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FINANCIAL IMPACT OF FUNDING REFORMS FOR SUPPORT AT HOME

Executive Summary

The *Aged Care Act 2024* passed by both houses of parliament on 25 November 2024 with bipartisan support for Chapter 4 "Funding for Aged Care Services" and a number of amendments to the original Bill introduced. The *Act* included the funding reforms resulting from the Aged Care Taskforce Report (Aged care reforms and reviews | Australian Government Department of Health and Aged Care) as well as other measures that were not part of the Taskforce recommendations..

StewartBrown has been very supportive of the Taskforce Recommendations and the Governments clear desire to ensure the financial sustainability of the aged care sector to meet the current and future demands of older Australians. Bipartisan support was strongly welcomed by older Australians and the sector more broadly, and it establishes a strong foundation for the future.

There has been, and will continue to be, considerable public comment as to the nature and extent of the funding reforms prior to the new *Aged Care Act* and this will continue as the *Rules* (replacing the *Principles*) are released for consultation. Much of the focus of the Aged Care Taskforce Report funding reforms related to Residential Aged Care to ensure it becomes more financial sustainable. However, the Report also contained important recommendations in relation to people receiving aged care services into their home.

Taskforce Report and Recommendations

In 2023 the Australian Government established an Aged Care Taskforce. The Taskforce's December 2023 Report commenced with the statement "Australia's aged care needs are increasing as the population ages, and expectations of quality improvements are high. However, the aged care sector is currently not in a financial position to meet expected demand, deliver on the required quality improvements or invest to meet Australia's future aged care needs".

In summary, the Taskforce supported funding reform that involved a greater level of consumer contribution for everyday living and accommodation services to meet the actual cost of providing those services. This is contingent on the consumer having the financial means to pay the actual cost and a system that provides a sufficient safety net for those that do not have the financial means.

Service Lists

Recommendation 1 of the Taskforce Report stated that the Support at Home (SaH) program should be underpinned by a clearly defined service list with inclusion and exclusion principles.

The Government has released the consultation draft of the Aged Care Rules as they relate to the service list, and the draft provides details of what is both included under the various service categories as well as specific exclusions. A somewhat simpler guidance can be found in the Support at Home handbook. The service listing is divided into three primary domains being Clinical (which has no client contributions), Independence and Everyday living.

There are two areas that may cause providers, and consumers, some level of consternation and that is the inclusion of some personal care services such as showering in the Independence domain rather than Clinical domain and the impact of potential clinical requirements on different models of care management. This means that all providers under the SaH program for the first two years (at least) will need to be registered in the Level 4 category which requires compliance with some relevant standards.

In the draft *Rules* there were caps placed on cleaning (52 hours per annum) and gardening (18 hours per annum) but it has been announced that these caps will be removed from the final version of the *Rules*.

Funding and Co-Contributions

The Taskforce recommended that a fee for service model for SaH be established and that consumers only pay a co-contribution for services rendered, and that the co-contribution vary based on the type of service accessed. The new *Aged Care Act* and *Rules* implements the recommendations of the Taskforce and the principle that all clinical care should be funded by the taxpayer (government).

Table 1 sets out the level of co-contribution for each type of participant and the type of service based on the domain in which it is included.

Table 1: Summary of consumer co-contribution levels by service domain

<table>
<tr><th></th><th>Clinical Supports</th><th>Independence</th><th>Everyday living</th></tr>
<tr><td>Full pensioner</td><td>0%</td><td>5%</td><td>17.5%</td></tr>
<tr><td>Part pensioner</td><td>0%</td><td rowspan="2">Part pensioners and CSHC holders will pay between 5%-50% based on an assessment of their income and assets. For part pensioners this will be based on their Age Pension means assessment. CSHC holders will undergo a separate assessment for Support at Home.</td><td rowspan="2">Part pensioners and CSHC holders will pay between 17.5%-80% based on an assessment of their income and assets. For part pensioners this will be based on their Age Pension means assessment. CSHC holders will undergo a separate assessment for Support at Home.</td></tr>
<tr><td>Self-funded retiree (holding or eligible for a Commonwealth Seniors Health Card - CSHC)</td><td>0%</td></tr>
<tr><td>Self-funded retiree (not eligible for a Commonwealth Seniors Health Card)</td><td>0%</td><td>50%</td><td>80%</td></tr>
</table>

There are limited direct financial implications for providers in relation to the co-contributions however there are likely to be some indirect benefits and risks some of which are outlined below:

