Challenger **Tech**

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# Your residential aged care questions answered

**By Michael McLean, Technical Services Manager**

Residential aged care is a multifaceted area of advice. Some aspects of aged care advice are more complex than others and involve detailed calculations, intricate definitions and assessments which can change over time. This article answers common aged care questions Challenger Tech receives from advisers.

**Rates and thresholds are as at 1 July 2019 unless otherwise stated.**

## 1. How is my client's means-tested amount calculated?

The means-tested amount (MTA) is a measure of an aged care resident's means and is determined on an ongoing basis from a resident's income and assets assessment, if they choose to complete it. A resident's MTA can change over time if the resident's assessable income and assets change. This can be an ad hoc review when a client updates their information with Centrelink or at a quarterly automated review each 1 January, 20 March, 1 July and 20 September. The MTA calculation is:

> A resident's MTA can change over time if the resident's assessable income and assets change.

MTA = (income-tested amount + asset-tested amount) / 364

Where, income-tested amount = (assessable income – income-free area[1]) x 50%

Asset-tested amount =

- 17.5% p.a. of assets between $49,500 and $168,351.20
- 1% p.a. of assets between $168,351.20 and $406,053.60
- 2% p.a. of assets above $406,053.60

1 $27,284.40 for singles and $26,764.40 for couples (each).

The MTA is used primarily for three reasons:

1. To determine whether the resident is classified as low means (see Challenger Tech June 2018 article); and
2. To calculate a low means resident's daily accommodation contribution (DAC) (see Question 7 on page 5); and
3. To calculate all residents means-tested care fee (MTCF).

## 2. How can my client reduce their means-tested care fee?

The MTCF is calculated as:

MTCF = MTA – maximum accommodation supplement (MAS)

The MAS is set by the Government on 20 March and 20 September each year and is currently $57.14 per day. A resident can not pay a MTCF higher than their cost of care.

Residents who have assessable income above the income-free area[2] will have an income-tested amount. If they also pay a MTCF then reducing assessable income may help to reduce their MTCF. Strategies to reduce assessable income include:

- Investment bond in a trust;
- Reducing deemed assets – for example paying a refundable accommodation deposit (RAD) or purchasing personal assets;
- Challenger CarePlus; and
- Long-term annuity with nil residual capital value (RCV).

Clients with assessable assets equal to or above $49,500 will have an asset-tested amount. If they also pay a MTCF then reducing assessable assets may help to reduce their MTCF. Strategies to reduce assessable assets include:

- A funeral bond (up to $13,250) or prepaid funeral expenses (unlimited) – if a client has both, then only the prepaid funeral is exempt, not both. However, a burial plot can be an exempt asset on top of either a funeral bond or prepaid funeral;
- Challenger CarePlus;
- Home renovations or upgrade – Only if one spouse remains living in the former home; and
- Super accumulation – for those under Age Pension age (see Question 10 on page 7).

The Challenger Aged Care Calculator can help advisers determine what strategies may benefit their clients. Consider Table 1 overleaf, which shows the year one cash flow for a resident who has paid a $400,000 RAD and has $180,000 left over in cash and term deposits.

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2 $27,284.40 for singles and $26,764.40 for couples (each).

Table 1: Challenger Aged Care Calculator 'Results' tab

**Client**

**Assessable income & assets for aged care**

| | | |
|---|---|---|
| **Assets for aged care purposes:** | | $580,000 |
| **Income for aged care purposes:** | | $27,124 |
| **Daily means-tested amount:** | | $73.23 |
| Income component: | $0.00 | |
| Asset component: | $73.23 | |

**Care fees**

| | Daily | Annual |
|---|---|---|
| **Basic daily care fees:** | $51.21 | $18,692 |
| **Means-tested care fee:** | $16.09 | $5,873 |
| **Accommodation amount:** | $0.00 | $0 |
| **Extra service fee:** | $0.00 | $0 |
| **Total:** | **$67.30** | **$24,565** |

**Age Pension**

| | |
|---|---|
| **Annual Age Pension:** | $24,081 |
| **Fortnightly Age Pension:** | $926.20 |
| **Means test:** | Full pension |
| **Maximum annual Age Pension:** | $24,081 |

Table 1 shows an asset-tested amount of $73.23 per day, but no income-tested amount. This confirms that reducing assessable assets for this client will help to reduce their $16.09 per day MTCF, but reducing assessable income will not.

## 3. How will the accommodation interest rate change for my client?

The maximum permissible interest rate (MPIR) is charged on any outstanding RAD and calculates the equivalent daily amount. The MPIR is generally set for a resident on the day they enter care, however it can change if they move rooms within a facility.

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The MPIR is updated on 1 January, 1 April, 1 July and 1 October each year. Although this is not important for many existing residents, it can create an interesting consideration for new residents.

The MPIR is equal to the general interest charge (GIC) less 3%. The GIC for the next immediate period is usually announced by the Australian Taxation Office (ATO) a month in advance. This provides advisers with an opportunity to assess whether their clients will benefit financially by moving into care before or after the quarterly review of the MPIR.

