Funding High-Quality Aged Care Services

By David Richardson
Senior Research Fellow, Australia Institute

and

Jim Stanford, Economist and Director, Centre for Future Work

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Level 1, Endeavour House, 1 Franklin St
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Tel: (02) 61300530
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About the Authors

David Richardson is Senior Research Fellow at the Australia Institute, with four decades of experience in fiscal and macroeconomic policy analysis.

Dr. Jim Stanford is Economist and Director of the Centre for Future Work, and Honorary Professor of Political Economy at the University of Sydney.

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Summary

Australians have been rightly shocked by repeated exposés of widespread mistreatment, neglect and even abuse of elders in our aged care system. Long-standing problems in the system became even more acute during the COVID-19 pandemic, which posed such a danger to older Australians (especially those in residential care facilities): three-quarters of all deaths due to COVID-19 in Australia occurred in aged care facilities. In response to these concerns, the government appointed the Royal Commission into Aged Care Quality and Safety. The Commission compiled exhaustive evidence of systematic failures in the aged care system, identifying in particular the roles of inadequate government funding, undervalued and precarious employment arrangements, and the conflicted incentives of private for-profit providers in causing this crisis in care. The Commission's final report, issued in March 2021, contained 148 recommendations to urgently repair the system and provide better care to our seniors. Of particular note are several recommendations relating to employment practices in aged care: including the need for permanent employment (not casual, agency, or gig jobs), the need for binding minimum staffing ratios and time allotments, the need for registration and regulation of support workers, and the need for much better training opportunities and clearer career paths.

The comprehensive and ambitious scope of these recommendations gives rise to a common question: How will we pay for all that? This funding issue must be placed in an appropriate context. First, aged care services is not just a budgetary 'cost' for government. This report documents that aged care is also a vital, valuable industry in its own right: employing 400,000 Australians, generating some $25 billion in annual GDP, and lifting national incomes, employment, and tax revenues at a time when Australia needs all of those. Expanding the quantity and quality of aged care services should be seen as an economic opportunity, not just a fiscal expense. Second, strengthening the generational 'pact' which underlies aged care – with each successive generation of elders cared for by those who come after them – has valuable and efficiency-enhancing economic effects. It allows Australians to make important decisions through their lives (about education, careers, home ownership, investments, and more), safe in the knowledge that they will be adequately cared for in their old age. Finally, large government deficits are both inevitable and desirable as the economy recovers from the COVID-19 pandemic. The economy will need more government spending, funded through deficits, for years to come, and in this context it is not appropriate to worry about 'funding' every dollar of incremental expense on aged care (or any other social priority, for that matter).

Nevertheless, in the longer-term government will need to mobilise incremental fiscal resources to support the crucial reforms recommended by the Royal Commission. While those recommendations were not specifically costed, research from several sources indicates they will require incremental resources of at least $10 billion per year (or 0.5% of national GDP or more). This is modest in the larger picture of the fiscal and economic capacity of Australian governments. Section III of this report compares Australia's tax base to other industrial countries, and to previous periods in our own history. Raising incremental resources on this scale will merely offset some of previous reductions in overall taxes in Australia, and would leave Australia's fiscal base far smaller than most other OECD countries – including those which have done much better at delivering quality aged care to their elderly.

Table 1 Options for Financing Aged Care Service Improvements (Target Annual Revenue of $10 Billion)
Increase the Medicare Levy by 1%
A Progressive Aged Care Levy
Retain the 37% Personal Income Tax Bracket
Reforming Taxation of Investment and Capital Income
Reforming Company Taxes
Source: Authors' compilation as described in text. Benchmark incremental revenue equal to 0.5 per cent of national GDP.

Finally, Part IV of this report reviews five specific options through which the Commonwealth government could mobilise $10 billion in incremental annual funding to provide a strong foundation for implementing the Royal Commission recommendations. The options considered are summarised in Table 1. Each would raise at least $10 billion per year (or 0.5% of GDP). Two were proposed by the respective Royal Commissioners (a 1-point increase in the Medicare Levy proposed by Commissioner Briggs, and a set of changes in personal income tax rates similar to that proposed by Commissioner Pagone). Others would utilise other levers in the tax system to mobilise more resources: including cancelling legislated tax cuts for high-income Australians, reforming lucrative tax preferences on investment and capital income, and reforming loopholes in the company tax system. The distributional impacts of the five proposals vary; the least 'fair', in terms of the share of additional tax collected from higher-income households, is the flat-rate medicare-style levy. But all of these measures would be positive, in that they would underpin an improvement in a core element of our social programs that will enhance security, equality, and safety for elder Australians for years to come. The government could use any one of these measures (or a combination of them) to raise the funds necessary to implement the major part of the Royal Commission’s recommendations.

In sum, there can be no argument that Australia – one of the richest countries in the world – cannot ‘afford’ to provide top-quality, respectful care to the elders who helped build our economy and our society. There is in fact a panoply of revenue options readily available to the Commonwealth government to support the ambitious and quick implementation of the Royal Commission’s recommendations. That effort must start with the 2021-22 Commonwealth budget. There is no immutable economic or fiscal ‘constraint’ holding back the government from doing right by Australia’s elders. The only question is whether this government places enough priority on caring for our seniors with the quality and dignity they deserve.

Introduction: A Crisis of Care

This report investigates the economic and fiscal context for the provision of aged care services in Australia. The report comes in the wake of the final report of the Royal Commission into Aged Care Quality and Safety, which made numerous important recommendations for improvements and reforms in how aged care services should be delivered, regulated, and funded. The Royal Commission itself was a response to continuing scandals of inadequate care, neglect and even abuse that have been documented for years in many aspects of Australia's aged care system. The COVID-19 pandemic, and the acute risks which it posed to our elders (especially those living in residential care facilities), made it all the more urgent for these systemic failures to be documented, addressed, and repaired.

The legacy of scandals and abuse in Australia's aged care sector dates back decades, well before COVID-19. The Howard government deregulated the aged care sector with the *Aged Care Act 1997,* facilitating a rapid expansion in private for-profit provision of care, and reducing staffing and reporting requirements (Dabarera, 2021). By 2000, still in that government's tenure, horrifying instances were already emerging of poor care and abuse (Harris, 2021).

Minor reforms to aged care delivery and oversight did not stem the flow of scandal. In 2018, the ABC's *Four Corners* program (ABC, 2018a, 2018b) revealed widespread poor conditions in residential aged care. Over 1300 staff in nursing homes were consulted in the ABC investigation, exposing critical problems such as substandard care and inadequate food. Research based on a sample of 800 homes revealed that they were spending just $6.08 per resident per day on food: less than is spent for prison inmates, and barely one-third of the $17 per day average food expense for the community at large (ABC, 2018a). In some cases up to half of nursing home residents were malnourished.

Systematic understaffing was documented, in addition to widespread problems of undertraining and poor working conditions for aged care staff. Due to the federal government's deregulation of the sector, there are no minimum staffing ratios in Australian nursing homes – except for state-run facilities in Victoria and Queensland. And despite the fact that many residents have complex care needs, aged care staff can be employed with as little as six weeks training, and in some job categories do not have specific registration or qualification requirements.

The Royal Commission into Aged Care Quality and Safetu was announced by Prime Minister Scott Morrison the day before the first of the two *Four Corners* episodes was broadcast. This was not a coincidence. The government knew that Australians would be properly outraged at this shocking evidence of poor care. Announcing the Commission was its effort to manage the resulting public anger. Now, almost three years later, it is incumbent on the government to move quickly to enact the Commission's recommendations. It cannot be allowed to use the Commission solely as a tool for dissipating public anger and delaying action: its recommendations must lead to real change. To achieve this goal, Australian society must continue to express its strong demand for real improvements in aged care delivery, so that the Commonwealth government responds with appropriate ambition and resources.

Even before the Royal Commission, ample evidence has attested for years to the inadequacy of aged care services in Australia. For example, the Productivity Commission (2020, p. 14.17) reported that in 2018, over one-third of older people living in households and in need of assistance, reported that those needs were not fully met. That proportion was higher for people with a profound or severe disability (over 40 per cent). Many consequences flow from that chronic shortfall, including tying up hospital beds (since hospitals will not discharge many patients until they are satisfied they have adequate home assistance).

Another critical failure of the existing system is long waiting lists for care, because of government rationing of service provision. In some tragic cases, individuals on waiting lists died before their turn to receive care came due (see Connolly, 2020). The government has approved new home care packages for eligible recipients, but this spending has been slow to roll out and long waiting lists remain. As part of its regular review of government services, the Productivity Commission reports on the time taken between the assessment by Aged Care Assessment Teams (ACAT) and the offer of a home care package. For Australia as a whole, the median wait was 7 months for a Level 1 package and 34 months for a Level 4 package.[1] Those needing Level 4 packages thus must wait for much or all of their expected life span.

The mental health of nursing home residents has also been a critical concern. Some estimates suggest that almost half of nursing home residents suffer from mental illness, not counting dementia (Magarey, 2017). Many are unable to access GP mental health treatment plans through Medicare because of legal exclusions, while nursing homes are not compelled (and usually decline) to fund mental health services for residents (such as treatment by a psychologist). *Four Corners* (ABC, 2018a) also

[1] Productivity Commission (2020), Section 14.

reported widespread instances of depression, anxiety, and suicidality among residents directly related to the quality of their care.

The quality of care in for-profit homes – which account for a growing share (currently 40 per cent) of residential aged care spaces in Australia[2] – has been the subject of particular scandal and scrutiny. Government-run homes perform best on the range of indicators reviewed by the Royal Commission, ahead of both for-profit and not-for-profit facilities (Royal Commission into Aged Care Quality and Safety, 2020). Private facilities perform the worst. But only nine per cent of Australian facilities are government-run.

Ultimately a conflict of values underlies the many issues and scandals that led to the Royal Commission. On one hand is the basic moral need for our elders to be treated with dignity and humanity. On the other hand are previous Commonwealth decisions to hand over more control of the aged care system to private providers, operating within a deregulated and competitive environment. Government claimed (unjustifiably) that a market-based system would give Australians more 'choice', and promote 'efficiency'. In fact, the opposite has occurred: the profit motive drives providers to cut costs and corners in care, while undertaking activities (like bloated financial and marketing functions) that might be good for 'business' but provide no benefit for those receiving care. In addition to short-changing customers and their family with poor-quality care, the increasingly concentrated private aged-care industry has a dubious record on other ethical practices: for example, Ward (2018) documents widespread tax minimisation by large profitable aged-care providers.

THE COVID-19 PANDEMIC AND AGED CARE

The COVID-19 pandemic threw into even starker relief long-standing weaknesses in the staffing and delivery of aged care services, particularly in residential facilities. Many underpaid staff faced the need to cobble together shifts over multiple sites to achieve enough income to live on. But multi-site staffing practices could facilitate outbreaks across multiple homes. This pattern was reinforced by the precarious employment conditions of many aged care workers: some are employed as casuals, many work part-time (short hours under 20 hours week are common), and providers regularly use agencies to meet their employment needs. All these precarious employment arrangements undermine safety protocols: with poor training and staff continuity, and limited or no access to paid sick leave (apart from federal pandemic leave, which was implemented after the pandemic began). The inability of aged care providers

[2] Royal Commission into Aged Care Quality and Safety (2021), Volume 1, p. 50.

(especially private facilities) to increase staffing when outbreaks occurred – a consequence of long-term short-staffing and reliance on agency employment – made matters worse (Davey, 2020).

The consequences of poor staffing and quality practices were tragically prevalent in Victoria, as a result of that state's concentrated COVID-19 outbreak (Royal Commission into Aged Care Quality and Safety, 2020c). However, the same outcomes could have occurred in any Australian jurisdiction. Notably, very few state-run aged care facilities in Victoria experienced COVID-19 cases, and none of the 685 COVID-19 deaths that occurred in aged care (making up 75% of total COVID deaths in Australia) were experienced in state-run facilities (Cousins, 2020).

In many cases, adequate staffing was not available to allow visits by family members, even when risks could conceivably have been managed (Royal Commission into Aged Care Quality and Safety, 2020c). This further impacted on quality of life for residents, including their physical, mental, and emotional wellbeing.

Training in the use of personal protective equipment in residential aged care settings was described as 'completely inadequate' – neither compulsory, nor of a high standard (Royal Commission into Aged Care Quality and Safety, 2020c). This finding was reinforced by a detailed survey of over 1500 aged care nurses undertaken by the Australian Nursing and Midwifery Federation (2020). That study highlighted systemic failures in planning and preparation for COVID outbreaks in aged care facilities, widespread absence of infection-control training, chronically inadequate staffing levels, and chronic shortages of PPE supplies.

The lesson here is that staff, and their conditions of employment, are not properly valued within businesses that are driven by bottom-line profits. That is having adverse outcomes for the people receiving care. Again, the prerogatives of cost-cutting conflict with the need for quality, person-centred care.

Ultimately, aged care must be considered as a public service – and quality care must be provided as a basic right to every older person who needs it, regardless of their financial circumstances. The recommendations of the Royal Commission to build an aged care system based around a universal entitlement to high-quality care represents an opportunity to break with this shameful legacy of inaccessible or inadequate care for our elders. There is no doubt that this will require the investment of significant resources. But as with any question about government expenditures, the matter boils down to a question of social priorities. Given the contribution that our older generations have made to building our country and our economy, laying the foundation for the prosperity that most of us enjoy today, the least we can do in return is ensure that they are provided for with high-quality clinical and social supports, dignity, and fairness when they need these things. This report will show that providing top-quality, universal aged care is eminently feasible in economic and fiscal terms – so long as we make it the national priority it should be.

OVERVIEW OF THIS PAPER

The rest of this paper is organised as follows. In Part I, the major findings of the Royal Commission, especially those relating to staffing, training, and quality issues, are reviewed and summarised. This sets the stage for our subsequent consideration of how those necessary reforms will be financed.

In Part II, the existing economic and fiscal parameters of the existing aged care system are described – including the broader economic and social benefits that flow from the production and delivery of aged care services. Aged care is, after all, a substantial industry in its own right: employing close to 400,000 Australians, and generating tens of billions of dollars in value-added every year. Seeing the sector as a source of growth and opportunity, rather than as a 'cost' item, contributes to a more well-rounded appreciation of its role and value.

Part III of the report provides a detailed review and discussion of Australia's fiscal capacity: that is to say, the ability of government, particularly the federal government, to mobilise economic and financial resources to provide essential public services. This analysis confirms that Australia's fiscal capacity is ample. Claims that the government is fiscally prevented from undertaking a necessary and beneficial expansion of aged care services reflect ideological biases, not economic realities. By both historical and international standards, there is plenty of room in a country as wealthy and productive as Australia to ensure that our elders receive a level of care befitting our respect for and responsibility to them.

In Part IV, we discuss specific opportunities to meet the challenge of financing aged care reform. We consider the likely scale of additional expenses likely to be required to substantively implement the Royal Commission's recommendations. While no itemised estimation of those costs has been conducted to date, evidence suggests that additional investments equivalent to between 0.5 and 1.0 per cent of Australian GDP will be required (phased in over several years) to support the major improvements identified by the Commission. Some of those additional expenses can and will be absorbed through normal general revenues and expenditures. There were some discussions in the Royal Commission regarding a sequestered account to fund aged services, but most observers are unconvinced that this approach would be useful – and we concur. And for the foreseeable future, it is inevitable that the Commonwealth government is going to incur significant fiscal deficits, anyway – due to the after-effects of the COVID-19 pandemic and recession. These deficits are a normal, and indeed helpful, policy response for an economy that is just emerging from the fastest, deepest recession in postwar history. In that context, it is neither necessary nor desirable to confirm that every dollar of additional aged care expenses must be 'funded' from offsetting government revenues.

Nevertheless, it is also clear that in the long run, the Commonwealth government will need to mobilise additional resources, above and beyond its current and anticipated revenue portfolio, to underpin the necessary and sustained improvements in aged care identified by the Royal Commission. To that end, Part IV identifies five distinct revenue tools which would each raise new revenues equivalent to at least 0.5 per cent of GDP – the lower bound of the cost estimate discussed above. Any one of those options (or some combination of them) could underwrite the major part of improving aged care services.[3] This confirms that Australia has ample fiscal capacity to fulfil our obligation to our elders – and to the workers who deliver essential services to them, to be able to perform that work in safe, well-trained, fairly compensated jobs.

The conclusion of the report restates the major findings, and summarises the policy and political imperatives now before the Commonwealth government to act on the Royal Commission's recommendations. The government has both a moral responsibility and the economic capacity to respond fully and quickly to the Commission's directions.

[3] And if total incremental expenses exceeded the 0.5% of GDP benchmark, government could wholly or partially enact an additional choice from the five options, and/or absorb the remainder within its existing budgetary base.

I. The Royal Commission's Findings

The Royal Commission into Aged Care Quality and Safety was created in response to a growing list of scandals regarding inadequate care, neglect, and outright abuse in Australia's aged care system. Three eminent Commissioners were appointed to inquire into all aspects of aged care quality, delivery, funding and regulation:[4] including the Honourable Tony Pagone QC, Ms Lynelle Briggs AO, and the Honourable Richard Tracey AM RFD QC. Sadly Mr Tracey died during the course of the Commission's work. Mr Pagone served as Chair of the Commission, and the Commissioners were supported by an able staff, including eight Counsels Assisting.

