



StewartBrown

Integrity + Quality + Clarity



Australian Government

Department of Health

Aged Care Workforce Strategy Taskforce

Submission (June 2018)

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1. EXECUTIVE SUMMARY

Overview

StewartBrown produces the largest financial performance benchmarking survey in the aged and community care sector. Detailed operational, equity and staffing data each quarter for residential aged care facilities and home care packages. The *Aged Care Financial Performance Survey (ACFPS)* service commenced in 1995 and has grown exponentially due to the requirement for Boards and executive management to be able to compare and contrast their operations to that of other facilities and programmes within the sector. Over a number of years the format of the results of the survey has become more granular in content, and has become an integral part of the budget, forecasting and review processes within each participant organisation.

Subscribers to the ACFPS include some of the biggest providers nationally, independent stand-alone providers, faith-based and community providers, culturally specific providers, as well as government bodies, including the Department of Health (DOH), Aged Care Financing Authority (ACFA) and aged services sector peak bodies and service providers.

The ACFPS surveys quarterly financial and non-financial data for residential (by facility) and home care (by program) at a granular level. In addition, the survey obtains specific segment information and key balance sheet information at organisation (approved provider) level every six months.

Survey Analytics

The respective residential aged care, home care packages and organisation surveys consisted of the following data sets:-

- ◆ Detailed operating and equity results to December 2017 half year
- ◆ 171 provider organisations participated
- ◆ 126 provider organisation level financial metrics included
- ◆ 915 residential facilities included (*35 facilities excluded*)
- ◆ 401 Home Care programs (*21,400 packages*)
- ◆ Comparisons with 3 listed aged care entities (Estia/Japara/Regis)

The profile of the participants based on the residential aged care geographic spread is:

Number of Residential Facilities	Major City	Inner Regional	Outer Regional/Remote	Total
<i>Survey (December 2017)</i>				
Facilities included	600	224	91	915
Facilities excluded	21	6	8	35
Total Survey facilities	621	230	99	950
DOH Service Listing (A)	1,647	642	383	2,672
State/local government	33	113	94	240
Service Listing less state/local government (B)	1,614	529	289	2,432
Coverage - % of (A)	37.7%	35.8%	25.8%	34.2%
Coverage - % of (B)	38.5%	43.5%	34.3%	37.6%

Summary of Survey Results

Sector Observations

- Legislative and policy uncertainty is influencing provider “behaviour” and strategies
- Slowdown of capital equity infusion continues due to declining financial performance
- New developments are integrating segments (residential/assisted living/home care/ILU’s)
- Still a large number of older “hostel” style facilities that need to be significantly refurbished
- Sector still struggling with deregulation of HCP (pricing/staffing/systems/technology)
- *My Aged Care* portal still has some deficiencies in navigation and reliability
- Increased community education around accommodation pricing and funding is critical
- Funding and revenue streams are a major concern to providers
- Increased issues around staffing and related costs

Organisation Level

- Net assets remained neutral when compared to FY17
- Cash + financial assets = 51.0% of total debt (*external and resident debt*)
- Operating revenue increased by 3.67%
- Employee expenses increased by 6.81%
- Earnings Before Tax (surplus) decreased by 59.9%
- Earnings Before Tax return on assets employed (ROA) was marginal at 0.5% pa
- Net operating loss sustained (*after eliminating revaluations and non-recurrent revenues*)
- Operating result (*) return on assets employed (ROA) was negative (0.1% pa)
 * *Operating result excludes non-recurrent revenues (revaluations/gains on sale/donations)*

Residential Care

- Average ACFI per bed day (pbd) for survey participants was neutral (\$171.84 pbd)
- Occupancy levels for survey participants remained neutral (94.4% average occupancy)
- Total care hours per resident per day increased to 3.06 hours per resident per day (FY17 2.91 hours)
- Direct care costs increased by 2.96% (\$134.58 pbd)
- Earnings Before Tax (EBT) average for residential facilities reduced by \$1,618 per bed per annum (pbpa) to \$1,617 pbpa (from \$3,236 pbpa)
- EBITDA average for residential facilities reduced by \$1,326 pbpa to \$7,071 pbpa
- 21.3% of residential facilities recorded a negative EBITDA (16.1% for FY17) (*representing cash loss*)
- 41.3% of residential facilities recorded a negative EBT (33.9% for FY17)

Home Care Packages

- Revenue per client day (pcd) average for survey participants reduced by 5.03% (\$3.70 pcd)
- EBT (surplus) average per client day for survey participants reduced by \$2.13 pcd to \$3.24 pcd
- Revenue utilisation (average unspent funds) has deteriorated by 4.7%
- Unspent funds average per client has increased by \$1,157 per client (to \$5,412 per client)
- Staff hours per client per week has remained neutral (average 7.14 hours per week)

StewartBrown Aged Care Reports

StewartBrown issues detailed financial reports and analysis involving the aged care sector as follow:-

- Residential and Home Care sector reports (quarterly)
- Provider Organisation report (bi-annual)
- Listed Provider Analysis report (bi-annual)
- Corporate Administration report (annual)

Copies of these reports are located at <http://www.stewartbrown.com.au/>

Commentary

The overarching theme of the December 2017 results is the deterioration of financial performance in each of the respective segments which is potentially placing a number of aged care organisations in a financially vulnerable position.

