HEALTH AND COMMUNITIES AND LOCAL GOVERNMENT SELECT COMMITTEES JOINT INQUIRY INTO LONG-TERM FUNDING OF SOCIAL CARE

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March 2018

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Summary

We are researchers from the Health Economics Group at the Universities of East Anglia, the Personal Social Services Research Unit at the London School of Economics and Political Science and the Pensions Policy Institute. We have undertaken joint research on the interactions between reforms to the State Pension and reforms to long-term care funding.

The principal findings from our research which are relevant to this inquiry are:

1. Under the current long-term care funding system, we project that public expenditure on long-term care for older people would have to rise by 40% between 2020 and 2030, and by a further 26% between 2030 and 2035, just to keep pace with demographic change and likely real rises in earnings of care staff. The previously planned lifetime cap on care costs and associated increase in the asset threshold in residential care would add some £1.8bn (2015 prices) to public expenditure on long-term care by 2030, an increase of 14% on projected expenditure for that year under the current system.

2. We have examined the Conservative Party manifesto suggestion of including housing wealth in the means test for home care and introducing a single capital limit of £100,000 in both residential and home care. We estimate that these two changes could save £0.7bn (2015 prices) per year in public spending on long-term care by 2030, assuming that in the case of couples, only half of housing wealth would be included in the home care means test, whereas for single people the whole of their housing wealth would be included. An alternative version which includes in the residential care means test one half of the housing wealth of couples where one partner is in residential care (instead of disregarding it for couples as now) but applies a lifetime cap on care costs, would add about £0.2bn (2015 prices) to public spending on long-term care by 2030.

3. We have also investigated scenarios involving more generous eligibility criteria for adult social care. If for example all older people with moderate care needs were offered, subject to the means test, a personal budget sufficient to fund around 8 hours of home care per week, some 600,000 more older people would receive publicly funded care in 2020 at a cost of some £2.8 billion (2015 prices). This is by way of illustrative example and does not include the cost in respect of younger adult groups.

4. Revenue raising measures targeted specifically at people over State Pension age, such as increasing income tax rates or extending National Insurance on earned income for those over State Pension age, could raise revenue ranging from several hundreds of millions to over a billion pounds per year.

5. Savings from uprating the State Pension by earnings rather than the triple lock could be used to pay for more generous uprating of disability benefits and parameters of the long-term care means tests. If a lifetime cap on care costs was introduced, it would at first benefit mainly service users with higher wealth and incomes; but, if savings from replacing the triple lock were used to fund a more generous (i.e. a lower) cap, over time this would increase the benefit to services users on lower incomes.

Introduction

1. We are researchers from the Health Economics Group at the Universities of East Anglia, the Personal Social Services Research Unit at the London School of Economics and Political Science and the Pensions Policy Institute. Since 2014 we have been analysing the interactions between State Pension and long-term care reforms with funding from the Nuffield Foundation through a project called Care and State Pension Reform (CASPeR). The project was conceived when reforms to the State Pension system and to the long-term care system were both planned for introduction in April 2016. Little attention had been given to how the two systems interact with each other. We took as given the structure of the two sets of reforms and examined how they would interact under different assumptions on how the levels of key parameters would be set each year in the future.

2. A single tier State Pension was introduced in April 2016 as planned. Reforms to introduce a lifetime cap on an individual's liability for their care costs were postponed until 2020 and have now been superseded by a forthcoming Green Paper on the future funding of long-term care. The Government plans to publish this Green Paper in the summer of 2018. Meanwhile alternative options for reforms to the long-term are funding system continue to be suggested. As part of our research we have been able to examine the likely costs and distributional effects of some of them.

3. Many commentators have argued that, quite apart from how long-term care is funded, there is a need to expand the funding available to Local Authorities to meet rising demand for social care. The House of Commons Communities and Local Government Committee recommended in March 2017 that the Government should 'address the funding pressures being felt now; ensure that funding for social care is linked to need and rising demand ……'. (Communities and Local Government Select Committee (2017). The Committee urged that the Green Paper which had been recently announced by the Chancellor of the Exchequer, should consider 'taking funding from a wide range of sources, including hypothecating national taxation (income tax, National Insurance Contributions, asset taxes, inheritance tax) and all age-related expenditure (the State Pension, including the funding for the triple lock pension guarantee…..)'.

4. We have recently started to examine the scale of funding which might be needed to meet the funding pressures. We are also investigating some of the possible ways in which to fund increased public spending on long-term care for older people, whether that extra funding is for an expansion in Local Authority funded services or for changes to the means tests that are applied to establish user contributions towards home and residential care.

5. In this submission, we summarise the main relevant findings from our research to date. Our research is on-going and we expect to publish further analyses in the near future.

6. We summarise our findings under 3 headings: the costs and distributional effects of reforms to the long-term care means test; the cost of increasing expenditure on long-term care for older people to address some of the funding pressures identified by the CLG committee; and possible avenues for funding extra public spending on long-term care for older people.