The Commission conducted 25 public hearings and workshops in locations across Australia. It received over 10,000 submissions, and also undertook an extensive programme of original research – engaging experts from several universities, consulting firms, and other resources. It published an interim report (Royal Commission into Aged Care Quality and Safety, 2019) in October 2019, in three volumes. The interim report focused mostly on cataloguing the evidence collected during its investigations regarding systemic failures and widespread neglect in existing aged care delivery. The Commission also published a stand-alone interim document on the impact of the COVID-19 pandemic on aged care services and safety (Royal Commission into Aged Care Quality and Safety, 2020c), in response to the tragic concentration of illness and death among elders receiving care.[5]

The Commission's final report was released on 1 March 2021. Unfortunately, the publication of that final report occurred under unfavourable circumstances – with the public's attention distracted by continuing regional outbreaks of the COVID-19 pandemic, Australia's unsuccessful national programme of vaccination, and a major scandal regarding sexual assaults and harassment in Parliament House. The rushed and unplanned release of the report, with no notice or 'lock-up' for journalists to properly report on it, diluted the public attention and focus which the report deserved. It is now incumbent on all stakeholders in the process, not least the government itself, to respond fulsomely to the report and its recommendations. It must not be relegated to the political and policy back burner, amidst ongoing political dramas in Canberra. The

[4] The Commission's Terms of Reference, including seven specific instructions, are published here: https://agedcare.royalcommission.gov.au/about/terms-reference.

[5] Of Australia's 909 deaths from COVID-19 at time of writing, 685 (or over three-quarters) were among seniors receiving aged care – almost all in residential aged care facilities, and most in Victoria. See Australian Department of Health (2021).

Commonwealth's response to the Commission's findings and recommendations should commence with the upcoming 2021-22 budget, which must confirm the government's willingness to allocate significant resources to the implementation of the Commission's vision.

The final report contained 5 volumes and over 2800 pages of text. The Commissioners issued 148 specific recommendations. In some cases, the two Commissioners differed in specific recommendations (including on how to fund aged care reforms, as discussed in detail in Part IV of this report). Unfortunately, this may provide an opportunity for the government to downplay or discard certain recommendations.

Here is a summary of several of the Commission's key findings and recommendations:

Inadequate Service: The Commissioners strongly condemned the failure of the existing system to provide adequate care to seniors. "Substandard care and abuse permeate the Australian aged care system." (Volume 1, p. 68.) Evidence suggests that at least one-third of residents in aged care facilities experience sub-standard care, including assaults, overuse of physical and chemical restraints, and inadequate or inconsistent staff attention.

Universal Entitlement: A core and powerful recommendation of the Commission is to establish a universal rights-based aged care system, in which every elderly Australian can access the care they need. This implies a reduction or phasing-out of user fees and other financial hurdles to accessing care. It would also require the government to ensure adequate supply of services (both home care and residential), to avoid rationing and delays in access.

Structure of Ownership: The Commissioners expressed concern about the role of private for-profit providers in aged care delivery, particularly in residential care, in light of evidence that the quality of care in those facilities is demonstrably poorer. "Government-run residential aged care providers perform better on average than both not-for-profit and, in particular, for-profit aged care providers." (Volume 1, p. 72.) Government-run facilities have the best outcomes in quality and health indicators, but they account for a small share of total beds in the wake of privatisation and fiscal restraint implemented by government over the last quarter-century. Moreover, among for-profit and non-profit providers there has been a noted consolidation and concentration of ownership in recent years – with the 10 largest chains now responsible for 39% of all places (Volume 1, p. 64), and a growing share of seniors being cared for in large facilities. The Commissioners urged a focus on building smaller facilities, where care can be more personal and flexible than in larger operations.

Regulatory Failure: The prevalence of sub-standard care, neglect, and abuse confirms the failure of the existing regulatory regime for aged care, and the Commissioners condemned the 'light touch' approach (including a reliance on self-regulation) that has characterised the Commonwealth government's approach over the past generation. A high-quality system needs "continuous monitoring and investigation" (Volume 1, p. 77), and the Commissioners proposed many sweeping changes in regulatory practice. These include a new system governor capacity, the transfer of standards regulation to a renamed Australian Commission on Safety and Quality in Health and Aged Care, a new system for benchmarking and public reporting on quality outcomes, and a stronger system for reporting serious incidents and enforcement of standards.

Star Rating System: To assist aged Australians and their families in selecting providers for aged care, and to put more pressure on providers (especially private homes and agencies) to improve their standards, the Commissioners recommended adoption of a star-based rating system for providers. This would assign easy-to-understand ratings to providers, on the basis of measurable indicators – including staffing levels, the results of regulatory assessments, and notices of non-compliance with standards. Consumers would thus have more confidence regarding the quality of the services they use, and the systematic underperformance of private facilities on these criteria would become more apparent. Of course, ratings and consumer information are not a replacement for rigorous regulation to ensure that safety standards are universally achieved. But this system could enhance the pressure on laggard providers to improve their quality of care.

Workforce Issues: Many sections of the report emphasise the importance of a stable, well-trained, well-compensated, and adequate workforce to high-quality aged care services. After all, in aged care (like other human services), the quality of work *is* the quality of care. It is impossible to distinguish between the training and working conditions of those delivering the care, and the quality of care received by their clients: they are one and the same thing. "A highly skilled, well rewarded and valued workforce is vital to the success of any future aged care system… The evidence is clear that the quality of care and the qualify of jobs in aged care are inextricably linked." (Volume 1, p. 124.)

The Commissioners documented the many weakness and failures of existing staffing and professional development systems in the sector. "Australia's aged care system is understaffed and the workforce underpaid and undertrained. Too often there are not enough staff members, particularly nurses, in home and residential aged care." (Volume 1, p. 76.) The Commissioners cited low wages, poor working conditions, chronic lack of investment in training, limited promotion opportunities, and the absence of visible career pathways as contributing to high turnover and recruitment challenges in the sector. With aged care providers needing to expand their workforce by an estimated 130,000 new positions by 2050, the crisis in the aged care workforce must be urgently addressed to improve retention of existing workers, and attract new recruits to the sector.

Among many concerns in this area, the Commissioners highlighted the erosion of registered nurses in the residential care sector (falling from 21% of all staff in 2003 to just 15% by 2016), a parallel decline in the proportion of enrolled nurses, and a surge in reliance on less-qualified personal care workers (who accounted for 70% of staff by 2016).[6]

The Commissioners made several important recommendations to improve the quantity of staffing, and the quality of training, compensation, and support for them. These include:

- Registration and regulation of personal care workers, including requirements for initial and ongoing training.
- Closing the wage gap between occupations in aged care and equivalent work in other parts of the labour market (especially the acute health care sector). Specifically, the Commission recommended a collaborative work value case be initiated at the Fair Work Commission involving all relevant unions, providers, and the government.
- Wage increases should be an explicit objective of a new funding model for aged care, with benchmark prices for services determined "at a level that enables workers to be renumerated to reflect what similar workers are paid in similar sectors." (Volume 1, p. 129.)
- Previous deregulation which allowed providers to allocate government funding across staff categories has led to the downgrading of skills and qualifications (and specifically the diminishing proportion of registered nurses engaged in aged care). So the Commissioners recommended a system of strong and binding staffing ratios to increase the care time provided for seniors in care, ensure a higher proportion of that time is provided by nurses, and ensure that residential facilities have a registered nurse on site at all times. This critical recommendation would have a transformative impact on the quality of work, and the quality of care, throughout the sector. Ensuring adequate trained staff are available at all times, and that those staff have adequate time to do their

[6] See Royal Commission Final Report, Volume 1, p. 63.

jobs properly, is a central prerequisite for achieving a universal, high-quality system.

- The Commission highlighted the risks to staff quality and stability arising from various forms of non-standard, temporary, agency, and ‘gig’ work in aged care service delivery. It concluded that permanent employment arrangements are necessary for achieving the training, stability, and enhanced quality goals set in its other recommendations. “We consider permanent employment as a mode of engagement of the workforce is more compatible with achievement of our broad objectives.” (Volume 1, p. 131.)

Funding: Of course, the far-reaching and urgent reforms proposed by the Commissioners to improve the quality, safety, and regulation of aged care services will require substantial resources to facilitate better staffing, better governance, and better care. The Commission did not attempt to ‘cost’ its various specific recommendations, but Commissioners did make a range of proposals to enhance both interim and long-term funding for the system. Their overarching goal is to ensure that the aged care system rests on a reliable, transparent, and equitable financial foundation compatible with universal entitlement to high-quality services. Specific recommendations include:

- Immediate funding to address the emergency in care quality, including better indexation of Commonwealth funding, an increase in the Basic Daily Fee for residential facilities, more support for providers in rural and remote areas, and immediate financial support for providers to cover training programs for existing and future workers.

- The Commissioners also recommended a restructuring of the system for financing capital investments in aged care facilities, to replace the existing model (based on Refundable Accommodation Deposits).

- Stronger Commonwealth funding for aged care providers must be accompanied by a strong regime of financial reporting, regulation and enforcement to hold providers accountable for the proper use of the public funding they receive – including new powers for prudential regulation to rest with the system governor.

- An independent pricing authority would set benchmark prices for various aged care services to serve as a guide for funding allocations. Those benchmarks must be consistent with the quality goals (including trained, professional staffing, and binding staffing ratios) identified in other recommendations.[7]

- The Commissioners provided two separate proposals for long-term funding arrangements which would enhance the fiscal foundation for aged care services. Commissioner Briggs advocated a 1 per cent Medicare-style levy to help fund enhancements in aged care (Volume 3B, Chapter 25). Commissioner Pagone proposed a hypothecated revenue stream, based on adjustments to personal income taxes, to provide a secure channel of regular funding to cover a share of all costs associated with aged care (Volume 3B, Chapter 20). These proposals are discussed further in Part IV of this report, along with other options for funding necessary improvements in the aged care system.

The Royal Commission has thus mapped out a holistic, ambitious, and fundamentally humane vision for how Australia can and must provide high-quality care to every senior who needs it. The existing patchwork system of public subsidies, unaccountable private provision, deregulation, inadequate enforcement of standards, and an aged care workforce treated as a just-in-time input (rather than a vital asset to be nurtured and developed) is failing Australian seniors and wasting public resources. The Commissioners' recommendations in the area of workforce and staffing are especially urgent: mandated staffing ratios and skill mix, guarantees regarding training and capacity, and the registration and regulation of care workers will all help to transform employment in this vital sector of our economy into an attractive, rewarding careers – rather than insecure, undervalued jobs (or, worse yet, gigs). The priority for the Commonwealth government now – starting with its upcoming budget – must be to start making this hopeful vision a reality.

[7] The Commissioners' recommendations regarding 'unit prices' need to be refined in light of the negative experience of other caring services organised on a similar model – most notably the NDIS. See Baines et al. (2019) for a detailed investigation of the negative consequences of unit pricing and market delivery for the quality of disability service work.

II. The Economic and Social Importance of Aged Care Services

The delivery of aged care services is a large and vital industry, that plays an important and positive role in Australia's economy. It is not a 'cost item' for governments to minimise. Rather, it is an important source of employment and income, that adds greatly to Australia's GDP and labour market performance. It even generates significant revenues for government, directly and indirectly, as a result of the salaries paid and economic injections associated with the industry. All this, of course, is on top of the most important benefit of the system: namely, the opportunity to serve elderly Australians with top-quality care, provided with dignity and professionalism, in the last years of their lives.

Table 2 summarises just some of the major indicators of the economic importance of the aged care sector, compiled from various sources considered and discussed in more detail below. Existing categories established by the ABS and other data sources do not allow a precise statistical description of aged care (due to distinctions between residential and home care services, between aged care and other residential services, and other overlapping categories). But Table 2 provides a reasonable overview of the sector's overall economic footprint.

Table 2
Economic Dimensions of the Aged Care Sector

Total Revenues	$27 billion
Value-Added (GDP)	$22 billion
Employment	400,000
Wages and Salaries Paid	$20 billion
Income Tax Paid[1]	$3 billion
Consumer Spending Supported	$15 billion
Supply Chain Purchases	$5 billion

Source: Authors' compilation and estimates from ABS (various), National Institute for Labour Studies (2020), Aged Care Financing Authority (2020), Royal Commission into Aged Care Quality and Safety (2021).

1. Based on Australia's average personal income tax ratio.

The spillover and indirect economic benefits of aged care services are significant and wide-ranging, and should be taken into account when considering the costs and benefits of increased financial support for the sector. The industry employs 400,000 workers, representing over 3 per cent of total employment in Australia. Those workers receive a total of around $20 billion in wages and salaries. Despite the unduly low level of average compensation in the sector (a problem discussed further below), this constitutes a very important flow of household income. Aged care workers then spend that income: indeed, because of low average compensation levels, personal savings among aged care workers are low, so virtually all of their compensation is reinjected back into the economy (either in income and other taxes paid back to government, or in consumer spending on all the goods and services they and their families purchase). Aged care providers (both residential facilities and home care and support services) also inject billions of dollars per year in demand for various inputs, materials, supplies and services – purchased from a long and complex supply chain that reaches across Australia.

Through all these linkages, therefore, the provision of aged care services provides an important boost to national economic and employment performance. The core purpose of the sector, of course, is to provide aged Australians with essential care and support when they need it. That is ample motivation for society to invest the resources needed to deliver high-quality, accessible aged care. But there are also important economic benefits which arise from those investments, including:

- Direct employment and incomes for people working in the sector.
- Indirect business activity and employment in the supply chain which sells inputs and services to aged care providers.
- Higher consumer spending thanks to the purchasing power of people employed in the aged care sector (and the supply chain which services it).
- Tax revenues recouped by government through income tax, GST, and company tax arising from all this activity.
- Enhanced economic and social inclusion and stability arising from Australians' confidence that they will be well cared for as they age.

The expression of social solidarity represented by a commitment to universal, needs-based aged care services – as envisioned so powerfully by the Royal Commission – will itself have important and far-reaching economic consequences. The growing economic literature on the value of social capital and trust[8] highlights the importance of security and inclusion to individuals' lifelong economic behaviour and decisions. People who fear constantly about their future, and face reasonable risk of being denied the basic requirements of life – including, in this case, the risk of ending their lives in poverty without access to basic caring services – will behave differently, and experience documented incidence of numerous health and economic problems. This, in turn, poses significant costs on the rest of society – including fiscal costs arising from physical and mental disease, and other problems. In this regard, assuring all Australians that they will be well cared for as they age, makes a meaningful contribution to their economic and social well-being throughout their lives.

THE AGED CARE WORKFORCE

The provision of aged care services is a major source of employment in Australia. According to the most recent National Aged Care Workforce Census and Survey conducted in 2016 (and reported in National Institute of Labour Studies, 2017), close to 400,000 Australians were employed in the sector: 366,000 as waged employees, and another 28,000 as agency workers, contractors, and self-employed. The allocation of the existing waged workforce between residential care facilities (which account for almost two-thirds of all jobs in the sector) and home care and support services is summarised in Table 3. Similarly, about two-thirds of all workers perform direct care roles, with the remaining third in a wide range of administrative and support functions. Counting contractors, the aged care sector makes up round 3.5 per cent of total employment in Australia in 2016.

Table 3
The Aged Care Workforce, 2016

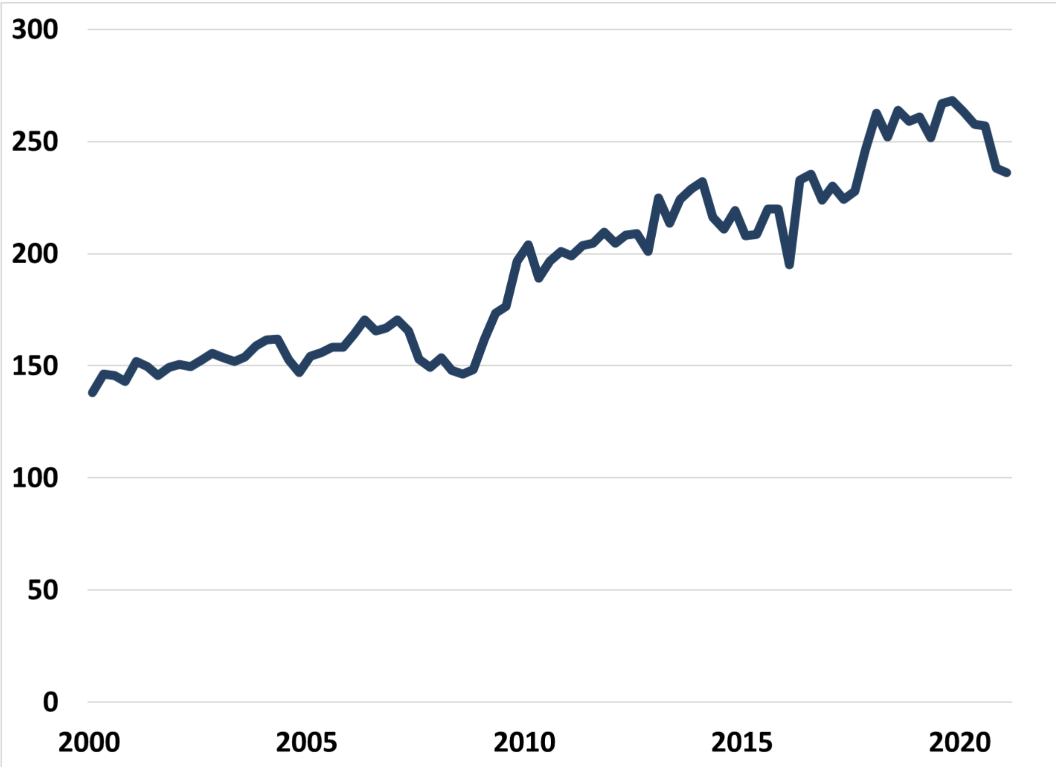
	Residential Care	Home Care and Support	Total
Total	235,764	130,263	366,027
Direct Care Providers	153,854	86,463	240,317
Others	81,910	43,800	125,710

Source: Authors' calculations from National Institute of Labour Studies (2017). Includes waged (pay-as-you-go) employees only.

