



Australian Government
Productivity Commission

Housing Decisions
of Older Australians

Productivity Commission
Research Paper

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The Productivity Commission

The Productivity Commission is the Australian Government's independent research and advisory body on a range of economic, social and environmental issues affecting the welfare of Australians. Its role, expressed most simply, is to help governments make better policies, in the long term interest of the Australian community.

The Commission's independence is underpinned by an Act of Parliament. Its processes and outputs are open to public scrutiny and are driven by concern for the wellbeing of the community as a whole.

Further information on the Productivity Commission can be obtained from the Commission's website (www.pc.gov.au).

Foreword

The Commission's flagship research paper *An Ageing Australia: Preparing for the Future* identified that many older Australians are asset rich but income poor, and flagged challenges for government budgets stemming from the ageing of Australia's population. In its second flagship research paper, *Housing Assistance and Employment in Australia*, the Commission investigated the link between housing decisions and government assistance.

This, the third flagship research paper, continues the investigation of issues relating to the ageing of Australia's population, this time focusing on the housing choices made by older Australians. It considers available statistical evidence on the financial and accommodation aspects of housing decisions and draws out some of the policy issues affecting the wellbeing of older Australians and the broader community. The report examines the policies affecting the supply and cost of residential aged care and other age-specific housing, the influence of the tax and transfer system on housing decisions, and the issues in using home equity release to support living standards in retirement. In reaching its conclusions, the Commission drew on evidence from a survey of older Australians conducted on its behalf.

Along with *Superannuation Policy for Post-Retirement*, these reports should support informed discussion and policy formulation to enhance national welfare in an environment of an ageing Australian population.

This paper was produced by a team led by Mary Cavar, and included Catherine Bain, Roger Hassan, Lisa Leong, Evelyn Lesh, Alex Maevsky, Greg Thompson and Miriam Veisman-Apter. It was overseen by Commissioners Karen Chester and Ken Baxter.

Peter Harris

Chair

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This project utilised data from a number of collections of the Australian Bureau of Statistics (ABS), including confidentialised unit record data, as well as data from the Household, Income and Labour Dynamics in Australia (HILDA) survey. The HILDA project was initiated and is funded by the Department of Social Services, and is managed by the Melbourne Institute of Applied Economic and Social Research (Melbourne Institute).

The conclusions and views reached by the Commission on the basis of these data are those of the Productivity Commission. They should not be attributed to the Department of Social Services or the Melbourne Institute.

Abbreviations

ABS	Australian Bureau of Statistics
ACAT	Aged Care Assessment Team
ACFA	Aged Care Financing Authority
ACOSS	Australian Council of Social Service
AIHW	Australian Institute of Health and Welfare
APRA	Australian Prudential Regulation Authority
ASFA	Association of Superannuation Funds of Australia
ASIC	Australian Securities and Investments Commission
CACP	Community Aged Care Packages
CDC	Consumer directed care
CGT	Capital gains tax
CHSP	Commonwealth Home Support Programme
COAG	Council of Australian Governments
COTA	Council on the Ageing
CRA	Commonwealth Rent Assistance
CURF	Confidentialised Unit Record File
DAP	Daily accommodation payment
DMF	Deferred management fee
DSS	Department of Social Services
DVA	Department of Veterans' Affairs
EACH	Extended Aged Care at Home
EACH-D	Extended Aged Care at Home — Dementia
ERP	Equity release product
GDP	Gross domestic product
HACC	Home and Community Care
HCP	Home Care Package
HILDA	Household, Income and Labour Dynamics in Australia Survey

LVR	Loan to value ratio
MHE	Manufactured home estate
NNEG	No Negative Equity Guarantee
OECD	Organisation for Economic Cooperation and Development
PC	Productivity Commission
PLS	Pension Loans Scheme
RAD	Refundable accommodation deposit
RTO	Registered training organisation
SEQUAL	Senior Australians Equity Release Association of Lenders
SIH	Survey of Income and Housing
VET	Vocational education and training

OVERVIEW

Key points

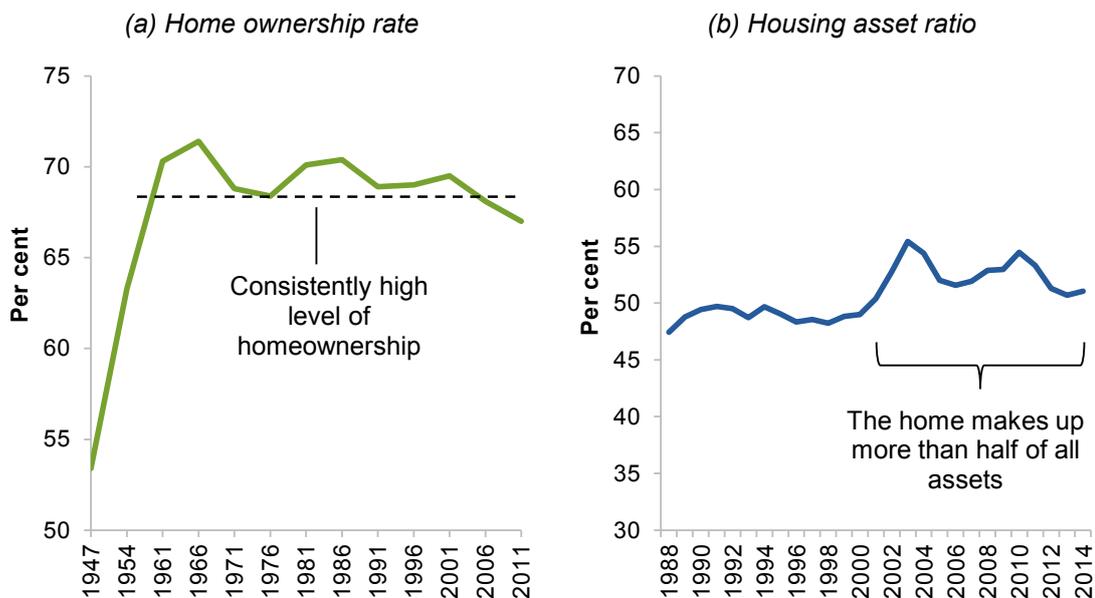
- Housing is integral to people's wellbeing, particularly for older Australians. For many older people home ownership provides security and independence in retirement.
- Older Australians strongly prefer to age in place. Most people are happy staying in their family home, despite a common perception that such homes are too big for them.
- For others, age-specific housing options provide more integrated accommodation and care, offer a way to release home equity, and may delay entry into residential aged care. Growth in retirement villages and manufactured home estates has been strong, despite planning restrictions.
- About 15 per cent of older Australians are renters, and these people are generally a highly vulnerable and economically disadvantaged group.
- There is a general lack of affordable downsizing options for older Australians, due in large part to the red tape and inconsistencies within state and territory land planning regimes.
- Residential aged care is effectively transforming into an end of life care service. The age of admission is increasing (now 83 years on average), average tenure is about 2 to 3 years, and care needs are higher.
- Many older people are reluctant to plan or get advice for possible future care and end of life needs. Decisions can be prompted by crises, and made when the person is vulnerable.
- There are positive signs from the recent reforms in aged care, including improved financial viability, transparency, and consumer sovereignty. However, further reform is needed.
- About 800 000 older Australians receive home care. Older people's desire to age in place aligns with governments' fiscal goals — in most cases, assistance for home care is considerably less costly than for residential aged care. Nevertheless, there may be merit in increasing co-contributions for both home and residential aged care.
- Most of older Australians' wealth is in the family home, but it remains an untapped source of retirement income. Many older Australians, including some of the poorest retirees, continue to save (spending less than their Age Pension) even very late in life. The main reasons for such behaviour are precautionary saving and a strong aversion to debt in old age.
 - This precautionary saving is driven by uncertainty around longevity, health and residential aged care needs, and is a potentially expensive form of 'self-insurance' that can lower living standards in old age.
- Most older Australian home owners on low incomes could achieve a modest retirement living standard over the remainder of their lives by drawing on their home equity.
- Financial equity release products could facilitate withdrawal of home equity to fund retirement needs. However, this market is small and unlikely to grow in the near term:
 - Most providers are diffident due to small market size and the risk of reputational damage.
 - Broader reluctance by older people to tap into home wealth and strong aversion to debt, coupled with the high cost of such products are impeding demand. The tax and transfer treatment of the family home further reinforces this.

Overview

Housing forms a large part of the Australian economy and is an integral part of people’s wellbeing. In addition to serving a basic human need for physical shelter, contributing to physical and psychological health and emotional security, it is a key determinant of people’s wealth and financial security in old age. Residential land and dwellings account for more than half of total household assets, two-thirds of Australian households are home owners, and for most people the family home is the single largest source of wealth (figure 1). The dual nature of housing — being an essential part of everyday *consumption* as well as a major *investment* asset — means that housing decisions bring up policy issues that span many aspects of wellbeing.

The growing longevity and ageing of Australia’s population, as well as other structural and demographic changes, elevate the policy imperative to understand what drives the housing decisions of older people and the consequences for their wellbeing. This study aims to explore the drivers of those decisions, as well as some of the barriers to better outcomes. It provides important information to inform likely future public policy discussion.

Figure 1 **Importance of home ownership in the Australian economy**



Source: Productivity Commission estimates based on ABS data and Kryger (2009).

In undertaking this study, the Commission commissioned a survey of older Australians to better understand the motivations for their housing decisions (box 1). The Commission also undertook quantitative analysis to explore two areas that have been the subject of some recent public comment:

- the scope to increase living standards of older Australians through accessing the equity in the family home to supplement their retirement incomes
- the effect on Age Pension eligibility if some value of the family home were integrated into the Age Pension assets test.

Box 1 Commission's survey of older Australians

In the course of this project, the Commission identified a paucity of recent data on the behavioural drivers of specific decisions relevant to the study. Previous surveys did not address some of the issues directly, and often tended to focus on a particular aspect of housing decisions (either the accommodation dimension, or the investment and financial dimension), rather than providing a comprehensive survey-based examination of the factors. The Commission engaged RFI Group to conduct a survey that addressed this gap in the evidence.

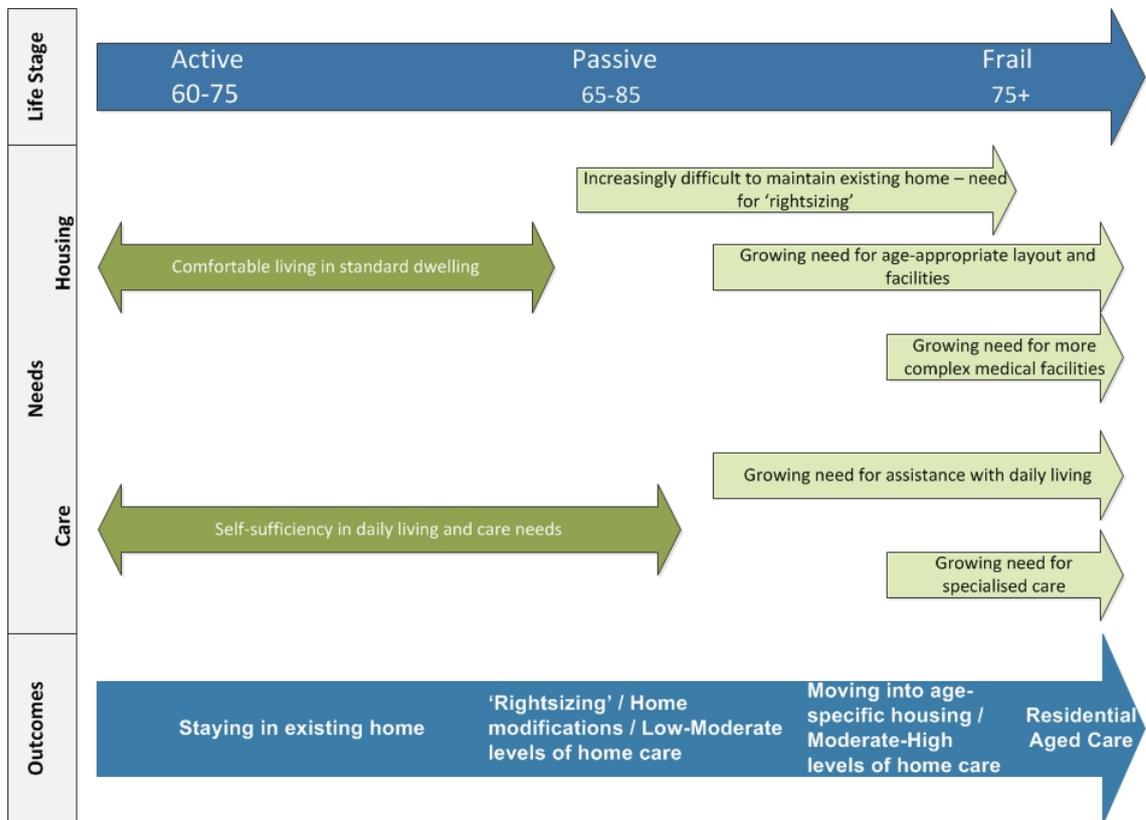
The survey questionnaire covered older people's attitudes and views on a range of housing and retirement issues, including: planning for retirement; attitudes towards the family home, debt, and bequests; downsizing; housing preferences; and awareness of, and attitudes towards, home equity release products. The survey was conducted online in September 2015, and involved about 1500 Australians aged 60 years and over. It was designed to be representative of the Australian population in terms of age, gender and location. Subsequent analysis of survey responses also indicates that the survey is broadly representative of the distribution of older Australians by socio-economic background.

The survey questionnaire and full results are available online.

Accommodation choices of older Australians

Housing plays a particularly important role for the growing population of older Australians. Older Australians are more likely to own their home than younger people, and their living standards become more dependent on the nature and quality of their accommodation as they age. The quality and location of housing can influence physical and psychological health and social engagement. People can also develop a personal attachment to their family home, and perceive it as a source of memories, security and comfort in old age. The role played by housing and its desirable characteristics change as a person ages, progressing through the active, passive and frail stages of retirement (figure 2).

Figure 2 Housing and care needs — a simple schema

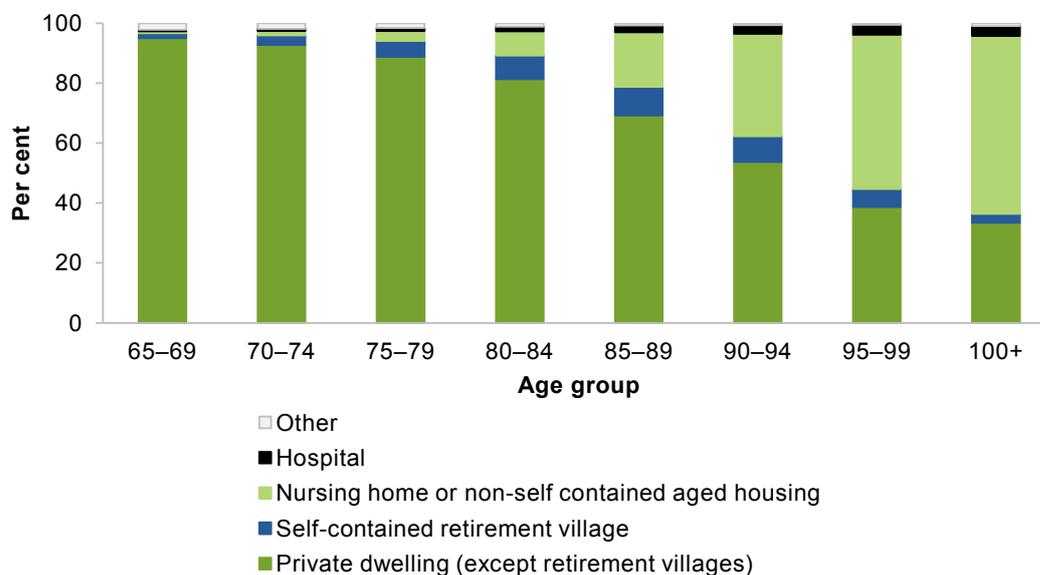


Older people prefer to ‘age in place’

The survey data and other evidence of older people’s housing decisions unambiguously reveal that the majority of older people prefer to ‘age in place’. This does not necessarily mean never leaving the family home, although housing mobility does decline in old age. For many older people the ‘rubber band’ attaching them to the family home is the desire to remain in the local community. The preference to age in place is not unique to Australia — the phenomenon has been noted in other countries, such as New Zealand, United States and the European Union.

The vast majority of older Australians are living in private dwellings, and about 80 per cent own their home. Most people that make the move to age-specific housing are forced to do so by declining health, but this consideration does not factor prominently until very late in their lives. For all age groups up to the age of 90, mainstream housing is the dominant form of accommodation (figure 3).

Figure 3 Older people in private and non-private dwellings, 2011



Source: ABS (Census of Population and Housing, 2011).

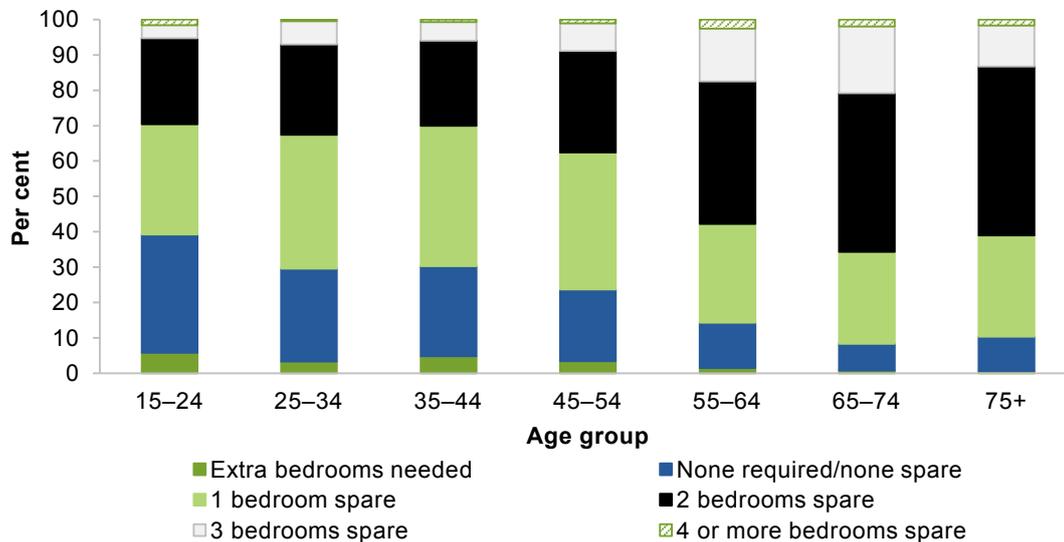
The capacity of a person to age in place — and their quality of life if they do — can be affected by the appropriateness of the family home to their changing needs, the scope for home modification, the availability and cost of home care, or the availability of suitable alternative accommodation within the local community. For some people, their care and accommodation needs may be better addressed by accessing *age-specific* housing options, such as a retirement village, mobile home community, or ultimately residential aged care.

Small households, big houses — not necessarily a problem

A common presumption is that older people are living in houses that are too big for them. About three-quarters of those aged over 75 live in detached houses and a similar proportion have residences with three or more bedrooms. Measures of housing occupancy indicate substantial spare capacity (figure 4).

However, surveys show that the majority of older people are satisfied with their dwellings and often find other uses for spare rooms, such as to accommodate guests or for hobbies. Moreover, detached houses are generally easier to modify to address the changing needs of older occupants. More broadly, measures of housing utilisation are a poor indicator of what people actually want. More sophisticated studies show that a large number of bedrooms in the house is less of a concern for older people than the design and layout of the house, or the size of the garden.

Figure 4 **Housing capacity utilisation for different age groups (2011-12)**



Source: ABS (Survey of Income and Housing, 2011-12).

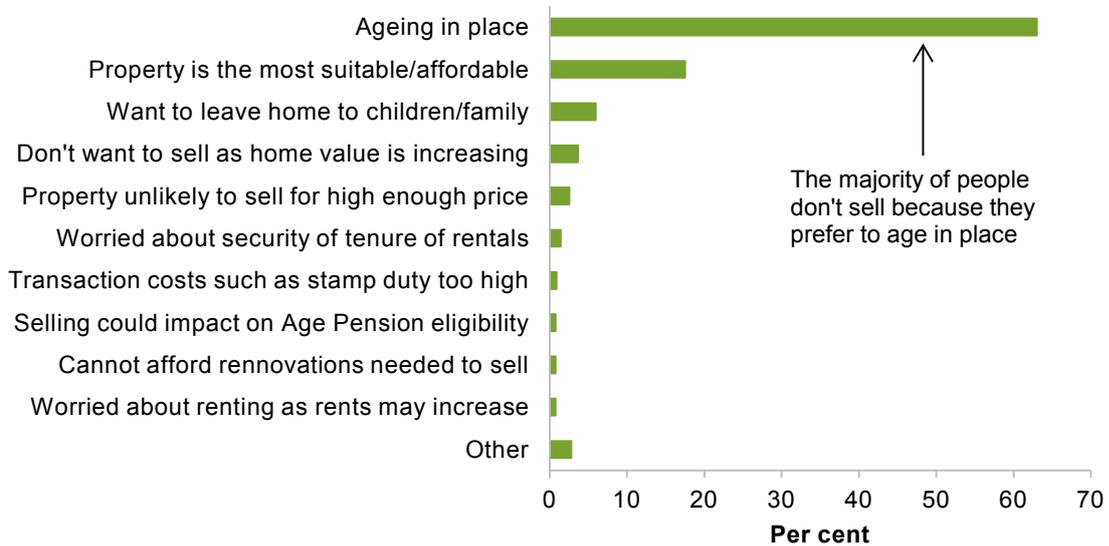
Most older Australians will not downsize during their retirement

Downsizing is often presented as a win-win for older people who struggle to maintain their property and also wish to release some equity to supplement their income. However, this remains a relatively uncommon path for older Australians. According to the Commission's survey, about one in five older Australians have sold their property and purchased a less expensive home since turning 50, and about 5 per cent have sold and moved to renting. Of the older home owners that have not moved yet, about 15 per cent had strong intentions to do so at some point in the future. The primary reasons for not selling the family home are a very strong desire to age in place and the lack of suitable downsizing options (figure 5).

When people do downsize it tends to happen relatively early in retirement — over 85 per cent of older Australians who downsize do so before they turn 70. The key motivations for moving from the family home are linked to securing more age-appropriate accommodation, either in terms of size and characteristics, or location.

Only about one-sixth of those who downsized (representing under 4 per cent of older Australian home owners) did it primarily to release housing wealth. Moreover, financial considerations may sometimes be a barrier to downsizing. Downsizing does not mean 'down valuing' — single storey homes can cost more than double storey family homes, as can the properties with age-appropriate modifications. Furthermore, selling a house and securing alternative accommodation can involve substantial transaction costs.

Figure 5 Reasons for older Australians not selling the family home^a



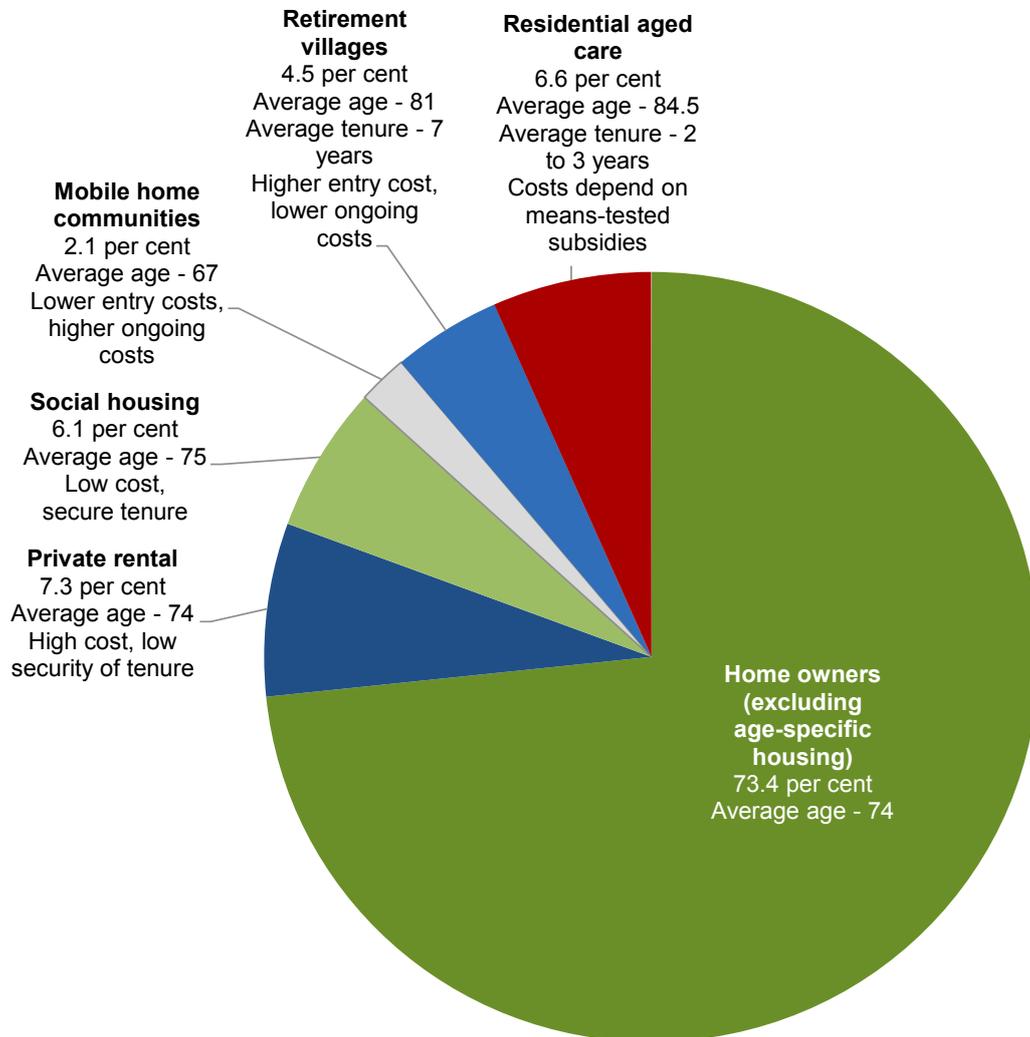
^a The category for 'Ageing in place' groups three possible answers including those who wanted to stay in their home as long as possible, those who had an emotional attachment to the property, and those who liked or were familiar with their property's location.

Source: Commission survey.

Older renters are a significant and vulnerable minority

A small but significant minority (close to 15 per cent) of older Australian households are renters rather than home owners. Older people are also more reliant on public housing than younger renting households — about half of renters older than 75 are renting publicly (figure 6).

Figure 6 The form and tenure of older people's accommodation, 2011

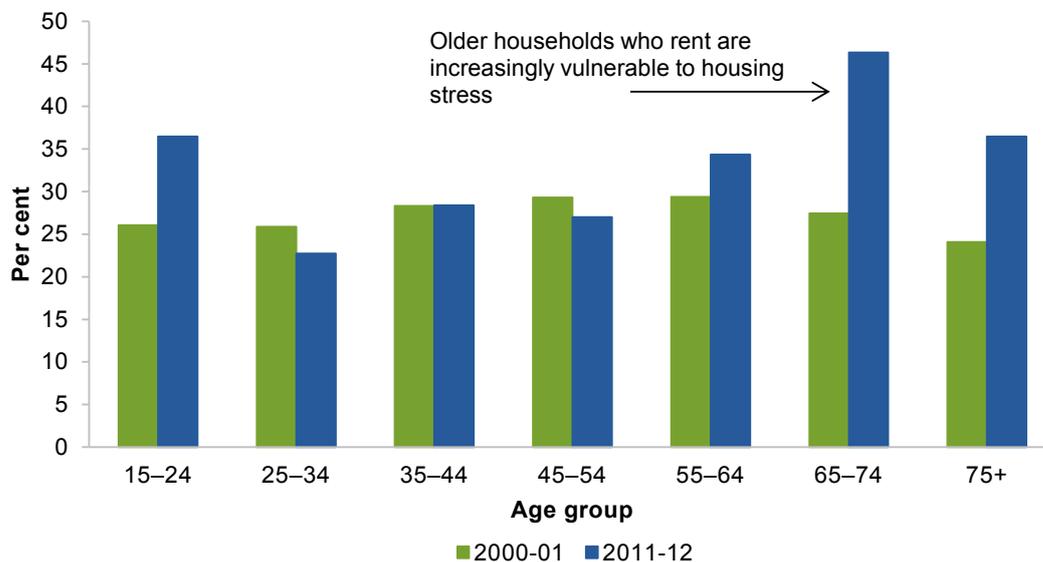


Source: Productivity Commission estimates based on ABS and HILDA data.

Renting in older age is associated with a number of potential risks, including poverty, homelessness and adverse impacts upon mental health and wellbeing. Although older people who receive the Age Pension are eligible for Commonwealth Rent Assistance, several recent reviews¹ found that the payment was too low. Housing affordability stress is common, and over the past decade it has grown substantially among older renters (figure 7). In addition, older people as a group are likely to be disproportionately affected by the insecurity of tenure inherent in private rental. For most older Australians who rent, it is a necessity rather than a desirable choice of tenure. There is merit in a dedicated review of Commonwealth Rent Assistance to ensure that some of the most disadvantaged members of the Australian community receive adequate housing support.

¹ For example, the Henry Review and a 2015 review by the Reference Group on Welfare Reform.

Figure 7 Renters — incidence of housing affordability stress^a



^a Defined as a situation where housing costs exceed 30 per cent of gross household income.

Sources: ABS (Survey of Income and Housing Costs, 2000-01; Survey of Income and Housing, 2011-12).

Social housing could provide a lower cost and secure tenure option to older people who are forced to rent. However, the supply of social housing has been static, while demand and waiting lists have increased. Growing residualisation² of this housing option means that inadequate supply is affecting some of the most vulnerable older people.

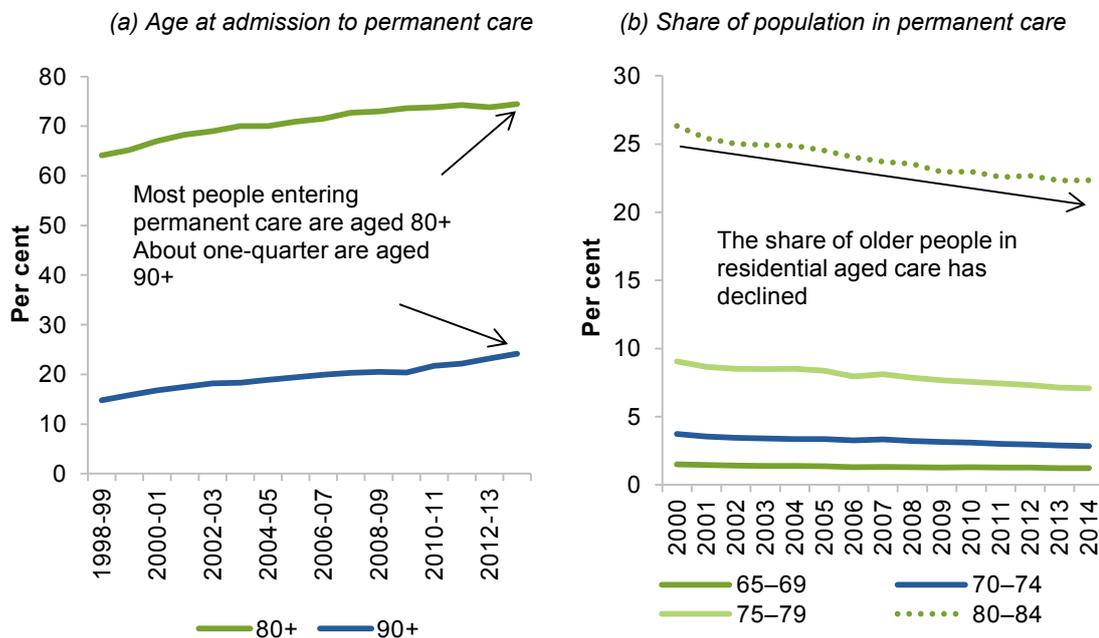
The disadvantages faced by older renters are particularly pertinent to older Indigenous Australians, who are much more likely to be renting than non-Indigenous older Australians. Nearly half of Indigenous Australians aged over 55 are renting, and older Indigenous Australians are also far more likely to be in public housing than other older people.

Residential aged care is transforming into an end of life option

The age of admission into residential aged care is increasing with an average age today of 83 (figure 8), because of delayed morbidity, greater prevalence of couple households in older age, and people’s preference to delay or avoid entry into residential care. For those in residential care, care needs tend to be higher and average duration of stay was last measured at about 2 to 3 years. Anecdotal reports suggest that average tenure may have decreased further since then. Residential aged care is effectively transforming into an end of life care service.

² Residualisation is the tendency for a particular housing option to become increasingly the preserve of the most disadvantaged.

Figure 8 Trends in residential aged care use



Source: Productivity Commission estimates based on AIHW data.

The strong preference of older people to age in place and delay entry into residential aged care is a driver for growing integration of accommodation and aged care services in the housing options that precede residential aged care. There is a growing demand for home care and modifications to prolong the stay in the family home. Retirement village operators are expanding their care and health services and increasingly co-locating with residential aged care facilities.

It is likely that the trend for integration of accommodation and aged care services will continue and any policy barriers impeding this evolution of the market will impose increasing costs on older Australians.

Housing as a store of wealth — theory and practice

Simple life-cycle theories predict that a person would provide for their retirement by saving (and investing) some of their income during their working life and then use that wealth to fund their lifestyle in old age. As a durable good and a source of wealth, housing is one of the three potential sources of income in retirement, along with the Age Pension and private savings (including superannuation).

There are several mechanisms for drawing on housing wealth in old age, including:

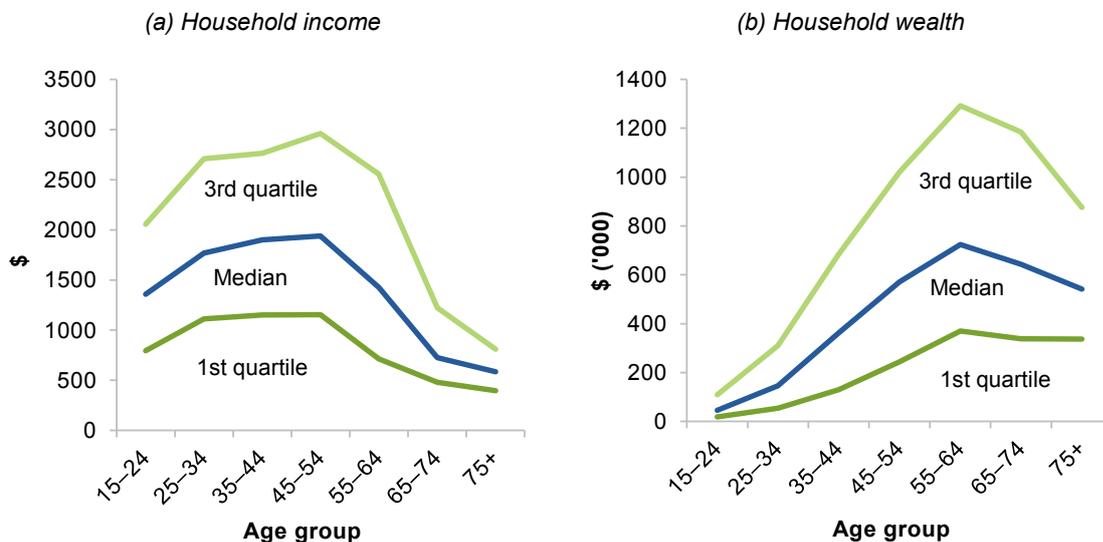
- selling the home either in whole or part
- renting out the home
- drawing down equity using a financial equity release product.

Given the importance of housing in the overall wealth of Australians, it is reasonable to expect it to play a prominent role in funding retirement. However, the evidence paints a more complicated picture.

Older Australians are asset rich and income poor...

Older Australians today are both wealthier than their younger counterparts and past generations of older people. About 80 per cent of them are home owners who benefited from significant growth in house prices, particularly in the nation's capital cities — about 5.5 per cent per year on average over the past decade. However, the vast majority of retirees have low incomes and rely substantially on the Age Pension (figure 9).

Figure 9 **Distribution of household income and wealth**



Source: ABS (Survey of Income and Housing, Australia, 2011-12).

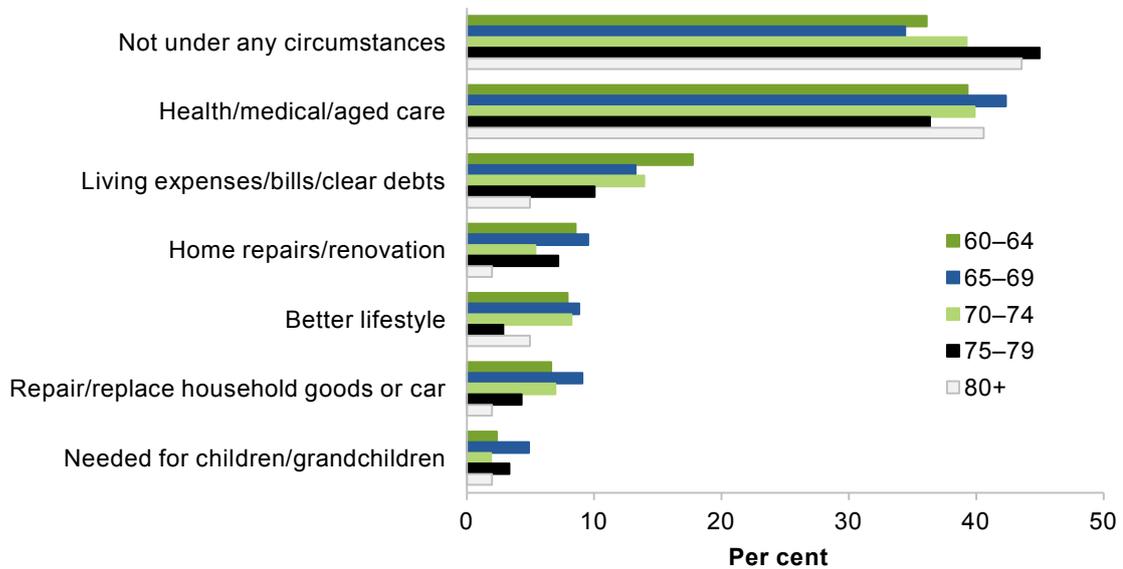
...and yet continue saving in old age

Surveys show that when older Australians are transitioning into retirement and a lower income, they are more likely to cut expenditure than draw down their wealth. Consumption typically declines in old age. In part, this is a consequence of declining health and growing

frailty — as people age, they tend to reduce their overall consumption, but increase their consumption of public health services.

The tendency to spend less than their pension and to accumulate assets is particularly common among the oldest and poorest retirees. A longitudinal study of age pensioners found that the wealthiest pensioners tended to draw down their wealth early in retirement but reversed this trend later in life, whereas those with the least assets tended to grow their wealth (by being net savers) throughout retirement. Moreover, when households eventually do draw on their wealth, home equity is typically accessed as a last resort (figure 10). For most older home owners, the family home is a major source of growing wealth throughout retirement.

Figure 10 Older people are reluctant to draw on their home equity



Source: Commission survey.

Several factors are behind these outcomes, in particular the intrinsic preferences of older people, such as their:

- desire to leave a bequest, albeit less so than in the past
- precautionary saving to ‘self-insure’ for unexpected future health or aged care needs.

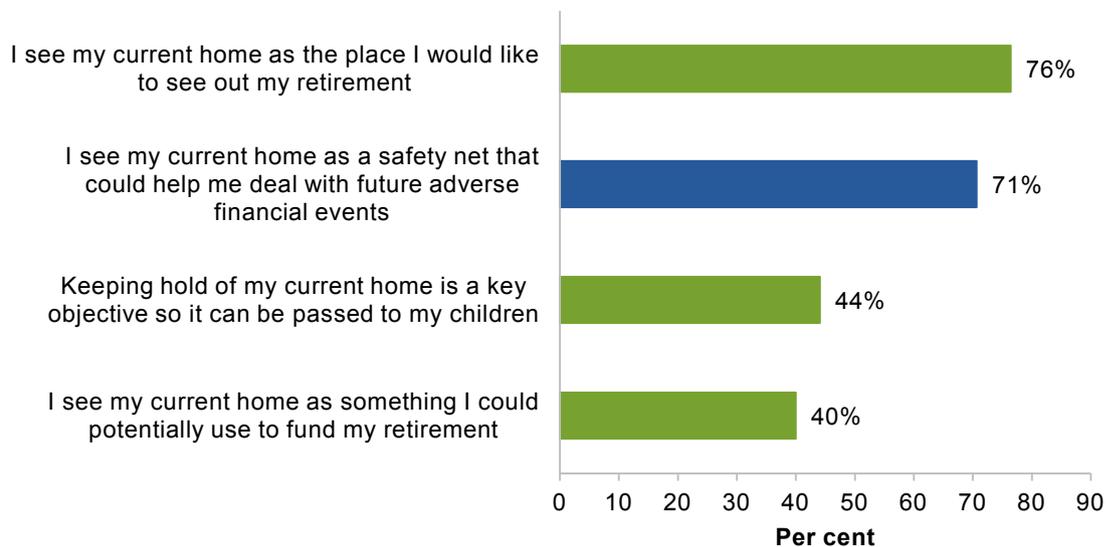
A problem of over-saving and unintended bequests?

Recent surveys suggest that most older people are more concerned about meeting their own financial needs, than about passing on wealth to their children. Key financial concerns of older people are outliving their savings, inflation eroding the standard of living, and paying for health and care costs. Surveys also indicate that bequests are a less important

motivator for more recent retirees than for previous generations of older Australians. Nonetheless, while the data on bequests are patchy, they show that the value of bequests is substantial. Bequest sizes have grown somewhat recently, albeit less rapidly than house values.

It is difficult to discern what proportion of bequests are an unintended consequence of over-saving to fund future and uncertain financial needs. A longitudinal study of pensioners found most leave as bequests a high proportion of their initial wealth because they maintain a ‘buffer’ stock of savings. And survey evidence indicates that precautionary saving is a key driver of decisions by older Australians, with the family home playing a leading role in this context (figure 11).

Figure 11 Perceptions of the role of the family home in retirement^a



^a Percentage of respondents agreeing with the statement.

Source: Commission survey.

There is nothing wrong with precautionary saving per se — it is not irrational for people to be risk averse and to seek financial security by maintaining a financial buffer in old age. However, the wellbeing of older Australians can be compromised, and relative living standards can be lower than necessary, if such decisions are not based on a rational assessment underpinned by sound information.

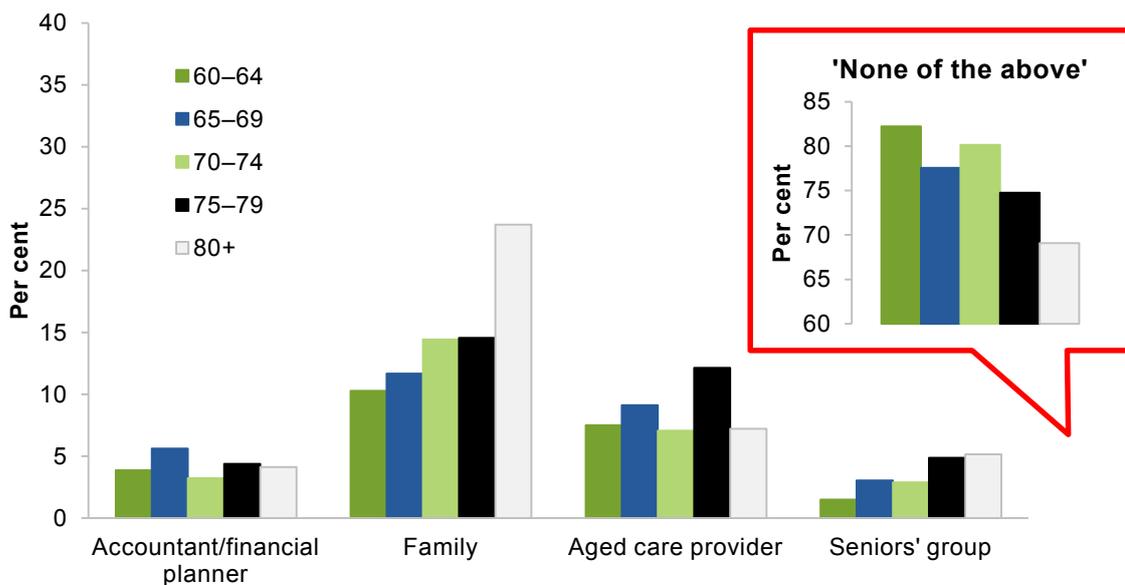
Decisions are not always well-planned or informed

There is some evidence that cognitive constraints and imperfect information are affecting financial planning of older Australians. Many people are reluctant to plan for their possible

future ill health and end of life needs. However, this creates a risk of decisions being prompted by crises, rushed and made at a time when the person is vulnerable.

Even where this aversion to planning is overcome, long-term decisions are inherently very complex. The Commission’s survey of older Australians found that about one-third are uncomfortable with their own financial planning for retirement. Surveys also show that some people have poor knowledge about key aspects of retirement decisions, such as their expected longevity, the likelihood and cost of going into residential aged care, and the operation of various government policies. These uncertainties collectively can mean that holding on to the family home can become an expensive form of self-insurance. There is also a reluctance to engage financial and other specialist advice or even speak to family members to inform decisions (figure 12).

Figure 12 **Where do older people seek advice on funding aged care costs?**



Source: Commission survey.

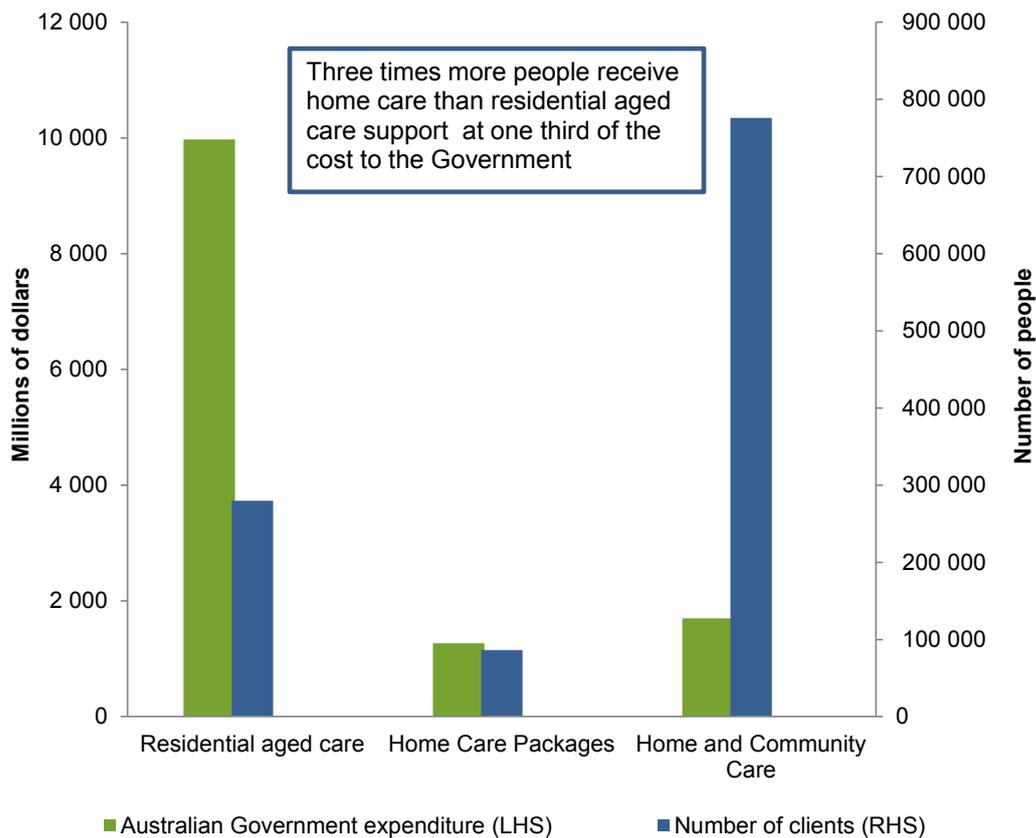
Housing and aged care policies — some scope for reform

Ageing in place should be supported – a case of aligned interests

There are strong grounds for ensuring that policies do not impede ageing in place. This is the preferred option for the vast majority of older people and the number of older people in private dwellings is likely to grow as the population ages. Furthermore, to the extent that ageing in place substitutes for other accommodation and care options that receive a greater

government subsidy, it may also be aligned with the governments' fiscal sustainability objectives. Although the care needs are typically higher for residential aged care, ultimately delivering home care requires much less public funding (figure 13).

Figure 13 **Aged care clients and costs to government**



Source: SCRGSP (2015).

Importantly, this should not translate to ‘blank cheque’ policy for home care support across the board, particularly for lower levels of home care, where it is unlikely to be a substitute for entry into residential aged care. There is scope to improve the means test for home care (discussed later) and to increase the level of co-contributions overall.

Policy focus is increasingly and appropriately shifting from residential aged care, to supporting older people to live independently in the community. The Australian Government has been increasing the provision of home care services, with about 800 000 older Australians receiving some form of home care, while reducing the number of new residential aged care places. The introduction of ‘consumer directed care’ will give consumers greater choice and flexibility in addressing their home care needs. There are plans for further reform of consumer directed care by moving away from regional rationing and linking the packages directly to consumers. Importantly, these changes are likely to

promote further competition and innovation in the sector, given the home care sector is fragmented with a large number of small, mostly not-for-profit, providers.³

A recent evaluation of the reforms implemented in the delivery of home care has found that both providers and consumers require more information and support in the transition to consumer directed care. As providers are adjusting to consumer directed care, they have reported substantial administrative burdens, which affected the cost of service delivery. The Australian Government should ensure that home support is delivered efficiently and in a timely manner, and that better information and support are available to facilitate reform implementation.

Age-specific housing options could be better integrated

The goal of policy should be to ensure that older Australians can transition along the spectrum of aged care and accommodation needs as simply and cost effectively as possible. Some policies appear to be limiting the flexibility of age-specific housing, particularly retirement villages, to address the preferences and needs of older Australians.

Retirement villages wishing to provide aged care services face significant and disparate regulatory red tape. This spans all levels of government, including local government requirements (such as the need for development approvals) and the regulations covering aged care supply, such as the accreditation and approvals of the providers and the allocation of bed licences.

The structure of fees charged by retirement villages is very complex, and can vary within and across villages and over time. While state government regulations aim to protect consumers through restrictions on operators' business models and extensive disclosure requirements, consumers still find it difficult to compare the affordability of different villages. This may create uncertainty and confusion for prospective and existing residents. The consequences for consumers of making the wrong decision are exacerbated by high exit costs. Providers have also argued that prescriptive regulations around the structure of their fees are inhibiting the flexibility of the industry.

There are also issues with the allocation of government support across the age-specific housing options. Currently, Commonwealth Rent Assistance applies to manufactured homes but does not for most retirement village units, even where the accommodation services and target demographic are similar. This appears inequitable to both suppliers and consumers and can also distort accommodation choices.

³ For example, there are currently about 500 operators providing 66 000 home care packages across Australia.

Planning and development approvals are a problem across the board

As with many other industries, state and local planning systems create barriers to expansion and innovation in both mainstream and age-specific housing. There are only a limited number of statewide planning policies that deal with housing for older Australians as a systemic issue, and local government implementation can also be significantly improved.

Operators of retirement villages and aged care services reported significant red tape in dealing with planning and development approvals, both for new facilities and for modification and redevelopment of existing outdated stock. Age-specific housing development is often disadvantaged relative to other housing or commercial development. Planning rules that constrain the development of smaller, higher density residential properties inhibit downsizing, and innovative housing proposals often face NIMBY opposition. The desire of most older people to age in place strongly signals a need for revision of state and local government planning regimes, to reduce the barriers to the supply of new housing options. Reforms in this area could potentially deliver the greatest gains in affordability and diversity of housing options for older Australians.

Reform in residential aged care needs to continue

There have been some positive changes

A number of reforms to residential aged care have commenced since the Commission's 2011 *Caring for Older Australians* inquiry. The most fundamental reform was to clearly separate accommodation and care costs and payments. Other welcome changes include public disclosure of residential accommodation prices and providing customers greater freedom to choose their preferred accommodation payment method. These are expected to increase transparency and flexibility.

It will take some time to ascertain the longer-term impact of these reforms on the wellbeing of older Australians and on overall efficiency. However, there are some positive early signs. The residential aged care sector appears in better financial shape than a couple of years ago, principally because of the reform governing the choice of accommodation payment method.

But some problems remain

A number of important recommendations from the Commission's 2011 inquiry have not been adopted. In particular, consumer directed care reform has not extended to residential aged care. There are also still tight and inflexible controls on the supply of residential aged care places. Supply is determined through regional aged care provision ratios based on projections of people older than 70 and the number of existing beds. The current arrangements are intended to provide for equitable access to services and to manage the

Commonwealth's fiscal risk. However, they also restrict competition, protect legacy and ill-suited stock, reduce incentives for innovation, and restrict the capacity of the supply side to respond to structural and demographic changes in demand (for example, through transferring or trading places between providers).

Some form of rationing of government support for both home and residential aged care is still necessary, given the high embedded subsidy and governments' fiscal constraints, but the form and extent of it can clearly be improved. The main rationing mechanism should be on the demand side, where prospective aged care recipients undergo an extensive needs assessment to establish eligibility and level of service they will receive. In this context, the supply side restrictions (namely, bed licensing) are redundant and are not meeting the requirements of older Australians needing to enter residential aged care.

Communication about current arrangements can be improved

A natural consequence of reforms that give older people greater control and choice over their accommodation and aged care is increased complexity for consumers. Stakeholders have argued that reform consultation and information provision to date has focused more on the provider than the consumer. The Commission's survey indicates low awareness of reforms among older Australians. This has affected implementation of the reforms and impeded the capacity of older Australians to make informed decisions about their care.

Nevertheless, information provision and overall transparency for consumers is improving. The Australian Government has introduced the MyAgedCare website, phone and personal contact support service to provide information on accommodation and aged care options and policy arrangements, as well as on other relevant issues, such as financial equity release products. This service is a work in progress, but is a step in the right direction. Some seniors' advocacy groups are also stepping in to fill the gap.

Tax and transfer policies and housing

At the Australian Government level, owner-occupied housing enjoys favourable treatment on both the taxation and transfer sides of the budget. The principal home is exempt from the means tests for the Age Pension. It is also exempt from capital gains taxes that apply to the sale of many other assets. There is also a range of government support arrangements for other forms of accommodation and aged care, for which the means tests treat owner occupied housing favourably, or exclude it altogether. On the other hand, at the state and territory governments level, conveyances of residential property are subject to stamp duties. The complex interplay of these policies can distort housing decisions and lead to inequitable outcomes.

Stamp duties are an inefficient tax on housing mobility

All states and territories levy stamp duties on the sale value of residential properties. These taxes are simple to administer, but ultimately are a distortionary tax on residential mobility. For older Australians, they are a potential impediment to moving out of their family home and into a residence that better meets their needs. Nevertheless, surveys indicate that stamp duties are a relatively minor determinant of residential mobility of older Australians, when compared to the barriers to the supply of suitable and affordable housing, and the strong over-riding preference of many older people to avoid moving unless absolutely necessary.

Multiple reviews have recommended the abolition of stamp duties, and there is a strong case to do so in principle. The lost revenue from this change could be recouped through extending the scope of state land taxes to principal residences. Land taxes are a far more efficient tax than stamp duties and the change offers an opportunity to improve overall efficiency, and remove a secondary impediment to optimal housing decisions for older Australians.

There are some implementation challenges in moving to a broad-based land tax, including cash-flow concerns for low-income retirees living in high-value family homes. One option to address this concern could be to allow low-income older people to defer payment until the dwelling is eventually sold. A small number of local governments around Australia have already implemented similar schemes for council rates.

Exemption of the family home from the Age Pension means test

The family home has been exempt from the Age Pension means test since 1912. At the time of its introduction, the exemption was justified by the government of the day as being necessary to make older people more independent of their relatives. Since then, there have been virtually no government attempts to explain the rationale for the exemption, with the exception of Prime Minister Hawke in 1984, who observed:

... there is a feeling ... throughout the community there is some special significance attached to the home. People don't like to feel that that is something which is included in some sort of testing in their rights in regard to the pension.

The family home now has an ingrained role in Australia's retirement savings and income system. Nevertheless, its exemption from the Age Pension means test creates an incentive for over-investment in principal residences, discourages downsizing and generally reinforces the perception that the family home should not play a role in the retirement funding mix. In effect, by giving home ownership a special status, the means test distorts and constrains the range of accommodation and retirement income choices of older Australians. The exemption is also inequitable — it favours home owners over non-home owners, who are typically less wealthy and possibly in greater need of assistance.

Multiple reviews have argued for the abolition or the setting of a cap on the exemption. Removing the family home exemption would be the most efficient and equitable outcome,

but this appears intractable in the immediate future. At a minimum, there is a strong case on equity grounds to set a limit on its value.

The Commission conducted illustrative and simplified analysis to investigate the effect of setting a cap on the principal residence exemption on eligibility for the Age Pension. Importantly, this analysis is only intended for indicative purposes and does not represent a comprehensively designed policy proposal. The latter would involve a thorough consideration of the entire means test, to ensure that it is well targeted and internally consistent. Based on the Commission’s analysis, setting a cap on the exemption at about the median house price value is unlikely to significantly affect eligibility for the Age Pension. Doing so in 2010 would not have affected the Age Pension payments of the vast majority of pensioners and would have reduced the proportion of the age-eligible population receiving the Age Pension by less than 3 percentage points (table 1). The latter group would comprise people who in 2010 held a median household wealth of about \$1.6 million. The limited impact of setting the cap on the family home exemption is in part due to the fact that for many pensioners the income test would still be the relevant test.

Notwithstanding the limited effect of this change on the proportion of people eligible for the Age Pension, there could still be significant fiscal savings to governments due to the sheer size of the Age Pension bill (a total of \$42 billion in 2014-15) and other government benefits available to pension recipients. More fundamentally, it would provide a much needed signal from the Australian Government that the home is an asset that can be drawn upon by older Australians.

Table 1 Impact on Age Pension eligibility of changing the assets test
Proportion of population of Age Pension age, 2010

	<i>Threshold beyond which principal residence is included in the assets test</i>						
	Fully included	\$440 000 (median)	\$500 000	\$750 000	\$1 000 000	\$1 250 000	Current treatment
Proportion on Age Pension	62.3	70.8	71.4	72.5	72.8	73.1	73.3
Impact on proportion eligible for Age Pension	-11.0	-2.5	-1.9	-0.8	-0.5	-0.2	0.0
Proportion whose Age Pension is reduced	45.9	10.6	7.5	3.0	0.9	0.4	0.0

Careful consideration of other policy levers and implementation would be needed

Any change to the treatment of the family home in the Age Pension means test needs to be considered in the context of a broad retirement incomes review. The Commission’s recent research report *Superannuation Policy for Post-Retirement* also identified the need for such a review — and that the imperative, while not immediate, was now near term.

Introducing a limit on the principal residence exemption would involve several complex implementation issues, including administration and compliance. There would be a strong case for phasing in the change gradually over time, to allow people sufficient time to plan and adjust their retirement decisions.

A key issue would be at what level to set the cap and whether it should reflect the significant regional variation in house prices. For example, the median house price in Sydney is nearly twice that in Adelaide. If the objective of keeping some home value exempt is to quarantine a particular level of *housing services* (as opposed to housing wealth) from the assets test, regional variation in the exemption would be needed.

The means tests for aged care co-contributions could be improved

The recent reforms to aged care have placed a greater emphasis on co-contributions by introducing income tested co-contributions for home care packages and broadening means testing for residential aged care. However, there may be merit in further increases in co-contributions (by relying more on assets) for both home care and residential aged care.

Means test for residential aged care support — scope for more co-contributions

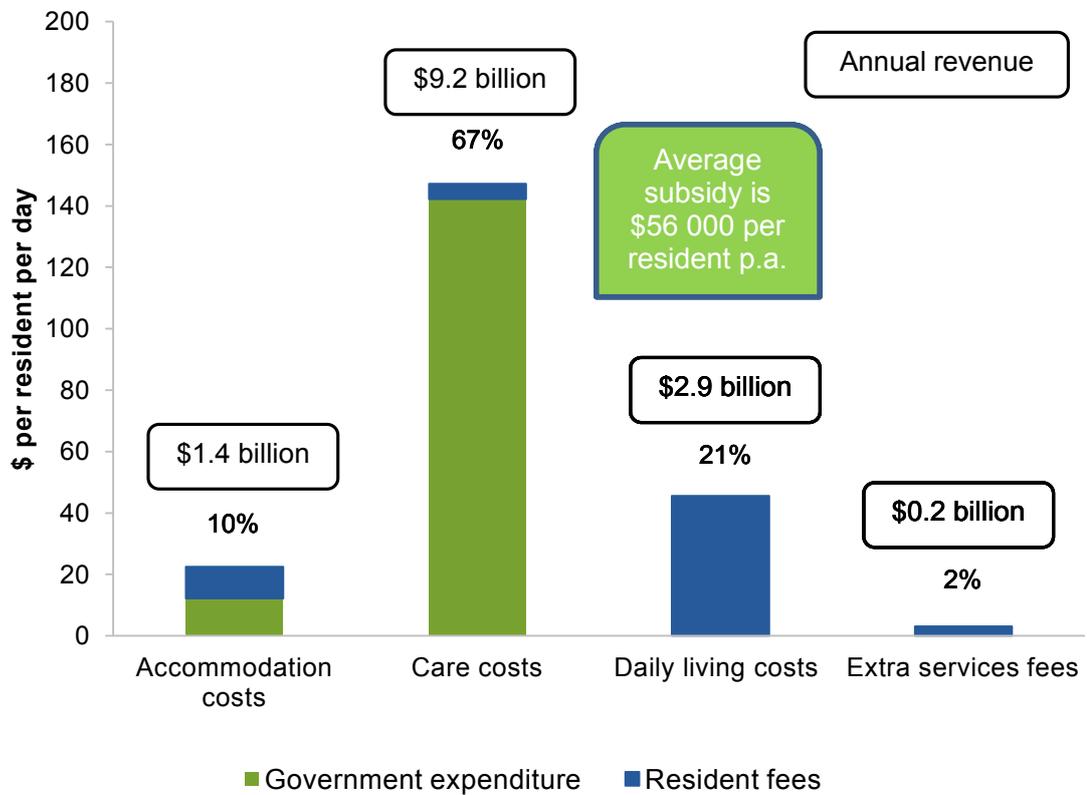
While aged care residents are responsible for their daily living costs, they receive means tested government support for accommodation and care costs (figure 14). Over 40 per cent of residents in aged care have their accommodation costs subsidised and virtually everyone receives a subsidy for the care component.

