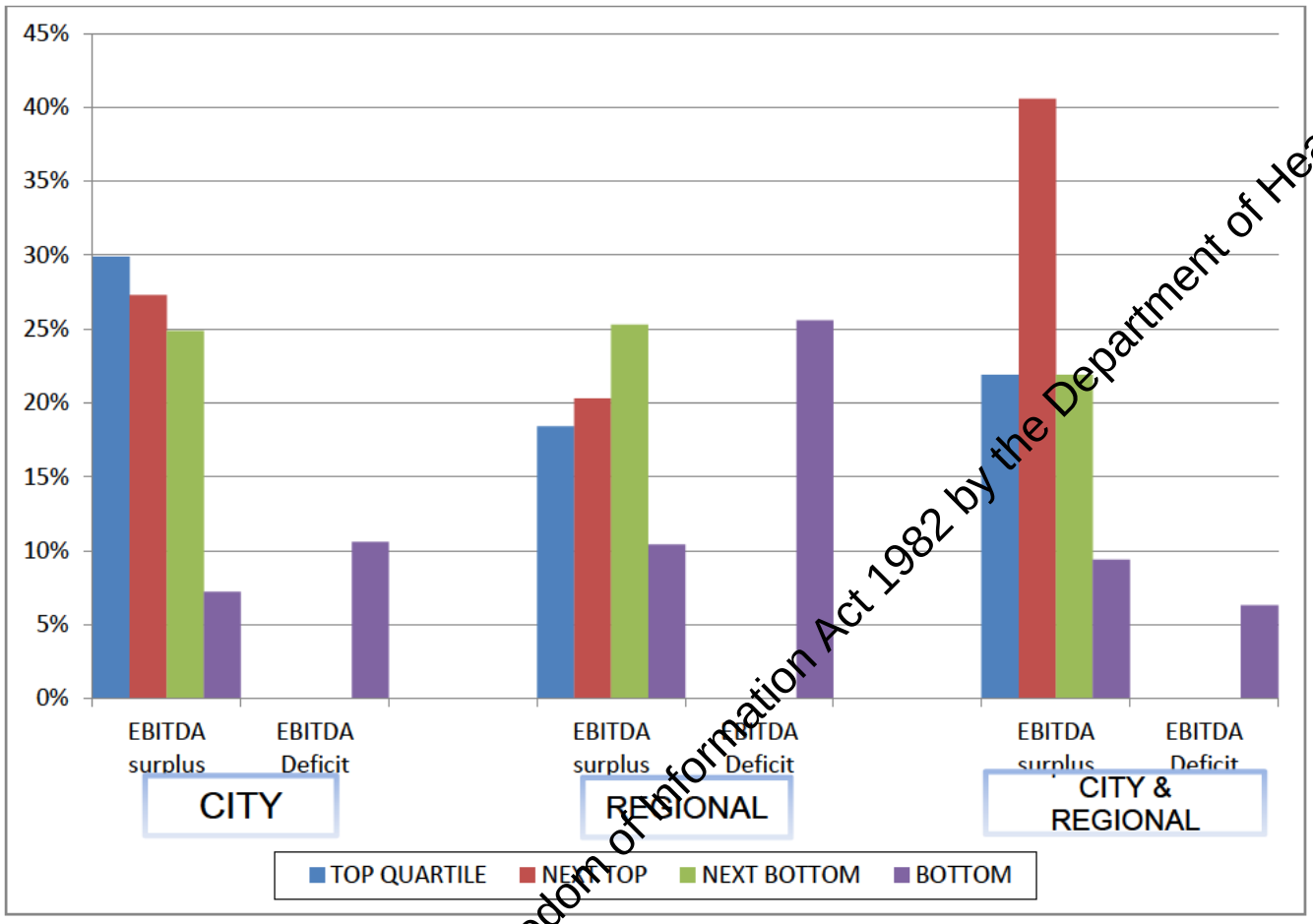
Attachment C – Sector profitability/EBITDA by location – 5 year trend



The graph above shows the percentage of profit making providers by location. Categories are reported as city, city/regional, and regional, based on where each provider operates the majority of their operations.

The results show that the most profitable providers are those who predominantly conduct their operations on city areas. This consistently shows around 80% of providers making a profit. Regional and remote areas lag behind reporting 56% of providers making a profit in 2016. Although these providers lag behind their city counterparts, it is of note that their numbers have increased 11% from 45% levels in 2014.