[8] Reviewed and summarised, for example, by Pickett and Wilkinson (2009), Christoforou and David (2014), and Field (2017).

For comparison purposes, therefore, aged care employment is considerably larger than other sectors which capture far more attention from policy-makers. For example, there were almost twice as many aged care workers in 2016 than total employment in the mining industry (under 220,000) that year, much more than the entire agriculture industry (265,000), and almost twice as many as worked in finance (210,000).[9] Aged care should thus be seen as a major driver of Australia's economic and employment performance – not just a 'cost item' for governments to worry about at budget time.

Figure 1. Employment in Residential Care Services.



Source: ABS Detailed Labour Force Statistics.

ABS statistics allow us to provide a more detailed and up-to-date disaggregation of employment in the residential care segment of the overall aged care sector.[10] As noted above, residential care encompasses about two-thirds of all jobs in aged care. As illustrated in Figure 1, employment in residential care grew substantially over the last dozen years: adding over 100,000 new positions since 2008 – an annual rate of job-growth of over 5 per cent per year. This rapid growth accentuated the challenges facing the industry in recruitment and retention of qualified staff. Like other industries

[9] Authors' calculations from ABS Detailed Labour Force Statistics.

[10] The ABS category 'Residential Care Services' also captures employment in non-aged-care residential service facilities, but most of these jobs are in aged care facilities.

in Australia, employment in residential care declined significantly, but temporarily, during the COVID-19 pandemic, with over 25,000 jobs disappearing between February 2020 and February 2021.

A further breakdown of ABS data for employment in the residential care sector is provided in Table 4, which reports employment for males and females, and full-time workers and part-timers. We consider data for 1985 (when the ABS began to collect this data) through to 2020 (before the pandemic disrupted employment statistics). We also present data for 2008, just before the sector embarked on the strong employment growth experienced in the last 12 years.

Table 4
Composition of Residential Care Employment

	Total Employment (000)	Share Male	Share Female	Share Full-Time	Share Part-time
1985	110.4	23.0%	77.0%	72.3%	27.7%
2008	149.1	11.6%	88.4%	44.9%	55.1%
2020	254.0	16.3%	83.7%	43.4%	56.6%

Source: Authors' calculations from ABS Detailed Labour Force Statistics.

Residential aged care workers are predominantly female: women make up 84 per cent of the workforce. In fact, aged care has become even more feminized over the last generation. In 1985, men accounted for close to one-quarter of aged care workers; today they account for just one in six. Aged care is thus similar to other human and caring service industries (such as disability services and early childhood education and care) in having a highly feminised workforce. And the steady expansion of caring services ensures that women care workers will play an ever-larger role in Australia’s overall labour market in coming years. Human and caring services sectors depend vitlly on a highly feminised, and painfully undervalued, workforce. Lifting the standards of work and care in these sectors will be vital: both for improving the jobs of hundreds of thousands of low-paid women, and ensuring that customers and clients receive the very best care possible.

Table 4 also reveals a growing reliance on part-time work in the aged care sector. In 1985 just over one-quarter of jobs were part-time. Today over half of all jobs in residential care services are part-time. Part-time work is especially common among women: almost 60 per cent of women in the sector work part-time. The heavy dependence on part-time roles, many with inadequate or irregular hours, clearly contributes to the problems of staff retention and turnover, and the absence of defined career paths. During the pandemic, this chronic job insecurity also exacerbated the risks facing aged Australians from COVID-19: many part-time aged care workers work in two or three different part-time jobs at different workplaces. This pattern of multiple job-holding obviously enhanced the risks of spreading contagion.

Chronic job insecurity contributes to the stress and health risks associated with working in this sector. As Sherwood (2012) aptly summed up, aged care is “one of the most stressful industries to work in, with research finding that aged-care workers tend to work longer hours, get paid less and report more cases of work-related stress, depression and anxiety compared with other professions.” This makes it all the more unfair and unsustainable that the sector increasingly relies on less qualified, poorly paid personal care workers, in precarious, insecure jobs.

Table 5

Median Earnings, Direct Care Workers, Residential Care, 2016

	Hours Worked per Week				
	5-15	**16-34**	**35-40**	**Over 40**	**Total**
Nurse Practitioner	na				1000
Registered Nurse	525	1050	1493	1600	1352
Enrolled Nurse	355	800	1050	1000	946
Personal Care Attdt.	389	689	860	850	750
Allied Health Pro.	340	692	969	942	820
Allied Health Asst.	310	627	855	868	750
All Occup’ns	400	709	940	1000	800

Source: National Institute for Labour Studies (2017).

Data regarding earnings in aged care confirm the relatively low level of incomes paid to aged care workers – another key concern raised by the Royal Commission (see Table 5). Startling data on low incomes in the sector was provided by the National Aged Care Workforce Census and Survey in 2016 (National Institute of Labour Studies, 2017).

Across all occupations and working hours categories, median weekly earnings for the workers providing direct care in residential aged care facilities were just $800 per week. That was more than one-third below median weekly earnings across the Australian labour market that year ($1250 per week).[11] These workers are asked to provide the most vital and personal support to individuals in the last years of their life, in circumstances that are both physically and emotionally demanding – yet they are substantially undervalued by the current funding and staffing arrangements.

Additional insight into earnings in the aged care sector is also provided by the ABS publication *Australian Industry, 2018-19.*[12] This data covers only *private* residential aged care facilities.[13] The most recent data (for June 2019) indicate total employment of some 285,000 workers, and a total wages bill of $12.4 billion.[14] That implies an average annual salary for all workers in the sector (not just the direct care workers surveyed in Table 2) of just $43,600 – or around $835 per week. Again, that is substantially lower than average wages across Australia's economy.

For all private residential care facilities (including non-aged care facilities[15] and not-for-profit agencies), an occupational breakdown of employment in 2018-19 is provided in Table 6 below. This shows that medical staff (mostly nurses) account for just 14 per cent of total employment in private residential care facilities. Allied health, social and welfare professionals make up another 14 per cent. 42 per cent of total employment now consists of personal care assistants. The remaining staff include a wide range of other assistants, administrators, and other support staff.

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[11] From ABS Characteristics of Employment data.

[12] ABS (2020) *Australian Industry, 2018-19*, Cat No 8155.0, 29 May.

[13] In this case the data cover only aged care facilities; other forms of residential care are reported separately.

[14] Excluding superannuation and other labour costs.

[15] Aged care facilities account for 87 per cent of total employment in residential care facilities reported in this table.

Table 6 Employment by Occupation, Private Residential Care Workers, 2018-19		
	no.	%
Nursing staff	44,856	13.8
General medical practitioners	602	0.2
Personal care assistants	138,308	42.4
Allied health, social and welfare professionals:		
Physiotherapists	981	0.3
Occupational therapists	1,059	0.3
Speech pathologists and audiologists	146	0.04
Dietitians and nutritionists	75	0.02
Support coordinators	5,173	1.6
Social workers	3,374	1.0
Welfare support workers	7,777	2.4
Other medical, allied health, social & welfare	26,241	8.1
Total allied health, social and welfare professionals	44,826	13.8
Administrative and clerical workers, managers and professionals	36,898	11.3
Ancillary workers	36,806	11.3
Other staff nec	23,325	7.2
Total Employment	**326,069**	**100**
Source: ABS (2020) *Australian Industry, 2018-19*, Cat No 8155.0.		

We are also able to disaggregate employment data according to the size of the facilities involved. Those figures are reported in Table 7. They confirm the finding of the Royal Commission that there has been an ongoing concentration of residential care in larger facilities, which in turn have been consolidated into a small number of very large chains.

Table 7 Residential Care Employment and Revenue by Size of Entity				
Size of Enterprise	**Employment at end of June**	**per cent**	**Sales and service income**	**per cent**
Small (0–19 staff)	7,184	2.2	819	3.7
Medium (20–199 staff)	98,166	30.1	6,209	28.1
Large (200 or more staff)	220,719	67.7	15,075	68.2
TOTAL	326,069	100.0	22,102	100.0

Source: ABS (2020) *Australian Industry, 2018-19*, Cat No 8155.0.

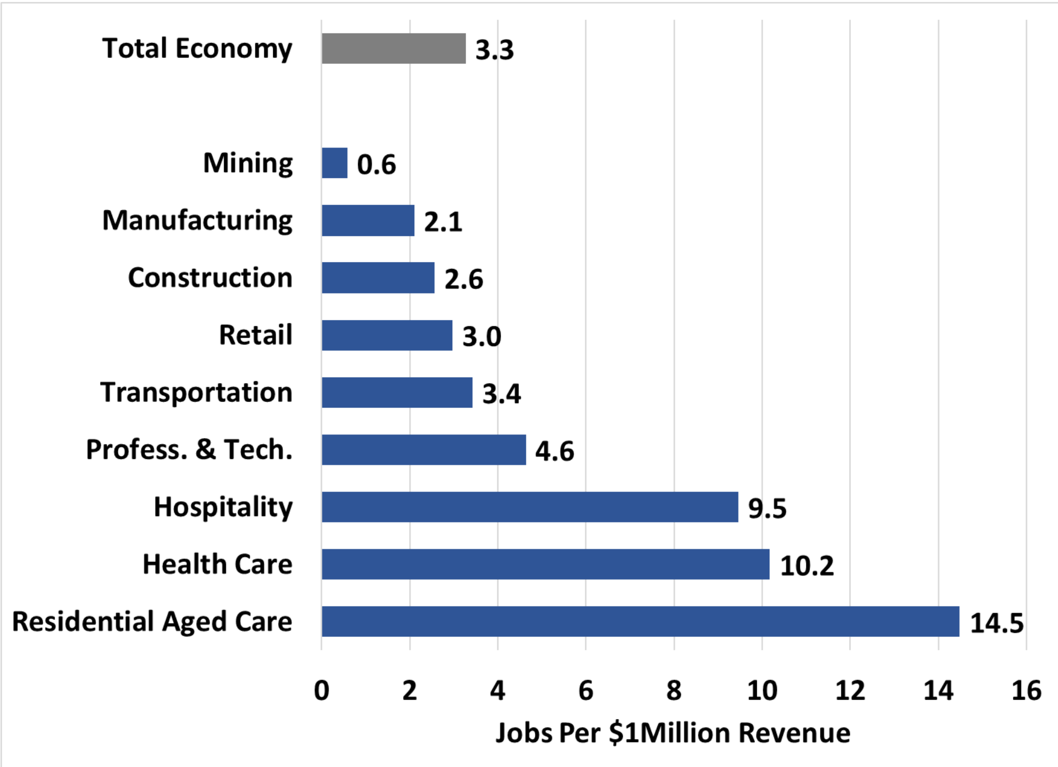
Table 7 shows that over two-thirds of residential care workers work in large facilities, with 200 or more staff.

To gain additional perspective on the changing occupational make-up of the aged care workforce, we attained unpublished information from the ABS. The results are presented in Table 8, which compares employment in the main occupational categories in 1991 and 2020.

Table 8 Residential Care Employment by Occupation				
	Feb-91 (000)	**Aug-20 (000)**	**Growth (% pa)**	**Change in Share Total (%)**
Managers	4.7	14.0	4.5	1.8%
Health professionals	49.5	51.7	0.2	-18.1%
Health and welfare support workers	10.7	11.9	0.4	-3.6%
Carers and aides	14.3	125.5	9.3	38.0%
Cleaners and laundry workers	11.5	8.8	-1.1	-5.5%
Other	38.3	43.8	0.6	-12.5%
Total	129.1	255.7	2.8	
Source: Author’s calculations from unpublished ABS data.				

Table 8 shows that overall employment in residential care grew at 2.8 per cent per annum over the three decades covered here. However, there are vast differences in the trajectory of different occupations. The absolute number of health professionals employed in the sector (mostly consisting of nurses) hardly changed during this period, despite the near-doubling of total employment. Thus their share in the total workforce was halved: from almost 40 per cent of workers in 1991 to just 20 per cent in 2020. The relative employment share of other health workers also fell significantly. In contrast, carers and aides grew dramatically as a share of the workforce: from 11 per cent in 1991 to almost half by 2020. This reflects the aggressive substitution of qualified and regulated health professionals with less qualified, lower-paid staff – driven in large part by the logic of cost-cutting, private profit, and fiscal austerity. The quality of those jobs, in turn, has been undermined by the use of precarious employment strategies, wage suppression, and inadequate training opportunities. The slow growth in other occupations, and the outright decline in cleaners and laundry workers, reflects contracting-out strategies which have also become dominant in the sector. Meanwhile, employment grew relatively quickly for managers over this period: that category increased its share of total employment by half.

Figure 2. Jobs Created per $Million of Revenues, 2018-19



Source: Author's calculations from ABS, Australian Industry, Catalogue 8155.0. Private sector providers only.

By all these indicators, it is clear that aged care is a large and important employer in Australia, and that its overall employment footprint has been growing (until the onset of the COVID-19 pandemic). In addition, the aged care industry is very labour intensive.

For example, every million dollars in revenue in residential aged care services translates into 14.7 jobs, compared with an average of only 3.3 jobs for every million dollars in revenue experienced in the broader Australian economy (see Figure 2).[16] A key priority of government economic policy as the economy continues to recover from the pandemic will be emphasising job-creation in all parts of Australia. Expanding aged care services is one of the very best ways to achieve that goal.

And while there are many motivations (including customer preferences and fiscal savings) for supporting aged Australians in their own homes for as long as is safe, the reality is that many elders eventually require some form of residential care late in their lives. Thus the demand for residential services will continue to grow. Instead of seeing this as a 'cost pressure' that needs to be controlled, it should be understood as an economic opportunity: to provide a necessary service, to the highest quality standards, and employing well-paid well-trained people to provide that service.

THE AGED CARE SUPPLY CHAIN

In addition to its direct employment and service provision, the aged care sector also has a major impact on other parts of the Australian economy. It is important to appreciate that aged care is not a stand-alone activity that exists separately from the rest of the economic system. In this section, ABS data regarding the input-output structure of the economy is analysed to illustrate how other industries benefit from the activities of the aged care sector via its purchases of goods and services.

We begin in Table 9 by examining the various industries that supply inputs to aged care providers. The analysis is constrained by a lack of disaggregated ABS input-output data on aged care. The closest category published by the ABS is an industry group titled "residential care and social assistance services". Over half of this category (53 per cent) consists of residential care services for the elderly. Other activities included within the composite category include residential care for the disabled (9 per cent of the total) and other groups (including mental health and substance abuse residential services, at 8 per cent). That broad sector also includes social assistance and home care services, particularly for the elderly and disabled (14 per cent). Finally, another 16 per cent of the total sector consists of child care services.[17] This is a large and diverse sector, but in aggregate about two-thirds of this broad category consists of aged care services – delivered both in residential care facilities and through home care and other services.

[16] Author's calculations based on ABS (2020) *Australian Industry*, Cat no 8155.0, 29 May.

[17] Another one per cent is government consumption of fixed capital. The proportions here are for 2016-17 and are set out in ABS (2019) *Australian National Accounts: Input-Output Tables (Product Details) - 2016-17*, Cat No 5215.0.55.001, 15 November.

Table 9 Major Supply Industries to Residential Care and Social Assistance Services, 2017-18		
		Residential care and social assistance services purchases $m
Supply Chain Purchases		
1103	Dairy product manufacturing	527
1305	Clothing manufacturing	450
2502	Other manufactured products	496
3301	Wholesale trade	1,211
3901	Retail trade	497
6601	Rental and hiring services (except real estate)	405
6702	Non-residential property operators and real estate services	833
6901	Professional, scientific and technical services	1,202
7210	Employment, travel agency and other administrative services	1,499
7310	Building cleaning, pest control and other support services	773
Sub-Total: Top 10 Supply Industries		7,893
Other Supply Industries		8,184
Total Supply Purchases		**16,077**
Other Income Flows		
P1	Compensation of employees	51,648
P2	Gross operating surplus & mixed income	3,681
P3	Taxes less subsidies on products	70
P4	Other taxes less subsidies on production	951
Australian Production		**72,427**
Gross Value Added **(P1+P2+P4)**		56,280
Source: ABS (2020) *Australian National Accounts: Input-Output Tables, 2017-18*, Cat No 5209.0.55.001.		

So it is reasonable to interpret the broad intersectoral relationships described here as representative of aged care services.