The current means test for residential aged care support only incorporates the first \$158 000 of the aged care resident's home, and only when there are no remaining protected residents in the family home. Since residential care is typically the final place of accommodation in a person's life, the family home is no longer an accommodation option, nor a vehicle for precautionary saving. The likely primary motivation for retaining the home in such situations is for bequests, and the current arrangements are effectively a subsidy for this preference. There is a strong case for including more of the value of the family home in the means test for residential aged care.

Means testing for home care should include assets

Currently the means testing for home care services only covers income. A more comprehensive means test that incorporates assets may be warranted to better align it with people's capacity to pay. The arrangement where those with relatively high levels of assets are not under any obligation to use them to finance home care is inequitable.

Figure 14 Sources of revenue for residential aged care providers



Source: ACFA (2015).

Using home equity in retirement — scope, barriers and policy issues

In recent years, much has been written about the improved wellbeing and benefits for older Australians if they made greater use of the equity in their family home to supplement their retirement incomes. While there are several ways of drawing on housing wealth, proponents of this argument often advocate using financial equity release products.

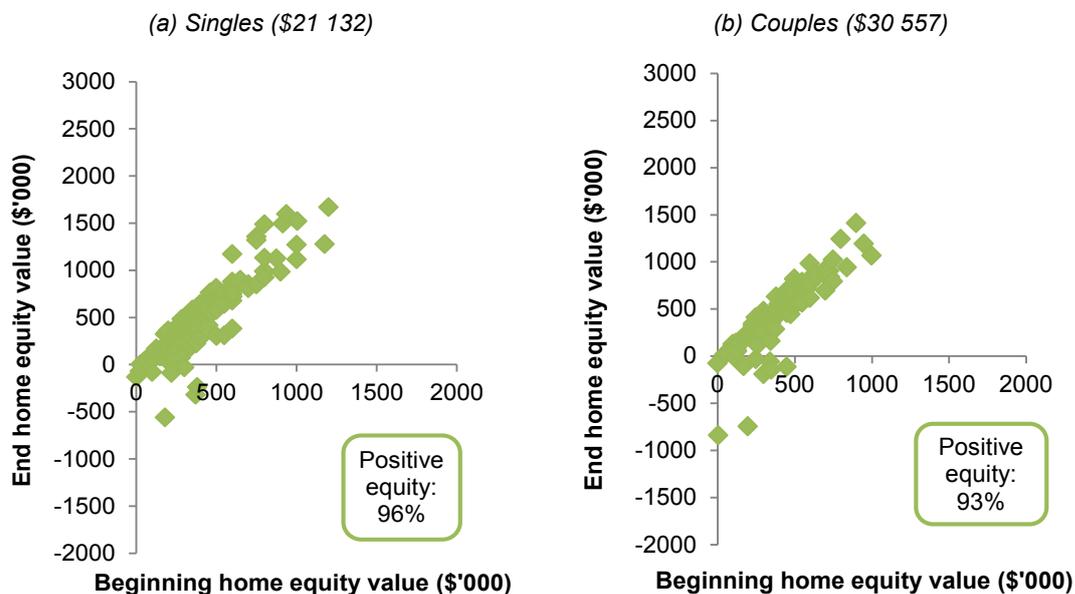
Setting aside the potentially valid precautionary and bequest motives for not drawing on housing wealth, there is some basis to those claims. However, there are limits to the scope for using home wealth to supplement incomes in old age, and financial products to facilitate such home equity withdrawal are not necessarily attractive for their intended demographic.

Most retirees could modestly increase incomes by using home equity

The Commission conducted illustrative quantitative analysis on the scope for improving the living standards of older Australians through accessing the equity in the family home. The analysis drew on the 2010 HILDA data sample of about 900 home-owning age pensioner households. It sought to demonstrate the expected end-of-life home equity balances of the current population of age pensioners if they used housing wealth to boost their incomes to a particular ‘retirement standard’ over the rest of their lives.

The data showed that about 40 per cent of Age Pension recipients that owned their homes (half of single person households and about one-third of home owner couples with at least one Age Pension recipient) did not meet a ‘modest retirement standard’.⁴ The vast majority of those people (more than 90 per cent) could use their home equity to reach and maintain this income level over the rest of their lives. For about 5 per cent of households that need to borrow to meet the modest standard, the amount of home equity would not be enough to maintain that standard over the rest of their lives (figure 15).

Figure 15 **Using home equity to boost incomes to a ‘modest’ living standard^a**

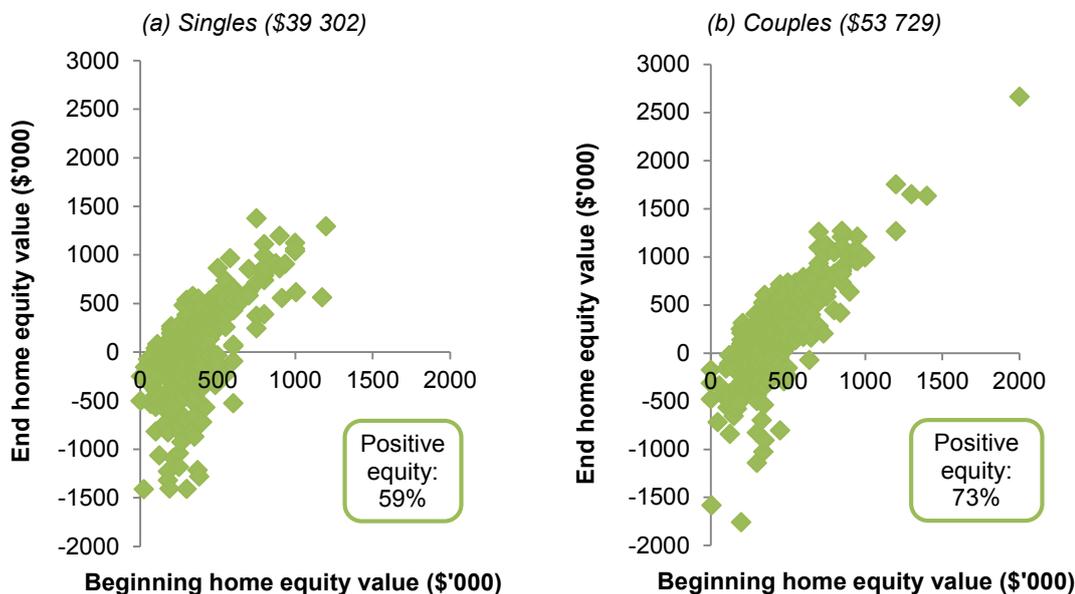


^a Beginning home equity values and retirement income standards correspond to 2010.

However, the risk of exhausting their home equity (reflected in the size of the group that does so) escalates rapidly if the older household uses its home wealth to move beyond a modest living standard (figure 16).

⁴ The income levels necessary to achieve particular living standards in retirement are published by the Association of Superannuation Funds of Australia.

Figure 16 **Using home equity to boost incomes to a ‘comfortable’ living standard^a**



^a Beginning home equity values and retirement income standards correspond to 2010.

What are the current prospects of financial equity release markets?

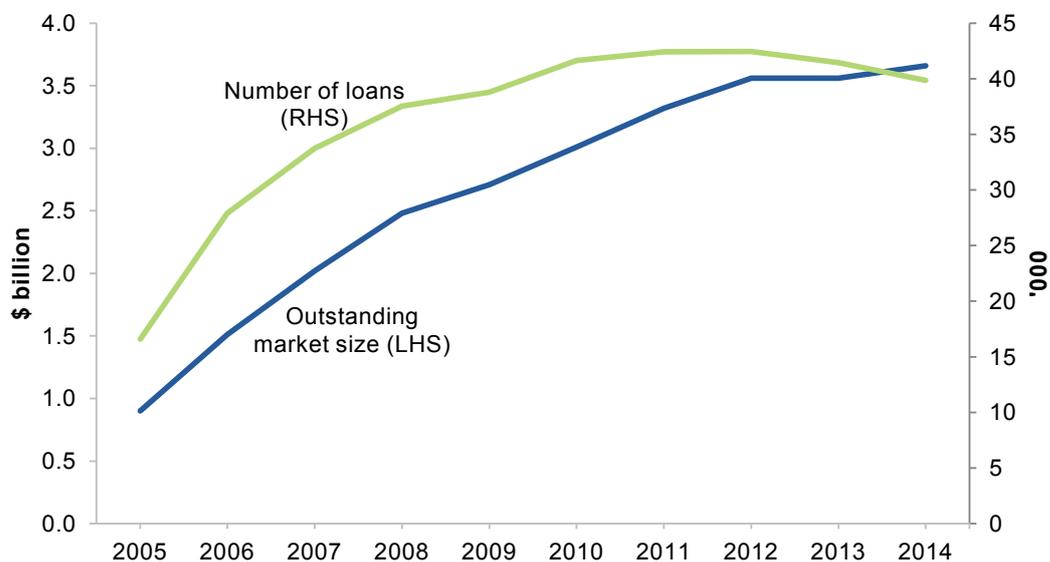
The equity release market remains very small

Equity release products (ERP) can take the form of credit and debt-free products and both types are available in Australia. Reverse mortgages (a credit product) make up the vast majority of the market. Some new debt-free products are beginning to emerge but involve greater complexity as they involve an actual equity transaction. There are also some niche credit products, including reverse mortgages provided specifically for the purpose of funding refundable accommodation deposits for residential aged care.

The ERP market is very small, covering an estimated 1–2 per cent of older home owners. The value of outstanding reverse mortgages — about \$3.7 billion — accounts for 0.4 per cent of the \$926 billion of home equity owned by older Australians. The market was growing at a moderate pace in the early 2000s, but in recent years growth has plateaued (figure 17).

The average age of a reverse mortgage consumer is 75, and the average outstanding loan size is \$92 000. Common uses of the funds are to supplement regular income, repay debts and make home improvements. The majority of borrowers are in lower income brackets, supporting the view that reverse mortgages are typically a ‘last resort’ option.

Figure 17 **Size of the reverse mortgage market**



Sources: Hickey (2013, 2015).

There are significant barriers to greater uptake and provision

The Commission’s survey indicates wide awareness of ERP products — three-quarters of older people have heard of them and this proportion increases with age. Nevertheless, there are impediments on both the demand and supply sides of the market that appear to be reinforcing each other and preventing the market from growing. Such products are inherently more expensive than standard mortgages because they place longevity and (perhaps) housing price risks on the financier, and the resultant higher interest rates and fees are an unavoidable barrier to greater demand. Demand for ERP is further constrained by a combination of:

- entrenched household preferences, including a strong aversion to debt and stigmatisation of ERP products, as well as a desire to preserve home equity as a precautionary saving or bequest vehicle
- riskiness and uncertainty about the eventual costs for consumers, particularly in the case of credit products
- the effect of equity withdrawal on eligibility for the Age Pension and aged care support
- low availability of products, often dependent on the type and location of the home.

There is also a lack of interest in the products among both investors and providers. The small size of the ERP market is a key issue in and of itself. Many potential providers remain diffident — finding it not worth their trouble to offer the products, particularly given the risks of reputational damage due to negative perceptions and possible adverse

events (although the risk of the latter is reduced by the 2012 consumer protection regulations). The issues on the supply side are compounded by somewhat inconsistent and at times excessive regulatory requirements.

Overall, demand-side impediments appear to be a more substantial barrier. Consequently, there is limited scope to grow the market through supply-side intervention by governments or innovation by providers.

Regulation of the ERP market could be improved, but overall is not the key barrier

Reverse mortgages are subject to a number of prudential and consumer protection requirements. These include the requirement of a ‘No Negative Equity Guarantee’, controls on maximum loan value ratios and capital adequacy requirements as well as the requirement that consumers obtain legal and financial advice.

The regulations do not appear to be a major constraint on the operation of providers. The No Negative Equity Guarantee was part of a self-regulated regime that preceded regulation by ASIC. That regulation was largely welcomed by the sector for giving it a stamp of legitimacy. Nevertheless, the combination of the requirements on negative equity protection, loan to value ratios and capital adequacy requirements appear unnecessarily risk averse and exceed prudential requirements in other comparable jurisdictions (like the United Kingdom and Canada). For example, the loan value restrictions appear redundant in the presence of the No Negative Equity Guarantee.

A possible problem for the market is that regulation has so far focused solely on reverse mortgages. To the extent that the reputation of providers benefits from consumer protection regulation, there should be consistent Commonwealth regulation across all ERPs, not just for reverse mortgages. ASIC is currently examining the regulation of emerging debt-free equity release products.

Role for government depends on policy context

The Commission has previously argued the case for a government-backed ERP to facilitate greater co-contributions to the cost of aged care.

... if the Government requires care recipients with low income, but with assets, to contribute to their care costs, a vehicle is required that allows recipients to draw down small regular sums of money. Such a scheme is unlikely to be attractive to private providers and, if offered, is likely to involve very high set-up costs. (PC 2011, p. 112)

The Australian Government remains the overwhelming funder of aged care, and there is both capacity and merit in older Australians contributing more to their care costs. A shift to more comprehensive means testing and greater co-contributions would require governments to pay close attention to the risks for low-income older people that have substantial wealth locked up in the family home, but no ready way to access it. The policy

options that could be considered in that context include greater government involvement in ERP, as proposed by the Commission in the past.

However, in the absence of major changes to safety nets and co-contributions, the case for government support for private ERP providers or direct provision of ERPs is weak. Measures that result in the government assuming longevity risk from providers could lead to moral hazard and further elevate the government's fiscal exposure. The Australian Government (and ultimately taxpayers) is already bearing much of the base cost of longevity risk through the Age Pension and aged care support. Conversely, if governments provide ERPs themselves, they could impede the development of an already fragile private market.

One current attempt by the Australian Government to provide a subsidised reverse mortgage scheme for pensioners — the Pension Loans Scheme — appears both inefficient and ineffective. In 2014, it was only being used by about 0.04 per cent of Age Pension age households in Australia. In part, this is a consequence of multiple design flaws of the program. However, the Commission's survey indicates little interest in the program even if those design flaws were addressed.

There may be a case for some light handed government intervention, such as provision of information on the operation of ERP products and the existing consumer protections. For example, the Commission's survey indicated that only about 20 per cent of older Australians are aware of the No Negative Equity Guarantee protections. However, such policies are unlikely to fundamentally transform the market, given that older people appear reluctant to utilise such products, even in the presence of stronger measures.

Summing up

The housing decisions of older Australians bring up many important policy issues that span multiple aspects of wellbeing. Some of the issues that directly affect housing decisions of older Australians have broader applications like housing affordability, and are either not limited to older people, or extend beyond housing decisions. This study has not attempted to address all aspects of housing decisions of older Australians, instead focusing on selected policy 'hotspots' to identify potential first steps to improving the outcomes for older Australians and the broader community.

However, as the study progressed, the twin imperative of comprehensive reviews of retirement income policy and housing affordability for low-income households became increasingly apparent.

1 About this study

Housing forms a large part of the Australian economy and is an integral part of people's lives. Residential land and dwellings account for more than half of total household assets, two-thirds of Australian households are home owners, and for most households, the family home is the single largest source of wealth.

Housing plays a particularly important role in the lives of older Australians — a growing segment of the Australian population. The housing needs of people change as they get older, and housing services make up an increasing proportion of their consumption. Older people as a group also tend to own their homes — about 80 per cent of older Australians are home owners — and they account for a relatively large share of overall housing wealth. With house prices having risen by 5.5 per cent per year on average over the past decade, older households today are wealthier than both younger households and older households a decade ago. Despite having substantial wealth locked up in the family home and the changing nature of their housing and care needs, most people do not draw on their home equity throughout their retirement.

Even small changes in housing outcomes can have a significant impact on older people's financial circumstances, social inclusion and other aspects of their wellbeing — including physical, mental and emotional health. This study aims to explore the drivers of housing decisions of older Australians, as well as some of the barriers to better outcomes.

1.1 Background to this study

This study is the Commission's third 'flagship' research project. It complements a number of recent Commission publications.

Relevant recent studies

The Commission's inquiry report on *Caring for Older Australians* (PC 2011) explored the entire spectrum of issues affecting Australia's aged care system, including various policies that distorted the accommodation outcomes of older Australians. The recommendations in that report set in train a set of reforms of the aged care system, the implementation of which is still continuing.

In its flagship research paper *An Ageing Australia: Preparing for the Future* (PC 2013), the Commission identified that many older Australians are asset rich but income poor. The paper also flagged the challenges for government budgets from the ageing of Australia's

population, particularly if the pension age were to remain unchanged in the face of growing longevity. It drew attention to the potential benefits of using housing equity to help fund government-provided services and relieve some of the fiscal pressures associated with an ageing population.

Links between government assistance and housing decisions were the focus of the Commission's second flagship research paper *Housing Assistance and Employment in Australia* (PC 2015a). Most recently, the questions of when and how people access their superannuation were examined in the Commission's research paper *Superannuation Policy for Post-Retirement* (PC 2015b).

How does this study contribute?

This study revisits and expands on some of the issues raised in those studies. Similar to the approach adopted in previous flagship research projects, it does not present a comprehensive assessment of all relevant issues, instead focusing on a selection of key research questions.

- What are the housing and financial decisions of older Australians, and what are the reasons behind these decisions?
- What are the barriers to older Australians making housing choices that best suit their needs and preferences? This study examined three key policy areas:
 - the tax and social security treatment of the family home
 - the availability and accessibility of residential aged care and other age-specific accommodation options
 - the availability of financial market solutions to enable older Australians to access the equity in their homes.
- What progress has been made towards removing or reducing such barriers, and what opportunities exist for further reform?

An important part of this study is the presentation of a 'report card' on progress against the 2011 *Caring for Older Australians* recommendations (appendix B).

What this study did not cover

The focus of this study is on the implications of older Australians' housing and accommodation decisions, and the interplay between aged care and housing. It did not examine broader supply-side issues in the housing market, nor look at non-accommodation elements of aged care (which were covered in *Caring for Older Australians*). The study also did not consider the adequacy of retirement incomes.

1.2 Conduct of the study

This research project commenced in June 2015 and spanned six months, with a final report released in December 2015.

In the course of this study, the Commission drew upon available data and existing research on the issues and consulted widely with stakeholders. It also conducted a survey of the views of older Australians on the key accommodation, aged care and financial decisions of their lives. Finally, it presented some illustrative quantitative work on the effect of some changes in policy and people's decisions that relate to the wealth stored in the family home.

Consultation

Commissioners and staff conducted visits in Sydney, Canberra and Melbourne, meeting with almost 100 people across 50 organisations. These included advocacy groups, financial industry representatives, academics and researchers, government departments, agencies and regulators (appendix A).

The Commission also conducted a roundtable focused on factors affecting the housing outcomes of older people — specifically the preference of many people to 'age in place'. The roundtable was held in Sydney on 25 September 2015, and was attended by academics, consultants, departmental staff and other relevant stakeholders.

The Commission is grateful to all participants for their contribution to this study.

Survey

The Commission engaged RFI Group to conduct a national survey of older Australians on the reasons for housing decisions relevant to this study. Although there were publicly available data on general consumption, saving and investment outcomes, including housing choices, there were no recent surveys that comprehensively addressed the behavioural drivers of specific decisions relevant to this study.

The Commission's survey canvassed older Australians' views on issues such as: planning for retirement; housing preferences and downsizing; savings, debt and bequests; and home equity release products. The survey was conducted online in September 2015, and involved 1500 Australians aged over 60 years.

Key results from the survey are presented throughout the report. A more detailed description of survey methodology is given in appendix C, and the full survey results are available on the Commission's website.

Illustrative scenarios

The Commission also prepared simple illustrative examples of the effects of selected policy changes on household income and wealth, assuming particular behavioural responses by households. This analysis used data from the Household, Income and Labour Dynamics in Australia (HILDA) Survey. It consisted of two streams of work.

The first sought to assess the implications of modifying the concessional treatment of the principal residence in the Age Pension assets test. It investigated the effect of setting different limits on the principal residence exemption on Age Pension eligibility. The second area of work sought to show to what extent older Australian home owners on low incomes could reach a benchmark standard of retirement income by drawing from their home equity through debt-based equity release.

The results of these two areas of illustrative work are presented in chapters 5 and 6, respectively. A detailed account of the methodology is given in appendix D.

1.3 Structure of the report

The remainder of the report is structured as follows. Chapter 2 formulates the objectives for housing policy, and sets out a framework for analysing older people's housing decisions, the factors affecting these decisions and the policy implications.

Chapter 3 presents evidence on older Australians' housing and financial decisions in current and recent historical contexts.

Chapter 4 examines age-specific housing options that address the accommodation and care needs of older Australians, and discusses barriers to the supply of age-specific housing. It also considers the effect of recent aged care reforms, and future directions for reform. (A more detailed description of recent progress on aged care reform is given in appendix B.)

Chapter 5 explores the impact of Australia's current tax and transfer architecture on the housing decisions of older Australians, with a particular focus on the treatment of the principal residence in the means test for the Age Pension.

Chapter 6 outlines developments in the home equity release market and discusses the extent to which older Australians are using equity release products to draw on the wealth in their homes. It also considers possible barriers to efficient operation of the market for these products.

Appendix A contains details of stakeholders consulted for the study. Appendix B summarises progress to date against the 2011 *Caring for Older Australians* recommendations. Appendix C gives details of the methodology used for the Commission's survey. Appendix D describes the methodology behind the illustrative quantitative work.

2 Putting housing decisions in a policy context

Key points

- Housing plays a unique role in the lives of older Australians. In addition to providing physical shelter and contributing to the physical and psychological wellbeing of older people, it is a source of wealth that can facilitate financial security in retirement.
- This study aims to facilitate efficient and equitable housing outcomes for older Australians, and spans both the accommodation and financial aspects of housing decisions.
- People can develop a strong attachment to their family home and local community. It is natural for older people to want to ‘age in place’ for as long as possible, and policies should not impede this.
- Several features of accommodation can influence the wellbeing of older people, including its location, size, design, layout and facilities, as well as security of tenure.
- As people’s aged care needs rise, age-specific accommodation and ultimately, residential aged care, may become necessary. It is important that policies facilitate a smooth transition along this spectrum.
- While housing wealth built up over a person’s working life can be a source of income in retirement, people may choose not to draw on it, because they wish to leave a bequest, or as a precaution for uncertain future needs.
- Governments should not second guess what is in people’s best interests.
 - However, government involvement may be warranted if financial, accommodation and aged care decisions are impeded by poor or asymmetric information.
 - Governments may also assist where outcomes are distorted by existing policies, such as the treatment of the principal residence in the Age Pension and aged care means tests, and the regulatory arrangements affecting the supply of age-specific housing.
- People can draw on their housing wealth by selling the house, renting it out, or by using a financial equity release product.
- Financial equity release products allow people to draw on their housing wealth without moving home. However, there could be other issues on both the demand and supply sides of the equity release market that prevent its development.

The role for any policy is to improve the living standards of the broader community. A common perception is that this is code for focusing purely on financial considerations such as wealth and incomes. However, living standards are much broader than that and encompass other less tangible aspects of wellbeing, such as health and social cohesion.

Housing decisions, particularly those made in old age, raise policy issues spanning multiple aspects of wellbeing — provision of a basic human need for physical shelter, contributing to physical and psychological health and emotional security, and determining wealth and incomes that enable a person to fund their lifestyle.

It is challenging to incorporate all of the drivers and implications of housing decisions in an economic framework. However, the end goals for policy are relatively clear. At a high level, this study seeks to promote outcomes where:

- older Australians consume the housing services that correspond to their preferences and needs, while making rational decisions on how much housing wealth they accumulate and retain
- the housing services required by older Australians are provided cost effectively
- the provision and consumption of age-specific housing is efficient and sustainable over time. This includes:
 - fiscal sustainability for current and future generations
 - no undue barriers for investment in new supply of accommodation
 - competitive pressures to encourage innovation, cost reductions and quality improvement.

In pursuing those outcomes, which economists would regard as efficient, it is important not to forget about fairness and equity. The need for a safety net system that avoids poverty and homelessness, and guarantees a minimum level of aged care and housing irrespective of capacity to pay is broadly accepted. This objective is fundamental for this study.

Creating a level playing field for similar groups across the community is also important. For example, those with similar levels of income and wealth may reasonably expect to be subject to the same taxation and social security treatment irrespective of the sources of income, composition of wealth or particular housing choices.

It is also desirable to examine the ‘intergenerational equity’ of the current policies and outcomes, to assess whether they impose disproportionate burdens or confer disproportionate benefits on particular generations of Australians.

Finally, while the focus of this study is on the housing decisions of older Australians, the overriding concern and perspective for the analysis is on generating the best outcomes for the community as a whole.

The rest of this chapter provides an overview of the issues affecting housing decisions, some of which are examined in more detail in the remainder of the report.

2.1 Life cycle theory of consumption and saving

Housing decisions tend to involve substantial financial outlays and often play out over long periods. They should, therefore, be viewed in the context of a person's broader consumption, saving and investment decisions over their lifetime.

The original life cycle theory of consumption (Modigliani and Brumberg 1954) is based on the idea that people make their consumption and saving decisions at any point in their lives on the basis of the income they expect to receive over their entire lives. The income that people earn is not constant over their lifetimes. However, by building up and running down their assets, people can smooth their consumption patterns and match them to their needs at different ages, independently of their incomes at each age. The theory effectively predicts that a person would provide for their retirement by saving (and investing) some of their income during their working life and then run down that wealth in old age.

The central tenet of the theory is widely accepted by researchers as a factor in decision making. However, many researchers have argued that there are several other factors that could affect consumption and investment over a person's life to the point where the expected saving and dissaving pattern would not arise.

Why would behaviour not conform to simple life cycle theories?

There are many reasons for people's behaviour to diverge from theoretical predictions. Some drivers have an intrinsic origin — the characteristics, life circumstances and preferences of the person, as well as the quality of their decision making. Others relate more to 'environmental' factors, such as the characteristics and performance of relevant markets, government policy settings and the overall performance of the economy.

People's circumstances differ

It is too simplistic to assume that every older Australian would follow the same economic path over their life. There is great diversity in the Australian population. People start off on different levels of wealth, have different lifetime income earning capacities and can have markedly different preferences about the key economic decisions in their lives. There are a number of disadvantaged or vulnerable groups, including Indigenous Australians, for whom the questions of home ownership and accumulation of wealth for future needs may not even arise. A more immediate challenge is avoiding poverty and homelessness (chapters 3 and 4).

In addition to the diversity across the Australian population, there are indicators of *generational* change that could mean that the baby boomer retirees of today and tomorrow will make different consumption, saving and investment decisions than the generations of older Australians that preceded them (chapter 3).

Bequests are an important factor

The desire to transfer some wealth to other family members (in particular, to children) is often a factor in consumption and saving decisions. At its simplest, a person who is strongly motivated to bequeath their wealth would have a greater incentive to build and preserve it, rather than consume it in their lifetime.

The Australian evidence on the strength of the bequest motive as well as on actual bequest levels is generally sketchy (chapter 3) and there is some debate among economists and other social scientists about its role in the consumption and saving decisions of older people (Judd et al. 2012). Some survey evidence may indicate that the bequest motive is not a major consideration and some researchers have argued there has been a generational change in attitudes to bequests best summed up by the phrase ‘spending the kids’ inheritance’ (Olsberg and Winters 2005).

Changing demographic factors may also play a role. Increased longevity means that a bequest would not reach its recipient until later in life, when it would be less needed. Thus, parents may focus on assisting children earlier in life and have a lower incentive to preserve wealth late in their own lives.

Precautionary saving

Over the long term, consumption and saving decisions are affected by significant uncertainty about key future events in a person’s life. There is uncertainty over the future level of income and value of assets, as well as key factors affecting lifetime consumption, such as longevity and future health.

Older people can insure themselves against longevity risks through financial markets, for example by purchasing a lifetime annuity. However, uptake of such products is very limited, possibly because of their characteristics (PC 2015b). The market for such products can also be affected by information asymmetries (discussed below) that might make it simpler and less costly for a person to self-insure through precautionary saving.

Saving for a rainy day in the future means that a person is consuming less today. If this behaviour persists through the person’s life, it is likely that they will leave a bequest that is larger than what they originally contemplated — an unintended bequest — and will have consumed less over their life than they intended.

There is nothing wrong with precautionary saving per se — it is not irrational for people to seek financial security by maintaining a financial buffer in old age. However, the wellbeing of older Australians can be compromised if such decisions are not based on a rational assessment underpinned by sound information, or if those decisions are affected by problems and deficiencies in financial and accommodation markets.

Furthermore, the Australian Government bears most of the costs of longevity through the Age Pension and other forms of financial support in aged care and health. This welfare safety net would be expected to diminish the desire by most older people to save for precautionary reasons.

Market failures, transaction costs and cognitive constraints

A fundamental principle in economics is that rational decision making and well-functioning markets lead to the most efficient outcomes for individuals and the community. However, those pre-requisites are not always present, and in some cases government intervention may be warranted to improve on the market outcome.

Market failures and transaction costs

Markets can fail for a variety of reasons. One type of market failure relevant to this study arises from information asymmetries in financial decisions and in decisions that relate to age-specific accommodation markets. A general lack of information could also lead to poor outcomes (box 2.1).

Even in the absence of conventional market failures, no real-world market fully meets the textbook definition of a perfect market. Arranging any transaction involves some unavoidable costs and some transactions may not proceed because the costs of arranging them, such as the cost of gathering information and engaging legal and financial intermediaries, are too high.

Box 2.1 Information asymmetries and poor information

Information asymmetries

When one party knows more about aspects of the transaction than the other, the informational disadvantage could give rise to various poor outcomes. One possible consequence is 'adverse selection'. When one party cannot easily verify the quality of what the other party is offering, this could lead to bias to lower quality or higher risk transactions. Another potential problem is 'moral hazard', which involves a party modifying their behaviour after the transaction to exploit their information advantage.

For example, the financial, housing and aged care options of older people are very complex and older people could often benefit from specialist advice. However, it can be difficult for some people to overcome the distrust of financial and other specialist advisors when there is no easy way to assess the quality of the advice.

(continued next page)

Box 2.1 (continued)

Information asymmetries can also affect insurance products, such as lifetime annuities (Creighton et al. 2005). The uptake of such products can become biased in favour of high risk customers who try to take advantage of knowing more about their circumstances than the insurer. This can raise the premiums for everyone and make the product unattractive to lower risk customers.

Governments can use a variety of policies to target information asymmetries, including provision of information and regulation of those that have the information advantage to prevent them from exploiting it. In some cases, it may even be optimal for the government to take on the role of provider of the service.

Poor information

For people to make appropriate choices, it is essential that they can rely on sound information. Sometimes important information may not be available in the market. This could happen if the cost of providing such information exceeds what individuals are willing to pay for it. If providing such information will result in a broader public benefit, there may be a reason for government to become involved in its provision.

Older people may be particularly vulnerable to information deficiencies when they are pressured to make decisions due to a health or financial crisis. Many of those decisions are also difficult to reverse, exacerbating the costs.

Cognitive constraints

Even where sound information to underpin decisions is available, all people operate under cognitive constraints (particularly when long-term planning is involved) and can also exhibit behavioural biases that distort decisions. Examples of potentially suboptimal decision making include ‘myopia’ and inconsistent decisions over near and distant future (box 2.2). Most people typically also use mental shortcuts and rules of thumb that deliver a ‘good enough’, but not necessarily the best outcome.

A key issue for this study is whether older Australians are efficiently managing their longevity and other longer-term risks through their decisions on housing equity. For example, if people draw down their housing and other wealth early in retirement and have very low income in old age, this could suggest myopia or ill-informed decision making. However, it may also reflect a preference for greater consumption when a person is younger, healthier and generally more active.

Evidence of slow drawdown of wealth in retirement coupled with substantial unintended bequests could indicate that some people are engaging in excessive precautionary saving. This could arise from poor information and problems in insurance markets as well as from a person’s cognitive limitations or biases. However, it may also be difficult to discern unplanned bequests from those that were intended.

Box 2.2 Biases in long-run financial planning and pre-commitment

There is a growing body of economic and psychological research investigating the behavioural biases affecting people's long-run financial planning, and in particular, saving behaviour. There is research showing that while people are often rational about their long-term plans, short-term impatience can get in the way of those plans. Simply put, there is a gap between long-run intentions that favour saving and short-run actions that lean to consumption.

A number of economists have argued that housing (and other illiquid assets) play an important pre-commitment role for households that realise that they will struggle with financial discipline and may spend more than what is in their long-term interests. In such situations, a household will keep some of its wealth in housing and other illiquid assets to safeguard those assets from lapses in self-control. Housing wealth would only be accessed once all of the liquid assets have been completely drawn down.

Sources: Angeletos et al. (2001); Levin (1998).

Other factors affecting life cycle consumption and saving

Life course factors

Non-economic factors also play a significant role. Various events in a person's life such as health problems, involuntary unemployment, and changes in family and household structure, could influence saving and consumption (Judd et al. 2012).

It is also unreasonable to conflate a person's life stages simply into the pre- and post-retirement phases. For most people, the retirement phase of their lives involves a long period over which the preferences and needs can change markedly. Although this still simplifies reality, this study adopted the classification often used in the superannuation industry (figure 2.1).

Macroeconomic and socio-demographic factors

Every person is a member of the broader community and economy and those 'external environment' factors play a major role in individual decisions. Considerations such as general economic growth, the unemployment rate, inflation and interest rates — though not a focus for this study — can clearly affect individual decisions about consumption, saving and investment.

Similarly, demographic factors, particularly those that affect household formation, such as increasing longevity and the ageing of the population, would affect people's decisions. Social factors, such as cultural attitudes to consumption, saving and home ownership are also likely to play a role.

Figure 2.1 **Three phases of retirement**

Active Ages 60-75	Passive Ages 65-85	Frail Ages 75+
Continuation of lifestyle but more time for leisure, travel and family	Shift to more passive activities Travel is closer to home.	Restricted mobility means leisure activities are limited
Some part-time work	Some unpaid charitable work	Reduced contribution to economy and society
Increased expenditure on leisure. Majority still net savers	Increased expenditure on health. More frugal lifestyles	Increased expenditure on health and aged care
Housing upgrade	Housing 'rightsizing'	Retirement village or nursing home

Source: Rice (2014).

2.2 The role of housing

Housing plays a unique role in people's lives. It is a key part of most households' consumption and an important contributor to the wellbeing of the occupants. A house is also a durable good and home ownership can be a significant investment decision and ultimately, a major source of a household's wealth (chapter 3).

Housing consumption — the lifestyle benefits and age-specific needs

The benefits of having a home extend well beyond securing basic shelter. Some of these are economic and more amenable to measurement (box 2.3). Others are less tangible, but no less important, aspects of wellbeing. The quality and location of housing can influence physical and psychological health and social engagement (Davey et al. 2004; Faulkner and Bennett 2002). People can also develop strong feelings of personal attachment to their family home, and perceive the home as a source of memories and security and comfort in old age.

Box 2.3 Measuring the consumption value of home ownership — net imputed rent

Net imputed rent is an approach used to convert the benefits of owning a house into a dollar equivalent. It involves estimating the net financial benefit that the home owner obtains by virtue of not having to make rental payments for their property. There are two methods for measuring net imputed rent. The 'market value' method used by the ABS involves estimating the market rent that the property would attract if it were commercially rented, net of housing costs. The 'opportunity cost' method involves estimating the financial benefits the home owner could obtain if they invested the proceeds from selling their home in the next best alternative.

The inclusion of net imputed rent in income estimates provides a more accurate reflection of true income levels of households and allows more meaningful comparisons of household incomes across different tenure types. For example, in 2011-12, the median net imputed rent for Australians aged over 65 who owned their homes was about \$230 per week, which compares to median private rental of about \$240 per week.

Sources: ABS (2008); Saunders and Siminski (2005); Productivity Commission estimates based on ABS (2013b).

Three key aspects of housing outcomes influence an older household's wellbeing:

- type and security of tenure
- location
- characteristics of the dwelling.

Security of tenure is a very important consideration for housing choices of older Australians. There is research showing that older people who know that they have stable long-term accommodation demonstrate better physical and psychological health (Freilich et al. 2014).

Outright home ownership generally provides the greatest security of tenure. It also provides owners with the greatest freedom to customise their accommodation to their needs. These could be important drivers of a preference for home ownership, over other forms of tenure such as rental.

Location is another key determinant of housing decisions and would generally become more important as physical mobility decreases due to frailty. Depending on individual circumstances, ageing and life events can either be a force for change or for the status quo. People develop a psychological and social attachment to a location in which they have lived for a long time. On the other hand, there could be strong push factors if the current location does not meet the infrastructure and services needs of the household, if another location has broader lifestyle advantages, or if there are other reasons to move, such as a desire to live closer to family. At any rate, the lack of supply of suitable accommodation in the right location can be a barrier to moving out of the family home.

Finally, the characteristics of the dwelling itself are fundamental. The nature of the housing demanded and the way it is used changes with the age of the person, and the preferences

may vary across the population. The suitability of a dwelling to the needs of an older person can depend on its size and physical characteristics (Davey et al. 2004; Judd et al. 2010).

Maintaining a large house and garden can become progressively more difficult with age. Other life events such as children moving out of the home or the death of a partner can also mean that a smaller dwelling would be more suitable. However, conclusions about the underutilisation of existing housing stock by older people should be drawn with great caution, because the way a house is used can change significantly following retirement. For example, retirees spend a greater proportion of their time at home, and maintaining the garden can become an important pastime. Retirees can also find alternative uses for 'vacant' bedrooms in the house, including as home offices or for hosting grandchildren and other family visitors (Judd et al. 2010).

The design, layout and facilities within the home are no less significant than its physical size. The arrangement and accessibility of living spaces, kitchens and bathrooms, safety features such as non-slip surfaces and hand rails, and appropriate heating and ventilation become more important as a person becomes more frail.

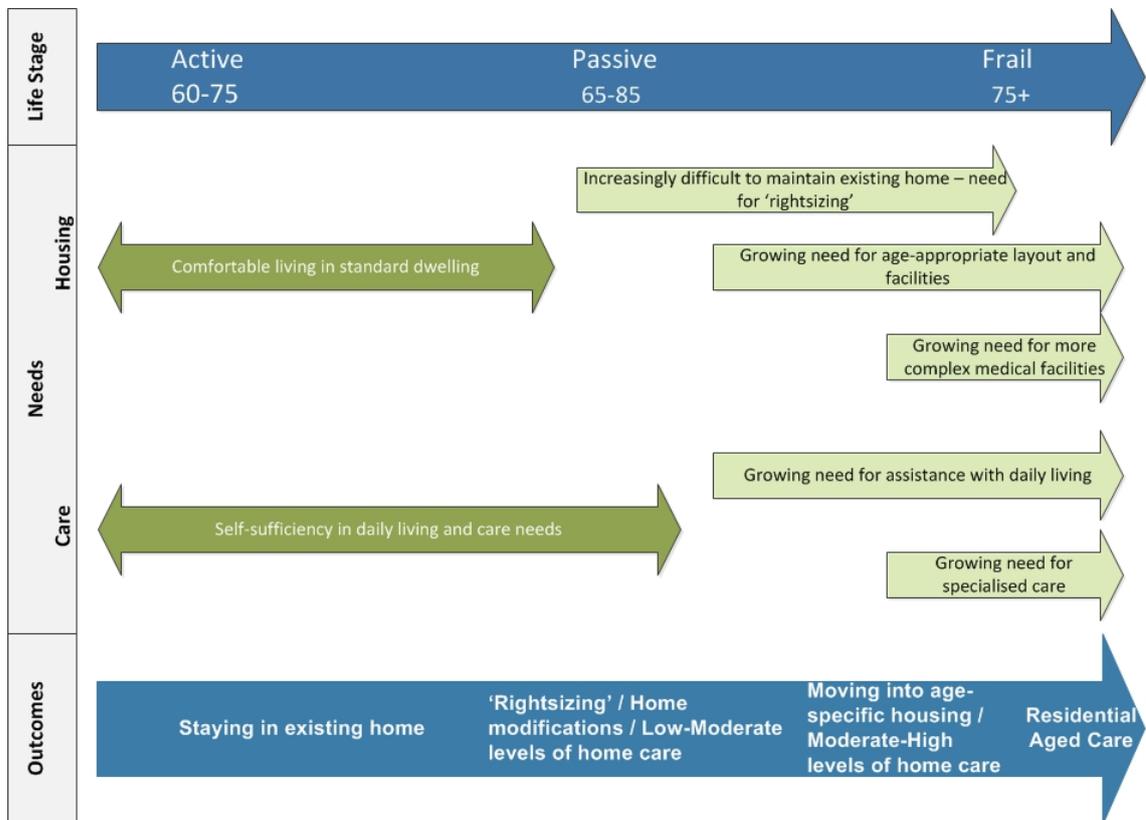
Ageing in place and other accommodation options

The feelings of attachment to the family home or the neighbourhood, and the disruption of moving, can provide a strong incentive to 'age in place'. Ageing in place has different meanings to different people, but is generally broader than simply staying in the family home. For many older people the 'rubber band' attaching them to the family home is the desire to remain in the local community. Whether this is feasible depends on many factors.

Some of the age-specific housing needs may be accommodated by modifying the family home. The extent of the required modification depends on both the needs of the occupants and the original design and adaptability of the residence. Technological change and the evolution of health and aged care provision models may also enable greater ageing in place. For example, the ability to perform some medical procedures in the home may reduce the push to move out.

Nevertheless, there are practical limitations, as well as financial constraints on the ability of older people to age in place (figure 2.2). For many people, alternative forms of accommodation may be more suitable at some point in their lives. Several forms of age-specific accommodation are available, including manufactured homes, retirement villages and residential aged care. These target different wealth and income segments of the population, provide a range of support and health services and cater to a range of needs.

Figure 2.2 Housing and care needs — a simple schema



The policy issues affecting the demand and supply of those forms of accommodation span a variety of areas. They include consumer protection regulations to address information asymmetries and equity concerns, and land planning regulations affecting the capacity of providers to align supply with demand (chapter 4).

A fundamental role in housing outcomes and the overall wellbeing of older Australians is played by aged care policy. The Australian Government regulates the supply of both home and residential aged care. It also provides financial support for older Australians using those services and has specific arrangements for rationing and allocating the supply and demand of aged care. Substantial reforms to aged care policy commenced in 2013 and the process will continue over the next few years.

Housing options for low-income older people that do not own a home

Although about 80 per cent of older Australians own their homes, a significant minority do not. Some home owners are also involuntarily driven to sell their home and move to public or private rental, often for financial reasons. Most of those people tend to have low incomes — drawing an Age Pension that was designed with a primary focus on home owners — and have little accumulated wealth (chapter 3).

Renting in older age is associated with a number of potential risks, including poverty, homelessness and impacts upon mental health and wellbeing (chapter 4).

It is important that the accommodation and care needs of this part of the community are recognised. Various forms of government involvement (some of which are outside the scope of this study) are relevant and important including:

- ensuring that support payments, such as the Age Pension and Commonwealth Rent Assistance, are set at an appropriate level and are well targeted
- ensuring an adequate supply of social housing
- ensuring that existing regulations, such as land use planning, do not unnecessarily constrain the supply of affordable housing for those that need it (chapter 4).

Housing as an investment good

For home owners, the long lasting nature of their house (and virtual permanence of the land on which it is built) means that they can combine their consumption of housing services with investment. Consequently, housing is the main source of wealth for most older Australians (chapter 3).

There are several mechanisms for drawing on housing wealth in old age. These include:

- selling the home either in whole or part
- renting out the home
- drawing down equity using a financial equity release product.

This decision can be very complex because it requires a household to manage uncertainties and risks about future income needs. It is also difficult to disentangle from the issues that relate to the accommodation needs and preferences of the household. Where equity withdrawal involves moving out of the family home, householders have to secure alternative accommodation. Barriers to the supply of age-appropriate accommodation, as well as aged care services, can be both a source of poor housing outcomes and, indirectly, a disincentive for some equity release options.

There are other potential challenges to using housing as a vehicle for managing life cycle consumption. Fundamentally, a house is an illiquid asset, and the owner typically faces substantial costs and constraints in withdrawing housing wealth. Houses are ‘lumpy’ assets (Dvornak and Kohler 2003). Most real estate transactions involve the sale of the entire property and it can be difficult to sell a part of the interest. There are also substantial transaction costs in buying and selling houses. These can include taxes and duties, the cost of searching for the property, and the financial costs of engaging advisors, real estate agents and conveyancers.

Equity release products

One option for drawing on housing wealth that does not entail the disruption and cost of moving out of the family home involves using financial markets to release home equity. Australian financial markets provide a range of options. Some of these are mainstream financial instruments aimed at the broader population. Other products, such as reverse mortgages, are aimed specifically at the older population and retirees. A key characteristic of such age-specific instruments is that it is not necessary to have a particular level of income to access them, and repayments are typically not required until the instrument is terminated.

The market for equity release products for older Australians is relatively new and small. There may be several potential barriers to its development on both the demand and supply sides, some of which are unavoidable. For example, the small size and slow growth of the market may be due to low underlying demand for such products. Older Australians may simply not find this form of equity release attractive compared to other options. There may also be scope to review regulation of the market to ensure it is not an undue barrier to market development (chapter 6).

Taxation, transfers and housing

At the Australian Government level, owner-occupied housing enjoys favourable treatment on both the taxation and transfer sides of the budget. The principal residence is exempt from the means tests for the Age Pension. It is also exempt from capital gains taxes that apply to the sale of many other assets. There is also a range of government support arrangements for other forms of accommodation and aged care, which are typically means tested, but exclude owner occupied housing from that test. On the other hand, at state and territory government level, conveyances of residential property are subject to stamp duties — effectively a tax on the mobility of home owners.

The complex interplay of these arrangements affects the incentives to acquire and dispose of owner-occupied housing, in the context of both accommodation and investment choices. These policies also directly affect government fiscal outcomes. The fairness of the tax and transfer arrangements that apply to home owners vis-à-vis non-home owners, including those that may have substantially less net wealth, is a further important consideration.

The effects on efficiency and equity for the broader community are discussed in chapter 5.

2.3 What role for policy?

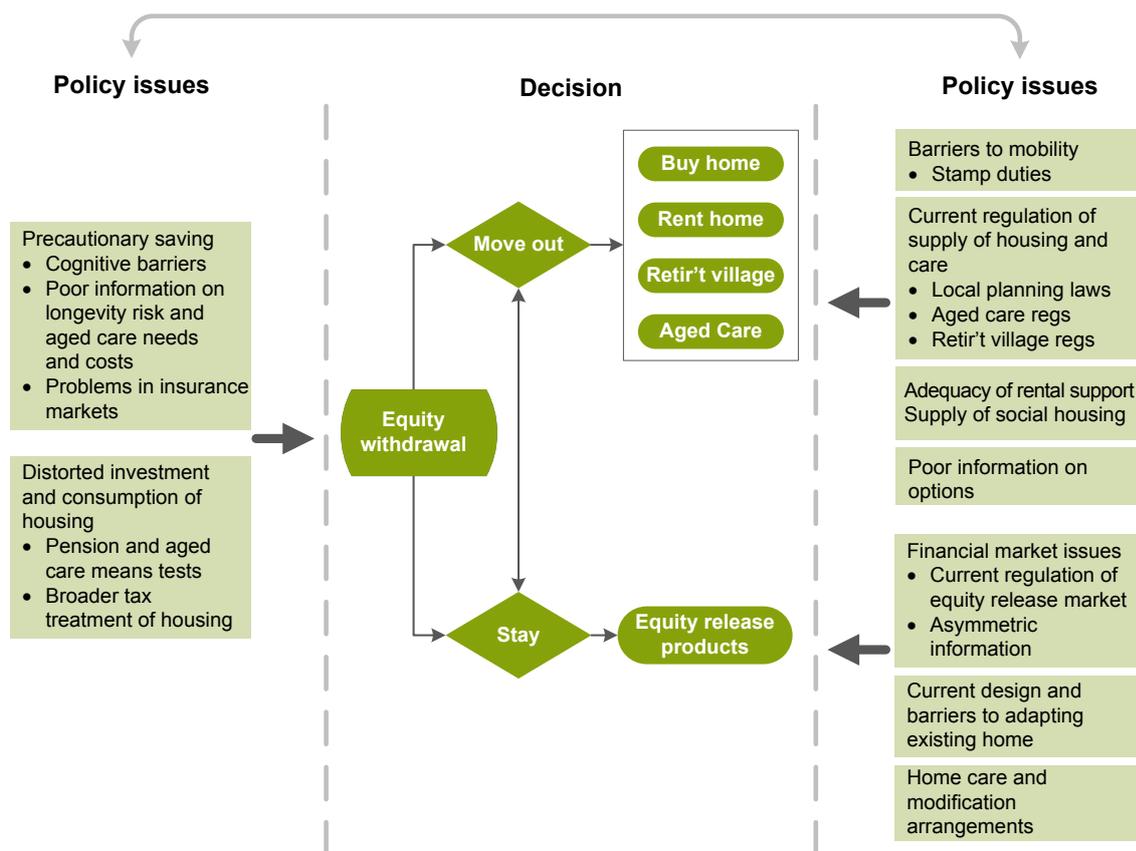
The dual function of housing in people's decisions, the complexity of people's preferences, the heterogeneity of individual circumstances and the limitations of available data make it difficult to specify the optimal housing outcomes for older Australians. However this study

focuses on a more relevant question — what factors could be distorting decisions and leading to outcomes that are not optimal and therefore detrimental to the living standards of older Australians and the community as a whole (figure 2.3).

Some of the issues that directly affect housing decisions of older Australians have broader application and are either not limited to older people, or extend beyond housing decisions. As noted in chapter 1, reviewing issues such as the adequacy of the Age Pension arrangements or the regulations affecting the supply of residential housing is beyond the scope of this study. Those issues should ideally form the basis of more comprehensive inquiries.

Nevertheless, the issues examined in the following chapters provide a ‘road map’ of potential first steps to achieving better housing outcomes for older Australians and the broader community.

Figure 2.3 Policy issues affecting housing decisions of older Australians



3 Evidence on older Australians' housing decisions

Key points

- Most older Australian households are home owners, and for most, the family home is the largest household asset.
- The importance of housing increases with age. Home equity makes up a relatively greater share of wealth for older home owners, and accounts for the large disparity in wealth between home owners and non-home owners. The share of housing in overall consumption also grows as people become older.
- Older households are typically 'asset rich, income poor': they have lower incomes but greater wealth than younger households, as a result of asset accumulation and debt reduction over the life cycle. Households aged 65 to 74 years had the highest average home equity per household, at about \$480 000 in 2011-12.
- Expenditure tends to decline and its composition changes in older age, and older households show a strong propensity to save. Precautionary saving — preserving assets for future 'rainy days' — is a key motive for older people. Most older Australians also intend to leave a bequest, primarily the family home.
- Drawing on home equity to pay for retirement appears to be a last resort for most older Australians.
- Most older Australians strongly prefer to remain in their homes as long as practical. Housing mobility declines with age. The proportion of older households that do move house (about one-third) are more likely to move into smaller and/or less expensive homes.
- The gap between male and female life expectancy is narrowing and there is a growing prevalence of couple households among those aged 65 years and older.
- Older people are now less likely to move into residential aged care than in the past — only about 22 per cent of those 85 years and older have done so — and this happens later in life.
- A small but significant minority of older Australian households are renters rather than home owners, and they are disproportionately likely to be experiencing housing stress, and lower wellbeing more generally. This is particularly pertinent to older Indigenous Australians, who are much more likely to be renting compared to non-Indigenous older Australians.
- Recent cohorts of older Australians appear to behave differently than their predecessors in several key respects — they are more likely to be working longer and to have a mortgage, and less likely to be fully reliant on government transfers.

This chapter presents evidence on older Australians' housing and financial decisions. Section 3.1 sets out a broad context within which these decisions are made. Section 3.2 examines housing decisions from an investment perspective — how the home as an asset

fits into older Australians' income and wealth, expenditure and saving decisions. Section 3.3 considers the consumption side of housing decisions — older Australians' preferences and decisions in terms of where they choose to live.

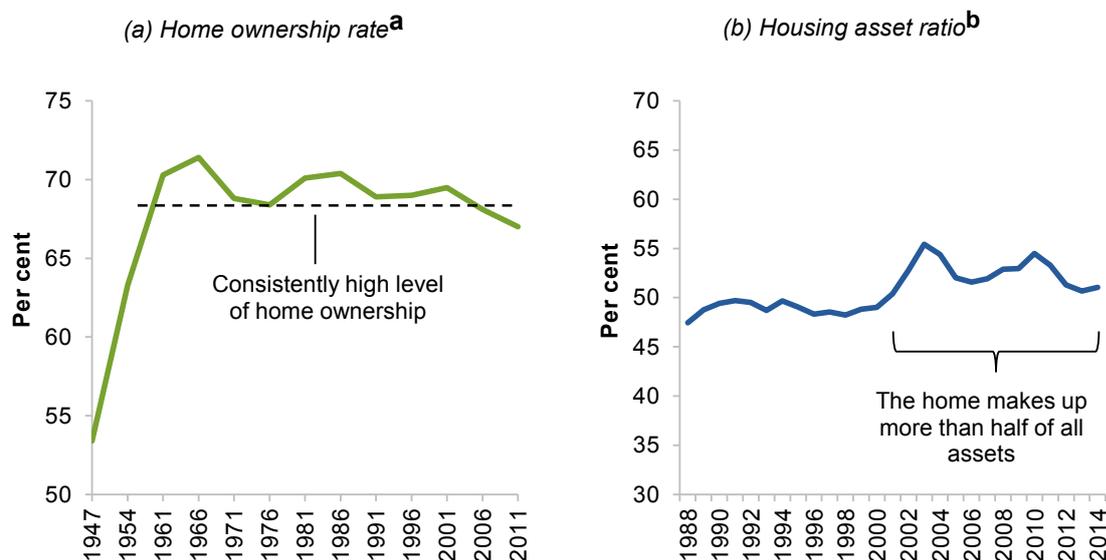
Housing has wide-ranging implications for people's physical, mental and emotional health, as well as for social cohesion and engagement. Conversely, people's characteristics and preferences in relation to health, lifestyle, family and financial circumstances will affect their housing decisions. The aim of this chapter is to shed light on what these decisions are in the Australian context, how older Australian households differ from their younger counterparts and the reasons why they might make these decisions.

3.1 Housing decisions in the Australian context

Housing is a large part of the Australian economy

A lot of Australia's wealth is tied up in housing. Two-thirds of Australian households are home owners (as of 2011), a proportion that has been roughly consistent over the past three decades (figure 3.1, panel a). Australia's home ownership rate is not unusual by OECD standards, and is similar to that in other English-speaking countries (annex, figure 3.27).

Figure 3.1 Home ownership rate and ratio of housing assets to total household assets



a Proportion of owner occupied private dwellings. **b** Ratio of residential land and dwelling (housing) assets to total household assets (nominal).

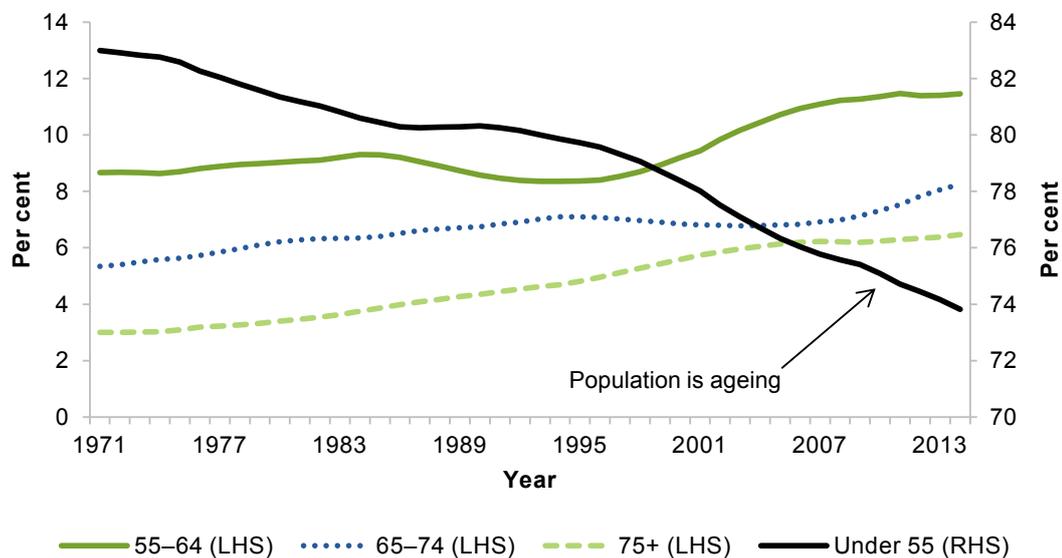
Sources: Productivity Commission estimates based on ABS (*Australian National Accounts: Finance and Wealth, Mar 2015*, Cat. no. 5232.0; *Census of Population and Housing, 2011*, Cat. no. 2037.0.30.001; *Measures of Australia's Progress, 2010*, Cat. no. 1370.0) and Kryger (2009).

Since 1988, housing has made up about half of total household assets (figure 3.1, panel b), and for all except 15–24 year old households, the home asset is the single largest source of wealth (annex, figure 3.28). A little under half of those who own their home are outright owners (without a mortgage), though this ratio differs greatly across age groups (discussed in section 3.3).

Older Australians make up an increasing share of the population

The Australian population is ageing. There have been notable increases in the proportions of older age groups in the Australian population over recent decades, and a corresponding decrease in the share of the population aged under 55 years (figure 3.2). In 2014, more than 25 per cent of the population was aged 55 years or over, compared with 17 per cent in 1971. It is important to note, however, that Indigenous Australians have a much lower life expectancy compared to non-Indigenous people, with the result being that there are relatively few older Indigenous Australians. Only 3 per cent of Indigenous people are aged over 65 years, compared with 13 per cent among non-Indigenous people (AIHW 2011).

Figure 3.2 **Estimated resident population, by age group, Australia 1971–2014^a**



^a Years ended June. Age groups aggregated from single-year age data.

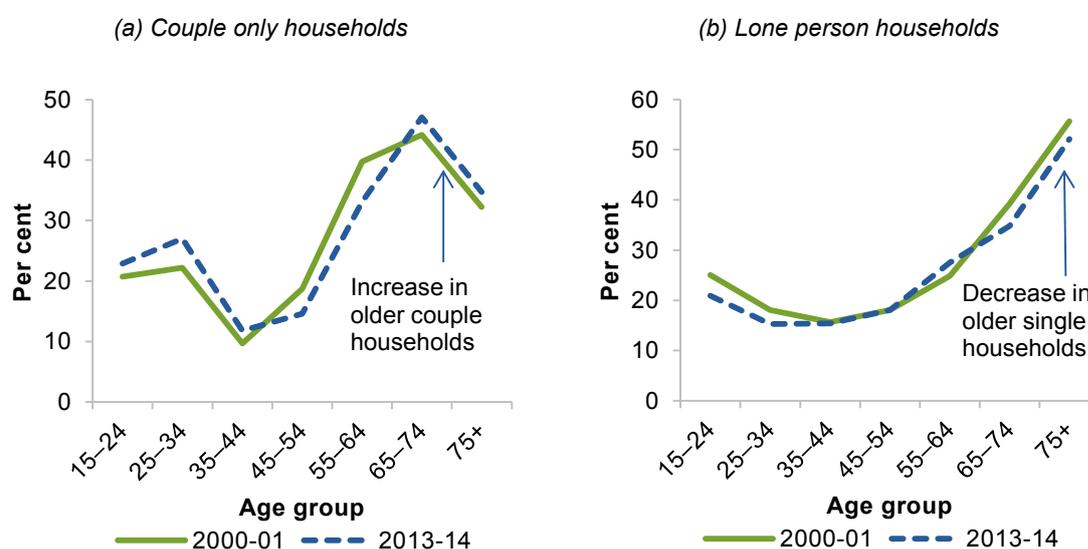
Source: Productivity Commission estimates based on ABS (*Australian Demographic Statistics, December 2014*, Cat. no. 3101.0).

At the same time, the gender gap in life expectancy has narrowed, with male longevity rising faster than female longevity over the past three decades (annex, figure 3.29). The gap between male and female life expectancy at birth has decreased steadily, from 7.0 years in 1982 to 4.4 years in 2010–2012, and the proportion of men in the Australian

population aged 65–74 years is now about equal to the proportion of women in this same age group.

This decreasing gap between male and female longevity has contributed to an increase in the prevalence of couple rather than single households among those aged 65 years and over (figure 3.3). This change may have important implications for housing decisions. For example, lack of an informal carer at home can be a driver of entry into residential aged care.

Figure 3.3 Couple-only and lone-person households^a
2000-01 and 2013-14



^a Age of household is defined as age of household reference person.