7. Our analysis is based on a number of linked computer models which make projections of future State Pension costs, the future demand for long-term care for older people, its total costs, the division of those cost between the public and private sectors under different

economic, demographic and policy scenarios. The models allow us to examine the distributional effects (e.g. which groups would pay more or less for their care) under different forms of the means tests for care. The models are described in detail in Adams et al. (2016a).

8. We assume that the older population of England will increase, by age and gender, in line with the 2016-based Office for National Statistics principal population projection, that disability rates will remain constant and that earnings in the long-term care sector will rise broadly in line with Office for Budgetary Responsibility (OBR) assumptions for average earnings. The economic assumptions underlying the results presented here are consistent with those published by the OBR in January 2018. They do not take account of the revisions to the short term assumptions published with the March 2018 Spring Statement, but it is unlikely that those recent revisions would materially affect our analysis.

9. All the analysis of long-term care presented here relates to the older population (aged 65+) and to England.

10. More detailed papers describing the analysis underpinning this evidence can be found on the CASPeR web site (http://www.pensionspolicyinstitute.org.uk/casper).

<u>The costs of proposals to reform the means test for long-term care funding</u>

11. Our latest projections are that, under the current funding system, public expenditure on long-term care for older people (including disability benefits that are used to pay for care) would have to rise by 40% between 2020 and 2030, and by a further 26% by 2035, just to keep pace with demographic change and likely real rises in earnings of care staff. This is a rise from £9.4 billion to £11.1 billion in 2030 and £13.2 billion in 2035 (all in 2015 prices), and corresponds to a rise from 0.5% of GDP to 0.6% (2030) and then 0.7% (2035).

12. By comparison, over the same period we project that spending on the State Pension will rise from 4.4% of GDP to 5.9% of GDP assuming the new State Pension and the basic State Pension for people retiring before April 2016 are uprated annually by the 'triple lock' (the highest of the increase in average earnings, prices or 2.5%).

13. Following the Commission on Funding Care and Support (CFCS 2011), reforms were planned which would bring in a lifetime cap on what an individual has to pay towards their care costs. A means test would still apply until this cap was reached, and would also continue thereafter for the daily living costs ('hotel costs') element of residential care costs. As part of the reforms, for residential care there was also planned to be an increase in the asset threshold, above which residents would have to meet the whole of the costs of their care until they reached the cap. Using levels of the increased asset threshold, the cap and the daily living costs originally planned for implementation in April 2016, our latest projections suggest that these reforms would increase public spending on long-term care by £1.8billion (in April 2015 prices) by 2030 compared with the current system. The average weekly gain in 2030 from these reforms among residential and home care users aged 80+ would range from £20 (in April 2015 prices) for those in the lowest fifth of the income distribution[2] to £47 for those in the highest fifth. Expressed as a percentage of income, the gains are more equal across income groups.

[2] Income distribution is defined with respect to all people of that age group.

14. In May 2017, the Conservative Party published proposals in their election manifesto which would bring housing wealth into the means test for home care, with the possibility of a system to enable payments to be deferred until the home is sold (e.g. on death or entry to a care home). The proposals would also increase the total amount of assets that would be completely disregarded in the means test. There would be a single limit of £100,000 below which assets and any income from them would be completely ignored in the means test. No help with care costs would be available where assets are above £100,000. Subsequently the Prime Minister said there would also be a lifetime cap on care costs.

15. Details were not given on precisely how housing wealth would be included in the home care means test or indeed on the level and form of the lifetime cap. Issues which would have to be determined include:

    i. In the case of couples, the current home care means test is usually based on the income and assets of only the partner receiving home care. **How much of the value of a couple's (jointly owned) home would be included when housing wealth is included in assessable assets?**

    ii. If at least some of the value of the joint home of couples is included in the means test for home care, **would the value of a couple's home continue to be completely ignored for the means test for residential care or would the treatment of housing wealth be the same in home and residential care?**

    iii. The 12 week disregard that applies to housing wealth in the residential care means test is at least in part designed to give the person entering care time to sell their home, although it also gives time for the resident to set up a deferred payment arrangement with their Local Authority. **Would there be a 12 week disregard for home care?** If not it might be hard to justify one for residential care.

    iv. If a 12 week disregard were applied to home care, **would there be a 12 week disregard for residential care where one has already been applied for home care?**

16. We have examined the costs of two possible approaches based on the Conservative Manifesto proposals and on the components of them:

    i. The whole of housing wealth is included in the home care means test for single people and half of it is included for couples. There is a 12 week disregard on housing wealth in home and residential care. Housing wealth continues to be disregarded in full for couples where one partner is in residential care.

    ii. The whole of housing wealth is included in the home care means test for single people and half of it is included for couples. The same applies in residential care (i.e. in place of a full disregard of housing wealth where a partner continues to live in a care home resident's home, half of the value of the home is included in the residential care means test). There is no 12 week disregard on housing wealth in home or residential care. However a lifetime cap at a level equivalent to that originally planned for 2016 (£72,000) is applied.