Most of the 114 industries measured by the ABS input-output system sell some output to this aggregate residential care and social services sector. From this list, Table 9 reports the 10 largest supply industries, each of which sells at least $400 million of output per year to the aged care (and related) industries. Table 8 also includes data for wage and non-wage incomes generated in the residential care and social services sector, and an indicator of its importance in Australia’s overall GDP.

The aged care sector purchases some $16 billion worth of supplies, machinery, inputs, and services from other parts of the economy. The ‘top ten’ supply sectors listed in Table 9 (each with sales of over $400 million to aged care customers) account for about half of that total ($8 billion). The full range of other goods- and services-producing businesses in the supply chain provide the remaining half. The largest individual supply-chain sectors are service providers like wholesale trade; professional, scientific and technical services; and various administrative services – each of which sells over $1 billion per year to the aged care sector.

In sum, the combined supply chain purchases of this sector amounted to close to 1 per cent of national GDP. And the supply chain linkages described in Table 9 do not include other important and valuable linkages: for example, aged care workers receive education and training services, which are not captured in this table.

Total value-added in this broad residential care and social services sector amounted to over $56 billion in 2017-18 – representing 3 per cent of Australia’s national output that year. Combined with the sector’s extensive supply chain, this confirms the industry has a significant and positive impact on national economic performance. By investing in the provision of high-quality aged care, we are not just fulfilling our responsibility to treat our elders with the respect and love they deserve. We are also expanding an industry which is a legitimate and valuable part of Australia’s economy.

It is interesting to examine the allocation of the sector’s value-added between the various contributing factors of production: including compensation for labour, profits (or operating surplus) for owners, and mixed-income for self-employed and small business. Most value-added (or industry GDP) is paid to workers, who received over 90 percent of the sector’s total value-added in wages, salaries, and other entitlements (such as superannuation). This reflects the labour-intensive nature of production in this industry (noted above), as well as the important role played by public and non-profit providers (which means that profit payments are relatively smaller than in other parts of Australia’s economy).

We have also reviewed the evolution of the major input-output relationships demonstrated by the aged care sector. Over the past 15 years[18] there has been relatively little change in the fundamental structure of the industry's purchases and payments. The data indicate a gradual increase in purchases of (outsourced) services of various kinds (including business, cleaning, food, and administration), and also a decline (by half) in the proportion of total output paid in profit. The small and declining share of private profit in the industry's overall business model is testimony to the incompatibility of the private profit motive with delivery of vital human and caring services. For-profit providers play a large role in this sector (accounting for over 40 per cent of spaces in residential aged care, and over 20 per cent of customers served through home care[19]). As documented and exposed by the Royal Commission, the quality of care provided in for-profit facilities is consistently inferior. Yet even from the perspective of investors and owners, this is a relatively unrewarding industry – despite the avoidable hardship imposed by for-profit delivery models on both workers and participants.

This finding is confirmed by data from the ATO, which reports a relatively small profit margin among private residential care providers: $676 million in total operating profit across some 860 private firms in 2018-19.[20] Similarly, according to the ABS *Australian Industry* reports, the private aged residential care services industry[21] generated combined operating profit of $906 million in 2018-19, less than 5 per cent of total revenues. The thin profit margins in private facilities reflect the fundamentally inappropriate nature of private services delivery for a population that, more often than not, has very limited personal resources, in the context of chronic underfunding and fiscal restraint from government. This only reinforces the inherent tendency of private providers to cut costs, downgrade labour and staffing, and cut corners – producing the unacceptable quality outcomes documented by the Royal Commission. All of this confirms that the provision of this vital service is best organised through well-funded, well-regulated public and not-for-profit agencies.

Finally, the ABS input-output statistics also provide interesting insight into the ultimate use of these services. Of the total production of the residential care and social services sector, around one-third ($24 billion in 2017-18) was purchased (or paid for) by households as part of their final consumption expenditure. Two-thirds of total output

[18] The ABS commenced reporting on residential care and social services as a defined industry in its national accounts system in 2006-07, so that is as far back as this analysis can be extended.

[19] Aged Care Financing Authority (2020).

[20] See Australian Tax Office, Taxation and Superannuation Statistics, https://www.ato.gov.au/About-ATO/Research-and-statistics/Tax-and-superannuation-statistics/.

[21] In this case the data on 'private' providers also includes not-for-profit agencies.

(some $48 billion) was paid for by government, on behalf of individual residents. A small share of total output of residential care and social assistance services (under $1 billion) is purchased as an input by the health care services sector. This affirms the leading role of government in providing these vital services – and if the Royal Commission's recommendation for the establishment of a universal needs-based entitlement to aged care is fulfilled, that leading role will be expanded further.

A PACT BETWEEN GENERATIONS

Every society needs some sort of arrangement for aged care: that is, for supporting and caring for its elders when they are no longer able to work and produce. As Doughney and King (2006) stressed, those arrangements may be organised through a range of monetary, market, or direct approaches, such as:

- Charity.
- Personal savings (such as superannuation).
- Family care and support.
- State provision of incomes or in-kind services.

In every case, what is 'consumed' by seniors today (in actual food, clothing, shelter, and care) represents an allotment shared from the output of goods and services produced in the economy today. Importantly, this is true whether aged care services are 'pre-funded' (through individual savings or some kind of pre-funded social insurance system) or supported more directly out of current incomes (such as government current revenues or family current incomes). Either way, seniors are supported by the real labour performed by other Australians today – and the amount that other Australians consume today must be reduced by an amount reflecting the current output which we provide to our elders.

In this context, provision of aged care can be seen as a pact between generations. Seniors supported their children and grandchildren by working, paying taxes, raising families, and allowing us (individually and collectively) to develop our economic and social well-being. We are much better off thanks to their work, savings, and sacrifice. Now, in return, we repay that support by caring for them. Yes, that means allocating a share of current output – a small share, as discussed below – to providing them with top-quality care and security, in large part facilitated through the system of taxes and government spending. That is simply a modern reflection of the similar intergenerational pacts which underpinned elder care in previous generations and societies.

This pact between generations must also reflect a pact of solidarity between Australians of different socio-economic status. If aged care is delivered through the 'market', it is inevitable that quality care will only be available to better-off families that can afford it. For most Australians, who struggle to pay their monthly bills from wage packets that have been stagnant for years, the prospect of undertaking voluntary personal saving to finance future aged care expenses is utopian. Ironically, many aged care workers themselves, who earn well under average weekly earnings, fall into this category: their wages are too low to pay for (among many other unmet needs) private provision of aged care for themselves or their loved ones. Surely these workers who provide dedicated work in aged care facilities today, deserve to be confident that they, too, will be taken care of with dignity and quality when they need it.

Consumption by the elderly is provided out of current production, and that requires somehow limiting the claims of the working-age population on current output. This is true even in a self-funded model, dependent on savings – like the superannuation system. While expenditure by superannuants is paid for from a fund accumulated during their working lives, this does not imply there are no costs to the rest of the community, including the current working population. Even in this system they must forego some of the production which they could otherwise consume. Financially, those adjustments are mediated through taxes, changes in asset prices, and/or changes in consumer prices. One way or another, what seniors consume today is obtained from what workers produce today. And that is how it should be.

It is often argued that seniors are entitled to assistance in their old age because they paid taxes through their working lives. This is another expression of that intergenerational pact underpinning the aged care system. The Royal Commission expressed such a view when it said:

> "The Australian community generally accepts that older people have earned the chance to enjoy their later years, after many decades of contribution and hard work. Yet the language of public discourse is not respectful towards older people. Rather, it is about burden, encumbrance, obligation and whether taxpayers can afford to pay for the dependence of older people." (Royal Commission on Aged Care Quality and Safety, 2019, p. 1)

We do not think these sentiments are just platitudes. This intergenerational pact has real economic meaning. It reflects a social commitment that runs deeper than market transactions and financial flows.

The Nobel economist Paul Samuelson developed a model of social security arrangements to show that an efficient intergenerational allocation of income is achieved if each generation of income earners supports its retired population.[22] Economists understand this pact as a replacement for a ‘market’ that cannot exit. While the present generation of income earners can support present retirees, there is no market in which a compensating transfer or ‘payment’ can be directed from future generations of workers to the working age population. The present generation of income earners can provide income for today’s retirees, but the latter have nothing to give in return. Likewise, there is no way the present working population can make a market ‘deal’ with the next generation to obtain a similar guarantee: many future workers are not even born yet, so current income earners cannot make ‘deals’ with future wage-earners. In the absence of being able to strike such deals over time, even conventional market-oriented economists acknowledge we instead need a social and political intergenerational pact, that can only be underwritten by the government. In other words, only government can complete this absent ‘market’ by enforcing implicit guarantees on the part of future generations. Through government taxation and spending, today’s workers support today’s elders us with care and income support – and they, in turn, will be supported by a future generation of workers when it is their time.

Aged care also has an insurance dimension since not everyone will need it, but for some it will be essential. That consideration also argues for collective provision, since market mechanisms never provide satisfactory solutions to broad needs for social insurance (due to uncertainty and imperfect information, high administration costs, perverse selection effects, and other problems). The insurance aspect of aged care is apparent to the extent that contributors are considered as making an implicit ‘exchange’ with government, paying taxes today in exchange for a commitment that the government will collect taxes from future generations to finance their care if they need it. With government playing that role in organising and guaranteeing the system, the accumulation of a fund (as proposed in a social insurance model of aged care) is unnecessary. Current taxes are exchanged for an expectation that the system will be maintained over time. Ultimately the continued flow of these benefits is dependent on the willingness of yet-unborn generations to similarly tax themselves.

In summary, there is a real economic foundation to the ethical willingness of Australians to provide top-quality care to our elders. Providing that care through a universal, needs-based system, funded generously from current tax collections, reflects an economic pact between generations that serves an essential and productive economic purpose. Caring for elders (like caring for others who need it, like children or

[22] Samuelson (1958).

people with disability) cannot be adequately arranged through market transactions. It requires the power and foresight of government to organize a system in which those who need care today have access to it – and those who will need care in the future can be confident they will receive it, too. That is a precondition for allowing every Australian to live their economic lives – making optimal decisions about education, work, home ownership, and other vital choices as they go – in a secure and efficient manner.

III. Australia’s Fiscal Capacity and Aged Care Services

Australia is one of the wealthiest countries in the world. Blessed with an abundance of natural resources, a skilled and educated workforce, a very successful and profitable business sector, and strong trading relationships with other countries, our output and income levels (measured by indicators such as GDP produced per capita) rank in the very top tier of industrial countries. Moreover, our governments and public institutions possess a powerful and flexible array of fiscal and revenue tools with which to provide a network of vital services and programs to enhance the quality and security of life of Australians. This network is imperfect, and many programs (like aged care) have suffered needlessly from years of inadequate funding and attention from governments and providers. But these failures cannot convincingly be ascribed to a shortage of money or resources. To the contrary, Australia has enormous, untapped fiscal capacity with which to support the improvement and expansion of needed services – including, if we choose, implementing the Royal Commission’s agenda for improved quality and safety in aged care.

This section of the paper will review several broad indicators of the capacity of our economy and society, led by the Commonwealth government, to finance improvements in any public service deemed essential by our community. It documents that Australia has a relatively low and undeveloped base of public revenues compared to most other industrial countries, and that that revenue base has stagnated in recent years – lagging behind the growing demands of Australians for high-quality public services. Indeed, one reason why demand for public services tends to grow over time in industrial countries is precisely because of demographic ageing.[23] In that context, the collective decision to allocate more resources to meeting those needs is both efficient and desirable: collecting more taxes to fund more public and caring services is not a ‘burden,’ it is in fact an economically efficient response to public demand for more of those services.

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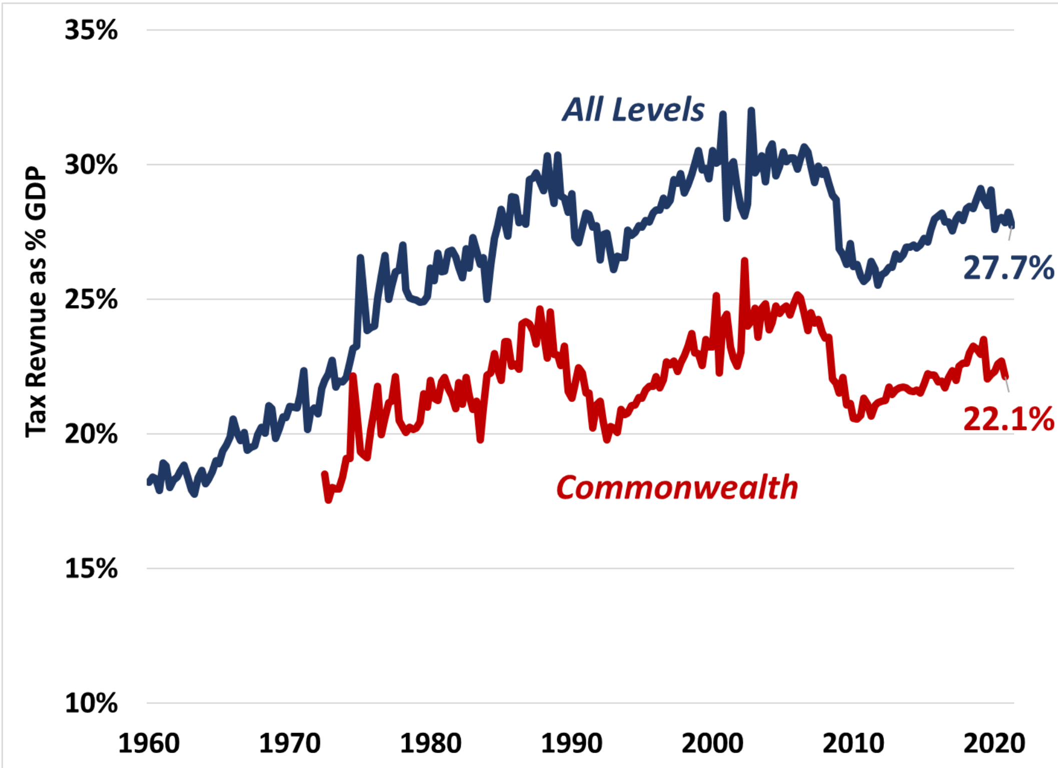
[23] There are other reasons, in addition to demographic factors, why demand for public services demonstrates a positive correlation with income levels over time. There is evidence that public services (like education, health, and others) is a superior good for which demand increases disproportionately with income (see Keating, 2018). In this context, arbitrary attempts to suppress the natural increase in the relative importance of public services over time, as exemplified by Australia’s bizarre ‘tax ceiling’ of 23.9 per cent of GDP, are doomed to failure; see Richardson and Browne (2018).

TAXES IN HISTORIC AND INTERNATIONAL PERSPECTIVE

The common complaints that taxes in Australia are 'too high' or 'getting higher' is disproven by basic fiscal data, measured both over time and across international comparisons. Figure 3 illustrates the trend in total tax revenues (for all levels of government, and for the Commonwealth alone) dating back to 1960, measured relative to GDP.[24] Aggregate taxes grew markedly during the initial postwar decades, as Australia expanded (and financed) the major expansion in public services and income supports achieved during that era. Not coincidentally, that was also the period of the most vibrant and sustained economic growth and rising living standards in Australia's history. Far from 'stifling' economic growth and impoverishing Australians, the growth of taxes in the postwar era – and the programs they paid for – supplemented Australians' standard of living (with a robust 'social wage') and reinforced strong macroeconomic conditions.

Figure 3. Tax Revenues as Share of GDP, 1960-2020



Authors' calculations from ABS National Income Accounts, Tables 3, 17 and 18. Includes taxes on production (GST), imports, income, and wealth.

[24] The disaggregation by level is unavailable prior to 1972.

Since the latter 1980s, however, that gradual trend of rising taxes stopped – despite the apparent continued growth of public demands for high-quality public services (including programs for our growing population of seniors). Aggregate tax ratios have fluctuated with macroeconomic conditions: falling in the recession of the early 1990s and the GFC in 2009-2010, rising through the sustained expansion of the 2000s. More recently, overall tax inflows have declined relative to GDP during the COVID-19 pandemic and resulting recession.

But within that cyclical pattern, the long-run level of taxes has stagnated or even declined slightly, In 2020, the Commonwealth government took in approximately 22 per cent of national GDP in tax revenues; under 6 percent was collected by lower levels of government.[25] Combined tax collections in 2020 were about one-half per cent of GDP less than the average aggregate tax ratios over the past 30 years.

