School of Management
Haymarket Campus
University of Technology, Sydney
P.O. BOX 123
Broadway NSW 2007

Email: marie.delarama@uts.edu.au
Phone: +61 2 9514 3604
Fax: +61 2 9514 3817

12th November 2008

Committee Secretary
Community Affairs Committee
Department of the Senate
PO BOX 6100
Parliament House
Canberra ACT 2600
Email: community.affairs.sen@aph.gov.au

Re: Inquiry into Aged Care Amendment (2008 Measures No. 2) Bill 2008

Dear Committee Secretary,

Please find attached our comments regarding the proposed amendments to the above Bill. Particularly we raise concerns regarding the lack of acknowledgement of the type of ownership and the lack of transparency in publicly available information regarding changes in ownership in the aged care sector. Further, we question why subsidies are granted regardless of profit status, which has a tendency to encourage a focus upon short-term efficiencies and undermines the social responsibility imbued in the provision of a community care service (see Section 1).

We highlight the recent Australian collapse of ABC Learning and the healthcare experience from the US as cautionary evidence for the aged care sector. We also focus on studies which have signified the for-profit tendency to capitalise upon the quality of care given the asymmetrical nature of aged and child care services (see Section 2).

Given the recent instability in financial markets globally, we question the market logic of the subsidy incentives that encourage private equity investment as these expose the fundamental social responsibility of care provision for the elderly and children to the fluctuations and instabilities of the global market (see Section 3).

Finally, we make direct comments in regards to items we support in the proposed amendments to the legislation. From our earlier comments we draw a recommendation for potential inclusion or future discussion (see Section 4).

1. Why are government subsidies provided without regard to profit status?
Proposed amendments to the Bill do not distinguish between the non-for-profit entities, small commercial operators and large investment entities in the sector. The government subsidies provided – regardless of financial status or profitability – remain a matter of concern. While we acknowledge the proposed addition of Item 7 (Section 8-3A: Key Personnel) may contribute toward transparency, we recommend a further measure to publicly account for ownership transfers (see Section 4).

1.1 Reducing costs to maximise profitability?
Our trust in for-profit aged care providers can grow if regulation guides the direction of subsidies within the aged care sector to counter-balance the potentialities for market failures. In this regard, Tannous and Luo (2006) note that:

> "Market failure exists in the provision of residential aged care services in Australia due to the imperfection of competition that arises out of government actions…relatively fewer for-profit facilities operated in less than highly accessible regions and were more likely in larger sized compared to those not-for-profit. This is going to have important future impact on the availability of facilities in rural and remote regions. Increasingly not-for-profit operators are closing their facilities or moving away from the provision of aged care and they may not be necessarily replaced with for-profit providers."[1]

We make a cautionary note regarding these findings and the lack of discriminatory decision-making in regards to the distribution of subsidies. In particular, we note that subsidies should particularly encourage service provision in rural and remote areas and in the provision of high care services for those with less access to expensive care facilities.

1.2 The marketisation and inevitability of an aged care industry?
Furthermore, we draw attention to the intent and the investment horizon of private equity investment in the care provision services (see Section 3). We argue that the enticement of government subsidies in the sector does not ensure the subsidies' maximised operational efficiency. Providing subsidies without taking into account the profit status of the entity is altering the aims of what the

[1] Tannous, K. & Luo, K. (2006) Ownership of Residential Aged Care Facilities in Australia, *Macquarie Economics Research Papers*, No. 8/2006, November, ISSN: 1834-2469

subsidies are supposed to achieve in the first place (are they the means or the ends? are they integral or peripheral to entry?), creating an uneven playing field of non-profit vs. for-profit competition (if indeed this is the new market reality) and also distorting the sense of direction of the sector where there seems to be a linear approach towards the marketisation of the aged care field.

All entities in the sector are competing for the same limited pool of subsidies. Are these subsidies evolving into what are called 'perverse subsidies' which "undermine market decisions about investment and reduce pressure on businesses to become more efficient"?[2]

We understand that providing subsidies to attract private investment can be legitimised as a means of increasing the efficiency within a sector which some consider to be a 'cottage' industry. Our review suggests the significant presence of private equity and large corporate ownership in the aged care sector indicating this short-term market incentive has achieved its aims. However we argue that in some circumstances, this subsidy incentive encourages short-term private ownership to capitalise upon government funding without addressing long term needs of care provision in the sector. In the next section, we cite lessons from the Australian childcare sector and the example of the US health care system as cases where market forces can encourage private monopolies, short-term instability and increased costs for users.

