Challenger **Tech**

For adviser use only.

February 2019

Challenger CarePlus – Cash flow strategies for residential aged care

By Sean Howard, Technical Services Manager

Challenger CarePlus (CarePlus) is designed for clients who have been approved to receive Government-subsidised aged care services. CarePlus is comprised of a lifetime annuity which provides regular guaranteed income to pay for aged care costs and a life insurance policy which provides a guaranteed sum insured payable to nominated beneficiaries or the estate.

CarePlus can work efficiently with Centrelink and aged care means testing to reduce assessable income and assets where commenced before 1 July 2019. The lifetime annuity receives a deduction amount which immediately reduces assessable income and over time reduces assessable assets[1]. The life insurance policy produces no assessable income and immediately reduces assessable assets by assessing the surrender value which is the discounted sum insured[1].

In this article we will look at the various client scenarios where CarePlus can improve financial outcomes for clients entering or living in residential aged care. For more information on CarePlus, please see the Challenger CarePlus Product Disclosure Statement and Technical Guide.

Clients who sell their former home

The decision to keep or sell the former home can have cash flow implications for clients because of the assessment for Centrelink and aged care purposes after entry into residential aged care. For Centrelink purposes, the former home is automatically exempt under the assets test for two years from the date the client vacates the home[2].

The decision to keep or sell the former home can have cash flow implications for clients because of the assessment for Centrelink and aged care purposes after entry into residential aged care.

1 Legislation has been passed 14 February 2019 and subject to Royal Asset to change the means test treatment of lifetime annuities and life insurance policies commenced on or after 1 July 2019 and further analysis of this treatment will be provided in future editions of Challenger TechNews.

2 For couples, the two year exemption commences from when the last member of a couple vacates the former home.

For aged care purposes the asset value of the former home is exempt where the home is occupied by a protected person[3]. Where the former home is not occupied by a protected person, the home is assessed up to the home exemption cap (currently $166,707[4]).

Clients who initially keep their former home and subsequently sell the home must consider the Centrelink and aged care implications of the sale. For Centrelink purposes, the sale proceeds will be immediately assessed and the client will become classified as a non-homeowner. Clients often sell their former home to pay for their accommodation as a lump sum which is exempt for Centrelink purposes. There can be a reduction in Centrelink entitlements if the sale proceeds are significantly more than the lump sum accommodation payment. For aged care purposes, the sale proceeds will be immediately assessed even where they are used to pay for their accommodation as a lump sum. There can be an increase in aged care costs if the sales proceeds are more than the home exemption cap.

For more information on the assessment of the former home, please see the Challenger Tech article 'How is the family home assessed for my aged care client'.

Case study

Evelyn is single, 85 years old and has been approved for residential aged care. She lives in her own home worth $700,000 and expects to receive net rent of $450 per week after she moves out. She has $250,000 invested in term deposits and $5,000 of personal contents.

The aged care facility has an advertised accommodation payment of $350,000 as a refundable accommodation deposit (RAD). Evelyn expects to have personal expenses of $50 per week when she moves into residential aged care.

Evelyn pays $200,000 as a RAD and the $150,000 balance of the accommodation payment as a daily accommodation payment (DAP) and invests $50,000 in term deposits. Her cash flow position will be as follows:

Table 1: Cash flow summary for first year

Cash flow	
Age Pension[5]	$13,922
Investment income[6]	$1,400
Rental income	$23,400
Expenses	($2,600)
Total	**$36,122**
Care fees	
Basic daily fee[5]	$18,491
Means-tested care fee[5]	$7,716
DAP	$8,910
Total	**$35,117**
Tax payable	**($245)**
Net cash flow	**$760**

3 Spouse or dependent child, carer eligible for an income support payment living in the former home for the past two years or close relative eligible for an income support payment living in the former home for the past five years.
4 Thresholds as at 1 January 2019. Applies separately to each member of a couple.
5 Rates and thresholds as at 1 January 2019.
6 Term deposits interest rate assumed 2.8%.

If Evelyn pays $200,000 as a RAD, she will have a cash flow surplus of $760 in the first year.

Evelyn subsequently sells her home, pays the outstanding accommodation payment as a RAD and invests $600,000 in term deposits. Her cash flow position and estate value will be as follows:

Table 2: Cash flow summary and estate value for first year

Cash flow	
Age Pension[7]	$12,943
Investment income[8]	$16,800
Expenses	($2,600)
Total	**$27,143**
Care fees	
Basic daily fee[7]	$18,491
Means-tested care fee[7]	$15,144
Total	**$33,635**
Net cash flow	**($6,492)**
Estate value	**$948,383**

Evelyn's Age Pension entitlement will reduce to $12,943 per annum as a result of the increase in assessable assets. Her home was an exempt asset however the sale proceeds, which were not used to pay the outstanding accommodation payment, will be assessable.

