

# Accommodation Bonds. Are they protected?

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This article first appeared in *Precedent*, the professional journal of the Australian Lawyers Alliance (Issue 86, May/June 2008)

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## PROLOGUE

**Client:** *“The nursing home wants us to pay a \$250,000 bond so mum can go into a home. We just can’t afford it. Our only option is to sell the family home. It is mum’s life savings and we just don’t know how safe it is.”*

If you haven’t been faced with this situation yet, there is a strong chance you will at some stage in the future.

In light of the recent corporate collapse of Lifecare, a Queensland-based nursing home provider, this article attempts to clarify issues relating to the security of accommodation bonds payable to nursing home providers and what happens when things go wrong.

## WHAT IS AN ACCOMMODATION BOND?

An accommodation bond (**bond**) is a means tested payment or series of payments to an aged care facility to secure entry into the facility<sup>1</sup>. Entrants to certain aged care nursing home facilities have been required to pay bonds from as early as 1987 (then described as Entry Contributions). The requirement to pay large bonds, up to as much as \$250,000 or even more, to secure entry into private nursing home facilities is increasingly common. In 2004 it was estimated that over \$4.3 billion in bonds was held by aged care providers in Australia<sup>2</sup>.

The bond payment system emerged out of the need to bolster the aged care sector to meet the demands of an ageing population by introducing a source of private funding to fund the development and improvement of the scale and quality of aged care accommodation facilities. In addition to improving the efficiency, sustainability and infrastructure of the aged care sector, it was also seen as a means of securing any outstanding payments to providers at the time

of the resident's departure.

**Bonds generally have the following features:**

- Bonds are available to providers to be used for any purposes relating to the provision of aged care facilities and services, provided it is an approved purpose within the meaning of the *Aged Care Act 1997* and that the funds are applied in accordance with the prudential standards<sup>3</sup> stipulated in the *User Rights Principles 1997*<sup>4</sup>;
- The bond must not exceed the maximum amount under sections 57-12, 57-13 or 57-23 of the *Aged Care Act 1997*. In practice this means that the resident must retain the minimum permissible asset value, which amounts to approximately 2½ times the annual single rate aged pension<sup>5</sup>;
- Residents may pay the accommodation bond by way of a lump sum, or by instalments<sup>6</sup>;
- If the resident does not pay the bond prior to entry, the provider is entitled to charge interest until such time as the full amount of the bond has been paid<sup>7</sup>. Provisions relating to interest must be stipulated in the bond agreement and the interest rate charged cannot exceed the maximum permissible interest rate<sup>8</sup>;
- Providers may deduct annual retention amounts for a period not exceeding five years. The agreed retention amount does not change during the life of the accommodation bond agreement.
- The maximum retention amount is capped by the Government and cannot exceed \$3,360 per year<sup>9</sup>;
- Providers are entitled to make further deductions for any outstanding amounts owing under the bond agreement, resident agreement or an extra service agreement prior to refunding the bond balance. This could include debts arising from unpaid daily accommodation fees<sup>10</sup>;
- The *Aged Care Act 1997* does not specify precisely how the bond should be invested but the provider must comply with the Prudential Standards (see below);
- Providers cannot use the bonds for purposes which do not relate to providing aged care facilities or services to its residents;
- The principal sum of the bond (minus valid deductions) is refundable 14 days after the resident leaves the facility or within 14 days after sighting

evidence of the grant of probate or letters of the administration of the estate of a resident who has subsequently deceased<sup>11</sup>;

A prospective resident cannot be asked to pay an accommodation bond unless they have entered into an agreement which sets out the respective duties and responsibilities of the aged care provider and the resident's rights under that agreement. The bond agreement must be entered into either before or within the first 21 days of residency<sup>12</sup>. Practitioners involved in the transaction should ensure that the bond agreement complies with section 57-9 of the *Aged Care Act 1997*.

After an accommodation bond agreement has been executed, the provider must provide the resident and/or their representative with a copy of the bond agreement and a written copy of the refund guarantee of the bond balance<sup>13</sup>.

## **THE REGULATORY FRAMEWORK**

The Government first announced a prudential scheme to safeguard accommodation bonds in 1997. Prior to 1997, bonds (or entry contributions) were paid to providers without the Federal Government's protection.

The restructured regulatory scheme came into force on 31 May 2006 to guarantee the refund of all bond balances held by approved providers under the *Aged Care Act 1997*. The new regulatory framework also operates retrospectively, protecting all entry contributions made prior to 1 October 1997.