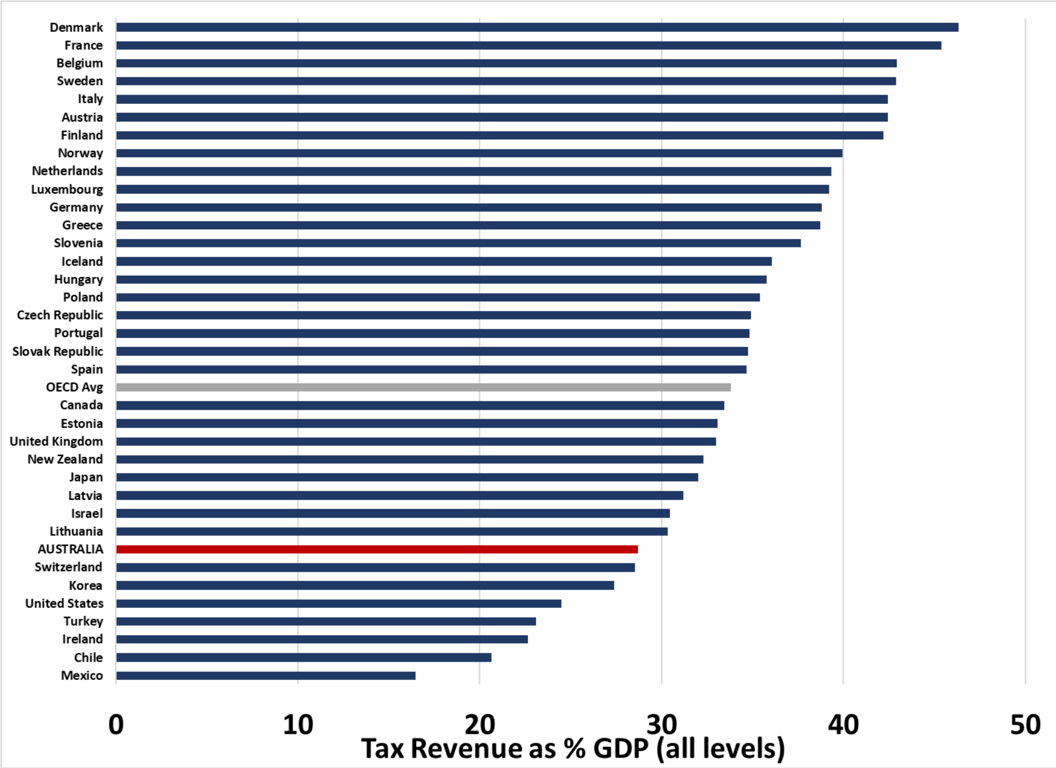
Some political leaders and business commentators, motivated by an ideological desire to constrain the role of government, have argued this level of taxes should not go any higher. More specifically, the current Commonwealth government has stated a bizarre commitment to keeping aggregate Commonwealth taxes below 23.9 per cent of GDP.[26] But this reflects their values and political priorities, not any economic rationale. Emerging economic and social priorities – including the need to improve care for Australia's aged population – clearly justify an increase in tax collections, so long as Australians support that choice. The allocation of current production between private individual uses and social or collective uses (such as public and human services) is wholly dependent on the preferences of society, not on any supposedly immutable economic 'laws.'

The relatively modest level of taxes in Australia's economy is also apparent through the lens of international comparisons. Figure 4 indicates the proportion of GDP collected in taxes (by all levels of government) in the industrial countries that make up the OECD. Australia has the seventh smallest tax base relative to GDP of the 36 OECD countries. We thus fall in the lowest fifth of industrial countries, with an aggregate tax base about 5 percentage points of GDP below the OECD average.

[25] These statistics, based on national accounts data, differ slightly from those reported in public accounts data (such as Appendix D to the Commonwealth budget) due to different definitions and treatment of accruals, but the historical pattern is similar.

[26] See Richardson and Browne (2018).

Figure 4. Tax Revenue as Share GDP, 2019 or Latest



Source: Authors' calculations from OECD Tax Statistics. All levels of government.

Moreover, Australia is one only a few OECD countries in which the aggregate tax ratio has *declined* since the turn of the century. Most other countries have increased their aggregate tax ratios during this period, for various reasons: reducing deficits, meeting new demands for public and social programs, or redistributing income in the face of growing economic inequality. On average, the aggregate tax ratio increased by 0.5 percentage points of GDP across the OECD between 2000 and 2019. In Australia, in contrast, it fell by some 1.8 percentage points. While Australia has long been one of the lowest-taxing industrial countries in the world, therefore, our ranking on that score is falling even further over time.

Some might celebrate the relatively low level of taxes in Australia as a sign of 'prosperity.' Unfortunately, there is another side to the coin: this underdeveloped fiscal capacity inevitably translates into relatively poor public services. This poor level of service is painfully visible in aged care, among other public and human services. The Royal Commission documented that Australia's support for aged care services is much smaller (relative to GDP) than in many other industrial countries.[27] Its research also

[27] See, for example, the evidence in Rehabilitation, Aged and Extended Care Group et al. (2020), Research Paper #2 published by the Royal Commission.

documents a clear correlation between the level of taxation in various industrial countries, and the level of aged care provided: quality and funding standards are highest in high-tax jurisdictions (like the Nordic countries), and lowest in lower-tax countries (most notably the U.S.). There is no doubt that chronic public underfunding of aged care services has contributed to the shocking failures that were documented by the Royal Commission. Repairing that damage, and preventing similar neglect and abuse in the future, will clearly require measures to enhance the fiscal foundation for aged care services. We face a fundamental choice as a society in determining whether our infatuation with 'competitive taxes' outweighs our commitment to top-quality care for our elders.[28]

STARVING THE BEAST

Throughout the austere economic and fiscal policies that have dominated policy over most of the last generation, the goal of suppressing and reducing taxes has been a central priority among conservative commentators and policy-makers. Part of their support for tax cuts ultimately stems from their effect in creating an apparent need to control government spending, in order to reduce the deficit that results from tax cuts. Far from being committed to eliminating deficits (as often claimed), this conservative approach actually *creates* deficits as part of a strategy to win support for resulting spending cuts – which otherwise would be resisted by voters. Those seeking to downsize government programs can avoid head-on confrontations with citizens concerned about the erosion of public services, by portraying spending cuts as an inevitable part of fiscally responsible budget management.

This approach, often called 'starving the beast,' aims to reduce revenue so that policy makers will eventually see the need to cut spending. Nobel economist Paul Krugman (2010) put it this way:

> "Rather than proposing unpopular spending cuts, [conservatives] would push through popular tax cuts, with the deliberate intention of worsening the government's fiscal position. Spending cuts could then be sold as a necessity rather than a choice, the only way to eliminate an unsustainable budget deficit."

[28] In this regard, the level of taxes is an important channel through which the 'generational pact' discussed above is effected in a modern economy: a share of the real current output of today's economy is allocated to caring for aged Australians, and the tax system is a crucial mechanism through which most of that transfer occurs.

Of course, U.S. President Donald Trump did exactly this early in his term, with massive tax cuts for corporations and high-income households causing an enormous federal budget deficit – unprecedented in non-recessionary times.[29] That deficit grew much larger still when the COVID-19 pandemic struck. Republicans tolerated that deficit when it was the result of tax cuts. But now they have suddenly shifted ground and begun to emphasize the necessity of reducing the deficit – as an excuse to limit or reduce government support for Americans affected by the pandemic and resulting recession.

Australian conservatives have pursued similar strategies, and this helps to explain why Australia's overall government revenue base has stagnated and eroded (and much smaller than other industrial countries), despite glaring needs for improvements in important public services and infrastructure. Tax cuts implemented during the Howard government during the expansionary 2000s set the stage for budget deficits when the economy slowed down – seemingly reinforcing the argument for spending cuts. And in the wake of inadequate funding, many public services take on a chaotic appearance, further reinforcing the arguments of downsizers and privatisers. For example, the audit report established following the election of the Coalition Government in 2013 urged government to vacate any service delivery or other activity that could be operated by the private sector. Given this stated ideological belief that 'private is best', it is not surprising that the share of private for-profit providers has continued to grow in aged care (and other human service sectors), despite the documented negative impacts of private provision on quality and safety. Meanwhile, the fiscal noose around public service delivery has been tightened further by repeated cuts in personal and company taxes implemented by the Coalition government since then.

DEFICITS AND DEBT IN CONTEXT

The emergence of very large deficits as a result of the COVID-19 pandemic and recession has added an extra degree of drama to ongoing fiscal debates. Even though their own tax cuts significantly weakened the fiscal base of government (and thus exacerbated COVID-era deficits), conservatives are now seizing on those deficits to justify restraint in government program spending. Already we have seen important public programs and supports (like JobKeeper subsidies and the Coronavirus Supplement for unemployed workers) eliminated in the name of deficit reduction[30] –

[29] See discussion in Richardson (2017).

[30] Those programs were not adequately structured or monitored, either, with the result that some needed funds were denied for significant segments of the workforce (including short-tenure casual staff), some employers did not pass JobKeeper subsidies onto qualifying staff, and some private firms even effectively used the subsidies to pad their payouts of dividends and executive bonuses.

even though continued uncertainty about future outbreaks of COVID, delays in vaccine distribution, and other risks still very much cloud the economic horizon. These large deficits will certainly be invoked by those who would reject the Royal Commission's calls for urgent and comprehensive improvements in the aged care system.

The December Mid-year Economic and Fiscal Outlook (MYEFO) for 2020-21 projected an expected government deficit of $198 billion in 2020-21, equal to almost 10 per cent of GDP. Government debt was $491 billion or 25 per cent of GDP, and heading for $952 billion and 43 per cent of GDP by 2030. The cost to government of servicing this increased debt has been very modest, however, thanks to very low interest rates. Net interest payments by the Commonwealth government for 2021-22 are expected to rise by just $500 million compared to the previous year (to a total of $14.0 billion), equal to just 0.7 per cent of GDP.[31] Low interest rates will save the government $1.5 billion on refinancing older, more expensive borrowings over the next year, offsetting much of the increase in interest costs resulting from the larger debt (Cranston 2020).

Instead of elevating deficit reduction to the top of the list of priorities (especially given how inconsistently that goal has been advanced by conservatives in the past), a more balanced approach must be taken. This is especially vital at a moment when the well-being of Australians is threatened by unprecedented health, economic, and environmental risks. As Richardson (2011, p.18) puts it, "the fiscal balance should be decided by a pragmatic concern for government priorities and reaction to the needs of the economy and society." Even cautious international institutions such as the International Monetary Fund (2020) now make it clear that countries will need to maintain large fiscal deficits to protect public health and ensure economic recovery from the pandemic.

The Governor of the Reserve Bank of Australia, Philip Lowe, has also emphasised that the deficit is not the top priority for policy-makers:

> "We shouldn't be worried [about the debt]. [Spending] is the right thing to do... we have the capacity to borrow, our interest rates are as low as they've ever been, the Australian Government has a long record of responsible fiscal policy, so the budget accounts are in reasonable shape. And if ever there's a time to borrow, now is it." (Quoted in Speers, 2020).

Richardson (2021) also emphasises that "in a world of super-low interest rates," public debt is no longer the problem it once was. He cites data showing "that taxpayer debt is getting "cheaper" even faster than it is getting "bigger". The result is an interest bill

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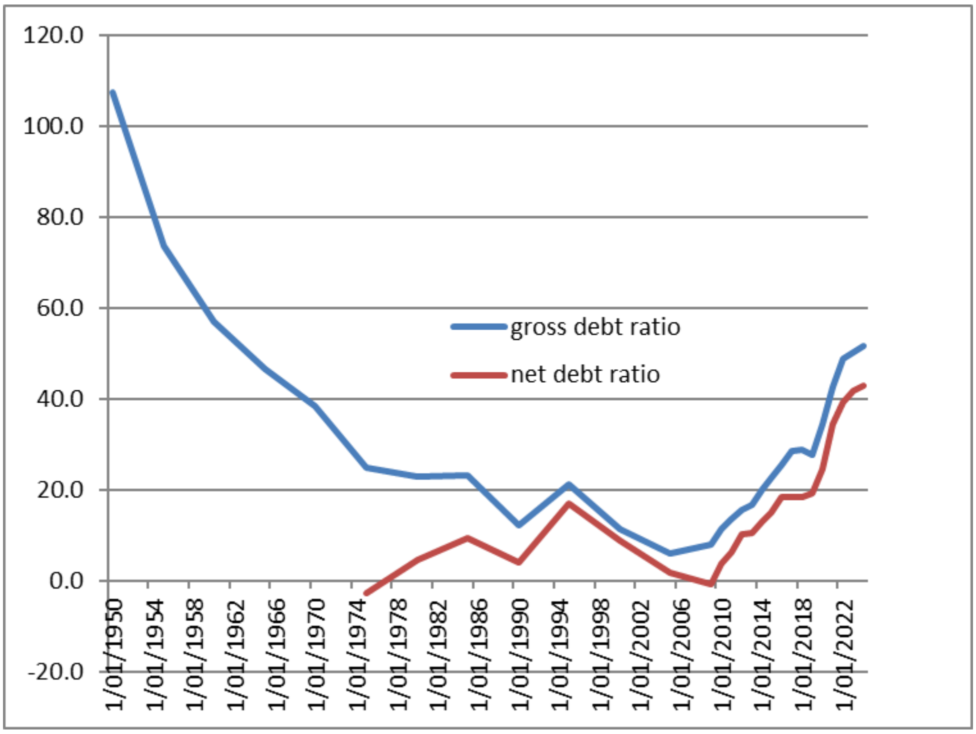
[31] See Treasury (2020), p. 53.

that is still falling – just not as fast as it was forecast to do pre-COVID. Richardson makes it clear that normally he would be a debt worrier, but that “the collapse in interest rates has given governments more room to move.”

In considering the level of government debt it is always instructive to compare Australia’s position compared with its own history, as well as the contemporary experience of other economies. For example, the Commonwealth government’s debt was much higher on the eve of Australia’s postwar golden age. In 1950, government debt was 107 per cent of GDP (Reserve Bank of Australia, 1997). That would be approximately $2,080 billion as a percentage of today’s GDP. Figure 5 illustrates Australia’s gross government debt to income ratio from 1950 to 2020, together with net debt from 1975 onwards. Also included are projections and forecasts through to June 2024. Note that earlier figures for the Commonwealth gross debt include some borrowings on behalf of the States and Territories.

Figure x. Net and gross debt as share of GDP %.



Source: Reserve Bank of Australia (1997); ABS (2020) and Australian Government (2020) *Mid-year economic and fiscal statement*.

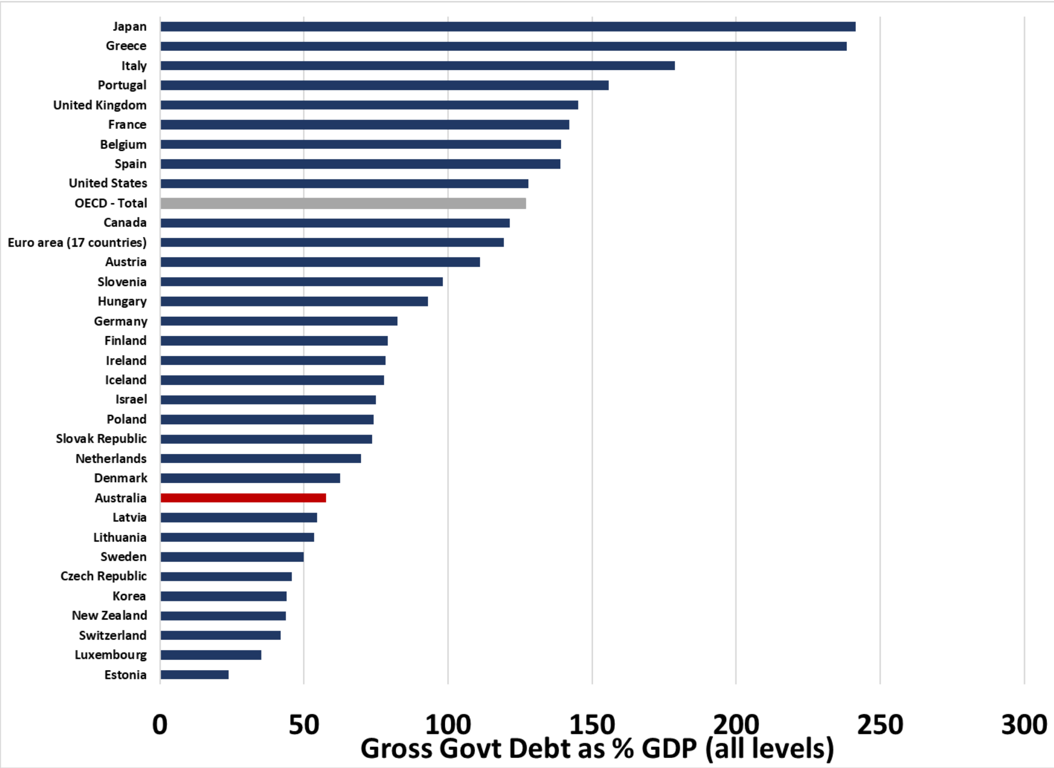
As can be appreciated from Figure 5, Australia’s gross debt to GDP ratio in mid-2021 will be 42.5 per cent and the net debt ratio 34.5 percent.[32] Australia’s debt declined substantially over the course of the postwar period. In net terms, Commonwealth debt

[32] Net Commonwealth debt is gross debt less financial assets held by the Commonwealth.

actually disappeared in 2005–06, and then reappeared in 2009–10 with the global financial crisis. In historical terms, Australia's present debt is moderate despite large COVID deficits.

Australian government debt is also very low compared with other developed economies. Figure 6 shows Australia's recent gross government debt compared with other industrial countries, expressed as a ratio of debt to GDP using OECD data.

Figure 6. Gross Government Debt, Industrial Economies (% GDP) 2020



Source: OECD Economic Outlook database.

