

# The Treasury

## Budget 2017 Information Release

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[40]	Not in scope	

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## The effect of the Pay Equity Settlement on residents with assets above the threshold

To: Hon Dr Jonathan Coleman, Minister of Health

Copy to: Hon Nicky Wagner, Associate Minister of Health

### Purpose

1. To outline the cost impact of the Pay Equity Settlement (the Settlement) on aged care residents with assets above the threshold, and a possible short term mitigation.

### Key points

- The Government's current policy position is that aged residential care is means tested, with residents that can afford to pay for their care doing so, up to the point at which their assets drop to \$220,000.<sup>1</sup> After which, they pay all their income towards the cost of their care, including their New Zealand Superannuation income.<sup>2</sup>
- The Settlement, which increases the wages paid to the workforce that provides care in this setting, will result in a higher annual cost for aged residential care. Current policy settings dictate that the 11,070 residents paying the maximum contribution towards the cost of their care will face increases of around \$74 a week (GST inclusive) or 7.9 percent from 1 July 2017.<sup>3</sup> This is in addition to a [38] percent assumed status quo price increase.
- The impact for these residents of paying a higher cost for their care is that their assets will reduce to the threshold level faster, at which point the government funds the full Settlement costs. A higher aged residential care cost as a result of the Settlement does not represent a barrier to accessing care.
- The Government may wish to provide relief for aged care residents with assets above the threshold (on the basis that the increase and its size are unusual and could not have been anticipated by residents). The Ministry has identified a number of options to remove or reduce the fiscal impact on residents but does not recommend any change to the current policy. The Ministry considers that the principles of this means tested policy are sound and notes that this price increase will not act as a barrier to care.
- Should the Government want to remove or reduce the cost impact on residents who pay the maximum contribution (on the basis that the increase and its size are unusual and could not have been anticipated by residents), the Ministry recommends removing the price increase for year 1 of the Settlement only (2017/18) at a cost of \$37 million and proceeding with driving system efficiencies to address costs in later years. This one off cost would need to be met by the Crown from its between Budget contingency as DHBs and providers have not accounted for this cost pressure.
- The Ministry would continue with its strategy to alleviate price increases beyond year one through encouraging the sector to realise net efficiency savings made possible by the expected benefits of the

<sup>1</sup> Residents' weekly payments are also limited to the cost of rest home care which is the first level of aged residential care.

<sup>2</sup> Residents are able to retain a Personal Allowance for their own use of \$43.45 a week.

<sup>3</sup> The precise amount will depend on national negotiations between representatives of DHBs and providers that will occur this month. Note that the cost provided in a previous paper of \$66 a week was a GST exclusive figure.

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Settlement (being reducing turnover and employment of more skilled and efficient staff) and reflecting these in DHB contract negotiations with providers.<sup>4</sup>

## Recommendations

### The Ministry recommends that you:

- a) **note** that on 1 July 2017 aged care residents with assets above the threshold are facing a 9.8 percent price increase, consisting of 7.9 percent (around \$74 a week, GST inclusive) as a result of the Pay Equity Settlement (the Settlement) and the assumed status quo price increase;
  - b) **note** that the Ministry of Health (the Ministry) recommends that the current maximum contribution policy continues and that residents bear the increased cost arising from the Settlement in year 1 (2017/18), with effort to be made to mitigate costs in later years through realising efficiency savings and reflecting these in contract negotiations;
  - c) **note** that should the Government want to provide relief to aged care residents, removing the price impact on residents of the Settlement for year 1 only will cost \$37 million and will require additional Crown funding;
  - d) **note** that the Ministry has identified other options to remove or reduce the price impact on residents arising from the Settlement, all of which are more expensive and/or complicated to implement and are not recommended;
  - e) **agree** that aged care residents who are paying the maximum contribution should meet the full price increase arising from the Settlement; **Yes/No**
- OR**
- f) **direct** officials to proceed with putting in place a mitigation for 2017/18 and to prepare a Cabinet paper to seek funding. **Yes/No**

Hamiora Bowkett  
Chief Strategy and Policy Officer  
**Strategy and Policy**

**Minister's signature:**

**Date:**

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<sup>4</sup> Note that the Settlement will also impose some extra costs, such as by adding pressure to increase wages for employees who are not care workers that will also have to be met through efficiency savings.