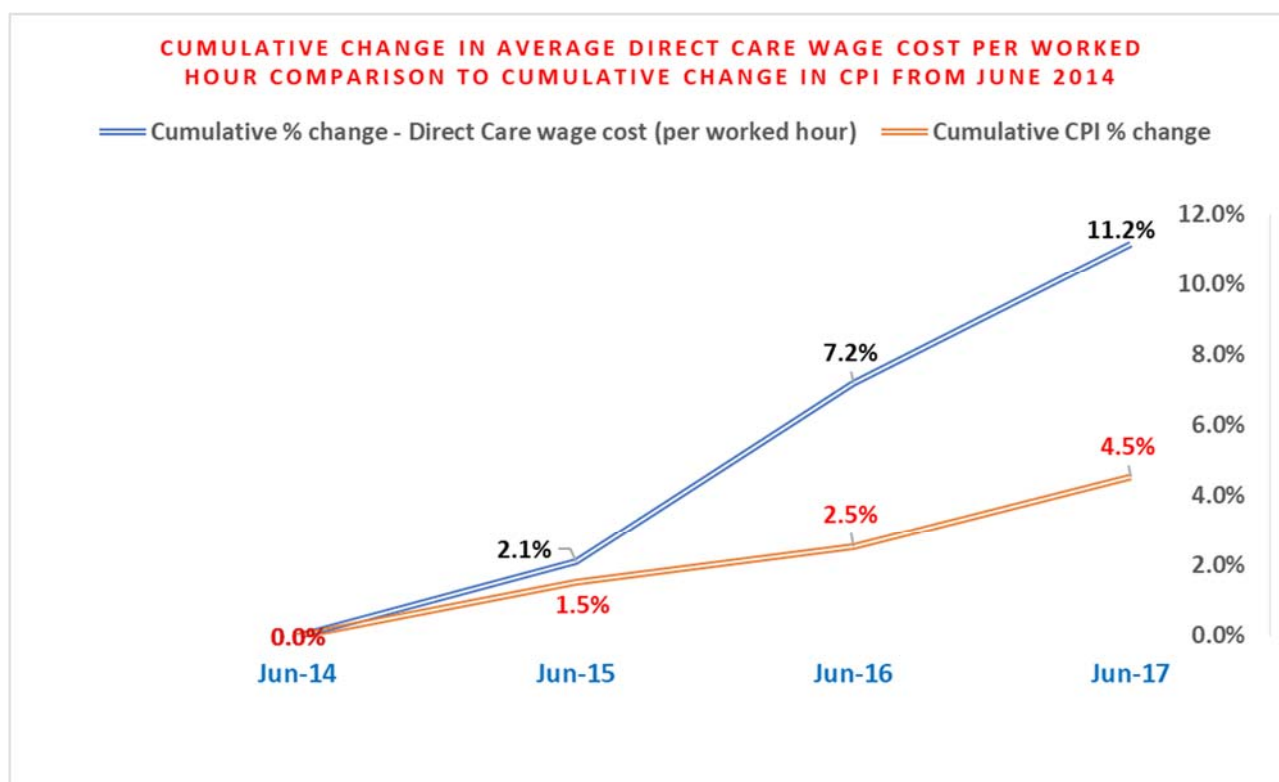
Residential aged care in particular has shown a marked downturn in operating results due to a combination of the COPE indexation freeze, amendments to the ACFI scoring matrix, ACFI downgrades and increased costs. In fact average ACFI income has remained neutral at \$171.85 per bed day compared to \$171.13 at December 2016 and \$171.84 at June 2017.

The impact of the regulatory changes and cost pressures, and particularly staff costs has resulted in the alarming statistic that 41.3% of residential facilities reported an operating loss for the six months to December 2017, and even more disconcerting is that 21.3% of facilities had negative EBITDA (indicating a cash loss from operations).

Average Earnings Before Tax (EBT) for the period ending December 2017 for residential care was \$1,617 per bed per annum, which equates to an unsustainable amount of \$31.10 per bed per week.

Of further note is that the direct care staffing hours per resident per day increased from 2.91 hours to 3.06 hours, with no additional revenue to compensate for these increased staffing hours combined with rate increases from pre-existing enterprise agreements.

Direct care staffing costs are also increasing at a higher rate than CPI on both cumulative and year-on-year metrics, as indicated in the below graph.



Year	Jun-14	Jun-15	Jun-16	Jun-17
Average Direct Care hourly wage cost (<i>per worked hour</i>)	\$ 38.42	\$ 39.24	\$ 41.19	\$ 42.71
Cumulative % change - Direct Care wage cost (<i>per worked hour</i>)	0.0%	2.1%	7.2%	11.2%
Cumulative CPI % change	0.0%	1.5%	2.5%	4.5%

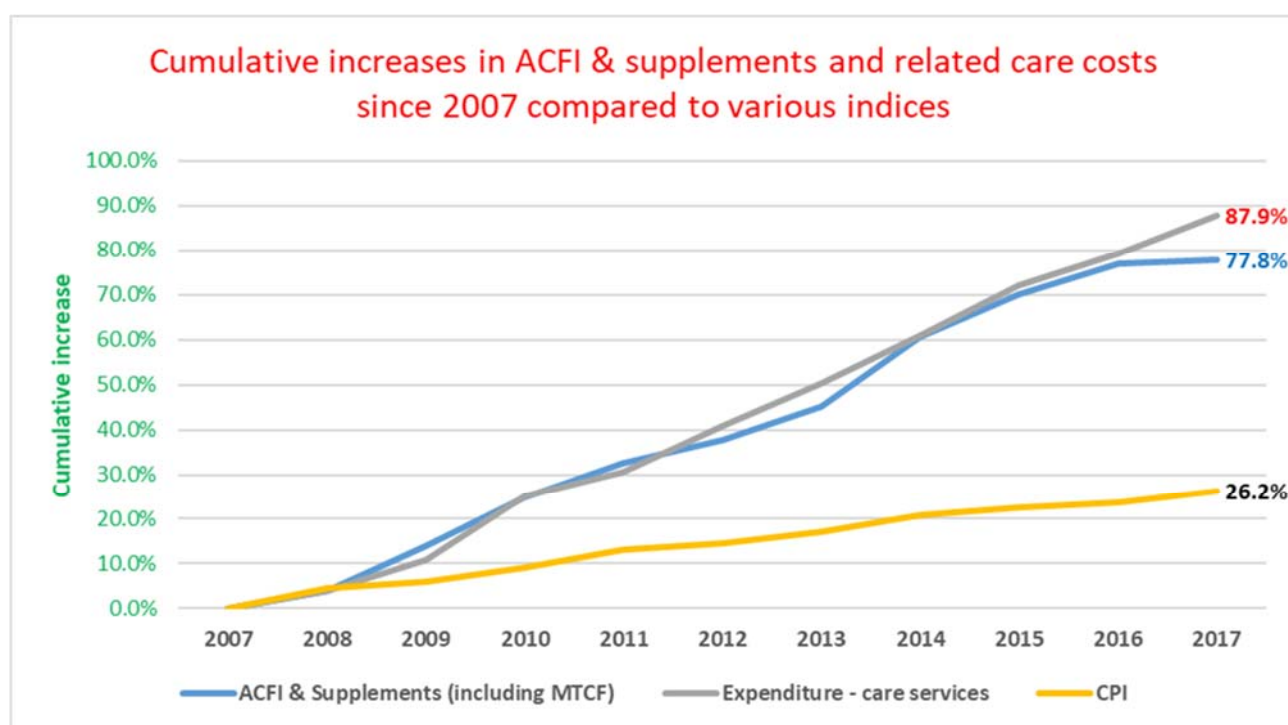
The effect of potentially increasing a legislated (mandated) direct care staffing hours to 4.3 hours per resident per day would increase the care staffing costs by an overall average of \$53.09 per bed per day, including on-costs and workers compensation premium (\$19,379 per bed per annum) which have a dramatic effect that over 85% of participating facilities in the survey would be operating at an EBT loss.

Occupancy levels in residential care facilities remained steady at 94.4% average occupancy, however should there be facility closures due to financial stress this will heavily impact the vulnerable aged requiring high care accommodation.