2. ABC Learning and the American healthcare system

In this section, we briefly examine the recent developments in the Australian childcare sector and the transformation of the American health care system. While we acknowledge these sectors have different structural, regulatory and geographical variables, we note some comparisons as a means of highlighting our calls for caution in government incentives that may entice the full-marketisation of the aged care sector.

2.1 Lessons from ABC Learning for the aged care sector

We consider the potential for similarities to occur between the experience of another highly subsidised community service 'industry' and the aged care sector. At its height, ABC Learning evolved into a highly sophisticated property and finance exemplar with its raison d'être – the provision of child care – seemingly becoming rather peripheral to the company's success and growth. However, now that ABC Learning has unravelled, the beleaguered company has shown government subsidies can create a monopoly of supply of care provision in some areas leaving communities exposed if the major player collapses. Further, this

[2] Myers, N. & Kent, J. (2001) *Perverse Subsidies*, Island Press, ISBN: 1559638354

situation becomes further complicated as government is prompted to rescue and unravel the corporate structure of ABC Learning and to provide funding to avoid the short-term collapse in the provision of a fundamental community service. [3,4]

On the demand side, government subsidies can encourage monopolistic behaviour and constrain the growth in the care providing sector. For example, since the emergence of ABC Learning, the increase in taxpayer funding of child care seems to have contributed to high fees in a constrained and increasingly ABC-dominated childcare market, rather than an increase in places. Arguably, as is typical of a monopolised market, there is more money to be made from constraining the market and charging high fees, than from expanding the number of child care places.

The description of the aged care sector as reflecting the 'cottage' nature of the industry after the publication of the Hogan Report seemed to suggest that this was somehow a negative connotation on the way the aged care sector is run and managed. Given again the monopoly of supply that we have seen with ABC Learning in the childcare sector (especially in regional areas), would it be in the national interest to have monopolies or oligopolies of supply encouraged to replace the still heterogeneous structure of the sector?

According to the Productivity Commission (2008) non-profits in the aged care sector comprised 61.4% of the sector[5]. The notable influx of for-profit participation particularly from large entities has seen the for-profit share now around 26.9% with government-owned facilities comprising the rest.

According to Macquarie Bank, around 70% of its operating income in aged care is from the Commonwealth government.[6] Similarly in child care, ABC Learning regularly acknowledged that its continued existence depends on government childcare policies. In its 2007 Annual Report, the company had a section entitled 'Economic Dependency' which states: 'The operation of childcare centres and training colleges benefit from the continued support by statutory authorities of the Federal Governments as well as the Federal Government's policies on the provision of subsidies to the childcare industry and benefits provided to parents of children attending childcare centres.' (ABC Learning 2007).

---

[3] Carson, V. (2008) Investor doubted ABC's viability, Sydney Morning Herald, November 11 http://business.smh.com.au/business/investor-doubted-abcs-viability-20081110-5lo5.html

[4] Horin, A. (2008) Women tolled warning bells but no one wanted to listen, November 8 http://www.smh.com.au/news/opinion/adele-horin/badele-horinb/2008/11/07/1225561134611.html

[5] Productivity Commission (2008) Trends in Aged Care Services: Some implications, Productivity Commission research paper, September ISBN: 9781740372640

[6] MCAG RCA Regis Merger (2007) Aged Care Funding Review, May 2007, Powerpoint presentation.

2.2 Lessons from the American healthcare sector

WR Scott (2000) in his study of the transformation of the American healthcare system[7] noted that the American healthcare field was originally characterised by the professions (such as the American Medical Association or AMA) governing entry, training, and work for the practice of medicine and resisting the emergence of organisations beyond the non-profit community hospitals. The professional dominance by the AMA ensured boundary control with a strict definition of a healthcare provider.

After World War Two, the healthcare field saw the rise of medical specialists and specialist organisations which were alternatives to the AMA. The sector fragmented and home health agencies and disease centres proliferated alongside traditional community hospitals.

By the 1980s, the sector was deregulated and formalised cost-benefit analysis by insurance groups and others created the for-profit business: the Health Maintenance Organisation or HMO (eg Kaiser Permanente, CIGNA, Humana etc). The HMO combined insurance and healthcare and became the dominant organisation displacing non-profit community hospitals and freestanding physicians. Thus, the healthcare field in America was transformed and associated costs grew with such a transformation. Today, American health expenditure as share of GDP is the highest amongst OECD countries.[8]

GF Davis (2005) reflecting on this experience suggests:

> "…once a practice proves profitable, whole fields can change their shape through the entry of newcomers and the restructuring of incumbents. Moreover, appropriate practice becomes codified in a new logic of appropriateness, reflected in both rhetoric and practice…once a field has been restructured, either due to state actions or market pressures, the next step is for a new set of practices to become a settlement – the way things are done here."[9]

Thus we ask the committee to review the provision of subsidies in the Bill and take into account the profit status of entities in the subsidies' distribution.

