

Affinity Aged Care News

Impacts of a Change in Maximum Permissible Interest Rate

The first of July brought with it the usual indexation changes to rates and thresholds. It also brought a change to the Maximum Permissible Interest Rate (MPIR). On 1 July the MPIR was changed from 6.36% to 6.15% affecting new residents and those who move facilities.

While on the surface of it this would appear to have made daily payments cheaper, it is a case of “yes but no”. The “yes” is for the market price payers who elect to pay a Daily Accommodation Payment (DAP). Under the old MPIR a Refundable Accommodation Deposit (RAD) of \$500,000 would have an equivalent DAP of \$87.12 per day. Under the new MPIR the equivalent DAP is \$84.25 per day, a saving of \$2.87 per day or \$1,048 per year.

The “no” is for Low Means residents who elect to pay by Refundable Accommodation Contribution (RAC). You see a drop in the interest rate actually increases the value of the RAC – this may seem illogical or unfair but it’s true. *Let’s look at the calculation...*

If we have a resident who is a full pensioner with \$80,000 in assessable assets. Their Daily Accommodation Contribution (DAC) will be calculated at \$16.35 per day (being 17.5% of their assets above \$46,000). To convert their DAC to a RAC we get their DAC per year and divide it by the MPIR. Under the old MPIR this calculation would have converted \$16.35 per day to a RAC of \$93,833 – pretty difficult for someone with \$80,000 in assets to fund. But under the new MPIR the RAC is \$97,037 – even harder for some who still only has \$80,000 in assets.

The issue is compounded the higher the DAC. Let’s say we had a low means resident who was a full pensioner with \$150,000 in assets. Their DAC would be \$50 per day (being 17.5% of their assets above \$46,000). When we convert this to a RAC under the old MPIR we get a RAC of \$286,950 and under the new MPIR we get a RAC of \$296,748 – the change in the interest rate by only 0.21% has created a RAC that is almost \$10,000 higher.

Of course interest rates are always changing and there are plenty of experts out there who can tell you what they think will happen and why. Depending on who you listen to at the moment interest rates are going to stay the same or drop further. Let’s assume interest rates did drop, and with them the MPIR. If the MPIR dropped by 0.25% to 5.9% a DAC of \$16.35 per day would have an equivalent RAC of \$101,148 and a DAC of \$50 per day would have an equivalent RAC of \$309,322. So what can residents do?

Well they can’t change the MPIR, but they can seek advice and look at restructuring their assets and income. Simple strategies such as gifting and pre-paying funeral expenses can have a big impact on someone’s ability to afford care. Let’s take the resident with \$80,000 in assets and assume they gift \$10,000 and pre-pay their funeral expenses at a cost of \$15,000. Their DAC would reduce from \$16.35 per day to \$4.33 per day (a saving of \$12.02 per day or \$4,388 per year). Their equivalent RAC would drop from \$97,037 to just \$25,698.

Many Low Means residents will say they can’t afford to get financial advice but in our opinion, they can’t afford not to!

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- Many Low Means Residents will say they can’t afford to get financial advice but in our opinion, they can’t afford not to.

Keeping and Renting the Home

From 1 January next year, it is proposed that aged care residents who choose to keep and rent their former home will no longer be eligible for an exemption of the rent when calculating their cost of care. The change has been described as “improving the fairness and equity of aged care means testing arrangements for new residents” and is expected to increase the amount the government receives through means tested care fees by around \$26 million over 5 years.

How it works now

Under the current rules, people who pay towards the cost of their aged care accommodation by daily payment and rent their former home have their home exempt from the calculation of their pension and any rent received exempt from their pension and the calculation of their cost of care. All accommodation payments that are levied on a daily basis are eligible, these include post reform residents who are paying a Daily Accommodation Contribution (DAC) or a Daily Accommodation Payment (DAP) and pre reform residents who are paying a periodic payment or an accommodation charge.

It should be noted, that simply paying towards the cost of aged care accommodation on a daily basis is only one part of the criteria, they also need to rent the home for the exemption to apply. Of course the rent doesn't need to be commercial or at arms-length, it can be a notional rent paid by a grandchild, but rent does need to be paid.

How will the proposed rules work?

From 1 January 2016 people who enter aged care and rent their former home will have the rental income included in the calculation of their cost of aged care. The value of the home and the rent will continue to be exempt for the calculation of pension entitlement and people who are living in aged care prior to 1 January will not be affected by the change. For those currently considering moving into aged care, the timing of that move could have a significant impact on their cost of care if they wish to keep and rent their home.

Let's look at an example

Dorothy is 85 and currently lives at home with support from her family and a home care package. Dorothy's house is worth \$850,000, she has \$140,000 in the bank and \$10,000 in personal effects. Dorothy's husband built their house when he returned from the war and she doesn't want the home to be sold. Dorothy has had a few respite stays at an aged care facility close to her, she has formed a good relationship with a number of the staff and she has said that if she needs to go to aged care in the future this is where she would like to stay. The facility has a market price of \$400,000 RAD or \$67.40p.d DAP. Dorothy's children think she would get \$400p.w rent (net) from her home when she moves into aged care.

Dorothy moves into care prior to 1 January, paying \$90,000 towards her RAD.

Cost of Care-	Income-
Basic Daily Care Fee \$47.49 pd	Age Pension Entitlements \$22,365 pa
Daily Accommodation Payment \$52.23 pd	Rent from Home \$20,800 pa
Means Tested Care Fee \$4.12 pd	Interest @ 2.5% \$1,250 pa
Extra Out of Pocket Costs \$10 pd	Total Income \$44,415 per annum
Total \$41,552 per annum	Surplus Income \$2,863 per annum

Dorothy moves into care after 1 January, paying \$90,000 towards her RAD.

Cost of Care-	Income-
Basic Daily Care Fee \$47.49 pd	Age Pension Entitlements \$22,365 pa
Daily Accommodation Payment \$52.23 pd	Rent from Home \$20,800 pa
Means Tested Care Fee \$28.14 pd	Interest @ 2.5% \$1,250 pa
Extra Out of Pocket Costs \$10 pd	<u>Total Income \$44,415 per annum</u>
Total \$50,319 per annum	Deficit Income \$5,904 per annum

People who are considering moving into aged care should seek specialist advice. We would be happy to discuss the best way to fund aged care with any of your prospective residents.

Why Choose Affinity Aged Care?

Entry into aged care can be a challenging time for both the person and their family. The finances are notoriously complex with possible implications for:

- Keeping or selling the family home
- Aged care facility fees
- Centrelink Age Pension/DVA Pension entitlements
- Cash flow requirements
- Potential tax implications
- Intergenerational wealth transfer

Most financial planners have only a limited understanding of aged care financial advice. Even most advisers find it overwhelming! It is very much a 'niche' that demands specialist attention and hands on experience. Affinity Aged Care Financial Advisers are your aged care financial specialists. Your loved one's aged care needs are the sole focus of our advice process.

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