The anticipated equity and private investment into residential aged care has slowed, predominantly due to legislative and policy uncertainty, and more directly due to the low financial returns. The average EBT return on assets employed (ROA) was a mere 0.5% and after excluding non-recurrent revenue streams such as revaluations and fair value gains on property and investments, the ROA represented a negative return of minus 0.1%

The financial viability of outer regional, rural and remote aged care providers is reaching a pivotal point. Some 56% of residential facilities in these geographic locations are operating at a loss, with 33% now operating at a cash deficiency. There are few opportunities for existing providers to merge or sell their facilities to larger providers, meaning that remedial funding will be essential in our opinion.

ACFI residential care subsidies are now cumulatively increasing at a lower rate than the costs of providing direct care (refer below graph). This will create further financial tension and risk the potential of reducing staffing hours to attempt to remain financially viable.



	2007 \$ pbd	2017 \$pbd	Cumulative Increase
ACFI & Supplements (including Means-tested care fee)	\$96.66	\$171.84	77.8%
Expenditure - Direct Care services	\$71.63	\$134.58	87.9%

Accommodation pricing for residential care (Refundable Accommodation Deposits and Daily Accommodation Payments) have not translated into a major equity pipeline. This is due to the number of supported residents (over 45% nationally) and consumer reluctance to pay high accommodation prices commensurate with the average housing prices.

At December 2017, the average surplus from accommodation revenue and accommodation costs (by majority being depreciation and refurbishment) equated to \$3,387 per bed per annum. Assuming a new residential bed costs around \$280,000 to build and the depreciated bed value is currently around \$175,000 this is, in itself, not a sustainable return (being less than 1.95% pa).

However, this surplus is due to low depreciation charge (buildings depreciated over 40+ years and little to nil refurbishment factored in). If buildings were depreciated at 4% (25 years effective life) as we would recommend, then this would create a deficit rather than a surplus.

Home care did not escape the performance downturn with a revenue decline of 5.03% underpinning an overall reduction in profitability of 39.7%. Staffing hours per client per day were maintained at existing levels, and with increased pay rates this also was a major contributing factor to the downturn in results.

Since June 2016 the number of approved providers in home care has increased nationally by 307 (61.5% increase) however the number of funding packages has only increased by 2.77% (from 72,272 packages to 74,205 packages) since deregulation in February 2017.

In conclusion, with the home care national prioritisation queue (consumers assessed for funding but not yet allocated full funding) swelling by 15,698 since June 2017 to now be over 104,600, coupled with the estimated 83,500 new residential beds being required over the next 10 years to meet the ageing population demands, the sector requires significant investment.

For this investment to occur the sector must be financially sustainable and, in our opinion, urgent action is required to allow providers to access alternative revenue streams and have less reliance on government funding.

In this regard, we would recommend that a COPE (indexation) increase of 3.00% be approved effective from 1 January 2018 which would increase ACFI revenue by an average of around \$5.15 per bed day (\$1,880 per bed per annum). This would also increase the ACFI base for the July 2018 COPE indexation.

Targeted regional and remote subsidies need also to be implemented as a priority in our opinion.

A number of the Tune Review recommendations should also be implemented as soon as practicable (1 July 2018 or 1 January 2019) including:-

- ✓ Recommendation 14 - effective deregulation of Basic Daily Fee for residential care
- ✓ Recommendation 16 - compulsory consumer contributions for CHSP
- ✓ Recommendation 12 - compulsory to charge the basic (care) fee for home care packages
- ✓ Recommendation 11 - comparability of home care prices on My Aged Care site
- ✓ Recommendation 7 - Level 5 home care package funding to be introduced
- ✓ Recommendation 3 - ACAR for bed licences to be removed within 2 years, leading to deregulation of residential aged care

2. ORGANISATION ANALYSIS

The following tables include the balance sheet and financial performance of aged care providers at an organisational level rather than at individual segment level. For the purposes of this analysis, we have included the detailed information provided by 125 organisations who are representative of all states and demographics.

The same provider organisations were used to compare their operating performance for the 2017 financial year to the six months ended 31 December 2017.

Analysis of Organisations by Size

Operating Revenue Range (\$ million per annum)	DECEMBER 2017 (6 months)			
	<\$10M	\$10M - \$30M	\$30M -	>\$100M
Number of organisations	32	52	24	17
<i>Number of organisations %</i>	25.6%	41.6%	19.2%	13.6%
Number of facilities	32	121	142	428
<i>Number of facilities %</i>	4.4%	16.7%	19.6%	59.2%
Number of residential beds	2,078	9,973	11,706	27,573
<i>Number of residential beds %</i>	4.0%	19.4%	22.8%	53.7%
Number of home care clients (packages)	475	935	3,534	13,243
<i>Number of home care clients (packages) %</i>	2.6%	5.1%	19.4%	72.8%

Operating Results for six months ended 31 December 2017

Operating Revenue Range (\$ million per annum)	DECEMBER 2017 (6 months)			
	<\$10M	\$10M - \$30M	\$30M - \$100M	>\$100M
Income & Expenditure	\$'000	\$'000	\$'000	\$'000
<u>Revenue</u>				
Operating revenue	103,810	469,369	766,290	2,115,417
Other revenue	3,070	16,055	24,287	40,350
Other income	1,137	12,011	26,399	33,335
<i>Total revenue</i>	108,018	497,435	816,977	2,189,102
<u>Expenses</u>				
Employee expenses	69,157	331,028	517,525	1,487,040
Depreciation and amortisation	7,725	37,118	56,226	136,942
Finance expenses	623	3,093	4,204	14,828
Other expenses	27,186	126,266	225,902	513,910
<i>Total expenses</i>	104,691	497,504	803,856	2,152,719
Surplus (EBT)	3,327	(70)	13,121	36,383

Operating Surplus (Deficit) (six months to December 2017)	2,190	(12,081)	(13,278)	3,048
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Operating Surplus (Deficit) - 2017 financial year (annual)	4,800	8,209	4,154	86,336
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Ratios

<i>EBT return on assets (ROA)</i>	0.8%	0.0%	0.5%	0.6%
<i>Operating surplus return on assets (ROA)</i>	0.5%	-0.6%	-0.5%	0.0%
<i>Operating surplus % of operating revenue</i>	2.1%	-2.6%	-1.7%	0.1%
<i>Employee expenses % of operating revenue</i>	66.6%	70.5%	67.5%	70.3%
<i>Depreciation as % of property assets</i>	3.2%	2.9%	3.2%	3.2%