# The effect of the Pay Equity Settlement on residents with assets above the threshold

## Context

1. An in-principle agreement has been reached between the Crown, Employers and E tū, Public Service Association (PSA), New Zealand Nurses Organisation (NZNO) and New Zealand Council of Trade Unions (NZCTU) to settle the care and support worker negotiations referred to as “the TerraNova case”.
2. From 1 July 2017 providers will be funded to pay the increased wages through negotiated increases in the aged residential care contract prices and the Ministry will fund DHBs the increased costs.
3. One of the flow-on impacts of the Settlement will be an increased cost to residents in aged residential care facilities who pay the maximum contribution from 1 July 2017.
4. On 14 November 2016, Cabinet noted:
  - a. that the proposed settlement would increase the cost for residents in aged residential care facilities with assets above the threshold by about \$130 per week in year 1 (\$6,900 per annum) increasing to \$240 per week in year 5 (\$12,600 per annum);
  - b. the estimated number of residents in aged residential care facilities affected by the increase in cost is 11,070.
5. Subsequent modelling with improved data has shown that the impact on these residents is significantly less. Updated costs are around 7.9 percent or \$74<sup>5</sup> (GST inclusive) per week in year 1 (\$3,850 per annum) increasing to 10.9 percent or \$109 per week (\$5,641 per annum) in year 5.

## Background: resident’s payment towards the cost of their care

6. Under current legislation, the price aged residential care providers receive is set by negotiation between representatives of providers and representatives of DHBs. Providers cannot charge anything more than the agreed price for standard residential care services.
7. Currently the prices agreed are for the four categories of residential care (rest home, dementia, hospital and psychogeriatric). The price also varies across the country. These price differences have been maintained since they were calculated in 1999 by applying percentage increases to prices each year.
8. People who enter aged residential care have to pay a portion of the costs themselves. The DHB pays the difference between the resident’s contribution and the contracted price. The amount residents pay is determined by a financial means assessment based first on an asset threshold. Residents with assets below the threshold pay all their income towards their care, apart from a personal allowance of \$43.45 a week retained from New Zealand Superannuation<sup>6</sup>.
9. If a resident has assets above the threshold (\$220,000 for singles, \$120,000 excluding house and car for couples where one is in care) he/she is required to pay the ‘maximum contribution’ for their care. The ‘maximum contribution’ is set in legislation equal to the rest home price. As of 1 July 2016 it was in the range of \$884.03 to \$971.53 per week, depending on location.
10. As a result of paying the maximum contribution towards the cost of their care, each year around 1,200 of the 11,070 residents who have assets above the threshold reduce their assets to the threshold level. As a result they stop reducing their assets and pay only from their income. This is always a lower payment. The higher weekly payments as a result of the Settlement will mean that these residents reach this point around two weeks earlier than otherwise. All residents will continue to be able to afford residential care, some will just pay at a lower rate sooner.

<sup>5</sup> A previous paper included a figure of \$66 a week which was a GST exclusive figure.

<sup>6</sup> Small amounts of interest income are excluded.

## Effect of increasing care worker wages

11. The simplest and most desirable method to fund providers so they can pay increased care worker wages is for DHBs to negotiate a higher price for each of the four categories of care. To date this has been the working assumption for implementation.
12. As per previous advice, the increased price will be paid by residents, by DHBs or both, depending on the situation. For clarity:
  - a. Those residents whose assets are below the asset threshold will not be affected by price increases as a result of the Settlement. The DHB pays all the increase.
  - b. Those residents with assets above the threshold will pay more because the rest home price will increase and the 'maximum contribution' is set equal to the rest home price. This is consistent with the Government's current policy, which requires residents who can afford to pay for the cost of their care to do so, with the weekly amount limited to the rest home price, and enabling residents to retain at least \$220,000 in assets.
  - c. Where residents with assets above the threshold are in the dementia, hospital or psychogeriatric categories of care the DHB pays the difference between the rest home price and the price of those categories, so both residents and their DHB will pay more.