---

[7] Scott, WR (2000) *Institutional Change and Healthcare Organisations*, University of Chicago Press

[8] OECD (2008) OECD Health Care Data – Frequently Requested Data http://www.oecd.org/document/16/0,3343,en_2649_34631_2085200_1_1_1_1,00.html accessed November 2008

[9] Davis, GF (2005) Firms and Environment in Smelser, NJ and Swedberg, R. (eds) *Handbook of Economic Sociology*, Princeton University Press.

2.3 Contract failure theory

Given incentives in the form of government subsidies can encourage private investment in the provision of care services, we find reason to propose non-profit providers may have more incentive to direct funds towards their intended purpose in the delivery of quality care, given their non-profit status.

Looking at demand side theories, of particular relevance to non-profit aged care providers is what Weisbrod (1988) describes as types of "trust-type nonprofits" (TRUNPOs) and the notion of contract failure. TRUNPOs are organisations "that are thought to provide trustworthy information to consumers who cannot easily judge the quality of services for themselves." (p.10) [10]

According to contract failure hypothesis, non-profit service providers are preferred over for-profit counterparts in industries where there are high levels of information asymmetry such as the aged care sector where the children of aged parents are unable to closely monitor the quality of care services their parents receive.

Therefore, non-profits arise where ordinary contractual mechanisms do not provide consumers with adequate means to assess producers leading to consumer distrust of private providers and establishing a marketplace for non-profit service organisations (Hansmann 1987)[11]. According to Weisbrod, "unlike private enterprise, such an institution [the non-profit organization] does not reward sellers who take advantage of consumers' informational handicaps." [12] Or as Hansmann puts it:

> "The non-profit producer, like its for-profit counterpart, has the capacity to raise prices and cut quality in such cases [of informational asymmetries] without much fear of customer reprisal; however, it lacks the incentive to do so because those in charge are barred from taking home any resulting profits. In other words, the advantage of a non-profit producer is that the discipline of the market is supplemented by the additional protection given the consumer by another, broader 'contract', the organization's legal commitment to devote its entire earning to the production of services." (1980: 844)[13]

[10] Weisbrod, B.A. (1988) *The Non-profit Economy*, Cambridge MA: Harvard University Press

[11] Hansmann, H.B. (1987), 'Economic Theories of Non-profit Organization', in W. W. Powell (ed.), The Nonprofit Handbook, Yale University Press, New Haven, pp.27-42.

[12] Weisbrod, B.A. (1989), 'Rewarding Performance that is Hard to Measure: The Private Non-profit Sector', Science, 244 (4904): 541-546.

[13] Hansmann, H.B. (1980) The Role of Non-Profit Enterprise, *Yale Law Journal*, 89 (5): 835-902

For proof, Rose-Ackerman asserts that empirical evidence collected by Weisbrod shows that "non-profits providing long-term care generally take less advantage of their informational superiority over customers than do for-profits"(Rose-Ackerman, p. 722).[14]

3. The government is the underwriter of last resort, and the taxpayer is the ultimate creditor

The beleaguered example of ABC Learning where the Federal Government has proven to be the underwriter of last resort (after prior warnings that such an event could occur especially from community childcare providers) may be a situation which the Government may face should the drought of financial investment continue in the private sector.

Citing dela Rama's submission last year to the Senate Inquiry into Private Equity Investment, Senator Ursula Stephens noted,

> "unlike other areas where private equity investment tends to be high risk and speculative, this is an area of economic activity that is in essence underwritten by government subsidies and will continue to be because of the nature of aged care provision."[15]

Given the lengthy financial crisis that continues to occur globally, events in the US, UK and Australia have shown that in highly sensitive and economically important sectors (finance, banking and childcare respectively) government is truly the underwriter of last resort and the taxpayer is the ultimate creditor.

We recall the press release of ANZ Capital at the time of its entry into the sector when it bought Ibis Care:

> "ANZ Capital said ANZ is pleased to provide IBIS Care with access to investment-banking solutions that are historically only available for Wall Street-sized firms. ANZ Capital invests in companies looking at growth, acquisitions and buy-outs, in particular profitable businesses with good management teams. This is our first private equity investment into the aged care sector. We are pleased to be supporting IBIS Care's top quartile management team with their growth and acquisition plans."[16]

---

[14] Rose-Ackerman, S. (1996) Altruism, nonprofits and economy theory, *Journal of Economic Literature*, 34 (2): 701-728

[15] p.E84 in Senate Standing Committee on Economics (2007) Reference: Private equity investment and its effects on capital markets and the Australian Economic, Hansard, Thursday, 26 July.