Balance Sheet Summary as at 31 December 2017

Operating Revenue Range (\$ million per annum)	DECEMBER 2017			
	<\$10M	\$10M - \$30M	\$30M - \$100M	>\$100M
Balance Sheet	\$'000	\$'000	\$'000	\$'000
<u>Assets</u>				
Cash and financial assets	310,644	1,354,740	1,589,222	3,491,162
Operating assets	21,455	98,285	107,005	212,212
Property assets	483,563	2,585,099	3,544,422	8,639,188
Intangible assets	18,110	98,125	155,595	610,284
<i>Total assets</i>	833,772	4,136,249	5,396,244	12,952,846
<u>Liabilities</u>				
Refundable loans	459,428	2,332,235	2,824,237	6,931,557
Borrowings	33,879	110,508	208,135	467,674
Other liabilities	49,615	197,800	433,051	1,237,443
<i>Total liabilities</i>	542,922	2,640,543	3,465,424	8,636,674
Net Assets	290,850	1,495,707	1,930,820	4,316,172
Net Tangible Assets	272,740	1,397,581	1,775,225	3,705,888
Net Tangible Assets (average by organisation)	8,523	26,877	73,968	217,993

Ratios

<i>Net assets proportion % total assets</i>	34.9%	36.2%	35.8%	33.3%
<i>Property assets proportion % total assets</i>	58.0%	62.5%	65.7%	66.7%
<i>Cash + financial assets % refundable loans</i>	67.6%	58.1%	56.3%	50.4%
<i>Cash + financial assets % debt</i>	63.0%	55.5%	52.4%	47.2%

Brief Commentary

- The operating surplus for the six months ended December 2017 has significantly deteriorated when compared to the 2017 financial year. This is consistent with the results at facility and home care package level
- The smaller organisations in the range \$10 million or less have a lower administrative cost structure (particularly the relationship between fixed and variable costs) and have had a lower operating surplus decrease for the December period
- The “middle” sized organisations (both in the \$10m - \$30m and \$30m - \$100m) brackets are increasingly vulnerable for both an operating and capital perspective as their ability to reduce costs and maintain capital adequacy is more restricted
- The operating surplus return on assets (ROA) is not financially sustainable for organisations in all brackets

Not-For-Profit and For-Profit Distinction

Regulatory Environment

When analysing the financial performance and viability of the sector, there has been certain commentary as to the distinction between and financial performance of the Not-For-Profit (NFP) and For-Profit (FP) providers. It should be noted that all providers operate under the *Aged Care Act 1997* and the related legislative and regulatory environment.

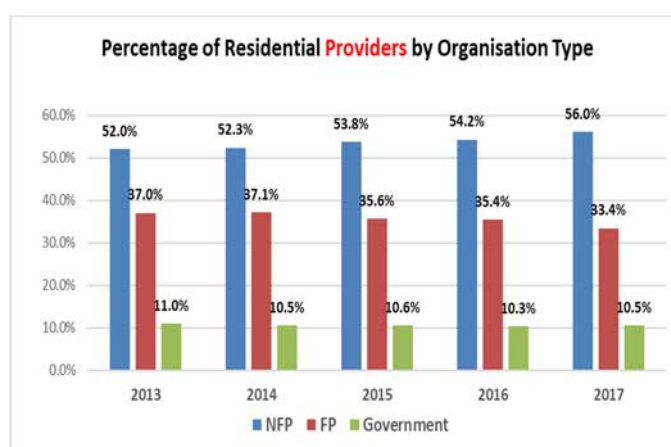
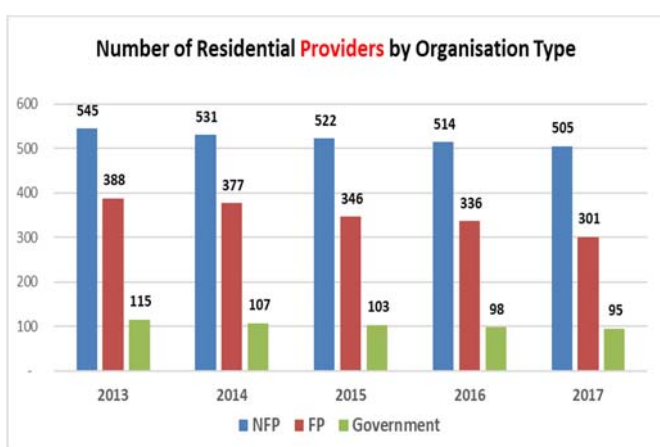
Government subsidy funding, consumer access, choice of providers and eligibility to receive aged care services make no distinction between for-profit, not-for-profit or government owned providers.

Apart from certain taxation differentials, the operating, staffing and financial performance of all providers is performed under the same funding model.

Accordingly, as both the FP and NFP providers operate in the same funding, geographic and regulatory environment, the importance of a financially viable and dynamic aged care sector, including both FP and NFP providers, cannot be underestimated.

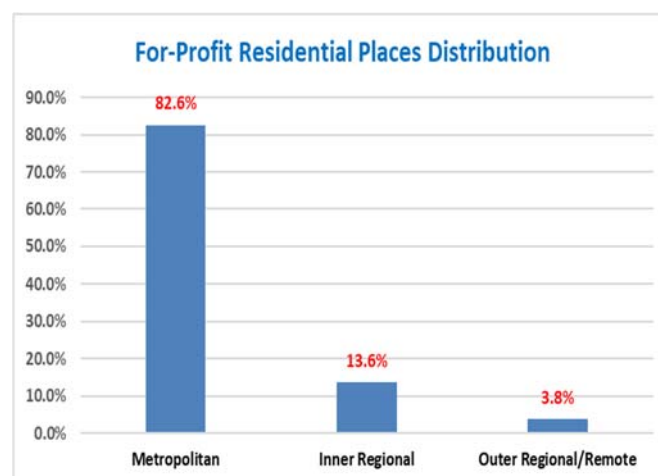
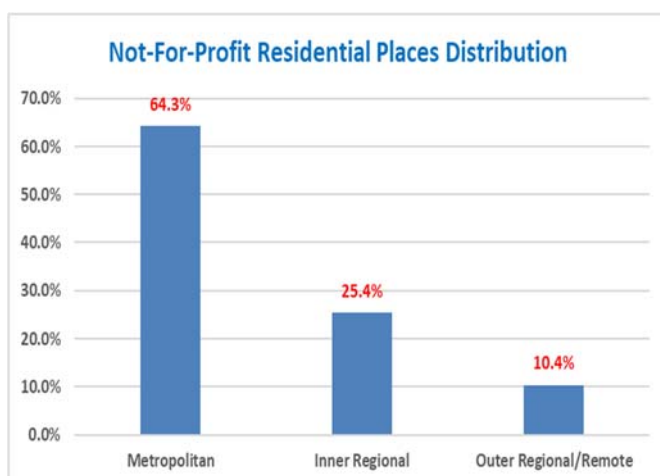
Analysis of Providers by Ownership

The graphs below show the number of providers by ownership and the respective percentages. It is interesting to note that the percentage ownership between NFP and FP providers has remained fairly consistent since the *Living Longer Living Better* reforms.



Geographic Distribution by Ownership

The below graphs detail the geographic distribution of residential aged care places (beds) by ownership which highlights that the FP providers are to a greater extent located in the major metropolitan centres. As would be expected, the financial performance in metropolitan areas has significant advantages due to the critical mass of residents, staff and service suppliers and, accordingly, the ability to build and operate residential facilities on a larger and more efficient scale.



