HOW SHOULD AGED CARE BE FUNDED?

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The Aged Care Royal Commission is currently considering how aged care should be funded. During September 2020, Paul Keating put forward some interesting ideas about the role of the family home in financing aged care, which we think warrant further consideration.

It has previously been suggested that the financial needs of the elderly, including aged care, be pre-funded via an employer levy much like the current superannuation system. This was proposed in 2018, when Keating noted that longevity has improved significantly since the superannuation system was designed, and we can no longer expect that system to be adequate to finance all the needs of those who live well beyond age 80.

He has now instead proposed a post-payment model in respect of aged care. Under this arrangement, unless the individual pays for aged care from resources at their disposal at the time, the government would pay for aged care as required and recoup the cost after the person's death from the proceeds of their estate.

This makes sense because the assets the elderly could use to fund their own aged care are typically not in a liquid form. Usually the family home, which by then is largely or completely debt-free, is the major asset. The family home can be readily liquidated after death, to provide post-payment for care that has been delivered in old age.

THIS AVOIDS HAVING TO MOVE OUT OF AND LIQUIDATE THE HOME EARLIER, WHICH CAN BE VERY STRESSFUL. BUILDING UP EQUITY IN THE FAMILY HOME, BY PAYING OFF A MORTGAGE OVER MANY YEARS, IS A FORM OF PRE-FUNDING FOR OLD AGE, WHERE THE ASSET ACQUIRED IS ILLIQUID.

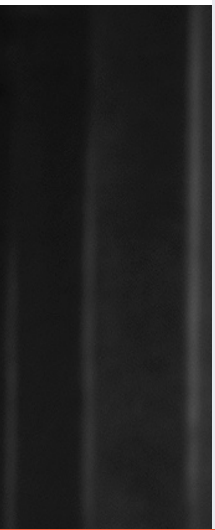
The proposal involves recognizing the pre-funding that is implied in buying a home, and that it may be inconvenient to liquidate that asset to pay for the aged care required until after the individual concerned has died.

Effectively, the government would be giving a loan to the individual (paid straight to the aged care provider) which is then repaid to the government on death. This is not a new concept - banks have been providing reverse mortgage products, which turn the illiquid equity in the family home into liquid resources with the debt repayable on death, for many years. Such products also often provide a guarantee that if the property value at death is less than the amount to be repaid then the remaining debt is waived.

Given the private sector already offers such products it could be argued that the government should not address the same need, but with a different charging structure which would make it difficult to compare the alternatives. However, there is also the question of a safety net – a minimum standard of aged care available to everyone, no matter what resources they have, or how long they live. This can only be provided by the government – as they do with the age pension - to ensure no-one is destitute in old age.

Under the proposal, the amount required to be repaid from the estate would be linked to the amount of aged care support actually provided by the government. The estates of people who require many years' worth of aged care support would repay more than those who require only a short period of aged care. The government will guarantee that the amount required to be repaid will not exceed the proceeds from the sale of the home (and any other resources), and any remaining debt will be waived. This is the aged care safety net – the government meets the costs of a minimum standard of aged care regardless of whether there are sufficient resources to repay the likely costs.

Aged care is just one of the things people plan for in retirement and old age. It is pre-funded partly through the superannuation system, and partly outside it through acquiring assets, including a home. It makes sense that all the amounts pre-funded, including superannuation and the family home (if one has been acquired), should be applied to meet the individual's needs, including aged care.



There needs to be consistency of treatment of the family home in relation to pension entitlement and aged care. One possibility is that there be a universal pension with the pension payments treated as a loan repayable on death in the same way as payments for aged care. A homeowner who has other liquid assets could be allowed to opt out of receiving the pension at any time in order to avoid having an increasing debt to the government repayable from their estate when they die.

Alternatively, instead of a universal pension, a homeowner could have the right to opt in to receiving a pension at any time, with the pension payments treated as a loan repayable on death.

The proposed approach also has implications for whether superannuation could be used as a source for a deposit on a first home. Approached this way, that would simply be exchanging one asset in the overall pre-funding arrangement for another.

In summary, we see the family home as an important element of a holistic approach to providing for all one's needs in old age, including aged care.   We therefore expect that in most cases the value of the family home would be at least partly required to pay for the needs of the elderly, including aged care.

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ANY QUERIES REGARDING THIS STUDY OR OTHER AGED CARE FUNDING MATTERS CONTACT THE TEAM AT PFS CONSULTING TODAY