Australian gross public debt (over 50 per cent of GDP, counting state and Commonwealth) is less than half the average for all OECD countries (127 per cent of GDP). Even with the pandemic, Australia's debt to GDP ratio remains well below most other countries. With near-zero interest rates, with the Reserve Bank playing an active role (through its 'quantitative easing' strategies) in purchasing government bonds, and with an overarching need for further injections of government stimulus, it is clear that Australia's debt can and must continue to grow. This is appropriate given the economic circumstances which the country faces.

IV. Financing Options

EXISTING FISCAL SUPPORT FOR AGED AUSTRALIANS

Before addressing Australia's fiscal capacity to increase aged care spending, it is important to locate current spending within the broader envelope of fiscal assistance and support for aged Australians. Table 10 summarises recent budget estimates, including the major components of assistance to the aged as recorded in Commonwealth Budget Papers. It also includes major assistance for retirement provided through superannuation tax concessions: including preferential tax treatment of contributions, and lower tax rates on earnings generated within a superannuation fund.

Table 10
Fiscal Dimensions of Aged Policies ($m)

	2019-20 actual	2020-21	2021-22	2022-23	2023-24
Income support for seniors	50,104	53,549	51,425	53,089	54,977
Super tax concessions on contributions		21,000	23,250	23,800	25,250
Super tax concessions on fund earnings		22,150	22,550	24,000	24,900
Aged Care services	19,757	21,849	23,032	24,500	25,851
Veterans' community care and support	991	850	903	806	718
Aged care quality	236	688	231	227	224
Allowances, concessions and services for seniors	379	570	79	74	70
Other	1,379	480	317	249	249
Total		121,136	121,787	126,745	132,239
Share GDP %		6.21	6.05	6.02	5.98

Source: Australian Government 2020-21 Budget Paper No 1, 6 October.

Table 10 does not reflect the government's recent announcement of an additional 10,000 home care packages announced in conjunction with the 2020-21 MYEFO. Also excluded are some COVID-19 related payments to the aged care sector also announced in the MYEFO.

Commonwealth support for aged care services is budgeted at $21.8 billion in 2020-21. That needs to be put in the context of the total budgetary support for seniors and their welfare, estimated in Table 10 at $121.1 billion for the same year. That implies aged care accounts for less one one-fifth of total Commonwealth spending on seniors. It also implies that the estimated costs of necessary improvements to aged care services are also small relative to the overall fiscal support provided to seniors.

Table 10 also indicates that under current policy settings, the share of national output going to the elderly is set to decline somewhat from 6.2 per cent in 2020-21 to 6 per cent in 2023-24. Some fiscal support for the elderly (particularly subsidies to superannuation) can be volatile, as they depend on the earnings of the super funds which attract concessional taxation. This is important context for any consideration of the fiscal effects of implementing the Royal Commission recommendations.

There is a tendency among some policy and financial commentators to focus on fiscal payments by government as an indicator of a 'proclivity to spend'. However, the effective transfer of resources embodied in tax expenditures (such as superannuation concessions) must also be part of the discussion: they have the same bottom-line impact on the government's fiscal balance as an outright expenditure, and their social and economic effects are often both more opaque and more regressive than outright government spending. In this light, 'failure to properly tax' is at least as much of a problem as 'proclivity to spend'. In this regard, it is especially important to note that Commonwealth fiscal support for superannuation is more twice as much currently as its support for aged care services; and a disproportionate share of those tax concessions benefits high-income Australians.[33] This puts the fiscal implications of addressing the Royal Commission's recommendations into important context.

[33] In the case of superannuation tax concessions, for example, evidence indicates that over 40 per cent of the total value in superannuation tax treatment is received by the highest-income tenth of Australian households; see Grudnoff (2015).

CUTS IN AGED CARE SPENDING 2013-2017

In the 2013-14 Budget, Commonwealth aged care spending was budgeted to be $14,039 million for that year.[34] Federal support for aged care services has been significantly restrained in the years since then, and this has contributed importantly to the crisis in funding and quality that sparked the Royal Commission. We estimate the cumulative impact of fiscal restraint imposed since 2013 in the following manner. When changes are made to previously-announced programs, they are recorded in annual budget documents, with the value of the year immediately preceding the budget compared to the budget year and three more years (the forward estimates). The last year of this estimate is likely to provide the best estimate of the ultimate and ongoing impact of a particular policy change. Note that this estimate is not adjusted for subsequent population or price impacts.

On this basis, we estimate that expenditure restraint announced since 2013 has reduced ongoing aged care expenses by an annual total of over $1.5 billion (see Table 11), a reduction of 11 per cent compared to initial spending in 2013.[35] Nevertheless, with all our qualifications in mind we can present the following table to show the pattern of cuts associated with the change in government in 2013.

Table 11
Cuts to aged care in various budgets ($ million)

	Annual Cut[1] ($m)
2014-15 Budget	-270
2014-15 MYEFO	-14
2015-16 Budget	-57
2015-16 MYEFO	-719
2016-17 Budget	-464
Total	-1523

Source: Authors' compilation from Commonwealth Budget Papers, various years. 1. Estimated annual impact in last year of forward estimates.

[34] This figure includes the listed items Residential and flexible care, Veterans' community care and support, Home support, Home care, and National partnership payments – assistance to the aged. Australian Government (2013) *2013-14 Budget Paper No 1*.

[35] The estimate for 2016-17 is approximate, reflecting a budget measure titled "further revision of the Aged Care Funding Instrument." But there were other cuts to aged care spending (including measures associated with the introduction of the NDIS), but it is not clear whether they were real cuts, measures taken up by the states, or offset by other measures.

Subsequent to the 2016-17 budget, there have been several announcements of increased spending for aged care – including in the most recent MYEFO, which promised 10,000 additional home care packages and other incremental improvements. Those announcements, however, were to a large extent only offsetting the impact of earlier spending reductions. Of course, overall Commonwealth spending for aged care services has grown in nominal terms throughout this period (reaching close to $20 billion by 2019-20). The spending restraint reported in Table 9 represents a reduction in expenses that would have been incurred under previous policy settings. Nevertheless, the legacy of fiscal austerity imposed in the initial years of the Coalition government's present term are another critical part of the fiscal context for considering the Royal Commission's recommendations.

From a longer-term perspective, the cumulative impact of decades of fiscal restraint on funding for aged care services is much larger and more devastating than the evidence reported in Table 11. The Royal Commission itself estimated the cumulative impact of Commonwealth funding reductions since 1997 as amounting to $9.8 billion per year by the time of the 2018-19 budget.[36] Once again, this is crucial context for considering the fiscal requirements of improving aged care provision: it will take significant fiscal investments just to offset the damage of previous spending cuts, let alone to start to lift aged care to a higher quality standard.

HOW MUCH DO WE NEED?

The Royal Commission report did not explicitly cost its recommendations for improvements to aged care, including the important changes it proposed in working arrangements (including staffing ratios, training, and registration). It is obviously challenging to measure the anticipated increase in expenses arising from such a broad and complex array of reforms in precise dollar terms. But the Commission's report did refer broadly to the likely increment in total government funding that will be required to support the necessary reforms. For example, Volume 3 of the report indicated Australians should expect an increase in total government support for aged care of $10 billion per year or more.[37] And the broad order of magnitude of the anticipated increase in expenses needed to achieve a historic improvement in aged care quality[38] can also be gleaned from several different sources:

[36] Royal Commission into Aged Care Quality and Safety (2021), Volume 1, p. 13.

[37] See Royal Commission into Aged Care Quality and Safety (2021), Volume 3A, p. 62.

[38] While this section of the report focuses on the central role of increased budgetary resources to implement the Royal Commission's recommendations, we also emphasise that money alone cannot

- In its most recent *Intergenerational Report*, the Treasury Department projected an increase in total government funding for aged care (including both residential care and community and home-care service provision) measured as a share of Australian GDP: rising from around 1% in 2019-20 to 1.7% by 2054-55 (Treasury 2015, p. 71). That rise reflects the expected effects of demographic ageing on the demand for existing aged care services (not changes in policy or level and quality of service delivery). Note that this demographically-driven increase in aged care expenses (under existing policy settings) is well-understood, and has been considered already within the design of current fiscal policies. It is not a surprise, nor is it something that must be 'funded.'

- In initial research provided for the Royal Commission, Deloitte (2020) projected a less dramatic increase in baseline expected total government expenditures on aged care (including residential care, home care, CHSP and other services), reaching 1.34% of GDP by 2050. Deloitte also estimated the impact of three potential scenarios of improved aged care services (dubbed 3-star, 4-star, and 5-star) which would increase that baseline expenditure path by between 0.3% and 0.8% of GDP over a multi-year phase-in period.

- Research prepared by Duckett et al. (2020), before the Royal Commission issued its final report, suggested a required increase in federal funding of at least $7 billion per year – and that does not include the effects of population growth or wage increases (as the Commission eventually recommended).

- In his recommendation regarding potential sources of funding for improved aged care services, Commissioner Pagone (Royal Commission, 2021, Chapter 20, p. 767) cited results of additional simulations (adapting cost drivers from the Deloitte model) suggesting the impact of high-quality policy reforms could be higher: adding as much as 1.4% of GDP to future annual expenditures. This is higher than estimated by other sources,[39] and until verified by additional cost studies should be considered an upper bound of potential fiscal increments.

- Comparisons of aged care funding in various industrial countries compiled for the Royal Commission (Flinders 2020) confirm that government funding for aged care in Australia is smaller (relative to GDP) than other surveyed OECD

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solve the system's crisis: improvements in governance and accountability, particularly regarding the operation of for-profit facilities and services, is also critical to successful reform.

[39] This amount is significantly larger than the funds that would be generated by Commission Pagone's own proposed funding measure (a hypothecated aged care levy).

countries. Funding would have to increase by about 0.4% of GDP for Australia to reach the median of the sample of countries considered in that review.

The total increase in expenditure associated with aged care services in coming years will reflect a combination of normal demographic pressures and (hopefully) significant improvements in service quality. In turn, increases in those costs will be funded from various sources: including some from individual contributions, co-payments and fees; funding for direct health services for aged Australians (which should be considered a cost of the existing health system, not an aged care expense); and incremental resources dedicated to aged care (both residential and community). In this regard, not all of the increase in expenses which will be required to improve aged care service quality in light of the Royal Commission recommendations should be ascribed to aged care budget items.

Given this context, it is reasonable to anticipate that incremental government funding required to implement the crucial Royal Commission recommendations regarding improved aged care delivery (not including personal contributions and direct medical costs) would range between 0.5% and 1.0% of GDP, phased-in over a multi-year period. Not all of this new expenditure needs to be 'funded' with specific, targeted revenue measures. In fact, the context of continuing recovery from the COVID-19 recession, it is not clear that *any* of this new aged care funding needs to be explicitly matched with new revenue sources. As discussed above, in a cyclical context, a continuing excess of government expenditure over revenue is essential and beneficial to support net aggregate demand conditions, job creation, and private-sector incomes. At this moment in history, it is not desirable to increase taxes to offset these required improvements in the quality of aged care services. However, in the longer-run, as the economy builds back toward fuller utilisation of productive resources, it is reasonable to gradually implement corresponding revenue measures that will broadly balance this significant and sustained improvement in aged care services.

To that end, and to demonstrate the flexible and strong revenue-generating capacity of Australia's government, we present below five separate options to fund increased aged care by an amount equivalent to ***at least 0.5% of national GDP*** (or at least $10 billion per year in current dollar terms). The options are summarised in Table 12. If incremental costs associating with necessary improvements in aged care turn out to exceed 0.5% of GDP, more than one of these options (in whole or in part) could be implemented – and/or the additional increment could be funded through a combination of reallocation from other budgetary items or deficit financing. What is clear is that 'ability to pay' is not a meaningful or legitimate constraint on Australia's capacity to implement top-quality aged care services for our elders. To the contrary, there is a panoply of funding options available to the Commonwealth to fulfil its moral and social responsibility to implement these recommended reforms.

Table 12 Options for Financing Aged Care Service Improvements
Increase the Medicare Levy by 1%
A Progressive Aged Care Levy
Retain the 37% Personal Income Tax Bracket
Reforming Taxation of Investment and Capital Income
Reforming Company Taxes
Source: Authors' compilation as described in text. Benchmark incremental revenue equal to 0.5 per cent of national GDP.

To put the task of raising incremental revenues equivalent to 0.5 per cent of national GDP in context, consider the following findings from our review of Australia's current government revenue base in historical and international perspective that was discussed in Section III above:

- The ratio of aggregate taxes in Australia to GDP in 2020 was 0.5 percentage points lower than the average over the last 30 years. Increasing revenues by that amount, therefore, would simply lift the aggregate tax ratio back to its long-standing average level.
- The ratio of aggregate taxes in Australia to GDP is about 5 percentage points lower than the average for all industrial countries. Increasing revenues by 0.5 per cent of GDP would thus close just one-tenth of the gap between Australia and the normal pattern of taxation in industrial countries.
- The average ratio of tax revenues to GDP in the OECD has increased by 0.5 percentage points of GDP since the turn of the century (although in Australia it fell during this time, by 1.8 percentage points). Increasing revenues by 0.5 per cent of GDP would thus merely the match the average *increase* in the total tax revenue share experienced in other countries in this period.

By any of these indications, therefore, it is obvious that an increase in the government's revenue base of this scale is modest, by both historical and international standards.

It is also important to note that much of this incremental funding would simply serve to reverse the cumulative impact of previous historical cutbacks in fiscal support for aged care that have been imposed over the past quarter-century by various

Commonwealth governments – starting with the major deregulation and privatisation initiatives implemented by the Howard government in 1997. Indeed, as Commissioner Pagone noted, “the collective decisions of successive governments have cut more than $9.8 billion from the budget for aged care in 2018–19.”[40] It is not coincidental that this amount corresponds closely to the minimum level of additional funding which needs to be provided to meaningfully implement the Commission’s recommendations: additional funding of $10 billion is required merely to offset those previous reductions in funding, and begin to repair the damage that has resulted from a quarter-century of fiscal restraint.

It should also be noted that not all of the Royal Commission’s recommendations entail spending *more* money – and some of them, accompanied by other sensible reforms in the management and accountability of the aged care system, could in fact produce fiscal *savings*. The fragmented, overlapping, rent-seeking structure of private aged care imposes many wasteful costs – such as the deadweight burden of excess corporate management (including marketing and financial functions that have little relationship to provision of care). Moving more aged care into the public sector would enhance the fundamental economic efficiency of care provision (avoiding duplication and unproductive corporate overhead) as well as improve quality of care. Rolling back the sector’s ineffective and costly reliance on employment agencies and labour hire (a staffing model which funnels significant funding into the pockets of intermediaries) in favour of planned and stable staffing systems could also unlock significant long-run savings. Timely provision of home care and residential care can avoid unnecessary use of the more expensive acute health care system – which is where many elders end up when they do not receive timely, less costly interventions and supports. Our simulations below take no account of these potential savings; but in addition to providing additional funding, the implementation of the Royal Commission’s recommendations should also feature a systematic effort to identify ways to reduce unproductive costs as the sector is being reformed.

One final point is relevant to the consideration of the various options facing the Commonwealth government for financing improvements in this vital service. The Commonwealth government remains nominally committed to an aggregate cap on taxation, such that total federal taxes are not supposed to exceed 23.9 per cent of GDP. This ceiling is political and symbolic in nature, and serves only to insulate austere governments from public and democratic pressure to fully satisfy Australia’s social and economic needs. There is no economic rationale for such a cap, and taken seriously it would interfere with the necessary expansion of public services to meet emerging needs (like early child education) or evolving social challenges (such as the ageing

[40] Royal Commission into Aged Care Quality and Safety (2021), Volume 1, p. 13.

population) in coming years. All of the financing options identified below, therefore, presuppose that this needless and counter-productive 'cap' on revenues is either ignored or abandoned.

FIVE POSSIBLE FUNDING SOURCES

This section will review the broad features and revenue-generating potential of five potential revenue tools which the government could engage, to cover at least the major portion of incremental costs associated with implementing the Royal Commission's recommendations. The fact that such a diverse set of options is available reinforces the core message of this report: namely, that Australia has abundant capacity as a wealthy society to fund essential and humane services, from numerous potential sources. We can have a healthy debate about the pro's and con's of different revenue-raising options, taking into account criteria such as fairness, efficiency, and simplicity. The final strategy for funding aged care improvements could even draw on some combination of these fiscal tools – raising revenue from two or more different options. But regardless of which specific budgetary measures are ultimately chosen, there can be no debate that Australia can 'afford' to make these improvements. We obviously can, if we choose to.

Increase the Medicare Levy by 1%

In her recommendation regarding funding of required aged care reforms, Commissioner Briggs proposed a one percentage point increase in the existing Medicare Levy (see Recommendation 144 and Chapter 25 in Volume 3 of the Commission's final report). This increase would be termed the 'Aged Care Improvement Levy.' Commissioner Briggs did not propose a hypothecated levy (in that there would be no legislative tie between the funds raised and the end purpose). Since the improvement levy would cover only a portion of total Commonwealth aged care expenses, whether it is hypothecated or not becomes a matter of largely symbolic importance (since the aged care system would still need additional financing from other sources). In this regard, Commissioner Pagone's proposal is structurally and legislatively identical to the existing Medicare Levy on which it would be based.[41]

The Medicare Levy is a flat rate 2% tax on taxable income of Australians at all income levels. It is not paid by those whose taxable income falls below the $18,200 tax-free threshold. Above that level, most taxpayers pay 2% of taxable income targeted to

[41] The Medicare Levy, similarly, offsets only a minority portion of total Medicare costs, was never intended as a hypothecated system, and is not legislatively ascribed to be spent only on Medicare purposes.