- Providing more services to part-pensioners and self-funded retirees who, in the main, do not access the current home care system due to the existing means testing regime. They may find the proposition of utilising a support at home package primarily for clinical services an attractive one
- Participant behaviour may change so that clinical supports are prioritised over non-clinical supports due to not having to make a co-contribution to clinical supports
  - Benefit - clinical services generally attract a higher margin than light touch, high usage services such as domestic assistance and gardening
  - Risk - that there may a decline in the higher usage non-clinical support services (independence and everyday living) that make up a major part of current service provision, although this should not be advocated
- Greater risk of bad debts and more time spent on collecting fees - consumer contributions through either the Income-Tested Fee or Basic Daily Fee accounts for less than 5% of all payments for services today. Given that there is going to be a significant shift to co-contributions for many common services, including by full pensioners, this will raise the risk of providers needing to have a focused attention on invoice payments to ensure they are being paid for those services. Currently bad debts is not significant due to the low level of consumer contributions.

Care Management

Under the SaH system, 10% of a participant's on-going fee budget will be allocated for care management services and credited to the provider fee account at the service account level. This means that the care management funds will be pooled to be used across all the participants within each service. Providers will invoice against the service account for the hours of care management provided.

There are several implications of this change:

- Systems will need to be in place to be able to record all time spent by care partners and clinical care partners on billable care management matters (as defined by the handbook) to support the invoices to Services Australia
- Systems will also need to be able to tag that information against individual clients should the intention be to be able to inform participants how much care management they have received in any given budget period
- There will be a loss of revenue from care management service of up to 10% of the value of the package (currently capped at 20% of the package value) reducing the margins for care management and contribution to overheads

However, the Department indicates that some functions funded today via care management, is expected in the future to be delivered via services (e.g. scheduling) and that this is expected to be considered by IHACPA when setting their service prices due out in draft in December and in final version in February.

- Providers will need to assess the care management needs of the individual participants and allocate their pooled care management fund resources according to their assessment of the individual's needs

Funding Impacts

In broad terms, providers of home care services have three current sources of revenue being:

- Provision of services (direct or brokered) - on average 69% of total revenue
- Provision of care management - on average 18.6% of total revenue
- Package management fees - on average 12.4% of total revenue

Under the SaH program, there will no longer be a charge for package management as these costs will be absorbed into the service prices. In addition, there will be a reduction of care management revenue of up to 10% depending on what a provider is currently charging, though some of this difference may be returned in the national efficient price for each service as set by IHACPA.

Under the SaH program there will only have two primary revenue streams, both of which are capped by the government, being subsidies/fees for services provided and care management fees derived from 10% of the allocated budget of a participant.

The immediate financial implications of these changes could be significant, and adversely affect the financial sustainability of providers should the service prices to be set by government not fully compensate providers for those lost revenue streams.

Scenario Modelling

The modelling summarised in *Table 2* has been based on four scenarios:

Current Position - this summarises the financial performance of home care providers based on data from the StewartBrown *Aged Care Financial Performance Survey* for FY24

Scenario 1 - maintaining current levels of profitability through increased service pricing to compensate for loss of package management revenue and reduction in care management revenue

Scenario 2 to 4 - increasing the overall profitability of providers. For the sector to continue to grow and meet the future demand and desired levels of service, it not only remain sustainable it needs to achieve a return that is considered "investible" (a point referenced by Aged Care Minister Anika Wells). The current average of 3.5% profit margin is considered to be insufficient to meet this criteria. *Scenarios 2 to 4* provide a range of operating result return on revenue percentages by way of comparison.

Assumptions

- All modelling is based on FY24 dollars adjusted for changes in policy, with the exception of excluding the new higher package funding level. No indexation of costs or revenue has been built into the modelling
- Package management and the reduced margin for care management has been allocated proportionately to direct and brokered services
- Care management does not include an allocation of package management
- *Care management as a % of revenue* is based on actual revenue charged (received) as distinct from the available package revenue. This explains why this percentage is above 10% as compared to the 10% when based on available package revenue

Table 2: Scenario modelling of changes to revenue streams and pricing under Support at Home program