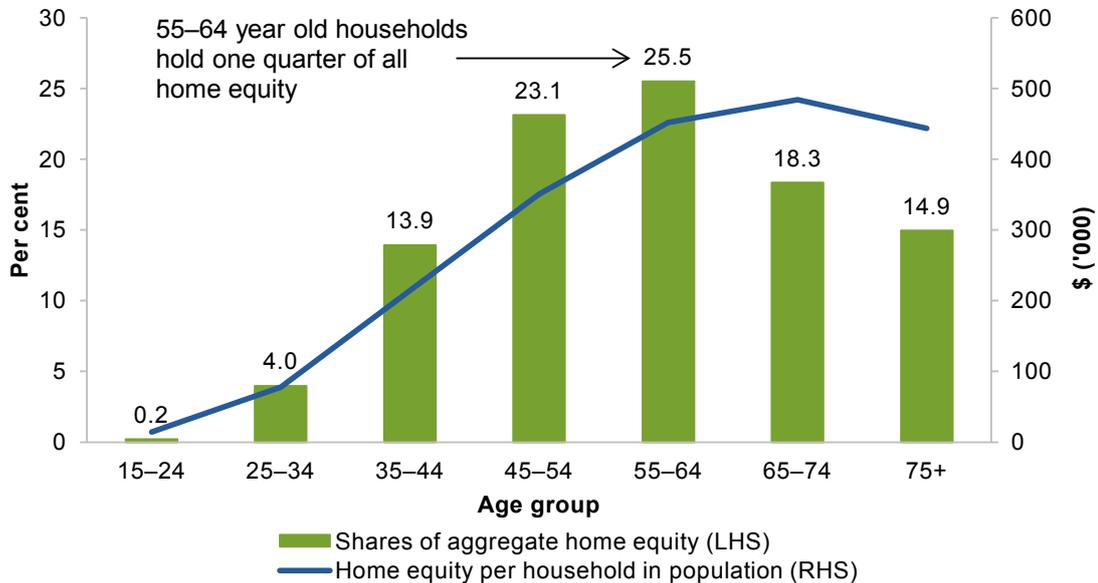
Sources: Productivity Commission estimates based on ABS (*Household Income and Wealth, Australia, 2013-14*, Cat. no. 6523.0; *Survey of Income and Housing Costs, Australia, 2000-01 Basic CURF*, Cat. no. 6541.0.30.001).

Older Australians own a large share of total housing wealth

Older Australians, as a group, hold a large share of overall home equity (aggregate value of home assets less aggregate value of home debt). In 2011-12, households aged 55 years and over held almost 59 per cent of total home equity, with over 40 per cent of this share attributable to households aged 55 to 64 years (figure 3.4). Home equity per household in the population was highest for households aged 65 to 74 years, averaging about \$480 000 (in 2011-12).⁵

⁵ Mean home equity — calculated by dividing aggregate home equity across 65–74 year old households by the number of 65–74 year old households in the population (per the 2011 Census). As a comparison, median home equity for this age group in 2011-12 was \$380 000 (ABS 2013b).

Figure 3.4 Shares of aggregate value of home equity, by age group^{a,b}
2011-12



^a Home equity for each age group is calculated as aggregate home assets (value of owner-occupied dwelling) less aggregate home debt (value of all loans secured against that dwelling). ^b Age of household is defined as age of household reference person.

Source: Productivity Commission estimates based on ABS (*Survey of Income and Housing, Australia, 2011-12 Basic CURF*, Cat. no. 6541.0.30.001).

3.2 Housing as a store of wealth

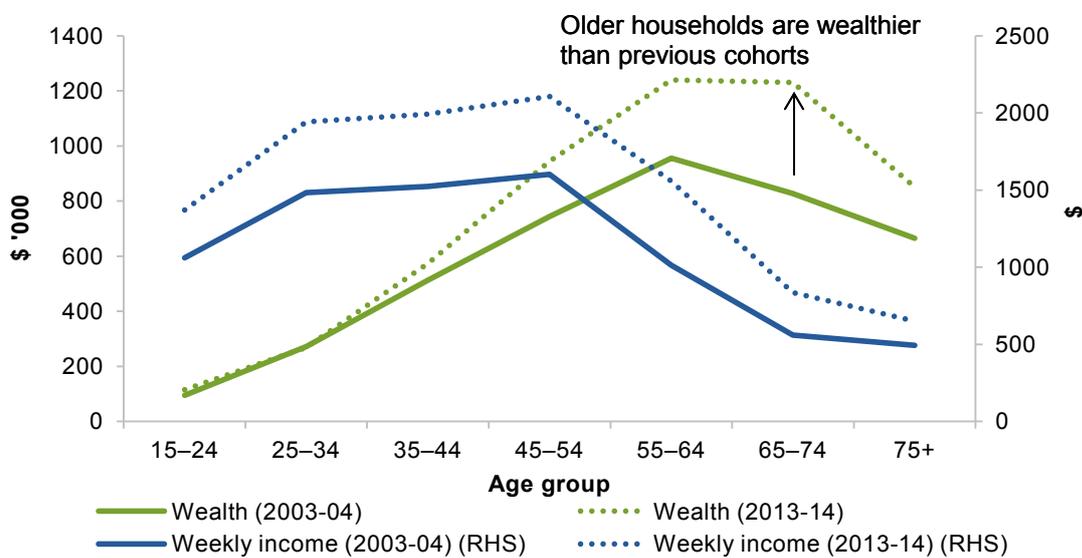
As discussed in chapter 2, housing serves two distinct purposes. Housing can be viewed as an investment good: a store of wealth than can be used as a source of income to fund retirement or leave bequests to future generations. At the same time, housing is a consumption good, meaning that it provides shelter and accommodates people’s physical, emotional, social and familial needs, which change as they age. The first of these dimensions is considered in this section, while the second is discussed in section 3.3.

Along with the Age Pension and private savings (including superannuation), housing wealth is one of the three potential sources of income from which older households can pay for their retirement, including their living expenses and care needs. The interrelatedness of financial and housing decisions means that housing must be viewed in the context of how incomes, assets, expenditure and saving change over the life cycle.

Older households tend to be ‘asset rich, income poor’

Older Australians are generally wealthier, but with lower incomes, than their younger counterparts, and wealthier than their counterparts a decade earlier (figure 3.5). Previous research has attributed this improvement in the wealth position of older households to factors including higher incomes, rising house prices and a tax and transfer system that is favourable to older people (Daley et al. 2014).

Figure 3.5 **Average household income and wealth, by age group^{a,b}**
2003-04 and 2013-14

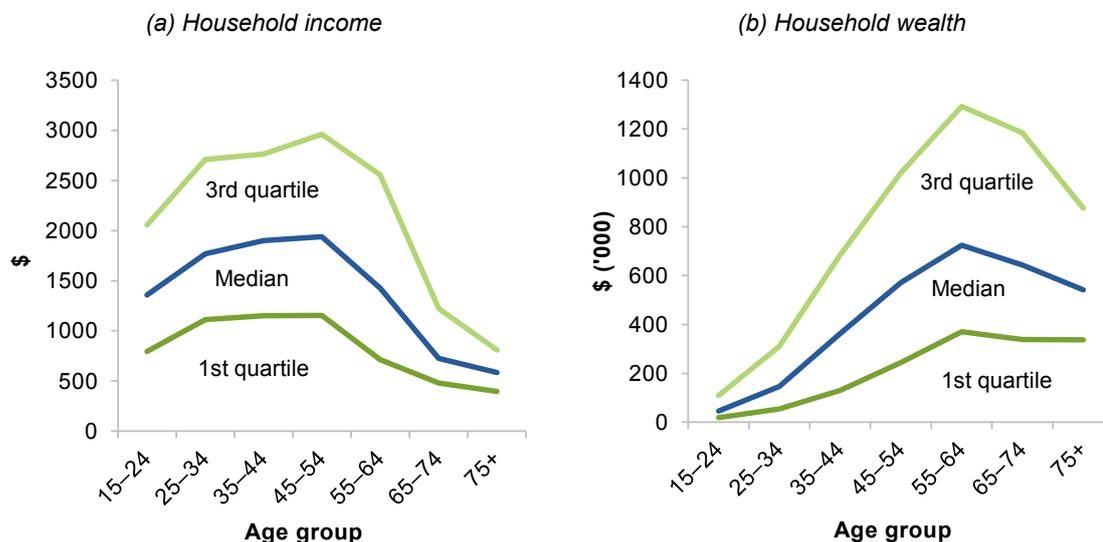


^a 2013-14 dollars (2003-04 figures adjusted using the GDP implicit price deflator for household final consumption expenditure). Wealth is defined as the ‘household net wealth’ variable in the Survey of Income and Housing (2003-04) and ‘net worth of household’ in 2013-14. Observations are only captured if values are positive or equal to zero. ^b Age of household is defined as age of household reference person.

Sources: Productivity Commission estimates based on ABS (*Household Income and Wealth, Australia, 2013-14*, Cat. no. 6523.0; *National Accounts: National Income, Expenditure and Product*, Cat. no. 5206.0; *Survey of Income and Housing, Australia, 2003-04 Basic CURF*, Cat. no. 6541.0.30.001).

Older households typically have higher asset values and lower debt levels than younger and middle-aged households (annex, figure 3.30). This pattern is primarily driven by the accumulation of and subsequent reduction in home debt over the life course, as many older households are able to pay off their mortgages and become outright home owners (annex, figure 3.31). The gradual accumulation of household wealth over the life course is reflected in the increasing dispersion in the distribution of wealth among older age groups (whereas income is more dispersed among younger age groups) (figure 3.6).

Figure 3.6 **Distribution of household income and wealth^{a,b}**
2011-12



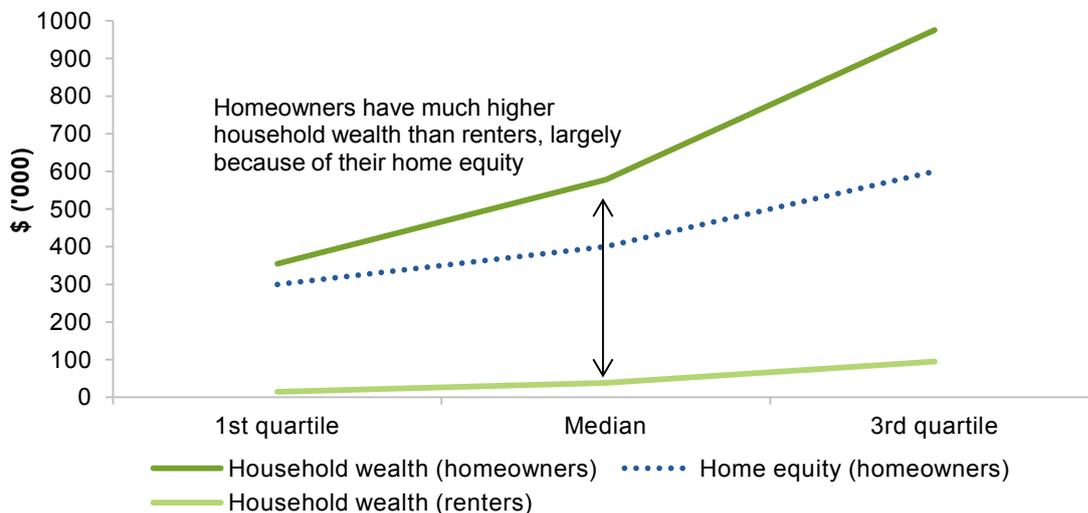
^a Observations are only captured if values are positive or equal to zero. ^b Age of household is defined as age of household reference person.

Source: Productivity Commission estimates based on ABS (*Survey of Income and Housing, Australia, 2011-12 Basic CURF*, Cat. no. 6541.0.30.001).

Although households across all age groups have a large share of their wealth in their homes, this is even more so for older home owners. The importance of home equity in household wealth for older households means that the minority of households aged 65 years and older who are renting have far lower levels of household wealth compared to home owners (figure 3.7).

On the other hand, older households have lower private incomes than their younger and middle-aged counterparts, and many are substantially reliant on the Age Pension. Whereas wage and salary income is the main source of household income for the majority of young and middle-aged households, this changes dramatically for those aged over 55 years. Most households aged 65 years and older rely on government pensions and allowances as their main source of income (figure 3.8). Further discussion of the Age Pension and its recipients is contained in chapter 5. High rates of involuntary retirement — about 42 per cent of Australians aged 55–64 years in 2011 retired for reasons they cannot control — can also lead to lower income and wealth in older households. Further, people who retire involuntarily often have lower levels of education and work in particular industries (such as telecommunications, retail/wholesale trade and manufacturing) (PC 2015b).

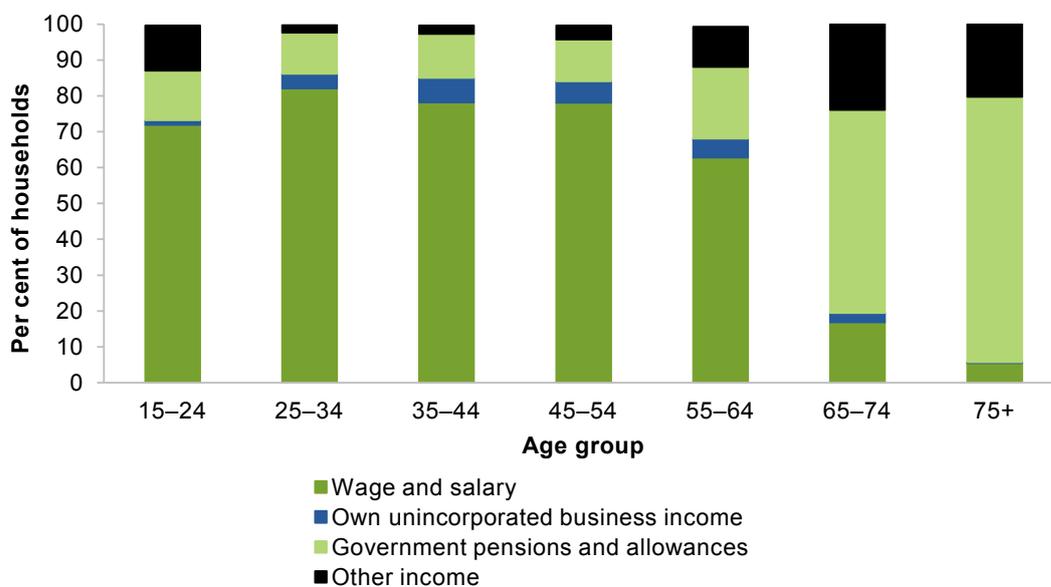
Figure 3.7 Distribution of wealth, 65+ households^a by tenure type
2011-12



^a Age of household is defined as age of household reference person.

Source: Productivity Commission estimates based on ABS (*Survey of Income and Housing, Australia, 2011-12 Basic CURF*, Cat. no. 6541.0.30.001).

Figure 3.8 Main source of weekly household income, by age group^{a,b}
2011-12



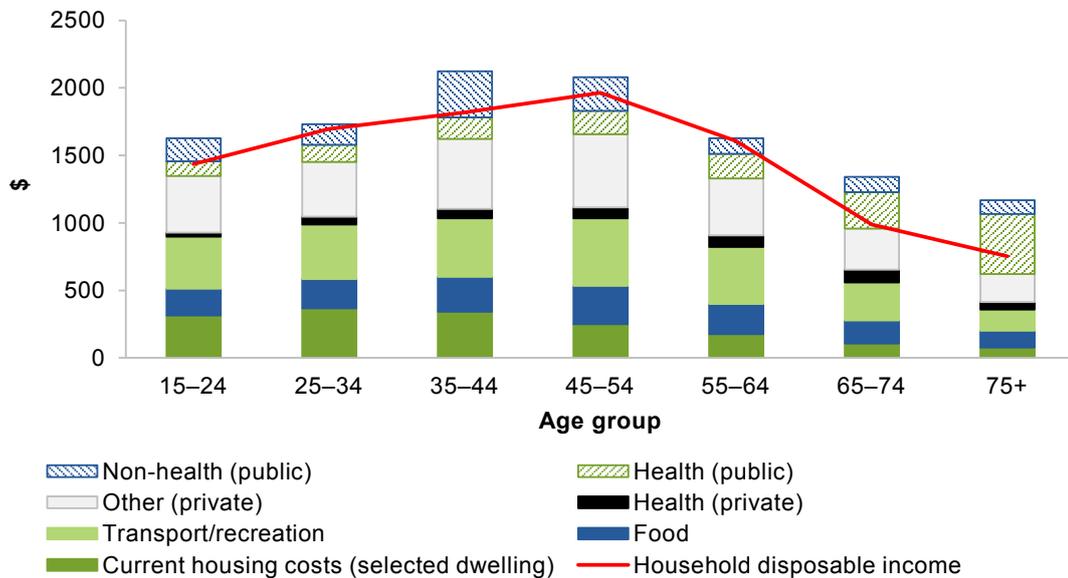
^a Observations are only captured if income is positive. ^b Age of household is defined as age of household reference person.

Source: Productivity Commission estimates based on ABS (*Survey of Income and Housing, Australia, 2011-12 Basic CURF*, Cat. no. 6541.0.30.001).

Expenditure patterns and levels change with age

Older Australian households spend less, on average, than do their younger counterparts. However, the increase in private expenditure on health and medical care associated with older households is modest compared with the increase in public health care expenditure (figure 3.9). Publicly-funded expenditure on health for households aged 75 years and over accounted for 38 per cent of all average weekly household consumption by this age group, compared to 20 per cent for 65–74 year old households — reflecting the significant increase in the cost of health services associated with ageing (PC 2013).

Figure 3.9 **Average weekly household consumption, expenditure and income, by age group^{a,b}**
2009-10



^a Age of household is defined as age of household reference person. ^b 2013-14 dollars (2009-10 figures adjusted using the GDP implicit price deflator for household final consumption expenditure). Observations are only captured if expenditure in a category is positive or equal to zero. **Food** includes non-alcoholic beverages. **Health (private)** is household expenditure on medical care and health expenses. **Other (private)** is household expenditure on other goods and services, besides housing costs, food, transport, recreation and health and medical expenditure. **Health (public)** is social transfers in kind for health. **Non-health (public)** is social transfers in kind (excluding for health).

Sources: Productivity Commission estimates based on ABS (*Household Expenditure Survey and Survey of Income and Housing, Australia, 2009-10*, Cat. no. 6540.0; *National Accounts: National Income, Expenditure and Product*, Cat. no. 5206.0).

Household expenditure on almost all categories of goods and services decreases with age (figure 3.9). Older households typically spend less on housing costs⁶, transport and recreation, whereas food and health care account for a higher proportion of their overall expenditure. Because the majority of older Australian households own their homes outright, their housing costs are typically very low, yet they enjoy the benefits from continuing to live in their homes. These benefits, less housing costs, can be estimated as ‘net imputed rent’. This source of value (relative to overall household expenditure) becomes markedly more important with increasing age (annex, figure 3.32).

Older households are slow to draw down on their wealth

Evidence from other studies suggests that age pensioners generally preserve wealth in old age, spending cautiously and even continuing to save, with the result being that many leave substantial bequests. A longitudinal analysis of Centrelink records found that age pensioners typically drew down about 2.5 per cent of their wealth per year until death (Wu et al. 2015). The study found that wealthier pensioners generally decumulated assets in early retirement but tended to accumulate in later life, and lower wealth pensioners began accumulating (net savers) early on. The study also found that the median pensioner who passed away during the survey period (1999–2007) left residual wealth equal to 90 per cent of the amount recorded at first observation (Wu et al. 2015). This tendency to run down household wealth slowly in older age — rather than more rapidly towards the end of life, as might be predicted by life cycle theory (chapter 2) — is reflected in the relatively strong wealth positions of even the oldest households.

Drawing on home equity is often a last resort

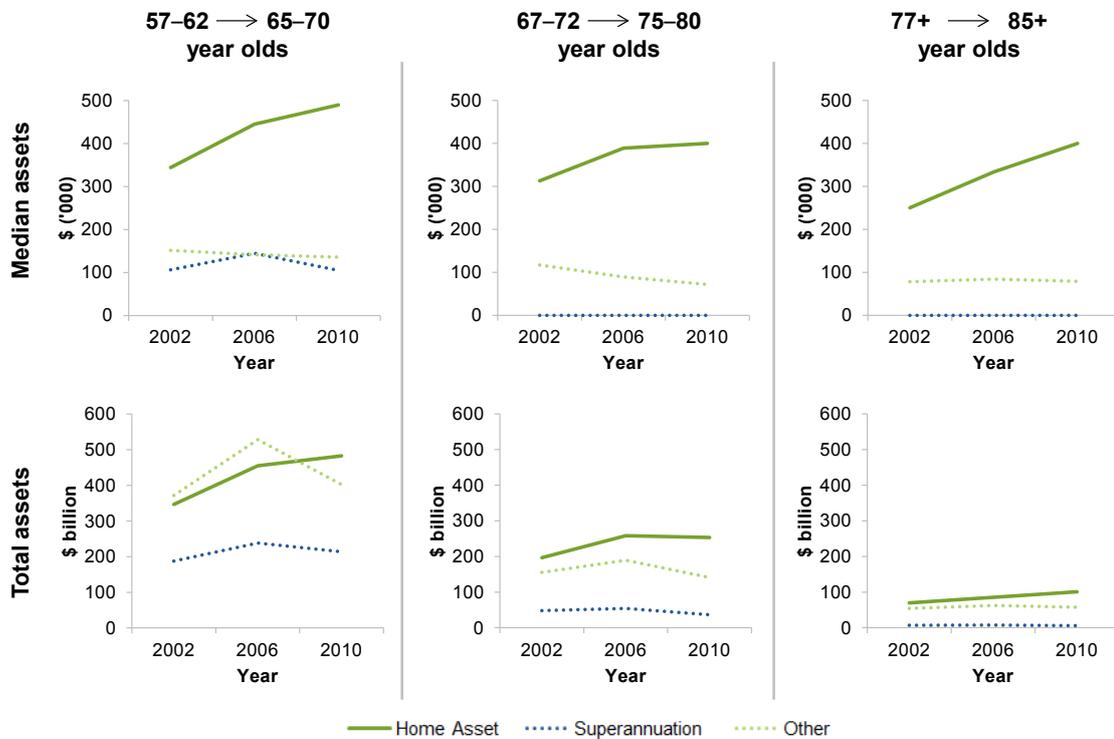
There are several mechanisms for drawing on housing wealth in old age. These include:

- selling the home either in whole or part
- renting out the home
- drawing down equity using a financial equity release product.

Home equity makes up a greater proportion of wealth for older people than for their younger counterparts, and its proportion significantly increases with age. It appears that when Australian retirees (both younger and older) do draw down their wealth, they are more likely to do so through other assets, and preserve their home equity (figure 3.10). Home equity is typically accessed as a last resort (figure 3.11).

⁶ ‘Housing costs’ refers to recurrent expenditure by households in providing shelter for themselves. For home owners, this includes mortgage repayments, council and water rates and body corporate fees, whereas for renters it covers rent payments (ABS 2013a). Housing costs are distinct from the concept of ‘imputed rent’, which refers to the estimated benefits (value) that accrue to owner-occupiers from living in their dwelling (rather than renting it out). Net imputed rent refers to these benefits (imputed rent) minus the costs (housing costs).

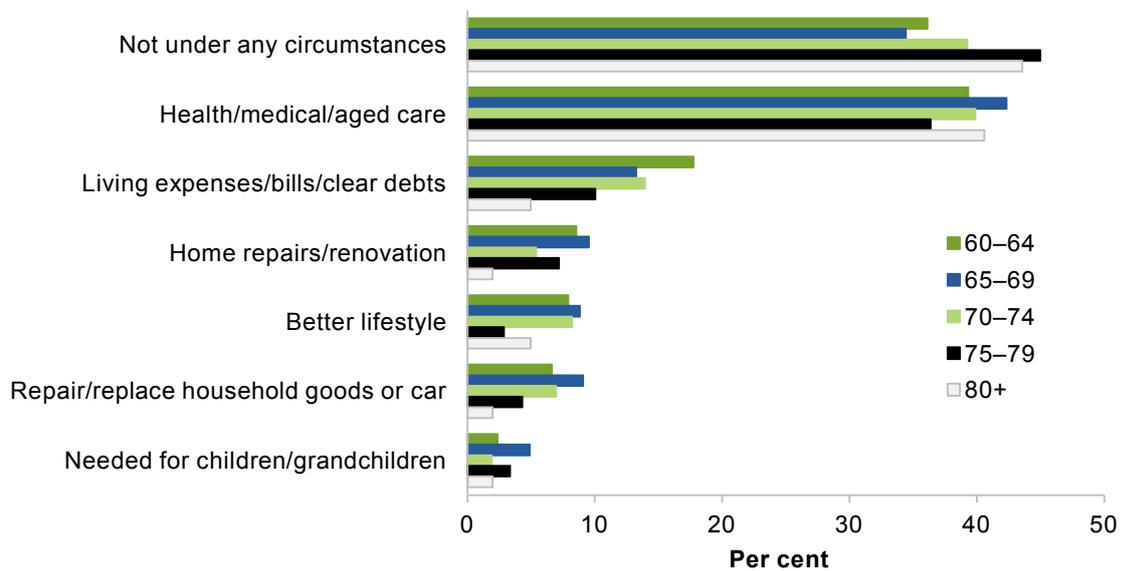
Figure 3.10 **Change in assets of cohorts over stages of retirement^{a,b,c}**
2002–2010



a All years are in 2010 dollars. **b** Other includes other property assets, other financial assets, other non-financial assets and bank accounts. Data are population weighted. **c** In order to utilise wealth data from the HILDA wealth modules available in 2002, 2006 and 2010, a cohort of home owners was followed through each four-year period and their asset values calculated in each year.

Source: Productivity Commission estimates based on HILDA release 13.1, various waves.

Figure 3.11 Older people are reluctant to draw on their home equity
 Under what circumstances would you use your home to fund your retirement?^a



^a Percentages for each age group do not necessarily sum to 100 as respondents could choose more than one option.

Source: Commission survey.

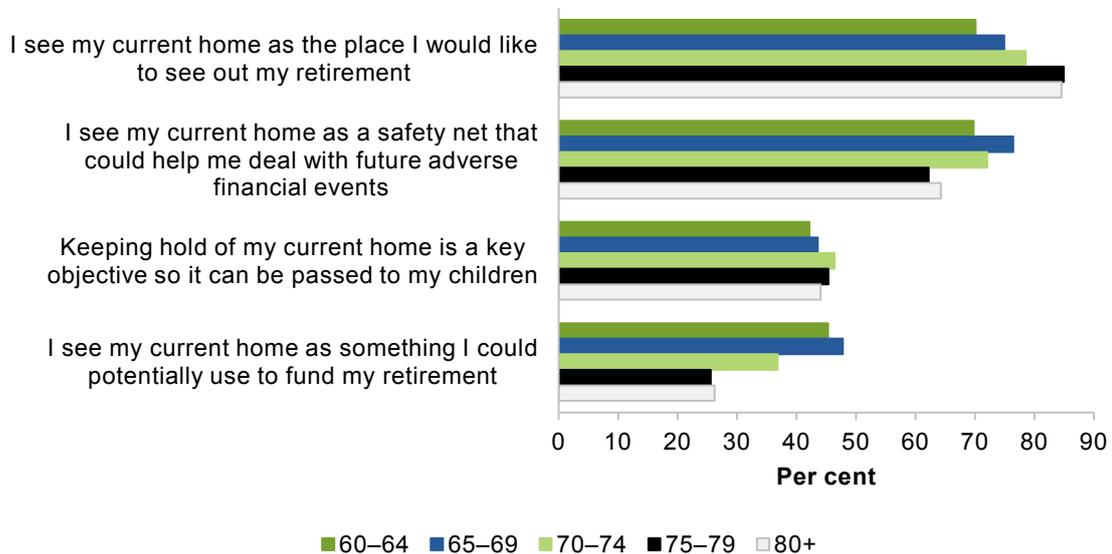
Older Australians tend to refrain from drawing on their housing wealth because of strong attitudes towards the role of the family home. The majority of older Australians prefer to see out their retirement in their current home — a motive that becomes stronger for older age groups — and generally see their home as a financial safety net, rather than a main source of funding their retirement (figure 3.12). The majority of older Australians acknowledge that their current home will not play a role in funding their retirement or have never thought of their home in that way (Commission survey).

When older households choose to avoid drawing down on their equity, or even to add to their wealth by continuing to save, they forgo current consumption. This may be driven by one or both of two key motives (chapter 2):

- precautionary saving — uncertainties about future health and aged care needs and longevity can encourage self-insurance for the ‘rainy days’ ahead
- bequests — a preference to leave wealth to future generations reduces the incentive to draw it down in the person’s own lifetime.

Figure 3.12 **Perceptions of the role of the family home in retirement, 2015**

Do you agree^a with the following?



^a Respondent either somewhat agrees or strongly agrees (4 or 5 out of 5). Responses from home owners only.

Source: Commission survey.

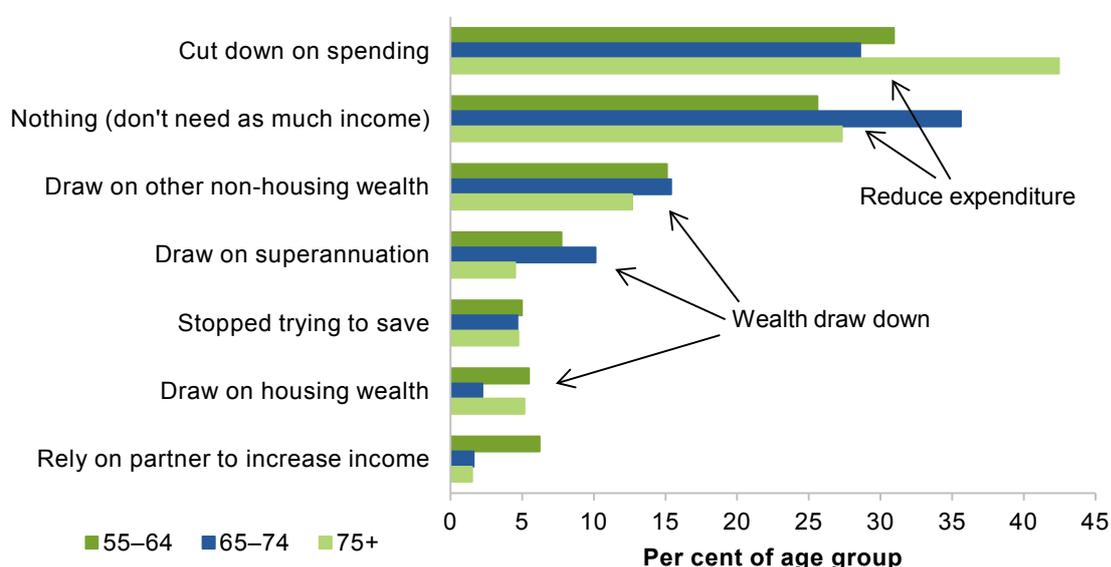
Precautionary saving is a strong motive in old age. Older people may elect to maintain some level of precautionary savings for unintended events, such as adverse health issues or the need to enter residential aged care. Previous research has indicated that many older Australians are very concerned about being able to afford health, medical and aged care costs in later life, as well as the need for sufficient savings to last (and maintain value) for their lifetime (NSA and Challenger 2013). There is a significant chance that older people will require aged care services later in life — about 22 per cent of people aged 85 years and older are users of residential aged care. Further, males (females) aged 65 years today have a 50 per cent (64 per cent) chance of reaching 85 years. Despite this, many older Australians are reluctant to engage financial and other specialist advice or even speak to family members to inform decisions about aged care costs (annex, figure 3.33).

There is also evidence that older home owners who access their home equity by downsizing and ‘selling up’ (rather than by releasing equity via reverse mortgages or similar options) are likely to have been affected by poor health, relationship breakdown or bereavement prior to selling their home (Ong et al. 2013). Based on the Commission survey, almost three quarters of home owners saw their home as a safety net to deal with potential adverse events (figure 3.11).

Given that the family home is generally used as the primary savings vehicle for Australian families, the level of precautionary savings people choose to maintain can affect their housing decisions. For example, people may be over-saving if they continue to live in their

family home, when releasing some equity (through downsizing or an equity release product) could increase consumption and improve wellbeing, while still maintaining adequate precautionary savings. Figure 3.13 shows the methods people have used to cope financially when their income declined as they began to transition into retirement. The majority of people in this situation either cut down on spending or did not need as much income as before.

Figure 3.13 Methods used to cope with reduced income while transitioning to retirement, as a proportion of age group^{a,b,c} 2011



^a This was a multiple response survey question. ^b Some categories have been aggregated: 'Drawing on housing wealth' involves either selling the house or moving to lower cost accommodation. ^c Reduction in income coming about from retiring gradually, such as taking on a job with fewer hours or responsibilities prior to retirement.

Source: Productivity Commission estimates based on HILDA release 13.1, wave 11.

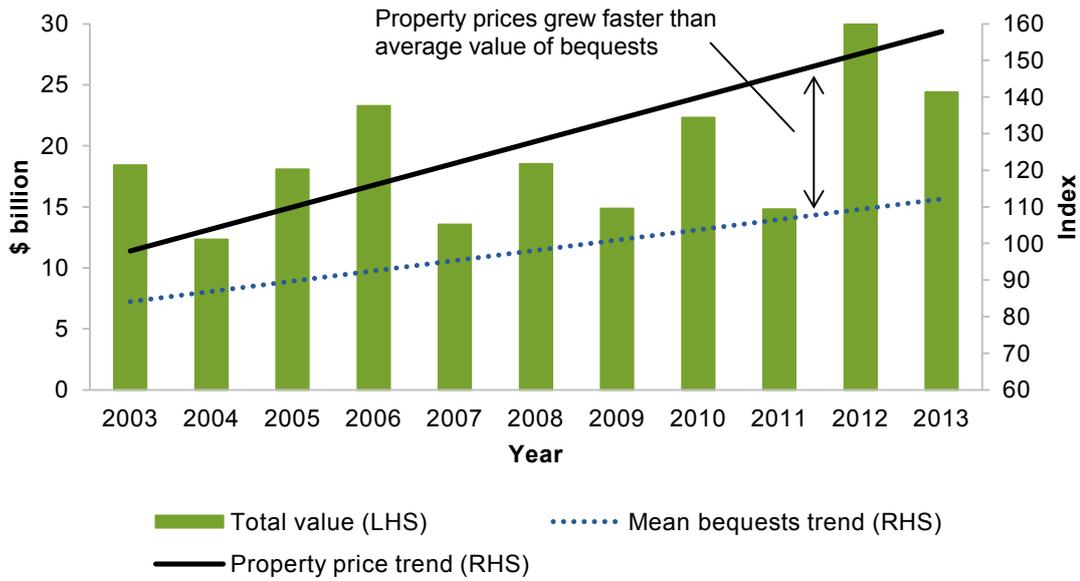
Older Australians are leaving substantial bequests

Some studies have found that the size of bequests is growing (Kelly and Harding 2006; PC 2013). About 69 per cent of Australian retirees plan to leave a bequest, compared with 64 per cent in the United Kingdom or 56 per cent in the United States. While intended and actual outcomes may differ, one study found that the median value of bequests Australian retirees *expected* to leave was more than three times the global average (HSBC 2013).

There has been an increase in the mean value of bequests over time (figure 3.14). The total value of bequests received in Australia grew from \$18 billion to \$24 billion (in

2013 dollars) between 2003 and 2013. Part of this increase in the total value of bequests is likely to come from an increase in property prices over this period.

Figure 3.14 **Real aggregate^a and mean^b bequests, by year**
2003–2013



^a Aggregate value of bequests in 2013 dollars and is population weighted. ^b Mean bequests trend shows the linear trend of the mean value of bequests given. It was calculated using real aggregate values divided by total deaths (less infant deaths) in that year.

Sources: Productivity Commission estimates based on ABS (*Deaths, Australia, 2012*, Cat. no. 3302.0; *Deaths, Australia, 2013*, Cat. no. 3302.0) and HILDA release 13.1, all waves.

When asked about the trade-off between consumption in retirement and leaving bequests, Commission survey results showed that 83 per cent of older Australians prefer having the best possible quality of life in retirement compared to leaving as much as possible to their beneficiaries. Nonetheless, the vast majority of respondents (88 per cent) intended to leave their home for their beneficiaries to inherit.

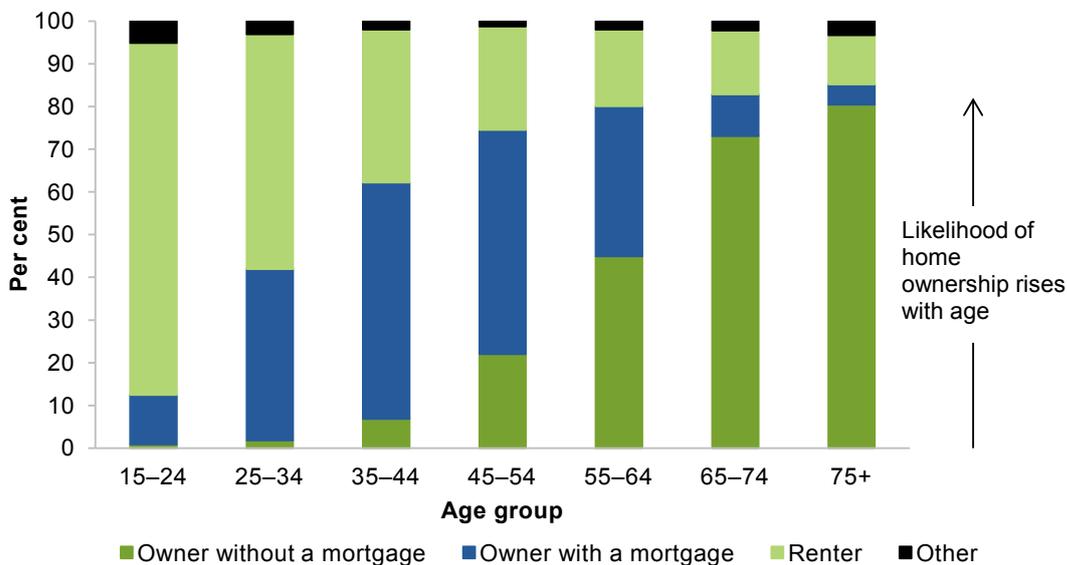
3.3 Housing as a place to live

At the most basic level, housing as a consumption good provides shelter and accommodation. However, the nature of ownership, location and characteristics of housing can have pervasive effects on people’s physical, psychological and social wellbeing.

Most older Australians are home owners, and stay that way

Older households are much more likely to be outright home owners than younger households (figure 3.15). As households age, they tend to transition from being mortgagees to outright owners; eight in ten 75+ households are outright owners. Researchers have noted that many older Australians see home ownership as a crucial factor in enabling their continued independence as they age. For example, a survey by Olsberg and Winters (2005) of home owners aged over 50 years found that most saw home ownership as an investment for the future, and four out of five respondents believed that owning a home gives people freedom to make decisions about their lifestyles.

Figure 3.15 Household tenure type by age group^a
2011-12



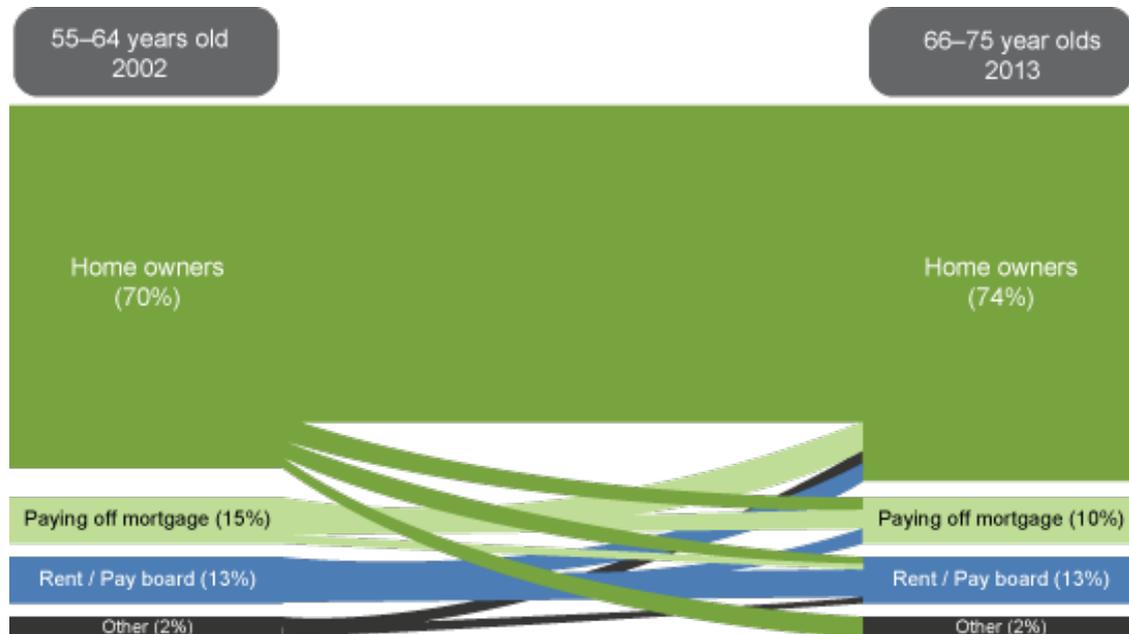
^a Age of household is defined as age of household reference person. **Other** includes households that are not owners or renters, but have another tenure arrangement (including rent free).

Source: Productivity Commission estimates based on ABS (*Survey of Income and Housing, Australia, 2011-12 Basic CURF*, Cat. no. 6541.0.30.001).

Relatively low housing mobility (discussed later in this section) means that households effectively lock in their choice of tenure for substantial periods. The Household, Income and Labour Dynamics in Australia (HILDA) survey was used to perform an analysis of housing tenure transition over eight years for two groups — younger and older retirees — which showed that the majority of older people remained in their original type of accommodation and tenure at the end of the period (figure 3.16).

Figure 3.16 Changes in tenure type^{a,b}, 2002–2013

(a) Younger retirees^c



(b) Older retirees^d



^a Population weighted. Percentages may not add to 100 due to rounding. Ribbons are not included if they represent less than one per cent of the grouping. ‘Other’ includes Rent free/Life tenure, Rent-buy schemes and Not stated. ^b This analysis followed a cohort of individuals through retirement to see how their tenure changed. ^c The cohort was aged between 66–75 years in 2013 so that everyone passed the retirement age threshold of 65 years at some point during the period. ^d The cohort was aged between 81–90 years in 2013 so that everyone passed the age threshold of 80 years at some point during the period.

Source: Productivity Commission estimates based on HILDA release 13.1, all waves.

While the transition away from home ownership accelerated for the older group, it is still not a dominant path even for those who are in their 80s. Notably, the transition from outright home ownership to having a mortgaged property, which would incorporate equity withdrawal through reverse mortgages, was an option elected by a very small proportion of retirees. This path also includes a small proportion of home owners that became mortgagees after moving home and acquiring a more expensive home. In general, over half of all older home owners who take out a mortgage sold up to a more expensive home.

Older renters are a small but vulnerable minority

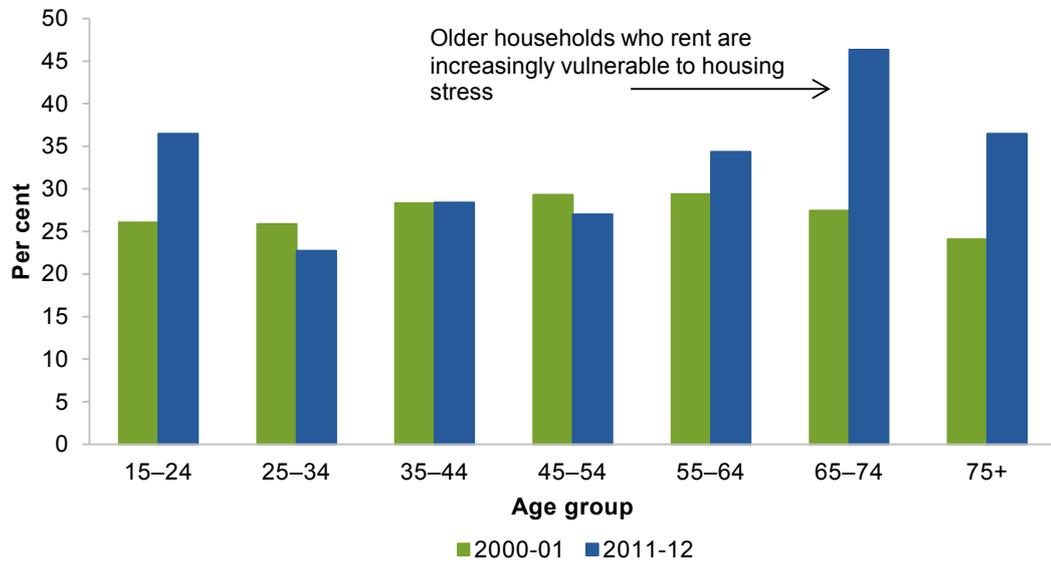
A small but significant minority (about 14 per cent) of older Australian households rent rather than own their homes, and the likelihood of renting increased somewhat among middle-aged (45–54 year old) and pre-retirement (55–64 year old) households between 2001 and 2011 (annex, figure 3.34).

Older renting households are disproportionately likely to be experiencing housing affordability stress (figure 3.17) — where housing costs (rent payments) take up more than 30 per cent of household gross income (Wood, Ong and Cigdem 2014). As noted in previous research, older renters are also likely to be affected by the insecurity of tenure inherent in renting, which can result in:

- detrimental effects on mental health and wellbeing (Olsberg and Winters 2005)
- increased risk of poverty and homelessness (ACOSS 2014)
- fewer options when health, frailty or disability require a transition to age-specific accommodation (Millane 2015).

Older people are also more reliant on public housing than younger renting households — about half of renters older than 75 years are renting publicly (annex, figure 3.35). About 30 per cent of the public housing stock is occupied by people over the age of 65 years (AIHW 2014a). These are largely single person households (about two thirds, depending on the source), and predominantly female. The over-representation of older women in public housing likely reflects the higher life expectancy for women and traditionally lower economic participation by women. About half of older public housing tenants have had a tenure of over 10 years (McNeils 2007).

Figure 3.17 **Renters — incidence of housing affordability stress^{a,b}**
2000-01 and 2011-12

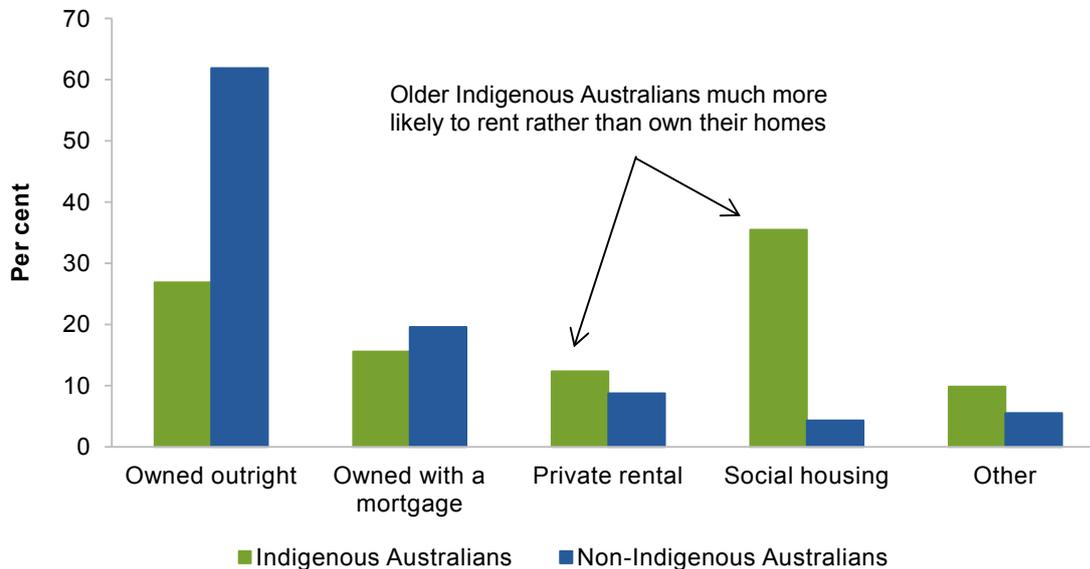


^a Defined as a situation where housing costs exceed 30 per cent of gross household income. ^b Age of household is defined as age of household reference person.

Sources: Productivity Commission estimates based on ABS (*Survey of Income and Housing, Australia, 2011-12 Basic CURF*, Cat. no. 6541.0.30.001; *Survey of Income and Housing Costs, Australia, 2000-01 Basic CURF*, Cat. no. 6541.0.30.001).

Older Indigenous Australians are also much more likely to be renting than their non-Indigenous counterparts. Nearly half of Indigenous Australians aged over 55 years are renting, compared with 13 per cent among the non-Indigenous population. Older Indigenous Australians are far more likely to be in public housing (figure 3.18). This means older Indigenous Australians are likely to be disproportionately affected by the disadvantages that face older renters.

Figure 3.18 **Housing tenure, Australians aged 55+, by Indigenous status^a**
2011



^a **Social housing** Renting from a state or territory housing authority (public housing) or from a housing co-operative, community or church group. **Other** includes people who did not specify the type of landlord or tenure, and other tenure types such as residential park, housing provided by employers and life tenure schemes.

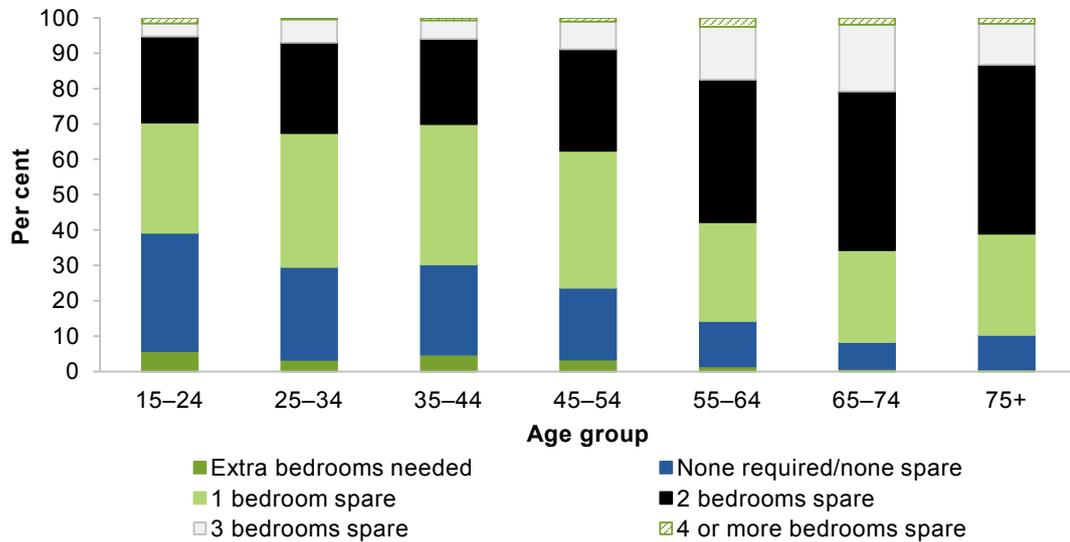
Source: Productivity Commission estimates based on ABS (*Census of Population and Housing, 2011*, Cat. no. 2037.0.30.001).

Many older people live as couples or alone, in ‘family-sized’ homes

The typical older Australian household consists of a couple or a single person living alone — these two household types increase in prevalence for older age groups (annex, figure 3.36). About three quarters of those aged over 75 years live in detached houses (annex, figure 3.37), and a similar proportion live in residences with at least three bedrooms. Indeed, one-third of 55–64 year olds and almost one quarter of 65–74 year olds lived in homes with four or more bedrooms in 2011, significant increases on the proportions for those age groups in 2001 (annex, figure 3.38). This translates to many older households having multiple ‘spare’ bedrooms (as defined under the Canadian National Occupancy Standard⁷) (figure 3.19). This general pattern contrasts with the experience of many older Indigenous Australians, who are more likely to be affected by poor housing conditions and overcrowding than non-Indigenous Australians (AIHW 2014b).

⁷ A measure of housing utilisation, this standard assesses how many bedrooms a household needs or has spare (or whether there are ‘none required, none spare’) by applying a set of criteria that determine a reasonable number of bedrooms appropriate for a given family size and composition (ABS 2013a).

Figure 3.19 Housing utilisation, by household age group^a
Households by Canadian National Occupancy Standard, 2011-12



^a Age of household is defined as age of household reference person.

Source: Productivity Commission estimates based on ABS (*Survey of Income and Housing, Australia, 2011-12 Basic CURF*, Cat. no. 6541.0.30.001).

However, previous research has indicated that older households often use spare bedrooms for home offices, accommodation for relatives, and for hobbies and storage (Judd et al. 2010). More generally, survey evidence from previous studies has shown that most older home owners are happy with their current dwelling. Judd et al. (2010) reported that 90 per cent of home owners surveyed believed their home to be suitable for their needs. This may be as much because of the location of the dwelling as the house itself: Olsberg and Winters (2005) found that most older people regarded pleasure and familiarity with their local area as the most important reason for preferring to stay in their current dwelling, with a much smaller proportion emphasising emotional attachment to the home itself.

Older home owners are more likely to be satisfied with their current dwelling than older renters — the Australian Institute of Health and Welfare (AIHW 2013b) reported that about 60 per cent of home owners rated their satisfaction with their home at least 8 out of 10, compared with 46 per cent among private renters and 40 per cent among those in social housing. However, stakeholder consultation for this study raised the point that many older people are satisfied with their dwelling until an ‘event’ (commonly, a fall) occurs. This can lead to a reconsideration of the suitability of the current dwelling and possible alternatives that might better meet the household’s changing needs.

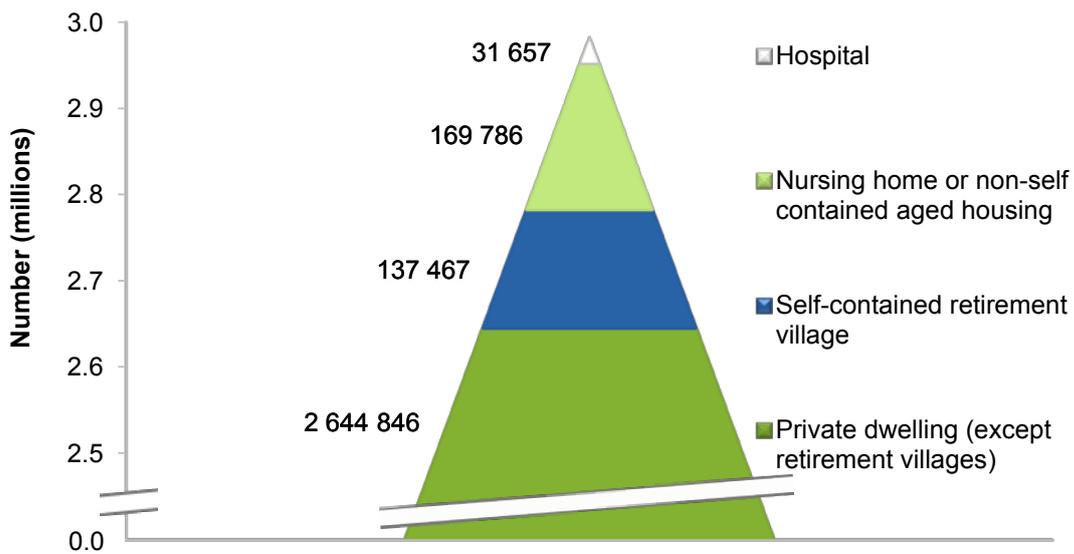
Older couple households are more likely (compared to older lone-person households) to stay in their current home rather than move house (discussed below). Living as a couple might delay a move by either person to residential aged care as they are likely to have

greater access to informal care from their partner. Age-specific housing options are discussed further in chapter 4.

People strongly prefer to age in place

The vast majority of older Australians live in private dwellings (figure 3.20, and figure 4.1 in chapter 4).⁸ Survey data show that older households strongly prefer to age in place as long as practical. For example, the Commission survey found that 83 per cent of people aged 60 years or more saw living in their own home as their preferred living arrangement. A minority, increasing with age, expressed a preference to live in a retirement village. As noted earlier, three quarters of survey respondents agreed or strongly agreed that they saw their home as the place they wished to see out their retirement (figure 3.12).

Figure 3.20 **Persons aged 65+ living in private and non-private dwellings^a**
2011



^a Figure excludes ‘other’ dwellings, which include other non-private dwellings (various categories), as well as other dwellings (migratory, offshore and shipping dwellings). **Hospital** includes public hospitals, private hospitals, and psychiatric hospitals and institutions.

Source: Productivity Commission estimates based on ABS (2011 *TableBuilder Basic*, Cat. no. 2072.0).

Housing mobility declines with age: less than 8 per cent of households aged 55 years and over moved in 2010, a much lower proportion than among younger households (annex,

⁸ Private dwellings can consist of a house, flat, or room, or even a caravan, houseboat, tent, or dwelling attached to an office or shop. They also include self-contained retirement villages. Private dwellings are distinct from non-private dwellings, which provide a communal or transitory type of accommodation (ABS 2011). People living in private dwellings may have different tenure types — they may be owning or renting the dwelling.

figure 3.39). The primary reasons for not selling the family home are a very strong desire to age in place and the lack of suitable downsizing options (annex, figure 3.40). The preference to age in place is not unique to Australia — the phenomenon has been noted overseas, such as in New Zealand, the United States and the European Union (Davey 2006; Farber and Shinkle 2011; Mestheneos 2011). Recent Commission work showed that Australia's residential mobility across all ages is relatively high by international standards, but broadly similar to comparable English-speaking countries (PC 2014).

Older people move home for health, family and financial reasons

The decision to move can be motivated by 'pull' factors (such as being closer to friends and family or better lifestyle) or 'push' factors (such as ill health, loss of a spouse, or financial considerations) (Kendig, Clemson and Mackenzie 2012).

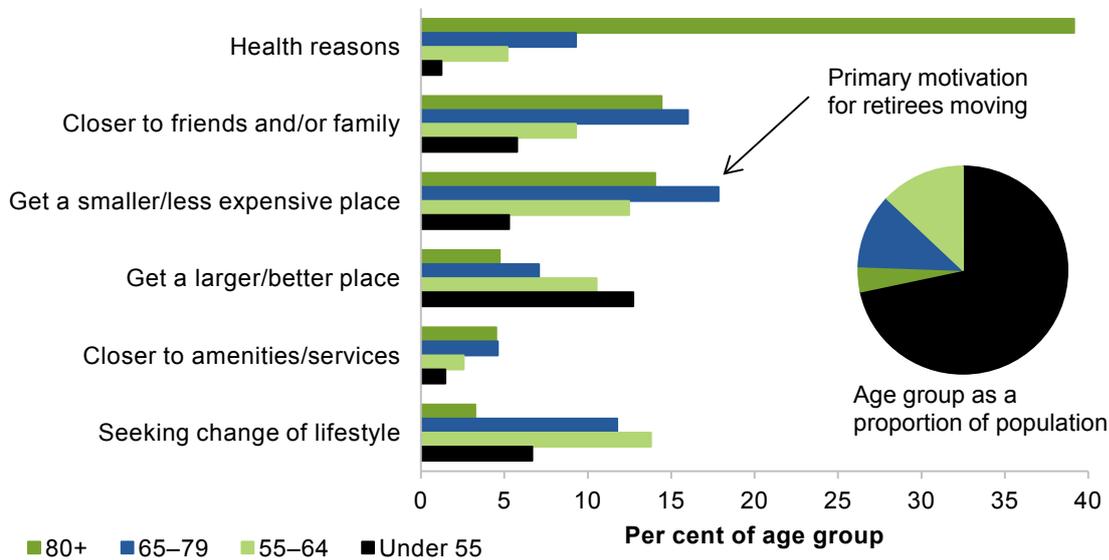
The older households that do move tend to have some common characteristics that could shed some light on the push and pull factors affecting housing mobility of the aged, as revealed in analysis based on HILDA data.

- **Renters are more likely to move.** Older households that rent are about four times as likely to move as those that own their homes outright — 12 per cent of renters moved in 2010 compared to just 3 per cent of outright home owners. This is likely due to lower security of tenure for renting households.
- **A lone person is more likely to move.** Ageing in place may be more difficult for people who do not have partners to assist them in old age and this may precipitate a move into age-specific accommodation. About 7 per cent of older lone person households moved in 2010, compared to 4 per cent of people from couple households.
- **Older households tend to move greater distances.** Households in which the reference person is aged 75 years and over generally move further than younger households. Almost three quarters of these households moved more than 10 kilometres to their next home in 2010, compared to under half of all households in younger age groups. The availability of suitable housing in the local area may be one of the drivers of this outcome.

Survey data show a variety of reasons for moving in old age. The relative importance of those factors can differ substantially between age subgroups (figure 3.21). Older people tend to move home for health reasons, to be closer to friends and family, or to get a smaller or less expensive place. This accords with other research showing that downsizing is a strong motive for moving house among those older people who do move (Judd et al. 2014).

Downsizing is also an option used by older people to improve their financial position. Analysis of HILDA showed that in 2011, about 5 per cent of older people who had to make some kind of decision as a result of their financial circumstances sold their house or moved to lower cost accommodation as a result.

Figure 3.21 Top reasons people move home^{a,b}
2002–2013



^a Multiple response question. ^b Population weighted.

Source: Productivity Commission estimates based on HILDA release 13.1, all waves.

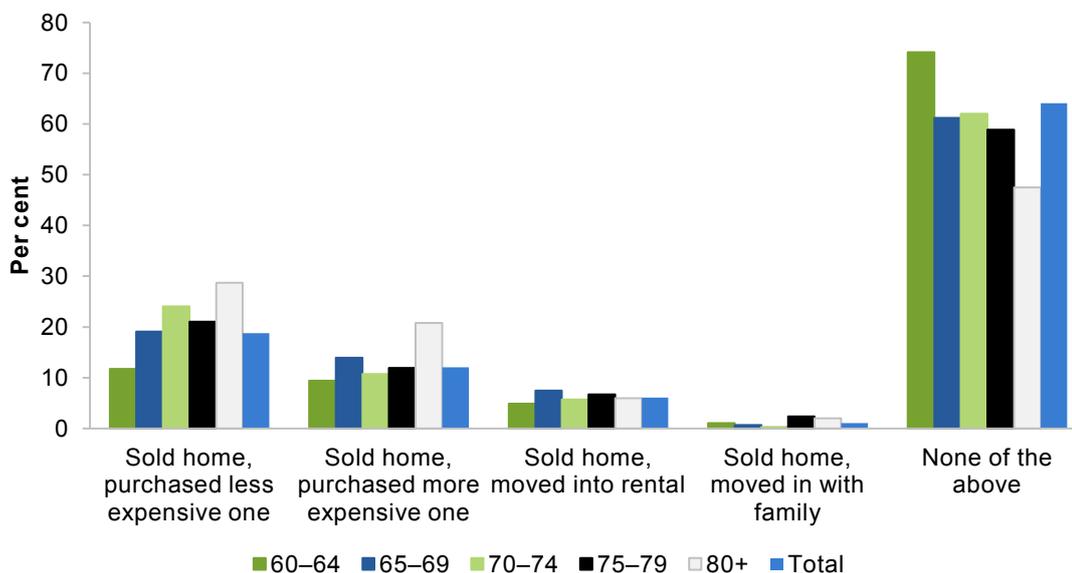
Older home owners are more likely to move into less expensive accommodation

Evidence from the Commission survey indicates some housing mobility among older Australians, mostly in the form of ‘down valuing’ — selling the home to purchase a less expensive one (figure 3.22). (This may not entirely correspond to downsizing, in that a smaller dwelling may not always be a less expensive one, and vice-versa.) Relatively few older people reported having sold their property to move into rental accommodation or move in with family.