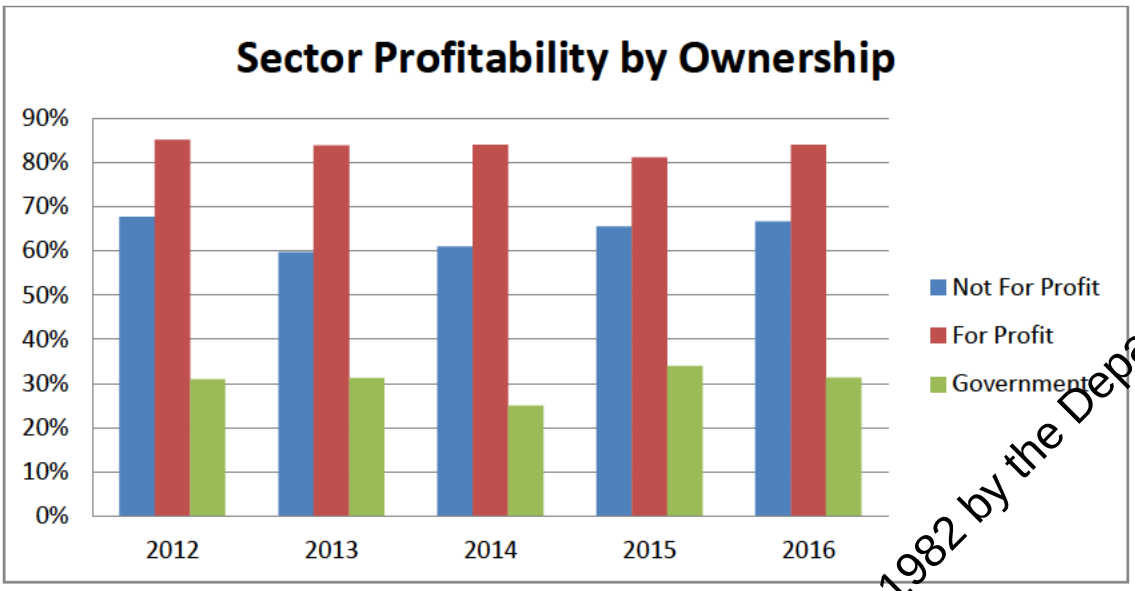
Attachment D – Quartile analysis – 2016 EBITDA (per bed day) by location



The above graph shows the percentage of providers by location in the quartiles that they fit into based on reported EBITDA.

The graph illustrates that although regional providers make up the largest proportion of providers that reported an EBITDA deficit, many within those areas showed strong results. Both providers in city and city/regional also displayed a spread of very profitable through to loss making.

Attachment E – Sector profitability/EBITDA by organisation type – 5 year trend



The graph above shows the percentage of profit making providers by organisation type.

In 2016 each ownership segment had the following providers and facilities:

- Not-for-profit – 513 providers with 1,581 services
- For-profit – 333 providers with 860 services
- Government – 99 providers with 244 services

The graph shows that for-profit entities are consistently the most profitable providers, with consistently 80 to 90 per cent of providers making a profit from year to year.

Not-for-profit and Government providers are significantly more likely to report losses. This statistic is often not the best indicator of success for not-for-profit and government entities as they often have different business models, motives and funding sources.

OI
HOT ISSUES

RESDIENTIAL AGED CARE SECTOR VIABILITY

OVERVIEW

- The Australian Government is the principal funder of aged care, providing estimated funding of $18.6 billion in 2017-18 to support aged care consumers and the sector.
- The Government took measures in the 2016-17 Budget to slow the higher than anticipated growth in funding claims from providers but funding continues to grow.
- Government spending on aged care will continue to grow over future years and is expected to reach over $22.3 billion by 2020–21.

CURRENT SITUATION:

- The results of the March 2018 aged care benchmarking survey by accounting firm StewartBrown has shown that the profitability (average annual facility results) of residential care providers (predominantly comprising of not-for-profit providers) has decreased since June 2017. This has been attributed to the pause in ACFI indexation in 2017-18 while costs (mainly wages) continue to grow.
- StewartBrown results show 43 per cent of residential services making a loss now. Aged Care Financing Authority (ACFA) data shows historically around one-third of providers operate at a loss.
- ACFA's most recent 2016-17 annual report (not yet released) reported an increase of 3.1 per cent in average Earnings before Interest, Taxation, Depreciation and Amortisation (EBITDA) per resident per annum from 2015-16 to 2016-17.
- The 2018-19 Budget package includes a range of measures to support the aged care sector, including a more flexible model of managing residential care and home care expenditure which is more responsive to consumer demand.
- Further support for the residential care sector include 13,500 new residential care places through Aged Care Approvals Round (ACAR) and the allocation of $50 million to support residential aged care providers to transition to the new Aged Care Quality Standards and from 1 July 2018, the previous indexation pause on residential aged care funding was mainly lifted, increasing subsidies for all residents.
- The Government recognises that the cost to deliver services in rural and remote Australia often comes at a higher cost and is continuing to support aged care in rural and remote areas, through the Viability Supplement. On top of that $40 million has been allocated in new capital grants and an expansion of the National Aboriginal and Torres Strait Islander Flexible Aged Care Program through the More Choices for a Longer Life Package will be achieved.

STAKEHOLDERS

- The three aged care peaks, Aged Care Guild, Aged and Community Services Australia (ACSA) and Leading Age Services Australia (LASA) have proposed an 'Industry Transition Package' of $675 million for a year to bridge the financing gap while Government continues to work on necessary structural reform to meet changes in consumer demand and future financial requirements.

NEXT STEPS

Residential Care Funding Reform

- The Government is committed to having an aged care system that supports older Australians while ensuring aged care expenditure is affordable and sustainable. To progress this commitment the Government is examining options for long term residential care funding reform. The Government has commissioned reports on options for funding reform and commenced a landmark Resource Utilisation and Classification Study (RUCS) of the sector to determine a solid evidence base on what drives care costs in residential aged care, both at the resident level and facility level. The study, which will take place during the course of 2018, will inform Government's consideration of funding reform options.

s22(1)(a)(ii)

ACFA Interim Report

- The chair of ACFA Mike Callaghan is currently preparing an interim report on sector viability for the Government in late 2018.

DEPARTMENTAL CONTACT

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