Financial Sustainability by Ownership

When assessing the operating financial performance comparison between the NFP and FP providers, the first quartile of facilities owned by NFP providers achieve a facility financial result at least equivalent to the FP provider facilities.

The overall financial performance of the NFP provider organisations is reduced due to the far greater exposure of facilities in the Outer Regional and Remote geographic locations, many of which run at a substantial operating loss. This geographic differential needs to be considered when assessing the overall financial performance of the sector.

The following table includes financial data extracted from the StewartBrown *Aged Care Financial Performance Reports* (December 2017 and June 2017 data) combined with extracted financial data for the same periods for large FP providers.

It should be noted that percentage split between NFP and FP providers by both the number of facilities and number of residential places is similar to the AFCA numbers which are for the whole sector.

	Combined (Dec-17)	Combined (June-17)	ACFA (June-16)
Data Set			
<i>Number of organisations</i>	133	133	949
<i>Number of facilities</i>	1,072	1,057	2,669
<i>Number of facilities (% of total number)</i>	40.12%	39.56%	100%
<i>Number of residential beds</i>	81,827	80,262	195,825
<i>Number of residential beds (% of total number)</i>	40.77%	39.99%	100%
<i>Number of home care clients (packages)</i>	18,626	18,175	n/a
Ownership (*)			
<i>Number of facilities (NFP)</i>	725	717	1,557
<i>Number of facilities (FP)</i>	347	340	864
<i>Number of residential beds (NFP)</i>	49,091	48,391	110,178
<i>Number of residential beds (FP)</i>	32,736	31,871	76,630
Ratios			
<i>Operating surplus return on assets (ROA) (**)</i>	0.12%	0.95%	1.59%
<i>Operating surplus % of operating revenue (**)</i>	0.82%	3.05%	3.90%
<i>Employee expenses as % of operating revenue (**)</i>	69.91%	68.42%	65.51%
<i>Depreciation as % of property assets</i>	3.05%	2.96%	3.27%

(*) Excludes government owned facilities

(**) Operating revenue and operating surplus excludes non-recurrent items (revaluations/gains on sale/bequests/donations)

Financial Analysis

The above table confirms the continued decline in financial performance from June 2016 (ACFA) to December 2017, primarily for the reasons previously noted. Of considerable interest as that with the inclusion of FP providers (who have a greater proportion of facilities in metropolitan areas) the combined financial performance is also not at a sustainable level.

The operating surplus return on assets employed (ROA) has deteriorated to be 0.12% per annum (from 1.59%) and is a clear detraction from generating future capital end equity investment.

Return on Assets (ROA)

This ratio relates to the operating surplus (recurrent surplus) as a measure of the total assets employed.

The ROA ratio is used to assess what levels of real return providers are achieving in relation to the assets employed (irrespective of the debt/equity/notional debt). The only variable is whether assets have been revalued or held at historical cost.

As residential aged care has a high capital requirement and consequently a large equity investment, the ROA ratio provides an indication of the returns in relation to the capital intensity and, accordingly, are an important indicator of the overall financial returns required to maintain ongoing viability.

3. RESIDENTIAL AGED CARE ANALYSIS

Analysis of Operating Losses by Facility

The effect of the reduced facility performance as a result of the combination of the COPE freeze, amendments to the ACFI scoring matrix, ACFI downgrades and increased costs has resulted in many facilities moving into an increasingly financially vulnerable position.

Table 1: Analysis of facilities making EBT and EBITDA losses

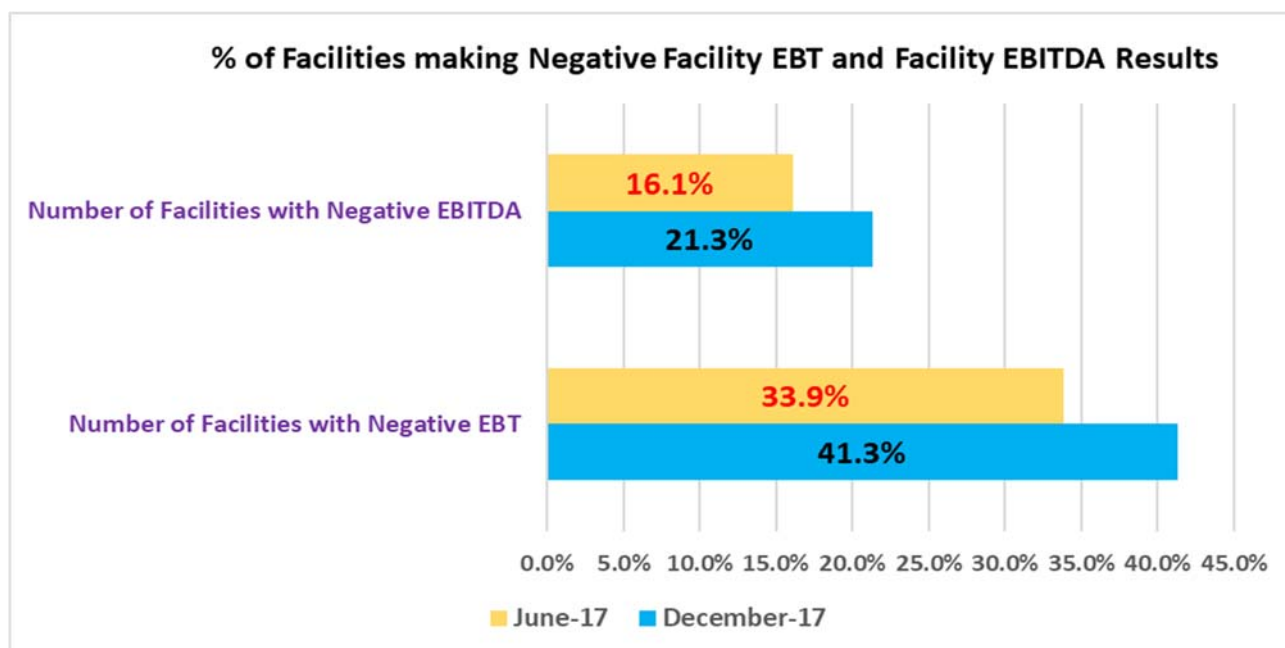


Table 2: Analysis of facilities making EBT losses (by remoteness)