The 2006 reforms envisaged the imposition of increased statutory obligations on providers to enforce higher standards of accountability and transparency for accommodation bonds. Bonds are regulated by the following Acts:

1. The *Aged Care Act 1997*;
2. The *Aged Care (Bond Security) Act 2006*;
3. The *Aged Care (Bond Security) Levy Act 2006*
4. The *User Rights Principles* made by the Minister from time to time under section 96-1 of the *Aged Care Act 1997*

### **Prudential Standards to be met by Providers**

An approved provider is required to comply with three prudential standards

which are set out in the *User Rights Principles 1997*. Those standards are as follows:

**1. The liquidity standard**

The liquidity standard requires providers to maintain a sufficient level of liquidity to ensure that they can refund the bond balances (and any entry contributions made prior to 1997) as and when they may fall due over the following 12 months. Approved providers are also required to implement and maintain a documented liquidity management strategy to identify the minimum level of liquidity which they can safely possess, as well as develop a strategy to maintain that level<sup>14</sup>.

**2. The record standard**

An approved provider is required to keep an up-to-date record of all bond holdings which is required to be audited each year. The bond register must accurately identify all bond deposits and the deductions which are made from each individual bond. Specifically, those records must demonstrate the date, amount and purpose for each deduction which occurs. The bond register is also required to keep track of when a refund is due with interest calculations as they fall due<sup>15</sup>.

**3. The disclosure standard**

The disclosure standard is designed to ensure that comprehensive, accurate and up-to-date information obtained through adhering to the liquidity and records standard is made available. Disclosure of the provider's compliance with the prudential standards must be made to the Department of Health and Aging (the Department) annually<sup>16</sup>. The provider is also required to provide all bond paying residents and/or their representatives with a copy of the following information within 4 months of the conclusion of each financial year<sup>17</sup>:

1. an account of the number of bonds which are held in compliance with the *Aged Care Act 1997* and a statement of compliance with the Act;
2. a copy of the bond entry which relates to the applicable resident within the bond register;
3. a copy of an independent auditor's opinion as to whether the provider has complied with the prudential standards.

The provider has an additional obligation to provide the information which is

stated above, plus the most recent statement of the provider/organisation's audited accounts, to a resident and/or their representative within 7 days of the request being made. This information may be requested at any stage during the financial year<sup>18</sup>.

In relation to prospective residents, the provider has a duty to make disclosure to a prospective resident and/or their representatives, of the following information within 7 days of receiving the request<sup>19</sup>:

1. an account of the number of bonds held in compliance with the *Aged Care Act 1997* and a statement of compliance with the Act;
2. a copy of an independent auditor's opinion as to whether the provider has complied with the prudential standards
3. The most recent statement of the provider/organisation's audited accounts.

## **WHEN AN APPROVED PROVIDER DEFAULTS IN REFUNDING THE BOND**

The *Aged Care (Bond Security) Act 2006* (**the Bond Security Act**) was established to protect accommodation bonds paid to approved providers by providing a safety net that allowed the Commonwealth to refund residents in the event that their approved provider defaulted on its refund obligations because of insolvency or bankruptcy. The protection is provided to accommodation bonds, as defined in the *Aged Care Act 1997* (the Act), which are subject to a range of regulatory obligations, including prudential requirements, established in the Act.

The Bond Security Act sets out the framework for the operation of the guarantee scheme and the series of statutory declarations which must be made before a resident can recover their bond from the Commonwealth.

The critical trigger is an "insolvency event" which is defined in section 6 of the Bond Security Act. An insolvency event occurs in the following instances<sup>20</sup>:

- a winding up order is made against the approved provider entity, or
- the directors of an approved provider have passed a special resolution to wind up the company or
- the creditors of an approved provider entity have passed a resolution to wind

up the company at the second meeting of creditors<sup>21</sup>.

Even in circumstances where a provider does not have a premises to accommodate its residents, is unable to meet its obligations as and when they fall due or has entered into administration, it is not deemed an insolvency event within the meaning of the Act. As a consequence, residents are at risk of being placed into “limbo” during the period prior to the occurrence of a recognised insolvency event. This is what transpired following the collapse of Lifecare. Despite the fact that the landlord had taken steps to evict Lifecare from the facility, forcing residents to urgently find alternative accommodation, residents were not yet entitled to make a claim against the guarantee scheme for the refund of their bonds.

The Act provides the Minister with the power to make an ‘insolvency event declaration’ in circumstances where an approved provider is under external administration and the Department has satisfied itself that the provider is required to refund at least one bond balance. This declaration substitutes for one of the insolvency events described above.

The Secretary must make a ‘default event declaration’ as soon as practicable after becoming aware that:

- i) an insolvency event has occurred (by way of a trigger event or declaration); and
- ii) that at least one outstanding bond balance is payable.