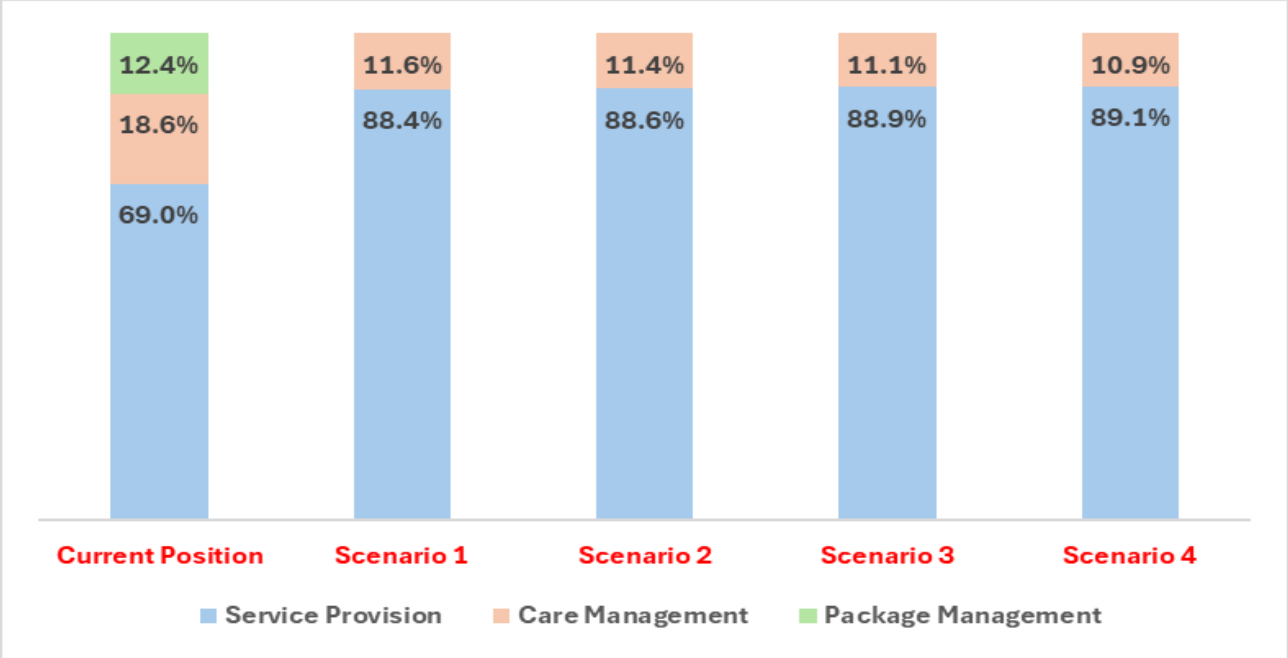
(Dollars per package per day unless otherwise stated)	Current Position *FY24 Survey Average (Actual)*	Scenario 1 *FY 24 Adjusted for Reforms*	Scenario 2 *Adjusted for Reforms + Increased Return*	Scenario 3 *Adjusted for Reforms + Increased Return*	Scenario 4 *Adjusted for Reforms + Increased Return*
Revenue					
Direct and brokered services	54.15	69.36	70.58	72.73	74.54
Care management	14.60	9.09	9.09	9.09	9.09
Package management	9.69	-	-	-	-
Total revenue	**78.44**	**78.45**	**79.67**	**81.82**	**83.63**
Costs					
Direct and brokered services	47.54	47.54	47.54	47.54	47.54
Care management	7.94	7.94	7.94	7.94	7.94
Administration and support services	20.21	20.21	20.21	20.21	20.21
Total costs	**75.69**	**75.69**	**75.69**	**75.69**	**75.69**
Operating result (per package per day)	**$ 2.76**	**$ 2.76**	**$ 3.98**	**$ 6.14**	**$ 7.94**
Operating EBITDA (per package per annum)	**$ 1,209**	**$ 1,210**	**$ 1,657**	**$ 2,442**	**$ 3,102**
KPIs					
Operating result return on revenue	*3.5%*	*3.5%*	*5.0%*	*7.5%*	*9.5%*
Gross margin on direct and brokered services (dollars)	$ 6.61	$ 21.82	$ 23.04	$ 25.20	$ 27.00
Gross margin on direct and brokered services (%)	*12.2%*	*31.5%*	*32.6%*	*34.6%*	*36.2%*
Gross margin on care management (dollars)	$ 6.67	$ 1.15	$ 1.15	$ 1.15	$ 1.15
Gross margin on care management (%)	*45.7%*	*12.7%*	*12.7%*	*12.7%*	*12.7%*
Direct and brokered services as % of revenue	*69.0%*	*88.4%*	*88.6%*	*88.9%*	*89.1%*
Care management as % of revenue	*18.6%*	*11.6%*	*11.4%*	*11.1%*	*10.9%*
Package management as % of revenue	*12.4%*	*0.0%*	*0.0%*	*0.0%*	*0.0%*
Revenue utilisation	*86.3%*	*86.3%*	*87.7%*	*90.0%*	*92.0%*
Available package revenue (per client per day)	$ 90.89	$ 90.89	$ 90.89	$ 90.89	$ 90.89
Available package revenue (per annum)	$ 33,175	$ 33,175	$ 33,175	$ 33,175	$ 33,175
Care management as % of available package revenue	*16.1%*	*10.0%*	*10.0%*	*10.0%*	*10.0%*
Package management as % of available package revenue	*10.7%*	*0.0%*	*0.0%*	*0.0%*	*0.0%*