[16] Mr. Robert Read, Senior Manager at ANZ Capital in ANZ (2006) Media Release: ANZ Capital Supports Leading Aged Care Operator IBIS Care Pty Ltd, 21 March.

Now that the investment banking model has been largely discredited with the spectacular collapses or organizational restructuring of the same Wall Street--sized firms, it ought to be acknowledged that entry into the aged care sector by for-profit entities - who previously had little interest in the sector - was mainly due to the boom part of the last financial cycle where easy credit allowed short-term, speculative investment. As we are now entering a period of downturn what type of financial guarantee does the Government have available in rescuing aged care homes whose operational viability may be undermined by the current economic conditions?

Below is a table of ownership activity by private equity entities in the sector. Note the 'flipping' of the aged care investment by Citigroup a year only after its purchase of DCA Group.

Table 1: Private Equity Owners in the Aged Care Sector

Company	Private Equity Owner	Corporate Owner	Year Acquired or Established (Exited)
Craigcare	Hastings Funds Management	Westpac	2003 (2006)
DCA Group	CAID Pty Ltd	CVC & Citigroup	2006 (exited 2007 to BUPA)
Ibis Care	ANZ Capital	ANZ Bank	2006
Primelife	B&B Communities Group	Babcock and Brown	2005 (exited 2008 to Lendlease and Stockland)
Principal Healthcare Group	AMP Capital Investors	AMP	2006
Retirement Care Australia/Regis	Macquarie Capital Alliance Group	Macquarie Bank	2005

Citigroup sold-on this interest to BUPA for around $1.225B. In comparison, the Government budget is only $8.6B a year for the sector, thus some of the market valuation for aged care entities is quite staggering. Again, should multi-billion dollar entities which have greater financial leverage and scope than the Federal Government be allowed to continue to access the subsidies in the sector? Are these subsidies being used for their intended purpose or are they the means to which they can increase their shareholders' or unitholders' returns?

The reliance on government subsidies is such that in the 2007 Financial Report of Macquarie Capital Alliance Group (the parent of operator Retirement Care Australia now known as Regis) noted that such reliance is a source of credit risk:

> "c) Credit risk
> At the group level, there are no significant considerations of credit risk. However subsidiaries of MCAL and MCAIL have concentrations of credit exposure as follows:

…

- A significant proportion of the day-to-day receipts of RCAH (Retirement Care of Australia Holdings) and its controlled entities are sourced from the Commonwealth Government."[17]

Later in the same document, MCAG's Financial Risk Management reiterated this risk for the group:

"b) Credit risk

At the group level, there are no significant considerations of credit risk. However certain subsidiaries have concentrations of credit exposure as follows:

- A significant proportion of the day-to-day receipts of Retirement Care Australia Holdings (RCAH) are sourced from the Commonwealth Government

…

"In each case, the creditworthiness of the counterparties mitigates the risk associated with the concentration of exposure to one counterparty.

"The Groups have policies in place to ensure that cash deposits are appropriately spread between counterparties with acceptable credit ratings."[18]

The above excerpts suggest that according to the risk management strategies of these new entrants, there is an amount of preparedness to face, if and when, such a risk crystallises.

As a two-tiered system has now evolved with the increased marketisation – and as even some argue, the commoditisation[19] – of the aged care sector, then surely a two-tiered system to the distribution of subsidies must now be established to best reflect the current commercial reality.

4. Comments supporting amendments in the proposed Bill and a Recommendation

Below contains our support to sections in this Bill that address issues of ownership and control. Additionally, we draw a recommendation based upon our comments developed in earlier sections regarding ownership transparency in the sector.

[17] p.43 in MCAG (2007) Financial Report, Macquarie Capital Alliance Group, Macquarie Bank
[18] Ibid., at p.86
[19] Paid Care Research Symposium, University of Sydney, 28th-29th November 2007

Item 7
Section 8-3A: Key Personnel
We support the addition of this item. Given the short-term investment horizon of some for-profit entities in recent years, this addition is an acknowledgement that who owns and controls the aged care entity is as equally important as those who run and manage them.

This addition will enhance the responsibility and governance arrangements when an entity may decide for purely investment reasons to enter the sector. This will encourage accountability and transparency in the ownership arrangements. This will also allow concerned stakeholders to assess those entities that highlight the attractiveness of government subsidies as the principal means in entering the sector are wont to forget that they are also responsible in providing high quality services to the residents and fair provision of working conditions to their staff.