For example, the MPIR for entry between 1 July 2019 and 30 September 2019 is 5.54%. On 3 September 2019, the ATO released the next GIC rates which predetermined that the MPIR between 1 October 2019 and 31 December 2019 is going to be 4.98% (a reduction of 0.56%). For a client with a RAD of $400,000 who intends to pay their accommodation entirely as a daily amount, this means a saving of $2,240 per year if they decide to (and are able to) enter care from 1 October 2019. On the other hand, a lower MPIR means a higher refundable accommodation contribution (RAC) calculation for a low means resident (Question 7 on page 5).

## 4. Why would my client NOT pay their accommodation payment as a lump sum?

Generally it makes sense to pay a lump sum for aged care accommodation, for the following reasons:

- Exempt asset for Age Pension assessment;
- No income is assessed for the aged care MTA; and
- Guaranteed savings equal to the MPIR.

Residents are able to pay a partial lump sum for their accommodation if they are not able to afford to pay the full lump sum. They can also deduct the daily accommodation payment (DAP) from their partial lump sum if they choose to.

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However like most advice, there can be exceptions to the rule. Scenarios where it might not be best to pay a lump sum for a client include where they:

- Expect to earn greater returns (after tax) than their MPIR;
- Have a short life expectancy – paying a RAD may be a greater burden on administration than it might be a benefit financially;
- Have large unrealised capital gains on investments – selling assets in order to pay the RAD may create large capital gains tax; and
- Don't want to sell their former home and don't have other available funds.

## 5. Should my client use a reverse mortgage to pay for their accommodation?

A reverse mortgage is a loan which allows a person to borrow money against a property, usually their home. The loan can be in the form of an income stream or a lump sum, but regular repayments don't have to be made and compound interest is added to the loan balance. Reverse mortgages which cater specifically for aged care residents are sometimes called 'aged care loans'.

A reverse mortgage could be considered where an aged care client wants to keep their home, but has few available assets to fund their aged care fees, or where the comparison rate of the reverse mortgage is less than the MPIR. However there are some important considerations:

- Comparison rates for reverse mortgages may be greater than the MPIR[3];
- Reverse mortgages can have application fees (considered in the comparison rate calculation);
- Maximum loan amounts and loan-to-value ratios (LVRs) apply;
- Assessable assets will not be reduced by the reverse mortgage – Using a reverse mortgage to pay a RAD could increase a person's MTCF; and
- The loan may have to be repaid after the specified loan term, for example after three, five or seven years.

Aged care clients wanting to keep their home and fund their DAP can consider the pensions loan scheme (PLS) offered by the Government as a potentially cheaper option to commercial reverse mortgages. The PLS interest rate is currently 5.25% p.a. with no application fee. However the PLS is only offered as an income stream and therefore cannot be used to pay the RAD. See Challenger Tech's August 2019 article for more information on the PLS.

Aged care clients wanting to keep their home and fund their DAP can consider the pensions loan scheme (PLS).

3 La Trobe 7.60% p.a., Heartland Seniors Finance 6.44% p.a., IMB Bank 5.61% p.a. as viewed online 03/09/2019.

## 6. What is the 28-day rule for lump sum accommodation payments?

Within the first 28 days from entry into permanent residential aged care, a resident who chooses to pay for their accommodation as a lump sum must be left with the minimum permissible asset amount (currently $49,500).

The calculation of a person's assets for the purpose of the minimum permissible assets has one difference from the assessable assets calculation for the purpose of the MTA. Where a protected person is not living in the former home, it is not capped for the purpose of the minimum permissible assets, and the entire value of the home counts. This means where the former home is not protected, a resident can use all their assets outside of the home to pay a RAD/RAC (as long as their share in the home is worth at least $49,500) within the first 28 days from entry.

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For a couple, it is still combined assessable assets divided by two. This means effectively a couple must be left with $99,000 assessable assets after one spouse pays a RAD/RAC within the first 28 days from entry.

The minimum permissible asset amount should be listed as the 'minimum amount of net assets' on a resident's initial means assessment and fee advice letter from Centrelink. However, if a resident does not disclose their income and assets to Centrelink/DVA the minimum permissible asset amount does not apply.

Importantly, from the 29th day onwards, a resident can pay any amount as a lump sum without limitation.

## 7. How do I calculate the DAC/RAC for my low means resident client?

The DAC is equal to the lower of a resident's daily MTA and their facility's daily accommodation supplement amount.

The DAC is equal to the lower of a resident's daily MTA and their facility's daily accommodation supplement amount.

The maximum accommodation supplement (MAS) is currently $57.14 per day with lower supplements applying for certain facilities. As at 31 December 2018, 48%[4] of all facilities were eligible for the MAS (up from 35% at 31 December 2017[5]). When modelling your client's scenario and their facility's accommodation supplement is not known, it is recommended to assume the maximum amount.