How price increases affect payments by residents and DHBs is illustrated in Annex A.

13. Table 1 below sets out the total cost that would be borne directly by residents in aged-residential care with assets above the threshold. The modelling indicates that for each of these residents they will pay around 7.9 percent more than otherwise or \$74<sup>7</sup> per week in year 1 (\$3,860 per annum) increasing to 10.9 percent more or \$109 per week (\$5,656 per annum) in year 5. These increases would be on top of the 'status quo' increases. The increase on 1 July 2017 could therefore be up to 9.8 percent. Further detail is included in Annex B.

Table 1. Estimated cost of care worker wage settlement on residents with assets above the threshold						
	2017/18	2018/19	2019/20	2020/21	2021/22	5 year total
Costs borne by residents	\$37m	\$47m	\$50m	\$48m	\$63m	\$245m
Extra weekly cost above the status quo increase (GST incl)	\$74	\$89	\$93	\$85	\$109	
Assumed status quo <u>annual</u> price increase	[38]					
Extra price paid by residents above status quo	7.9%	9.4%	9.7%	8.7%	10.9%	
Total post settlement <u>annual</u> price increase	[38]					

## Reducing the cost impact on residents with assets above the threshold

14. The cost residents pay will be less if the price of rest home care can be reduced. As a result of the Settlement increasing the overall cost, DHBs will have a stronger incentive to find efficiency savings, while still maintaining the quality of care. The Settlement itself should assist with delivering some types of efficiencies. Higher wages should result in reduced cost to providers from reduced turnover of staff and through the employment of more skilled and therefore more efficient staff. On the other hand, it will also impose some extra costs, such as through adding pressure to increase wages for employees who are not care workers.
15. DHB, providers, the Ministry and consumer representatives are undertaking a funding model review for aged residential care during 2016/17 [HR 20170222 refers]. This will be an opportunity to consider whether the way providers are funded incentivises the most cost efficient services.

<sup>7</sup> A previous paper included a figure of \$66 a week which was a GST exclusive figure.

## Options to offset the cost to residents with assets above the threshold

16. The Ministry does not recommend any change to the current policy, which would see the maximum contribution paid by aged care residents above the threshold rise with the rest home price from 1 July 2017, and for residents to pay the full price increase. The Ministry considers that the principles of this means tested policy are sound and notes that this price increase will not act as a barrier to care.
17. However, it may be desirable to provide relief either because of the unusual size of the price increase and short lead in time, or because it is the result of the application of the new pay equity policy to this specific sector (unlike other cost increases such as the minimum wage which impacts that are across all sectors) and could not have been anticipated by residents. It is important to note that doing so will shift the cost from the resident to either the Crown, DHB or provider and will require additional funding as they are outside of the Care and Support Worker Settlement Agreement.
18. Should the Government wish to reduce the impact of the Settlement on aged care residents paying the maximum contribution, the most feasible option is to remove the impact for one year only, giving time for residents to adjust to the new payment level. If you choose this option final operational detail will need to be confirmed eg, the treatment of GST. This would have a one off cost to the government of \$37 million. The Ministry would continue with its strategy to alleviate price increases beyond year 1 through encouraging the sector to realise efficiency savings made possible by the expected benefits of the Settlement and reflecting these in DHB contract negotiations with providers.
19. The Ministry has identified other options to remove or reduce the impact on residents with assets above the threshold. These are outlined in table 2 and described below. The Ministry does not recommend any of these alternative options on the basis of cost and/or feasibility of implementation.
20. Officials have considered whether reducing the impact of the Settlement would have any precedents for the impact of the Settlement on other people who receive either subsidised or unsubsidised care support services. For example, some people receiving respite care in aged residential care facilities are given a subsidy rather than having their costs paid in full by the DHB. The Ministry does not consider that the pay equity supplement approach would set any precedent because of the unique means testing regime for long-term aged residential care.