Once the default declaration has been made, it is then incumbent on the Secretary to identify each outstanding bond balance and to verify the validity of any deductions which have been made to the bond balance in accordance with the *User Rights Principles 1997*<sup>22</sup>. This also includes calculating interest on the unpaid bond balance pursuant to section 12 (2)(c) of the Bond Security Act and sections 23.79D of the *User Rights Principles*. The interest component of the claim is critical, as the new aged care provider will invariably be charging the resident interest on any unpaid bond amount.

Upon collating this information the Secretary is then required to make a ‘Refund Declaration’<sup>23</sup> in respect of each resident who is entitled to a bond refund. The

content of that declaration must state the amount which the Secretary deems is refundable, taking into account any legitimate deductions which can be proven plus the payment of interest on the principal sum. The Commonwealth has an obligation to pay the amount specified in the refund declaration to the recipient within 14 days of making the refund declaration<sup>24</sup>.

Immediately after the refund declaration is made by the Secretary, any rights to recovery which the former resident had, as a creditor of the approved provider, are subrogated to the Commonwealth<sup>25</sup>. If the Commonwealth is unsuccessful in recovering bond refunds from the approved provider, the Minister for Ageing may impose a levy on all other approved providers to recover the full cost (plus administrative costs) pursuant to the *Aged Care (Bond Security) Levy Act 2006*.

#### **LIFECARE- COLLAPSE OF AN AGED CARE PROVIDER**

Slater & Gordon was retained by the representatives of five former residents of Lifecare's dementia aged care facility in Carrara, Queensland. Lifecare was operated by Lifestyle Care Providers Pty Ltd, one of four companies which collapsed as a result of insolvency. Our clients' unfortunate predicament proved to be the first known occasion that an approved provider failed to repay a bond, resulting in the first successful group claim being made under the *Bond Security Act*.

As a result of Lifecare being evicted from the facility, our clients were forced into finding alternative accommodation within a suitable aged care facility in September 2007. After some months waiting for their bonds to be repaid, our clients became concerned that Lifecare had dissipated their bonds and would be unable to refund the bond amount as a result of insolvency. In this case, the bonds were valued between \$120,000 and \$150,000 per resident with a collective amount of \$632,500 owed to our clients. These bond deposits represented a significant proportion of our client's life savings and were desperately required for the purposes of securing entry into their new aged care facilities.

In our claim to the Department, our clients disputed the outstanding bond

balance which had been identified by the liquidators. Lifecare claimed that it was entitled to make deductions and had done so pursuant to the Residential Care agreement. We argued that the validity of those deductions could not be substantiated as a result of Lifecare's failure to provide statements accounting for the deductions as required by the *User Rights Principles 1997*. This issue was a significant concern for our clients given that a collective amount of over \$52,000 in unaccounted for deductions had been made.

On 25 March 2008 our clients received notice from the Government that the full amount of their bonds, without any deductions, were to be refunded with interest. The basis for disallowing the deductions was due to the Department's finding that the bond agreements did not comply with the requirements of section 57-9 of the *Aged Care Act 1997*.

### **Lessons from Lifecare**

Whilst the residents were satisfied with the outcome of the claims process, it took nearly 6 months from when they were forced into relocating to another facility until receipt of the refund declaration by the Department. This delay may be partly explained by the fact that this was the first claim of its kind and partly by reason of the way in which the Act is structured.

The initial delay arose because liquidators were not appointed until 14 January 2008. The Department advised that the Bond Security Act did not provide it with legal standing to commence the insolvency process and advised our clients to seek legal advice. The directors of Lifecare ultimately declared insolvency and called a members meeting to appoint liquidators.

On 17 January 2008, the liquidators notified the Secretary that an event, defined as an insolvency event within the meaning of section 6 of the *Bond Security Act*, had occurred. Once the liquidators had notified the Secretary that an insolvency event had taken place, the Department was then placed under an obligation to make the first declaration (the default event declaration) as soon as practicable. It took the Department some 5 weeks to do so, because it wanted to obtain access to the companies' records to satisfy itself:

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- (a) that a *valid* resolution had been passed to appoint a liquidator of Lifecare; and
  - (b) that there was at least one bond balance outstanding.

Although pleased that the entire amount of the 'refund declarations' were made, the legislative basis for doing so was unexpected. The Department found that whilst 52% of the total amounts to be refunded were to be refunded under the provisions of the *Bond Security Act*, an amount representing 48% of the amounts to be refunded were to be refunded under the 'act of grace' arrangements provided for under section 33 of the *Financial Management and Accountability Act 1997*.