Of the 19 per cent of all respondents in the survey who reported having sold their property and purchased a less expensive one since turning 50 years old, most had done so relatively early in retirement — by their mid-60s. Only 16 per cent of those older home owners who had not down valued since turning 50, reported being very likely to do so in the future.

Figure 3.22 Proportion of older people who sold their home and moved since turning 50 years of age^a

Persons aged 60 years and over



^a Respondents were asked to answer the following question: ‘Since turning 50 have you done any of the following?’ (1) Sold the property in which you live and purchased a less expensive one; (2) Sold the property in which you live and purchased a more expensive one; (3) Sold the property in which you live and moved into a rental property; (4) Sold the property in which you live and moved in with children/family; (5) None of the above.

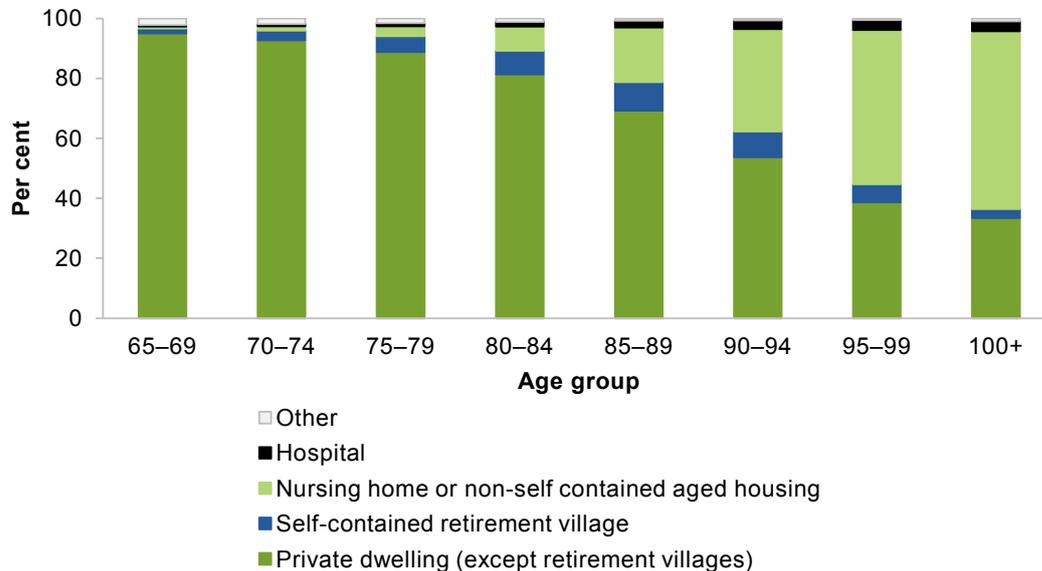
Source: Commission survey.

Residential aged care is increasingly an end-of-life option

Moving to age-specific accommodation — including retirement villages, residential aged care and other retired or aged accommodation⁹ — tends to occur relatively late in people’s lives (chapter 4). Living in residential aged care becomes increasingly likely as people age, though a substantial proportion of older people stay in private dwellings even into very old age (figure 3.23).

⁹ The Census uses the terminology ‘nursing homes’ and ‘accommodation for the retired or aged (not self-contained)’, with the latter referring to communal-style accommodation ‘provided for retired or aged people who are generally in good health and capable of looking after themselves’ (ABS 2011). However, except where referring to Census data, the term ‘residential aged care’ is used in this report to refer to non-private, age-specific accommodation in which residents receive ongoing care. Forms of age-specific housing are discussed in greater detail in chapter 4.

Figure 3.23 Older people in private and non-private dwellings
2011



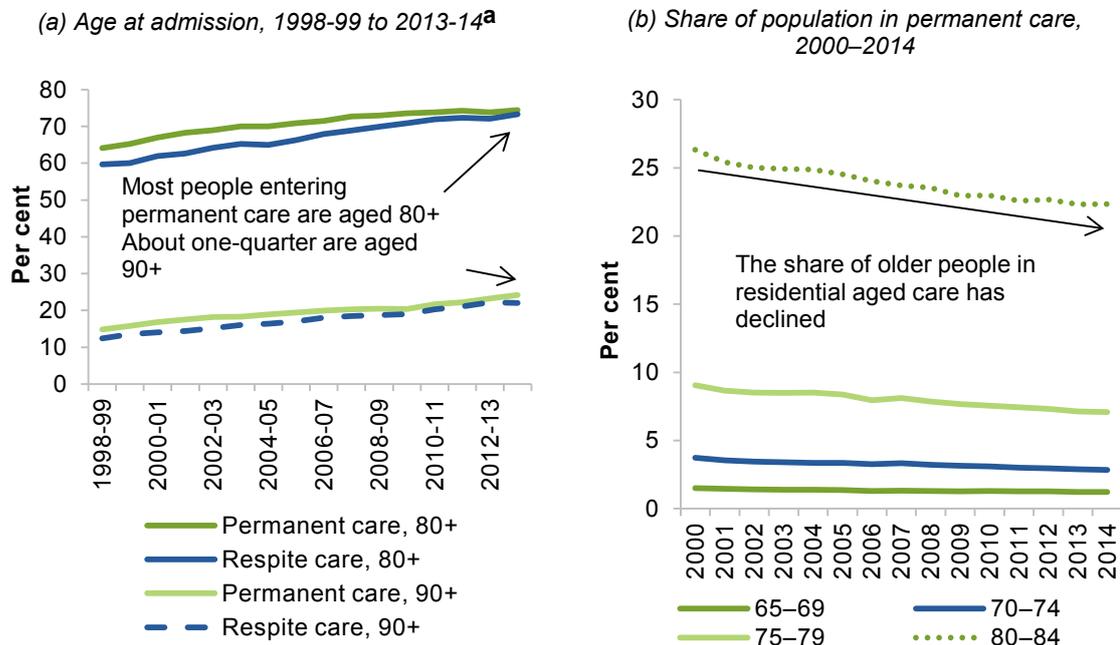
Hospital Includes public hospitals, private hospitals, and psychiatric hospitals and institutions. **Other** Includes both other non-private dwellings (various categories), as well as other dwellings (migratory, offshore and shipping dwellings).

Source: Productivity Commission estimates based on ABS (2011 TableBuilder Basic, Cat. no. 2072.0).

The age of admission into residential aged care has been steadily increasing, making it largely the preserve of people aged 80 years or more (figure 3.24, panel a). These data accord with other studies indicating the vast majority of older Australians prefer to remain in their own homes for as long as practical. Fewer older people (as a proportion of the population) are moving into residential aged care (figure 3.24, panel b), and those who enter aged care do so later in life.

One reason for this trend is the strong growth in home and community care services (AIHW 2014c). People whose needs might in the past have resulted in early entry to low-level aged care are instead choosing to stay in their homes and access community care services, holding off on aged care facilities as a last resort for high level care (Judd et al. 2010; Olsberg and Winters 2005; PC 2011).

Figure 3.24 Trends in residential aged care use



^a Transfers are excluded from admissions.

Sources: Productivity Commission estimates based on AIHW (2012, 2013a, 2014d, 2015).

Another driver is older people's strong and growing resistance to the use of residential aged care. Many fear that their care needs will not be met, particularly those who have witnessed the negative experiences of their own friends and family in such facilities (Judd et al. 2010). Most people do not wish to go into an aged care facility unless it is absolutely necessary, and would prefer to receive care in their own home. They are only willing to seriously consider residential aged care in extreme circumstances; generally when they become completely incapable of looking after their own health and safety (Bupa 2012). The increased incidence of couple households in older age groups may also help to delay entry into residential aged care, by making it easier to remain in the family home.

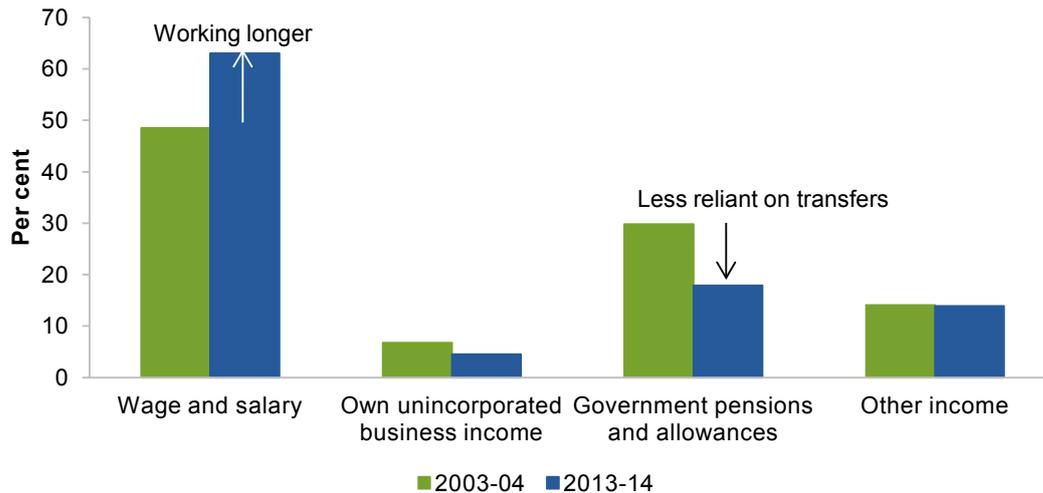
According to the Commission survey, less than 8 per cent of people aged 60 years and over believe it is very likely that they will ever move into residential aged care. Of the 21 per cent of respondents who rated this outcome as at least somewhat likely, most did not expect to enter residential aged care for another ten or more years (Commission survey). Age-specific housing is discussed further in chapter 4.

Some generational changes are occurring

There is evidence suggesting that recent cohorts of retirees behave differently than their predecessors in key respects. Compared to equivalent-aged households in 2003-04, households aged 55-64 years in 2013-14 are more likely to be drawing income from

wages, salaries or business, and less likely to be relying on government pensions and allowances as their main source of income (figure 3.25).

Figure 3.25 Main source of weekly household income, 55–64 year old households^{a,b}
2003-04 and 2013-14



^a Does not include households with zero or negative income. ^b Age of household is defined as age of household reference person.

Sources: Productivity Commission estimates based on ABS (*Household Income and Wealth, Australia, 2013-14*, Cat. no. 6523.0; *Survey of Income and Housing, Australia, 2003-04 Basic CURF*, Cat. no. 6541.0.30.001).

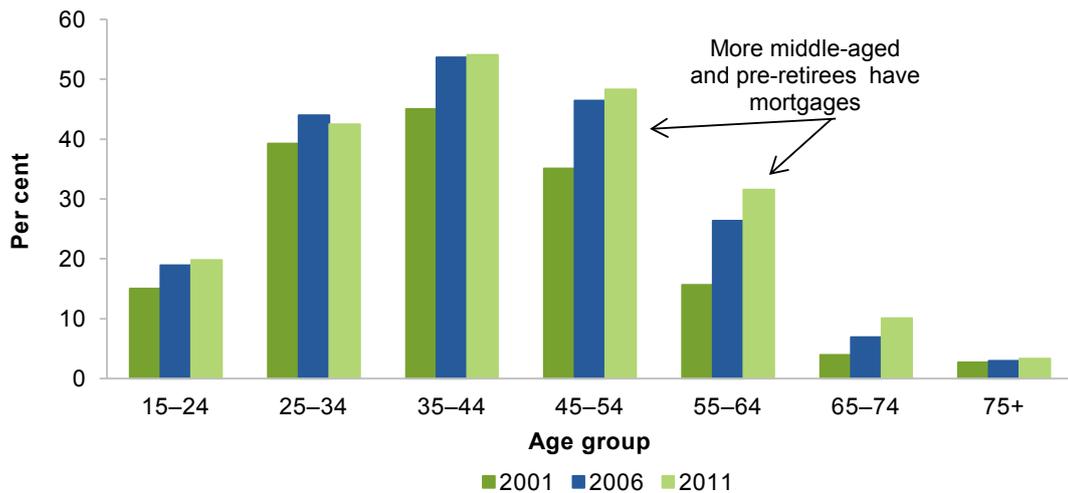
This cohort is more likely to be working longer than the equivalent-aged households a decade earlier. In 2013-14, 77 per cent of 55–64 year old households had at least one employed person, and almost 41 per cent had two or more employed people, compared with 64 per cent and 36 per cent, respectively, a decade earlier.¹⁰ People in the ‘baby boomer’ cohort also tend to have higher asset values and higher debt levels — with increasing numbers of mortgagee home owners (figure 3.26). This study has not examined what is driving those changes. Potential factors could include:

- the macroeconomic environment, such as low inflation and a long period of stable growth
- increasing longevity and improving health of older people
- structural change in the workforce — increased prevalence of white-collar jobs that are more amenable to continuing to work into older age
- changes in preferences

¹⁰ Productivity Commission estimates based on ABS (*Household Income and Wealth, Australia, 2013-14*, Cat. no. 6523.0; *Survey of Income and Housing, Australia, 2003-04 Basic CURF*, Cat. no. 6541.0.30.001).

- policy changes, including pension policy and the introduction of compulsory superannuation
- growing depth and flexibility of financial markets.

Figure 3.26 **Mortgagee home ownership, households by age group^a**
2001, 2006, 2011



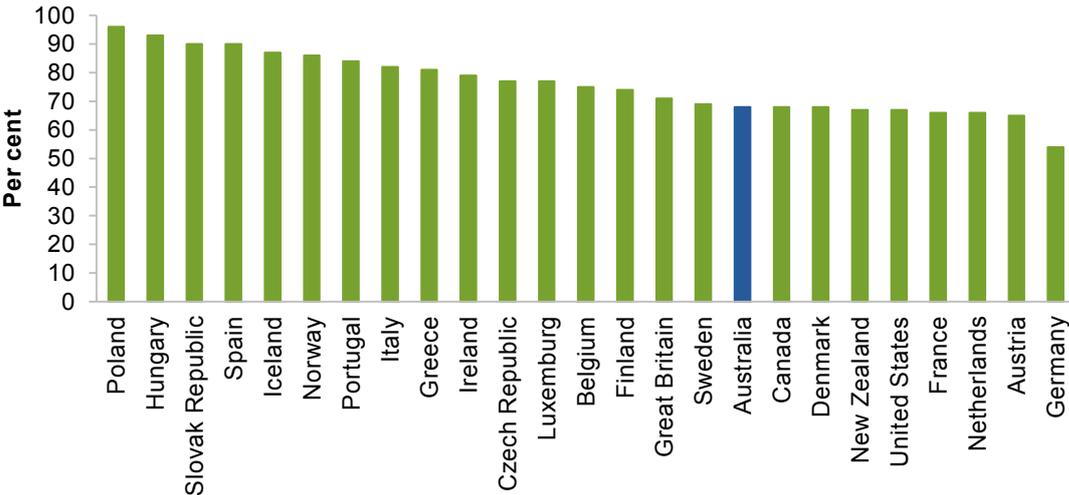
^a Age of household is defined as age of household reference person. Mortgagee home ownership refers to owners with a mortgage.

Sources: Productivity Commission estimates based on ABS (*Microdata: Census of Population and Housing, 2001, 2006 and 2011*, Cat. no. 2037.0.30.001).

These generational differences are likely to have a number of implications for housing decisions of older Australians in years to come. Older Australians in the next decade or two (dominated by the baby boomer cohort) are likely to be wealthier on average, but also with greater dispersion in the distribution of household wealth. They may be less risk averse than their predecessors, with a greater willingness to take on and hold debt, and to draw down on their home asset to fund their retirement and care needs. This might also reflect a weaker bequest motive, compared with previous cohorts. (Older Australians' attitudes to debt and to options for releasing equity from their assets are discussed further in chapter 6.)

Annex — Additional statistics

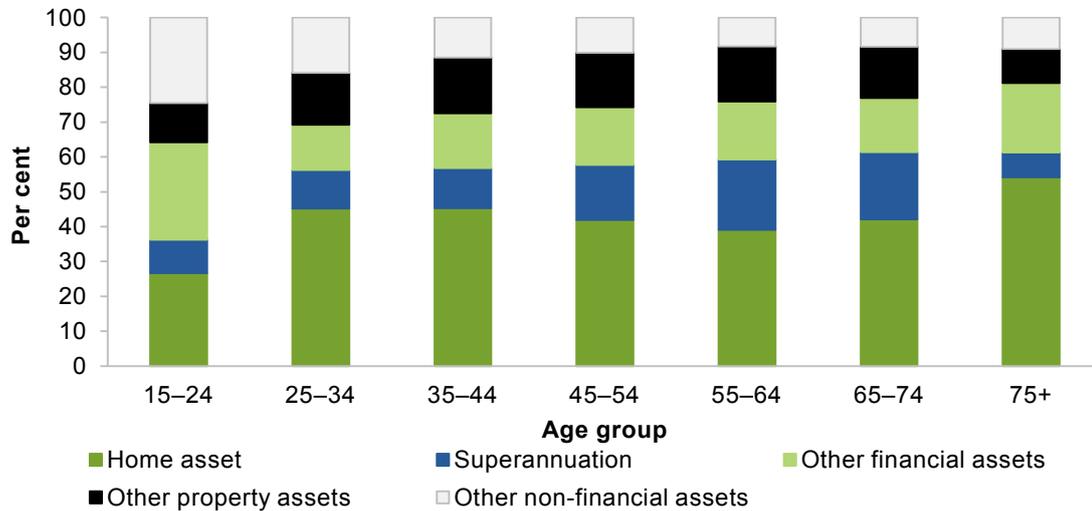
Figure 3.27 **Proportion of home owners, by country**
Selected OECD countries, 2006 or later^a



^a Year of collection and method of collection varies across countries and may impact on comparisons.

Source: Productivity Commission estimates based on ABS (*Measures of Australia's Progress, 2010*, Cat. no. 1370.0).

Figure 3.28 Shares of household assets^a, by source and age group^b
2011-12

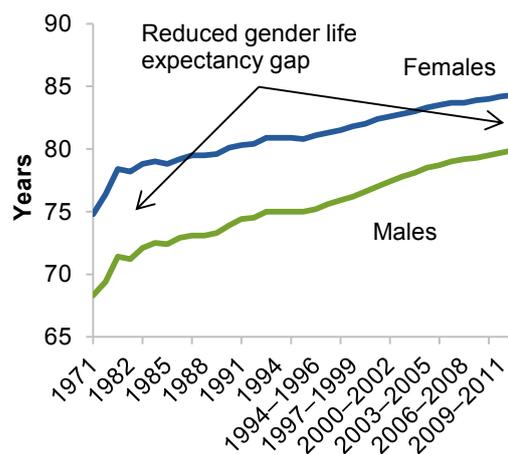


^a Observations are only captured if asset value is positive or equal to zero. ^b Age of household is defined as age of household reference person.

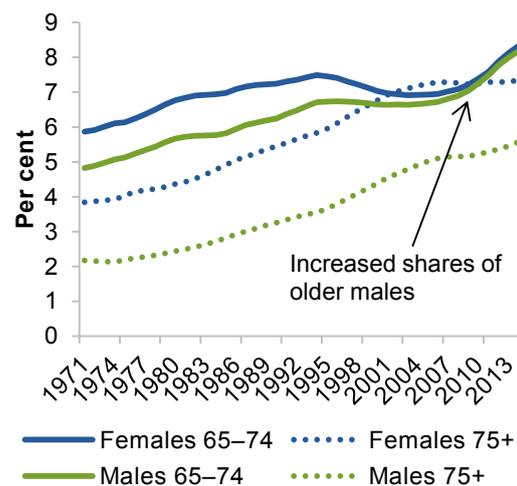
Source: Productivity Commission estimates based on ABS (*Survey of Income and Housing, Australia, 2011-12 Basic CURF*, Cat. no. 6541.0.30.001).

Figure 3.29 Male and female longevity

(a) Life expectancy at birth, 1971 to 2010-2012^a



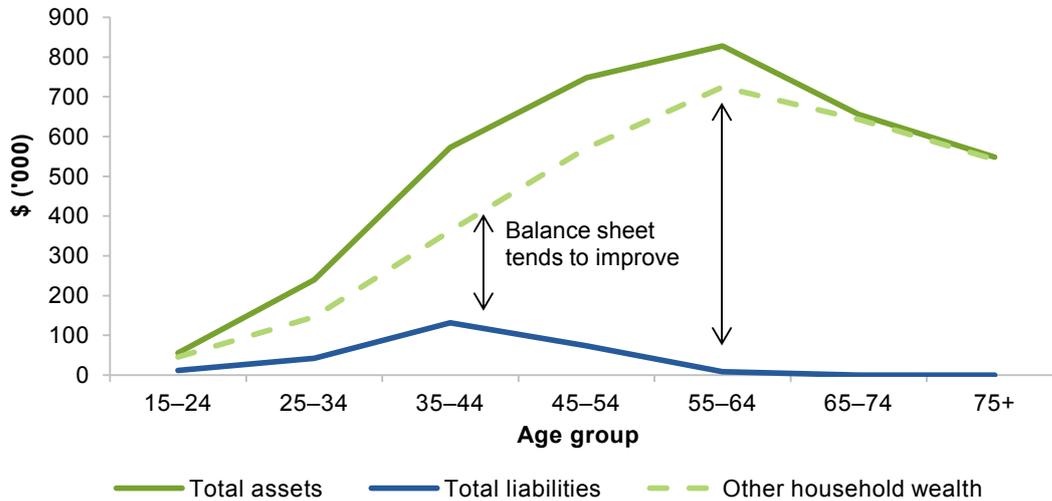
(b) Estimated resident population, selected categories, 1971-2014^b



^a Time periods not evenly distributed, due to data availability. ^b Years ended June. Age groups aggregated from single-year age data.

Sources: Productivity Commission estimates based on ABS (*Australian Demographic Statistics, December 2014*, Cat. no. 3101.0; *Australian Historical Population Statistics, 2014*, Cat. no. 3105.0.65.001).

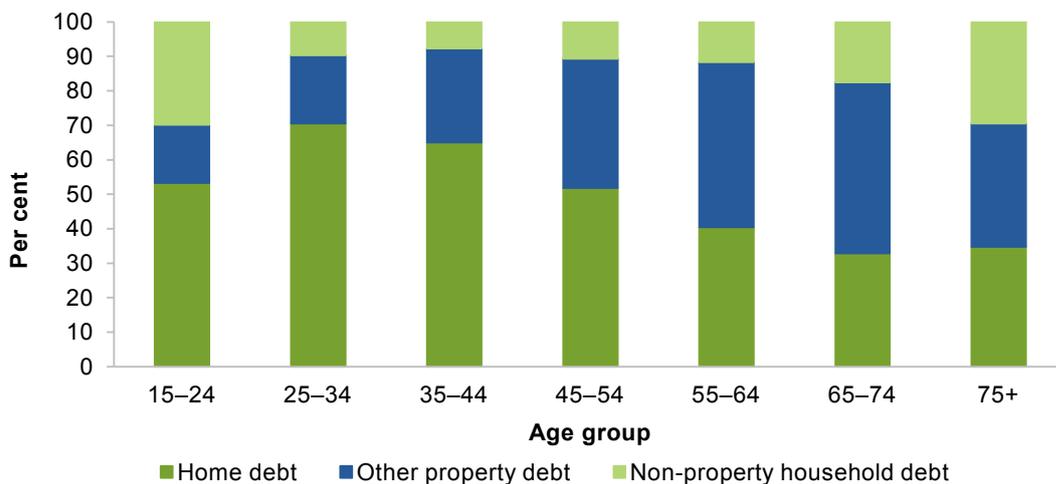
Figure 3.30 Median household assets, liabilities and wealth^{a,b}
2011-12



^a Observations are only captured if values are positive or equal to zero. ^b Age of household is defined as age of household reference person.

Source: Productivity Commission estimates based on ABS (*Survey of Income and Housing, Australia, 2011-12 Basic CURF*, Cat. no. 6541.0.30.001).

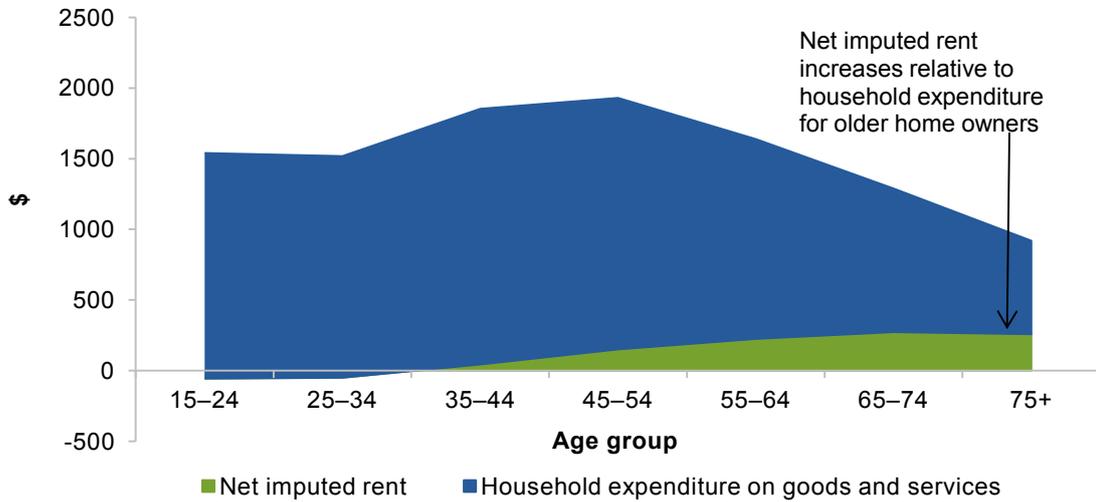
Figure 3.31 Shares of household liabilities^a, by source and age group^b
2011-12



^a Observations are only captured if liability value is positive or equal to zero. ^b Age of household is defined as age of household reference person.

Source: Productivity Commission estimates based on ABS (*Survey of Income and Housing, Australia, 2011-12 Basic CURF*, Cat. no. 6541.0.30.001).

Figure 3.32 Net imputed rent and household expenditure, home owners^a
2009-10 (2013-14 dollars)

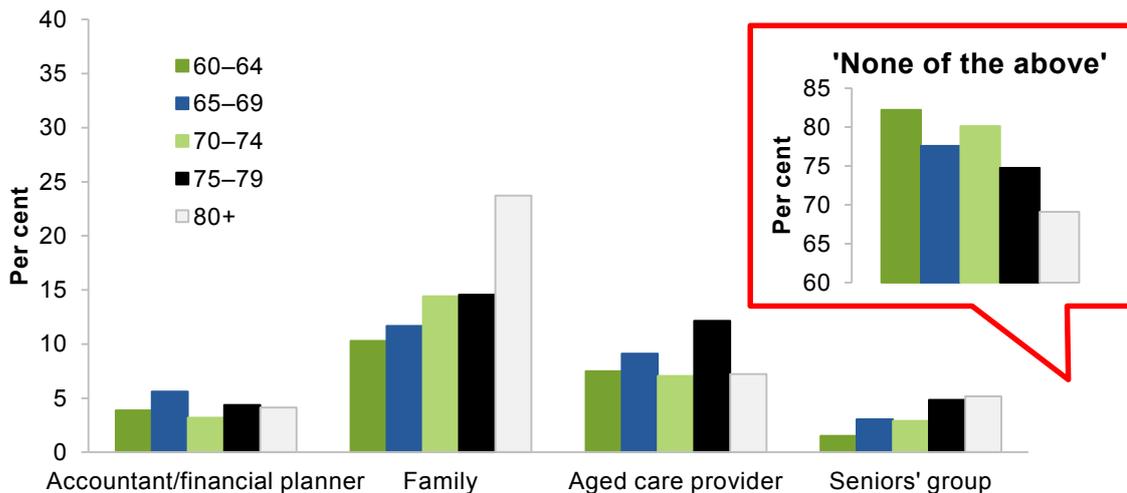


^a Age of household is defined as age of household reference person.

Source: Productivity Commission estimates based on ABS (*National Accounts: National Income, Expenditure and Product*, Cat. no. 5206.0; *Survey of Income and Housing, Australia, 2011-12 Basic CURF*, Cat. no. 6541.0.30.001).

Figure 3.33 Seeking advice on funding aged care costs

Have you spoken to any of the following about how you would fund the costs associated with moving into an aged care facility?^a

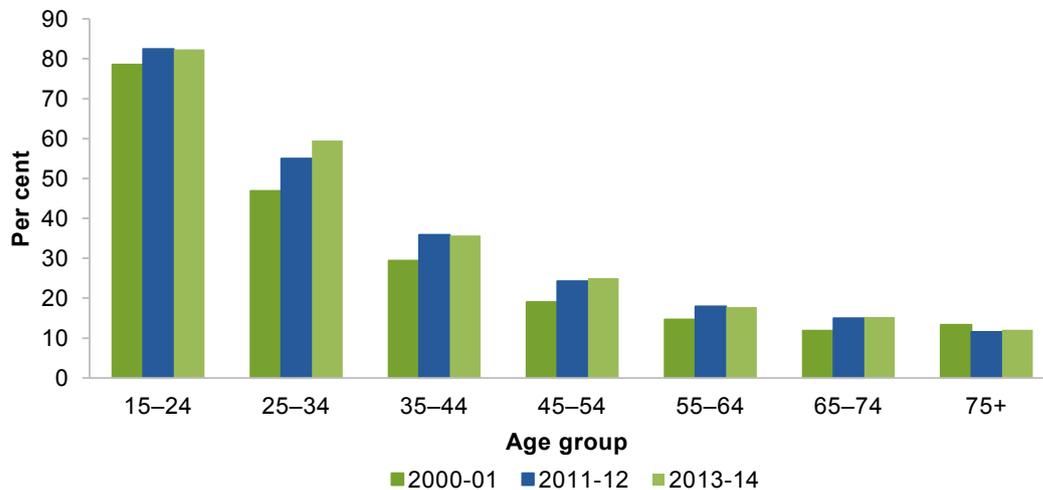


^a Percentages for each age group do not necessarily sum to 100 as respondents could choose more than one option.

Source: Commission survey.

Figure 3.34 Renters, households by age group^a

2000-01, 2011-12, 2013-14

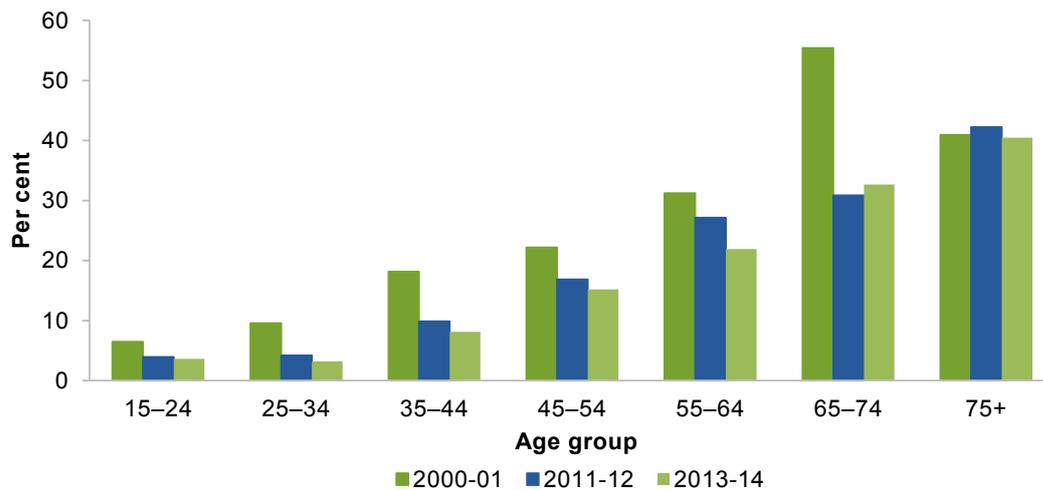


^a Age of household is defined as age of household reference person.

Sources: Productivity Commission estimates based on ABS (*Household Income and Wealth, Australia, 2013-14*, Cat. no. 6523.0; *Survey of Income and Housing, Australia, 2011-12 Basic CURF*, Cat. no. 6541.0.30.001; *Survey of Income and Housing Costs, Australia, 2000-01 Basic CURF*, Cat. no. 6541.0.30.001).

Figure 3.35 Renters — proportion renting publicly^a

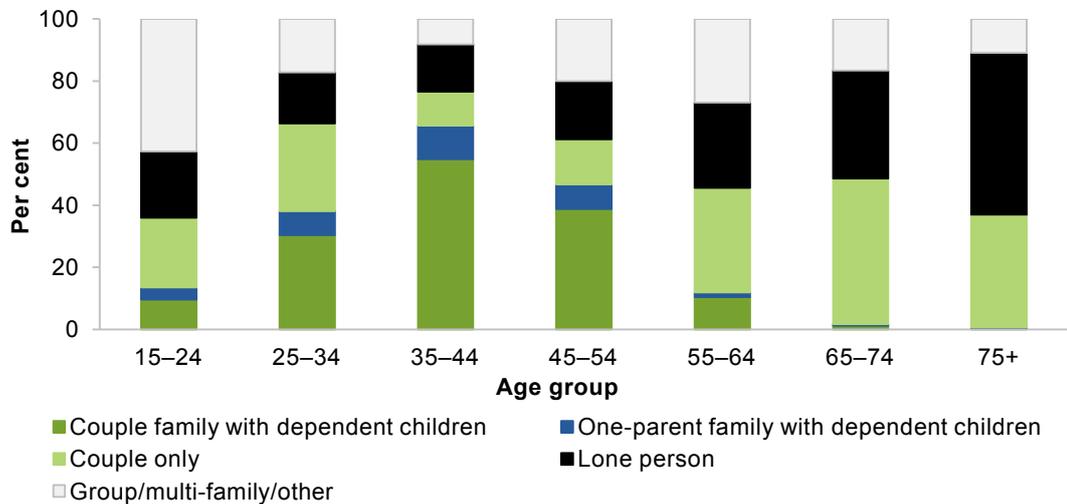
2000-01, 2011-12, 2013-14



^a Age of household is defined as age of household reference person.

Sources: Productivity Commission estimates based on ABS (*Household Income and Wealth, Australia, 2013-14*, Cat. no. 6523.0; *Survey of Income and Housing, Australia, 2011-12 Basic CURF*, Cat. no. 6541.0.30.001; *Survey of Income and Housing Costs, Australia, 2000-01 Basic CURF*, Cat. no. 6541.0.30.001).

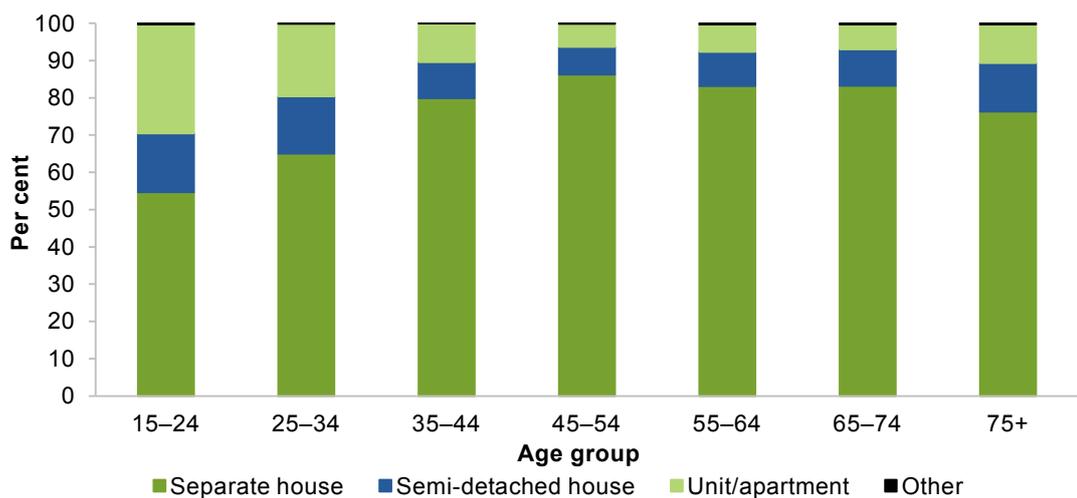
Figure 3.36 Household family composition by age group^a
2011-12



^a Age of household is defined as age of household reference person. Five categories of family composition have been grouped from a more detailed set of categories.

Source: Productivity Commission estimates based on ABS (*Survey of Income and Housing, Australia, 2011-12 Basic CURF*, Cat. no. 6541.0.30.001).

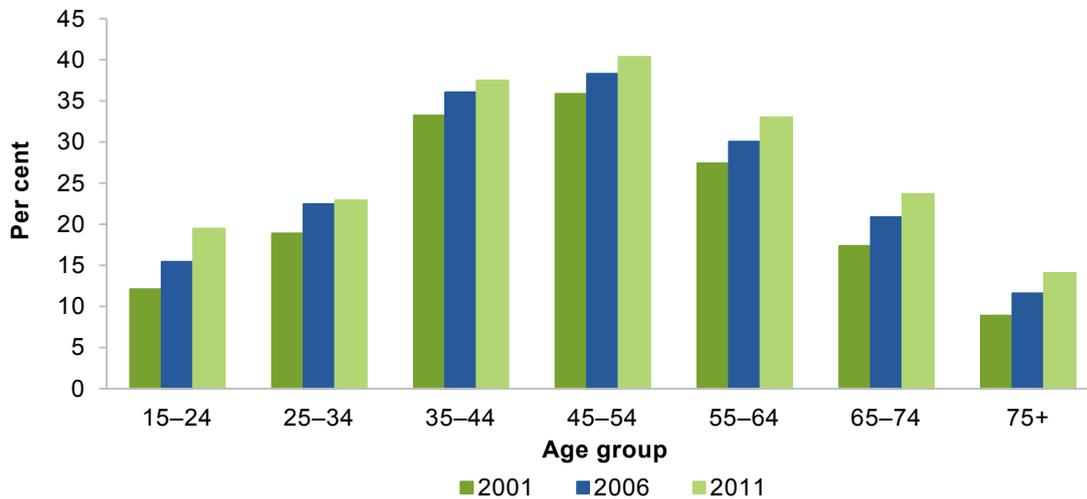
Figure 3.37 Household dwelling type by age group^a (private dwellings)
2011-12



^a Age of household is defined as age of household reference person. **Semi-detached house** refers to semi-detached, row or terrace houses or townhouses. **Unit/apartment** refers to flats, units or apartments. **Other** includes caravans, houseboats, improvised homes, and houses or flats attached to a shop or office.

Source: Productivity Commission estimates based on ABS (*Survey of Income and Housing, Australia, 2011-12 Basic CURF*, Cat. no. 6541.0.30.001).

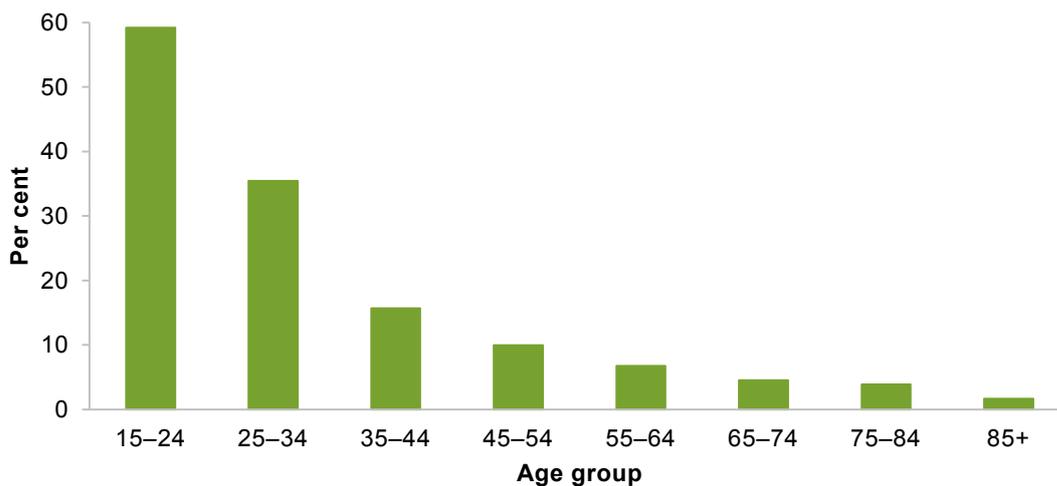
Figure 3.38 Households living in dwellings with four or more bedrooms, by age group^a
2001, 2006, 2011



^a Age of household is defined as age of household reference person.

Sources: Productivity Commission estimates based on ABS (*Microdata: Census of Population and Housing, 2001, 2006 and 2011*, Cat. no. 2037.0.30.001).

Figure 3.39 Proportion of households that moved, by age group^a
2010

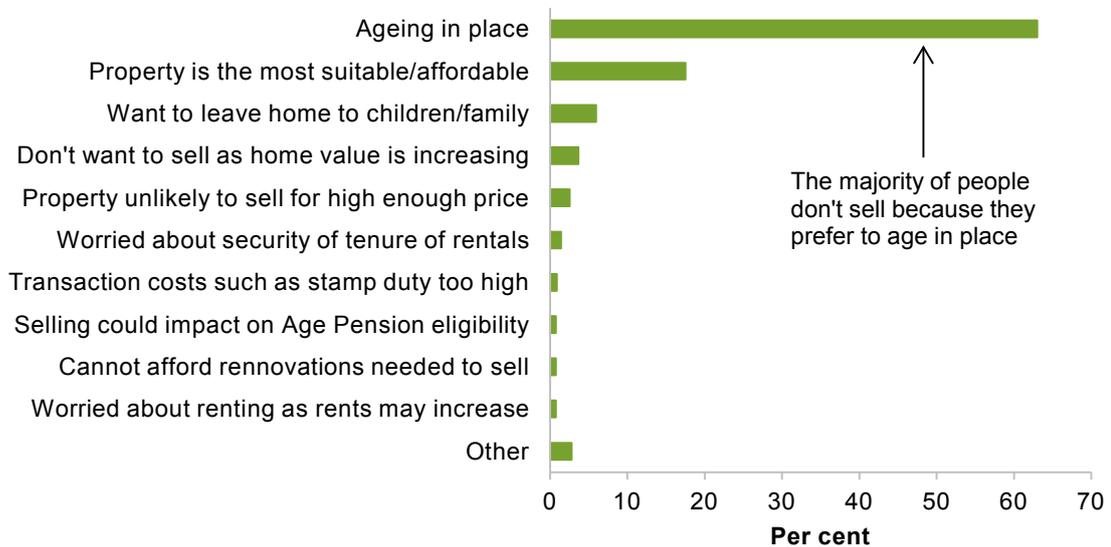


^a Population weighted.

Source: Productivity Commission estimates based on HILDA release 13.1, wave 10.

Figure 3.40 Reasons for older Australians not selling the family home^a

You have indicated that you are unlikely to sell your home. Why is this? (First priority out of a possible three)



^a The category for 'Ageing in place' groups three possible answers including those who wanted to stay in their home as long as possible, those who had an emotional attachment to the property, and those who liked/were familiar with their property's location.

Source: Commission survey.

4 Housing options for older Australians

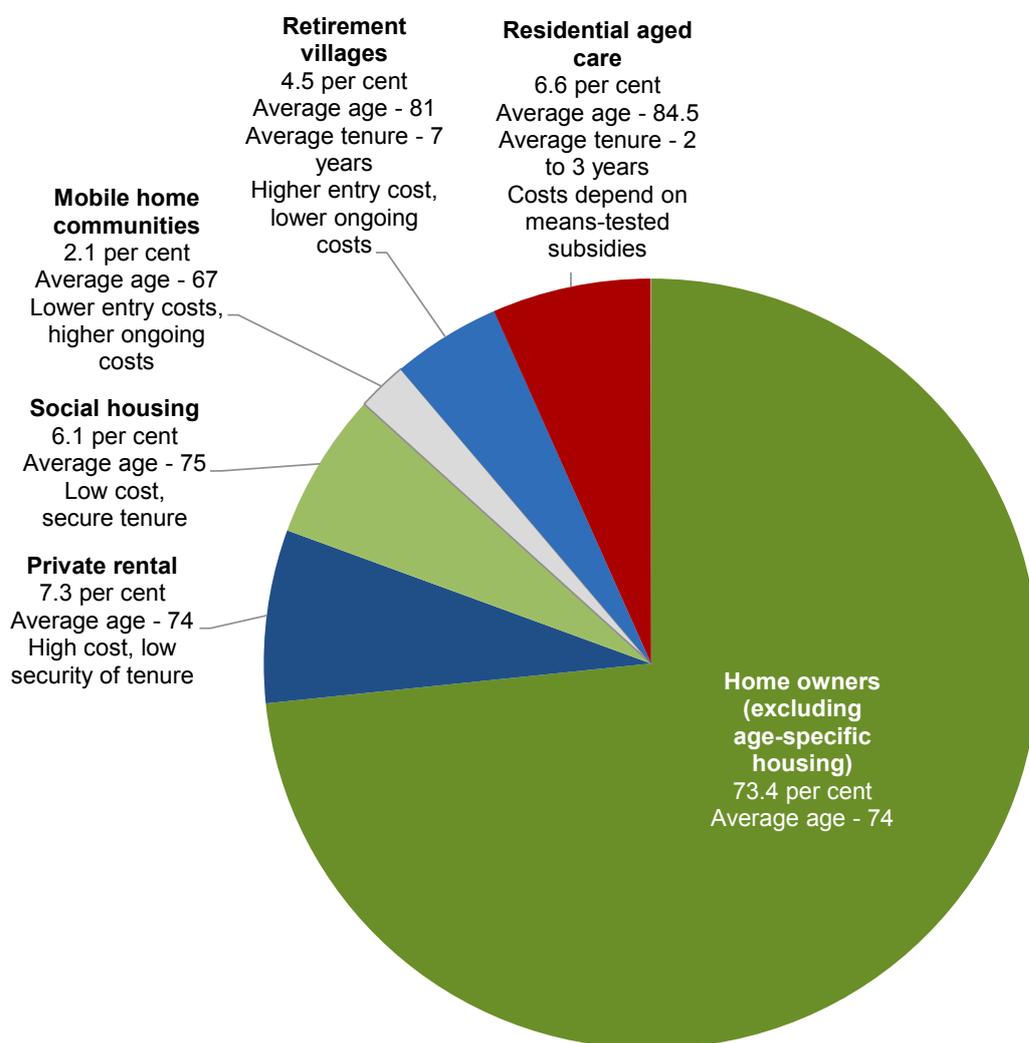
Key points

- The most popular housing option for older Australians remains their own home. To support the ageing population, the Australian Government has been reforming and expanding the provision of home care services. This has benefits for the Government, as home care is cheaper to provide than residential aged care, and consumers, who prefer to age in place.
- The use of residential aged care is declining. Entry into residential aged care has become largely an end-of-life decision, driven by ill health and frailty.
- The Australian Government has reformed fee structures in residential aged care, to separate accommodation and care costs. However, there are still substantial restrictions around the supply of residential aged care, in addition to needs-based assessments that determine individuals' eligibility for subsidised residential aged care. While rationing services based on need is important, existing supply restrictions are redundant and are stifling competition and innovation. As recommended by the Commission in 2011, removing supply restrictions will improve the housing and care options available to older Australians.
- The Commission's survey of older Australians found that current levels of awareness and knowledge regarding aged care are low. Effective provision of information on housing and care options will support older Australians in making better housing decisions.
- An increasing proportion of older Australians are choosing to move into age-specific housing, primarily in retirement villages and manufactured home estates, reflecting financial and lifestyle preferences.
 - Retirement village residents face a very complex structure of fees and charges. Reviewing state legislation that governs the financial models used by retirement villages may benefit both operators and residents.
 - Security of tenure in manufactured home estates is relatively low, and this disadvantages residents.
 - Commonwealth Rent Assistance is applied inconsistently across age-specific housing options, which creates inequities between similar older households.
- A substantial proportion of older Australians are in the private rental market. Low government subsidies and insecure tenure result in substantial disadvantage for this group. Commonwealth Rent Assistance and state-based residential tenancy legislation need to ensure low-income private renters are appropriately supported.
- The policies that affect older Australians' housing decisions are very fragmented, and there is no strategy that recognises the spectrum of choices, and their effects on aged care services. This patchwork of policy makes it difficult for older Australians to transition from one form of housing to another, as their care needs change.

The housing needs of older Australians evolve over time, which often means they need to consider changes to their accommodation as they age. While the vast majority choose to remain in their own home and make modifications or access home care services, a growing number of options are available to those who decide — because of lifestyle preferences, ill health and other concerns — to move (figure 4.1).

Figure 4.1 Where do older Australians live^{a,b}

Proportion of population over 65 in 2011



^a Due to data limitations, rates for home ownership, private rental and social housing at the individual person level have been imputed by applying population-weighted, household-level home ownership and rental rates from the 2011-12 Survey of Income and Housing to persons enumerated in private dwellings in the 2011 Census, for a given age cohort. ^b Average age and tenure figures refer to 2013-14.

Sources: Productivity Commission estimates based on ABS (*Census of Population and Housing*, 2011, Cat. no. 2037.0.30.001; *Survey of Income and Housing*, Australia, 2011-12 Basic CURF, Cat. no. 6541.0.30.001); Productivity Commission estimates based on HILDA release 13.1, wave 13; AIHW (2015); PwC (2015).

This chapter examines and assesses the key features of the major housing options available to older Australians. There are a number of other options available, such as the construction of a new, age-friendly home or a granny flat. However, researchers have suggested that the number of older people choosing these housing options remains relatively small (Pinnegar et al. 2012).

4.1 Home care — a key factor in housing decisions

The housing decisions of older Australians are driven by a number of factors, including health and financial reasons (chapter 3). As people age, health reasons become the most important consideration in the decision to move, and the availability of care and support services delivered in the home has a major influence on housing decisions.

The Australian Government funds an array of home care services, which can be delivered in most homes.¹¹ These services are funded under two separate Commonwealth programs — the Commonwealth Home Support Programme (CHSP) and Home Care Packages (table 4.1) (appendix B includes more detail on these programs). CHSP includes ‘entry-level’ services such as occasional domestic assistance and personal care, as well as home maintenance and home modification. Home Care Packages offer more intensive support, including nursing, allied health, and clinical services as well as more complex assistance and personal services (DSS 2015e).

Depending on the intensity of the support they require, older Australians will go through different application and assessment processes, and pay different fees, to access these services. According to service providers, this can create confusion and inefficient outcomes. For example, the CHSP and Level 1 Home Care Packages currently provide very similar services, but CHSP subsidies to providers are much higher. In addition, clients accessing services through the CHSP do not have to pay the income-tested fee charged for home packages (KPMG 2015). Concerns have also been raised about the efficiency and equity of the home modification and maintenance services funded by government (KPMG 2014).

These issues may be addressed as part of the Australian Government’s aged care reforms. For example, national screening and assessment processes have been introduced to the CHSP, and a client contribution framework has been developed (DSS 2015e, 2015k). In 2018, the Australian Government plans to integrate the CHSP and the Home Care Packages programs, which may further reduce overlap and inconsistencies.

¹¹ While there are no restrictions on the delivery of home care packages in retirement villages, some home maintenance and modification services are not provided to dwellings within retirement villages or in public housing. This occurs when the housing operator (either a private company or a state housing authority) has the responsibility for maintaining parts of the dwelling (DSS 2015c). In some cases, people living in units and apartments must obtain permission from their neighbours before work is carried out, which can delay or prevent necessary modifications (Easthope and van den Nouwelant 2013).

Table 4.1 Aged care services delivered in the home

	<i>Commonwealth Home Support Programme^a</i>	<i>Home Care Packages^a</i>
Services provided	<ul style="list-style-type: none"> • Entry level support services, either on a short-term or ongoing basis. Includes home modifications and home maintenance services • Goal is to prevent or delay entry into residential aged care 	<ul style="list-style-type: none"> • Home packages are classified into four levels of service provision, from low to high care • They include more complex support services, including clinical services, for older people who are able to continue living independently in their own homes with assistance • Goal is to act as a substitute for residential aged care
Eligibility	<ul style="list-style-type: none"> • From 2015, determined by the My Aged Care Regional Assessment Service 	<ul style="list-style-type: none"> • Determined by the Aged Care Assessment Team (process equivalent to residential aged care)
Allocation	<ul style="list-style-type: none"> • Eligible customers are referred to approved providers in their local area • No restrictions on number of services provided, but funding is limited. Government guidelines determine the maximum expenditure allowed (for example, there is a cap of \$10 000 on home modifications) 	<ul style="list-style-type: none"> • Up until 2015, packages were allocated to providers through a competitive tender process managed by the Department of Social Services. Eligible clients had to find a provider with an available package • Current reform is introducing Consumer Directed Care, allocating budgets to each eligible client, who can then choose a provider
Clients' co-contributions	<ul style="list-style-type: none"> • Determined by each provider • No income assessment required 	<ul style="list-style-type: none"> • Income tested co-contribution, based on an assessment conducted by the Department of Human Services • Minimum fee is equivalent to 17.5 per cent of the Age Pension and co-contributions are capped

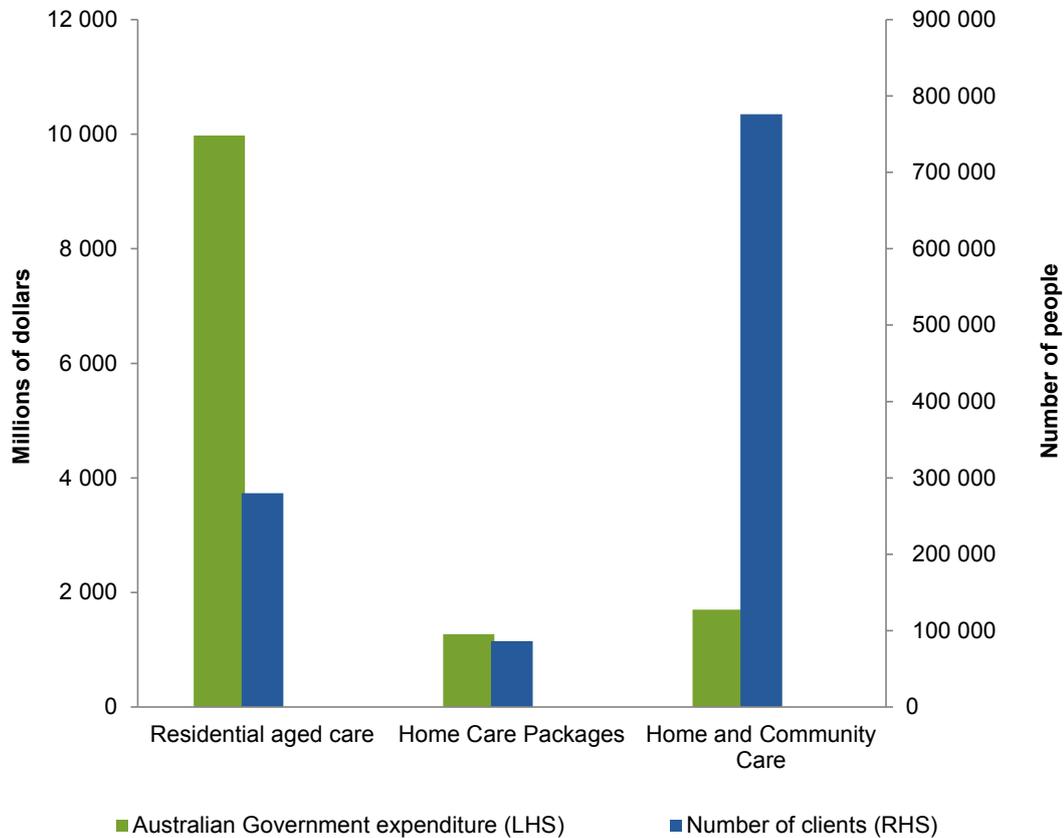
^a See appendix B for more information.

Sources: DSS (2014d, 2015e).

Considerations for future reform

Over time, the focus of aged care policy has shifted from residential aged care, to emphasise home care services and support independent living in the community. This shift is in line with the strong preference of older Australians to age in place. It also allows government to contain its aged care costs, as delivering home care requires much less public funding compared with residential care, despite much higher numbers of clients (figure 4.2).

Figure 4.2 **Aged care clients and costs to government^a**
2013-14



^a Home and Community Care has been amalgamated into the Commonwealth Home Support Program in 2015. For more detail, see appendix B.

Source: SCRGSP (2015).

As part of the changes to the aged care system, home care services have already undergone substantial reform in recent years and further changes are planned (table 4.2). It is important that reforms are based on consistent policy principles, which address any inequities in services that may exist in the current system.

Some aspects of home care services, such as home maintenance and modifications, are directly related to the housing decisions of older Australians. In the long term, the Department of Social Services has highlighted the need to improve the targeting of home maintenance services to older clients with the least ability to maintain their homes. It may also consider promoting universal design principles, which will minimise the need for home modifications, and providing information to residents who may consider downsizing as an alternative to major home modifications (DSS 2014g).

Table 4.2 Key changes in home care services^a

<i>Programs pre-reform</i>	2013	2015	2017	2018
Home and Community Care (HACC) National respite for carers program Day therapy centres program Assistance with care and housing for the aged program		Amalgamated into the Commonwealth Home Support Program (CHSP) <ul style="list-style-type: none"> • New assessment and referral arrangement through My Aged Care • New client contribution framework developed 		The CHSP and the Home Care Packages Program will be integrated from July 2018
	2013	2015	2017	
Community Aged Care Packages (CACP) Extended Aged Care at Home packages (EACH) Extended Aged Care at Home Dementia packages (EACH-D)	Amalgamated into the Home Care Packages Program , offering four levels of care <ul style="list-style-type: none"> • Consumer directed care for new packages • More comprehensive income testing for fees (from July 2014) 	<ul style="list-style-type: none"> • All packages based on consumer directed care • Providers will no longer be allocated packages through a central tendering process after 2015 	Packages will be allocated to consumers, rather than providers. Consumers will choose their preferred providers, who deliver government-subsidised services. Packages will be fully portable	

^a For more detail, see appendix B.

Sources: ACFA (2015); DSS (2015k).

More broadly, the Australian Government plans to increase the provision of home care services, while reducing the number of new residential aged care places, and expand consumer directed care, which will give consumers greater choice and flexibility in addressing their care needs (appendix B). These changes are part of a broader transition to a consumer-focused market in human services, which represents a substantial change for providers, consumers and government (Hatfield Dodds 2015).

Increasing the availability of home care services is important both in supporting individuals' choices and in containing public expenditure. The removal of supply restrictions for home care services, with the introduction of consumer directed care, is likely to promote further competition and innovation in the housing and care options available to older Australians. For example, operators of age-specific housing, such as retirement villages, are likely to face less red tape if they decide to offer home care services to residents (see below).

However, governments must ensure that these services are delivered in an equitable and efficient way, and that consumers and providers are adequately supported in the transition to a new consumer-led aged care system. A recent evaluation has found that while reform implementation was generally progressing well, both providers and consumers would benefit from additional support and information. For providers, the introduction of consumer directed care has created higher than expected administrative burdens, which have increased the cost of delivering services. For consumers, in some cases, the higher administration costs have meant that there is less budget available to cover care costs (KPMG 2015). Some of the concerns raised by the evaluation are likely due to teething issues in the implementation of reforms. However, where opportunities for further transparency and consistency have been identified, it is important that these are addressed promptly.

4.2 Older Australians in the housing market

The housing options available for older Australians are evolving, as more people are considering alternatives to ageing in the family home. Those who decide to move can choose between downsizing in the private market, and age-specific housing options, including retirement villages, mobile home communities and residential aged care.

Age-specific housing options cover a wide spectrum, in terms of costs and care services provided in conjunction with accommodation (table 4.3). A growing proportion of older Australians move along this spectrum, for example, from independent living at home, to accessing low level support services in a retirement village, to ongoing nursing care in a residential aged care facility. The goal of policy should be to ensure that such transitions are as simple and cost effective as possible.

Table 4.3 Key features of housing options for older Australians

	<i>Home owners</i>	<i>Private rental</i>	<i>Social housing</i>	<i>Mobile home communities</i>	<i>Retirement villages</i>	<i>Residential aged care</i>
Services offered	Home based aged care for eligible people	Home based aged care for eligible people	Home based aged care and other services for eligible people	Basic services from providers; can access home care	Varies by village, and some offer extensive services; can also access home care	Ongoing care
Access to government funded home modifications	Yes, subject to eligibility and waiting times ^a	Yes, but requires landlord agreement	No – done by housing provider	Yes, subject to eligibility and waiting times	Depending on services provided by retirement village	Not applicable
Legal ownership status/tenure structure	Own land and dwelling	Lease dwelling	Lease dwelling	Mostly own the dwelling and lease the land	Long-term license to occupy the dwelling	Not applicable
Security of tenure	High	Low – can be evicted without grounds	High – often lifetime tenure	Low – can be evicted without grounds in some jurisdictions	High	High
Regulation	Supply of care controlled by Cwlth	Varies by jurisdiction	Funded (and often provided) by States and Territories	Varies significantly by jurisdiction	Varies by jurisdiction	Supply controlled by Cwlth
Fee structure	Imputed rent	Market rent	Rent – fixed proportion of income	Purchase price of home + ongoing fees (some also pay at departure)	Ongoing fees + refundable lump sum at entry + departure lump sum	Subsidised ongoing fees. Can choose to pay refundable lump sum for accommodation
Interaction with tax/transfer system	Home exempt from the Age Pension asset test. Only part of the value included in residential aged care asset test	Age pensioners eligible for Cwlth Rent Assistance	Rents are subsidised	Age pensioners eligible for Cwlth Rent Assistance. Value of dwelling exempt from Age Pension means test	Mostly ineligible for Cwlth Rent Assistance. Entry contribution exempt from the Age Pension asset test	Means testing determines the fees payable. The value of the principal residence included up to a capped amount

^a In some dwellings, the body corporate must also agree to modifications.