<b>Table 2. Options for offsetting the cost of a care worker wage settlement on residents with assets above the threshold</b>						
	2017/18	2018/19	2019/20	2020/21	2021/22	5 year total
<b>Status quo: No policy change (previously noted by Cabinet)</b>						
Residents <u>extra</u> \$ and ( <u>extra</u> %) above status quo	\$74/wk (7.9%)	\$89/wk (9.4%)	\$93/wk (9.7%)	\$85/wk (8.7%)	\$109/wk (10.9%)	
Cost to the Crown	\$0m	\$0m	\$0m	\$0m	\$0m	\$0m
<b>Remove the impact for 2017/18 only</b>						
Residents <u>extra</u> \$ and ( <u>extra</u> %) above status quo	\$0 (0%)	\$89/wk (9.4%)	\$93/wk (9.7%)	\$85/wk (8.7%)	\$109/wk (10.9%)	
Cost to Crown	\$37m	\$0m	\$0m	\$0m	\$0m	\$37m
<b>Alternative option 1: Remove the impact</b>						
Residents <u>extra</u> \$ and ( <u>extra</u> %) above status quo	\$0 (0%)	\$0 (0%)	\$0 (0%)	\$0 (0%)	\$0 (0%)	
Cost to Crown	\$37m	\$47m	\$50m	\$48m	\$63m	\$245m

<b>Alternative option 2: Halve the impact</b>						
Residents <u>extra</u> \$ and ( <u>extra</u> %) above status quo	\$37/wk (4.0%)	\$44/wk (4.7%)	\$47/wk (4.8%)	\$43/wk (4.3%)	\$54/wk (5.4%)	
Cost to Crown	\$19m	\$24m	\$26m	\$24m	\$32m	\$126m
<b>Alternative option 3: Limit the <u>annual</u> increase to 3.9% (2.2% extra above the status quo increase of 1.7%)</b>						
Residents <u>extra</u> \$ and ( <u>extra</u> %) above status quo	\$20/wk (2.2%)	\$41/wk (4.4%)	\$64/wk (6.6%)	\$85/wk (8.7%)	\$108/wk (10.9%)	
Cost to Crown	\$28m	\$25m	\$16m	\$0m	\$0m	\$70m
<b>Alternative option 4: Grandfather the offset for existing residents only</b>						
Extra % above status quo for <u>existing</u> residents	0%	0%	0%	0%	0%	
Extra % above status quo for <u>new</u> residents	(7.9%)	(9.4%)	9.7%	8.7%	10.9%	
Cost to Crown	\$32m	\$28m	\$22m	\$15m	\$15m	\$112m