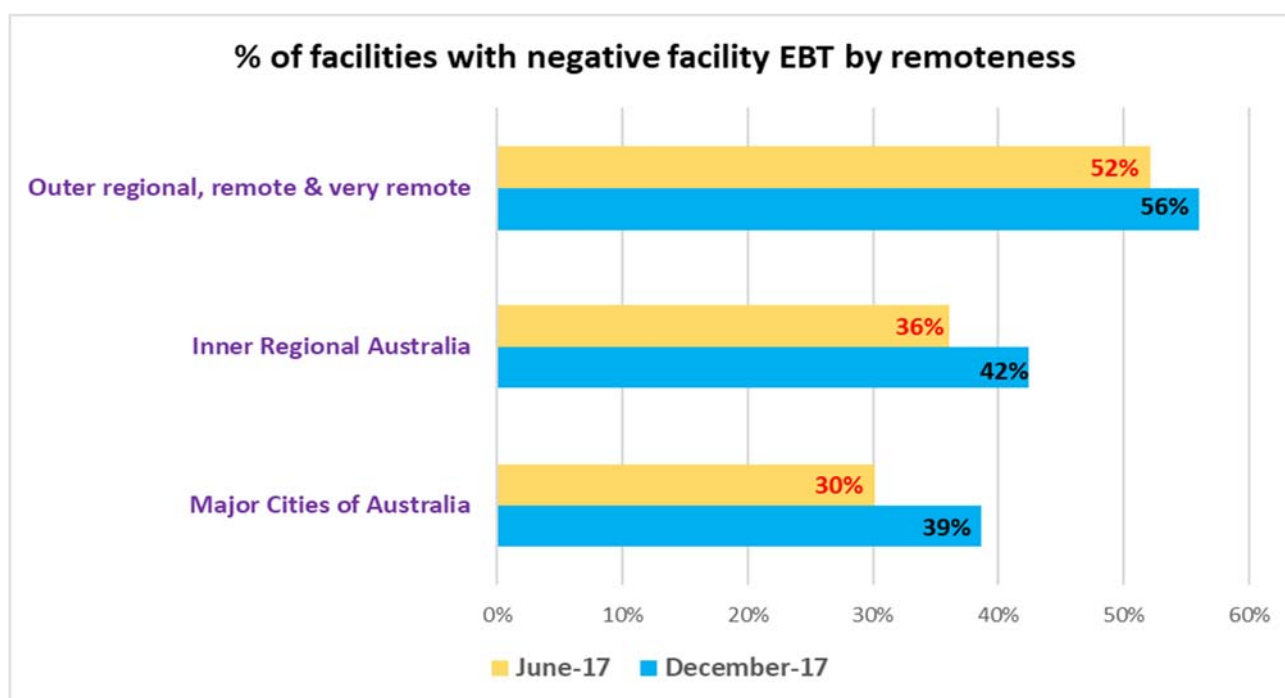
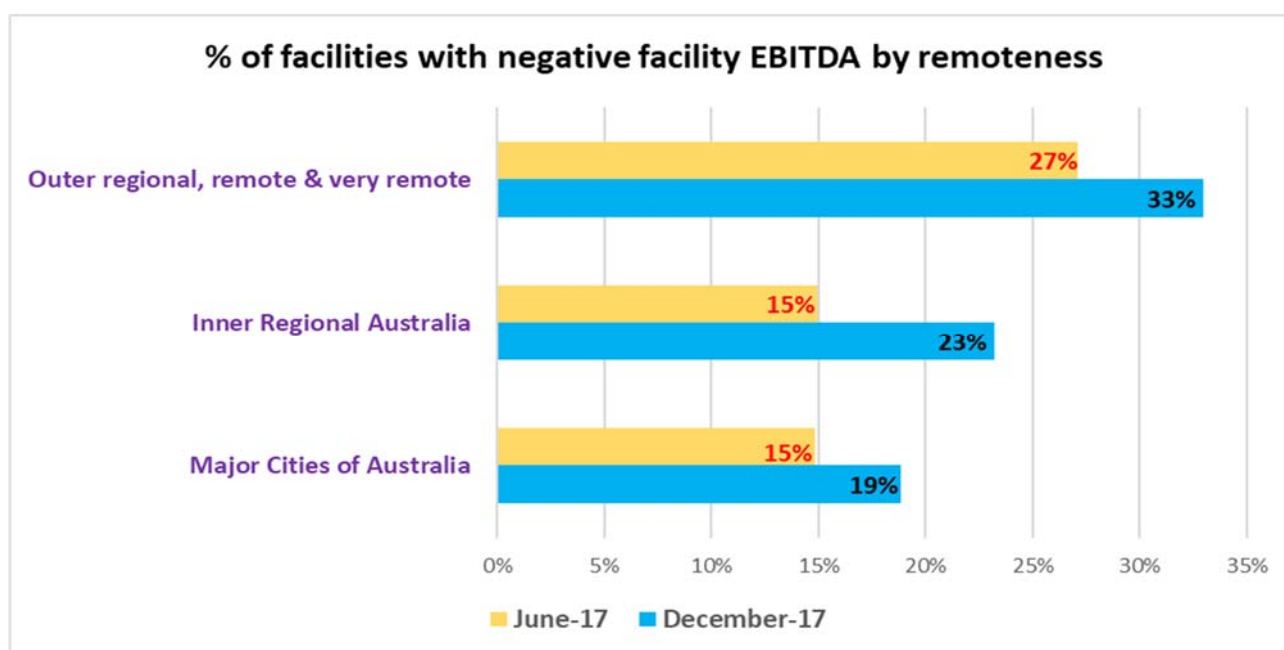


Table 3: Analysis of facilities making EBITDA losses (by remoteness)



Brief commentary

- ◆ The total percentage of facilities making an EBITDA loss has increased by a further 5.2%, from 16.1% to 21.3% of facilities of the total participation number (915 facilities). In addition to this a further 21 facilities who made both an EBT and EBITDA loss were excluded due to being outside the acceptable range
- ◆ The total percentage of facilities making an EBT loss has increased by a further 7.5%, from 33.9% to 41.3% of facilities in the total participation number
- ◆ Tables 2 and 3 graph the number of facilities making an EBT and EBITDA loss as a percentage of total number of facilities in their respective geographic location (remoteness). In relation to outer regional/remote/very remote facilities, 56% of facilities in this geographic area have made an EBT loss (33% have made an EBITDA loss)
- ◆ 42% of facilities located in inner regional made an EBT loss and 23% made an EBITDA loss
- ◆ Similarly, of the facilities located in major cities, some 39% of these made an EBT loss and 19% made an EBITDA loss

Direct Care Staffing Metrics

Direct Care staffing metrics include care staff costs and care staff hours. The ability to efficiently and appropriately align staffing levels to funding and facility design while meeting the care needs of the residents, leads to improvements in the facility's financial performance.

A summary of the direct care staff hours by category per resident per day for the Survey *Average* and Survey *First 25%* is included in the below table.