4.3 Home ownership

The vast majority of Australians choose to remain in their homes as they age. Reflecting the overall housing stock, dwellings occupied by older Australians are likely to be separate houses with three or more bedrooms. Most existing housing is unlikely to be suitable to the needs of older people if they develop a disability or require more intensive assistance (Judd et al. 2010).

Therefore, as people age, they may choose to downsize or make modifications to their home, so that it is more appropriate to their needs (box 4.1). Only about 10 per cent of older Australians choose to move to smaller dwellings, usually single storey units or apartments in the private market or retirement villages. Those who move often look for dwellings that require less maintenance than their existing home and give them a greater sense of security. The main barrier to mobility has been the availability and affordability of homes suitable for the needs of older people (Judd et al. 2014).

Box 4.1 Housing needs of older people

As people age, their housing needs and preferences may change, both in respect to a dwelling's location and its amenity. Generally, older people require dwellings that are suitable for their changing physical needs, with even surfaces, passages wide enough for wheelchairs, and appropriately designed bathrooms, toilets and kitchens. It is also important for the dwelling to be located close to services and facilities, such as medical clinics and public spaces, to allow residents to continue to participate actively in their community. Older people, particularly those living alone, are often concerned for their safety, and look for dwellings and communities that offer them a sense of security, for example through community patrols or the installation of emergency call devices in older people's homes (WHO 2007). The availability of housing that caters for the needs of older people can have substantial benefits for their individual wellbeing, as well as reducing health and aged care costs for governments (PC 2011).

A number of government initiatives, such as the development of the Liveable Housing Design guidelines, aim to support the supply of age-friendly housing and encourage the construction of accessible dwellings. The Commission recommended that the Australian Government develop building design standards for residential housing that meet the access and mobility needs of older people (PC 2011). However, such standards are yet to be developed by the Australian Building Codes Board.

A much larger proportion of older Australians modify their home to accommodate changing needs. A survey of older home owners found that 34 per cent of respondents had already modified their home (particularly bathroom and stair areas) and a further 40 per cent were likely to modify it in the future (Judd et al. 2010). Home modifications can have substantial benefits for residents, by supporting independent living and enhancing accessibility and safety in the home. They can also reduce the need for home care and the likelihood of entering residential aged care (KPMG 2014).

4.4 Private rental market

A substantial proportion of older Australians live in rental accommodation (chapter 3). While for some households rental accommodation is a choice that offers flexibility and lower transaction costs, many in the private rental market are negatively affected by a lack of stability and security of tenure (Kelly et al. 2013).

Older people are overrepresented both among public housing tenants (ABS 2015d) and among long-term renters in the private market (Stone et al. 2013). Those in social housing (which includes public and community housing) benefit from lower rents and secure tenure; however, the stock of social housing is insufficient to address growing demand (box 4.2) and the proportion of older Australians living in private rental accommodation is expected to rise in the coming years (SERC 2015).

Box 4.2 Older Australians in social housing

Social housing is an important housing option for low-income older Australians. About 25 per cent of people in social housing — over 150 000 people — are aged 65 and over (Productivity Commission estimates based on ABS (*Census of Population and Housing*, 2011 and *Survey of Income and Housing*, Australia, 2011-12)). Social housing (including public housing, provided by state and territory governments, and community housing, provided by not-for-profit groups) can offer older Australians an affordable and secure housing option (SERC 2015).

Within public housing, people over 65 accounted for over 30 per cent of residents (Cigdem, Wood and Ong 2015). Ageing in public housing can present challenges for both residents and providers. In some cases, the public housing stock is not suitable for the needs of older people, and there are shortages of appropriately sized dwellings that older people can move to. Researchers have also raised concerns about the delivery of aged care services within public housing estates, and the interaction of housing with other support services (McNeils et al. 2008). State housing authorities face multiple challenges in dealing with an increasing proportion of older residents, including the higher costs of subsidising accommodation for older people on low incomes (NHSC 2013). Some state housing authorities have been developing accommodation specifically for older people (for example, Department of Health 2013).

Community housing organisations represent only a small share of social housing (about 16 per cent of all social housing dwellings (SCRGSP 2015)). Some of these organisations have developed innovative solutions for addressing the housing needs of disadvantaged older Australians, such as volunteer-run group houses for low-income older people and housing services tailored to the needs of older homeless people (Abbeyfield Australia 2014; Wintringham 2014).

As the population ages, demand for social housing from older Australians is expected to rise (PC 2005). However, social housing supply has been stagnant over the past decade (PC 2015a). As a result, there is very limited available stock, and increasing numbers of low-income older people resort to renting in the private market (NHSC 2013).

Numerous reviews have raised concerns about the difficulties faced by older renters. Most recently, the Senate inquiry into housing affordability (SERC 2015) has highlighted three issues affecting the wellbeing of age pensioners renting in the private market.

- **Affordability** — Older Australians in the private rental market have substantially higher housing costs as a proportion of income than any other group in the population. In 2012-13, single people aged 65 and over who were renting in the private market spent 42 per cent of their income on housing, three times higher than the average housing expenditure (ABS 2015d).¹² Age pensioners who rent privately are eligible for Commonwealth Rent Assistance (CRA), in addition to their pension.¹³ However, this payment has not kept up with rising rents. In 2014, one in four CRA recipients aged 75 and over were in housing stress (SCRGSP 2015).¹⁴
- **Unstable tenure** — Compared to other developed countries, Australian tenancy laws offer relatively low security of tenure to tenants, including short lease terms and the ability of landlords to terminate leases without a specific reason (Kelly et al. 2013). Insecure tenure can have substantial negative effects on older people’s wellbeing and their ability to age in place (Jones et al. 2007; SERC 2015).
- **Restricted access to home modifications** — Evidence submitted to the Senate inquiry indicated that private landlords have little incentive to modify properties to suit the needs of older tenants. Older renters are forced to move as dwellings are no longer appropriate to their needs (SERC 2015).

Reflecting this combination of factors, some commentators regard older private renters as ‘one of the most disadvantaged groups in Australian society’ (SERC 2015, p. 271). In response to the difficulties faced by older renters, the Commission proposed in 2011 that COAG develop a strategic policy framework to ensure an adequate supply of affordable housing that meets the needs of an ageing population (PC 2011).

Since 2011, no new framework has been developed. The National Affordable Housing Agreement, which commenced in 2009, contains a number of objectives related to the supply of affordable housing; however, they do not relate specifically to the needs of older people (COAG 2009). The more recent Senate inquiry has called on the Australian Government to adjust aged care policies so they could better support older Australians in the private rental market (SERC 2015).

Beyond aged care policies, researchers have suggested a number of ways to improve supply and security of tenure in the private rental market, including regulatory changes and increases in CRA (Hulse, Milligan and Easthope 2011). Some changes to regulation are

¹² The proportion of income spent on rent by older Australians is also significantly higher than other private renters. In 2013-14, the median ratio of housing costs to income across all private renters was 20 per cent, and for all population groups, it was 14 per cent (ABS 2015d).

¹³ The amount of Commonwealth Rent Assistance is means tested, in a similar way to the Age Pension. Assistance is paid based on the individual household’s rent, up to \$129.40 a fortnight for a single with no dependent children (DHS 2015e).

¹⁴ Housing stress was defined as spending more than 30 per cent of income on rent (SCRGSP 2015).

being considered — for example, in Victoria, the current review of the *Residential Tenancies Act 1997* (Vic) will explore the viability of longer-term leases and the introduction of specific protections for older people (Consumer Affairs Victoria 2015b). Any improvements made to residential tenancy laws are likely to benefit older renters, and make the private rental market a more sustainable housing option for older Australians.

The Age Pension was developed to support older home owners, whose housing costs are much lower compared to people renting privately. Although older renters receive CRA in recognition of their higher housing costs, a number of past reviews have acknowledged that the level of CRA is insufficient to ensure pensioners in private rental accommodation maintain an adequate standard of living (for example, Harmer 2009; Henry et al. 2010; RGWR 2015). A dedicated review of CRA, which includes the structure and level of payment, is warranted to ensure it is effective in supporting low-income private renters who are at risk of poverty.

4.5 Mobile home communities

Mobile home communities comprise manufactured home estates (MHEs)¹⁵, where all residents live permanently in manufactured homes, and caravan parks, where residents can live in a variety of dwelling types (such as caravans or cabins) and stay for varied lengths of time (including short-stay holiday makers and permanent residents). In all mobile home communities, the ownership of the land on which the dwellings stand remains with the park owner. Residents can either own the home, and rent the site on which it stands, or rent both the dwelling and the site (Bridge et al. 2011).

Despite growing significantly over the past two decades, MHEs that are marketed specifically to older Australians remain a small part of the age-specific housing sector. In 2013, there were about 165 MHEs in Australia, primarily in New South Wales and Queensland (Colliers 2015).

A further 750 mixed-use caravan parks offer permanent residences alongside short-term accommodation (Colliers 2015). While many residents are over 50, mixed-use caravan parks offer affordable and crisis accommodation to disadvantaged Australians regardless of age. The expansion of MHEs has seen a trend towards gentrification of caravan parks, as larger corporations purchase older style caravan parks and convert them into MHEs. Investors are motivated by the steady income stream in MHEs (from government subsidised site fees or rents) as well as potential for capital improvements (Colliers 2015; Goodman et al. 2013).

¹⁵ In different cases, manufactured home estates have been referred to as residential parks, land lease communities, manufactured home villages and lifestyle villages. These terms all refer to communities where permanent residents own their home, which is manufactured off-site, and lease the land it stands on. For consistency, this chapter will use the term ‘manufactured home estates’.

Although some MHEs offer dwellings and amenities similar to those found in retirement villages, there are a number of differences between the two.

- **Target market** — Residents in MHEs are often younger than those in retirement villages. Unlike people entering retirement villages, whose decision to move is often motivated by deteriorating health, the decision to move into a MHE is primarily motivated by location and financial reasons, followed by a desire to live in a secure community setting. CRA eligibility can also affect the decision (Department of Housing and Public Works 2014; SPRC 2010).
- **Affordability** — The initial purchase price of a manufactured home is lower compared with retirement village units, while ongoing fees can be higher in MHEs. In many MHEs, residents receive any capital gains made when selling the property and are not charged deferred management fees (SPRC 2010). However, shared equity or capital gains arrangements have become more common across the sector (Department of Commerce 2014).
- **Government funding** — MHE residents who also receive the Age Pension are eligible for CRA, as they pay rent for the land their dwelling stands on, and in some cases, the dwelling itself. In 2010, about 80 per cent of MHE residents received CRA, compared with only three per cent of retirement village residents. This is in part due to different eligibility rules (SPRC 2010) (see the retirement village section below).
- **Security of tenure** — Residents in MHEs have significantly weaker security of tenure compared with retirement village residents. The level of consumer protection afforded to them is often similar to that of tenants in the private rental market, and in most jurisdictions, MHE residents can be evicted without grounds (Goodman et al. 2013). As they do not own the land on which their dwellings stand, residents can be affected if operators decide to change the way they use their land. Regulations in some jurisdictions have been changing to improve security of tenure (see below).

Regulation

The regulatory environment of MHEs and caravan parks varies substantially between jurisdictions. While in some states and territories (referred to as states in this chapter), acts and regulations are being reviewed and updated to reflect the more permanent nature of living in MHEs, in other states residents are only covered by the relevant residential tenancy act. Some states separate the regulation of MHEs and caravan parks, offering a higher level of protection to MHE residents (annex A includes a summary of regulatory arrangements) (Goodman et al. 2013).

For many residents, security of tenure is relatively low. For example, in all jurisdictions except Queensland and New South Wales, residents can be evicted without grounds if given sufficient notice. This is of particular concern for residents who own their dwellings. Even though, in principle, homes are relocatable, this can be a costly and complex exercise (Department of Commerce 2014).

In more recent years, reviews of legislation have resulted in more substantial levels of consumer protection and security of tenure for MHE residents. For example, in Victoria, MHEs that have registered after September 2011 must offer their residents site agreements with a minimum term of five years (Consumer Affairs Victoria 2013). Such reviews have been recently completed in Western Australia and New South Wales, and are currently being undertaken in Queensland and Victoria.

4.6 Retirement villages

With their popularity increasing faster than any other age-specific housing option, nearly 2300 retirement villages house more than 184 000 older Australians across the country (Grant Thornton 2014). Retirement villages are designed to cater to the needs and lifestyle of people aged 65 and over, and unlike other housing options, require the payment of an entry (or ingoing) contribution before moving in.

Independent living units are the most common form of retirement village dwelling. Some villages also include serviced apartments, where residents can access additional personal care services for a fee. Operators have reported high vacancy rates for serviced apartments, since ongoing fees are much higher than in independent living units and do not attract any government subsidises (unlike residential aged care) (RVA 2010).

There are two distinct groups of people who consider moving to a retirement village: older retirees, who wish to relocate due to declining health, and younger retirees, who are concerned about their future health needs, and may also be attracted to village amenities and lifestyle. Amenities and services that were most important to those considering relocation included outdoor living areas, assisted living facilities and access to medical services (Crisp, Butterworth and Anstey 2013). Many of those who moved to a retirement village were looking to downsize and chose a retirement village as it offered an independent, safe environment with emergency support and onsite maintenance (McCrindle Baynes 2013).

In response to the expectations of residents, retirement villages have been expanding the range of services they offer. Currently, more than half of villages offer medical assistance on call, in addition to maintenance services and some social or recreational facilities (Grant Thornton 2014). Services can be provided directly by the housing supplier, or contracted out to a third party.

Retirement village units are often priced in relation to the local property market, mostly at market prices or about 10 per cent below the cost of local apartments (Grant Thornton 2014). Residents' income levels tend to reflect average income for older people in the immediate area. Over half of residents (54 per cent) are full pensioners, and a further 34 per cent receive a part pension, which is similar to nationwide propensities. About 17 per cent of residents require assistance with activities of daily living, a lower proportion than the general community (Towart 2013b). Providers have argued that retirement village

residents tend to delay their entry into residential aged care, which generates savings for government (Grant Thornton 2014).

Tenure types and fees

Retirement villages offer different tenure types to residents.

- The loan/license (or license to occupy) model is used by about 50 to 60 per cent of retirement village operators. Under this model, the resident pays an entry contribution that gives them a licence to occupy a property in the village. The entry contribution, minus a deferred management fee, is refundable when the resident leaves the village. The license agreement is not registered with the Land Titles Offices, and offers lower security of tenure than leasehold or a freehold title.
- Leasehold comprises about 30 per cent of villages, offering the residents a long-term lease (for example, for 99 years) for a dwelling, in exchange for a lump sum payment. Leases are registered with the relevant Land Titles Offices, which offers residents security of tenure but may also attract stamp duties. When a resident leaves the village and the unit is resold, they are entitled to a lease termination payment, which is based on a proportion of the resale price (Blake and Craddock 2010; McCullagh 2014).
- Freehold and other tenure types (such as company titles and rental villages) are fairly rare, making up less than 10 per cent of villages (Blake and Craddock 2010; SPRC 2010).

The loan/license model is popular as it allows the village operator to retain ownership of the land, and gives them the flexibility to redevelop it, if required. The planning processes to develop a loan/license village are simpler compared with other tenure types, as there is no need to issue separate titles for dwellings. There is also no need to establish a body corporate (although regulations mandate the need to consult with residents on any changes to the village) (Blake and Craddock 2010).¹⁶

The main fees include a refundable entry contribution, a deferred management fee (DMF) payable when the resident leaves, and recurrent charges (or maintenance fees) for general services provided by the village operator (box 4.3 shows an illustrative example of fees). In some cases, residents continue to pay the recurrent charges even after they leave the village (Blake and Craddock 2010; Consumer Affairs Victoria 2015a). In addition, residents may be required to pay special levies to fund new services, or to refurbish their dwelling before it is resold (Consumer Affairs Victoria 2015a; Lend Lease nd).

In villages that operate under the loan/license model, the entry contribution is an interest free loan to the village operator, which is repaid upon departure. At that point, residents are also required to pay the DMF, which is calculated as a percentage of the entry contribution

¹⁶ The tenure type, as well as the services provided and the structure of fees, affect the operators' tax position (Colliers 2015; Gadens 2014). The taxation issues related to retirement villages are complex, and beyond the scope of this report.

or the resale price of the unit that accrues on an annual basis (SPRC 2010). While some village operators cap the fee after a number of years (for example, 3.5 per cent a year for 10 years), in some cases fees can accrue for as long as the resident remains in the village. In addition, the village operators often retain a proportion of the capital gains (up to 100 per cent) generated when the property is resold (Blake and Craddock 2010; McCullagh 2014). Refunds to departing residents must be made within time frames specified by regulations (McCullagh 2014).

Box 4.3 An example of fees in retirement villages

The most common contract signed by new retirement village residents is likely to involve a refundable entry contribution, a deferred management fee (DMF) capped at a proportion of the entry contribution, a share of the capital gains to be retained by the operator, and recurrent charges (PwC 2015). According to research by Blake and Craddock (2010), the most common DMF was 3 per cent per year of residence, capped after 12 years (at 36 per cent), and the most common operator entitlement to capital gains was 50 per cent. The example below illustrates these common fees and charges.

In 2015, the average entry contribution for a two bedroom unit in a retirement village was \$385 000 (PwC 2015). Assuming a resident stays for 12 years and annual capital growth is 3.5 per cent, the resale value of the unit would be about \$562 000.

Upon departure, the entry contribution would be refunded. The resident would need to pay the DMF, charged at \$138 600 (36 per cent of \$385 000). In addition, the operator would retain \$88 544 of the capital gain (50 per cent of the difference between the entry contribution and resale price). Therefore, the resident would receive:

$$\begin{array}{rcccccc}
 \$385\,000 & - & \$138\,600 & + & \$88\,544 & = & \$334\,944 \\
 & & \text{Deferred} & & \text{Resident's share} & & \\
 & & \text{management fee} & & \text{of capital gains} & &
 \end{array}$$

Different contract terms result in large changes in the resident's refund. For example, if the deferred management fee is calculated based on the resale value rather than the entry contribution, they will receive \$271 192, or 19 per cent less than they will receive in the scenario described above.

Under the leasehold model, similar conditions apply. The entry contribution is equivalent to the market value of the property and upon departure, the resident is entitled to a lease termination payment minus the DMF. In some cases, a leasehold resident will not receive their payment until a new resident takes over the lease (Blake and Craddock 2010).

There is considerable variation in villages' fees, and at times, different residents within the same village may be subject to different fee structures. The way fees are set changes over time, to reflect demand for dwellings, changes in ownership and fluctuations in property prices, which may affect the level of entry contributions, the share of capital gains charged and other contract terms (SPRC 2010).

The different fee structures make it difficult to compare the affordability of different villages, and may create uncertainty and confusion for prospective residents (a problem

that regulators are trying to overcome through standardised disclosure documents – see regulation section below) (SPRC 2010). A further concern for prospective residents is the availability of professional legal and financial advice before signing a contract. The cost of this advice can be high and only a limited number of solicitors specialise in this area (LACA 2007; Parliament of South Australia 2013).

While the quality of information provided to prospective residents on the fees payable could be improved in some instances (for example, by providing examples of typical fees), it is important to realise that the retirement village fee structure also offers benefits to residents. This model allows residents to access home equity, as well as defer a large proportion of their housing costs to a later stage in life.

CRA eligibility for residents

Residents who receive the Age Pension may also be eligible for CRA. However, to receive CRA, residents¹⁷ must pay an entry contribution that is lower than the ‘extra allowable amount’.¹⁸ In June 2014, this threshold was \$146 500 (DHS 2014a). This threshold is likely to be much lower than the entry contribution paid by many residents, given that the average entry contribution for a two bedroom unit in 2014 ranged between \$308 000 in South Australia and \$411 000 in New South Wales (PwC 2014). As a result, although the majority of residents receive the pension, a much smaller proportion also receive CRA. In 2009, only 3 per cent of retirement village residents were eligible for CRA, down from 30 per cent a decade earlier (SPRC 2010).

There seems to be an inequity between MHE residents, who are considered to be renters even if they own their dwelling, and therefore receive CRA, and retirement village residents, who do not receive CRA as they are considered home owners once their entry contribution passes the asset test threshold. While retirement village residents have higher security of tenure than those living in a MHE, they do not own their homes. In practice, this means that households with similar means purchasing similar accommodation will be treated differently for the purposes of CRA eligibility, based on the type of accommodation they choose, and this may skew housing decisions. More consistent and neutral treatment of the different age-specific housing options for the purposes of CRA would contribute to better housing decisions for older Australians.

¹⁷ Residents in rental villages, where there is no entry contribution, will be eligible for CRA if they receive the Age Pension. Very few retirement villages offer rental accommodation (Blake and Craddock 2010; SPRC 2010).

¹⁸ The extra allowable amount is defined as the difference between the non-home owner and the home owner thresholds, which are part of the Age Pension asset test, at the time the entry contribution is paid. If the entry contribution paid is lower than this amount, the resident is not considered to be a home owner. As a result, they may be eligible for CRA and their entry contribution is included in the assets test for the Age Pension. However, if the entry contribution paid is higher than the extra allowable amount, the resident is considered a home owner, they are not eligible for CRA and their entry contribution is not included in the assets test (DHS 2014a).

Regulation

In 2011, the Commission recommended that state and territory governments pursue nationally consistent retirement village legislation (PC 2011). This is yet to occur, and retirement villages are regulated separately by each state and territory.

The regulation of retirement villages relates primarily to consumer protection issues (Gadens 2014). This includes the contracts signed between operators and residents, defining the various tenure types offered by operators, fees payable, cooling off periods, and dispute resolution. Villages need to be registered in all jurisdictions (annex B includes a summary of regulatory arrangements). Larger operators also participate in a voluntary accreditation scheme (Retirement Living Council nd).

All jurisdictions stipulate certain information that needs to be provided to prospective residents and certain matters that need to be specified in contracts. The level of detail and uniformity provided differs between jurisdictions — in the case of New South Wales, for example, operators must use a standard contract (Gadens 2014). While these were introduced in an attempt to assist consumers, researchers suggest that this has not lessened the complexity of the documentation (Craddock and Blake 2012).

Operators have argued that the prescriptive regulations around their business models, and in particular the structure of fees, inhibit flexibility in the industry. According to the Retirement Living Council:

- new developers are prohibited from retaining any deposits paid by future residents to secure units in retirement villages that are being built. This raises the cost of financing new developments relative to other residential property developers
- operators are restricted in the payment options they can offer. For example, residents cannot prepay any of their recurrent charges and operators are not allowed to release any part of the entry contribution before a resident moves out
- it is difficult to convert units within retirement villages for alternative purposes, such as aged care beds (to allow ageing in place), offering short-term accommodation for residents' visitors, and offering rental units within a village (Retirement Living Council, pers. comm., 29 July 2015).

To the extent that the state regulations constrain the ability of operators to offer products and services that would enhance the housing choices of older Australians (for example, offering a variety of payment options), there may be a case for further review by state regulators. Any changes to payment options should balance the need for innovation with the need for clear disclosure, and avoid introducing further complexity.

Beyond concerns regarding the implications of consumer protection regulation, retirement village operators have also stated that planning and development policies present a substantial barrier to expansion. There are only a limited number of state-wide planning

policies that deal with housing for older Australians,¹⁹ and industry operators argue that in some cases these policies are not consistently implemented by local governments. Planning policies do not differentiate between retirement villages and other residential developments, despite the higher costs involved in constructing retirement villages. This may disadvantage developers of retirement villages attempting to acquire land (RPS 2015). Addressing concerns about the planning system is likely to benefit a number of sectors across the economy, including retirement villages.

Co-location with residential aged care

Since their inception, some retirement villages were co-located with residential aged care facilities (Jones et al. 2010). Currently, researchers estimate that about a third of retirement villages are co-located with aged care facilities. Their residents are likely to be older and in need of assistance with activities of daily living, compared with residents in other retirement villages (Towart 2013a).

Co-location with residential aged care can offer benefits to operators and residents. According to a large scale survey of aged care operators, co-located facilities were able to charge higher accommodation fees, and the value of the retirement village units increased when co-located. Further, cost sharing between retirement village and aged care operations resulted in improved financial performance (Grant Thornton 2009).

For residents, the availability of assistance in the case of declining health was a key feature that drew them to retirement villages (Crisp, Butterworth and Anstey 2013). However, access to subsidised aged care services depends on obtaining approval from the Aged Care Assessment Team (Jones et al. 2010). In some jurisdictions, operators of co-located facilities are required by regulation to emphasise to prospective residents that access to co-located aged care is not guaranteed. Past surveys of retirement village residents found that many expected to be able to move into aged care when the need arose:

[M]any residents (and their families) living in retirement villages co-located with a residential aged care facility believed that a place would be made available for them when required. Such assumptions were misplaced, and often resulted in a great deal of frustration for older people and their families. (Cheek et al. 2007, p. 15)

According to industry stakeholders, co-location of retirement villages and aged care facilities is likely to continue expanding, as consumers look for housing that allows them to age in place, and providers look for ways to attract more residents and increase unit values. Nearly all new retirement villages currently under development are either co-located with aged care or are being built close to aged care facilities. While obtaining

¹⁹ In New South Wales, there is a separate State Environmental Planning Policy for Seniors Housing, which also covers retirement villages. In Western Australia, the Residential Design Code includes specific incentives for retirement village development; however, local governments may choose not to adopt the code (RPS 2015).

approval to operate a retirement village or a residential aged care facility can be an onerous task, government policy does not appear to be inhibiting co-location.

Aged care services in retirement villages

About one in five retirement village residents receives publicly funded home care services (McCrindle Baynes 2013). Aged care services in retirement villages can be outsourced or provided directly by the village operator. Government funding may be available for services that are not part of the ongoing maintenance responsibilities of the operator to residents (such as external maintenance or gardening) (DSS 2015e).

The delivery of home care services within retirement villages can have advantages over services delivered in the community. These advantages were highlighted in the evaluation of Retirement Villages Care Pilot, an initiative funded by the Australian Government between 2003 and 2006. The pilot entailed 280 flexible care places that were offered by ten retirement village operators, to address the aged care needs of eligible residents (AIHW 2006).

The pilot enabled village operators to provide services more flexibly, due to the structure of funding, and more cost effectively, due to the co-location of recipients. This allowed for greater continuity of care compared with other community aged care programs. Co-location of recipients had other benefits such as preventative health care and effective medication management (AIHW 2006).

The successful pilot led to the development of the Retirement Villages – Ageing in Place initiative, which was funded in the 2006-07 Federal Budget. The initiative encouraged retirement village operators to become approved providers and offer community aged care services to residents (DoHA 2006). By 2010, researchers reported that ‘take-up of the initiative has been variable but growing’ (Jones et al. 2010, p. 35). Currently, there is no specific funding allocation for home care places in retirement villages.

Ongoing reforms in the aged care sector may make it easier for retirement village operators to provide aged care services or expand the care services they offer. For example, after 2015, retirement village operators that are also approved home care providers will no longer need to apply to the Australian Government to have funding allocated to them (DSS 2015i). This may encourage more older Australians to consider downsizing, as the availability of support services is a major consideration for those moving into retirement villages (Crisp, Butterworth and Anstey 2013).

However, stakeholders in this study have raised concerns about the ability of retirement villages to provide the full suite of aged care services, by converting retirement village dwellings into residential aged care units. Beyond the constraints that the Australian Government imposes on the supply of residential aged care beds (see below), building, planning and zoning regulations prevent the conversion of retirement village dwellings to residential aged care units (Retirement Living Council, pers. comm., 29 July 2015). At the

same time, aged care providers are prohibited from investing funds received as refundable accommodation deposits in the development of retirement villages (DSS 2015a).

4.7 Residential aged care

Residential aged care provides a range of accommodation and care options for older people who are unable to continue living independently in their own homes (PC 2011). While the accommodation available is a factor in older people's choice of aged care facility, the decision to enter aged care is usually motivated by declining health, cognitive impairment, requiring extensive assistance with activities of daily living and lack of social support (Kendig et al. 2010).

Between 2003-04 and 2013-14, the number of people in residential aged care grew by 27 per cent to 231 515.²⁰ However, usage rates (the proportion of residents in the population of people aged over 65) have declined from 7.2 per cent to 6.7 per cent. This decline reflects individuals' preferences to age in place. Those who are admitted into aged care are usually older people with complex health needs — 74 per cent of people are aged over 80 at the time of admission, and over 75 per cent of residents require high level care (AIHW 2012, 2014c; SCRGSP 2015).

The profile of operators has also changed over time, with more large-scale, for-profit provision. About a third of operators are private for-profit enterprises, and their share of residential aged care beds has grown in recent years from 32 per cent in 2006, to 37 per cent in 2014. The total number of aged care services has declined by 8 per cent over the same period, to about 2700 (SCRGSP 2015).

Accommodation in aged care

The accommodation standard in the industry has changed in recent years, with multi-bed wards replaced by individual rooms due to residents' demand for better accommodation options (for example, catering for couples entering aged care together) that offer privacy and personal space (Colliers 2015; Grant Thornton 2008). Amenities and services have also evolved in response to demand and resident expectations, leading to 'modern facilities [that] are less institutional with resident amenities, recreation and rehabilitation, storage and common areas that are more expansive' (Grant Thornton 2008, p. 5).

Improvements in accommodation standards have been supported by aged care policies. For example, since July 2014, newly built or significantly refurbished facilities are eligible for higher subsidies (DSS 2014c). Over time, regulatory requirements and resident demand

²⁰ A further 48 295 people received respite care in residential aged care facilities during 2013-14 (SCRGSP 2015).

have led to a decline in the average number of residents per room, from nearly 1.6 in 1999, to 1.2 by 2007 (Grant Thornton 2008).²¹

From the providers' point of view, modern single-room facilities generate much lower returns compared with older institutional nursing homes. Modern facilities require more staff, and therefore have higher wage costs. They also cost more to build compared with older style nursing homes (Grant Thornton 2009). Due to the rising costs of land, many of the new facilities are being built in outer suburbs, despite the strong preference of older people to move into residential aged care facilities located in established suburbs, close to their families (Grant Thornton 2008).

Fee structure and government subsidies

Older Australians in residential aged care are responsible for their own accommodation costs, and may receive some subsidies from government, depending on their assets and income. Care costs are mainly met by government, with some residents contributing to the cost of their care via means-tested fees. Aged care providers derive the bulk of their revenue from care fees and subsidies (figure 4.3).

This section will mainly describe costs relating to accommodation (appendix B provides further detail on the funding and delivery arrangements of aged care services).

All residents entering aged care after July 2014 are charged fees for their accommodation. In principle, residents are responsible for their own accommodation costs. However, about 40 per cent of residents in aged care are considered 'supported' residents, and are eligible for subsidised accommodation.

In addition, residents must pay:

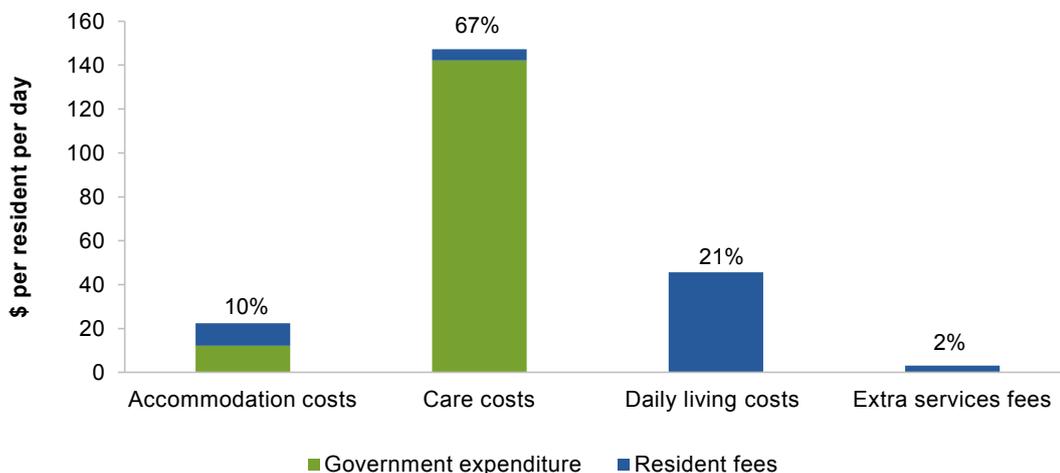
- a basic daily fee, amounting to 85 per cent of the Age Pension and intended to pay for daily living costs²²
- a means-tested care fee (ACFA 2015).

Those who are required to pay for their accommodation can choose to do so as a daily accommodation payment (DAP), a refundable accommodation deposit (RAD) or a combination of the two. If they choose a RAD, payment is due within six months (ACFA 2015). This allows new residents time to sell their former home if required. Since the introduction of the new fee structure, 41 per cent of new aged care residents chose to pay a RAD for their accommodation, a further 35 per cent paid a DAP, and 24 per cent chose a combination of RAD and DAP (ACFA 2015) (see appendix B for a full description of fees and charges).

²¹ One survey of residential aged care facilities found that only 38 per cent of high care services offered shared rooms (Grant Thornton 2009).

²² Based on September 2015 payment rates, the basic daily fee was \$47.86 (DSS 2015o).

Figure 4.3 Sources of revenue for residential aged care providers
2013-14



Source: ACFA (2015).

The choice of payment option may be affected by Age Pension means testing arrangements, which create incentives to pay residential accommodation costs through RADs (for residents who have sold their home), as they are exempt from the Age Pension assets test. However, RADs are generally included as assessable assets for the purposes of determining means-tested aged care costs (DSS 2015h) (see chapter 5 for a discussion on asset tests).

Some participants in the Commission’s aged care inquiry suggested that residents chose to pay large lump sums because they are not well informed about their payment options (PC 2011). From 2014, providers are required by legislation to publish information on accommodation prices and features, and an explanation of payment options in a consistent format (DSS 2014i). The increase in pricing transparency was expected to affect cash flows for residential aged care providers, as some residents switched from lump sums to daily payments, depending on individual circumstances. However, any decline in income was likely to be offset by the new fee structure, introduced as part of the reform (KPMG 2013). Early reports indicate improved financial results in the residential aged care sector since the reforms (ACFA 2015).

Regulation of supply

Residential aged care is regulated by the Australian Government, as part of the *Aged Care Act 1997* (Cwlth). Under the Act, the Australian Government regulates the establishment of new residential aged care services, ensures the quality of care and provides ongoing funding for the operation of services (DSS 2014a).

To be eligible for government funding, residential aged care services must be operated by an approved provider and be accredited by the Australian Aged Care Quality Agency. To become approved, applicants must demonstrate their suitability to provide aged care, including their experience in the sector and their ability to meet quality standards, their record of financial management, and the suitability of key personnel (DSS 2014k).

Once approved, a provider can only commence or expand their operations if they have been allocated residential aged care places by the Department of Social Services, or have purchased an allocation of places from another approved provider. Each year, new places are allocated based on an extensive planning system, that aims to ‘allocate places in a way that best meets the identified needs in the community’ (DSS 2014f, p. 17) (appendix B provides further detail).

While ensuring a consistent level of provision, the planning system for aged care has had negative implications for competition in the sector:

The Government utilises planning ratios to evenly distribute services across Australia; however, because these control the availability of aged care places there is an artificial scarcity that limits the scope for competition. This lack of competition decreases the normal pressures for efficiency and innovation, and can deprive consumers of choice

Current policies are relatively effective in providing for equitable access to aged care services. However there is scope to achieve these goals in ways which are less complex and would provide for greater flexibility and stronger competition. (DoHA 2012, p. 10)

Stakeholders have also raised concerns about the effects of the Australian Government’s regional planning approach on the location of new aged care services (PC 2011). The planning regions cover a large number of communities and new facilities may not necessarily be constructed where demand is highest.²³

A review of supply side restrictions in aged care has been foreshadowed for 2017 (KPMG 2013). Under current policies, both the supply side and the demand side of the aged care market are restricted. The regional planning approach sets limits on the number of new aged care beds, and in addition, each prospective resident undergoes an extensive needs assessment to establish whether they are eligible to enter residential aged care, and which level of service they should receive. While rationing the provision of subsidised aged care services based on individual needs is important given the high cost to government, the additional restrictions imposed on providers act primarily to stifle competition and innovation. Removing supply restrictions, coupled with changes to funding structures, is expected to generate more competition in the aged care sector, particularly based on the standard of accommodation offered.

In its 2011 inquiry, the Commission recommended removing all restrictions on the supply of aged care places, including residential and home care. It highlighted the fact that the

²³ For example, Tasmania is divided into only three planning regions, while the city of Melbourne and its surrounding areas comprise four planning regions (DSS 2015c).

Government’s fiscal exposure to residential aged care can be managed in ways other than supply restrictions, such as setting appropriate criteria for individuals’ needs assessments and determining co-contribution schedules. Some progress has been made towards relaxing supply restrictions (appendix B). In coming years, the removal of supply restrictions in aged care should remain an important policy goal for the Australian Government.

4.8 Common issues across housing options

There are substantial similarities between the issues faced by providers and consumers of age-specific housing, including residential aged care (table 4.4).

Table 4.4 Common policy issues affecting the provision of housing for older Australians^a

	<i>Home owners</i>	<i>Private Rental</i>	<i>Social housing</i>	<i>Mobile home communities</i>	<i>Retirement villages</i>	<i>Residential aged care</i>
Planning	Planning delays may affect the development of appropriate housing for older people					
Information provision	Older people should have access to timely information on the support services available to them if they wish to remain in their homes.				Substantial complexity of financial arrangements remains — further consideration of simplifying funding structures and improving the information provided to consumers	
Security of tenure		Legislation to enhance security of tenure		Legislation to enhance security of tenure		
Regulatory burden					Restrictions on business models should be reviewed	Supply restrictions should be removed
Subsidies		Cwth Rent Assistance should be reviewed to ensure effectiveness	Government funding cuts affecting supply	Cwth Rent Assistance should be reviewed to ensure effectiveness	Cwth Rent Assistance should be reviewed to ensure effectiveness	

^a Blue shaded boxes refer to policy areas that are the responsibility of the Australian Government; green shaded boxes refer to areas that are the responsibility of State Governments.

Consumers need better information

From the consumers’ point of view, the ability to make better housing decisions hinges on the availability of information both on the housing and care choices available to them and their costs, as well as longevity risks and the probability of requiring aged care (chapter 2). The Commission’s survey found that older Australians are poorly informed about the costs

of aged care, as well as the range of home care services available to them. Fewer than 10 per cent feel they are well informed about government funded services to assist them in their own homes. Only about 20 per cent of older Australians are aware of the aged care reforms, and a similar proportion feel they are well informed about the costs associated with moving into residential aged care (Commission survey).

The type of information provided to older Australians regarding their housing and care options, as well as the efficacy of communications, need to be considered by the Australian Government as reform implementation continues in the aged care sector.

Aiming for more flexibility in age-specific housing

Existing and prospective residents of age-specific housing are faced with highly complex financial decisions, given the way that fees are structured for MHEs, retirement villages and residential aged care. Not only is the structure of fees highly complicated and variable, but the contracts that older Australians must sign with operators can be very complex. In the case of retirement villages, all jurisdictions impose disclosure requirements on village operators; however, researchers have questioned the effectiveness of these disclosure documents in ensuring residents understand the contract they are entering into (Cradduck and Blake 2012). Disclosure requirements for MHEs vary substantially by jurisdiction.

Some jurisdictions are introducing standardised disclosure for MHEs and retirement villages, and this is likely to benefit prospective residents, as it may make it easier to compare the affordability of different options. Further disclosure and consumer protection should be balanced against the need to allow more flexibility in the market place (for example, through relaxing restrictions on payment options), which is likely to benefit both providers and residents.

Choices are affected by broad housing policy settings

For providers of age-specific housing — similar to many other sectors involved in housing and construction — gaining planning and development approvals for new dwellings or the redevelopment of existing housing can inhibit growth. For example, in Queensland, retirement village operators argue that planning schemes are a substantial barrier to expansion, as the way applications are assessed is inconsistent, and the costs involved lead to higher fees for residents (Transport, Housing and Local Government Committee 2012). Similarly, aged care operators in Western Australia have reported inconsistent and lengthy approval processes, which create substantial delays in constructing and redeveloping aged care facilities (Aged and Community Services Western Australia, pers. comm., 28 July 2015). Addressing the inefficiencies in Australia's planning system is likely to benefit many aspects of the housing market, including those relevant to older Australians.

Residents in different types of age-specific housing are eligible for different levels of assistance from the Australian Government. For example, households with similar income

and assets living in similar homes may receive CRA if they live in a manufactured home estate, but not if they live in a retirement village. This appears inequitable, and there is scope to review policy settings to ensure people in comparable circumstances are treated similarly. A dedicated review of CRA is also warranted in the context of the private rental market, where older Australians face substantial affordability pressures.

Private renters, as well as some residents of manufactured home estates, are affected by the low security of tenure offered by current residential tenancy legislation. It is important to review state-based protections offered to tenants to ensure security of tenure is improved. However, it is also important that any changes do not create disincentives for landlords to rent their properties to older Australians, if such a move is seen as limiting their flexibility in managing their assets.

Social housing is an important housing alternative for older Australians with low incomes, as it offers affordable rents and secure tenure. Older Australians already account for a substantial proportion of social housing tenants, and this creates challenges for providers who need to consider the needs of their ageing tenants. Further, the available stock of social housing has not kept pace with demand and prospective residents face long waiting times. As a result, many older Australians remain in the private rental market for long periods of time, which places them at risk of substantial disadvantage.

Considerations for future policies

The availability of suitable housing for older Australians should be an important consideration for policies designed to address the needs of an ageing population. Responsibility for this lies both with state and territory governments, which design the overarching housing strategies, and local governments, which are responsible for their implementation.

Currently, specific policies that affect older Australians' housing decisions are very fragmented, and there is no strategy that recognises the spectrum of choices, and their effects on aged care services. This patchwork of policy makes it difficult for older Australians to transition from one form of housing to another, as their care requirements change. Future policy should aim to support transitions along the age-specific housing spectrum (for example, from retirement village to residential aged care) by streamlining the information provided to prospective residents, and ensuring operators can expand their service offerings to cater for residents' needs. Regulations should not inhibit the development of integrated aged care solutions, which offer a variety of housing and care options.

A major challenge for policy makers is addressing the housing needs of older Indigenous Australians. The lower life expectancy and the poor housing conditions among the Indigenous population put older people at risk of further disadvantage. Older Indigenous Australians are far more likely to be in public housing, compared to the general population, and they often face difficulties accessing residential aged care that is appropriate to their needs and cultural preferences (chapter 3). Their use of home and community care is

nearly four times higher than the general population; however, this is not reflected in planning ratios (AIHW 2011; Cotter et al. 2011). Housing and aged care policies must ensure that older Indigenous Australians have access to housing options that address their needs and preferences.

More broadly, the housing decisions of older Australians occur within the context of the general housing market. Issues such as housing affordability and availability, the effect of planning and zoning systems, community concern regarding higher density developments in suburban areas — all have direct implications both for the housing wealth of older Australians and for the options available to them if they decide to relocate. Addressing market failures in the housing market will have benefits for older Australians, as well as the broader community.

Annex A Mobile home communities regulations

	NSW	Vic	Qld	SA	WA	Tas	NT	ACT
MHE legislation separate from other residential tenancies	Yes. New Act commenced in November 2015	No. Separate section in Residential Tenancies Act	Yes ^a	Yes	Yes	Residents may be covered by the Residential Tenancy Act	Yes, but Act only covers people who stay for longer than 12 months ^b	Residents may be covered by the Residential Tenancy Act
Caravan park legislation separate from other residential tenancies	Yes (same Act as MHEs)	No. Separate regulations under the Residential Tenancies Act	No	Yes (same Act as MHEs)	Yes (same Act as MHEs)	May be covered by the Residential Tenancy Act	Same as MHE	May be covered by the Residential Tenancy Act
Disclosure to prospective residents ^c	14 days before signing contract ^d	20 days before signing contract for MHE only	Yes – time not specified	Yes – to be given before or at time of signing	Yes – time not specified	No	Limited	No
Cooling off period	14 days	5 business days only for MHE	28 days (with some conditions)	No	5 business days	No	No	No
Rent increases	60 days' notice ^e	60 days' notice. Rent can only increase once in 6 months	Caravan parks – 60 days' notice MHE – 28 days' notice	Rent can only increase once in 12 months (generally)	60 days' notice. Rent can only increase once in 6 months	As per residential tenancies, if applicable	30 days' notice. Rent can only increase once in 6 months	As per residential tenancies, if applicable
Termination without grounds	Residents cannot be evicted without grounds	120 days' notice	Require 60 days' notice in caravan parks. MHE residents cannot be evicted without grounds	60 or 90 days' notice, depending on agreement type	60 or 180 days' notice, depending on agreement type	As per residential tenancies, if applicable	90 days' notice	As per residential tenancies, if applicable
Consultation with residents	Resident committee may be formed as a representative of residents	Resident committee may be formed as a representative of residents in a MHE	Resident committee may be formed as a representative of residents in a MHE	Resident committee may be formed and must be consulted by operator if established	Resident committee required if more than 20 long-stay residents on site	No	No	No

^a MHE legislation may also apply to converted caravans. ^b In caravan parks that also offer holiday accommodation, residents must stay for longer than five years to be covered by the Caravan Parks Act. ^c Standard disclosure documents include the agreement between operator and resident, a copy of park rules, and information about legal rights.

^d The new legislation also introduced compulsory standard site agreements. ^e Notice periods can vary depending on the contract.

Annex B Retirement village regulations

	<i>NSW</i>	<i>Vic</i>	<i>Qld</i>	<i>SA^a</i>	<i>WA</i>	<i>Tas</i>	<i>NT</i>	<i>ACT</i>
Definition of retirement village	Complex for retirees who signed prescribed village contracts	Complex for retirees where at least one pays ingoing contribution and services differ from aged care	Complex for retirees where all residents pay ingoing contributions	Complex for retirees where at least one pays an ingoing contribution	Complex for retirees where at least one pays an ingoing contribution	Complex for retirees where at least one pays an ingoing contribution	Complex for residents who are retired	Complex for retirees who signed prescribed village contracts
Registration other than Title Office	No	Yes – with Consumer Affairs	Yes – with Department of Housing	Yes – with Department of Health	No	No	No	No
Contract	Standardised	Structure and content as per regulations	Content as per regulations	Content as per regulations	Content as per regulations	Content as per regulations	Content as per regulations	Structure and content as per regulations
Prescribed disclosure documents ^{b,c}	General inquiry document and disclosure statement	Information factsheet and pre-contract disclosure statement	Public information document	Condition report, residence rules, remarketing policy and other documents	Information statement, notice of rights, and residence rules	Legal notice of rights and checklist	Disclosure document and checklist	General inquiry document and disclosure statement
Cooling off period ^d	7 business days	3 business days	14 days	15 business days	7 business days	5 business days	10 business days	7 business days
Increases in ongoing fees	Increase higher than CPI must be explained and consented to by residents	Increase higher than CPI must be explained and consented to by residents	Increase higher than CPI must be consented to by residents	Can increase by a 'reasonable' level	Not specified	Can increase by a 'reasonable' level	Increases not specified but need to be agreed to by residents	Increase higher than CPI must be explained and consented to by residents
Payment of fees after moving out ^e	Fees payable for max 42 days after moving out	Fees payable for max 6 months after moving out	Fees payable in full for 3 months, and then at a reduced rate for the next 6 months	Fees payable for max 6 months after moving out	Fees payable for 3 months (6 months if contract signed before April 2014) after moving out	Not specified	Not specified	Fees payable for max 42 days after moving out ^g
Refund of ingoing contribution ^f	Within max 6 months	Within max 6 months, unless moving into aged care	Within 14 days after unit resold	Within 10 days after unit resold, unless moving into aged care	Within max 45 days	Within max 6 months, unless moving into aged care	Within max 6 months	Within max 6 months

a New regulations will commence in South Australia in 2016. **b** In some cases (such as Western Australia) contracts and disclosure documents must include specific warnings about access to aged care. In other cases, such as New South Wales and the ACT, making representations about aged care availability can be an offence. **c** The documents must be in accordance with the structure and content included in the regulations. In all jurisdictions, other documents such as village budgets or village rules must be given or be made available on request. **d** New South Wales, South Australia and the ACT also allow for a 90 day settling in period. During this period, a resident can leave the village and only be charged fair market rent, for any repairs in excess of fair wear and tear, and an administration fee. **e** In all cases, ongoing fees are not payable once a new resident moves in. When vacating a unit, the former resident may also be charged for some or all the costs of refurbishment. Different arrangements may apply to strata title owners. **f** These timeframes do not apply for residents in strata villages, who purchased the unit, and receive any proceeds when a sale occurs, with no time limits. **g** Different regulations apply for retirement villages operating under the leasehold or company title model.

5 Tax and transfer treatment of housing

Key points

- In general, the tax and transfer treatment of housing in Australia favours home ownership over renting and over investment in other assets.
- The exclusion of the principal residence from the means test for the Age Pension may encourage investment in housing at the expense of other assets, and provides a marginal disincentive for older Australians to downsize to a home better suited to their needs and preferences.
 - In principle, including the full value of the principal residence in the Age Pension assets test would improve efficiency and equity.
 - However, given that support for home ownership is embedded in many government policies and in people's retirement planning, removing the exemption entirely in the immediate future is intractable.
 - At a minimum, there is a strong case on equity grounds for setting limits on the value of the principal residence that is exempt from the Age Pension means test.
- Stamp duties act as a barrier to housing mobility, and can discourage downsizing by older Australians.
 - Stamp duty concessions, which are available in some jurisdictions of Australia, may ameliorate some of the inefficiencies of stamp duties. However, they also raise concerns about fairness.
 - There is merit, on efficiency grounds, in making the principal residence subject to land tax and removing stamp duties on housing transfers.
- The inconsistencies in the treatment of assets across means tests for home care, residential aged care and the Age Pension result in mixed incentives, and are a source of unnecessary administrative complexity and confusion for older Australians — especially given that the means tests for the Age Pension and residential aged care are complex in their own right.
- There are equity grounds for incorporating the full value of a resident's former principal home in the means test for aged care.

The principal residence typically constitutes the majority of the wealth of older households. At the same time, a significant majority of older Australians rely primarily on a means tested Age Pension as well as other forms of government support for aged care and accommodation (chapter 3).

The way in which housing is treated by the tax and transfer system poses both efficiency and equity concerns. Tax and transfer policies can affect choices on whether to remain in one's current residence or relocate, as well as on whether to draw on housing wealth for income.

A key indicator of the efficiency and equity of the tax and transfer system, as it relates to housing decisions, is whether it treats different types of housing tenure, as well as different types of investments, in a neutral way. These and other efficiency and equity issues are discussed in this chapter.

5.1 The principal residence and the Age Pension

Features of the Age Pension in Australia

Australia's Age Pension is subject to a means test that incorporates income and assets tests (figure 5.1). An individual (or couple's) level of assets and income affects their eligibility for the Age Pension, as well as the amount of Age Pension they are entitled to receive. A range of assets are subject to the assets test, including: real estate, granny flat interests, life interests, financial investments, superannuation investments, income streams and business assets. Some assets are exempt from the assessment, including the principal residence (DHS 2015b).²⁴ Retirement village contributions in excess of the 'extra allowable amount' (defined as the difference between the home owner and non-home owner asset test thresholds) are also exempt from the assets test.

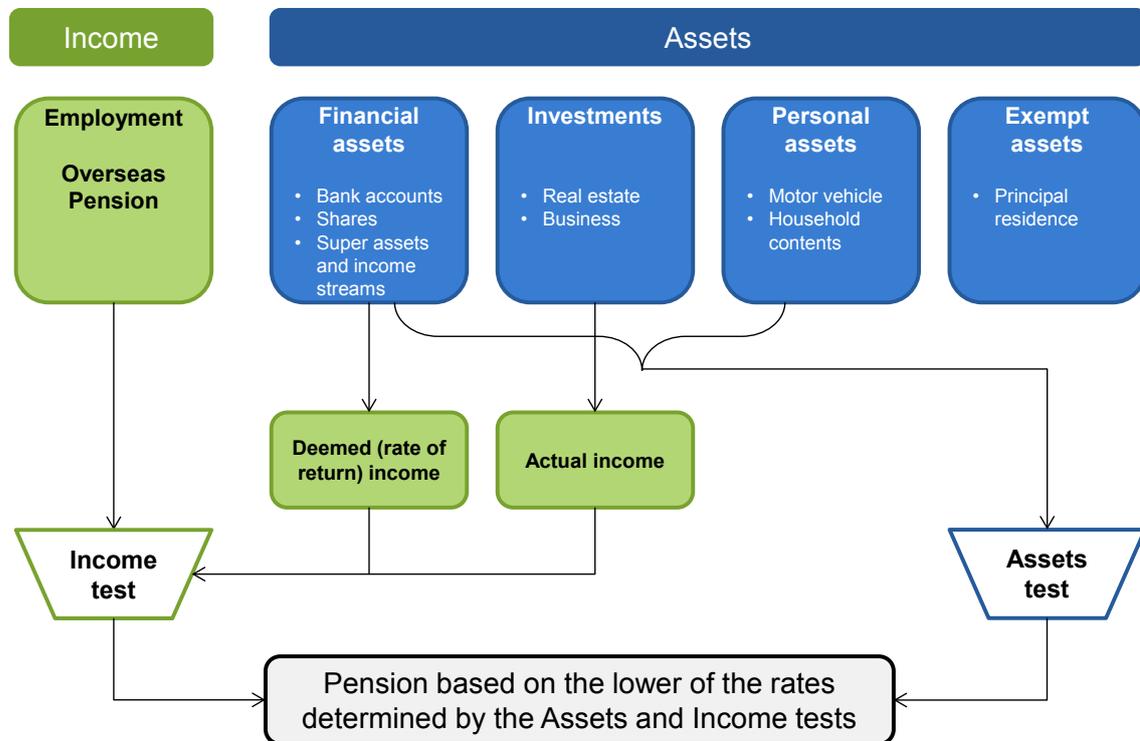
The principal residence is also not included in the means tests for most other Australian Government transfer payments, such as Family Tax Benefits Part A and B, Child Care Benefit, and Parental Leave Pay.

For those whose assets or income make them ineligible to receive the full Age Pension, payments are reduced by tapering. Currently, for income received beyond a threshold, pension payments are reduced by 50 cents in the dollar. For the assets test, every \$1000 in assets over the free area reduces Age Pension receipts by \$1.50 per fortnight (DSS 2014b).²⁵ The test that applies to a recipient is that which results in the lower rate of payment.

²⁴ Although the principal residence is formally exempt from the means test, non-home owners have a higher asset level exemption than home owners, so effectively the first \$149 000 of the value of the home is included in the home owner's assets test (where the assets test is the relevant means test).

²⁵ From 1 January 2017, the taper rate is scheduled to increase to \$3.00 per fortnight (Klapdor 2015).

Figure 5.1 An illustration of the means test for the Age Pension^a



^a A person's rate of pension payment is calculated by applying the income test and the assets test — whichever test gives the lowest rate of payment is the test applicable for that person.

Source: Adapted from Henry et al. (2009, p. 42).

In June 2013, there were over 2.3 million Age Pension recipients in Australia, which represented roughly 70 per cent of persons aged 65 and over in Australia (ABS 2015a). For the majority of people that receive a part pension, the income test is the reason for the tapering of payments (table 5.1), due to the relatively low thresholds at which the income test starts to apply, as well as the asset position of households. Furthermore, the assets test is virtually irrelevant for those who do not own their home. This likely reflects the relatively lower level of overall assets held by non-home owners. In 2011-12, median wealth for renters over 65 years of age was \$38 000. In contrast, their counterparts that owned the family home outright had net assets of approximately \$700 000, and home owners with a mortgage had median wealth over \$500 000 (chapter 3).

Table 5.1 Characteristics of Age Pension recipients

As at June 2013

	Number	Per cent
<i>Total</i>		
<i>Marital status</i>		
Married/de facto	1 336 393	57
Single/separated/divorced/widowed	1 015 746	43
<i>Home ownership</i>		
Home owner	1 766 926	75
Non-home owner	585 213	25
<i>Payment Status</i>		
Maximum rate	1 390 152	59
Reduced rate	959 775	41
<i>Payment under test (part pensioners)</i>		
Paid under income test	614 620	64
Home owner paid under assets test	334 923	35
Non-home owner paid under assets test	10 232	1
Income/asset test not coded	1 555	0.1
Total Age Pension recipients	2 352 139	100.0

Source: DSS (2014e).

What are the objectives of the principal residence exemption?

The history of the principal residence exemption from the pension means test dates back to the early 1900s. In June 1908, the Australian Parliament passed the *Invalid and Old Age Pensions Act* (Cwlth), which introduced means-tested age and invalid pensions, the former first coming into operation in July 1909 (ABS 1988). Initially, the means test for the Age Pension (which comprised separate property and income tests) gave concessional treatment for the value of the principal residence, but by December 1912, the full value of the principal residence was exempt from the means test (Clare 2008; Daniels 2011).

The exemption was justified at the time by the then Prime Minister, Andrew Fisher, on the basis that it would help make aged persons more independent of their relatives, and have positive effects on national prosperity:

Those who have built up a home ... are entitled to keep that home, and live in it if they can find the means ... Hitherto the best members of families have been called upon to contribute a most unequal proportion towards the support of aged or invalid parents and other relatives, and have thus been prevented from directing their means into productive channels ... we are able to make the recipients of these pensions practically independent of their relatives, and to do so more economically than is possible under any other system. (Fisher 1912, p. 6971)

Since the introduction of the principal residence exemption, the Age Pension underwent multiple changes including the abolition and reinstatement of the assets test, but the

principal residence exemption prevailed in various forms and guises. The exemption has persisted as home ownership rates rose from roughly 50 per cent in 1910-11 to almost 70 per cent in the 2000s (figure 5.2). Over the same period, life expectancy rose from 55 years for males and 59 years for females in the first decade of the twentieth century, to 80 years for males and 84 years for females by 2012 (ABS 2014).

The effects of the special treatment of the family home in the Age Pension have been the subject of many studies and reviews. However, over the years there have been scarcely any statements from Australian governments about the rationale of continuing with the policy.

One notable exception dates to the 1980s, when the Australian Government decided to reintroduce a previously abolished assets test, and established a panel to review the structure of the test. The panel recommended that the proposed assets test include the value of the principal residence because the alternative would be inequitable to renters (Stokes 2015). However, this recommendation was not followed. Then Prime Minister Bob Hawke explained the reason for doing so:

... there is a feeling ... throughout the community there is some special significance attached to the home. People don't like to feel that that is something which is included in some sort of testing in their rights in regard to the pension. And we have recognised that and have moved therefore to exclude the home, as it was indeed excluded in the first proposals. (Hawke 1984, p. 2)

What are the effects of the exemption?

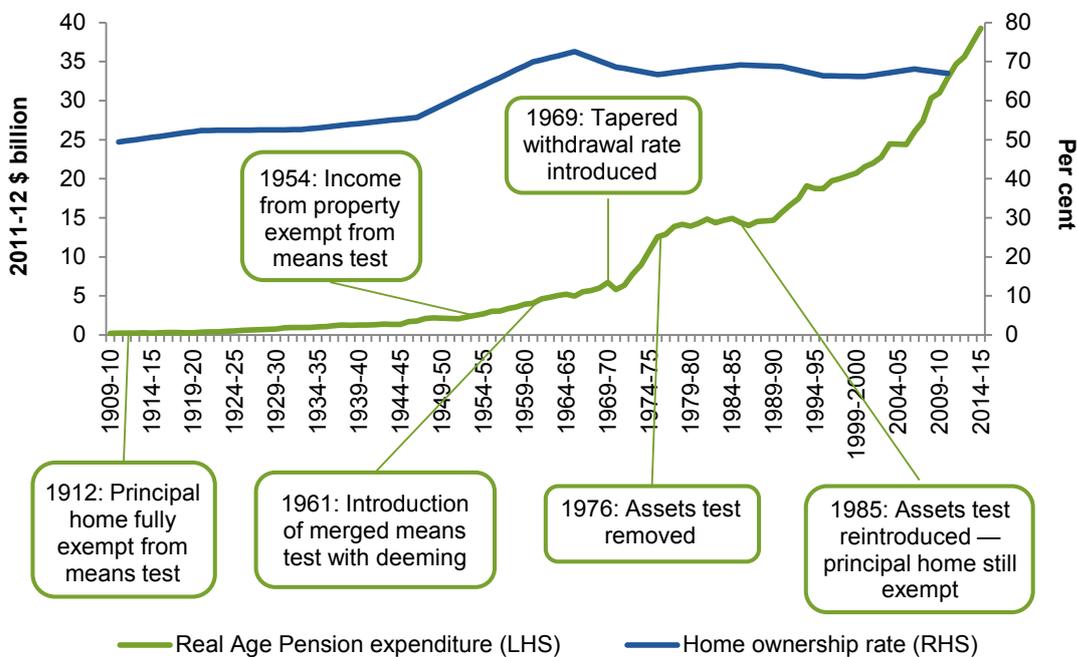
While the original rationale for exempting the principal residence from the Age Pension appears obsolete, the policy is now an ingrained part of both the Australian retirement savings and income system and the life course financial decisions of Australians.

One argument for retaining the exemption is that Australia's pension system now relies on home ownership and that any substantial changes to the exemption, if introduced in isolation, could create significant risks of poverty for a large number of pensioners. Home ownership is one of the pillars of retirement incomes. It can also perform a lifecycle income smoothing role (chapter 2). In addition, the principal residence can serve as longevity insurance, upon which retirees can draw for emergency purposes, and as a source of funding for aged care, in the event that other savings prove insufficient (Henry et al. 2009). In performing all of those roles, home ownership could also be argued to relieve the fiscal pressure on the Age Pension and other forms of government support.