Evelyn's means-tested care fee will increase to $15,144 per annum also as a result of the increase in assessable assets. Her home was capped at $166,707[11] however the entire sale proceeds, including the amount used to pay the outstanding accommodation payment, will be assessable.

If Evelyn subsequently sells her home and pays the outstanding accommodation payment as a RAD, she will have a cash flow deficit of $6,492 in the first year.

Evelyn purchases CarePlus with $400,000 and invests $200,000 in term deposits. Her cash flow position and estate value will be as follows:

Table 3: Cash flow summary and estate value for first year

Cash flow	
Age Pension[7]	$17,564
CarePlus payment[9]	$11,035
Investment income[8]	$5,600
Expenses	($2,600)
Total	**$31,599**
Care fees	
Basic daily fee[7]	$18,491
Means-tested care fee[7]	$12,512
Total	**$31,003**
Net cash flow	**$596**
Estate value	**$955,471**

7 Rates and thresholds as at 1 January 2019.
8 Term deposits interest rate assumed 2.8%.
9 Challenger CarePlus quote with monthly payments and no adviser fees as at 01/02/2019.

Evelyn's Age Pension entitlement will increase to $17,564 per annum as a result of the reduction in assessable assets and her means-tested care fee will reduce to $12,512 per annum as a result of the reduction in assessable assets and income.

If Evelyn purchases CarePlus, she will have a cash flow surplus of $596 in the first year and her estate will be worth $955,471 at the end of the first year. Compared to investing in term deposits she will be better off by $7,088.

Couple clients receiving care

For couple clients who live in residential aged care, it is important to understand the cash flow implications if one member of the couple dies. For Centrelink purposes, the total assessable assets and income of a couple are combined and are subject to illness separated couple thresholds under the assets and income tests. For aged care purposes, the total assessable assets and income of a couple are halved and then each member of the couple is individually assessed.

For couple clients who live in residential aged care, it is important to understand the cash flow implications if one member of the couple dies.

Where one member of a couple passes away and the surviving member inherits all the assets and income of the couple, they must consider the Centrelink and aged care implications of the inheritance. For Centrelink purposes, the surviving member will still have the same total assessable assets and income however they will become subject to lower single thresholds under the assets and income tests. For aged care purposes, the total assessable assets and income will no longer be halved for the surviving member.

For more information on Centrelink and aged care means testing, please see the Challenger Tech Aged Care Guide.

Case study

Henry and Harriet are a couple, both 85 years old and live in residential aged care. Henry moved into the aged care facility first and was classified as a low-means resident and Harriet subsequently moved in and was classified as an accommodation payment resident.

Henry paid $300,000 as a refundable accommodation contribution (RAC) and Harriet paid $450,000 as a RAD. Their aged care facility receives the maximum accommodation supplement of $56.59 per day[10]. They have $200,000 invested in term deposits and $10,000 of personal contents. They currently have personal expenses of $100 per week. Their current cash flow position is as follows:

10 Rates as at 1 January 2019.

Table 4: Cash flow summary for first year

Cash flow	
Age Pension[11]	$47,648
Investment income[12]	$5,600
Expenses	($5,200)
Total	**$48,048**
Care fees	
Basic daily fee[11]	$36,982
Means-tested care fee[11]	$7,848
DAC	$2,385
Total	**$47,665**
Net cash flow	**$383**

If Henry paid $300,000 as a RAC and Harriet paid $450,000 as a RAD, they will have a cash flow surplus of $383 in the first year.

Henry subsequently dies and his RAC is refunded to his estate. Harriet inherits his estate and invests $500,000 in term deposits. Her personal expenses reduce to $50 per week. Her cash flow position and estate value will be as follows:

Table 5: Cash flow summary and estate value for first year

Cash flow	
Age Pension[11]	$18,319
Investment income[12]	$14,000
Expenses	($2,600)
Total	**$29,719**
Care fees	
Basic daily fee[11]	$18,491
Means-tested care fee[11]	$16,308
Total	**$34,799**
Net cash flow	**($5,080)**
Estate value	**$954,670**

Harriet's Age Pension entitlement will reduce to $18,319 per annum as a result of the increase in assessable income and lower single thresholds applying under the Income Test. Henry's RAC was not deemed however Harriet's inheritance which was invested in term deposits will be deemed.