Once you know a client's DAC, you can calculate the equivalent RAC.

RAC = (DAC x 365) / MPIR

For example, a resident who enters care between 1 July 2019 and 30 September 2019 and pays a DAC of $57.14 per day will have an equivalent RAC amount of:

RAC = ($57.14 x 365) / 5.54% = $376,463.90

This amount can change over time as the accommodation supplement amounts index and/or as a client's MTA is recalculated with changes to their assessable income and assets. If a client were to change rooms within a facility and the MPIR had changed, their maximum RAC payable could increase or decrease.

4 ACFA seventh report of the funding and financing of the aged care industry 2019 – section 7.1.2.

5 ACFA sixth report of the funding and financing of the aged care sector 2018 – section 4.5.

## 8. How is the former home assessed for aged care residents?

For residents who enter permanent residential aged care on or after 1 January 2017, net rental income from the former home is assessed as income for both Age Pension and aged care. If no previous tax return is available to determine net rental income, then usually two thirds of the rental income is used as an estimate.

For the assets test, the assessment for Age Pension and aged care purposes is different.

For Age Pension purposes, the former home is exempt and the resident remains a homeowner for two years after entering care (or for a couple from when the second spouse also enters care or dies), after which the home is assessed as an asset and they become a non-homeowner.

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For aged care purposes, there is no two-year exemption. The former home is exempt indefinitely whilst a protected person (see Question 9 on this page) remains in the home. Where there is no protected person, the home is assessed up to the home cap, currently $168,351.20 (the home cap applies separately to each member of a couple).

Any residents who entered permanent residential aged care before 1 January 2017 may be entitled to further exemptions on the former home, which are explained in more detail in the Challenger Tech October 2018 article.

## 9. Can the exempt status of the former home change over time?

Yes. The former home can be initially exempt if a protected person is living in the home.

A protected person is a:

- spouse;
- dependent child[6];
- carer eligible for an income support payment who has been living in the home for the past two years; or
- close relative[7] eligible for an income support payment who has been living in the home for the past five years.

The most common income support payments are Age Pension, Disability Support Pension, Carer Payment and Newstart Allowance. Carer Allowance is not an income support payment for protected person purposes.

Carer Allowance is not an income support payment for protected person purposes.

The exemption can change over time, including in the following scenarios:

- Spouse dies;
- Spouse also moves into aged care;
- Carer or close relative loses their income support payment;
- Protected person moves out of the home; and
- Child is no longer 'dependant'.

6 Must be under 16 years of age or 16-24 in full-time education and cannot be receiving a social security pension, for whom the resident must be either legally responsible for the day-to-day care and welfare or legally obliged to provide financial support.

7 Parent, sister, brother, child or grandchild.

## 10. My client is going into aged care and is under Age Pension age, what issues should I be considering?

Unfortunately it is not uncommon to discuss an aged care client who has not reached Age Pension age with advisers. At 30 June 2018 3.4% of residents were under age 65, totalling 6,234[8]. A few considerations when advising these younger aged care clients include:

Super accumulation is not assessed for Age Pension or aged care purposes.

Residents with dependent children are exempt from paying a MTCF.

- **Super accumulation is not assessed for Age Pension or aged care purposes:** As opposed to super income streams which are assessed as an asset and may also have assessable income. Investing in super accumulation can therefore help these clients to maximise their Age Pension and minimise their MTCF. However, consider that super accumulation doesn't provide a client with a regular income stream and any earnings within the fund are taxed at 15%.
- **Residents with dependent children are exempt from paying a MTCF** – Given that these residents are younger there is a higher likelihood that they have one or more dependent children. Note that the 'dependent' status could be lost in future and if that happens the resident could begin to pay a MTCF.
- **National Disability Insurance Scheme (NDIS)** – The NDIS can pay daily accommodation amounts and means-tested care fees for eligible residents under age 65, but won't pay the basic daily fee, additional/extra services fees or accommodation lump sums. Where a person begins receiving care after turning age 65 then they cease being an NDIS participant. However, an NDIS participant who is already receiving aged care services when they turn 65 may continue to receive benefits under the NDIS.
- **Spouse still working** – Employment income is assessable for Age Pension and aged care purposes. Furthermore where the spouse is below Age Pension age they don't receive the benefit of the $7,800 per year work bonus, so all their employment income is assessable.
- **Spouse who loses Carer Payment** – When a care receiver enters permanent residential aged care the spouse's Carer Payment ceases after a 14-week adjustment period. At this point, if the spouse does not continue to receive an alternative income support payment, such as Age Pension, Disability Support Pension (DSP) or Newstart Allowance, they cease to be a protected person. This could affect the resident's DAC and/or MTCF.
- **Eligibility for DSP** – Although not eligible for Age Pension, an aged care resident who is below Age Pension age should automatically meet the disability eligibility for DSP.

8 GEN aged care data – 'People using aged care'.

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