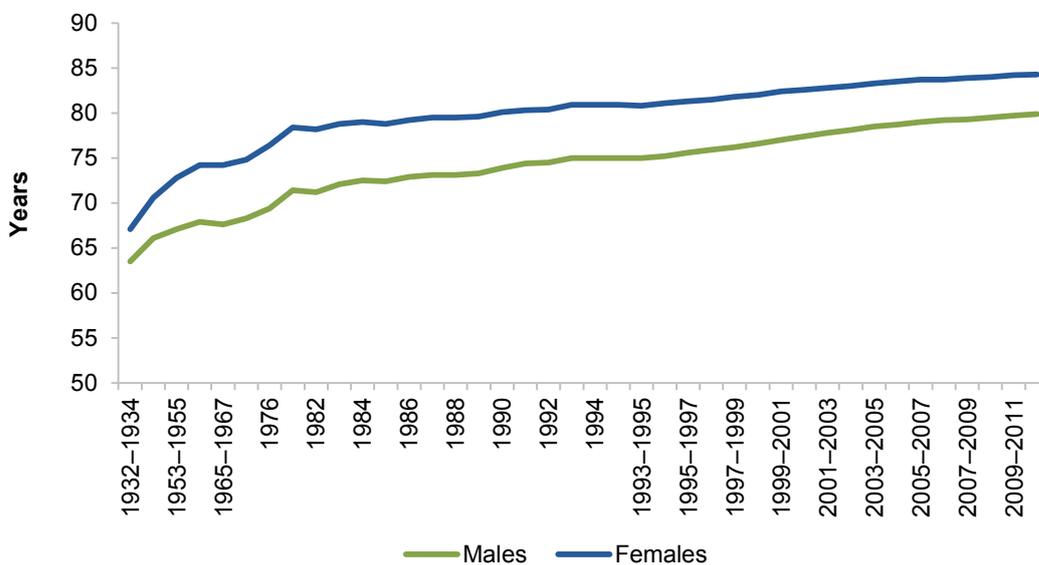
While all those benefits of home ownership cannot be denied, the key issue is whether the current structure of the Age Pension assets test distorts accommodation and investment choices of older Australians, leading to outcomes that are not beneficial for the community overall.

Figure 5.2 The Age Pension, home ownership, and longevity over time

(a) Age Pension and home ownership^{a,b,c}



(b) Life expectancy at birth



^a Data prior to 1970-71 comprise 'Old Age and Invalid' pensions. ^b Pension expenditure data recorded in pounds were converted to dollars using the rate £1 = \$2. ^c Age Pension expenditure is expressed in real terms, in 2011-12 dollars, and was deflated using the consumer price index from 1922 onwards. Data prior to 1922 were deflated using the Reserve Bank of Australia's pre-decimal inflation calculator.

Sources: ABS (*Australian Historical Population Statistics*, 2014 Cat. no. 3105.0.65.001; *Year Book Australia*, various editions, Cat. no. 1301.0; *Census of Population and Housing*, various editions); Clare (2008); Daniels (2011); DSS (2015m); RBA (2015a, 2015b).

The principal residence exemption provides a clear incentive for pensioners to own and live in their homes during retirement (AHURI 2014; Yates 2012). Retirees who decide to sell their principal residence may find themselves ineligible for the Age Pension due to the treatment of the proceeds of sale under the means test. Proceeds from the sale of the principal residence are treated as an exempt asset for up to 12 months if the proceeds are to be used to purchase a new principal residence. However, the proceeds are immediately deemed to generate income, which may affect eligibility under the income test. This can result in some retirees remaining in housing that is no longer suitable for their needs, so that their pension eligibility will remain intact.

The exemption may also encourage excessive investment in housing equity. The Commission has previously observed:

The current Age Pension assets test provides an incentive for older Australians to invest in their principal residence, encouraging capital into an asset that may not necessarily yield the best return for the individual or the nation. (PC 2011, p. 293)

Beyond these effects on incentives of older Australians, there is also a question of whether this arrangement is equitable. The exemption creates differences in the way otherwise similar pensioners are treated (box 5.1). In addition, issues of intergenerational equity arise under a pension system such as Australia's, in which current taxpayers fund entitlements for those who are currently of retirement age. As the proportion of the population who are of retirement age increases, a larger tax burden will be placed on working-age taxpayers in order to finance Age Pension costs (PC 2015c). This demographic shift raises questions about intergenerational equity.

Box 5.1 Evidence and views on the exclusion of the principal residence from the Age Pension means test

The exemption of the principal residence from the Age Pension assets test has a number of efficiency and equity effects. For example, it could discourage physically downsizing to potentially more suitable homes by older Australians (Daley et al. 2013; PC 2011). There is some empirical evidence to support this proposition. In a study of more than 2800 Australians who had moved at least once since turning 50, Judd et al. (2014) noted that many participants perceived the effect of downsizing on eligibility for the Age Pension as an obstacle to downsizing. Using data from the Household, Income and Labour Dynamics in Australia data set in a regression framework, Sane and Piggott (2011) compared the housing decisions of home owner pensioners and non-pensioners aged 65 and over. They found that although pensioners were more likely to move than non-pensioners, pensioners were less likely to downsize, thus providing support to the notion that the current Age Pension assets test discourages downsizing. The Commission's survey indicated that only a small number of older Australians who were unlikely to sell their home were motivated by concern about the effect that selling would have on Age Pension eligibility.

(continued next page)

Box 5.1 (continued)

The current treatment of the principal residence in the Age Pension assets test also has implications for equity. The National Commission of Audit (2014a) stated that exempting the principal residence from the assets test is inequitable, as it allows for high values of wealth to be sheltered from means testing, an observation also made in the Henry Review (Henry et al. 2010) and by researchers, such as Cho and Sane (2013).

Cowan and Taylor (2015) argued that current Age Pension arrangements in Australia are inequitable. They concluded that some pensioners with substantial housing wealth receive the Age Pension, potentially diverting resources from those in greater need of assistance (for example, renters). Cowan and Taylor also observed that because not all assets are treated the same under the Age Pension, pensioners in similar overall financial circumstances are treated differently, depending on whether they own a home or not.

Similarly, ACOSS (2015) stated that the exemption of the principal residence from the assets test compromises the equity of the Age Pension, because those with substantial wealth invested in their homes may receive a higher pension than those who are less wealthy overall.

Proposals for reform

Over the years, there have been a number of proposals to modify the test, and thereby enhance the efficiency and equity of the system. A number of recent reviews have recommended including a certain value of the principal residence in the Age Pension means test (box 5.2.)

What would be the effects of putting a limit on the exemption?

In principle, the best policy response to the distortionary and inequitable nature of the principal residence exemption would be to fully remove the exemption and include the entire value of the principal residence in a redesigned means test. This would result in a more equitable treatment of home owner and non-home owner pension recipients. The Age Pension assets test would treat the composition of assets more equally, ensuring that those who acquired wealth in the form of their own home were treated in a similar manner to those who held their wealth in non-housing assets.

However, given that home ownership is embedded in many government policies and in people's retirement planning, removing the exemption entirely in the immediate future is intractable.

Box 5.2 Suggested reforms to the Age Pension affecting housing**The Henry Review — cap for exemption**

The Henry Review (Henry et al. 2010) suggested that to increase the fairness of the means test for the Age Pension, a cap should be applied to the exemption of the principal residence — amounts above a specified cap would be included in the assets test, and be subject to deeming. It was argued that this arrangement would make an allowance for the primary role of housing in providing shelter, but also recognising that beyond this basic function, housing represents an asset that people purchase with an expectation of generating a future return. Henry et al. (2010) stated that such an approach would ensure that only housing of 'significant value' (p. 550) was targeted by the means test. They estimated that a cap of \$1.2 million would result in approximately 10 000 Age Pension recipients having their principal homes partially assessed under the means test.

National Commission of Audit — cap for exemption

The National Commission of Audit proposed that from 2027-28, the threshold for the inclusion of the principal residence in the Age Pension means test should be set at the indexed value of a residence valued at the time of writing at \$750 000 for couples, and \$500 000 for a single pensioner (NCA 2014a).

Rice Warner — cap for exemption and no part pensions

Rice Warner recommended that singles should be permitted to have \$250 000 in superannuation assets (\$350 000 for couples) plus a home value of up to \$1 million to be eligible for the Age Pension. For those with assets exceeding these amounts, no Age Pension would be payable — that is, tapering would be eliminated. Those with a home value in excess of \$1 million who wanted to obtain access to the Age Pension would need to sell their home, or alternatively, borrow against the property to reduce their net equity position to \$1 million. In their submission to the Australian Government's Tax White Paper, Rice Warner (2015) revised their threshold to \$1.5 million for the principal residence and up to \$500 000 for all other assets (including superannuation).

Grattan Institute — no exemption for principal residence

Recognising that including the value of the principal residence in the Age Pension assets test would disadvantage asset rich, income poor households, Daley et al. (2013) suggested that those who fail the assets test due to the value of their home be permitted to access the Age Pension, but for the Australian Government to accumulate a claim against the dwelling in return. The value of the debt to the Australian Government could be incorporated in the assets test, such that over time a person's net asset value might reduce to the point where they became eligible for the Age Pension (depending on the value set in the asset test threshold) without accumulating further debt.

Centre for Independent Studies — no exemption for principal residence

Cowan and Taylor (2015) advocated including the entire value of the principal residence in the Age Pension assets test. This was part of a three-pronged approach which also included legislating for a default reverse mortgage product to be offered by banks and superannuation funds, but guaranteed by the Australian Government, as well as deeming income from the reverse mortgage product and including it in the Age Pension income test.

At a minimum, there is a strong case to consider the proposal by the Henry Review (Henry et al. 2010) and the National Commission of Audit (2014a) to incorporate a threshold value of the principal residence in the assets test. Under this arrangement, treatment of the principal residence would remain concessional compared to other assets, with only the value of a residence beyond a certain amount incorporated in the assets test. The number of pensioners affected by the inclusion of the principal residence in the assets test for the Age Pension would hence depend on this value threshold. Any dollar limit placed on the exclusion of the principal residence could also be indexed — for example, the Western Australian Division of the Association of Independent Retirees suggested to the Commission that, if the principal residence was included in the means test, this amount should have a cap which would be indexed to the consumer price index (WA AIR sub., pers. comm., 8 August 2015).

Any particular threshold may also take into consideration community attitudes towards home values (box 5.3). However, community attitudes are not necessarily well informed about the distribution of home equity values across the population and about what constitutes a relatively expensive home.

Box 5.3 Community attitudes towards home ownership and the Age Pension

A recent survey of 1413 people by The Australia Institute (2015) found that two in three people consider a home worth \$1 million or more to be ‘expensive’, with one in three also considering that a home worth \$750 000 or more is ‘expensive’.

Three-quarters of people surveyed thought that retirees living in ‘expensive’ homes should still be able to access some form of Age Pension — 46 per cent favoured access to a part Age Pension, and 29 per cent thought that those living in ‘expensive’ homes should be able to receive a full Age Pension. Only 16 per cent of those surveyed believed that those living in ‘expensive’ homes should not be able to access any form of Age Pension.

Source: The Australia Institute (2015).

Building a threshold for the principal residence into the assets test

The Commission revised the current Age Pension means test to incorporate a number of threshold values of the principal residence, and applied this test to age pensioners in the Household, Income and Labour Dynamics in Australia (HILDA) database in 2010.²⁶ Due to data and modelling limitations, some of the real-world complexities of the means test were not captured in the Commission’s modelling. (The modelling and interpretive caveats are discussed further in appendix D.) The Commission’s analysis is therefore illustrative only, and the results obtained should not be interpreted as definitive estimates of the effects of changing elements of the means test.

²⁶ As noted, the Age Pension means test comprises an income test and an assets test, with the Commission’s modelled scenario changing the latter test.

The design of the revised means test was such that values of the principal residence beyond the threshold amount would be included as an assessable asset in the assets test for the Age Pension, and all other elements of the income and assets tests remain unchanged.²⁷

For both single and couple pensioner households who owned their homes, roughly half had a home equity value of between \$250 000 and \$500 000 in 2010. Only a small proportion of all home owner pensioners in 2010 had a home equity value in excess of \$750 000 — about 10 per cent of couples and singles altogether.

The Commission's illustrative analysis indicates that incorporating particular values of the principal residence in the Age Pension means test (in 2010) would generally have modest effects on overall eligibility for the Age Pension. Incorporating the principal residence would shift some people off the Age Pension entirely, and it would move others from the full pension onto a part pension. For example, the indicative effect of incorporating the value of the principal residence beyond \$440 000 (the estimated median Australian house price in 2010) in the Age Pension assets test would have been to reduce the proportion of the age-eligible population on the pension by less than 3 percentage points (table 5.2). The latter group would comprise people who in 2010 held a median household wealth of about \$1.6 million. The modelled limited impact of setting the cap on the exemption may in part be due to the fact that for many pensioners, the assets test is a less relevant constraint on eligibility and size of payments than the income test.

Table 5.2 Impact on Age Pension eligibility of changing the assets test
Proportion of population of Age Pension age, 2010

	<i>Threshold beyond which principal residence is included in the assets test</i>						Current treatment
	Fully included	\$440 000 (median)^a	\$500 000	\$750 000	\$1 000 000	\$1 250 000	
Proportion on Age Pension	62.3	70.8	71.4	72.5	72.8	73.1	73.3
Impact on proportion eligible for Age Pension	-11.0	-2.5	-1.9	-0.8	-0.5	-0.2	0.0
Proportion whose Age Pension is reduced	45.9	10.6	7.5	3.0	0.9	0.4	0.0

^a Median Australian house price in 2009-10, from ABS (*Housing Occupancy and Costs, 2011-12*, Cat. no. 4130.0).

Source: Productivity Commission estimates based on HILDA release 13.1, wave 10.

More recent data on home equity — as well as the incomes and assets of age pensioners — are not available, making it difficult to draw definitive conclusions about the full effects

²⁷ The exercise is intended for illustrative purposes and does not represent a comprehensively designed policy proposal. The latter would involve a thorough consideration of the entire means test to ensure that it is well targeted and internally consistent.

today of particular changes to the exemption. For example, house prices rose by over 6 per cent per annum, on average, in Sydney between March 2010 and March 2015. Growth in other regions however, was slower, or even negative — for example, in regional Western Australia, house prices declined by an average of 1.5 per cent per annum over the same period (ABS 2015f).

What about geographic variations in house prices?

Nationwide house price data mask significant differences in home equity values in different locations. Home equity values are generally higher for those age pensioners who live in Sydney and Melbourne compared to other capital cities, as well as regional areas (figure 5.3).

Recent growth in house prices in Sydney will have likely exacerbated this trend. For example, in December 2010, the median house price in Sydney was approximately \$644 000, which has increased to \$1 million by June 2015 (Nicholls 2015). Accordingly, a threshold of, for example, \$750 000 would affect proportionately more age pensioners in those cities than elsewhere. In established areas close to central business districts (in Sydney and Melbourne in particular), median prices are often much higher, and even a moderate threshold would affect relatively more households in these suburbs. For the Melbourne metro area, the median house price in June 2015 was \$706 000, and in inner Melbourne alone, the median was close to \$1.24 million (REIV 2015).

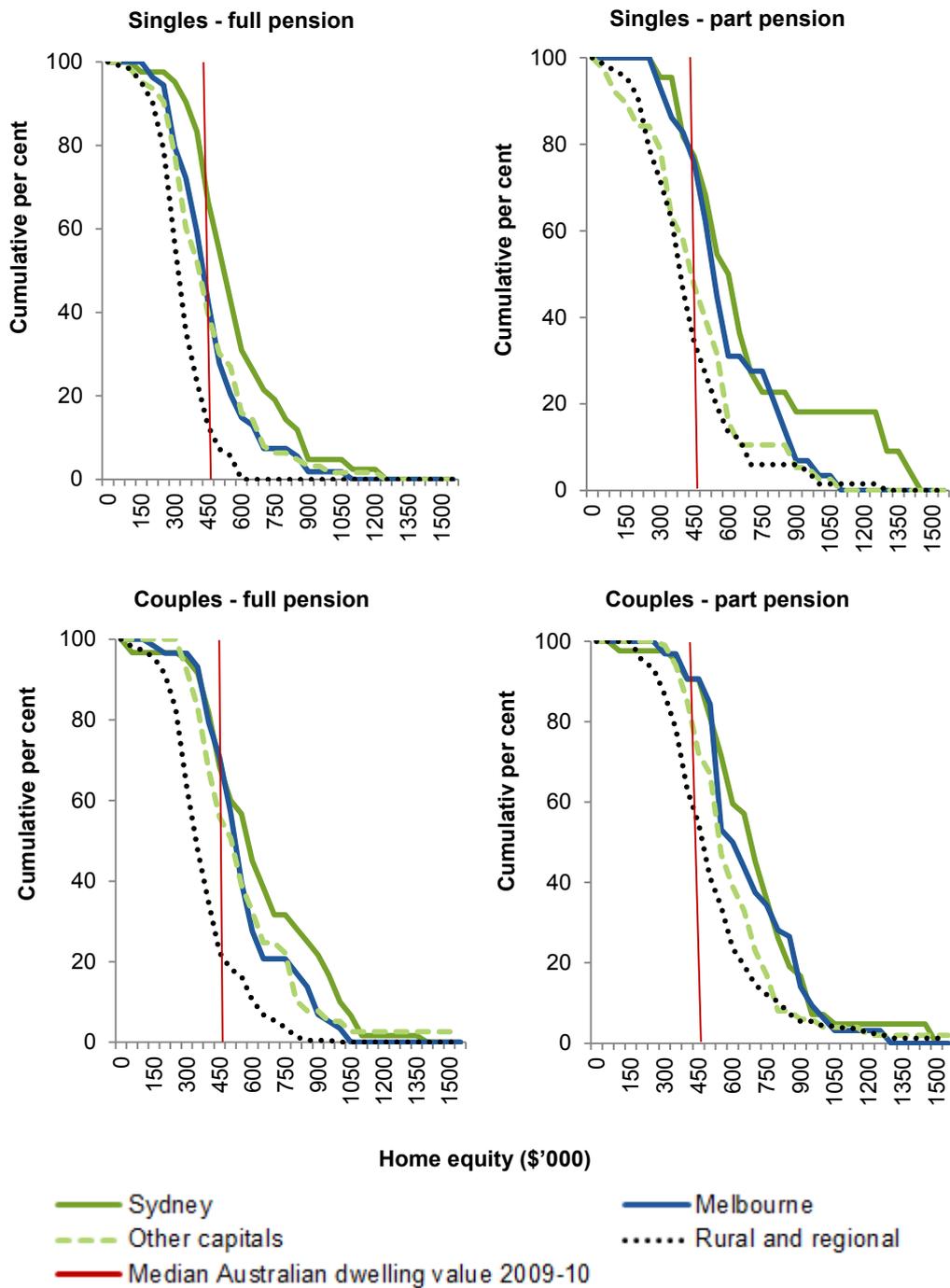
If the objective of the exemption is that a certain level of *housing services* is protected (rather than a particular level of housing wealth) it may be more appropriate to set different exemption thresholds based on location. This would recognise, for instance, that a modest home in the inner suburbs of Melbourne would be more expensive than the same home located in regional Australia.

Further research and modelling could be undertaken by the Australian Government to consider the full implications of incorporating some value of the principal residence in the assets test for the Age Pension, including how the effects might vary by geographic location.

More generally, if the policy change of incorporating the principal residence into the Age Pension means test was implemented, there would likely be a case for introducing the change gradually over time, to allow people sufficient time to plan and adjust their retirement decisions.

In addition, any inclusion of the principal residence in the Age Pension means test may stimulate the development of more sophisticated and readily available financial products to enable older Australians to access the equity in their homes, if they wish to do so (chapter 6).

Figure 5.3 Home equity distribution of age pensioners in 2010^{a,b}



^a Analysis pertains to person-level data; hence, home equity values for couples living together where both members of the couple receive the Age Pension were counted twice in constructing the above figure.

^b To categorise pensioners as either receiving a full rate of pension or part rate of pension, a tolerance of \$20 per week in reported Age Pension income was used so that the full and part pensioner split accorded more closely with observed administrative data.

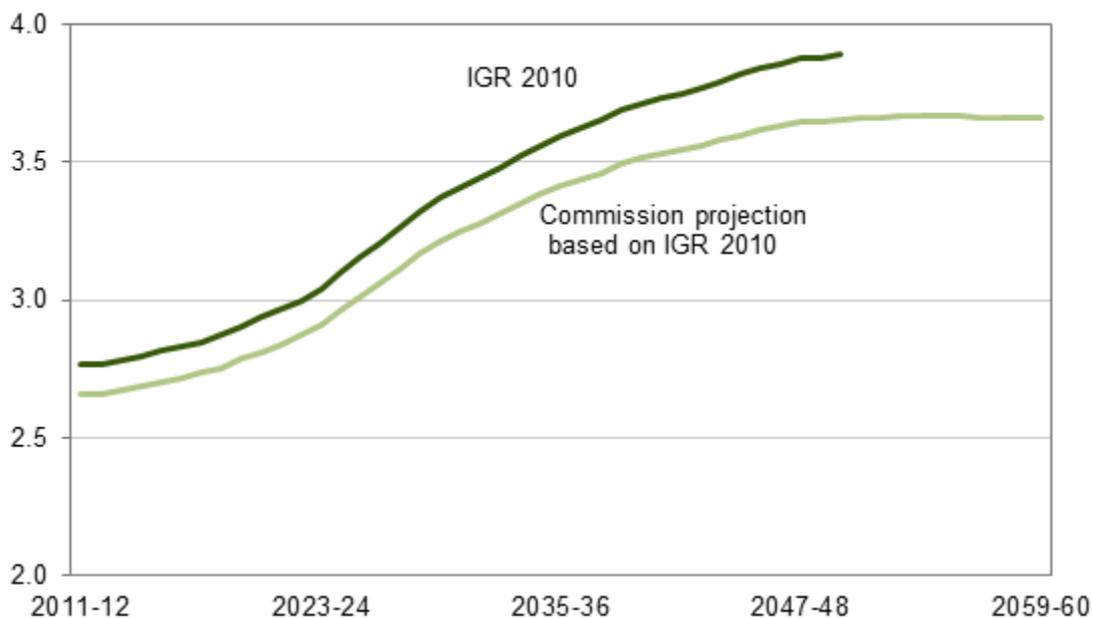
Sources: ABS (*Housing and Occupancy Costs, 2011-12*, Cat. no. 4130.01); Productivity Commission estimates based on HILDA release 13.1, wave 10.

Fiscal considerations

For 2014-15, Australian Government expenditure on the Age Pension was budgeted at roughly \$42 billion, representing approximately 2.9 per cent of GDP (Treasury 2015a) and roughly 10 per cent of total Australian Government expenditure (Australian Government 2015b).

Treasury (2015a) estimated that if current Age Pension eligibility rules were to remain in place, Age Pension expenditure would rise to 3.6 per cent of GDP by 2054-55 — about \$165 billion in today's dollars — attributable largely to an increase in the number of persons of eligibility age and increased life expectancies. Similarly, the Commission has projected that beyond 2035-36, Age Pension expenditure will rise above 3.5 per cent of GDP from current levels of roughly 2.8 per cent (figure 5.4) (PC 2013).

Figure 5.4 Projected Age Pension expenditure^{a,b}
Per cent of GDP



^a 'IGR 2010' refers to the 2010 Intergenerational Report. ^b Differences between IGR 2010 and the Commission's projection are due to the use of more recent budgetary costs data, changes to the superannuation guarantee, as well as differences in forecast growth in life expectancy and workforce participation rates.

Source: PC (2013).

Including the principal residence in the assets test for the Age Pension would reduce Australian Government expenditure on the Age Pension. The magnitude of reduction would depend partly on the threshold at which the principal residence became eligible for inclusion in the assets test (box 5.4).

For instance, as indicated above, placing a limit of \$1 million on the exemption of the principal residence would likely affect only a small proportion of those on the Age Pension. Nevertheless, given the magnitude of Australian Government expenditure on the Age Pension, even small changes in eligibility could have noticeable fiscal effects. The fiscal savings may rise further if the cap were not indexed, or if future generations of pensioners had more wealth and a higher level of home equity.

Though fiscal sustainability of the Age Pension is an important objective, no less important is how any saved funds from lower Age Pension expenditure might be used. There are various options, including tax reductions. As discussed in chapter 3, there are also some disadvantaged non-home owner groups that could benefit from greater government assistance.

Box 5.4 Estimates of the fiscal impacts of changes to Age Pension eligibility

Ding (2013) estimated that if a threshold value for the principal residence of \$500 000 was incorporated into the Age Pension assets test, the savings to the Australian Government would be limited. By 2035, the model used by Ding (2013) suggested that this change to the assets test would save the Australian Government approximately \$3.3 billion, mainly by increasing the proportion of self-funded retirees and part pensioners among the population aged 65 and over. In large part however, Ding's (2013) results may be attributed to the use of a model which assumes that households make a one-off decision at retirement on how to allocate their assets, including in housing. As a result, at retirement, households in the model choose housing assets valued at less than \$500 000 to avoid losing eligibility for the Age Pension. This modelling scenario does not capture the full complexities actually facing retirees who may have lived in their homes for many years and not wish to sell for a variety of reasons, including attachment to the home, transactions costs and precautionary saving.

Cowan and Taylor (2015) calculated that if their package of reforms were introduced, annual expenditure on the Age Pension would decline to roughly \$28 billion, leading to an annual budget saving for the Australian Government of over \$14 billion. The lower budget outlays projected arise from the movement of some full pensioners onto the part pension, as well as the movement of some age pensioners off the pension altogether. Indeed, under Cowan and Taylor's (2015) proposed thresholds, about three-quarters of single full pensioners would experience a reduction in their Age Pension, and approximately one-quarter of single part pensioners would be shifted off the Age Pension. Further, 75 per cent of full-pension couples would move onto a part Age Pension, and roughly one-third of couple age pensioners would lose their eligibility altogether.

5.2 Broader tax and transfer treatment of the principal residence

Beyond the exemption of the principal residence from the Age Pension assets test, a number of elements of the taxation system in Australia affect decisions relating to property, and influence residential choices, including those of older Australians.

Exemption of the principal residence from capital gains tax

In Australia, capital gains arising from the sale of the principal residence are not subject to capital gains tax (CGT). Australia is not unique in this regard. For example, in the United Kingdom, principal homes are exempt from CGT.

Effects on the consumption of housing

The exemption of the principal residence from CGT provides preferential tax treatment for investment in housing assets, compared to other personal assets. This creates an incentive to accumulate wealth in the form of owner-occupied housing (Wood, Ong and Winter 2012). King and Maddock (2015) suggested that the CGT exemption on principal residences allows people to accumulate real assets, which may help to ensure an adequate living standard after retirement. The Commission has previously noted that removing the CGT exemption for the principal residence as a stand-alone measure would reduce the tax preference for equity investment in owner-occupied housing and thus make the taxation system more tenure neutral with respect to housing (PC 2004).

The CGT treatment of the principal residence is often regarded as a ‘tax expenditure’. Treasury estimated the tax expenditure associated with the CGT exemption for the principal residence (table 5.3). Tax expenditures do not necessarily indicate lost tax revenues, as they typically do not take into account behavioural responses that may arise from a change in policy, or need to make assumptions about those responses (Pulo 2010; Treasury 2015c).

Table 5.3 Estimated and projected CGT tax expenditures for housing
\$ billion (nominal)

	2010-11	2011-12	2012-13	2013-14	2014-15
Main residence exemption	16.0	14.0	15.5	20.0	20.5
Main residence exemption — discount component	20.5	17.5	20.0	24.5	25.5
Total	36.5	31.5	35.5	44.5	46.0

Source: Treasury (2015c).

Given that the CGT exemption may encourage over-investment in owner-occupied housing, there have been various calls to reform this aspect of the taxation system (Yates 2009). However, ending the exemption of the principal residence from CGT would also pose significant administrative, compliance, adjustment and enforcement costs (PC 2004). Bourassa and Grigsby (2000) highlight three difficulties in particular:

1. Part of the capital gain on a particular asset may be attributable to inflation, and hence, a distinction must be drawn between nominal and real capital gains.

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2. Owner-occupied housing depreciates over time (in the absence of improvements), meaning that if capital gains on the principal residence are taxable, capital losses should also be deductible. This would reduce the net revenue a government could expect to collect from making the principal residence eligible for CGT.
 3. Accurate accounting of capital gains and losses requires accurate records of improvement expenditures, which would need to be audited by taxation authorities.

It is therefore unclear that any efficiency improvements from removing the exemption would outweigh the additional costs brought about by this change.

Investment effects

As well as having effects on the consumption of housing, elements of the taxation system also influence decisions to use housing as a form of investment, including for older Australians. The broader taxation system is currently under review as part of the Australian Government's Tax White Paper process, and a comprehensive analysis of the effect of taxation on housing is beyond the scope of this research paper.

In its *First Home Ownership* inquiry, the Commission considered that aspects of the personal taxation system, including the CGT regime and negative gearing, had combined to magnify the attractiveness of investing in residential property. The Commission accordingly recommended that these aspects of the taxation system be reviewed (PC 2004). The International Monetary Fund recently concluded that Australia's tax and transfer system provides support to owner-occupiers and investors, and has the effect of increasing the demand for housing (IMF 2015).

Similarly, the Reserve Bank of Australia recently observed:

... the interaction of negative gearing with other parts of the taxation system may have the effect of encouraging leveraged investment in property. In particular, the switch in 1999 from calculating CGT at the full marginal rate on the real gain to calculating it as half the taxpayer's marginal rate on the nominal gain resulted in capital-producing assets being more attractive than income-producing assets for some combinations of tax rates, gross returns and inflation. This effect is amplified if the asset can be purchased with leverage, because the interest deductions are calculated at the full marginal rate ... (RBA 2015c, p. 23)

The Reserve Bank of Australia has concluded that there is a case for reviewing negative gearing, but not in isolation, arguing that its interaction with other aspects of Australia's taxation system (such as CGT) should be assessed (RBA 2015c).

Imputed rent for owner-occupiers

Owner-occupiers enjoy a benefit from residing in their own home, which is often referred to as 'net imputed rent' (chapter 2).

When Australia's federal income tax was introduced in 1915, net imputed rental income was included as part of the income tax base, but was removed in 1923 (Pulo 2010). In the first half of the twentieth century, a number of European countries also imputed the value of rental income for owner-occupied housing, and included it in the tax base (Ozanne 2012). However, the practice was eventually abandoned in many countries, and today only a few countries (such as the Netherlands and Switzerland) tax imputed rent (Andrews, Sanchez and Johansson 2011). The two most recent European countries to abolish the taxation of imputed rent were Norway, in 2005 and Sweden, in 2007 (IMF 2012).

Taxation systems that do not tax net imputed rent (the difference between imputed rent and ownership expenses, such as mortgage interest payments, property taxes, maintenance and repairs, and depreciation) are sometimes regarded as biased in favour of owner-occupiers over renters (Callan 1992; Goode 1960). In addition, such taxation systems may increase the demand for owner-occupied housing compared to other productive investments, resulting in over-investment in housing (Bourassa and Hendershott 1994; Yates 2009). These incentive effects are common to both older and younger people facing the decision to rent or purchase a home.

However, taxation of imputed rent presents a number of practical policy design and implementation challenges. Principal among these is the need to find a valuation method, which generally creates difficulties due to the need to collect information on estimated home rental values, additional administrative responsibilities for tax authorities, and the need for home owners to keep more complex records (Bourassa and Grigsby 2000; Ozanne 2012). The ABS estimates imputed rent (chapter 3) by using information on private rents, and applying statistical techniques to produce predicted values of rent for owner-occupied dwellings (ABS 2008). These estimates are therefore not based on direct estimates of imputed rent, but on a general statistical analysis, and do not capture the full differences in imputed rent from private dwelling to private dwelling.

A further problem with taxing imputed rent is the ability of some households to pay the tax (PC 2004). Those on low incomes or with a limited cash flow (such as people on the full Age Pension) might find it difficult to pay the tax, and would face significant financial hardship. A deferral scheme could be used to address this problem, although this would also have the effect of increasing system complexity and administration costs.

5.3 Stamp duty as a barrier to housing mobility and land tax as an alternative

What are the effects of stamp duty on housing?

At the state government level²⁸, stamp duties (also commonly referred to as property transfer duties) are levied on conveyances for both residential and commercial properties. Stamp duties are administratively simple, as the duty is based on the reported sale price or market price of the property. Stamp duty schedules are generally progressive, with higher rates applying to transactions of greater value.

Stamp duties are also used in some overseas jurisdictions, including the United Kingdom (except Scotland) and most states in the United States of America.

Despite the appeal of their administrative simplicity, stamp duties have undesirable effects on economic efficiency. Principally, stamp duty can affect a household's decision to buy or sell property by adding to transaction costs. This 'tax on mobility' can result in people living in houses that do not provide the best match for their needs and preferences (Yates 2010). Possible additional effects include:

1. Increased commuting, adding to congestion.
2. Increased prevalence of renovations, or the purchase of larger houses than initially necessary, the latter in the expectation that a larger home will be required later in life.
3. Decreased labour market mobility, potentially leading to higher unemployment.
4. Reducing affordability by raising the costs of housing (Henry et al. 2010).

In the context of the housing decisions of older Australians, stamp duty creates a disincentive to downsize, by increasing the relative cost of moving to more suitable accommodation. In the Commission's survey, only a small proportion of older Australians indicated that they were unlikely to sell their home because of costs such as stamp duty, and Australia overall has relatively high rates of residential mobility (PC 2014). Nevertheless, as noted by Judd et al. (2012):

... decisions to downsize are potentially disproportionately influenced by the impact of stamp duties and older people may choose to stay in unsuitable housing rather than incur such costs. (p. 58)

Stamp duty was also noted as a disincentive to downsize by the Western Australian Division of the Association of Independent Retirees (WA AIR sub., pers. comm., 8 August 2015). A recent study by Davidoff and Leigh (2013) provided evidence of the effect of stamp duties in reducing property turnover. Using data on Australian house sales between 1993 and 2005, these researchers found that a 10 per cent increase in stamp duty lowered housing turnover by 3 per cent in the first year and 6 per cent over a three-year period.

²⁸ The term 'states' is used throughout this chapter to refer to states and territories.

In addition to preventing desirable housing outcomes, stamp duties can also have financial implications for older Australians wishing to access the equity in their homes through moving to a lower cost dwelling (PC 2013). The inefficiencies associated with stamp duties have received considerable attention in policy discussions. Henry et al. (2010) concluded of stamp duties:

Ideally, there is no place for stamp duty in a modern Australian tax system. Stamp duties generate large efficiency costs, as they discourage turnover in property ... The tax also imposes a higher burden on people who need to move, which is not equitable. The only positive feature of stamp duty — its relative simplicity — has long since ceased to justify its continued use ... (p. 263)

One difficulty posed by the removal of stamp duties, however, is the effect that lost tax revenue would have on state government budgets. In 2013-14, stamp duties on conveyances raised nearly \$16 billion for state governments (ABS 2015g), and the loss of this revenue would likely need to be at least partly compensated by increasing other, more efficient taxes (discussed below).

Stamp duty concessions

Some states have introduced stamp duty concessions for older Australians, which may partly negate the disincentives for downsizing and broader housing mobility (table 5.4). There is a general stamp duty home concession in Queensland that is not specific to older Australians. The concessional rate applies to the first \$350 000 of the home value, where the property in question is to be used as the principal residence (OSR (QLD) 2015).

Although stamp duty concessions and exemptions for pensioners may have positive effects on housing mobility, it is necessary to ensure that such concessions are appropriately targeted. For instance, setting upper limits on the value of concessions and exemptions could limit the effectiveness of the concessions in areas where property values have undergone significant increases due to land scarcity. Furthermore, policies targeted at those of Age Pension age would fail to ameliorate the disincentives to move faced by those in their 50s and early 60s, to the extent that downsizing decisions are made prior to retirement.

Concessions targeted at pensioners also have a redistributive effect, and therefore, raise issues about the equitable treatment of pensioners compared with other groups in society. Some may consider it inequitable, for instance, that a group who have had the opportunity to accumulate wealth throughout the course of their working lives (Daley et al. 2014) should be granted concessions on state taxes, whereas others, such as those on low incomes, or those who must frequently relocate for work purposes, are not.

Table 5.4 Stamp duty concessions specifically for older Australians

<i>State</i>	<i>Main eligibility requirements</i>	<i>Limit</i>
Victoria	Holders of Pensioner Concession Card, Health Care Card, Commonwealth Seniors Health Card, DVA Gold Card	Full exemption up to \$330 000 with sliding scale of concessional rates for properties valued between \$330 000 and \$750 000
Northern Territory	Senior citizens, pensioners, carers	Concession is an amount up to \$10 000 of stamp duty payable, with eligibility ceasing where the dutiable value of home/land exceeds \$750 000 and \$385 000 respectively
ACT	Eligible pensioners, consisting of: those in receipt of an Age Pension and who hold a pensioner concession card; those in receipt of a disability support pension and who are 50 years of age or over and who hold a pensioner concession card; those in possession of a DVA Gold Card for one year prior to the property transaction	\$20 duty for residential homes valued at \$625 000 or less, \$16.90 duty for each \$100 by which dutiable value exceeds \$625 000 up to \$807 000, and no concession above \$807 000; for vacant blocks, \$20 duty applies up to \$332 100, \$17.20 for each \$100 by which dutiable value exceeds \$332 100 up to \$391 700 with no concession above \$391 700

Sources: ACT Revenue Office (2015); NTG DTF (2015); SROV (nd).

Land tax treatment of the principal residence

Land taxes are levied by all state governments in Australia, except the Northern Territory. The particular rates levied, and thresholds at which land tax applies, vary across jurisdiction. However, one feature common to all jurisdictions is that owner-occupied housing is exempt from land tax. This removes about 60 per cent of land by value, and roughly 75 per cent of all residential land from the tax base (Henry et al. 2010). This contrasts to the United States, for example, where most jurisdictions charge annual taxes on the value of real property, including owner-occupied homes (Harris and Moore 2013; IRS 2014).

Comprehensive taxation of the value of land is an efficient form of taxation²⁹. Because the physical supply of land is ultimately fixed, taxes on its value will have little if any effect on how it is used, or how much of it used. Hence, a comprehensive tax based on the unimproved value of land would not distort land-use decisions (Daley and Coates 2015; Henry et al. 2010; PC 2004).

Exemptions from land tax, besides increasing complexity, also distort housing outcomes. If owner-occupied housing is not taxed, but rental housing is, the after-tax return on rental housing will encourage the purchase of owner-occupied homes over renting (PC 2004; Wood, Stewart and Ong 2010).

²⁹ In simple terms, an economically efficient tax is a tax that does not distort the behaviour of market participants.

Further, where investors in residential housing have to pay land tax, investors will bear part of the tax in the form of a lower return, or renters may bear part the tax through higher rents. Hence, the exemption of the principal residence from land tax also has an equity and tenure neutrality dimension.

Consequently, a broadened land tax regime which incorporates the principal residence is often seen as a superior alternative to the current regime of stamp duties on property transfers.

As noted above, the exclusion of the principal residence from land tax also has budgetary implications for state governments. It has been estimated that the exemption of the principal residence from land tax costs state governments roughly \$5 billion in foregone revenue if land tax were imposed at comparatively low rates on all residential properties (Daley and Coates 2015; Kelly et al. 2013). The design of a broadened land tax would need to give consideration to the revenue that would be lost by the states (box 5.5).

Box 5.5 Fiscal effects of removing stamp duties

Stamp duties are a significant source of revenue for state governments. In 2013-14, out of nearly \$69 billion collected by all state governments in taxation revenue, almost \$16 billion was collected from stamp duties on conveyances — roughly one-quarter of all revenue. Removal of stamp duties on conveyances would therefore have a marked impact on the budget position of states, and needs to be at least partly compensated by raising other, more efficient, taxes. One suggestion is that land tax could replace existing stamp duties.

Putting aside complexities such as progressivity of tax rates, tax-free thresholds and concessions, an annual land tax of \$1 705.60 per residential dwelling in 2013-14 across Australia would have raised revenue equal to that of stamp duties on conveyances collected by the states (ABS 2015e, 2015g). Wood, Ong and Winter (2012) considered the effects of replacing stamp duty with a broad-based land tax in Melbourne. They found that a package consisting of seven land tax brackets, with marginal rates ranging from 0.00 per cent at the lowest, to 1.37 per cent at the highest, would be revenue neutral. Over 50 per cent of landowners would be in the second-lowest tax bracket with a 0.92 per cent tax rate, and have an average annual tax liability of \$1306. More than half of revenue would also be raised by landowners in this tax bracket.

Although reforms to land taxes have the potential to generate similar levels of revenue to stamp duties, a transition strategy would be required to allow taxpayers to adjust to the removal of stamp duties and the imposition of land taxes on the principal residence. A number of options canvassed by the Henry Review included:

- Levying land tax only on land that had been acquired after a particular date.
- Grandfathering existing landholders and giving purchasers of owner-occupied housing a choice between paying stamp duty or paying land tax.
- Providing credits to be used against future land tax liabilities, with credits paid based on previous stamp duty paid or the land tax expected to be paid over a set period of ownership.
- Phasing in lower stamp duties and higher land tax simultaneously (Henry et al. 2010).

An additional concern is that older Australians who are asset rich and income poor would have an annual tax liability that they previously did not face under a regime of expanded land taxation. One possible approach to this problem would be to allow payment of the tax to be deferred until the home is sold (PC 2004), or to be paid out of a person's estate.

5.4 Taxation and transfer aspects of aged care

Complexity, inefficiency and inequity of means tests

Older Australians in need of some form of care or living assistance have a broad choice between receiving care in their principal residence, or within a residential aged care facility (chapter 4). The treatment of assets and income in means tests that determine the level of government assistance could influence the housing decisions of older Australians (table 5.5).

Table 5.5 Treatment of principal home and related income and assets^a

	<i>Out of Residential Aged Care (RAC)</i>		<i>In Residential Aged Care (RAC)</i>	
	<i>Age Pension</i>	<i>Home care support</i>	<i>Age Pension</i>	<i>RAC support</i>
Owner-occupied home	Exempt from assets test, assets threshold is \$149 000 lower than for non-home owners	Exempt	Exempt for two years	Exempt if occupied by protected person ^b ; otherwise up to \$158 000 included for means tested care fee
Former home if rented out	na	na	Exempt if paying for at least part of accommodation by daily payment	As above for means tested care fee; full value of former residence included for assessing ability to pay accommodation payment
Rental income from former home	na	na	Exempt if paying for at least part of accommodation by daily payment	Exempt for daily accommodation payments only (until 1 January 2016)
Refundable accommodation deposit	na	na	Exempt	Not exempt

^a Dollar amounts have been rounded to the nearest thousand dollars, and correspond to values as at August 2015. ^b A protected person is defined as a partner or dependent child, a carer eligible for an Australian Government income support payment who has been living in the principal home for at least two years, or a close relative who is eligible for an Australian Government income support payment who has been living there for at least five years. **na** Not applicable.

Sources: DHS (2015a, 2015b, 2015c); DSS (2015d, 2015l, 2015o).

The National Commission of Audit considered that there was scope for the means test for aged care to take into account the full value of a resident's home when assessing their contribution to aged care costs. Failing that, it suggested that the threshold for the cap of \$158 000 could be raised, noting that the current threshold is substantially below the current median home values both in capital cities and in the rest of Australia (NCA 2014a).

The Commission also considers that the means test for residential aged care ought to take into account a greater value of a resident's home. This would improve equity between home owners and non-home owners, and help to ensure that care recipients with the financial ability to do so should pay for their own accommodation. Because residential care is typically the final place of accommodation in a person's life (chapters 3 and 4), the family home is no longer a vehicle for precautionary saving. The primary motivation for an aged care resident to retain it is likely to be for a bequest. Although this may be an appropriate objective for their individual circumstances and preferences, it should not be done at the expense of enabling a person to shift the cost for their aged care to taxpayers. In effect, this would amount to taxpayers subsidising the bequests of those holding housing wealth. Hence, there may be merit in increasing co-contributions to achieve an appropriate balance between individual contribution to care and the degree of taxpayer financing.

A more comprehensive means test that incorporates assets may also be warranted for the delivery of home care. The financial capacity to pay for home care does not only depend on income — some assets can also be drawn upon to finance care. The arrangement where those with relatively high levels of assets are not under any obligation to use them to finance home care may be inequitable relative to the people with few assets that pay an income-tested care fee.

Further, the exemption of the principal residence from the Age Pension means test for those who have moved into aged care and who rent out their former home provides an incentive to retain, rather than sell, the home. If an aged care resident chose the latter, the net sale proceeds of the former home (putting aside amounts paid for a refundable accommodation deposit) would become an assessable asset under the Age Pension means test. This is compounded by income received from renting out the former home also being excluded from the Age Pension means test.

The inconsistencies in the treatment of assets across means tests for home care, residential aged care and the Age Pension result in mixed incentives, and are a source of unnecessary administrative complexity and confusion for older Australians — especially given that the means tests for the Age Pension and residential aged care are complex in their own right. Moreover, the current means tests raise equity concerns.

A case for further exemptions?

In its inquiry report *Caring for Older Australians*, the Commission noted that the equity, efficiency, and sustainability of the aged care system would be improved if the means test for the Age Pension treated income and assets in a consistent manner (PC 2011). This was

regarded as the ‘first best option’ for reform, which would ensure that people with different mixes of assets and income were treated consistently.

As an alternative, the Commission recommended the introduction of a government age pensioners saving account scheme. The purpose of the scheme was to provide age pensioners with a mechanism by which they could invest surplus savings generated from the sale of the principal residence, and for these funds to be exempt from the Age Pension means test. The funds could then be used to finance living costs, aged care requirements, and other expenses, and the product could be provided directly by government, or be contracted out to the private sector. Take-up of this scheme would have had the additional effect of strengthening the user-pays pillar of the aged care funding system (PC 2011).

One of the attractions of such a scheme was that it would overcome the disincentive effects created by the interaction of the Age Pension means test with the aged care system. An age pensioner who needed or wanted to move into a residential care facility or retirement village might have to sell their principal residence to do so. As highlighted by the Western Australian Division of the Association of Independent Retirees (WA AIR sub., pers. comm., 8 August 2015), the proceeds of the sale could leave pensioners with a surplus that would subsequently make them ineligible for the Age Pension, or face reduced pension payments. This provides a disincentive to move to more appropriate care. The Commission’s proposal could address this distortion. Similarly, the National Commission of Audit noted that there is no assets test for home care, and considered that there was scope to allow older people to use the equity in their principal residence to help finance their aged care costs generally (NCA 2014a).

There has also been some policy recognition of this effect. A pilot scheme for Age Pension recipients (and some other pension recipients over Age Pension age) who downsized to a home of lesser value was announced in the 2013-14 budget, but ultimately did not proceed. The scheme would have allowed pensioners to place at least 80 per cent of net sale proceeds after the purchase of a new home, up to a cap of \$200 000 into a special account that would be exempt from the Age Pension means test for a period of up to ten years, or until a withdrawal was made (DHS 2014b). However, the fact that a withdrawal of any size prior to the end of the ten year exemption period would have resulted in the removal of the exemption for the entire amount would have significantly curtailed the desirability of using the scheme to supplement retirement incomes.

Ultimately, however, although such policies could address some of the more evident distortions generated by the principal residence exemption from the Age Pension means test, they do not target the source of the problem. Indeed, they risk creating even deeper distortions by making home ownership a more effective financial safe-haven for circumventing the current means tests for the Age Pension and aged care. This could make more individuals eligible to receive the Age Pension. Doing so would create a further cost to the economy, due to the additional taxes which would be required to finance increased expenditure on the Age Pension. A removal of the principal residence exemption from the means tests remains the most efficient and equitable option for reform.

5.5 Assessment

The treatment of housing in Australia's tax and transfer system has myriad effects on housing incentives, including those of older Australians. Perhaps most significantly, the exclusion of the principal residence from the Age Pension assets test provides older Australians with an incentive to remain in their current homes, or those of a similar value.

Though the assets test threshold for receipt of the Age Pension is higher for non-home owners than home owners, this does little to address equity given that less than 1 per cent of all Age Pension recipients assessed under the assets test are non-home owners. The design of the system favours home ownership over other forms of tenure, and is also inequitable. Cho and Sane (2013) analysed the likely distributional effects of ending the exclusion of the principal residence from the assets test. Assuming that lower Age Pension expenditure was offset by lower taxes on labour income, their modelling showed that incorporating a limit on the principal residence exemption increased the welfare of all households with the exception of those in the richest wealth quintile. Accordingly, consideration should be given to including the value of the principal residence in the Age Pension means test, beyond some threshold level.

The exemption of the principal residence from CGT creates an incentive to accumulate wealth in the form of owner-occupied housing. Although the removal of the exemption would make the tax system more neutral with respect to housing tenure, there would be significant administrative and compliance costs that would likely negate any efficiency gains from the removal of the exemption. The efficiency of the taxation system would be improved if the exemption of the principal residence from land tax ended, and if stamp duties on the transferral of property were abolished. Inclusion of the principal residence in land tax will raise revenue for governments without distorting housing and investment choices. Abolition of stamp duties would remove disincentives to move to properties more closely aligned with the needs and preferences of individuals, such as older Australians who may wish to downsize.

In the *Caring for Older Australians* inquiry report, the Commission observed that aged care funding was supported by two pillars — a taxpayer funded pay-as-you-go subsidy and a user-pays element. Under this system, taxpayers bear the full financial risks associated with the public subsidy, which could be magnified by future demographic changes. Taxpayers also bear longevity risks associated with financing the Age Pension, and public health care costs (PC 2011).

With respect to aged care, there is limited scope for further increases in co-contributions to aged care if the Australian Government wishes to preserve the equity objective of charging on the basis of older people's capacity to pay. Nevertheless, there may be a case for increasing co-contributions if a greater balance between individual contributions and taxpayer financing is desired.

Overall, the current treatment of housing in the tax and transfer system favours owner-occupation over other forms of housing tenure, which has effects on efficiency and equity. A number of changes that could be made to enhance the efficiency of the system have been canvassed in this chapter and suggest a possible future direction for policies dealing with housing.

Given the significant nature of many of the canvassed changes, any actual implementation would likely best be carried out gradually, with transitional arrangements where appropriate. Further, inclusion of the principal residence in the Age Pension means test may also require the development of more mature financial products which would enable retirees to more readily access the equity in their homes.

6 Home equity release market

Key points

- Most older Australian home owners on low incomes could achieve a modest retirement living standard over the remainder of their lives by drawing on their home equity.
- Equity release products (ERPs) are designed to enable older home owners to withdraw equity while still living in their homes. Most currently available products are reverse mortgage loans, and these are the only ERPs that are regulated at the federal level, but new non-credit products are also emerging in some jurisdictions.
- The market for ERPs is small and has stagnated in recent years — with 40 000 outstanding ERPs nationwide, they comprise just 0.4 per cent of the home equity of older Australians. This is due to both demand and supply side constraints.
 - Demand is impeded by consumer preferences affecting the family home and debt; negative perceptions of the products; poor financial literacy and information; high costs and risks; and disincentives arising from the tax and transfer treatment of the principal residence.
 - Providers and investors show little interest in the products due to the relatively small market size; the risks caused by the uncertain timing and value of returns; costly prudential and regulatory requirements; the lack of a consistent regulatory framework across ERPs; and the reputational risk inherent in offering the products.
- Some of these impediments are unlikely to change. They simply reflect underlying consumer preferences, the commercial decisions of funders and suppliers, and fundamental characteristics of the products themselves.
- Providers could partially address certain impediments through greater investment in promotion, more innovative product design, and competitive pricing.
- Government could reduce regulatory barriers by easing the more prescriptive regulations on reverse mortgages, and developing overarching principles-based regulation for all ERPs.
- There is little rationale for active government intervention in the equity release market in the current policy environment. Options for intervention could be carefully considered in the event of substantial reforms to tax and transfer policies affecting the principal residence.

Home equity is a major store of assets among older Australians, comprising about half of the total wealth of people aged 65 years and over (ABS 2015b). This wealth has remained largely untapped not only because older people are disinclined to downsize, but also because their other options for equity withdrawal are limited.

People who prefer not to sell their home as they age may wish to withdraw equity from their home using financial products. Although many standard mortgage products allow the flexible withdrawal of home equity — via a line of credit, offset account or redraw facility

— retirees generally cannot access these products, because they require the borrower to provide evidence of their ability to make regular repayments.

This chapter discusses home equity release products (ERPs): financial products specifically designed to enable older people to access the equity in their homes without moving. They are typically available only to home owners aged at least 60 or 65 years, and do not require repayment to the provider until the owner either sells the home or passes away.

Section 6.1 explores the potential for Australian home owners to use ERPs to improve their standard of living in retirement. Section 6.2 gives an overview of the products available and their current use. Section 6.3 assesses the factors that are impeding the growth of this market. Section 6.4 discusses some of the options for overcoming these impediments. Section 6.5 considers whether greater government intervention in the market may be warranted in a broader policy context.

6.1 The scope for equity release in retirement

In recent years, many have argued for the benefits that could be enjoyed by older Australians if they drew from the equity in their family home to supplement their retirement incomes (Brownfield 2014; Cowan and Taylor 2015; Denniss and Swann 2014). Much of this discussion has advocated a major role for financial equity release products to assist ‘asset rich, income poor’ retirees.

The Commission conducted an illustrative quantitative analysis of the scope for equity release products to improve the living standards of older Australians. The analysis sought to demonstrate the expected end-of-life home equity balances of the current population of older people if they used housing wealth to boost their incomes to a particular living standard over the rest of their lives. The methodology and complete results of this analysis are discussed in greater detail in appendix D.

The Association of Superannuation Funds of Australia (ASFA) publishes quarterly standard income benchmarks for ‘modest’ and ‘comfortable’ retirement lifestyle standards. Both benchmarks assume that retirees own their own homes and are relatively healthy. The modest standard is considered to offer a slightly better retirement living standard than the Age Pension, but nevertheless only gives the opportunity to afford basic activities. The comfortable standard, by contrast, provides scope for the enjoyment of a range of leisure and recreational goods and services. In the 2010 HILDA sample of home owner age pensioners, approximately half of older single person households and one third of older couple households did not have incomes that meet the modest standard.³⁰

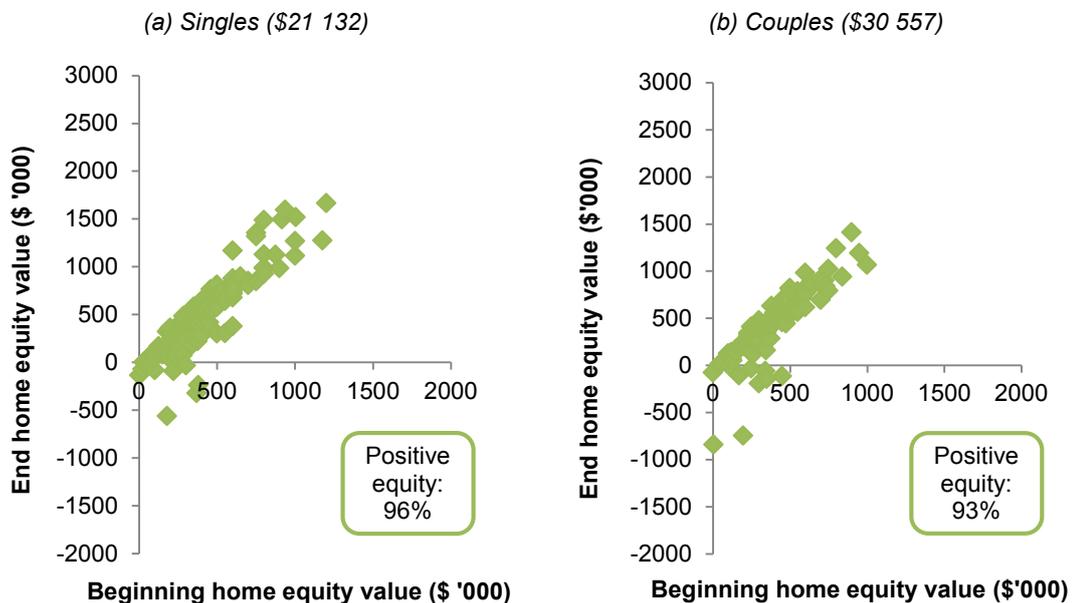
The Commission’s analysis considered whether older Australians below this standard — or between the two standards — could use a debt-based equity release product to reach and

³⁰ These benchmarks are used as indicative only; the Commission has not independently reviewed ASFA’s benchmarks or formed a view on retirement income adequacy.

maintain these income levels over the rest of their lives, without the size of the debt exceeding the value of their home (negative equity)³¹. Simulations were conducted in which people borrowed the equivalent of an income ‘top up’, bridging the gap between their total yearly disposable income and the income levels required to meet each standard. In the base scenario, house price growth was assumed to be 3.5 per cent per annum, and the interest rate was assumed to be 7 per cent per annum. The amount borrowed grew at a rate of 2.5 per cent per annum, equal to the medium-term inflation target, to allow the income ‘top up’ to maintain its expected real value.

The vast majority of people in the sample — more than 90 per cent — could use their home equity to reach and maintain the income necessary for a modest retirement standard over the rest of their lives without going into negative equity (figure 6.1). However, the risk of exhausting home equity increases if the older household releases enough equity to move beyond that standard (figure 6.2). When borrowing to the comfortable standard, about 40 per cent of single person households and nearly 30 per cent of couple households end up with negative equity on average. There are additional risks posed by the possibility of a rise in interest rates or a fall in house price growth (appendix D).

Figure 6.1 **Distribution of changes in home equity — modest living standard^{a,b}**

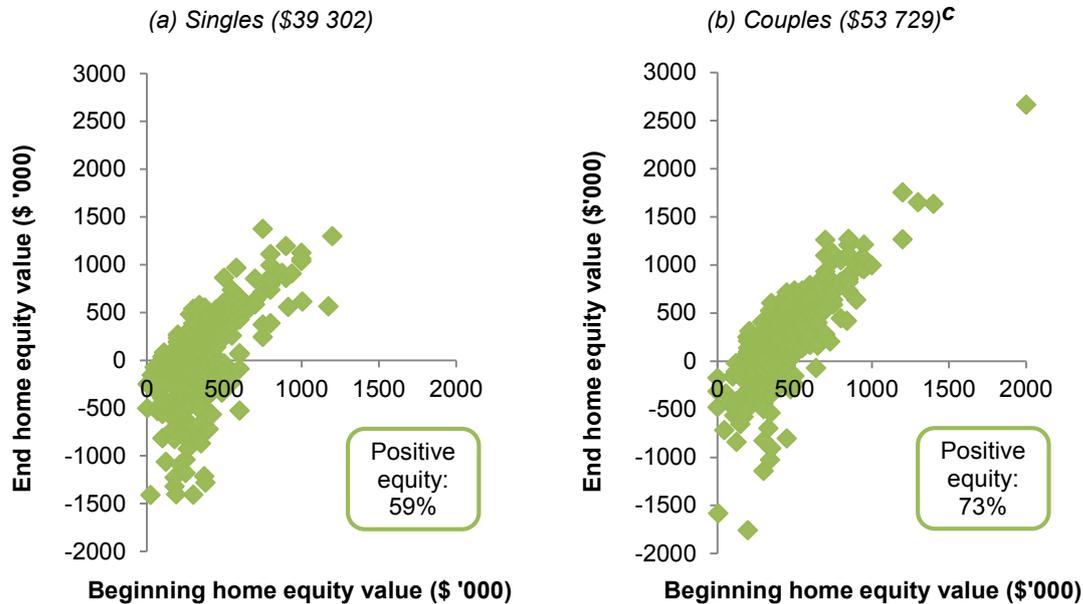


^a Beginning home equity values and retirement income standards correspond to 2010. ^b End home equity values are the average over 1000 simulations.

Source: Productivity Commission estimates based on HILDA release 13.1, wave 10.

³¹ Under current regulations, all reverse mortgages in Australia must include negative equity protection, and so the lower bound on the home owner’s equity is zero. Negative equity is therefore a strictly hypothetical element of this exercise, and does not relate to actual products on the market.

Figure 6.2 **Distribution of changes in home equity — comfortable living standard^{a,b}**



^a Beginning home equity values and retirement income standards correspond to 2010. ^b End home equity values are the average over 1000 simulations. ^c One positive outlier result is not shown.

Source: Productivity Commission estimates based on HILDA release 13.1, wave 10.

These results suggest that many retirees could modestly increase their living standards by using home equity as a source of income, although the extent of this improvement is likely to be limited. The remainder of this chapter discusses the market for financial products that provide a mechanism for this type of home equity withdrawal.

6.2 Overview of the private market

Equity release products can generally be categorised as either debt (or ‘credit’) products or debt-free (or ‘equity’) products. In Australia, a debt product is called a reverse mortgage, and the main debt-free product currently available is called a home reversion scheme. This section discusses these two product types and the current ERP market.

Reverse mortgages

The most prominent equity release product in Australia is the reverse mortgage: a loan which allows seniors to borrow money by using the equity in their home as security. No regular repayments are required — interest is instead rolled into the total debt. The term of the loan lasts until the borrower either sells the home or dies, at which point the amount owing is repaid in full. The name of the product refers to the fact that it operates as a

mortgage in ‘reverse’, in that the borrower’s equity is eroded over time until the home is sold.

Interest on reverse mortgages is generally charged at a variable rate set 1–2 percentage points above standard mortgage rates (Brown 2015). Providers add to this a range of fees, including the application fee, property valuation fee, other setup fees, early exit fee, and regular ongoing fees. The size of the debt can accumulate rapidly due to compound interest — interest accrues not only on the principal, but also on all prior interest and fees.

There are several other key features of a reverse mortgage product. The borrower can receive their funds as a lump sum, a regular income stream, a line of credit, or a combination of these. The total amount that can be borrowed is specified as a proportion of equity in the home, known as the loan to value ratio (LVR). The maximum available LVR is regulated such that it increases with the borrower’s age, and generally ranges from 15 to 45 per cent. Although interest will erode the remaining share over time, the borrower can never owe more than the value of the home upon sale. This protection, called the ‘No Negative Equity Guarantee’ (NNEG), is unique to reverse mortgages. The NNEG became a statutory requirement for all new reverse mortgages on 18 September 2012 (box 6.1), prior to which it was voluntarily included by most providers.