Table 4: Care staffing metrics for survey Average and survey First 25%

	Average			First 25%		
	Dec 17	June 17		Dec 17	June 17	
Care staff costs as % of total care expenses	58.61%	58.51%	↑	57.72%	57.26%	↑
Costs by type - \$ pbd						
Care management	7.98	7.46	↑	8.27	7.08	↑
Registered nurses	21.18	20.52	↑	17.37	16.34	↑
Enrolled & licensed nurses	9.39	12.60	↓	6.41	9.42	↓
Other unlicensed nurses & personal care staff	78.90	74.54	↑	70.20	65.99	↑
Allied health & lifestyle	7.16	5.95	↑	6.66	5.45	↑
Agency staff	3.59	3.16	↑	2.23	1.84	↑
Total care labour costs	128.20	124.22	↑	111.14	106.12	↑
Hours by type - hours worked per resident per day						
Care management	0.12	0.12	-	0.10	0.11	↓
Registered nurses	0.38	0.37	↑	0.32	0.29	↑
Enrolled & licensed nurses	0.29	0.26	↑	0.24	0.19	↑
Other unlicensed nurses & personal care staff	2.11	2.05	↑	1.92	1.84	↑
Allied health & lifestyle	0.15	0.12	↑	0.13	0.11	↑
Imputed agency care hours implied	0.01	n/a		0.02	n/a	
Total Care Hours	3.06	2.91	↑	2.73	2.53	↑

Brief commentary

- ◆ The category allocations are consistent with the Nurses and Midwifery Board of Australia, and accordingly AIN and TAFE qualified staff have been included with the “Other unlicensed nurses & personal care staff” classification
- ◆ Total labour costs have increased for both the survey *Average* and *First 25%* since June 2017, by 3.2% and 4.7% respectively
- ◆ Total care hours have increased for both the survey *Average* and for the *First 25%* by 5.3% and 7.7% respectively, and are now at 3.06 hours and 2.73 hours worked per resident per day respectively
- ◆ Initial feedback from providers in relation to an explanation for increase in care hours is that it may be partially due to the impact of influenza and gastro outbreaks

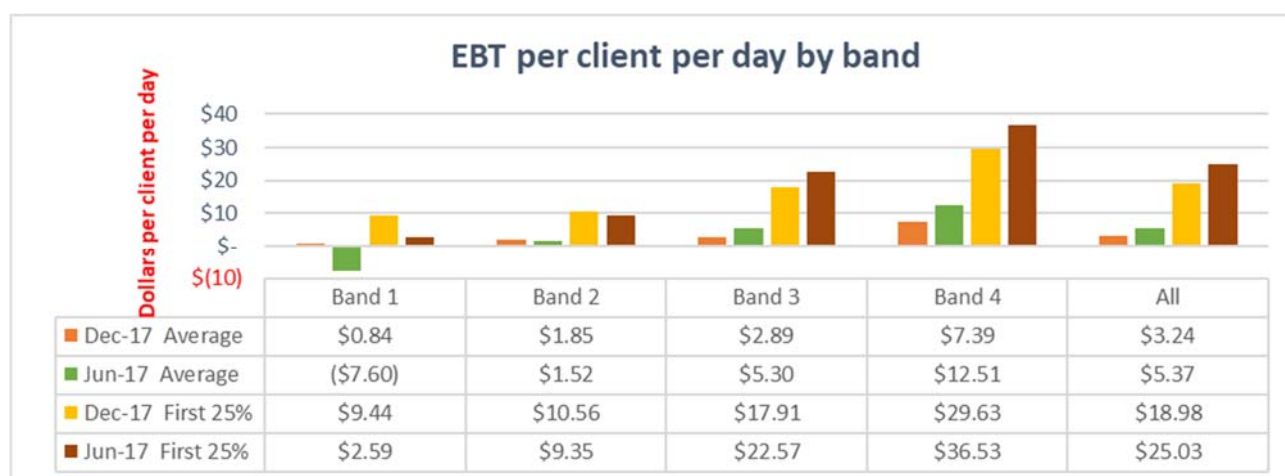
4. HOME CARE ANALYSIS

Results Overview

The December 2017 quarter showed a decline in the net result with the Survey's *Average* Earnings Before Tax (EBT) at \$3.24 per client per day (pcd) compared to \$5.37 pcd as at June 2017. The Survey *First 25%* also had a reduction in surplus by \$6.05 pcd to \$18.98 pcd.

For both the Survey *Average* and *First 25%* the profitability declines were in Bands 3 and 4, whilst Bands 1 and 2 had slight increases.

Table 5: Comparison of EBT (operating surplus) December 2017 and June 2017



Brief commentary

- ◆ Survey *Average* EBT per client per day has declined due to
 - Revenue reduction of 5.03% since June 2017
 - Total expenditure decrease of 2.4% - however, as this is lower than the decline in revenue the net result is a reduction in EBT
 - Reduction in expenses coming from case management and advisory, and administration and support costs, rather than from direct service and sub-contracted or brokered costs (this increased by 1.9%)
 - Band 4 revenue declining at a greater amount
- ◆ The survey *First 25%* has also declined for similar reasons: -
 - Revenue reduction of 1.6%
 - Total expenditure has remained roughly the same (only a 0.09% increase compared to June 2017)
 - Dramatic increased service provision and administration cost (9%)
- ◆ The decline in revenue may be due to providers reducing their pricing (due to increased competition) with service provision revenue (direct service and brokered) not reducing at the same rate as costs
- ◆ The EBT of Band 2 (survey *Average* and *First 25%*), comprised mostly of Level 2 & 3 packages, has increased because the reduction in expenses is greater than the reduction in revenue

5. CHALLENGES

Wages Funding Gap

There has been significant public comment - particularly from the Australian Nursing & Midwifery Federation (ANMF) on the joint requirement to increase the hourly rate for direct care staff (nurses and carers) as well as increasing the amount of direct care provided to residents to 4 hours and 18 minutes daily (4.3 hours).

We are not qualified to make comment in relation to the adequacy of the current or proposed direct care hours provided with respect to quality of care outcomes. This section is analysing and calculating the additional cost of increasing direct care hours, and consequently the government subsidy funding gap should the increased hours be mandated or required.

The following tables provide details of our methodology and calculations in this respect.