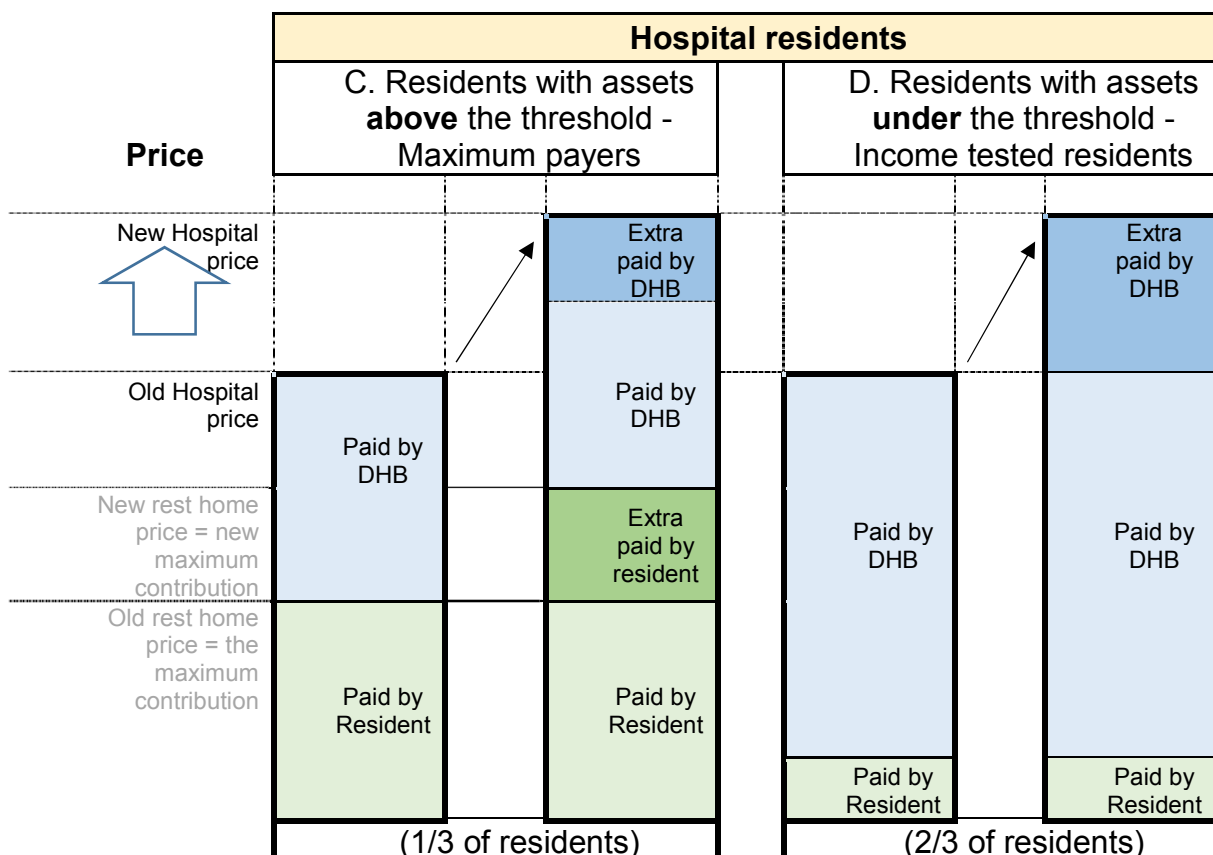
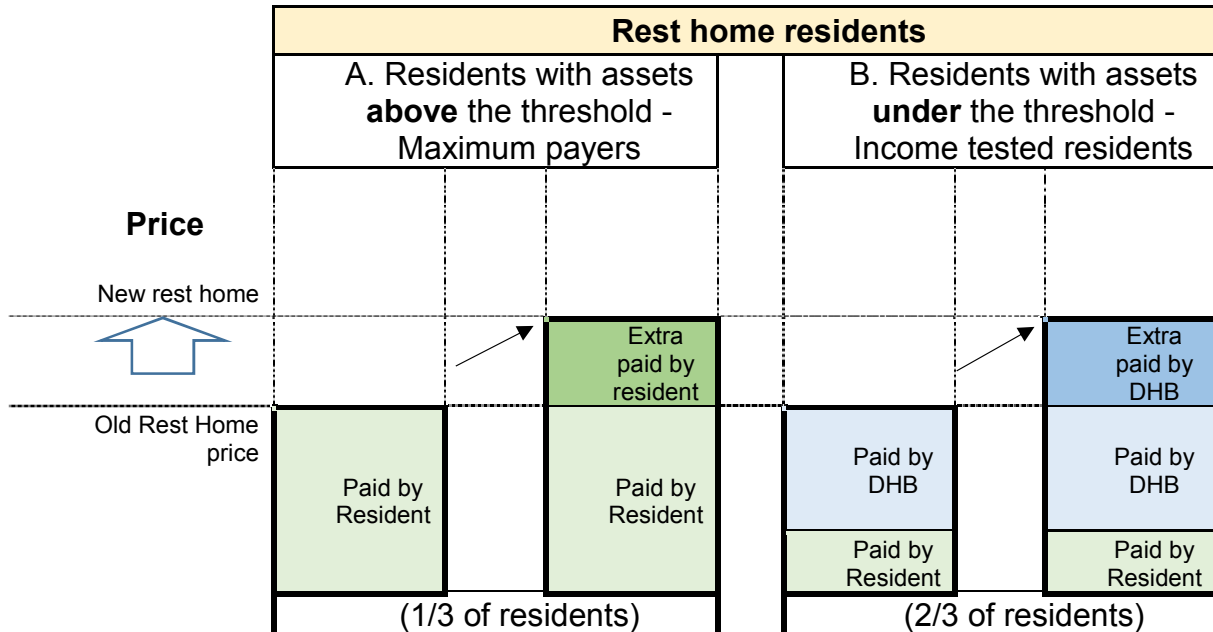
21. Option 1 completely relieves residents from paying more as a result of the Settlement. You might consider this approach if you judge that the large cost of residential care paid by only some residents (those that are in care for a number of years) should remain unchanged. For the large part, health related costs are borne by the community not the individual, and you may take the view that individual contributions should not be substantially greater than at present. Option 1 would increase the fiscal cost of the Settlement by \$245 million over five years. Testing of the payment system to date shows that it is feasible to implement. As a permanent option it would be desirable to ultimately be implemented through changes to the means testing legislation.
22. Option 2 would see the impact on residents halved. It is an illustration of the range of options that share the cost. This would reduce the impact on residents but limit the cost to the Government relative to Option 1. Any manner of ratios could be employed under this scenario.
23. Option 3 would smooth the increase in costs over time for residents, limiting the initial increase but making subsequent increases larger as a result. It might be preferred if you agree that that residents should pay the extra cost arising from the Settlement but are consider the annual increase for 2017/18 under the status quo to be unreasonably high and with insufficient lead in time.
24. Option 4 removes the extra cost for existing residents only on the basis that they should not face an unexpected increase. However, this approach would substantially complicate the payment system for many years and officials would need to do more investigation to know if it is feasible to implement.

