

Productivity Commission

Inquiry into Caring for Older Australians

Submission by and on behalf of the organizations listed on the cover sheet.

Spakia Pty Ltd is the Approved Provider of Trevu House Residential Aged Care.

We have already made submissions to the Commission regarding the effects of Fringe Benefits Tax and PBI status in our original submission.

The Commission referred to the submission by Spakia Pty Ltd and 6 other SA providers in its Draft Report.

In this submission we wish to make a range of additional comments that relate to these two issues having reflected on the Commission's Draft Report.

FBT Exemption

In our earlier submission we argued that the FBT exemption distorted the labour market and the Commission indicated some acceptance of that argument.

We consider that as labour markets for the aged care sector tighten due to demographic changes in the future and quite possibly issues related to wage rates, the distorting effect of the FBT exemption will become more important.

Accordingly as providers with no FBT exemption consider making investment in residential aged care, they will have to take into account the relatively greater scarcity of labour available to them caused by the FBT exemption.

This issue can only be resolved by private providers at significant additional cost that will reflect on the viability of new investment by the private sector.

Or, alternatively, the relative lack of labour availability will become a limiting factor in the private sector making new investments in residential aged care.

Accordingly we think the FBT Exemption should be created for all new employees and progressively withdrawn for existing employees.

PBI Income Tax Exemption

In the Draft Report Commission recommends the equal treatment of bonds and periodic accommodation charges in the assessment of pension eligibility.

If implemented this will have a number of effects:

- Existing bond pools will tend to reduce as the incentive to pay a bond rather than a periodic accommodation charge is eliminated
- The ability of generic high care facilities to raise bonds will be limited

While it is easy to see the logic of the Commission's recommendations in this area, there are significant effects.

Those with PBI Tax exempt status:

To access capital these organisations will be tending to substitute the use of bonds by

- Accumulating periodic accommodation charges to form an equity pool to leverage borrowings, and
- Using borrowings instead of bonds and incurring interest expense together with the very significant burden of repayment obligations compared to bond usage.

These two factors will significantly slow the ability of these organisations to aggregate the capital required to undertake new residential aged care developments, and of course, it is much less efficient than the use of bonds.

Private Providers

Private providers of residential aged care will have the same issues as noted for those with PBI exempt status.

However, private providers face an additional significant financial challenge.

Bonds are a liability on the balance sheet and as such are not affected by taxation.

The likely tendency for periodic accommodation charges to replace bonds pursuant to the Commission's recommendations will mean that company tax, currently at 30% will need to be paid on the income of periodic accommodation charges prior to these funds being aggregated and used for capital works.

Thus for every \$100 that a PBI Tax exempt organisation can put into capital works, the non exempt capital provider will only be able to fund \$70 for capital works.

Clearly a significant reduction in efficiency compared to the use of bonds for capital development as well as a distinct disadvantage for private providers.

Lenders Reactions

The combination of the reduction in bond pools together with the inevitable decrease in bond pool predictability will tend to decrease loan to value ratios and raise interest rate risk margins, especially in the current post GFC lending environment.

These negative factors will not be off-set by the existence of a periodic accommodation instead of an equivalent bond.

Will the industry be sufficiently viable to attract new capital?

The residential aged care industry has a continuing poor EBITDA return on investment that has all but stalled the development of new capacity.

Additionally, if bond retentions are to be removed, this will cause a significant reduction in EBITDA that is unlikely to be made up by additional increases in periodic accommodation charges

Against this low return background, coupled with the effects described above, it is hard to see how the industry will improve its viability sufficiently to attract the necessary capital to fund the increase in capacity that appears to be needed over the coming years.

Accordingly a significant objective of the reform process is very likely to be thwarted.

We would suggest some careful rethinking and further consultation with stakeholders around these issues

Other issues for Non PBI Providers

Pursuant to the Local Government Act in South Australia PBI Providers are compulsorily rebated 75% of the assessed Council Rate and no such rebate is provided to private providers.

A similar situation exists in the charging of water & sewage rates by the state utility where PBI providers are provided with a 25% rebate on the assessed charges and there are some lower priced alternative assessment methods

We understand that similar arrangements exist in most states.

In an overview context it seems as though the taxation element of the respective charges is rebated and the remaining charge reflects the cost of service provision.

Significant taxpayer subsidies paid to private aged care providers are effectively being taxed to support exactly the same service provision as is provided by PBI Status providers and it would be very helpful if the Commission were to make recommendations to address this situation.

We ask that the Productivity Commission have regard to the forgoing matters in their final report

Craig Brown

For & on behalf of Spakia Pty Ltd