Item 11
The additions to the section are welcome but there should be an inclusion that directly discourages opaque ownership arrangements.

It is significant to note that the notices of transfers of ownership of aged care entities that have occurred with publicly listed entities (such as the sale of the currently beleaguered Babcock and Brown's interests to LendLease[20] and Babcock and Brown's interests in Aevum to the Stockland group)[21] have been made through the Australian Stock Exchange as per their listing requirements.

A similar arrangement should be made where significant transfers of ownership must be publicly notified so stakeholders are aware of who the current owners are (see Table 2: Proposed Central Public Register).

Items 113 and 114
We support the reasoning behind these two items and the addition of Section 63-1C in the latter.

Option B
We support Option B which is to amend the regulatory framework. Option B acknowledges that the aged care industry is not stagnant and the amendments will better reflect the brave new world and aspects of the market reality of the sector. Greater transparency brings greater accountability to owners, and greater responsibility to all stakeholders.

---

[20] LendLease (2008) Stock Exchange Announcement: Lend Lease to invest in and manage leading listed retirement player, 1 October
[21] Stockland Group (2008) ASX Release: Stockland acquires strategic stake in Aevum, 13 October

Recommendation: Central Public Register of Owners of Aged Care Entities
The lack of publicly available information over ownership arrangements provokes uncertainty, distrust and questions over an owner's ultimate intentions. Item 11 will go some way to inform all stakeholders that owning an aged care home is a serious managerial and financial investment and should be treated as such; and that entering this sector is not a whim where government subsidies[22], prime real estate land[23], and solid, stable financial returns[24] are the only consideration of potential investors.

To complement Items 7, 11, 113 and 114 we propose that a central public register be established listing owners and managers of aged care entities. This should be made widely available online and this will provide a central point where ownership transactions can be analysed and publicised. The register should be structured to make available information on small, medium and large sized entities. Accumulated ownership transactions (including related entities) should be recorded and categorised by value ($) and size ('000s). This will address the information asymmetry on providers.

Below is a proposal of what a tentative register would contain and the data that it ought to have:

Table 2: Data in the proposed register

Size	Value	Ownership status	Owner	Manager	Date of Transaction
* List of nursing homes * How many homes involved * Geographic area	Small: <$1M Medium $1M-$50M Large: >$50M	Non-profit (commercial vs non-commercial); for-profit (listed, unlisted, private equity etc.)	Name of owners; executive officers of corporate bodies and related entities.	If the owner is not the manager.	This would contain the dates of entrance and exit of entities.

[22] According to Macquarie Bank, around 70% of its operating come is from the Commonwealth Government (limited number of aged care bed licences on issue). Source: MCAG RCA Regis Merger (2007) Aged Care Funding Review, May 2007, Powerpoint presentation.

[23] "One of the facilities acquired [by MCAG] was the Salvation Army Aged Care and Nursing Home and Hostel in the highly sort after residential suburb of Nedlands close to the Perth CBD and on the Swan River. Already the residents of a dementia hostel on the site, which was partly built with Commonwealth money have been told that they will have to move to enable the company to demolish the hostel to make way for planned higher return redevelopment of the site." – WA Senator Glenn Sterle, ALP Senate Hansard (2007)

[24] According to AMP Capital their Principal Healthcare Group forms part of their Social Infrastructure Fund in their investment portfolio entitled the Infrastructure Equity Fund. The expected income yield is between 8-10% and expected returns are 11%pa (although this would be somewhat lower this year) with the risk being low. The minimum investment required to enter this fund is A$10M. Source: http://www.ampcapital.com.au/institutions/infrastructure/ief.asp *accessed 10 November 2008*

The proposed register would help address the issues of transparency and accountability and would assist stakeholders in understanding the structure of the sector and with whom responsibility and accountability ultimately rests. Once established, the register may evolve into a central location and include existing data on quality, compliance, and qualified staff-to-resident ratios.

We suggest the departmental website of the Department of Health and Ageing to be the register's natural home.

Entering the care sector instils a core social responsibility[25] that must be acknowledged by all entities, especially those who have at their disposal financial leverage that is not as easily available to non-for-profit entities.

It is oft-quoted (and attributed to the former Governor-General Sir William Deane) that as a society, we are ultimately judged by how we treat our most vulnerable. It would be a sad reflection on our liberal democracy if we cannot effectively look after our aged.

Yours faithfully,

Marie dela Rama
Melissa Edwards
Bronwen Dalton

[25] Dela Rama, Marie (2007) Private equity, subsidies and the care sector, 31 October, Brisbane Institute http://www.brisinst.org.au/past-issue-details.php?article_id=69