Medicare costs.[42] These revenues fund only a small portion of total Medicare costs, but the Levy reinforces political understanding and support that Medicare is a vital public program that everyone must contribute to. As a flat-rate tax, the Medicare Levy is less fair than progressive personal income taxes (which charge higher marginal rates for those with higher incomes). Indeed, of the five funding options considered in this report, the Medicare Levy imposes the least additional cost on high-income earners – who can best afford to make incremental contributions to this essential public service.

The 2019-20 Commonwealth Budget projected that total revenues from the existing 2% Medicare Levy would equal $21.1 billion in 2022-23.[43] This forecast, of course, has been dramatically affected by the effects of the COVID-19 pandemic and resulting recession, but it is still valid as a benchmark of the baseline revenues generated by this measure once the economy has recovered to a normal level of activity. This includes the Medicare Levy Surcharge, which applies to individuals with taxable income over $90,000 who do not purchase private health insurance.[44] Separate data from the ATO suggests only around 2 per cent of the total revenue from the levy is due to the Surcharge.[45] Excluding the surcharge (which would not change under the Briggs proposal), a 1 percentage point increase in the Levy would thus be expected to raise $10.4 billion (meeting the desired threshold of 0.5% of GDP).

A Progressive Aged Care Levy

Commissioner Pagone proposed an alternative method of funding improvements to aged care service delivery (see Recommendation 138 and Chapter 20, Volume 3, of the final report of the Commission). He favours a hypothecated system, on grounds that this would strengthen the social commitment to funding aged care (although, as noted above, since his proposal would not fund all of the government's aged care expenses, the system would still need to rely on additional financing from other sources). Commissioner Pagone then proposes a variety of different combinations of adjustments in income tax rates to generate a flow of targeted funding which he suggests would be sufficient to fund the whole aged care system, after adjusting for an assumed proportional split between income taxes and other sources.[46]

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[42] There are various grounds for exemption from the levy based on dependents, medical needs, and other factors.

[43] Australian Government (2019) *2019-20 Budget Paper No 1*, p. 4-17.

[44] The Surcharge is justified as a means of encouraging people to buy private health insurance and thus reducing the cost of Medicare, but in reality it constitutes an enormous subsidy for private insurers.

[45] Data for 2017-18 from Australian Tax Office, Taxation statistics 2017-18 at https://www.ato.gov.au/About-ATO/Research-and-statistics/In-detail/Taxation-statistics/Taxation-statistics-2017-18/?anchor=Individuals#Chart6.

[46] See simulations reported on pp. 782-810 of Volume 3 of the final report.

As discussed above, we do not accept the logic of a fully hypothecated system: whereby the funding available for a service would be limited to the sequestered revenues arising from its targeted tax source (and all revenues from that source must be spent on the service in question). But Commissioner Pagone's approach does open the opportunity for a more flexible and tailoured set of revenue tools to support aged care, compared to the simple flat-rate structure of the existing Medicare Levy. More particularly, it would allow incremental funds to be raised in a progressive manner, with a larger proportion of new revenues collected from Australians with higher incomes. This is both morally appropriate and economically preferable. Progressive taxation limits the growth of income inequality (measured in after-tax after-transfer terms), supports stronger aggregate demand and spending,[47] and enhances social cohesion. On these grounds, we therefore propose a special aged care adjustment to Australia's existing personal income tax parameters to raise equivalent revenue as a 1-point increase in the Medicare Levy – but with fairer distributional effects.

Prior to the COVID pandemic and resulting recession, Commonwealth budget projections expected total gross personal income tax revenues to exceed $300 billion in 2022-23.[48] In order to raise an additional $10 billion per year in revenues (to meet the desired threshold of 0.5% of GDP), overall income taxes would thus need to increase by 3.3 per cent. If we wish to mirror the progressivity of the existing income tax structure with the new aged care adjustment, then all tax rates would be increased by an equivalent 3.3 per cent proportion (applied proportionately relative to the initial rates, not in absolute percentage points). Table 13 summarises the resulting changes in marginal taxes for various levels of income, and the incremental income tax which would be paid at each level.

The bottom tax rate (which currently applies to taxable incomes between $18,200 and $45,000) would be increased from 19% to 19.6%. The second tax bracket is raised by just over 1 percentage point, from 32.5% to 33.6%. The third tax bracket is lifted by an equal proportionate amount, from 37% to 38.2%.[49] Finally, the top tax bracket is increased from 45% to 46.5%. In every case, the increase in marginal tax rate is 3.3 per cent compared to the existing rate.

[47] Lower-income households have a very low propensity to save; hence, any increase in after-tax disposable income experienced among lower-income households translates into a much stronger increment in consumer expenditure than for higher-income households (which tend to save a significant proportion of extra disposable income).

[48] Australian Government (2019) *2019-20 Budget Paper No 1*, p. 4-17. This is a gross figure before the payment of refundable franking credits and other deductions.

[49] The current Commonwealth government plans to eliminate this tax bracket entirely in Stage Three of its proposed income tax cut program in 2024-25; the costs of this measure are discussed below.

Table 13 Progressive Aged Care Levy Payments by Income Level			
	Current Top Rate	New Top Rate	Extra Tax per year
Below $18,200	0.0%	0.0%	$0
$20,000	19.0%	19.6%	$11
$45,000	19.0%	19.6%	$168
$60,000	32.5%	33.6%	$329
$75,000	32.5%	33.6%	$490
$100,000	32.5%	33.6%	$758
$120,001	37.0%	38.2%	$1,084
$150,000	37.0%	38.2%	$1,450
$180,001	45.0%	46.5%	$1,975
$200,000	45.0%	46.5%	$2,272
$250,000	45.0%	46.5%	$3,014
Source: Authors' calculations from Commonwealth Budget documents.			

The incremental taxes paid at each level of income are shown in the final column of Table 13. Those below the tax-free threshold (representing the lowest-income 19% of tax-filers) pay nothing extra. Someone earning $20,000 taxable income would pay $11 extra. Someone earning $45,000 would pay an extra $168. That is slightly less than the current median taxable income.[50] Hence more than half of Australians would pay less than $200 per year in additional tax to support these far-reaching and essential reforms. Incremental tax payments increase with income. In contrast, someone with $180,000 taxable income (representing the 96th percentile of the income distribution) would pay an extra $1975 in taxes: equal to just over 1% of their taxable income.

Most Australians would pay less incremental tax under this proposal than under the across-the-board 1% increase in the Medicare Levy proposed by Commission Briggs. For example, someone with taxable income of $45,000 (close to the median income) would pay $450 in the additional Medicare Levy – almost three times more than they would pay under the progressive aged care adjustment ($168). However, at the top of

[50] Median income is the income level dividing the total population exactly in half: with 50% earning more, and 50% earning less.

the income distribution, this alternative proposal would increase the marginal tax rate by 1.5 percentage points, and would thus raise proportionately more than a flat-rate increase in the Medicare Levy. We estimate that taxpayers with taxable income below $172,500 would pay less incremental tax under this progressive adjustment than under the increased Medicare Levy.

Increasing all tax rates by the same proportion preserves the existing degree of progressivity in the tax system (by lifting all marginal tax rates in the same proportion). Thus this aged care adjustment preserves horizontal equity, so that the proportion of tax paid by someone with any given income stands in the same ratio to other income earners as before the change. Of course, this assumes the existing degree of progressivity in the income tax system is desired. Conceivably, the introduction of the aged care adjustment could also be an opportunity to improve the degree of progressivity in the tax system, by shifting the incidence of the new tax even more toward the top end of the distribution; any number of possibilities could be considered in that regard.

One additional dimension should be considered in relation to both of these proposals for new revenue measures targeted to funding aged care improvements. Research conducted for the Royal Commission indicated that most Australians would be willing to pay higher personal taxes to support improved quality of aged care (Ratcliffe *et al*., 2020). The average amount of additional tax which this majority would support is 1.4%. Both of the proposals for new revenue tools therefore fall comfortably within that margin of politically-supported tax increases.

Retain the 37% Personal Income Tax Bracket

In 2018 the Coalition government announced plans for a three-stage reduction in personal income taxes as the centrepiece of its fiscal strategy. These cuts will reduce federal revenues by a cumulative total of almost $300 billion over a twelve-year period, compared to status quo tax settings (Phillips *et al*., 2020). This clearly constitutes another effort by conservatives to ‘starve the beast,’ as explained above: imposing needless tax cuts, and deliberately weakening budget balances, in order to put more downward pressure on spending.

The first two stages of the program have been implemented (the second stage was accelerated in 2020, purportedly to stimulate economic activity as the economy recovers from the COVID-19 pandemic). The most expensive and unfair stage of the whole program, however, is yet to be implemented. The government’s timetable would see the Stage Three measures implemented in the 2024-25 financial year.

The provisions of the third stage of Coalition income tax cuts include the following:

- Reducing the 32.5% tax bracket to 30%.
- Eliminating the 37% tax bracket.
- Lifting the bottom threshold for the 45% tax bracket from $180,000 to $200,000.

This set of tax changes strongly concentrates its savings among higher-income Australians, as summarised in Table 14. Those with taxable income below $45,000 would receive no savings at all from these measures. Since $45,000 is just below the median tax-filer income, that implies that around half of Australians would receive no tax reductions at all. Those earning between $45,000 and $120,000 (the former lower threshold of the 37% tax bracket) receive modest tax savings, arising from the reduction in their marginal rate from 32.5% to 30%. The largest savings, however, are received by Australians with taxable income over $120,000. They receive a reduction in taxes worth 7 percentage points of their income over $120,000 (plus $1875 in savings on their income between $45,000 and $120,000). Maximum savings are available only to those earning $200,000 or more: their taxes are reduced by over $9000 (or up to 15 per cent).

Table 14

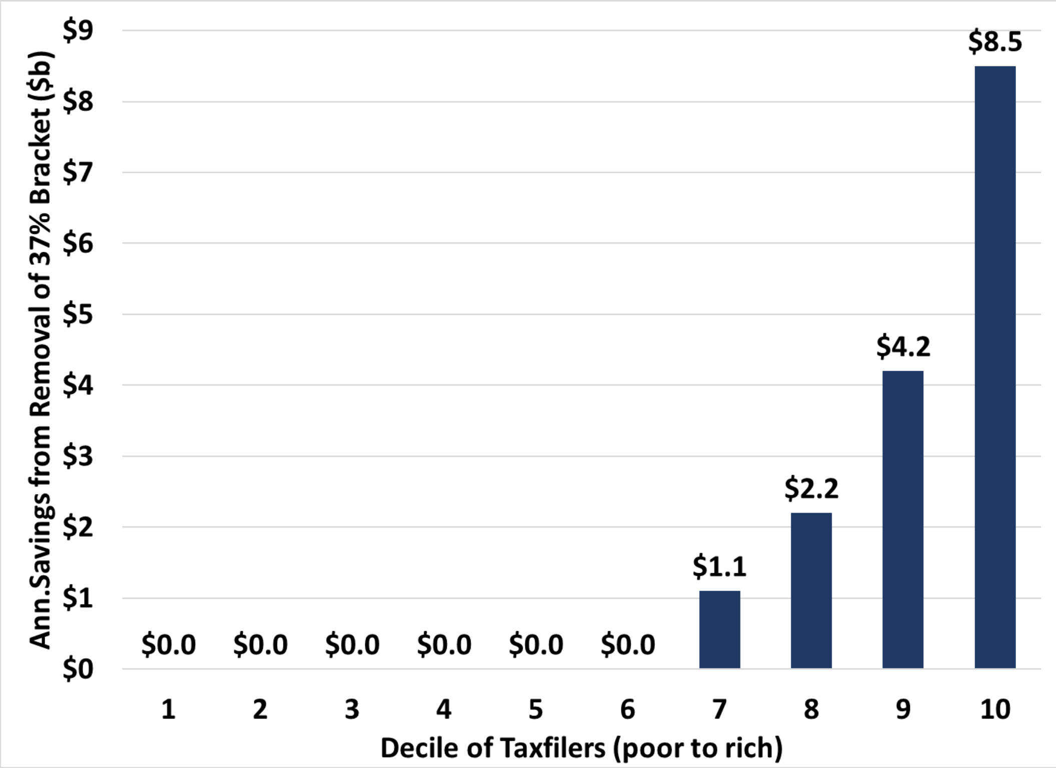
Stage 3 Income Tax Savings by Income Level

	Current	Stage 3	Saving
$45,000	$5,092	$5,092	$0
$75,000	$14,842	$14,092	$750
$100,000	$22,967	$21,592	$1,375
$120,000	$29,467	$27,592	$1,875
$150,000	$40,567	$36,592	$3,975
$180,000	$51,667	$45,592	$6,075
$200,000	$60,667	$51,592	$9,075

Source: Authors' calculations from Commonwealth Budget documents.

Most Australians, therefore, will receive little or no benefit from the Stage Three tax cuts. However, the size of concentrated savings for high-income groups is substantial – and as a result, the Stage Three measures are very expensive, even though few Australians benefit. Grudnoff and Richardson (2018) have simulated the distribution of benefits resulting from just the biggest Stage Three measure: the elimination of the 37% bracket. Total revenue lost from that measure alone is estimated at $16 billion per year once implemented (see Figure 7).

Figure 7. Distribution of Savings from Elimination of 37% Tax Bracket, 2024-25



Source: Grudnoff and Richardson (2018).

Over half the aggregate benefit from that one measure is received by Australians in the highest-income tenth of the population. 80% of the benefit is received by Australians in the highest-income fifth. No benefits at all from the elimination of that bracket are received by the lowest-income 60% of Australians.

The Stage Three tax cuts in general, and the elimination of the 37% bracket in particular, are highly disequalising measures which will substantially enhance the after-tax income of the richest Australians, but deliver literally no benefit to most. These measures are economically damaging (including by constraining potential expenditures of the government) and morally offensive. At a moment when government proclaims that reducing the deficit is a national priority, it is abhorrent that government would proceed with measures that substantially erode its revenue base for the benefit of a well-off minority.

Even more unacceptable is the notion that critical improvements in aged care services for Australia's seniors, who have contributed so much to our economic development over the last century, would be curtailed because of a targeted tax giveaway to wealthy households. Simply by cancelling the planned elimination of the 37% bracket, the government would retain revenues to provide an ample fiscal cushion (well in excess of the 0.5% of GDP target) to support aged care reforms.[51] This demonstrates dramatically that ability to fund high-quality aged care is completely a matter of policy choices and priorities, not economic or budget constraints. By choosing to cut taxes for the highest-income Australians instead of addressing critical quality concerns in aged care, this government would reveal how misplaced its priorities are.

Reforming Taxation of Investment and Capital Income

Australia's income tax system contains a wide range of preferential measures that favour individuals who receive income from financial and business investments. These measures include:

- Partial taxation of income from capital gains (an exemption of 50% applies to capital gains income). This exemption reduces taxable income for those claiming it by a combined total of over $25 billion per year, and reduces taxes paid by around $10 billion per year.[52]
- Preferential treatment of dividend income through the imputation and franking system (whereby taxpayers receive refundable credits representing corporate taxes paid by companies from which they received dividend income). Total franking credits claimed on dividends alone exceeded $10 billion in 2017-18.[53]
- Negative gearing provisions, which allow taxpayers to strategically deduct apparent losses on various investments (such as investment properties) from their income from other sources, in order to reduce their overall tax liabilities.
- Many other measures which are tailoured to favour individuals with business and financial investments, including deductibility of various investment-related expenses, special measures for small business income and property taxes, carry-forward of losses, and others.

Because ownership of financial and business assets is highly concentrated among the wealthiest Australians, the main benefits of these provisions are received by the highest-income taxpayers. For example, based on the most recent taxation data, some 69% of all net capital gains declared on personal tax returns (for the 2017-18 income tax year) were received by Australians with over $180,000 total income (representing

[51] The Stage Three measures have been legislated, and hence their impacts incorporated by government into its longer-run fiscal planning; in this context, therefore, cancelling a planned cut is equivalent to a revenue-raising measure.

[52] Authors' calculations from ATO Taxation Statistics, 2017-18, Individuals, Table 10a, and Department of Treasury (2021).

[53] Authors' calculations from ATO Taxation Statistics, 2017-18, Individuals, Table 10a.

just 4% of all tax-filers that year). That same small group of highest-income Australians also received over half of all dividend income.[54] By offering tailoured preferences for forms of income heavily concentrated at the top of the income distribution, these measures redistribute after-tax income upward, thus exacerbating growing inequality in Australia. In this way, well-off Australians avoid making a full proportional contribution to the cost of providing essential public services, such as aged care.

All of these preferential measures for owners of financial and business capital are backed with misleading economic arguments about why capital income should be taxed less heavily than income from other sources (like employment). A common argument is that these loopholes are necessary to avoid so-called ‘double taxation’: according to this theory, income generated from ‘capital’ is partly taxed when a company pays its own taxes, and therefore profits received by the human beings who own that company should be reduced accordingly. Moreover, it is argued, if taxes on capital (and the human beings who own it) are reduced, businesses will invest more, and the economy will grow faster to everyone’s benefit; this is the standard logic of trickle-down economics.