Table 6: Calculation of direct care staff costs as % of government subsidy

	\$ (per bed day)	Note
Government subsidy	188.59	1
Resident fees	63.22	2
Total residential revenue	<u>\$ 251.81</u>	
Direct care staff costs (A)	\$ 128.20	3
Direct care staff costs as % of total revenue	51%	
Direct care staff costs as % of government subsidy (B)	68%	

Note

1. Subsidy includes ACFI and supplements + Accommodation supplements
2. Resident fees exclude means-tested care fees (included with ACFI)
3. Direct care wages excludes workers compensation, hotel services, property and administration

Table 7: Calculation of cost of increased staffing hours per resident per day

	\$ (per bed day)	Note
Direct care staff costs (A)	128.20	
Workers compensation insurance premium (2.2%)	2.82	
Total direct care staff costs (C)	<u>\$ 131.02</u>	
Average staff costs (per resident per hour)	\$ 42.82	4
Total direct care staff costs (assuming ANMF ratio) (D)	\$ 184.12	5
Additional staff costs (D - C)	\$ 53.09	
Direct care staff cost uplift % (E)	24%	

Note

4. StewartBrown Aged Care Financial Performance Survey (3.06 hours per resident per day)
5. ANMF media release 5/4/2018 "4 hours and 18 minutes" (4.3 hours per resident per day)

Table 8: Calculation of funding gap

	20% Vacancy	Nil Vacancy	
	\$	\$	
	(\$'billion)	(\$'billion)	Note
Residential government subsidy funding (F)	\$ 12.1	\$ 12.1	6
Staff cost funded by subsidy (F x B) (G)	\$ 8.2	\$ 8.2	
Staff vacancy benefit (H)	\$ -	\$ (0.4)	7
Net staff costs funded by subsidy (G - H) (I)	\$ 8.2	\$ 7.8	
Staff cost lift % (E)	24%	24%	
Staff hourly wage adjustment % (J)	15%	15%	8
Adjusted staff cost funded by subsidy (I x E x J) (K)	\$ 11.7	\$ 11.1	
Additional funding required (I - K) (L)	\$ 3.5	\$ 2.9	
<i>Less Productivity savings (gains)</i>			9
Savings - reduced workforce turnover	\$ 0.3	\$ 0.3	
Savings - reduced workforce absenteeism	\$ 0.2	\$ 0.2	
Net productivity savings (M)	\$ 0.5	\$ 0.5	
Funding gap (L - M)	\$ 3.0	\$ 2.4	

Note

6. Productivity Commission - Report on Government Services 2018 (Table 14A.4)

7. Staff vacancy benefit is calculated as the percentage benefit if vacancies were reduced (no additional cost)

8. Hourly rate uplift (Korn Ferry Hay Group)

9. Productivity savings (Korn Ferry Hay Group - June 2018)

Korn Ferry Hay Group Remuneration Analysis

Korn Ferry Hay Group (KFHG) conducted a remuneration and evaluation benchmark analysis in relation to Personal Care Workers (PCW) and Nurses (Registered and Endorsed) on behalf of the Aged Care Workforce Strategy Taskforce.

Specific remuneration data collected from aged care providers was compared to other industry sectors for similar level roles/functions as far as responsibility, skills and experience. The approach taken by KFGH is appropriate for this style of analysis.

We have not reviewed the data nor the comparison benchmarking data so are unable to make comment in that regard.

We can, however, confirm that the conclusions drawn by KFHG, and the basis for them, is consistent with our understanding of the relative discrepancy between the fixed annual reward (effective salary package) of PCW and Nurses compared to other equivalent positions. We therefore concur that the staff uplift of 15% (refer note 8 above) is in the range required to enable parity to be closer.

Staff Vacancy Allowance

Staff vacancy rates are in the circumstance whereby there are not suitable staff numbers to provide the care and related service delivery at all times. Therefore any shortfall must be covered by either agency (contracted staff) or overtime hours.

In the case of the wages funding gap analysis (refer note 7 above) we have adopted the average vacancy rate of 20% and estimated the additional cost of agency commission or overtime allowances that would be saved should the vacancy levels be reduced (Nil Vacancy).

Commentary

On the basis of the respective assumptions adopted and using data obtained from the StewartBrown ACFPS, Korn Ferry Hays Group (as commissioned by the Workforce Strategy Implementation Taskforce) and provided by the Department, the additional funding required (funding gap) to meet the joint aspirations of increased direct care hours per resident per day and increase the average wages hourly rate by 15% with productivity gains offsets, it will require additional government subsidy or consumer funding within the magnitude of **\$2.4 billion to \$3.5 billion**.

It must be stressed that such a combination of increased care hours and uplift in wage rates will not occur in a single time frame and would have to be implemented progressively over some years. The purpose of this analysis is to clearly demonstrate the financial consequences of the funding gap that needs to be considered in any future considerations.

With reference to the operating results based on organisation size (refer **Section 2**), the funding gap will affect each provider organisation in the respective size categories. However, the organisations in the size bands less than \$10million per annum revenue and between \$10million to \$30million per annum revenue will not have the asset/equity base to ensure medium term sustainability in our opinion.

Residential Aged Care Inventory

Estimate of Additional Places Required

The Aged Care Financing Authority (ACFA) included the following statement in the *“Fifth report on the Funding and Financing of the Aged Care Sector (July 2017)”*

“It is estimated that the residential care sector will need to build an additional 83,500 places over the next decade in order to meet the provision target of 78 operational places per 1,000 people over 70 and over. This compares with 33,667 new places that came online over the previous decade. The estimated investment requirement of the sector over the next decade is in the order of \$35 billion.”

Profile of Current Residential Aged Care Facilities

The following tables provide a profile of current residential buildings based on an extract from the ACFPS. The Age (year groupings) is based on the year the facility first opened.

Table 9: Profile of current residential care facilities by year grouping

Age (years)	Total Number of Facilities	Facilities with Significant Refurburbishment	Facilities with no Significant Refurburbishment
1-5	28	17	11
6-10	84	13	71
11-15	92	17	75
16-20	106	16	90
20+	602	184	418
Total	912	247	665

Table 10: Profile of current residential care facilities by year grouping (percentage)

Age (years)	Total Number of Facilities	Facilities with Significant Refurbishment	Facilities with no Significant Refurbishment
1-5	3.1%	60.7%	39.3%
6-10	9.2%	15.5%	84.5%
11-15	10.1%	18.5%	81.5%
16-20	11.6%	15.1%	84.9%
20+	66.0%	30.6%	69.4%
Total	100.0%	27.1%	72.9%

Commentary

As noted above, ACFA estimate that an additional \$35 billion capital inflow will be required to build the additional residential aged care places required to meet the anticipated ageing population demand.

The above tables illustrate that there will be a requirement for significant capital inflows to refurbish and upgrade the existing residential facilities. It is interesting to note that 66% of facilities first opened 20+ years ago, and of these some 69.4% have not had a major or significant refurbishment.

It is not possible to estimate the full extent of capital required to upgrade the existing facility inventories, however, it would be reasonable to assume that this will greatly exceed the amount required for new constructions.

The bulk of the investment to fund the future capital expenditure required by the aged care sector is expected to be provided by the FP and NFP sectors. While Refundable Accommodation Deposits play a part in financing this investment, a large part is financed through borrowings from financial institutions.

Without sufficient operating profit to cover the interest cost and ultimate repayment of borrowings and an adequate return on investment outlaid by providers, the ongoing investment in the sector may not be justified. Clearly, it is essential for the future of the sector that profit levels are sufficient to encourage future investment in the sector, enable borrowings to be repaid over time and to provide a profit return to the provider whether FP or NFP.