The Department determined that an aggregate amount representing 48% of the total bond payments/instalment payments advanced to Lifecare were advanced to Lifecare prior to it becoming an "approved provider" within the meaning of the *Aged Care Act*. The Department determined that in order for the bond payments to be deemed an "accommodation bond" payment, it must have been advanced to an "approved provider". Lifecare held itself out to the residents as an "Approved Provider" and within months of the bond payments being advanced, it did in fact become a Commonwealth approved provider. However, the Department adopted a literal interpretation of the Act and decided that only those funds advanced to Lifecare after it became an approved provider could be protected by the *Bond Security Act*. To avoid leaving the residents without the protection that was intended to be afforded to them under the Act, the Government agreed to the Department's application for those amounts not capable of being characterised as "accommodation bond" payments to be refunded under the *Financial Management and Accountability Act 1997*.

The timing of when Lifecare became an approved provider appears to have created an artificial distinction that is not easily reconciled with the underlying intent and purpose of the Bond Security Act. Having disputed this interpretation with the Department we are hopeful that legislative changes will be made. We have since been advised by the Department that it will re-examine the operation of the Act following the Lifecare Case.

It is also worth noting that the Bond Security Act does not provide for the reimbursement of legal fees incurred in connection with assisting claimants to take steps trigger an insolvency event and/or in respect to the preparation of claims.

## CONCLUSION

Aged care residents who entrust what is often a large portion of their entire lifetime savings have a legitimate expectation that their bond will be protected. Given that only one insolvency event has been reported since the bond system was introduced, it is reasonable to infer that the accommodation bonds system is working reasonably effectively. Of course it is only early days.

Practitioners should advise prospective residents of an aged care facility:

- to be satisfied that the prospective provider is an approved provider registered on the register of approved providers maintained by the Commonwealth Department of Health and Ageing;
- to be satisfied that the premises of the aged care facility has been certified by the local government that it meets Australian Building Standards;
- to be satisfied that there are no conditions on the prospective provider's registration;
- whether the accommodation bond agreement complies with section 57-9 of the *Aged Care Act 1997*;
- to request that the provider discovers the following information within 7 days:
  - (i) the number of bonds which were not refunded in the last financial year in compliance with section 57-21 (3) of the *Aged Care Act*. Legal practitioners should also enquire as to whether the provider complied with this division.
  - (ii) The independent auditors opinion as to whether the provider complied with the Prudential standards (ie. the liquidity standard) in respect of the preceding financial year
  - (iii) The most recent statement of the provider/organisation's audited accounts.

- If a provider does default in its obligations to refund your client's bond then you should act quickly to trigger an insolvency event or petition the Minister to make the insolvency event declaration.

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<sup>1</sup> Section 57-2(1)(l) The Aged Care Act 1997

<sup>2</sup> Bishop, J, Hansard second reading speech of the *Aged Care (Bond Security) Bill 2005*, 8 December 2005, page 13

<sup>3</sup> Section 57-2 (k)

<sup>4</sup> Section 57-3 *Aged Care Act 1997*

<sup>5</sup> Section 57-12 (3) *Aged Care Act 1997*

<sup>6</sup> Section 57-17 *Aged Care Act 1997*

<sup>7</sup> Division 10 *User Rights Principles 1997*

<sup>8</sup> Section 23.69 (1) *User Rights Principles 1997*

<sup>9</sup> Section 23:71 *User Rights Principles 1997*

<sup>10</sup> Section 57-19 (1) (b) *Aged Care Act 1997*

<sup>11</sup> Section 57-21A (3) *Aged Care Act 1997*

<sup>12</sup> Section 57-2 (e) *Aged Care Act 1997*

<sup>13</sup> Section 23.43 of the *User Rights Principles 1997*

<sup>14</sup> Department of Health and Ageing *Financial Information (aged care)*, 16 May 2006, <http://www.health.gov.au/internet/wcms/publishing.nsf/Content/aging-prudential-guidelines>, (4 Feb 2008) pp 2

<sup>15</sup> *Ibid* pp 5

<sup>16</sup> Sections 23.39 and 23.40 *User Care Principles 1997*

<sup>17</sup> Section 23:42 *Aged Care Act 1997*

<sup>18</sup> Section 23.42(3) *User Rights Principles 1997*

<sup>19</sup> Section 23.43 *User Rights Principles 1997*

<sup>20</sup> Pursuant to section 6 of the *Aged Care (Bond Security) Act 2006*, equivalent stages in the bankruptcy process have occurred if the approved provider is an individual as opposed to a corporate entity.

<sup>21</sup> Section 9 *Aged Care (Bond Security) Act 2006*

<sup>22</sup> Sections 12 (1) and (2) of The *Aged Care (Bond Security) Act 2006*

<sup>23</sup> Section 13 of The *Aged Care (Bond Security) Act 2006*

<sup>24</sup> Section 16 of The *Aged Care (Bond Security) Act 2006*

<sup>25</sup> Section 15 of The *Aged Care (Bond Security) Act 2006*