Harriet's means-tested care fee will increase to $15,144 per annum as a result of assessable assets and income no longer being halved. Harriet inherited all of Henry's estate therefore her assessable assets and income have effectively doubled.

If Henry subsequently dies and Harriet inherits his estate, she will have a cash flow deficit of $5,080 in the first year.

11 Rates and thresholds as at 1 January 2019.
12 Term deposits interest rate assumed 2.8%.

Harriet purchases CarePlus with $350,000 and invests $150,000 in term deposits. Her cash flow position and estate value will be as follows:

Table 6: Cash flow summary and estate value for first year

Cash flow	
Age Pension[13]	$21,601
CarePlus payment[14]	$9,656
Investment income[15]	$4,200
Expenses	($2,600)
Total	**$32,857**
Care fees	
Basic daily fee[13]	$18,491
Means-tested care fee[13]	$13,625
Total	**$32,116**
Net cash flow	**$740**
Estate value	**$960,490**

Harriet's Age Pension entitlement will increase to $21,601 per annum as a result of the reduction in assessable income and her means-tested care fee will reduce to $13,625 per annum as a result of the reduction in assessable assets and income.

If Harriet purchases CarePlus, she will have a cash flow surplus of $740 in the first year and her estate will be worth $960,490 at the end of the first year. Compared to investing in term deposits she will be better off by $5,820.

Low-means clients

Clients who are classified as low-means residents typically have a cash flow surplus because the Government generally subsidises all or part of their accommodation. However the client will pay an accommodation contribution where they have assessable assets greater than the asset free threshold (currently $49,000[13]). Where the client has assessable assets closer to the first asset threshold (currently $166,707[13]), the accommodation contribution may create a cash flow deficit.

For more information on low-means residents, please see the Challenger Tech 'Must knows for low-means aged care residents'.

Case study

Brian is single, 75 years old and lives in residential aged care. He was classified as a low-means resident and is paying a daily accommodation contribution (DAC). His aged care facility receives a maximum accommodation supplement of $36.88 per day[13].

He has $100,000 invested in term deposits and $5,000 of personal contents. He currently has personal expenses of $20 per week. His current cash flow position and estate value is as follows:

13 Rates and thresholds as at 1 January 2019.
14 Challenger CarePlus quote with monthly payments and no adviser fees as at 01/02/2019.
15 Term deposits interest rate assumed 2.8%.

Table 7: Cash flow summary and estate value for first year

Cash flow	
Age Pension[16]	$23,824
Investment income[17]	$2,800
Expenses	($1,040)
Total	**$25,584**
Care fees	
Basic daily fee[16]	$18,491
DAC[16]	$9,826
Total	**$28,317**
Net cash flow	**($2,733)**
Estate value	**$102,142**

If Brian is paying a DAC, he will have a cash flow deficit of $2,733 in the first year.

Brian purchases CarePlus with $80,000 and invests $20,000 in term deposits. His cash flow position and estate value will be as follows:

Table 8: Cash flow summary and estate value for first year

Cash flow	
Age Pension[16]	$23,824
CarePlus payment[18]	$2,206
Investment income[17]	$560
Expenses	($1,040)
Total	**$25,550**
Care fees	
Basic daily fee[16]	$18,491
DAC[16]	$6,753
Total	**$25,244**
Net cash flow	**$306**
Estate value	**$105,182**

Brian's DAC will reduce to $6,753 per annum as a result of the reduction in assessable assets.

If Brian purchases CarePlus, he will have a cash flow surplus of $306 in the first year and his estate will be worth $105,182 at the end of the first year. Compared to investing in term deposits he will be better off by $3,040.

16 Rates and thresholds as at 1 January 2019.
17 Term deposits interest rate assumed 2.8%.
18 Challenger CarePlus quote with monthly payments and no adviser fees as at 01/02/2019.

Conclusion

CarePlus provides regular guaranteed income to pay for the client's aged care costs and a guaranteed sum insured, equal to 100% of the amount invested[19], payable to the client's nominated beneficiaries or estate to ensure intended beneficiaries receive their entitlements.

Where the client is not receiving the maximum Age Pension entitlement and is paying a means-tested care fee or if the client is classified as a low-means resident and is paying a DAC, CarePlus can reduce assessable assets and income and improve financial outcomes.

19 Residents of South Australia will receive 100% of the amount invested less the amount of stamp duty initially paid by Challenger.

Contact details

By phone

Challenger Tech team
1800 176 486
(during Sydney business hours)

By mail

Challenger Life Company Limited
Reply Paid 3698
Sydney NSW 2001

By email

challengertech@challenger.com.au

Website

www.challenger.com.au

35999/0219