Box 6.1 The statutory regulation of reverse mortgages

The Australian Securities and Investments Commission (ASIC) has been responsible for the regulation of equity release products since 2009. Reverse mortgages were initially subject to the same regulations as other credit products, until the *Consumer Credit Legislation Amendment (Enhancements) Act 2012* (Cwlth) introduced specific reverse mortgage regulations. This legislation strengthened consumer protections by mandating that, for a reverse mortgage contract to be valid, the following conditions must be met:

- inclusion of a No Negative Equity Guarantee
- provision of a prescribed ‘reverse mortgage information statement’ and projections of the potential effect of the reverse mortgage on the borrower’s home equity
- independent legal advice received by the consumer
- disclosure about the treatment of non-titleholder residents — and, if the occupancy of these residents is protected, the right to nominate a non-titleholder resident at any time
- exclusion of certain default terms (as set out by legislation) from the contract.

There are also regulations specifying the maximum loan to value ratio (LVR): a reverse mortgage is presumed by ASIC to be unsuitable if the LVR is greater than the sum of 15 per cent plus 1 per cent for each year of the borrower’s age above 55.

With the exception of the last two points and the LVR limits, these regulations resemble the self-regulated regime that was already in operation under the Senior Australians Equity Release Association of Lenders (SEQUAL), the representative body for the equity release industry. The SEQUAL code of conduct further required that providers strongly encourage consumers to seek independent financial advice, though obtaining this advice was not mandatory.

Sources: ASIC (2014a, 2014b); Burns (2014); Parliament of Australia (2012); SEQUAL (2009).

Aged care loans

A standard reverse mortgage may require the borrower to repay the loan if they move into a residential aged care facility (ASIC 2015d; Egan 2014). This has led to the creation of distinct ‘aged care loans’: reverse mortgages available for the specific purpose of paying for entry to aged care, generally through a refundable accommodation deposit (RAD).

Aged care loans attract the same fees and interest rates as other reverse mortgages, but are limited to a maximum term of five years (Heartland Seniors Finance 2015; Macquarie Bank 2015). These loans enable seniors to enter an aged care facility as soon as care is needed, without requiring the immediate sale of the home — the proceeds from which would impact their means-tested co-contribution. The owner is also able to rent out the house, and retains the option to move back in if their care needs change (Kavanagh 2015).

Trends in the reverse mortgage market

Although reverse mortgages are the most widely-used type of ERP among older Australians, the overall market is small. Despite expanding rapidly through the mid-2000s (figure 6.3), growth in the market slowed after the global financial crisis, which caused significant damage to both investor and consumer confidence. Funding was withdrawn as securitisation collapsed globally, and the number of active lenders in Australia fell from more than 15 to only 5. In recent years the market has flattened, with repayments roughly matching new drawdowns. At the end of 2014, there were about 40 000 reverse mortgages nationwide, with an estimated value of \$3.7 billion (Hickey 2015). This represents just 0.4 per cent of the home equity of older Australians³² (ABS 2015b). The proportion of seniors who have a reverse mortgage is estimated at 1–2 per cent, and does not appear to have risen since 2007 (Brown 2015; Cowan and Taylor 2015; SEQUAL and RFI 2008).

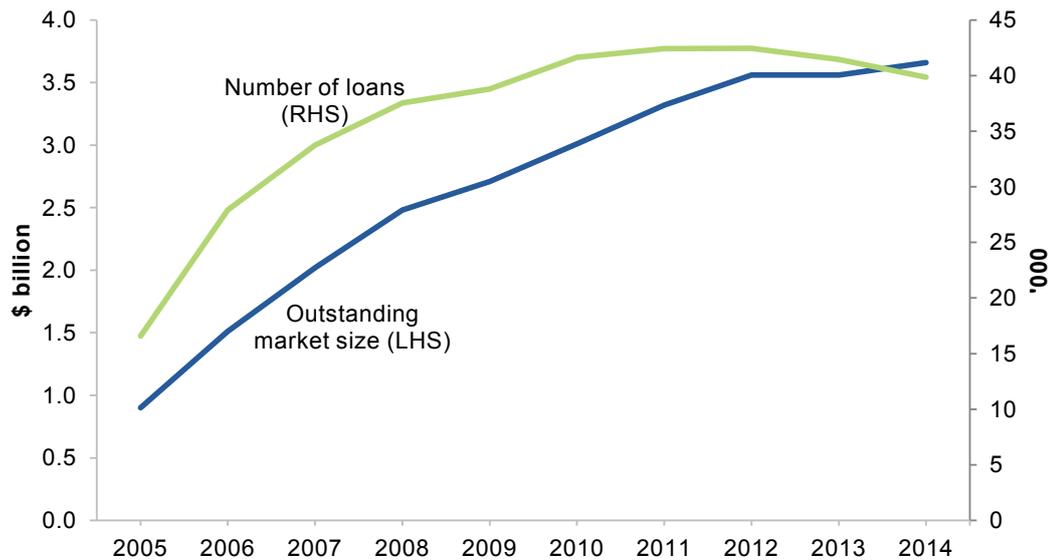
Stakeholders have suggested that there are some indicators of a modest revival in the market. Several lenders have reopened their books, and are among the increasing number of providers that are now also offering aged care loans (Brownfield 2014; Smylie 2014). Demand for this type of product seems to be growing (albeit from a very low base) following the aged care reforms, which placed an increased emphasis on user contributions to fund aged care accommodation (Egan 2014; Kavanagh 2015). So far, however, this segment of the market remains small — in 2014, an estimated 4 per cent of reverse mortgages were used for aged care purposes (Hickey 2015).

Reverse mortgage users tend to be older retirees borrowing fairly small amounts. Over three quarters of borrowers are at least 70 years old, with an average age of 75. The average value of outstanding loans is \$92 000, and the average LVR (which increases with age) is generally about 20 per cent (Hickey 2015). Stakeholders have noted that aged care loans are generally provided to even older consumers and tend to be for much larger

³² Calculated as the total value of reverse mortgages (across all ages) divided by the total value of home equity held by people aged 65 years and over.

amounts — consistent with the fact that most people entering aged care are aged 80 years or over, and refundable accommodation deposits average between \$300 000 and 400 000 (Kavanagh 2015; Seniors First 2014).

Figure 6.3 Size of the reverse mortgage market
2005–2014



Sources: Hickey (2013, 2015).

Equity release products have commonly been viewed as a ‘last resort’ solution for those who have few other assets, and lack the income to support themselves in retirement (SEQUAL and RFI 2008; Tsanadis 2013). Stakeholder consultation indicated that this is true of most current consumers, and although few participants in the Commission’s survey had used an ERP, those who had done so were in lower income brackets. This assertion is also supported by data showing that reverse mortgages are most commonly used for ‘necessity’ purposes: supplementing regular income, repaying debts and making home improvements. ‘Luxury’ expenses, such as travel and car purchases, occasionally occur in combination with these, but are typically not the primary purpose (Hickey 2015).

Home reversion schemes

The home reversion scheme is a debt-free equity release product that has been available in Australia since 2005. It is not a loan, but an actual sale of a home’s future value. The home owner receives a lump sum payment in exchange for a fixed proportion of home equity (up to 65 per cent). Relative to the actual present value of this equity, the lump sum is discounted based on the age and life expectancy of the recipient (or recipients in a joint contract). In effect, this discount represents rental payments on the sold share of the

property for the resident's remaining lifespan. Upon the sale of the home, the agreed proportion of the proceeds is repaid to the provider (ASIC 2015b).

Some comparisons between a reverse mortgage and a home reversion scheme, alongside a traditional mortgage, are illustrated in table 6.1.

Table 6.1 Comparison of equity release products and traditional mortgages

	<i>Standard mortgage</i>	<i>Reverse mortgage</i>	<i>Home reversion scheme</i>
Product type	Debt	Debt	Debt-free (equity)
No. of providers	Many	5–10	1
Market size	\$1.4 trillion	\$3.66 billion	\$482 million
Eligibility	Based on income and employment risk	Age 60 or 65+, available Australia-wide, but can depend on location, value or type of home	Age 60+, available in 90% of metropolitan Melbourne and Sydney postcodes
Payment types available	Lump sum and/or line of credit	Lump sum, income stream, line of credit	Lump sum
Max equity withdrawal	Up to 95%	15-45% of home value, increasing with age	Up to 65% of current home value (minus a discount)
Interest	Fixed or variable — calculated on principal outstanding	Variable interest with additional risk premium — compounding on principal, fees, and previous interest	None — expected rents and property growth are implied in discount
Timing of repayments	Interest is repaid regularly, principal must be repaid by end of loan term	Repaid with sale proceeds from home after owner moves out or dies	Provider takes share from sale of home, required after last owner dies
Leftover money	Depends on timing and method of repayment	Depends on length of loan, accumulated interest, house price and equity protection	Guaranteed to receive unsold share of equity, plus any rebates for early sale or excess proceeds
Possible to owe more than the value of home?	Yes — if home value falls or interest repayments are missed	Only for loans taken out before Sep 2012 — if no NNEG or if terms and conditions are breached.	No — cannot owe more than agreed percentage

Sources: ASIC (2011, 2015d); Bendigo and Adelaide Bank (2015); Deloitte (2015); Hickey (2015); Homesafe Solutions (2015).

Currently, the only provider of home reversion schemes in Australia is Homesafe Solutions, a joint venture of Bendigo Bank and Adelaide Bank. The product has strict eligibility criteria, and is only available to home owners residing in specified postcodes in greater Melbourne and Sydney (Brownfield 2014). Although detailed data are not available on the take-up of home reversion schemes, Homesafe owned \$482 million of the equity in their customers' homes as of June 2015 (Bendigo and Adelaide Bank 2015).

As interest in equity release grows, new debt-free products have begun to emerge on the market. Although these operate differently from home reversion schemes, they are similar in that they involve investors purchasing equity from home owners (box 6.2).

Box 6.2 **Emerging equity release products**

Fractional property investment

Fractional property investment is a new model of real estate investment, launched by DomaCom in 2013. Investors can purchase ‘units’ of properties, without needing to buy a single property outright. It is intended to reduce the risk of entering the property market by allowing less wealthy investors, such as self-managed super funds, to build a diversified portfolio.

DomaCom has announced an accompanying equity release product that will allow seniors to gradually sell equity in their home to fractional property investors, while still living in the property. Additional equity is sold every five years to pay rent to investors and a fee to DomaCom, but even if all equity is sold, the home owner retains a permanent right of residency and DomaCom covers all additional costs — equivalent to a no negative equity guarantee. The product was originally intended for release alongside the investment platform, but has been delayed pending approval by regulators.

Property Options for Seniors, Pensioners and Investors (Popi)

A new entrant into equity release, Popi Australia, has developed a ‘property option’ agreement under which a home owner receives an income stream in return for the capital growth on their home. The investor makes a monthly payment to the home owner, and gains the right to buy the home in the future at a pre-agreed price. Only a very small number of these products have been sold in South Australia since 2013. ASIC’s MoneySmart website warns that property options are unlikely to be covered by credit or financial services laws, potentially preventing access to some consumer protections.

Sources: ASIC (2015a); Brownfield (2014); DomaCom Ltd (2014).

6.3 What are the impediments to the private equity release market?

The low overall take-up of equity release products is not easily explained by any single cause. Rather, the market is constrained by a complex set of supply and demand factors that appear to reinforce one another.

Demand-side factors

The vast majority of older Australians are highly reluctant to monetise equity by tapping into the wealth in their homes (Commission survey; Olsberg and Winters 2005). Even people who are willing to consider ERPs often encounter a range of downsides to the products, and ultimately choose to avoid them. Several explanations for this behaviour are discussed below.

Preferences of older Australians

Many older Australians hold strong preferences not to access the wealth they have accumulated in the family home. Evidence shows that people tend to deplete their savings very slowly in retirement, and in some cases, even accumulate wealth. Much of this wealth is in the form of home equity (chapter 3).

There are several factors underlying these preferences. One explanation is that many Australians wish to keep the family home as an inheritance for their children or other beneficiaries (Commission survey; NSA and Challenger 2013). There is also evidence suggesting that large bequests are at times an unintended result of older people engaging in ‘excessive precautionary savings’: conserving the wealth in their homes as insurance against the risk of facing large medical or aged care costs towards the end of life (chapter 2; Commission survey). Retirees often keep their savings for ‘rainy day’ or emergency expenses, and would face a reduced capacity to meet these costs if they were to finance consumption from their home equity (Austen and Ong 2015). This risk averse behaviour may also be biased by the tendency of individuals to place greater weight on extreme events that occur with very small probabilities (Barberis 2013).

Some of the most important barriers impacting decisions about home equity are emotional factors, such as debt aversion and a strong attachment to the family home (Commission survey). These preferences contribute to a strong negative stigma around the use of debt in later life. People who spent their lives working to pay off a mortgage can be reluctant to go back into debt on their house, viewing it as a sign of failure.

There is evidence to suggest that some of these preferences will change across generations. Younger generations are more accepting of debt, and people are placing less emphasis on bequests (Commission survey; HSBC 2015; NSPAC 2012; Olsberg and Winters 2005; Ong et al. 2013). Although this generational shift will occur slowly, it will likely have a positive effect on demand for ERPs in the long term.

Negative perceptions of equity release products

Equity release products face an immense challenge in overcoming distrust throughout the community. A common view amongst retirees — and even many finance brokers and lenders — tends to be that ERPs take advantage of vulnerable elderly people, or that they are often used by family members to do so (Linden 2007; Ong et al. 2013; SEQUAL and RFI 2008; Smylie 2014).

Past media coverage of reverse mortgages may have resulted in long-lasting reputational damage. The entire industry became stigmatised after people faced substantial losses due to inappropriate products and the effects of the global financial crisis (ASIC 2005; Rose 2015). Although the market is now more regulated, the Commission’s survey found that awareness of the 2012 regulations is low, and most consumers still have overall negative perceptions and intentions regarding equity release. Consequently, little growth

has been seen in the market (Hickey 2015), and it is likely too soon to assess whether these consumer protections will result in greater demand.

Complexity of products and lack of information

Even older Australians who are willing to consider ERPs may be deterred by their complexity. Although older Australians are typically aware of the products, the majority have only a limited understanding of how they work (Commission survey). This is unsurprising, given that ERPs come with complicated risks, and have a range of possible implications for assets, liabilities and entitlements. They can require a high degree of financial literacy to understand, but many older people have low levels of financial knowledge, especially with regards to choosing financial products (ANZ and The Social Research Centre 2015; NSPAC 2013). Consequently, the industry has often argued that the main reason for poor demand is not that the products are unsuitable, but that most consumers do not understand them (SEQUAL and RFI 2008; SEQUAL sub., pers. comm., 7 August 2015; stakeholder consultation).

In part, these issues arise from a lack of information. Older people rarely have opportunities to learn about ERPs — most banks and lenders do not offer them at all, and so they are unlikely to be promoted by the institution with which someone has an existing relationship. There is little in the way of advertisements or other resources publicising information about what products are available, how they work, and what benefits they can have (Brownfield 2014). In addition, stakeholders noted that financial advisers are typically ill-informed about ERPs, and hence are unlikely to fulfil the need for information.

Pension and aged care disincentives

Current distortions in means testing arrangements may be holding back demand for ERPs. Many people for whom equity release would be suitable currently have little motivation to do so, because the value of their home is largely exempt from the assets tests for the Age Pension and for aged care co-contributions. These arrangements are inequitable, because they give preferential treatment to some home owners. People living in highly valuable homes can be eligible for the same level of government assistance as many renters and less wealthy home owners, and therefore do not need to use their home equity to fund their own retirement and care costs.

The same rules also act as a disincentive to equity release by encouraging older people to hold as much wealth as possible in their homes. Retirees who convert home equity into means-tested assets may have their entitlements reduced. People are therefore inclined to release only small amounts of equity that they can immediately use on non-means tested expenses, such as home improvements or living costs. As this payment structure is not suitable for all retirees' needs, and smaller amounts are more easily outweighed by large fees, the products are ultimately less appealing.

High costs and risk incidence

Consumers often avoid ERPs for the simple reason that they are too expensive (Commission survey). Reverse mortgages have higher fees and interest rates than other mortgages, and because no repayments are made, these costs rapidly escalate through compound interest — even when the amount borrowed is small. These costs compensate providers (financier or investor) for the collective incidence of tenor and house price risks that they ultimately bear, and also brokers for the administrative complexity of the products. But for consumers, many of whom identify fees and interest rates as the most important features of a reverse mortgage (SEQUAL and RFI 2008), this product feature is a strong deterrent.

The costs of a reverse mortgage are especially unappealing because they are not only high, but unpredictable (albeit ultimately capped by the NNEG). The home owner faces a range of risks, and can easily accumulate a very large debt — for example, if they live longer than expected, or if their equity is eroded by a fall in house prices or a rise in interest rates. This is at odds with the more conservative preferences of older people: retirees tend to be far more risk averse and loss averse than the general population (AARP and American Council of Life Insurers 2007; NSA and Challenger 2013). They show little interest in being locked into a long-term contract with substantial exit fees, or increasing their risk of financial distress in later life.

Debt-free equity release products create a means of releasing equity whereby many of the risks associated with house prices, interest rates and longevity are transferred to the provider. In a home reversion scheme, the share of equity owed to the lender is fixed, protecting the home owner from fluctuations in interest rates and property values. Homesafe's contract also includes conditions that explicitly mitigate other risks: in the event of the early sale of the home or very strong property appreciation, a rebate will be triggered that reduces the share owed to the provider (Brownfield 2014).

Although debt-free ERPs are less risky for consumers, this comes at a cost — a tradeoff illustrated by the scenarios in box 6.3. The true price of a debt-free product is paid not when the property is sold, but upfront out of home equity, in the form of a reduction in the cash payment to the home owner. The amount is discounted to reflect not only expectations of property values and longevity, but also the additional risks absorbed by the provider. Consequently, for a given LVR, a home reversion scheme will provide a smaller lump sum than a reverse mortgage (Hanewald, Post and Sherris 2014). While the home reversion scheme compensates for this by protecting considerably more equity for the eventual sale of the home, this delayed benefit is at odds with the time preferences of consumers, who place more weight on money received in the present. This may explain why, in countries where both products are available, home reversion schemes have seen low uptake compared to reverse mortgages (Reifner et al. 2009).

Box 6.3 Comparison of risks in a reverse mortgage and a home reversion scheme

Consider a 70-year-old single female whose home is valued at \$600 000, and who requires a \$100 000 cash lump sum. Suppose the home is expected to be sold in **15 years** and expected property appreciation is **3.5 per cent** per year. A reverse mortgage is available with an interest rate of **7 per cent**, and a home reversion scheme for this customer will apply a discount of **50 per cent**, such that one third of their equity (current value \$200 000) is sold. The below table shows the outcomes for a reverse mortgage and a home reversion scheme in this base case, and five alternative scenarios — one where the interest rate is **10 per cent**, one where the property value grows by only **1.5 per cent** per year, one where the property value grows by **5.5 per cent** per year, one where the home is sold in **22 years**, and one where the home is sold in **8 years**. All scenarios assume that there are no fees, and the provider's rebates for the home reversion scheme are not included.

These outcomes illustrate the ways in which a reverse mortgage exposes consumers to both upside and downside risks of changes in house prices, interest rates and longevity. In a home reversion scheme, consumers keep the same proportion of equity regardless of these fluctuations, so most of the risk incidence falls on the provider or investor. This makes the home reversion scheme a 'safer' product — but also means that if interest rates are low, house prices are strong, or the contract ends early, a reverse mortgage is ultimately cheaper.

	Reverse mortgage			Home reversion scheme		Better option?
	House value	Repayment	Remaining equity	Provider share	Remaining equity	
Base case	1 005 209	284 895	720 315 (72%)	335 070	670 140 (67%)	RM
High interest rates (10%)	1 005 209	445 392	559 817 (56%)	335 070	670 140 (67%)	HR
Low property appreciation (1.5 per cent)	750 139	284 895	465 245 (62%)	250 046	500 093 (67%)	HR
High property appreciation (5.5 per cent)	1 339 486	284 895	1 054 591 (79%)	446 495	892 991 (67%)	RM ^a
High longevity (22 years)	1 278 907	464 377	814 530 (64%)	426 302	852 605 (67%)	HR
Low longevity (8 years)	790 085	174 783	615 303 (78%)	263 362	526 724 (67%)	RM ^a

^a Rebates would apply to the home reversion scheme in these scenarios, reducing the advantage of the reverse mortgage, though these are unlikely to be sufficiently large to alter the outcome.

Sources: ASIC (2015c); Homesafe Solutions (pers. comm., 8 September 2015).

Supply-side factors

The current equity release market is characterised by its high costs and low number of providers, largely arising from a lack of funding — which is ultimately a function of low

demand. Despite some signs of renewed interest, there are a number of reasons why both investors and providers may remain reluctant to enter the market.

Small market size

A key reason for the low funding of the industry is that the profits available are simply not significant relative to the costs and risks (including reputational) of offering ERPs. This is in part because ERPs appeal only to a niche consumer base, and is exacerbated by the fact that the loans themselves are much smaller than most residential mortgages: new reverse mortgages in 2014 averaged \$79 500 (Hickey 2015), whereas new home loans averaged over \$325 000 (ABS 2015c). In total, reverse mortgages totalled only \$3.7 billion at the end of 2014 (Hickey 2015), compared to the \$1.4 trillion residential mortgage market where investors are focusing their efforts (Deloitte 2015). Despite the higher interest rate of reverse mortgages, this smaller asset base (and the resulting lack of risk pooling) results in low profits.

Even if some older people wish to release a larger amount of equity, a ‘high LVR’ segment of the market is unlikely to emerge due to the legislative restrictions on LVRs (box 6.1). In particular, LVR regulations may be a constraint on providing aged care loans. At present, it is difficult for consumers to use a reverse mortgage to pay the RAD unless the value of their home is already very high. For example, someone who is 83 — the average age of a person entering residential aged care (ACFA 2015) — would be restricted to borrowing up to 43 per cent of the value of their home. This means that to cover a RAD of \$430 000, their home would need to be worth at least \$1 million.

Like reverse mortgages, debt-free ERPs are perceived as an undesirable investment — potentially even more so, because they transfer risk from consumers to providers. Harper (2011) observed that home reversion schemes represent a new asset class, ‘pooled residential property’, that is not currently accepted by institutional investors.

Longevity risk and the No Negative Equity Guarantee

Many investors are unwilling to fund ERPs because of uncertainty about the timing and amount of returns. This arises primarily due to longevity risk: the possibility that the home owner will live beyond their life expectancy, delaying the sale of the home.

All ERPs carry longevity risk, but its consequences can be particularly severe for reverse mortgages, due to the statutory NNEG. The longer the borrower continues to live in their home, the more likely it is that the NNEG will be triggered, reducing the lender’s return. The NNEG therefore represents a significant shift in risk exposure from borrower to lender that does not exist elsewhere in the mortgage market.

Longevity risk is priced into reverse mortgages via the interest rate premium. Providers do not adjust this premium in line with the LVR, even though there is virtually no chance that

the NNEG will be triggered with an LVR under 30 per cent (Alai et al. 2014). Similarly, aged care loans have identical pricing to other reverse mortgages, despite the fixed length term that avoids longevity risk entirely, and the generally low life expectancy of people entering residential aged care. Consequently, consumers must often pay for an unnecessary NNEG, contributing to the demand barrier of high costs. Although differential pricing for low-LVR loans or aged care loans might attract more customers, it is unlikely to occur unless both providers *and* investors recognise this difference in risk, and believe that there is sufficient demand to justify the costs of offering greater product and pricing diversity.

Capital adequacy regulations

The Australian Prudential Regulation Authority (APRA) regulates the levels of capital held by financial institutions, relative to the riskiness of their assets. Residential mortgages are generally subject to concessionary capital adequacy requirements, but reverse mortgages are treated as ‘non-standard’ mortgages due to their ‘unique operational, legal and reputational risks’ (APRA 2010). Consequently, they carry a higher risk weighting, requiring providers to increase their capital holdings in order to offer the products. National Australia Bank (2014) observed that this requirement is likely to make ERPs less attractive for lenders. The Senior Australians Equity Release Association of Lenders (SEQUAL) indicated that it increases the cost to borrowers and limits the supply of funding (SEQUAL sub., pers. comm., 7 August 2015).

Despite the risks associated with reverse mortgages, this treatment may be inappropriate. The prudential requirements exceed those in comparable international markets, and have not been updated since the introduction of maximum LVRs and consumer protection regulations aimed at reducing risk. A key issue is that the same risk weighting is applied to all LVRs below 60 per cent — a low LVR for a standard mortgage, but a very high LVR for a reverse mortgage. The average LVR of a reverse mortgage is 13 per cent for people younger than 80 years and 25 per cent for people 80 years and older (Hickey 2015), implying a much lower level of risk. Although aged care loans have higher LVRs, they also run for much shorter terms, limited to five years, and thus pose lower risk.

Inconsistent regulatory framework for debt-free products

Debt-free equity release products operate in a complicated environment because they do not clearly fit under existing legislation. Commonwealth regulations for ERPs apply only to reverse mortgages. Consequently, the specific regulations that apply to debt-free products — and whether they are state or federal regulations — depend on the structure of the product itself (Brownfield 2014; Homesafe Solutions 2014).

This inconsistent framework is likely to prevent providers from offering ERPs more widely. For example, a home reversion scheme may appear to be a financial product, but is in fact treated as a property transaction, and hence regulated only by state real estate laws. Differences across jurisdictions are an impediment to the availability of these products, as

there are costs and challenges associated with writing different contracts in each state and negotiating stamp duty exemptions with state governments (Homesafe Solutions sub., pers. comm., 7 August 2015).

Regulating only the individual products currently on the market also creates a substantial barrier to entry for prospective product innovators. For example, the DomaCom product (box 6.2) has faced substantial delays while negotiating individual product characteristics with regulators. Providers must face the costs and challenges of navigating regulations that were not designed with their products in mind, as well as the risk of adverse changes to the regulatory environment after they have already entered the market.

Reputational risk

Many financial institutions are alert to the reputational risk embodied in the negative publicity that could be generated by offering ERPs. ERPs are inherently treated with suspicion due to the perception that they are designed to take advantage of vulnerable elderly people. A single, isolated instance of a poor consumer experience could result in significant reputational damage, with material costs to the provider's brand value far outweighing the profits available in such a small market.

Reputational damage can also occur through association with reverse mortgage products, even without the occurrence of a specific adverse event. In light of regulation, the practical risk of financial harm coming to equity release consumers is low, but many people are still unaware of these protections — and more familiar with prior media coverage of older people being unexpectedly hit with enormous debt or foreclosed upon. As such, a financial institution that gains most of its business through more traditional products, and relies on a long-term relationship with its customers, may not wish to be seen as a reverse mortgage provider (Rose 2015; Tsanadis 2013). Although some established financial institutions do offer a reverse mortgage product, they tend to view it as a niche market.

6.4 Overcoming impediments to greater use

Whose responsibility is it?

Not all of the problems raised in section 6.3 warrant government intervention. Rather, impediments to the equity release market can be viewed in three different ways.

First, some factors simply reflect underlying consumer preferences, the commercial decisions of funders and suppliers, and fundamental characteristics of the products themselves. These factors may change over time, particularly due to the ageing of the population and the baby boomer generation's greater tolerance for debt. However, despite the potential for growth, ERPs may not become significant enough for larger lenders to take interest, or for the dominant public perception to change.

Second, there are some factors that are more amenable to change, but would be most appropriately dealt with by the private market. For example:

- Low consumer awareness and understanding of ERPs could be addressed through greater industry spending on promotion and advertising. This role could be filled by an equity release representative body such as SEQUAL, or a consumer advocacy organisation such as National Seniors Australia or COTA Australia. To this end, SEQUAL launched a free information service for consumers in August 2015 (SEQUAL 2015a).
- Providers could develop innovative new products that are more appealing to both consumers and investors. For instance, debt-free ERPs may play a role in overcoming consumer debt aversion. In addition, DomaCom, a new entrant to the debt-free market, has tapped an alternative funding source in the self-managed super fund sector — which, relative to the banking sector, has less exposure to residential property and may potentially tolerate the long-term nature of the investment (DomaCom Ltd 2014; Scheule 2014).
- Providers could offer greater product differentiation and more attractive pricing even within existing regulatory settings. Alai et al. (2014) and Rawlinson (2006) found that at the LVRs offered in Australia (up to 45 per cent), the true risk premium for reverse mortgages is well below that implied by the interest rates on the market. This suggests that providers could drive growth by offering products with either lower interest rates or higher LVRs.

However, there is presently little indication of interest from current or new providers in pursuing these options. This may reflect a combination of excessive risk aversion, funding constraints, low competition, or simply the fact that there is little demand in the market. For example, although consumers may only need small ERPs, which carry minimal risk, private providers will not necessarily offer such products at an appropriate price — their funding costs assume the presence of NNEG risk, and they lack the economies of scale that would persuade investors to take interest in cheaper products.

Third, there are factors that may justify government intervention to support the equity release market on efficiency or equity grounds. Such intervention should be a response to impediments that reflect either a market failure or government failure, and thus cannot be resolved by the market alone. The case for government involvement on these grounds appears weak, beyond the removal of unnecessary regulatory constraints on providers (discussed below) and distortionary incentives for consumers. However, if such changes to incentives had the effect of compelling many Australians to draw on their home equity, this may prompt a role for government policy to ensure that ERPs are accessible and understandable to the wider population (discussed in section 6.5).

Potential for regulatory reform

Reverse mortgages are heavily regulated. This is primarily because they are more complex than most other loans, and yet are also targeted at a more vulnerable consumer group — the elderly. The current regulatory regime (box 6.1) was enacted in order to counteract the relative disadvantage of a retired senior in a reverse mortgage contract, who would typically have:

- lacked the information, financial literacy and cognitive ability to fully understand the risks involved and make an optimal decision
- been unable to negotiate crucial terms of the contract — such as default conditions, occupancy of non-titleholders, and protection against negative equity
- been unable to accurately determine the future value of the equity in their home or the future size of the debt — subject to fluctuations in property values, interest rates and their own lifespan
- lacked the financial resources to repay the debt should it grow far larger than expected (Burns 2014; Parliament of Australia 2012).

Although consumer protection regulations may typically be assumed to benefit consumers at the expense of providers, this is not necessarily the case for ERPs. A regulated industry can be mutually beneficial by inspiring greater confidence from both consumers and investors, and reducing the potential for negative publicity. SEQUAL — despite originally supporting the self-regulation of the industry through its own code of conduct — has shown support for enshrining consumer protections into law, in order to increase the willingness of consumers to engage in home equity release (SEQUAL 2011, 2015b). Similarly, Homesafe Solutions (2014) has indicated its support for national regulation of all ERPs, including its own product (the home reversion scheme).

However, as highlighted in section 6.3, some elements of the regulatory environment can also constrain potential market growth. Although this does not appear to be the key barrier to the provision of ERPs, there is scope to adjust regulation and thereby alleviate some constraints on supply.

Moving away from product-specific regulation

In order to address the problems caused by regulating at a product-specific level, the current reverse mortgage regulations could be replaced by an overarching principles-based regulatory framework for equity release products. This would have two main advantages.

First, regulations can protect not only consumers, but also the commercial viability of the industry itself. The current environment acts as a deterrent to all potential providers: if a new entrant were to offer a product without appropriate consumer protections, or one intended to take advantage of seniors, the resulting negative publicity would be likely to damage even safe, regulated providers simply by association. Regulating at the product

level *after* problems have occurred — as was the case for reverse mortgages — is too late to prevent reputational damage, and does nothing to prevent the same problems from repeating with a different product (SEQUAL sub., pers. comm., 6 August 2015).

Second, introducing an overarching regulatory framework would reduce barriers to entry by providing structure and certainty for potential market entrants. It would eliminate the costs providers must currently face in order to navigate a complex system, often relying on loopholes and exemptions. It would also reduce the risk that these regulations may change in the future and make their product unworkable.

Equity release regulations could be in part adapted from the reverse mortgage regulations, but in order to be appropriate for both debt and debt-free products, they should emphasise broader principles rather than specific design features. Principles-based regulation can promote innovation by allowing more new products to enter the market, conditional only on producing equivalent consumer protection outcomes to those already available (Black, Hopper and Band 2007). Such regulations could be broad enough to account for the fact that new types of products may involve different risk factors, meaning that the specific consumer protections of reverse mortgages would not always be appropriate or sufficient. They would also future-proof the power of regulators to consistently regulate all ERPs, without requiring frequent legislative amendment to meet a growing variety of products.

Some of the other regulatory changes that could be made — either within the current regime or alongside a move to principles-based regulation — are discussed below.

Letting providers choose to bear the risk

A number of the current regulatory requirements imposed on reverse mortgages — notably the mandatory NNEG, LVR limits, and capital adequacy requirements — appear to collectively impose an unnecessary burden on providers, as they do not appropriately differentiate between products with different risk profiles. By increasing costs and deterring entry to the market, these regulations may limit competition and reduce the diversity of product offerings available to consumers.

Of these regulations, the NNEG appears to be the most suitable in its current form. Despite being the main driver of high interest rates (section 6.3), the fact that it became mandated by regulation is unlikely to have had a material impact. Prior to 2012, the industry was self-regulated under the voluntary code of conduct developed by SEQUAL. The NNEG was required by this code — as would be expected, in order to promote consumer confidence and protect providers from the reputational risk attached to negative equity events. Consequently, the risk associated with the NNEG was already priced into most products.

On the other hand, relaxing the regulations on LVRs may be warranted. Removing maximum LVRs would allow providers to offer higher-value products at their own discretion, and may increase the diversity of product offerings — particularly for aged care

loans. The impact of this change may be small, given that providers are sufficiently risk averse that they typically offer LVRs *below* the current limits, and most consumers who consider ERPs only wish to access a small amount of equity (Commission survey; Hickey 2015). Nevertheless, the rationale for the present restrictions is largely unclear, and they appear to be redundant. From a consumer protection standpoint, the legislated NNEG already serves a dual role: it not only limits the size of the debt, but also shifts risk to the lender, such that it is not in their interest to enter into a reverse mortgage with a significant probability of eroding all of the home's equity. Lenders already have an incentive to provide appropriate LVRs, because they bear much of the risk of making larger loans.

APRA could further ease the regulatory burden on providers by adjusting capital adequacy requirements along a scale that better reflects the LVR ranges in the market. Providers could be allowed to compensate for the increased risk of reverse mortgages through either a higher risk weight *or* lower LVRs, giving them the flexibility to offer reverse mortgages without the costs of holding additional capital. However, as prudential regulations are determined in line with international agreements, APRA's ability to make major changes is limited. A simpler approach would be to subject reverse mortgages to similar risk-weighting rules to standard residential mortgages, provided that they meet certain requirements. This treatment would be in line with other countries, including Canada and the United Kingdom (Basel Committee on Banking Supervision 2013).

Additional consumer protections

Although reverse mortgages are now heavily regulated, some have argued that the legislation overlooked certain issues, and that there remain further avenues for consumer protection. Proposals for regulations raised in the literature and during stakeholder consultation for this study include: protecting the permanent right of residence, requiring financial advice in addition to legal advice, or otherwise enabling greater involvement from financial advisers and planners (Burns 2014; DAE 2014; Homesafe Solutions sub., sub., pers. comm., 7 August 2015; SEQUAL sub., pers. comm., 7 August 2015).

Such regulations have the potential to offer some minor gains to the market. Most notably, older Australians appear to value the guaranteed right to remain in the home. They are slightly more likely to state that the appeal of ERPs would be increased by such a protection than by a reduction in costs (Commission survey). For the most part, however, the private market can voluntarily offer these features and services. It is therefore likely that stakeholder interest in such policies is primarily about reducing reputational risk or creating new sources of customers, rather than meeting an actual necessity for stronger consumer protections.

In any event, there is little evidence to suggest that additional consumer protections would have a significant impact, given that the observable effects of such policies to date have been minimal. Consumer awareness of these protections is low, with only 21 per cent of people over 60 being aware of the statutory NNEG, and only 4 per cent stating that it makes the products significantly more appealing (Commission survey). Furthermore, the

market has not grown since regulations came into effect (Hickey 2015). While the impact of currently-implemented protections may become visible over time, the scope for further adjustment is relatively minor.

6.5 Government intervention in a broader policy context

Equity release provides one possible mechanism to enable older Australians to make welfare-improving decisions about housing equity. For example, ERPs have been proposed as a way to help older Australians to pay for private health care, and make home modifications and repairs that would enable them to age in their homes rather than in residential aged care.

For this reason, some have suggested a role for government to actively encourage equity release, beyond the removal of regulatory barriers. However, in the current policy environment, the Commission does not consider there to be strong efficiency or equity arguments for active government intervention. Such intervention is unlikely to warrant the costs because, regardless of government encouragement, older people are simply disinclined to tap into their housing equity (Commission survey).

Many have argued for government to facilitate the use of ERPs in the context of proposals for other policies — such as tightening means testing for the Age Pension — that could significantly affect the entitlements of home owners. Were there changes that compelled a large number of older people to draw down on their home equity, this would raise a number of equity concerns. ERPs are costly and unviable for small drawdowns; consumers lack information and may fear exploitation by providers; and many older people live in homes that are not considered by private providers to be suitable for equity release due to their location, value, or type of dwelling (PC 2011).

The remainder of this section discusses a range of options for equity release policies that have been proposed or attempted, in Australia and internationally. Broadly speaking, these proposals can be classed into two categories:

- assisting the private market to make ERPs more accessible, understandable and appealing to potential consumers, providers and investors
- directly providing a form of equity release to supplement pension income or fund government services, particularly for those who cannot access suitable private products.

Developing the private market

Many stakeholders, both in consultations for this study and in other contexts, have expressed the view that government should assist the growth of the private market to enable the widespread use of ERPs. Such policies could take a range of potential forms.

A relatively light-handed approach would be for government to provide a greater amount of readily accessible information about ERPs, and more actively promote their use. Better information could improve understanding of, and confidence in, the products, thus encouraging consumers, providers, investors and advisers to engage with the market. In particular, helping older Australians to understand how ERPs work, and informing them of the consumer protections in place, could play a key role in driving better housing decisions.

Information provision could, for example, take the form of an independent organisation that can advise consumers as to whether equity release is appropriate for them. Previously, a consumer education role was played by the Australian government-funded National Information Centre on Retirement Investments. However, the centre was defunded and ceased operations in early 2015. The government now offers only very general consumer information for equity release products, via a small section of the Australian Securities and Investments Commission (ASIC) MoneySmart website (ASIC 2015a).

A range of more active approaches for government involvement in equity release markets have been considered within Australia and internationally.

The Financial Conduct Authority — the UK equivalent of ASIC — is facilitating discussions with industry and consumer bodies about the future of the equity release market, the kinds of products that could exist, and potential ways of encouraging new entrants and innovation (Woolard 2015). By improving access to information and assisting coordination between stakeholders, this approach could ultimately benefit consumers through greater choice and improved products. For instance, some stakeholders suggested that new types of debt-free products could be developed in Australia by the superannuation and insurance industries.

Harper (2011) argued that government should intervene to grow the market for debt-free ERPs in Australia, as investors are currently too wary of new types of assets. This would aim to increase choices for consumers and institutional investors, and reduce the demand for public funds from retirees. However, an approach in which the government attempts to ‘pick winners’ in a new industry may be ill-advised. Focusing on specific products could reduce the incentive to innovate, and cause providers to focus on securing and retaining assistance rather than improving their products (NCA 2014b).

Cowan and Taylor (2015) proposed that the Australian Government could design a standard form default reverse mortgage annuity product, and insure the NNEG for providers of this product that meet certain requirements. This approach has been taken by the United States Government under the ‘Home Equity Conversion Mortgage’ (HECM) program, through which most of the US reverse mortgage market is insured.

There are several potential benefits to a HECM-style scheme. The existence of a government-endorsed equity release market could prompt greater awareness of ERPs on both supply and demand sides, as well as increasing trust amongst consumers and reducing reputational risk to providers. Insuring the NNEG would mitigate longevity risk — should

a borrower's debt exceed the value of their home, then the government, not the lender or borrower, would bear the loss. This would reduce the cost of funding reverse mortgages due to the pooling of tail risk, and the benefits could be passed on to consumers in the form of lower interest rates.

However, there are a number of downsides to government insurance.

- It would result in a substantial transfer of longevity risk — to which the government is already significantly exposed via the Age Pension, health care and aged care — and hence may need to be paid for through either taxes or additional product fees.
- It creates a high likelihood of a moral hazard problem: if lenders can transfer negative equity risk to the government, they may be inclined to encourage borrowers to take out reverse mortgages with higher LVRs than needed, resulting in greater costs and risks to both consumers and taxpayers. The high HECM default rate of 9.4 per cent may be indicative of this issue (Consumer Financial Protection Bureau 2012).
- By giving favourable treatment to reverse mortgages, it acts a disincentive to new and innovative market entrants to which a NNEG would not be applicable. This distortion might be avoided by developing equivalent arrangements for providers of debt-free ERPs, but this would result in greater complexity and increased administration costs.

Alternatively, government could design the product criteria without including financial incentives for providers. This type of scheme could enhance the availability of information for both consumers and providers, and impose restrictions to protect vulnerable home owners. However, it would not change the underlying economic characteristics of the product, and hence is unlikely to overcome either the existing market impediments or the equity issues raised by major reforms.

Providing a public equity release scheme

Many have argued that government may need to step in to directly provide ERPs where it is not financially viable for the private market to do so. This is typically proposed in the context of broader tax and transfer reforms that aim to address the sustainability of retirement incomes and government expenditure.

Funding retirement incomes

One approach to government provision posits equity release as a means of paying for general retirement consumption. In particular, it is often suggested that Age Pension reform could be facilitated by allowing Australians to use their home equity to delay the impact of any lost pension entitlements until the end of life. Daley et al. (2013) argued that the Age Pension assets test should include the principal residence in full, but that pensioners who fail the new test would be allowed to receive their payments in the form of a government-provided loan secured against their home. Similarly, Cowan and Taylor's (2015) proposal — centred around a stricter assets test and a government guarantee on

reverse mortgages in the private market — also included a role for government provision, in order to ensure that age pensioners with limited access to the private market would still be able to access their home equity.

The Australian Government already offers a little-known equity release product along these lines: the Pension Loans Scheme (PLS) (box 6.4). In its present state, the PLS does not appear to have any clear purpose — it was originally designed to accompany a proposed (but never implemented) assets test for the pension that would have included the principal residence (Arthur 2015), but is now in effect a stranded policy.

Box 6.4 The Pension Loans Scheme

The Pension Loans Scheme (PLS) is a limited form of reverse mortgage provided by the Australian Government through Centrelink. It is available to individuals or couples who:

- meet the age and residence requirements for the Age Pension or another ‘qualifying payment’ — including the Disability Support Pension, Carer Payment or Bereavement Allowance
- are either ineligible to receive this payment, or only eligible for a reduced rate, because their income or assets (but not both) are over the relevant limits.

The scheme allows users to nominate the amount they will borrow each fortnight, which acts as a ‘top up’ to any existing payments they receive. The total payment cannot exceed the maximum Age Pension amount. For example, a single part pensioner receiving \$500 per fortnight could use the PLS to borrow up to an additional \$367 per fortnight, such that their total payment is at the full pension rate of \$867 per fortnight.

The PLS is functionally equivalent to a reverse mortgage with a largely predefined set of features. It has a minimum age of 65 years, and funds can only be received as a regular income stream. The rate of compound interest is currently fixed at 5.25 per cent (compared with 6 to 7 per cent for commercial products), and full or partial repayments can be made at any time. A limit applies to the total amount that can be borrowed, depending on the equity in the property used as security (which does not need to be the retiree’s own home), the equity the owner wishes to keep, and their age when the loan is granted.

Source: DHS (2015d).

Despite being available since 1986, and in its current form since 1996, the PLS has seen very little uptake (Arthur 2015). In 2014, there were only about 800 loans outstanding under the scheme — representing 0.04 per cent of Age Pension age households in Australia — with a total value of \$31 million (ABS 2015b; Department of Human Services administrative data, DSS, pers. comm., 29 September 2015). There are several explanations for its low popularity.

- Consumer awareness of the product is low, and it has not been actively promoted to seniors. The Commission’s survey found that only 16 per cent of older Australians had heard of the PLS, and most showed no interest in using it.
- It is unavailable to people who already receive the full pension rate — the group most likely to need financial support in retirement. In effect, only those who are too wealthy

for the full pension can take advantage of the top up, whereas poorer home owners are unable to access the scheme at all (Denniss and Swann 2014).

- It is only available as a small fortnightly income stream, which is unsuitable for many part pensioners. People who are ineligible for the full pension are more likely to have other sources of income to cover their recurrent living costs. If they needed to access equity in the event of a large one-off expense, a more appropriate option would be a lump sum product offered by a commercial provider (PC 2013).

One way for government to improve access to equity release would be to expand the PLS to provide wider availability and greater flexibility. Utilising an existing scheme would be expected to reduce setup and administration costs, allowing government to instead focus on promoting awareness. Denniss and Swann (2014) suggested that to enable full pensioners to utilise the scheme, the maximum fortnightly payment could be increased to the full Age Pension rate, removing the ‘top up’ aspect. Another possibility would be for the scheme to allow limited lump sums to be drawn as an alternative to an income stream. For example, up to one year of payments could be taken as an advance for larger expenses, such as home modifications or health costs.

Making these changes could address the design flaws of the PLS, but they may not justify the risks assumed by government and taxpayers. There is also potential for implementation costs to be significant — if larger amounts were available through the PLS, its classification may change from social security policy to financial product, which would be subject to more complex reporting requirements (DSS, pers. comm., 11 August 2015). In addition, unless strict limitations were imposed on eligibility for the scheme or amounts that could be drawn, there would be a risk of crowding out the private market with a cheaper product.

Any move to alter the PLS should be preceded by a thorough review of the current scheme to determine whether it should be retained, and if so, what its objectives and characteristics should be. It should also account for the likelihood that most older Australians would not take interest in the PLS, even if it were expanded to allow larger income streams or lump sum drawdowns (Commission survey).

Funding government services

The other main approach to a government equity release scheme is to restrict the use of funds to specific purposes; generally government services. The Commission previously recommended that this type of scheme be introduced to facilitate requirements for greater user contributions to aged care, by ensuring that low-income home owners would be able to release equity to meet these costs (PC 2011). Similar schemes have also been suggested for other ageing-related expenses such as health care, and other housing costs such as property taxes (Brownfield 2014; PC 2013). Present examples of this approach include local council rates postponement schemes in Australia, and other deferred payment schemes abroad (box 6.5).

Box 6.5 **Deferred payment schemes**

In some parts of Australia, senior home owners can defer the payment of council rates through schemes that are akin to small reverse mortgages. State and territory-wide rates postponement schemes are available in South Australia and the ACT. Interest rates in these jurisdictions are low — close to the cash advance rate — and repayments can be made at any time, though they are only required following death or the sale of the home. Similar rates deferral options are also available from local governments in other states, though the interest rates are sometimes much higher. It is the Commission's understanding that the take-up of rates postponement schemes in Australia has been insignificant to date.

These schemes are also used internationally: the New Zealand Government offers a rates postponement scheme, some US states and Canadian provinces allow the deferral of property tax, and in the United Kingdom, a similar approach is used to defer payment for aged care.

Sources: ACT Revenue Office, pers. comm., 25 September 2015; DAE (2015); Government of Alberta (2013); National Council on Aging (2013); PC (2013); UK Government (2014).

The option to defer government payments would reduce housing costs and enable ageing in place, while posing a low risk of substantial equity erosion because the amounts borrowed are typically small. It could, for example, play a valuable role if land tax were extended to the principal residence (chapter 5). This would be unlikely to crowd out general purpose private products, because it could not be used to access cash directly.

However, the deferred payment approach may also encounter some challenges:

- Whereas existing rates postponement schemes add a known amount to the debt at regular intervals, payments for other government services can be unpredictable, and so the scheme is likely to be much more costly to administer.
- Some government services are bulk-billed or directly government funded, and thus do not require individuals to contribute. These expenses would be more challenging to adapt into a payment system capable of incorporating an equity release scheme.
- A higher capacity to pay for services may simply translate into higher prices, due to the heavy restrictions on supply in industries such as health and aged care. If prices rose to account for demand driven by equity release, this would substantially disadvantage non-home owners (PC 2013).

Assessment

Ultimately, it may be most prudent for governments to accept that there is currently little interest among older Australians in making use of financial equity release products. At most, government intervention in the private equity release market should likely be limited to information provision. Any further measures would require a careful consideration of all costs and distortions that might arise.

As the Commission has previously found, there may be a role for government provision as a part of wider tax and transfer reform — for example, to facilitate greater co-contributions to the cost of aged care (PC 2011, 2013). This would involve government acting as a provider of last resort; guaranteeing access to equity release for low-income home owners whom private providers are unwilling to serve. However, a public scheme would first need to be evaluated to assess whether the benefits (such as the reduction in public expenditure) would outweigh the costs of administering the scheme, the fiscal risks associated with housing prices and longevity, and private market concerns about crowding out.

The appropriate government policy in the equity release market, if any, would depend on the broader policy context and any reforms affecting the principal residence. For instance, a redesigned PLS could address equity concerns under a structurally reformed Age Pension means test. A deferment scheme could be an appropriate complement to increased aged care co-contributions or the introduction of a land tax affecting the principal place of residence. Relatively minor changes — such as imposing a high cap on the exemption of the principal residence from the Age Pension assets test — would correspondingly do little to necessitate policy intervention, beyond improving information in the private market, simply because the effects on housing decisions and on the wellbeing of older households would be small. And if the current policy environment is maintained, such that existing safety nets and exemptions negate the need to access home equity, there is little reason to explore these options at all.

Another key consideration is that the case for government intervention in the long term should not be assessed solely on the basis of current market conditions. In reality, changes to policies affecting the principal residence would be expected to drive both demand and supply for ERPs: consumers would have a greater need to access home equity, and providers would need to address market impediments in order to meet this demand. Evidence from the United Kingdom suggests a growing interest in ERPs under tax and social security reforms that better incentivise the use of home equity (Atkin 2015; Walker 2015). Although the extent to which the market would develop on its own cannot be predicted, providers will nevertheless respond to any changes in the needs and preferences of retirees, lessening the need for policy intervention.

A Stakeholder consultation

In preparing this research paper, the Commission consulted with a range of organisations, individuals, industry bodies, and government departments and agencies. The Commission also published information about the project on its website. This appendix lists parties the Commission consulted with through:

- visits and telephone discussions (table A.1)
- a roundtable on factors affecting the housing outcomes of older Australians, held in Sydney on 25 September 2015 (table A.2).

Table A.1 Consultations

Participant (listed by home state/territory)

Australian Capital Territory

Aged and Community Services Australia (ACSA)
Australia Institute
Council on the Ageing (COTA)
David Tune
Department of Social Services (DSS)
ARC Centre for Excellence in Population Ageing Research (CEPAR)
Henry Ergas
National Aged Care Alliance (NACA)
Retirement Living Council
Treasury

New South Wales

Actuaries Institute
Australian Prudential Regulation Authority (APRA)
Australian Securities and Investments Commission (ASIC)
Aveo Live Well
Catholic Health Australia
Centre for Independent Studies
Combined Pensioners and Superannuants Association of NSW Inc (CPSA)
Commonwealth Bank of Australia (CBA)

(continued next page)

Table A.1 (continued)

Participant

New South Wales

Deloitte
Financial Planning Association of Australia
GPT Group
Ingenia Communities Group
Lend Lease
Macquarie Group
Manufactured Housing Industry Association
Martin Lynch
Reserve Bank of Australia (RBA)
RetireAustralia
Rice Warner
Seniors First
SEQUAL
Stockland
UnitingCare
University of New South Wales (UNSW)

Queensland

National Seniors Australia

Victoria

Aged Care Gurus
Australian Centre for Financial Studies
Australian Unity Retirement Living
Consumer Action Law Centre
Council on the Ageing (COTA) Victoria
DomaCom
Grattan Institute
Heartland Seniors Finance
Homesafe Solutions
Housing for the Aged Action Group (HAAG)
Lifestyle Communities
Office of Senator Mitch Fifield
Paul Dwyer
Residents of Retirement Villages Victoria (RRVV)

Western Australia

Amana Living
Rachel Ong — Curtin University

Table A.2 Roundtable participants — Sydney, 25 September

<i>Participant</i>	<i>Organisation</i>
Barbara Squires	Barbara Squires Consulting
Heather Witham	Aged and Community Services Australia (ACSA)
Rachel Lane	Aged Care Gurus
Jacqui Phillips	Australian Council of Social Service (ACOSS)
Derek McMillan	Australian Unity Retirement Living
Rachel Ong	Curtin University
James Hickey	Deloitte
Sharon Rose	Department of Social Services (DSS)
Kathryn Mandla	Department of Social Services (DSS)
Ian Joyce	Department of Social Services (DSS)
Stewart Thomas	Department of Social Services (DSS)
Craig McInnes	Heartland Seniors Finance
Michael O'Neill	National Seniors Australia
Mary Wood	Retirement Living Council
Gavin Wood	RMIT University
Helen Wood	UnitingCare Ageing
Bruce Judd	University of New South Wales (UNSW)
Catherine Bridge	University of New South Wales (UNSW)
Eileen Webb	University of Western Australia

B Progress on aged care reforms

Key points

- Substantial reforms to aged care have been introduced following the Commission’s 2011 Caring for Older Australians inquiry report, including changes to residential and home care arrangements that both increase supply and improve its responsiveness to the needs of older people.
 - The introduction of consumer directed care in home care, public disclosure of residential accommodation prices and allowing customers greater choice of accommodation payment methods are expected to increase competition and improve the responsiveness of providers to demand.
 - Expansion of home care packages will give consumers greater opportunity to age in place.
- As most reforms have been implemented recently, and many apply only to new recipients of care, it will take some time to ascertain the longer-term impact of the reforms on the housing choices of older Australians.
- Notwithstanding reform progress to date, there is potential to further improve incentives for efficient provision of aged care services and remove supply-side constraints that limit the responsiveness and efficiency of providers.

The Australian Government subsidises a tiered system of aged care services, which includes care delivered in the home and in residential aged care facilities (table B.1).

The efficacy of aged care delivery is a key consideration in the housing decisions of older Australians. Many people only require low level support — for most older Australians, ‘entry level’ services provided in their homes are their only interaction with the aged care system (DSS 2015e). This is in line with the preferences of most older people to age in place and, with home care substantially less costly to deliver than residential aged care, also aligns with the government’s fiscal sustainability objectives.

Accordingly, policy focus has increasingly been shifting from residential aged care, to supporting older people to remain in their home. But trade-offs exist. Home support needs to be delivered efficiently and in a timely manner to maximise its benefit to consumers and increase their capacity to age in place.

Table B.1 Aged care services
2013-14

	<i>Number of clients</i>	<i>Average age</i>	<i>Proportion of people aged 65 years and over</i>	<i>Cost to government</i>	<i>Expenditure per person^a</i>
			Per cent	\$ million	\$
Home and Community Care^b — entry-level support at home	776 000	80.3	22.5	1 701 ^c	329.23
Home Care Packages — more complex support for people able to remain in their homes with assistance	83 000	82.3	2.4	1 271	360.26
Residential aged care — care and accommodation for people who are unable to continue living in their homes	231 500	84.5	6.7	9 976	2 827.92

^a These figures reflect the expenditure per person in the target population, including all Australians aged 65 and over, and Indigenous Australians aged over 50. ^b Amalgamated into the Commonwealth Home Support Programme in 2015. ^c This figure reflects the Australian Government's expenditure on the services delivered to older clients as part of the Home and Community Care program in all jurisdictions, except Victoria and Western Australia; and the Australian Government's expenditure on all Home and Community Care program services in Victoria and Western Australia

Sources: ACFA (2015); SCRGSP (2015).

Extensive reforms have been implemented across the aged care sector since 2012, following the Commission's inquiry report *Caring for Older Australians* (PC 2011). These reforms are aimed at creating a more sustainable and transparent aged care system that delivers services in line with consumers' preferences. The transition towards consumer-oriented services is already occurring for home care services. Some evaluation of these changes has occurred; monitoring and evaluating the effects of this transition on both consumers and providers will continue to ensure the reforms deliver positive outcomes across the community.

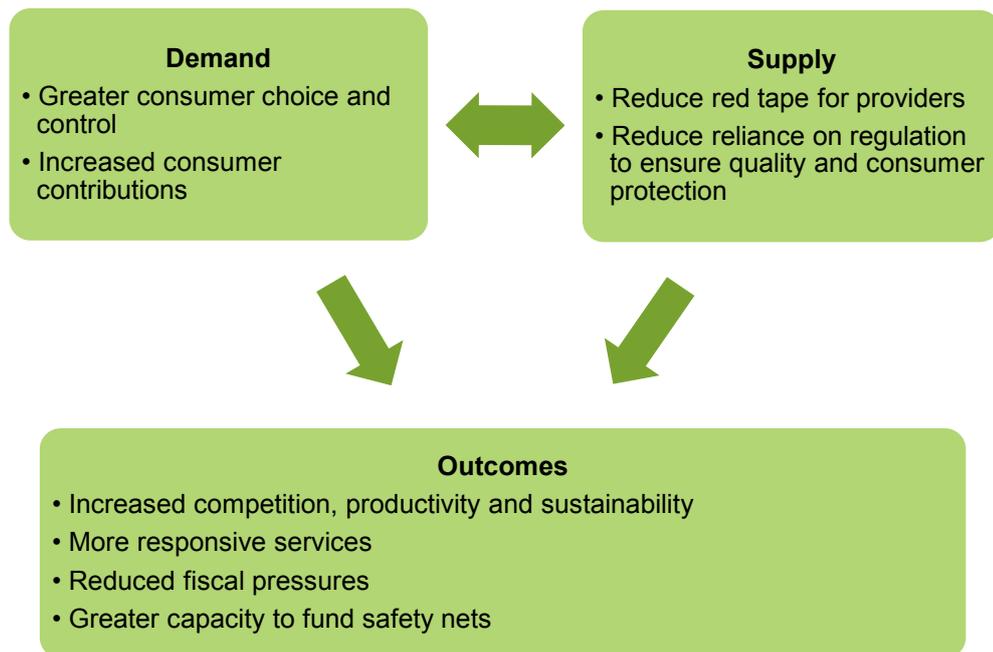
This appendix summarises the progress in implementing the recommendations contained in the Commission's 2011 inquiry. Sections B.1 and B.2 focus only on those recommendations relevant to the housing decisions of older Australians. Progress towards implementing all other recommendations is summarised in section B.3.

B.1 Recent reforms in aged care that affect housing decisions

Following the release of the *Caring for Older Australians* report, the Australian Government announced the *Living Longer Living Better* package of reforms to aged care in 2012 (further reforms were announced in 2015). Implementation commenced in 2013, and

announced reforms will continue at least until 2018. A key focus of these reforms was transitioning to a market-based system by increasing the level of consumer choice and control over services, and in turn the level of contestability in service provision, in return for greater contributions from those who can afford to pay (figure B.1, table B.2).

Figure B.1 **Aged care reform — moving to a market-based system**



Source: Adapted from CHA (2014).

Table B.2 Key changes in aged care services

Home and Community Care

Commission recommendations

- The Australian Government should be the principal funder and regulator of the Home and Community Care program (HACC). Assessment and referral to be carried out by the Australian Seniors Gateway Agency.

Progress to date

- The Commonwealth assumed full responsibility for HACC services for older people on 1 July 2012 for all states and territories except Victoria and Western Australia. These were amalgamated into the **Commonwealth Home Support Programme (CHSP)** from 2015.
- Services for older people in Victoria will transition to Commonwealth responsibility by 1 July 2016. These arrangements do not yet apply in Western Australia.
- There is a new assessment and referral arrangement through My Aged Care.
- A client contribution framework has been developed for CHSP services.

Community Aged Care Packages and Extended Aged Care at Home packages

Commission recommendations

- The Australian Government should remove restrictions on the number of community care packages.
- The Australian Government should replace current discrete home care packages with a single system of integrated and flexible care provision.
- The aged care system (including home care and residential aged care) should aim to be consumer directed.

Progress to date

- Home Care Programs amalgamated into the **Home Care Packages Program** in 2013, offering four levels of care.
- All packages are based on consumer-directed care from 2015, giving consumers greater flexibility.
- From February 2017, packages will be allocated to consumers, rather than providers. Consumers will be allocated a care budget and will choose their preferred providers, who will deliver government-subsidised services. Packages will be fully portable.
- The overall number of packages is still controlled by government. However, the number of packages available has increased.
- More comprehensive income testing for fees.

Residential aged care

Commission recommendations

- The Australian Government should:
 - remove restrictions on the number of residential bed licences;
 - remove distinction between residential high care and low care places and discontinue the extra service category;
 - allow accommodation bonds for all residential care, and give residents the choice of a periodic charge, an accommodation bond or a combination of these.
- Accommodation charges should be published by providers, and regulatory caps should be removed.
- The aged care system should aim to be consumer directed.

Progress to date

- The distinction between low care and high care has been removed.
- A new means tested fee structure has been introduced, in line with the Commission's recommendations. Regulatory caps on daily accommodation charges have been removed.
- Providers are required to publish accommodation charges in a consistent format.
- *The 'extra services' category has not been discontinued.*
- *Restrictions on bed licenses, extra services and accommodation payments are still in place.*
- *Consumer directed care has not been introduced in residential aged care.*

Sources: ACFA (2015); PC (2011).

Changes to home care services

In 2011, the Commission recommended that the Government replace the system of discrete care packages across community and residential care with a single integrated and flexible system of care entitlements. Care services would be provided to individuals according to an assessment of their need by a government-run ‘Seniors Gateway’, and individuals would be given choice of providers and the mix of services they use.

This recommendation has been partly implemented, through changes to the way home care is provided. Care at home programs were streamlined with the introduction of **Home Care Packages** in August 2013, which replaced a number of other discrete care packages, and all home care packages are, from 1 July 2015, delivered on a **Consumer Directed Care** (CDC) basis. This approach is intended to provide people with more choice and flexibility over the types of care and services they access and how those services are delivered (CHA 2014; DSS 2014a).