**END.**

Annex A – Understanding impact of price increase

When aged residential care prices increase:

- a) Rest home residents with assets above the threshold pay the full amount of the increase
- b) Rest home residents with assets under the threshold pay no more, the DHB pays the full increase
- c) Hospital residents with assets above the threshold pay the increase in the rest home price and the DHB pays the extra to the new hospital price
- d) Hospital residents with assets under the threshold pay no more, the DHB pays the full increase





**Annex B – Implications for residents with assets above the threshold**

*How long are people in care?*

Median length of stay is 18 months

*Average age in care?*

85 years old

*How many are currently below the threshold?*

21,000 people

*How many people are above the threshold and currently paying the maximum contribution?*

11,070 – refer table and graph below

*On average how long does it take for a person to spend their savings/assets before they reach the threshold?*

The median person never does, only 1,200 of 11,070 cross the threshold each year.

**Residents who own assets above the asset threshold pay the maximum contribution**

The effect on these residents of an increase in the price paid to providers to compensate them for increases in carers' wages is estimated to be as follows.

Year	Increased funding of residential care sought \$M ex GST	Increased funding paid by residents with assets above the threshold \$M ex GST	Payment by resident before Crown wage offer \$ per year GST incl	Payment by resident after Crown wage offer \$ per year GST incl	Extra payment by resident \$ per year GST incl	Percent increase in resident payment from the wage offer	Extra payment by residents \$ per week GST incl	Percent of Rest Home price for Maximum contribution to be unaffected by wage offer	Pay equity Supplement for Maximum contribution to be unaffected by wage offer
1	\$110m	\$38m	\$48,625	\$52,485	\$3,860	7.9%	\$74	92.6%	\$9.39
2	\$137m	\$48m	\$49,451	\$54,088	\$4,637	9.4%	\$89	91.4%	\$11.28
3	\$149m	\$52m	\$50,292	\$55,157	\$4,865	9.7%	\$94	91.2%	\$11.84
4	\$143m	\$49m	\$51,147	\$55,596	\$4,449	8.7%	\$86	92.0%	\$10.83
5	\$188m	\$64m	\$52,016	\$57,672	\$5,656	10.9%	\$109	90.2%	\$13.76

Payments per resident are average amounts; amounts differ because the rest home price differs between locations (territorial local authority areas) and the GST rate differs (12.3% for rest home and dementia and 12.9% for hospital and psychogeriatric)

**The location of residents paying the maximum contribution is as follows:**