Observations

- Revenue composition changes significantly with service revenue increasing from 69% of the total revenue for FY24 to 88.4% should the prices maintain current levels of return or to 89.1% should prices be increased to a level which increases profitability to a return of 9.5% of revenue
- The gross margin on service provision would need to increase from 12.2% for FY24 to 31.5% to maintain the current level of overall return on revenue (*Scenario 1*)
- The gross margin on service provision would need to increase from 12.2% for FY24 to 36.2% to improve the level of overall return on revenue to a 9.5% sustainable level (*Scenario 4*)
- If the gross margin on services prices were to increase to a level that supported a sustainable return to providers than is currently the case, revenue utilisation would increase from an average of 86.3% to an average of 92%. This level is what the sector should be aiming for at a minimum given the capping of quarterly unspent funds at the greater of $1,000 or up to 10% of the package value

The modelling is based on sector averages across all types of services. It is understood that some high-volume services such as domestic assistance, gardening and assistance with shopping, are likely to attract a lower margin to maintain a market referenced and competitive price. Similarly, more specialised services such as those in the clinical supports domain, or where staff require additional skills or training, the margins are likely to be higher. As a result, providers, IHACPA and the government will need to take into account the mix of services provided when assessing prices and their sensitivity in the market to ensure that the average margin required by providers to support their financial sustainability is achieved.

Figure 1: Revenue composition for current and scenario positions



Sustainable Level of Profitability

With respect to our recommended sustainable (investible) margin, we have considered this from several perspectives.

Historical Trends

A review of the margins for 2015 – 2017 showed an average profit margin of 7.8% (Top Quartile 20.9%). This was the profit margin levels leading up to deregulation and was considered (at the time) as being the floor level margin required for the significant new entries into the HCP market which occurred in the 2017 – 2020 period

Merger and Acquisitions (M&A)

In recent years there have been some significant M&A activity involving large and mid-tier providers. The majority of these transactions have been based on a capitalisation multiple based on a profit margin in excess of 14%

Top Quartile

Table 3 below is the summary results for the Top Quartile (by program) including the profit margin. Whilst understanding that we should not base the profit margin just on the Top Quartile, the sector needs to move the margins upwards towards these levels in order to make it "investable" for current and new providers. It is worth noting the decline in the Top Quartile margins since the 2015 – 2017 period with competition being one reason. However, the declining margins have inhibited new entrants and major strategic initiatives from many existing providers.

Table 3: Summary of results for Top Quartile (by program)

	FY24	FY23		Difference	FY22
Total revenue $ per client per day	$77.80	$71.48	↑	$6.32	$77.68
Operating result per client per day	$10.68	$10.32	↑	$0.36	$12.76
EBITDA per client per annum	$4,163	$3,912	↑	$251	$4,894
Profit margin	*13.7%*	*14.4%*	↓	*(0.7%)*	*16.4%*

Bottom Quartile

It should also be noted that for those programs not in the Top Quartile, 40.2% are running at a loss. The Bottom Quartile has an average operating loss of $10.62 per client per day. If the Bottom Quartile results improved to be at least a break-even level, the overall average result for the sector would increase to a surplus of $4.35 pcd (5.55% margin).

StewartBrown will continue to undertake analysis in this area including assessing what prices individual service prices may need to increase to from current levels to achieve necessary margins and cover costs of service provision including administration and support costs. Analysis will also be undertaken on the adequacy of prices when they are released. It is anticipated a draft IHACPA release of prices will occur in December, with final prices not known until the end of February 2025.

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For further analysis of the information contained in the report please contact our specialist analyst team

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