These arguments in favour of preferential treatment of investment and capital income are self-serving and unconvincing. Companies are expected to pay tax to reflect (and help pay for) benefits they receive (as economic institutions) from the provision of public services and infrastructure: such as transportation and communication infrastructure, education and training services, health care and other human services, policing and security, business support functions of government, and more. Company taxes are a recognition that successful businesses depend on the functioning of these effective public sector functions and services. Then, the taxes paid by the individuals who own those businesses reflect their own personal contributions (as distinct from the enterprises which they own) to the provision of public and social goods which they also personally benefit from. The claim that tax concessions to capital income somehow prevent an ‘injustice’ of excess taxation on these largely well-off individuals is specious and self-serving.

After all, it could equally be argued that workers also face ‘multiple’ taxation on their incomes. A worker pays a share of their wages and salaries to government in income tax. But then they pay tax again (via the GST) when they spend that (after-tax) income, and more again when they buy a home, consume various ‘sin’ products (like alcohol and tobacco), purchase petrol, and more. Abstract complaints about double, triple, or even quadruple taxation of individuals do not (and should not) interfere with

[54] All statistics in this paragraph are authors’ calculations from ATO Taxation Statistics, 2017-18, Individuals, Table 10a.

governments levying taxes on various flows of income and expenditure, balancing relevant factors such as ability to pay, fairness, and sustainability. The credibility of arguments for tax concessions for investment and capital income has eroded in light of both the growing inequality of personal incomes in Australia (due in significant measure to the growth and uneven distribution of financial and business wealth), and the failure of Australian businesses to respond to tax preferences with a stronger investment effort. Indeed, far from encouraging investors to 'take risks' and invest in new capital and technology, the real investment effort of Australian businesses has faded markedly over the past decade despite these expensive tax preferences. Total business investment (including in tangible capital assets and new technology and intellectual property) has fallen precipitously: from over 17% of Australian GDP in 2012 to just 10.6% in 2020 (the lowest in Australia's postwar history).[55] These lucrative tax preferences for capital gains, dividends, and other investments have spurred speculation in property and stock markets, not real accumulation and growth.

In this context, it is past time to start rolling back the myriad of expensive tax preferences which presently favour wealthy investors and owners. And linking this process to the need to fund sustained improvements in the quality of aged care services would provide an additional strong moral impetus for these overdue reforms.

The benchmark level of incremental funding for aged care improvements identified above (equal to 0.5% of GDP once fully phased in) could be achieved by merely moderating (not eliminating) just two of the most egregious of these tax preferences. Reducing the capital gains exemption from 50% to 25% would still leave a generous tax preference for investors, but reduce foregone revenues by over $5 billion per year. Similarly, adjusting the formula for dividend franking credits to allow deduction of one-half of imputed company taxes would scale back the cost of the franking system by over $5 billion per year.[56] Together, these two measures would thus rise $10 billion to support necessary improvements in the quality of aged care in Australia – with the overwhelming bulk of those extra revenues paid by the wealthiest segments of society. Once again, the decision comes down to one of social and moral priorities, not economic or fiscal 'logic': the choice is between further enhancing the wealth and privilege of a group of Australians who, in general, are already very well off, or allocating discretionary resources to meeting the concrete needs of our elders.

There are many other possible options for rolling back the cost of these and other expensive tax preferences for financial and business investments and ownership.

[55] Authors' calculations from ABS National Accounts data.

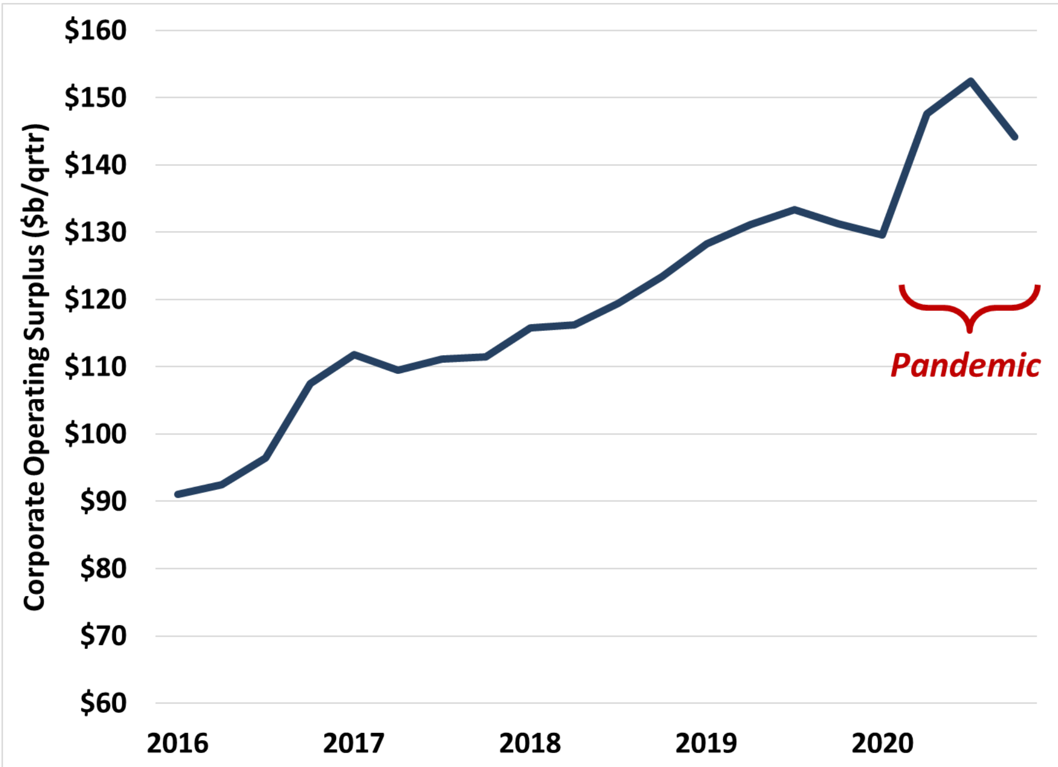
[56] Both estimates based on authors' calculations from ATO Taxation Statistics, 2017-18, Individuals, Table 10a, and Department of Treasury (2021).

Reducing franking credits for superannuation funds could raise $3 billion or more in additional revenues. The abolition of negative gearing loopholes would raise $2 to $4 billion. Countering tax avoidance using trusts could raise up to $2 billion per annum. These options are listed here solely to emphasise the range of choices which the government enjoys in determining how the cost of needed aged care improvements would be met.

Reforming Company Taxes

The economic downturn resulting from the COVID-19 pandemic represented the first recession in Australia's history in which company profits actually *increased*. Normally in a recession, company profits experience a disproportionate downturn: this is because business revenues decline with falling sales, but they cannot downsize employment or operating costs fast enough to keep pace. The result is lower profits (or outright losses) incurred until either the economy recovers or the company downsizes. In the 2020 recession, however, Australian company profits, perversely, increased. As illustrated in Figure 8, company operating surpluses surged even as the economy fell into recession and close to 1 million Australians lost work.

Figure 8. Corporate Operating Profits, 2016-2020



Source: Author's calculations from ABS National Income Accounts, Table 7.

Boosted by JobKeeper subsidies, other government aid, and strong sales for many items (such as groceries) during the pandemic, corporate operating profits equalled $575 billion for 2020 – 10 per cent higher than in 2019. As a share of total GDP, business profits hit their highest level in recorded history in 2020: representing 29 per cent of national output. The pandemic thus perversely culminated a long historic period of rising profitability in Australia, as business benefited from numerous favourable policies – including lower labour costs, deregulation, subsidies, and tax incentives and preferences. In the 50-year period from 1960 through 2010, corporate profits averaged 20 per cent of GDP. Thanks to growing corporate power, chronic stagnation in labour costs, and government favours, the current profitability of companies is well outside that traditional distributional pattern. Therefore it is reasonable to expect Australian companies to contribute more to vital community priorities – including aged care.

Ironically, even as business profits grew last year, company tax collections fell – in part thanks to various government aid programs. Company income taxes collected from non-financial businesses fell by 10 per cent compared to 2019. Company taxes paid by banks and other financial corporations (which profited during the pandemic) fell 25 per cent. Combined, company taxes shrank by over $15 billion. Relative to gross operating surpluses, the effective rate of income tax across the corporate sector fell by over 4 full percentage points last year, to under 15 percent.[57] Merely maintaining the effective rate of company taxation at its 2019 level would be sufficient to single-handedly match and exceed the 0.5% of GDP target identified above for new revenues to support improved aged care services.

The extraordinary circumstances of the pandemic mean that company profits and tax payments last year were unusual, and we would expect at least a partial return in coming years toward more normal pre-pandemic levels of profitability and taxation. Nevertheless, it is clear that corporate Australia continues to benefit from a long-run structural shift in economic power and wealth. It is therefore reasonable to expect that sector to contribute more to the maintenance of strong community and social standards – including, as a priority, providing high-quality universal care to our seniors. Traditional arguments that companies cannot be asked to pay more taxes or they will flee Australia for more lucrative foreign jurisdictions were never convincing, but today they ring utterly hollow. Australia’s business sector is uniquely profitable compared to foreign counterparts, and much of its profit stems from attributes (such as Australia’s natural resource base, or our extremely profitable banking and property sectors) which

[57] The effective rate of tax paid on operating profit is much lower than the statutory company rate (which is 30 per cent for large businesses) because of various deductions allowed in calculating taxable income.

cannot be ‘moved overseas.’ Moreover, emerging policy shifts around the world indicate that other countries, too, expect profitable businesses to pay more toward public services in the wake of the pandemic. U.S. President Joe Biden is moving to increase the U.S. company tax rate by almost half (to 21 per cent), and the U.K. government is lifting its company tax to 26 per cent.

In Australia’s case, the corporate sector could fund the desired increment in aged care expenses of 0.5% of GDP (presently around $10 billion per year) through an increase of just 1.7 percentage points in its effective rate of taxation (measured as a share of gross operating profits). Modestly increasing the base company tax rate would be a simple but blunt means of accomplishing that goal. We prefer other measures to target higher taxes on specific business sectors or activities that are especially worthy of critical attention. These could include:

- Doubling the major bank levy, which currently collects about $2 billion per year from the five largest financial institutions in Australia (the big 4 banks plus Macquarie Group).
- Reform of the Petroleum Resource Rent Tax (PRRT) to reduce opportunities for offshore transfer pricing by petroleum producers, which has resulted in them avoiding royalty taxes on non-renewable petroleum and gas production.[58]
- Limits on interest cost deductibility for companies, including on international interest payments.[59]
- Elimination of the use of offshore tax havens by Australian companies to transfer taxable profits out of the country (in line with accelerating international efforts to develop stronger global tax codes and a minimum global company tax).
- Application of existing company taxes to global firms (including digital platforms) on a pro-rated revenue basis to reflect their proportional revenues generated within Australia.

There are many other sensible and equitable reforms to the company tax system in Australia that could also contribute to the goal of raising sufficient revenues to fund the Royal Commission’s recommended improvements, but with no change to the headline 30 per cent basic company rate. However, the above measures alone would

[58] The nature of the problem and the potential revenue gains from addressing it are explored by Campbell (2019). Butler (2021) describes the case of Shell’s Gorgon LNG development, which is not expected to generate *any* PRRT royalty revenue despite tens of billions of dollars of gas sales.

[59] As explored in various research, such as Gravelle (2014) and Ingles and Stewart (2018).

be more than sufficient to meet the target of 0.5% of GDP. This would represent a modest enhancement of tax collections from Australian companies – which have never been more profitable.

A MATTER OF CHOICE

In sum, there is no economic or fiscal argument that Australia cannot 'afford' to make the overdue and essential improvements in the quality and safety of aged care service delivery that were identified by the Royal Commission. Australia is one of the wealthiest and most productive economies in the world. We already spend considerably less on aged care services, relative to the size of our economy, than many other industrial countries. Overall tax levels in Australia are substantially lower than is typical for OECD economies. One reason for Australia's relatively low tax collections is the existence of several arbitrary and disequalising loopholes and preferences in the tax system – which deprive government of tens of billions of dollars of foregone revenue, on dubious economic and moral grounds.

This report has stressed the importance of moving ahead, quickly and strongly, to implement the Royal Commission's recommendations. And we have identified a panoply of potential funding mechanisms which government could activate to support that effort. Our analysis confirms that the Commission's recommendations are appropriate, viable and affordable. It now comes down to the willingness of government to place appropriate priority on the safety, health and happiness of our elders – and the safety and well-being of the people who work every day, in hospitals, aged care residences, and in the community, to meet those needs.

Conclusions

Australians were rightly outraged by the exposure of systematic sub-standard care, neglect, and even abuse experienced by our elders. After the sacrifices they have made throughout their lives to develop our economy and society, they deserve much better. Australia is one of the wealthiest economies in the world, and can well afford to provide seniors with top-quality care and support in the last years of their lives. Moreover, since the provision of aged care services is itself an important source of work, income, and value-added, expanding and improving those services will provide a badly-needed injection of energy and stimulus to the overall national economy – supporting recovery from the fastest, deepest recession in Australia's postwar history.

The Royal Commission into Aged Care Quality and Safety has performed a historic service to Australians by comprehensively and exhaustively documenting the failures of our existing aged care system: fragmented, inadequately regulated, distorted by profit-seeking on the part of private providers, and chronically underfunded and understaffed. The Commission's 148 recommendations constitute a clarion call to action for Australian society.

The Commission challenges us to imagine an ethical and effective response to the needs of elder Australians: by endorsing a universal, accessible aged care system open to all who need it. It also quite rightly identified the critical investments that must be made in the aged care workforce as part of that transformation. In particular, its recommendations for binding staff ratios (including for nurses), benchmark times of care, regulation and registration for all care staff (including personal carers), and provision of high-quality ongoing training for staff are essential if the goal of high-quality, universal care is to be achieved. The quality of work *is* the quality of care – and the Commission's vision would see the aged care workforce finally treated as the valuable asset it is, rather than as a just-in-time productive input to be minimised and devalued.

It is now incumbent on the Commonwealth government, working in partnership with all stakeholders in the system (including aged care workers and their unions), to develop a plan for implementing the Royal Commission's recommendations, and rebuilding the aged care system on grounds of quality, accessibility, and accountability. A key issue to be confronted in this task will be mobilising adequate resources to fund this task. At the most immediate level, this is not an issue that should slow the implementation of the Royal Commission recommendations by a single day. The fact is that the Commonwealth government has unlimited financial resources to address any urgent social priority. It proved that amply during the COVID-19 pandemic, when unprecedented resources were mobilised to help Australians survive the health and economic consequences of the crisis. The government's current deficit is an expected, even beneficial side-effect of the extraordinary efforts it has taken over the past year. Investments in aged care improvements in the medium-term can absolutely be financed from general revenues, in the context of ongoing deficit financing that is both inevitable and appropriate.

In the longer term, however, as fiscal balances return to more normal and sustainable magnitudes,[60] we accept the desire to identify incremental revenue sources which would underpin a permanent expansion in fiscal support for aged care, essential to fulfilling the Royal Commission's vision. There are ample choices in this regard. Aggregate tax revenues in Australia (relative to the overall economy) are not high compared to our history – and much lower than in other industrial countries (including those highlighted by the Royal Commission as achieving better outcomes in aged care than Australia[61]). Targeting a sustained increase in revenues to fund aged care services on the order of 0.5 per cent of GDP would constitute a major contribution to implementing the Royal Commission's recommendations. This target is broadly equivalent to the order of magnitude contemplated in Commission Briggs' proposal for a 1 per cent Medicare-style levy. But there are other potential alternative revenue measures, with more equitable distributional effects, that could also be invoked to raise similar amounts.

Section IV of this report has described five such possibilities (including Briggs' proposal). All are economically and fiscally feasible. All would retain Australia's overall tax revenues within the range of our historical experience – and keep them far below the revenue bases of most other industrial countries. Ideally, most of the new revenues should be collected from those Australians who can most afford to pay toward such a pressing social need. So our proposals have emphasised revenue options that are progressive in their ultimate incidence. However, even a flat-tax-style option (like the Medicare-style levy) would have a positive net impact on Australian society: by funding the provision of a public service so vital to equality and the well-being of all seniors. The top priority is to move ahead with collecting and allocating the resources necessary to fulfil the Royal Commission's recommendations. Specific questions about the design and distributional impacts of resulting tax measures are clearly secondary.

[60] Although there is certainly neither a need nor an expectation that deficits must be eliminated entirely, even over the long term.

[61] See the review of international practices reported in Rehabilitation, Aged and Extended Care Group *et al*. (2020).

In sum, the Commonwealth government has a wide range of fiscal options at its disposal to support the urgent transformation of Australia's aged care system – including, in the medium term, the ability to simply pay for those changes out of its general budget (with no special 'financing' required). It should move forward immediately with this process, including with provisions in its upcoming 2021-22 budget. There is no shortage of money in this government to do right by Australia's seniors. The only issue is whether the government chooses to make repairing our aged care system the priority it should be.

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