In line with home care packages being delivered on a CDC basis, eligible consumers will be allocated a budget based on an assessment of their relative care needs, and from 2017, providers will compete on their service offering for consumers. Once a consumer has chosen a provider, the subsidy will be paid to that provider. As funding is ‘attached’ to the consumer, from February 2017 each consumer will also be able to choose to change provider and their funding will follow. The Government will still control the overall number of home care packages available through the aged care provision ratio (see below) (ACFA 2015).

As a result, from February 2017 providers will no longer be allocated home care packages through the Aged Care Approvals Round (see below) and consumers will no longer be limited to finding a provider with a ‘vacant’ package.

Further streamlining has occurred in the delivery of entry level aged care services. In line with the Commission’s recommendation, on 1 July 2012 the Commonwealth assumed full funding, policy and operational responsibility for Home and Community Care (HACC) services for older people in all states and territories, except Victoria and Western Australia. On 1 July 2015, the Commonwealth HACC program was replaced by the **Commonwealth Home Support Programme** (CHSP). From 1 July 2016, HACC services for older Victorians will transition to Commonwealth responsibility. Negotiations on the transition of Western Australian HACC services to the Commonwealth are at an early stage.

The CHSP is one consolidated program (replacing four previous programs, including the HACC) that provides entry level home support for older people who need assistance with daily living to keep living independently at home and in their community (DSS 2015e). With its greater focus on wellness, reablement and restorative care, it goes some way to addressing the Commission’s recommendation for the introduction of an intensive reablement service aimed at enabling independence, rehabilitation and restorative care.

The assessment of eligibility for the CHSP remains separate from other aged care assessments. To be eligible for services through the CHSP, prospective clients need to undergo an assessment by the My Aged Care Regional Assessment Service (RAS), which determines their needs and refers them to the relevant service providers (DSS 2015e). The assessment of eligibility for home care packages and residential aged care is undertaken by Aged Care Assessment Teams (ACATs) (known as Aged Care Assessment Services in Victoria). ACATs generally comprise, or have access to, a range of health professionals, including geriatricians, physicians, registered nurses, social workers, physiotherapists, occupational therapists and psychologists. The ACAT team assesses the care needs of an older person, and then works closely with the client, their carer and family to identify the most suitable aged care services available to them (PC 2011).

Screening and assessment for aged care services is being integrated into a nationally consistent process, which is in the final stages of implementation. Once fully implemented, screening (undertaken by the My Aged Care contact centre staff), home support assessment (undertaken by the RAS) and comprehensive assessment (undertaken by ACATs) will all be conducted using the National Screening and Assessment Form, with the results captured in a central client record. The form has been designed so that each tier of assessment builds on information collected in previous tiers and through previous assessments.

The Government plans to introduce a **single integrated care at home program** from July 2018, following consultation with the aged care sector. This will combine the Home Care Packages and the CHSP. Consultation will begin in 2015-16 (Australian Government 2015a). Amalgamating these programs may reduce administrative complexity and costs, as well as promote continuity of care. It will, however, involve some challenges for providers as well as the Australian Government, such as developing a consistent fee policy. Currently, the Australian Government sets the maximum fees for home care packages, while fees for services under the CHSP are determined by individual providers.

Facilitating ageing in place

The Commission addressed several aspects of age-friendly housing in its recommendations. Home modifications are the only area where the Commission's recommendation — to develop a national policy approach — has been implemented. In 2012, the Australian Government assumed responsibility for home modification and maintenance services, in all jurisdictions except Victoria and Western Australia, as part of the Commonwealth HACC transition. In 2016-17, the Commonwealth will also assume responsibility for home modifications and maintenance services in Victoria.

The Commission also recommended that the Australian Government develop building standards that meet the needs of older people. Voluntary standards for accessible design existed prior to the Commission's inquiry and these continue to be available (LVA 2015); however, no new building standard has been developed.

The Commission further recommended that COAG develop a strategic policy framework to ensure an adequate supply of affordable housing to meet the needs of an ageing population. No new housing policy framework has been developed. The National Affordable Housing Agreement, which commenced in 2009, contains a number of objectives related to the supply of affordable housing, but they do not relate specifically to the needs of older people (COAG 2012).

The regulation of retirement villages remains the responsibility of state and territory governments, as per the Commission's recommendation. The Commission also recommended that governments should pursue nationally consistent retirement village legislation. No progress has been made towards implementation. However, individual jurisdictions are reviewing and reforming their regulations (chapter 4).

Easing supply restrictions

In 2011, the Commission recommended that the Government remove regulatory restrictions on the number of community care packages and residential bed licences, the regional allocation of new aged care places, and the distinction between residential high care and low care places.

The **restrictions on the number of community care packages and residential bed licences** have not been removed. However, the total number of home care packages available will increase from about 72 000 to 100 000 by 2017. An additional 40 000 packages are expected to be available over the following five-year period, bringing total places to 140 000 by 2021-22. This reflects changes in the aged care provision ratio — the ratio for home care packages will increase from 27 to 45 for every 1000 people aged over 70 by 2021-22, while the residential aged care provision ratio will decline from 86 to 80 places for every 1000 people aged over 70 (ACFA 2015). The expansion of home care packages is designed to support the preferences of older Australians to age in place. However, there are constraints on the scope of home care to substitute for residential care.

The **distinction between low care and high care in residential care** was removed from 1 July 2014. Previously this distinction was used for determining conditions for allocating residential aged care places, care recipient approvals and classifications, and accommodation payment options. Any person with a permanent residential aged care approval may now be admitted to any residential aged care place, subject to availability and the provider's agreement (DSS 2014j). Removing this distinction is intended to provide residents with better access to the level of residential care that they need at their time of entry, rather than being limited by their approval. Accordingly, accommodation payment options are now available to residents regardless of whether they require a low or high level of care (see below).

The Commission also recommended that regulatory **restrictions on supplying additional services** in all residential aged care facilities be removed, and the distinction between ordinary and extra service bed licenses be removed. While all providers can offer

additional services, extra services as a distinct regulated category continues to exist and the distinction between ordinary and extra services has not been removed. Fees for extra services are approved by the Aged Care Pricing Commissioner (DSS 2015g).

Restrictions on the regional supply of new residential aged care places have not been removed. Each year, new places are allocated through the Aged Care Approvals Round, that aims to ‘allocate places in a way that best meets the identified needs of the community’ (DSS 2014f, p. 17).

This process has three stages³³ (DSS 2014k):

5. The Minister for Social Services determines the number of new aged care places to be made available to each jurisdiction for the financial year. For example, in 2014, a total of 17 849 new aged care places (including 11 196 residential care places) were made available (DSS 2015n).
6. The Department of Social Services determines the regional distribution of places. This distribution takes into account the needs of specific groups in the population, such as people with dementia.
7. Approved providers³⁴ can apply for places through the Aged Care Approvals Round, a competitive tender process that is determined by the Department of Social Services.

In response to the Commission’s recommendations, the Government contended that a premature removal of all supply restrictions would create significant risks both for consumers and the aged care sector, which would find it difficult to adjust to a fully competitive market environment in the short to medium term, with the potential for significant financial dislocation and closure of services (Australian Government 2012). Supply restrictions are due to be reviewed in 2017 (KPMG 2013).

Greater price competition and transparency

The Commission recommended a number of changes to the way that aged care services and accommodation are priced. These were largely aimed at providing more choice for older Australians, and improving the incentives for providers to respond to the needs of older Australians.

The Commission recommended that there be **separate payment arrangements** for the major cost components of aged care — with personal care charged according to capacity to pay, and accommodation and everyday living expenses the responsibility of individuals (subject to a safety net for those of limited means). Adopting this recommendation was a

³³ As part of machinery of government changes, the responsibility for aged care programs was transferred from the Department of Social Services to the Department of Health from September 2015.

³⁴ To become approved, applicants must demonstrate their suitability to provide aged care, including their experience in the sector and their ability to meet quality standards, their record of financial management, and the suitability of key personnel (DSS 2014k).

key element of the *Living Longer Living Better* reforms — as of 1 July 2014, separate charges apply for different elements of residential care (see chapter 4). New residents entering residential aged care from July 2014 can be asked to pay:

- an accommodation payment or contribution
- a basic daily fee, of 85 per cent of the basic rate of the single Age Pension. Full pensioners with low assets would only pay this fee
- a means-tested care fee, up to a capped amount (table B.3 provides further detail).

The Commission also highlighted that accommodation charges needed to better reflect the cost of providing that accommodation and suggested that providers be required to offer people a **choice of payment type**. Residents can now opt to pay for their accommodation through either a Refundable Accommodation Deposit (RAD) — a lump-sum payment that is fully refundable upon leaving the residence, and is guaranteed by the Government; a Daily Accommodation Payment (DAP) — a periodic rental type payment; or a combination of the two (DSS 2014f). Residents are given 28 days after they enter an aged care home to decide their payment method.

To reduce distortions in payment types preferences, the amount of a RADs cannot exceed the equivalent of the relevant DAP (DSS 2014f). Providers must use a the maximum permissible interest rate set by the Government to calculate equivalence between the RAD and the DAP.

The Commission recommended that **caps on accommodation charges** be removed to reflect differing standards of accommodation. Different maximum accommodation payments can now be charged for different room types. However, providers must seek approval to charge a RAD (or equivalent DAP) of more than \$550 000 (DSS 2014f).

To help drive competition, providers are now also required to **disclose accommodation price information**. From May 2014, aged care providers are required to publish maximum prices and descriptions for accommodation payments on the Australian Government's My Aged Care website, on their own websites and in the written materials given to prospective residents. They must publish the maximum RAD payable, maximum DAP payable, and an example of a combined payment method (for example, 50 per cent payment by lump-sum RAD and 50 per cent rental-type DAP).

The Commission also suggested that the Government charge residential aged care providers a fee reflecting the cost of providing a guarantee on the lump-sum payments they receive from residents. Accommodation lump sums are a source of interest-free debt financing for service providers. The Australian Government acts as an unsecured creditor for residential care providers and, in turn, provides a guarantee to older Australians who pay a bond or RAD for their accommodation. In June 2014, the maximum contingent liability for the government amounted to \$15.6 billion (Treasury 2015b).

The Government responded that it did not support charging such a fee, but that from 1 July 2014 it would instead require providers to insure any new accommodation bonds

that are paid by residents. The Government saw this approach as more efficient and involving lower administration costs than the Commission's approach (Australian Government 2012). However, the Government announced in the 2013-14 Budget that it would defer this requirement in response to concerns raised by providers (Australian Government 2013).

Changes to means tested co-contributions

The Commission proposed a single national care co-contribution regime be introduced, which would apply across the aged care system, whether services are delivered in the community or in a residential aged care facility. The rate of the private co-contribution would be set according to a person's financial circumstances, with the amount paid varying according to the underlying price (which would reflect both the complexity and extent of care). The Commission also proposed that a person's capacity to contribute to aged care be based on an assessment of both their income and their assets — it suggested that to promote equity, the assets test should include lump sums paid for aged care accommodation and the principal residence irrespective of whether or not there are 'protected persons' living in the home.³⁵

No single national co-contribution regime was introduced, but following changes implemented in July 2014, the **residential aged care means test** now applies to a broader range of fees and includes RADs (table B.3). From 1 January 2016, the current exemption from the aged care means test of rental income from an aged care resident's former home, where that resident pays at least part of their accommodation costs by a DAP, will be removed. This will align the means test for those who pay by a RAD and DAP.

³⁵ Under current arrangements, the former principal residence is not counted as an asset if, at the time of the assets assessment or the date of entry into care (whichever is earlier): a partner or dependent child is living there; a carer eligible for an income support payment has lived there for at least two years; or a close relative who is eligible for an income support payment has lived there for at least five years.

Table B.3 Means tested fees in residential aged care

Single person, dollar amounts as at September 2015

	Assets	0 – \$46 000	\$46 001 – \$157 987.20	Over \$157 987.20
<i>Income (annual)</i>				
0 – \$25 487.80 (full pensioners)		Only Basic Daily Fee (85 per cent of the basic rate of the single Age Pension – \$47.86 per day) is payable	Basic Daily Fee + subsidised accommodation fee (up to \$53.84 a day)	Basic Daily Fee + full accommodation fee + subsidised care fee ^a (means tested fee minus the maximum Government accommodation supplement amount)
\$25 487.81 – \$64 683.32		Basic Daily Fee + subsidised accommodation fee (up to \$53.84 a day)	Basic Daily Fee + either subsidised accommodation fee (up to \$53.84 a day) or full accommodation fee + subsidised care fee ^a , depending on the amount of assets and income	Basic Daily Fee + full accommodation fee + subsidised care fee ^a
Over \$64 683.32		Basic Daily Fee + full accommodation fee + subsidised care fee ^a	Basic Daily Fee + full accommodation fee + subsidised care fee ^a	Basic Daily Fee + full accommodation fee + subsidised care fee ^a

^a Annual and lifetime caps apply to care fees paid by residents. In September 2015, these were \$25 731.05 and \$61 754.55, respectively (DSS 2015o).

Source: DSS (2015o).

The assets test continues to include part of the value of a person’s former home (principal residence), up to a capped value of about \$158 000. However, exemptions remain for ‘protected persons’ such as spouses and close relatives or others who are caring for the care recipient and are in receipt of an income support payment (DSS 2015h) and no government-backed credit scheme was introduced.

The **income test for Home Care Packages** was changed in July 2014 and remains different to that applied for residential care as assets are exempt. Recipients of home care packages with incomes greater than about \$25 000 (or about \$38 000 for couples) are required to make a co-contribution to their costs of care in addition to the basic fee (table B.4).

Table B.4 Income tested fees for Home Care Packages

Single person dollar amounts as at September 2015

<i>Income</i>	<i>Maximum fee</i>
0 – \$25 487.80	Basic daily fee (17.5 per cent of pension)
\$25 487.81 – \$35 780.21	Basic daily fee + 50 per cent of income above \$25 487.80 (up to \$5 146.20 a year)
\$35 780.22 – \$49 296.00	Basic daily fee + \$5 146.20 a year
\$49 296.01 – \$59 588.41	Basic daily fee + \$5 146.20 a year + 50 per cent of income above \$49 296.00
Over \$59 588.41	Basic daily fee + \$10 292.41 a year

Source: DSS (2015o).

Consistent with the Commission’s recommendation to set a lifetime **stop-loss limit** on care recipients’ co-contributions, an annual cap (currently about \$26 000 for residential care and either \$5000 or \$10 000 for home care) and lifetime cap (about \$62 000 for both) now apply to means-tested care fees (DSS 2014h). The levels of the caps are in line with indicative limits proposed by the Commission.

Providing better information and making the system easier to navigate

Accommodation price disclosure requirements have been complemented by other measures to increase consumer access to information and make the system easier to navigate. This was in response to the Commission’s recommendation that the Government establish an Australian Seniors Gateway Agency to provide information, needs assessment, assessment of capacity to pay, care coordination and carer referral services.

The Australian Government introduced an Aged Care Gateway on 1 July 2013, consisting of the My Aged Care website and phone support service to provide access to information and services for seniors and their carers. The Government is aiming to eventually expand the Gateway to cover registration, screening and assessment, and some of these functions have been introduced in 2015 (DSS 2015j). For now, the means test continues to be applied by the Department of Human Services, not the Gateway. It is also intended that quality indicators for providers will be published on the My Aged Care website.

B.2 Impacts of reforms

Most of the changes discussed above have only been implemented recently. Therefore, it would be premature to ascertain with confidence the likely longer-term effects of reforms on competition between providers and the housing choices of older Australians. The reforms should, in principle, improve outcomes for older Australians and the broader community, and early reports have shown some positive indications.

The Aged Care Financing Authority (ACFA) has been tasked with monitoring the impact of the accommodation payment arrangement reforms. It has published a number of reports examining the progress of reform, as well as related issues such as the factors affecting the financial performance of aged care providers, access to care for supported residents and improving the collection of financial data from providers. The collection of data as part of the aged care reforms may also provide better information on the extent of unmet demand for aged care.

Prior to the introduction of reforms, aged care providers expressed concerns that reforms to payment arrangements would result in a shift away from lump-sum payments towards periodic payments, presenting challenges for those that rely on up-front capital to build new stock. ACFA has not found this to be the case. ACFA's survey data show that lump-sum payments held by providers have increased in all geographical areas, and that consumers prefer lump-sum payments. The complex financial arrangements around residential aged care may be supporting a preference for lump sums, which are seen as a simpler option compared with daily payments (chapter 4). Ongoing monitoring and analysis of changing lump-sum balances by ACFA will provide further insight into the impact of the new accommodation payment arrangements on providers.

In its 2015 report on the aged care sector, ACFA also found that:

- the overall financial viability of the sector has improved, with more efficient and profitable providers exhibiting the strongest growth. Profitability is underpinned by strong governance processes and financial management. Providers with a strong market focus, which updated and refurbished their facilities in response to residents' expectations, reported better financial performance
- average occupancy rates for home care packages and residential aged care have been fairly stable at about 88 and 93 per cent respectively. The share of high care residents in residential aged care facilities is increasing, and their average age is also increasing. For home care packages, there has been relatively low take up of level 1 packages (vacancy rates are about 50 per cent), while demand for level 2 and 3 packages has been growing. The take up of level 4 packages has remained stable
- the introduction of CDC into home care has increased costs for providers that need to adjust, build capability and implement new systems. To date, there has been reduced profitability among some home care providers as they adapt to CDC requirements. However, there is likely to be a significant transitional factor in these impacts
- income-tested fees for home care are expected to result in an increase in the costs of home care packages paid by consumers. Currently, consumer fees represent only 7 per cent of providers' income — the balance is made up of government subsidies
- there has been a significant increase in investment activity in the residential care sector, encouraged by accommodation payment reforms and the higher Government accommodation supplement. A total of \$1.5 billion of new work was completed in 2013-14 — an increase of 69 per cent on the previous year (ACFA 2015).

Beyond ACFA's work, the Department of Social Services has conducted separate evaluations on components of the aged care system.

- In 2014, an evaluation of the home modifications and maintenance services provided through HACC found a lack of consistency in service models and delivery, as well as shortages of suitably trained professionals such as occupational therapists and builders (KPMG 2014). Some of these concerns may be addressed with the introduction of national screening and assessment processes as part of the CHSP (chapter 4).
- Also in 2014, the Department of Social Services commissioned an evaluation of the implementation of the Home Care Packages program, including the effects of CDC (DSS 2015f). The evaluation found that reform implementation was generally progressing well, although it has created substantial administrative burden for operators, who felt they needed more information and support (KPMG 2015).

In addition to these evaluations, the Aged Care Sector Committee is expected to report to Government by December 2015 on an Aged Care Roadmap, which will investigate and prioritise what more needs to be done to move to a more sustainable, consumer led aged care market supported by regulation that is fit for purpose (Senate Community Affairs Committee nd). In 2016-17, there will be a review of the reform package announced in 2012.

B.3 Progress of other aged care reforms

Funding

Commission recommendations

- Charge residential providers a fee for the Government guarantee on accommodation deposits.
- Set the supported resident ratio on a regional basis, and introduce a sliding scale of penalties for not meeting this requirement, abolishing the fixed discount at the 40 per cent threshold.
- Appropriate subsidy levels for accommodation of supported residents, based on building standards.
- To assist older Australians to pay for care and support, the Government should introduce:
 - an Australian Age Pensioners Savings Account, to be exempt from means testing
 - a government-backed Australian Aged Care Home Credit Scheme.

Progress to date

- *The Government announced in the 2013-14 Budget that it would defer the requirement to insure new accommodation deposits in response to concerns raised by providers. Review of arrangements will occur in 2016-17 as part of the review of aged care reforms.*
- Supported resident ratios are under review by the Aged Care Financing Authority (ACFA).
- The accommodation supplement has been increased, with a higher supplement for newly built or refurbished facilities.
- *The Government did not support the recommendations to introduce the Australian Age Pensioners Savings Account and the Australian Aged Care Home Credit Scheme. A pilot program similar to the suggested savings account was announced in the 2013-14 Budget, but was cancelled.*

Care and support

Commission recommendations

- An intensive reablement service should be introduced.
- Federal, state and territory governments should promote expanded access to in-reach health care services and multi-disciplinary health care teams in residential aged care facilities.
- The Australian Government should set cost-reflective scheduled fees and rebates for the delivery of health care services to people in residential aged care or home care.
- The Australian Government should ensure that providers receive appropriate payments for palliative and end-of-life care, and have staff trained to discuss and put in place advance care directives.
- People supported by the disability care system prior to reaching the age threshold should continue to be supported through the disability care system, but be able to elect to be supported through the aged care system at any time.

Progress to date

- The Commonwealth Home Support Programme (CHSP) places a strong emphasis on reablement services. In addition, restorative care places will be incorporated into the aged care planning ratio from 1 July 2016.
- The 'Better Health Care Connections' programs provide funding to expand access to in-reach health care services.
- *There have been no changes to the determination of scheduled fees and Medicare rebates.*
- Palliative and end-of-life care funding is available under the Aged Care Funding Instrument. The National Disability Insurance Scheme allows people to choose if and when they want to change to the aged care system after the age of 65.

Quality framework

Commission recommendations

- The quality assurance framework for aged care should be expanded to include published quality indicators at the service provider level, and a Quality and Outcomes Data Set should be published to bring together evidence on best practice care.
- Results of community care quality assessments should be published.

Progress to date

- Development of a new quality framework is in progress.
- The responsibility for quality assessments has been transferred to the Australian Aged Care Quality Agency, which is expected to publish assessment reports for community care.

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Regulatory institutions

Commission recommendations

- Establish an independent Australian Aged Care Commission with responsibility for all regulatory matters, pricing and subsidies in aged care.
- Complaints should be determined by the Australian Aged Care Commission's Commissioner for Complaints and Reviews. The Gateway Agency should also have a separate office to handle complaints about its decisions. The Office of the Aged Care Commissioner should be abolished.
- A broad range of enforcement tools should be available to ensure that penalties are proportional to severity of non-compliance.
- All governments should agree to allow the Australian Government to become the principal funder and regulator of home care.
- Introduce a streamlined reporting mechanism for all aged care service providers (both community and residential care) based on the model used to develop Standard Business Reporting.
- Require residential aged care providers to disclose whether they have met all prudential regulations.
- Amend the missing resident reporting requirements to allow a longer period for providers to report missing residents.
- COAG should identify and remove onerous, duplicate and inconsistent regulations.
- To support policy research and evaluation, a national 'clearinghouse' for aged care data should be established, and the collection and reporting of data should be reformed.

Progress to date

- *The Government did not support the regulatory structure recommended by the Commission.*
- Other changes have been made to the regulatory structure, including the establishment of the Aged Care Quality Agency, the Aged Care Pricing Commissioner and ACFA.
- Responsibility for the Aged Care Complaints Scheme will be transferred to the Aged Care Commissioner from 1 January 2016.
- Commonwealth arrangements for Home and Community Care (now CHSP) do not yet apply to Western Australia. Negotiations to transfer responsibilities will commence in 2016-17.
- Some streamlining has occurred in financial reporting. The development of quality reporting mechanisms still in progress.
- Prudential standards require annual financial information be disclosed on request. *The Government did not support changing the missing resident reporting requirements.*
- The Aged Care Sector Committee has developed a Red Tape Reduction Action Plan, and some duplicative regulations have been repealed.
- The Australian Institute of Health and Welfare operates the national aged care data clearinghouse. Reforms to data collection and reporting in relation to financial reporting and CHSP activity reporting are underway.

Catering for diversity

Commission recommendations

- Ensure that accreditation standards are sufficient to deliver services which cater to the needs and rights of people from diverse backgrounds.
- The Australian Seniors Gateway Agency should ensure that people from diverse backgrounds, including those with limited English skills, have access to culturally appropriate information and assessment services.
- Scheduled prices for care services should take into account costs associated with catering for diversity.
- Rural and remote and Indigenous aged care services should be actively supported before remedial intervention is required.
- The Australian Government should partly or fully block fund services where there is a demonstrated need to do so based on specific service needs.

Progress to date

- National Ageing and Aged Care strategies have been developed for people from culturally and linguistically diverse backgrounds and LGBTI people, and funding allocated for training.
- A range of services, such as advocacy, have been designed specifically for people from diverse backgrounds.
- The National Aboriginal Torres Strait Islander Flexible Aged Care program has been expanded. The Remote and Aboriginal and Torres Strait Islander Aged Care Service Development Assistance Panel was established in 2011, offering professional support services to eligible aged care providers.
- ACFA is undertaking a study into issues affecting the financial performance of rural and remote providers.

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Carers and volunteers

Commission recommendations

- When assessing the care needs of older people, the Australian Seniors Gateway Agency should also assess the capacity of informal carers to provide ongoing support and approve entitlements where appropriate.
- Carer Support Centres should be developed to undertake a comprehensive and consistent assessment of carer needs, including training, respite, counselling and advocacy.
- Funding for services that engage volunteers should take into account the costs associated with administration, regulation, training and support.
- The Australian Government should implement an independent statutory Community Visitors Program for residential aged care facilities.
- A trial of more flexible arrangements for respite care should be conducted.

Progress to date

- A national gateway for carers is currently being developed.
- Carers can access a range of support services through the Commonwealth Respite and Carelink Centre and other programs. The assessment process for aged care services also examines carers' needs.
- *The Government stated it will consider funding issues relating to volunteers as part of funding priorities under the Commonwealth Home Support Programme and aged care subsidies. However, specific funding arrangements for volunteers are yet to be implemented.*
- *The Community Visitors Program was not implemented, as the Government did not support this recommendation. The existing Community Visitors Scheme has been expanded, to include visits to aged care residents.*
- Delivery of flexible planned respite care and carer services previously offered under HACC are now streamlined under the CHSP.

Aged care workforce

Commission recommendations

- Scheduled care prices should take into account the need to pay fair and competitive wages to care staff.
- The Australian Government should:
 - expand accredited courses to provide aged care workers with the skills they need
 - fund the expansion of 'teaching aged care services'
 - undertake an independent and comprehensive review of aged care-related vocational education and training (VET) courses and their delivery by registered training organisations (RTOs).

Progress to date

- In the 2015-16 Budget, the Australian Government redirected more than \$220 million over four years to 2018-19 to establish the new Aged Care Workforce Development Fund.
- In July 2013, the Australian Government announced additional funding through the Aged Care Workforce Supplement to improve the aged care sector's capacity to attract and retain skilled employees. In 2014, the Government redirected \$1.5 billion over five years from the Workforce Supplement into other subsidies for aged care providers.
- The Department of Health will undertake a stocktake and analysis of Commonwealth-funded aged care workforce initiatives.
- The teaching and research aged care services program provided funding to help establish a number of models. A trial and evaluation was conducted over 2012–2015. The Department is considering its findings.
- A review of aged care RTOs was conducted by the Australian Skills and Quality Authority in 2012-13 and made a number of recommendations for improvement.

C The Commission survey

The Commission engaged RFI Group to conduct a national survey of older Australians on issues pertinent to this study. The survey sought the views of older Australians on issues such as: planning for retirement; housing preferences and downsizing; savings, debt and bequests; and home equity release products.

Results from this survey have been used throughout this report, and full results are available online.

C.1 Rationale for undertaking the survey

In the course of this study, the Commission identified a paucity of recent data on the behavioural drivers of specific decisions relevant to the study. There were some existing surveys on the attitudes of older Australians on releasing equity from the home and reverse mortgage products. However, these tended to be either outdated (having occurred prior to significant changes in the market and in the policy and regulatory environment) or based on very small sample sizes.

More broadly, previous surveys often tended to focus on a particular aspect of housing decisions (either the accommodation dimension, or the investment and financial dimension), rather than providing a comprehensive review.

The Commission engaged RFI Group to conduct a survey that addressed this gap in the evidence.

C.2 Survey design and conduct

The survey questionnaire covered older people's attitudes and views on a range of issues, including:

- planning for retirement
- attitudes towards the family home, debt, and bequests
- downsizing
- housing preferences
- awareness of, and attitudes towards, home equity release products.

The survey was conducted online in September 2015, and involved 1524 Australians aged 60 years and over. The survey questionnaire was designed to take about 20–25 minutes to complete. RFI Group administered the survey, analysed the data received, and presented the findings and full results to the Commission.

C.3 Sampling and representation

This sample was chosen to be representative of the Australian population in terms of age, gender, state and area (regional, rural and metropolitan), with the exception that the number of people surveyed aged 80 years and over was set at a minimum of 100. To achieve this stratification of the sample, quotas were applied to completed responses (rather than to the initial selection) for age (representative for 60–69 and 70–79 cohorts, minimum of 100 for 80+ cohort), gender, state and area.

Some areas of potential sampling bias in the survey were identified:

- under-representation of people aged 80 years and over
- under-representation of people living in non-private dwellings, such as residential aged care
- under-representation of people from lower socioeconomic backgrounds (due to the online survey methodology, which could omit people without internet access or know-how)
- under-representation of people from very high socioeconomic backgrounds (who might not view the compensation for their time as sufficient to induce them to participate in the survey)
- over-representation of people with a higher level of financial literacy
- under-representation of people from language backgrounds other than English, or with low levels of English literacy (the survey was undertaken in English only).

A brief analysis of the extent of sampling bias in the survey is presented below.

Age and non-private dwelling representation

The Commission survey under-represented Australians aged 80 years and over (table C.1). This group accounted for about 19 per cent of the Australian population aged 60 years and over as at June 2014, but made up only 6.6 per cent of survey participants. This under-sampling was anticipated and seen as inevitable, due to the large proportion of this age group who are in non-private dwellings and are typically out of reach for surveys of this type. However, the requirement to survey at least 100 responses from people in this age group was considered sufficient for at least some high-level analysis.

Table C.1 Representation of people aged 80 years and over
Proportion of each age group within the population aged 60 years and over

Age group	Commission survey	ABS Demographic Statistics
	Per cent	Per cent
60–64	30.7	26.8
65–69	28.2	23.7
70–74	20.7	17.4
75–79	13.7	13.0
80+	6.6	19.2
Total	100.0	100.0

Sources: Productivity Commission estimates based on ABS (*Australian Demographic Statistics, December 2014*, Cat. no. 3101.0) and Commission survey.

Related to this under-sampling of people aged 80 years and over, the survey under-represented people living in non-private dwellings (table C.2). About 7 per cent of Australians aged 60 years and over were living in non-private dwellings as at the 2011 Census, compared to only 0.9 per cent (14 people) of respondents to the survey. This is a difficult cohort to survey; for example, the ABS *Survey of Income and Housing* does not cover people in non-private dwellings. Although a shortcoming, this was not a barrier to examining most of the decisions of interest to this study, which are made by people in private dwellings.

Table C.2 Representation of people living in non-private dwellings
Proportion of each age group living in non-private dwellings

Age group	Commission survey	Census
	Per cent	Per cent
60–64	0.2	3.1
65–69	0.5	3.3
70–74	1.3	4.0
75–79	1.4	5.9
80+	4.0	19.0
All people aged 60 years and over	0.9	6.8

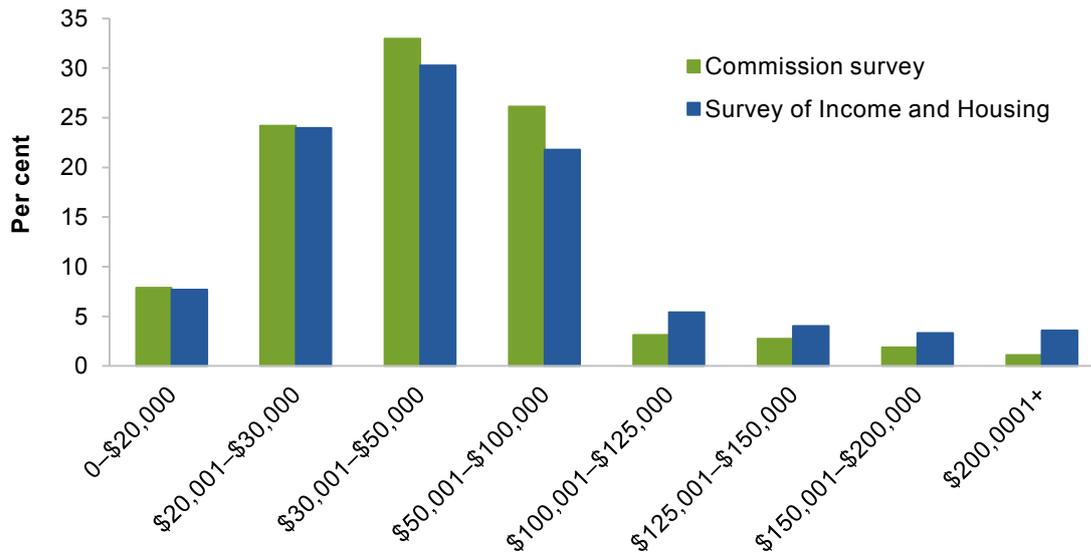
Sources: Productivity Commission estimates based on ABS (*2011 TableBuilder Basic*, Cat. no. 2072.0) and Commission survey.

Socioeconomic representation

The Commission survey slightly over-represented people in middle-income groups and under-represented those in higher income groups (figure C.1). It also appears to have

over-represented people in the lower wealth brackets, and consequently, under-represented those in the highest wealth brackets (figure C.2).

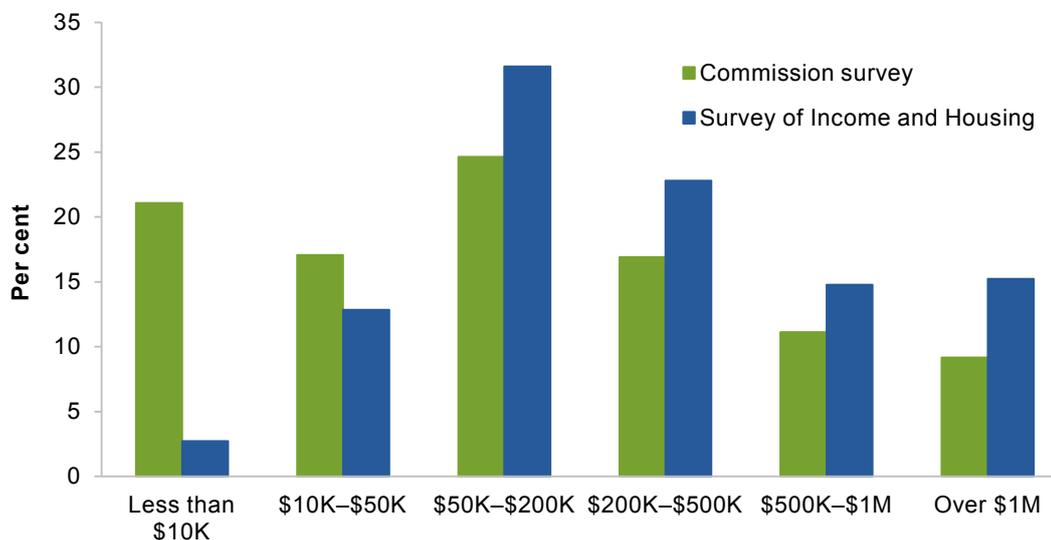
Figure C.1 Representation of household income groups^{a,b}
 Proportion of each income bracket within the population aged 60 years and over



^a Income figures from the 2011-12 *Survey of Income and Housing* adjusted to 2014-15 dollars using the GDP implicit price deflator for household final consumption expenditure. ^b Age of household refers to age of household reference person.

Sources: Productivity Commission estimates based on ABS (*National Income, Expenditure and Product*, Cat. no. 5206.0; *Survey of Income and Housing, Australia, 2011-12 Basic CURF*, Cat. no. 6541.0.30.001) and Commission survey.

Figure C.2 Representation of household wealth groups^{a,b}
 Proportion of each wealth bracket within the population aged 60 years and over



^a Total value of household assets, excluding the home asset. Wealth figures from the 2011-12 Survey of Income and Housing adjusted to 2014-15 dollars using the GDP implicit price deflator for household final consumption expenditure. ^b Age of household refers to age of household reference person.

Sources: Productivity Commission estimates based on ABS (*National Income, Expenditure and Product*, Cat. no. 5206.0; *Survey of Income and Housing, Australia, 2011-12 Basic CURF*, Cat. no. 6541.0.30.001) and Commission survey.

However, caution should be exercised in comparing self-reported income and wealth, as any discrepancies may reflect methodological differences. For example, the Commission survey asked people to select one of several preset income and wealth brackets, and allowed them the option of ‘Rather not say’ (for income) and ‘Not sure’ (for wealth), whereas the *Survey of Income and Housing* asked for specific dollar values for sub-categories of income and wealth.

Receipt of the age pension may be a more objective indicator of a person’s income and wealth than self-reported income and assets. On this basis, the Commission survey does not appear to have substantial socioeconomic bias. Just over 75 per cent of survey respondents aged 65 years and over were receiving either a full or part age pension (Commission survey), compared with about 70 per cent of the Australian population aged 65 years and over (chapter 5). Further, some key characteristics of pension recipients in the Commission survey — the proportions of full and part pensioners, and the extent of home ownership — are broadly comparable with those of pension recipients in the Australian population (table C.3).

Table C.3 Representation of Age Pension recipients

Characteristics of Age Pension recipients

<i>Characteristic</i>	<i>Commission survey</i>	<i>Department of Social Services (as at June 2013)</i>
	Per cent	Per cent
<i>Home ownership</i>		
Home owner	78.0	75.1
Non-home owner	22.0	24.9
<i>Payment status</i>		
Part pension	42.0	40.8
Full pension	58.0	59.2

Sources: Commission survey; DSS (2014e).

D Quantitative analyses

This appendix describes two strands of quantitative work undertaken in the course of the Commission's research. The first involved modifying the means test for the Age Pension to incorporate some value of the principal residence. The second related to an illustrative Monte Carlo simulation exercise, which examined the scope for improving the living standards of older Australians through accessing the equity in the principal residence.

D.1 Age Pension means test

As discussed in chapter 5, the Age Pension means test comprises an income test and an asset test. This means test was replicated and applied to the sample of older Australians in wave 10 of the Household, Income and Labour Dynamics in Australia (HILDA) database. (Wave 10 of HILDA, with data values pertaining to 2010, was chosen for this analysis, because it is the most recent available HILDA release that includes the wealth module, and hence, incorporates detailed information on assets.)

The means test constructed by the Commission did not deem income from those financial assets that are subject to deeming rules under the current Age Pension means test. Instead, the actual income received from financial and other assets that would be subject to deeming was directly assessed under the income test. There is insufficient disaggregation in the HILDA income data to enable a proper application of deeming.

There were some other complexities of assessment arrangements that were not captured by the test constructed by the Commission. While the test distinguished between singles and couples, it did not distinguish between 'regular' couples, and couples separated by illness, the latter of whom, for example, can have greater assets before the part pension phases out (DHS 2015b). In wave 10 of HILDA, only 11 Age Pension recipients were married with a spouse living in an institution.³⁶ The transitional rate of pension applies to people who would have received a lower pension payment due to changes to the Age Pension income test in 2009. The Commission did not model transitional rate pensions. In addition, the Work Bonus operated from 20 September 2009 to 30 June 2011, under which only 50 per cent of the first \$500 of employment income earned in a fortnight was assessed under the income test (DSS 2013b). Due to the inability in HILDA to determine the week in which employment income was earned, the Commission has not incorporated the Work Bonus in its means test.

³⁶ In HILDA, the definition of institutions is general and, therefore, extends beyond residential aged care homes to other institutions, such as gaols.

The replication of the Age Pension means test allowed the derivation of an imputed Age Pension income variable for people whose income and assets made them eligible to receive the Age Pension.

Having recreated and applied the existing Age Pension means test to the HILDA sample, the test was modified to incorporate a range of threshold values of the principal residence, leaving all other elements of the assets test (and income test) unchanged. Under the new test, home equity values beyond the specified threshold were counted as an assessable asset, and the resulting effect on the share of the age-eligible population on the Age Pension was calculated (table D.1).

Table D.1 Impact of changing the assets test on Age Pension eligibility
Proportion of population of Age Pension age, 2010

	<i>Threshold beyond which principal residence is included in the assets test</i>						Current treatment
	Fully included	\$440 000 (median)^a	\$500 000	\$750 000	\$1 000 000	\$1 250 000	
Proportion on Age Pension	62.3	70.8	71.4	72.5	72.8	73.1	73.3
Impact on proportion eligible for Age Pension	-11.0	-2.5	-1.9	-0.8	-0.5	-0.2	0.0
Proportion whose Age Pension is reduced	45.9	10.6	7.5	3.0	0.9	0.4	0.0

^a Median Australian house price in 2009-10, from ABS (*Housing Occupancy and Costs, 2011-12, Cat. no. 4130.0*).

Source: Productivity Commission estimates based on HILDA release 13.1, wave 10.

The use of wave 10 of HILDA meant that the income and asset data used in constructing the modified assets test correspond to dollar values in 2010. An alternative to using 2010 dollar values for income and assets would be to uprate the value of income and assets to 2015. The Commission did not use this approach because it is problematic in a context in which the age of individuals is an important variable of interest. To achieve consistency in the treatment of variables, if the level of income and assets were uprated, ideally age should have been adjusted as well.

However, the age of all individuals in HILDA could not simply be uprated by five years and left without further modification. Some of the older Australians in the sample may have died since 2010, and so any uprating exercise is made difficult by the likely mortality characteristics of the sample. Further, additional individuals would have become eligible for the Age Pension in that time, adding to the complexity of changes in the sample which would occur as time progressed. To avoid these complications, all of which raise their own methodological issues, 2010 dollar values were used in the analysis.

D.2 Monte Carlo simulation

Upon reaching retirement age, the sources of income available to individuals typically diminish, as people retire from paid work altogether, or reduce their hours of paid work. Some Australians of retirement age might however, wish to maintain lifestyles requiring levels of expenditure greater than the level of income often accessible to them at that stage of their lives. One potential source of income is drawing on home equity. A Monte Carlo exercise has been used to investigate the effect of borrowing against home equity to boost living standards in the context of an uncertain lifespan.

The Australian Government Actuarial Life Tables for 2010–12 were used for information on the frequency of death at particular ages, which corresponded to the ages of home owner pensioners (and their partners) in the 2010 HILDA database (wave 10). The data on the frequency of deaths was used to construct a life expectancy distribution for each age. This included an expected age of death (mean), as well as the average numbers of years around which a person's expected age of death may vary (standard deviation). In doing so, it was assumed that the distributions were normal, and the validity of this assumption was checked by computing Jarque-Bera test statistics.

The life expectancy distributions were used, along with a person's age and sex, to generate 1000 random ages at which a person might die. Although the age to which an individual can expect to live may be influenced by income and wealth, those influences were not built into the ages of death used in this exercise. The 1000 ages of death permitted the calculation of 1000 sets of years of life remaining, obtained by subtracting each random age of death from a person's current age. This information was used to determine the borrowing requirement against the principal residence, as well as the value of equity remaining in the principal residence at the end of the household's life.

The Association of Superannuation Funds of Australia (ASFA) publishes quarterly retirement standard benchmarks, which estimate 'modest' and 'comfortable' retirement lifestyle standards (table D.2). Both benchmarks assume that retirees own their own homes and are relatively healthy.³⁷ The modest standard is considered to offer a slightly better retirement living standard than the Age Pension, but nevertheless only gives the opportunity to afford basic activities. The comfortable standard, by contrast, provides scope for the enjoyment of a range of leisure and recreational goods and services.

³⁷ These benchmarks are used as indicative only; the Commission has not independently reviewed ASFA's benchmarks or formed a view on retirement income adequacy.

Table D.2 Age Pension payment rates and ASFA standards

September quarter 2010

	<i>Maximum Age Pension (single)</i>	<i>Maximum Age Pension (couple combined)</i>	<i>ASFA 'modest' standard (single)</i>	<i>ASFA 'modest' standard (couple)</i>	<i>ASFA 'comfortable' standard (single)</i>	<i>ASFA 'comfortable' standard (couple)</i>
Total yearly amount (\$)	18 619	28 070	21 132	30 557	39 302	53 729
Per cent of Age Pension	na	na	114	109	211	191

Sources: DSS (2015b); SeniorAu (2011).

It was assumed that people borrowed against their home equity to bridge the difference between their total yearly disposable income and the standards estimated by ASFA. Disposable income incorporated all government transfer payments, including the Age Pension.

Extra income obtained from accessing home equity is not treated as income under the income test for the Age Pension (DSS 2013a). However, the means test may apply if the proceeds are spent in a particular way (table D.3). Hence, on the basis of the Social Security rules, amounts borrowed by households in the simulations were assumed to leave Age Pension income unchanged.

Table D.3 Equity withdrawal and Age Pension treatment

<i>Use of loan proceeds</i>	<i>Income test</i>	<i>Assets test</i>
Purchase of non-financial assets (e.g. vehicle)	Not assessed	Assessable
Invested in financial instrument	Deeming rules apply	Assessable
Purchase of consumer goods and financing living expenses	Not assessed	Not assessed

Sources: David (2014); Davies (2007); Treasury (2005).

Given that there were 1000 randomly drawn ages at which a person might die, the simulation exercise yielded 1000 different borrowing requirements, and hence, 1000 different end-of-life values of home equity. The amount borrowed was assumed to grow at an annual rate of 2.5 per cent, equal to the medium-term inflation target, and hence, allowed the 'income top up' to maintain its real expected value. The interest rate on borrowing was set at 7 per cent per annum.

To determine the value of home equity at the end of life, it was necessary to apply a rate of house price growth. The simulation assumes annual house price growth of 3.5 per cent for all households, regardless of geographic location.

The simulation exercises were divided into a group for singles and a group for couples, as they are paid different rates of pension and have different ASFA standards.

Singles

Among single recipients of the Age Pension in the HILDA database, average home equity was roughly \$380 000, and the median equity was \$350 000. There were a total of 439 Age Pension recipients in this group (table D.4).

Table D.4 Home equity characteristics of age pensioners^a

	<i>Minimum reported equity^b</i>	<i>Median equity</i>	<i>Mean equity</i>	<i>Number of households</i>
Single Age Pension households	1 500	350 000	379 339	439
Couple Age Pension households	5 000	402 174	462 729	453

^a Includes only those Age Pension recipients who were reported as home owners. ^b Excludes three single and three couple households, who each reported a home equity value of zero.

Source: Productivity Commission estimates based on HILDA release 13.1, wave 10.

The simulation involves the pensioner borrowing (by reducing home equity) an ‘income top up’ to reach the relevant ASFA standard. A total of 226 households (51.5 per cent of all single home owner Age Pension households) needed to borrow to reach the ‘modest’ retirement standard. In doing so, the vast majority of people in the sample (more than 90 per cent) could use their home equity to reach and maintain the income necessary for a modest retirement standard over the rest of their lives without going into negative equity. When the benchmark level of income was the ASFA comfortable standard, 345 households (78.6 per cent of all single home owner Age Pension recipients) needed to borrow to reach the standard. The majority of those borrowing retained positive equity in their homes at the end of life (table D.5; figure D.1).

Table D.5 Single home equity borrowing^a

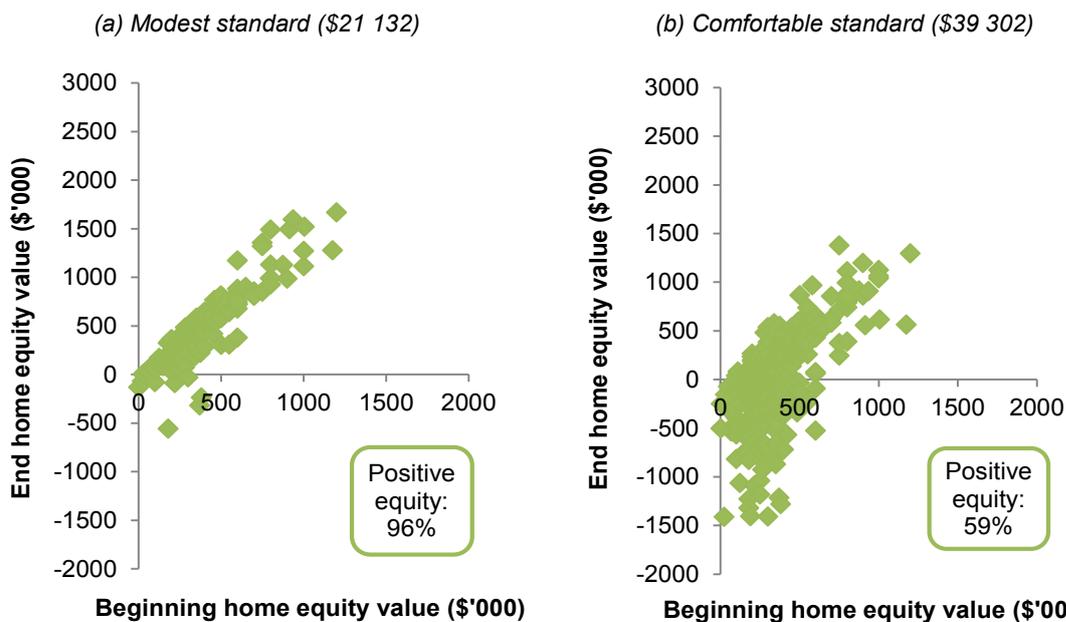
Home equity at end of life

	Negative equity		\$0 — \$249 999		\$250 000 — \$499 999		\$500 000 — \$749 999		\$750 000 — \$999 999		\$1 million and over	
	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%
Modest standard	8	3.5	43	19.0	99	43.8	45	19.9	18	8.0	13	5.8
Comfortable standard	142	41.2	97	28.1	53	15.4	33	9.6	13	3.8	7	2.0

^a Results correspond to averages over 1000 simulations.

Source: Productivity Commission estimates based on HILDA release 13.1, wave 10.

Figure D.1 Distribution of changes in home equity — singles^{a,b}



^a Beginning home equity values correspond to 2010. ^b End home equity values are the average over 1000 simulations.

Source: Productivity Commission estimates based on HILDA release 13.1, wave 10.

Couples

In the simulation for couples, there were a total of 333 households, where both members of the couple received the Age Pension, and 120 households where only one member of the couple was an Age Pension recipient — a total of 453 households. As with the simulation for singles, it was assumed that couples borrowed an annual amount to bridge the gap between their total disposable income and the ASFA modest and comfortable standards.

Given that members of a couple have different life expectancies and live to different ages, it was necessary to make assumptions on when borrowing ceased. For simplicity, the analysis assumed that the household ceased borrowing against the equity in the principal residence once the first member of the couple died. Extending the structure of the simulations to consider other possibilities is very complex, and is an opportunity for further research.

In contrast to singles, fewer couples have to borrow to reach the ASFA modest standard — a total of 146 households (or 32.2 per cent of all couple home owner Age Pension recipients). The most marked contrast occurs in relation to borrowing to reach the comfortable standard of retirement, where a similar proportion of couple households borrow as single households (346 households, or 76.4 per cent of all couple home owner households), but a larger proportion retain positive equity upon the death of the first member of the couple (table D.6; figure D.2).

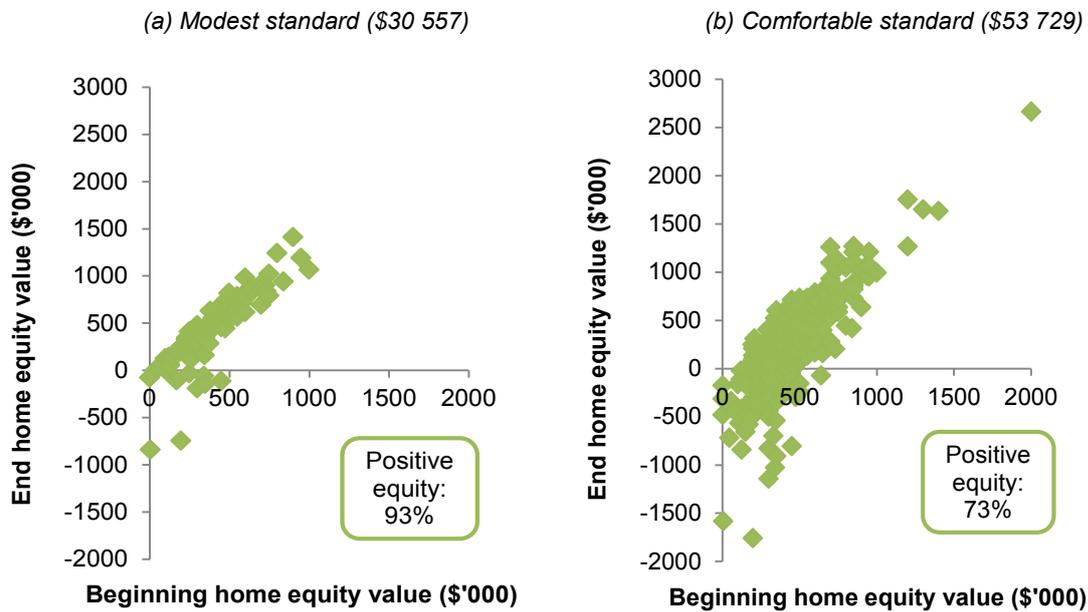
Table D.6 Couple home equity borrowing^a
Home equity at end of life

	<i>Negative equity</i>		<i>\$0 — \$249 999</i>		<i>\$250 000 — \$499 999</i>		<i>\$500 000 — \$749 999</i>		<i>\$750 000 — \$999 999</i>		<i>\$1 million and over</i>	
	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%
Modest standard	10	6.8	24	16.4	55	37.7	37	25.3	15	10.3	5	3.4
Comfortable standard	95	27.5	94	27.2	73	21.1	45	13.0	20	5.8	19	5.5

^a Results correspond to averages over 1000 simulations.

Source: Productivity Commission estimates based on HILDA release 13.1, wave 10.

Figure D.2 Distribution of changes in home equity — couples^{a,b}



^a Beginning home equity values correspond to 2010. ^b End home equity values are the average over 1000 simulations.

Source: Productivity Commission estimates based on HILDA release 13.1, wave 10.

Sensitivity analysis

The results obtained above are partly dependent on the assumptions made in the simulation. The effects of changing the interest rate, the rate of growth of the ‘income top up’, and house price growth, were all explored.

Changes to the interest rate

A higher interest rate represents a higher cost of borrowing for those drawing down on home equity, and therefore a lower balance of home equity at the end of life. This is reflected in the analysis, which shows that an interest rate of 10 per cent per annum would lead to a lower share of households retaining positive equity at the end of the life of the household (tables D.7 and D.8). Conversely, setting a lower interest rate (5.25 per cent per annum) results in more households having positive home equity at the end of life (tables D.9 and D.10).

Table D.7 Single home equity borrowing with a 10 per cent interest rate^a

Home equity at end of life

	<i>Negative equity</i>		\$0 — \$249 999		\$250 000 — \$499 999		\$500 000 — \$749 999		\$750 000 — \$999 999		\$1 million and over	
	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%
Modest standard	16	7.1	51	22.6	92	40.7	41	18.1	14	6.2	12	5.3
Comfortable standard	177	51.3	81	23.5	50	14.5	21	6.1	9	2.6	7	2.0

^a Results correspond to averages over 1000 simulations.

Source: Productivity Commission estimates based on HILDA release 13.1, wave 10.

Table D.8 Couple home equity borrowing with a 10 per cent interest rate^a

Home equity at end of life

	<i>Negative equity</i>		\$0 — \$249 999		\$250 000 — \$499 999		\$500 000 — \$749 999		\$750 000 — \$999 999		\$1 million and over	
	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%
Modest standard	11	7.5	29	19.9	52	35.6	37	25.3	13	8.9	4	2.7
Comfortable standard	128	37.0	82	23.7	66	19.1	39	11.3	16	4.6	15	4.3

^a Results correspond to averages over 1000 simulations.

Source: Productivity Commission estimates based on HILDA release 13.1, wave 10.

Table D.9 Single home equity borrowing with a 5.25 per cent interest rate^a

Home equity at end of life

	<i>Negative equity</i>		\$0 — \$249 999		\$250 000 — \$499 999		\$500 000 — \$749 999		\$750 000 — \$999 999		\$1 million and over	
	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%
Modest standard	7	3.1	37	16.4	99	43.8	52	23.0	18	8.0	13	5.8
Comfortable standard	117	33.9	107	31.0	60	17.4	36	10.4	16	4.6	9	2.6

^a Results correspond to averages over 1000 simulations.

Source: Productivity Commission estimates based on HILDA release 13.1, wave 10.

Table D.10 Couple home equity borrowing with a 5.25 per cent interest rate^a

Home equity at end of life

	<i>Negative equity</i>		<i>\$0 — \$249 999</i>		<i>\$250 000 — \$499 999</i>		<i>\$500 000 — \$749 999</i>		<i>\$750 000 — \$999 999</i>		<i>\$1 million and over</i>	
	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%
Modest standard	7	4.8	26	17.8	55	37.7	37	25.3	16	11.0	5	3.4
Comfortable standard	77	22.3	100	28.9	80	23.1	44	12.7	26	7.5	19	5.5

^a Results correspond to averages over 1000 simulations.

Source: Productivity Commission estimates based on HILDA release 13.1, wave 10.

Changes to the rate of payment growth

In the base simulation, it was assumed that the annual amount borrowed grew at 2.5 per cent each year, the midpoint of the Reserve Bank of Australia's target band for inflation. With annual growth of 2.5 per cent, the real purchasing power of the 'income top up' should remain intact. However, some might wish to maintain a standard of living commensurate with the broader population. Hence, simulations were run in which the growth rate in the payment was set at 4 per cent per annum (which is akin to average annual growth in average weekly ordinary time earnings over the past 10 years), with all else held equal. The results show that increasing the annual growth rate of the payment leaves fewer home owners with positive equity at the end of the life of the household, but that the majority still retain positive equity (tables D.11 and D.12).

Table D.11 Single home equity borrowing with a 4 per cent payment growth rate^a

Home equity at end of life

	<i>Negative equity</i>		<i>\$0 — \$249 999</i>		<i>\$250 000 — \$499 999</i>		<i>\$500 000 — \$749 999</i>		<i>\$750 000 — \$999 999</i>		<i>\$1 million and over</i>	
	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%
Modest standard	9	4.0	49	21.7	96	42.5	44	19.5	15	6.6	13	5.8
Comfortable standard	155	44.9	93	26.7	51	14.8	27	7.8	12	3.5	7	2.0

^a Results correspond to averages over 1000 simulations.

Source: Productivity Commission estimates based on HILDA release 13.1, wave 10.

Table D.12 Couple home equity borrowing with a 4 per cent payment growth rate^a

Home equity at end of life

	<i>Negative equity</i>		\$0 — \$249 999		\$250 000 — \$499 999		\$500 000 — \$749 999		\$750 000 — \$999 999		\$1 million and over	
	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%
Modest standard	10	6.8	27	18.5	52	35.6	37	25.3	15	10.3	5	3.4
Comfortable standard	106	30.6	91	26.3	69	19.9	43	12.4	19	5.5	18	5.2

^a Results correspond to averages over 1000 simulations.

Source: Productivity Commission estimates based on HILDA release 13.1, wave 10.

Changes to house price growth

In the base simulations, it was assumed that house prices grew at an annual rate of 3.5 per cent. The rate of house price growth affects the value of home equity a household has at the end of their life — a higher rate of house price growth would lead to greater home equity at the end of life, and vice-versa.

Simulations were run in which the annual rate of house price growth was set at 1.5 per cent, and also at 5.5 per cent. Lower house price growth reduced home equity at the end of life, compared to the base simulation, for both singles and couples (tables D.13 and D.14). Conversely, a higher rate of general house price growth had significant effects on raising home equity at the end of life for those who borrow against their homes (tables D.15 and D.16).

In the base simulations and the sensitivity test simulations, couples generally possessed greater levels of equity at the end of life than singles, indicating that the former tend to be in a stronger financial position.

Table D.13 Single home equity borrowing with a 1.5 per cent house price growth rate^a

Home equity at end of life

	<i>Negative equity</i>		\$0 — \$249 999		\$250 000 — \$499 999		\$500 000 — \$749 999		\$750 000 — \$999 999		\$1 million and over	
	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%
Modest standard	16	7.1	72	31.9	95	42.0	27	11.9	12	5.3	4	1.8
Comfortable standard	173	50.1	99	28.7	50	14.5	12	3.5	11	3.2	0	0.0

^a Results correspond to averages over 1000 simulations.

Source: Productivity Commission estimates based on HILDA release 13.1, wave 10.

Table D.14 Couple home equity borrowing with a 1.5 per cent house price growth rate^a

Home equity at end of life

	<i>Negative equity</i>		<i>\$0 — \$249 999</i>		<i>\$250 000 — \$499 999</i>		<i>\$500 000 — \$749 999</i>		<i>\$750 000 — \$999 999</i>		<i>\$1 million and over</i>	
	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%
Modest standard	12	8.5	37	25.3	63	43.2	28	19.2	3	2.1	3	2.1
Comfortable standard	129	37.3	94	27.2	72	20.8	31	9.0	13	3.8	7	2.0

^a Results correspond to averages over 1000 simulations.

Source: Productivity Commission estimates based on HILDA release 13.1, wave 10.

Table D.15 Single home equity borrowing with a 5.5 per cent house price growth rate^a

Home equity at end of life

	<i>Negative equity</i>		<i>\$0 — \$249 999</i>		<i>\$250 000 — \$499 999</i>		<i>\$500 000 — \$749 999</i>		<i>\$750 000 — \$999 999</i>		<i>\$1 million and over</i>	
	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%
Modest standard	5	2.2	23	10.2	68	30.1	67	29.6	33	14.6	30	13.3
Comfortable standard	90	26.1	99	28.7	68	19.7	39	11.3	24	7.0	25	7.2

^a Results correspond to averages over 1000 simulations.

Source: Productivity Commission estimates based on HILDA release 13.1, wave 10.

Table D.16 Couple home equity borrowing with a 5.5 per cent house price growth rate^a

Home equity at end of life

	<i>Negative equity</i>		<i>\$0 — \$249 999</i>		<i>\$250 000 — \$499 999</i>		<i>\$500 000 — \$749 999</i>		<i>\$750 000 — \$999 999</i>		<i>\$1 million and over</i>	
	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%
Modest standard	4	2.7	17	11.6	42	28.8	45	30.8	20	13.7	18	12.3
Comfortable standard	64	18.5	76	22.0	86	24.9	46	13.3	35	10.1	39	11.3

^a Results correspond to averages over 1000 simulations.

Source: Productivity Commission estimates based on HILDA release 13.1, wave 10.

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