    In each case, the current lower and upper capital thresholds are replaced with a single threshold of £100,000.

17. We estimate that by 2030 version (i) of these proposals save £0.7bn (in 2015 prices) in public spending on long-term care for older people. There would be a cost to the public purse of implementing the single capital threshold of £100,000 of some £1.2bn but this would be more than offset by savings from including housing wealth in the home care asset test. The effect of version (ii) of the proposals would be an additional cost to public expenditure on long-term care for older people of some £0.2bn by 2030, compared with a continuation of the current system.

The cost of addressing some of the long-term care funding pressures

18. We have explored two scenarios on expansion of eligibility for publicly funded community-based care for older people. These are intended to be illustrative, to give an indication of the scale of resources that could be required to meet possible changes to eligibility criteria. We do not in these scenarios assume any change to the means test for community-based care.

19. The Care Act 2014 provides for national minimum eligibility criteria for publicly funded adult social care. While Local Authorities have discretion to operate more generous eligibility criteria, in general only people with high levels of care needs (critical or substantial) receive publicly funded care. Moreover, not everyone with high needs receives publicly funded care: some people are not eligible under the means test – because of their savings and/or incomes – and some may not want to receive publicly funded care.

Scenario 1: Care for people with high level needs, subject to means test

20. Our first scenario involves assuring a minimum level of personal budget[3], subject to the means test, for all older people with a high level of need. More specifically we investigate a scenario under which older people with three or more limitations in Activities of Daily Living (ADLs) (such as bathing, dressing and feeding) would be eligible for medium intensity (around 8 hours per week) home care and older people with two ADL limitations would be eligible for low intensity (around 3 hours per week) home care[4].

21. Our modelling suggests that, if this scenario was implemented by 2020, some 185,000 additional older people would receive personal budgets for low intensity home care and some 330,000 additional older people would receive them for medium intensity home care in 2020. These numbers are projected to rise in 2030 to 225,000 and 410,000 respectively. The net cost to local authorities would be £2.05 billion in 2020 and is projected to rise to £3.0 billion in 2030 (at constant 2015 prices).

22. It should be noted that some older people meeting the criteria in terms of ADL limitations might not in practice apply for and accept publicly funded care. This could apply especially to older people with incomes such that they would be required to contribute to the cost

[3] A personal budget is a statement from a Local Authority that sets out the cost to the local authority of meeting an adult's care needs

[4] Personal budgets sufficient to fund these levels of care would be guaranteed for all those who meet both these ADL-based eligibility criteria and the means test conditions (but whose needs were not sufficiently high to receive residential care or high intensity home care).

of their care through user charges. (People who would be ineligible for any publicly funded care because of high incomes or savings are excluded from the estimates above).

Scenario 2: Care for those with moderate needs

23. Our second scenario involves extending the eligibility criteria to cover those with moderate needs, again subject to the means test. A study by Fernandez et al. (2013) investigated the impact of extending eligibility to include moderate needs. Their analysis showed that to provide care for moderate needs would imply a total of 889,000 older service users in 2010 and 1,075,000 older users in 2020.

24. Since there are currently around 400,000 older Local Authority funded service users, this implies that the number of older publicly funded service users would need to rise by over 150% by 2020. We assume that the additional service users would receive, subject to the current means test, a personal budget sufficient to purchase medium intensity home care of around 8 hours per week.

25. Our modelling suggests that, if this scenario is implemented by 2020, some 620,000 additional older people would receive personal budgets for medium intensity home care. This is projected to rise to 700,000 in 2025 and 810,000 in 2030. The net cost to local authorities would be an estimated £2.8 billion in 2020 and is projected to rise to £3.45 billion in 2025 and £4.4 billion in 2030 (at constant 2015 prices).

<u>Potential revenue raising options</u>

26. HMRC analysis projects that for the 2018-19 tax year increasing income tax rates for all taxpayers by 1p in every £ would raise £4.8bn (HMRC 2018) for the UK. As an alternative, a reduction of income tax personal allowances for all taxpayers by £100 would raise £580m (HMRC 2018).

27. If the purpose of the revenue to be raised is to fund higher public expenditure for older people (at least those who need care), and given concerns over intergenerational fairness, it may be of interest to consider how much revenue could be raised from measures aimed at raising revenue solely from older people. We have examined illustrative measures which modify income tax or National Insurance contributions (NI) for people over State Pension age.

28. The analysis is based upon 2014-15 income data; we have not attempted to adjust the analysis to current prices or make projections for the future[5]. The analysis is intended to provide an order of magnitude of impact only.

29. In the 2014-15 tax year, 22% of UK taxpayers were aged over State Pension age (SPa), accounting for 17% of income tax liability. The 22% correspond to 6.8m individuals over SPa (approximately two thirds of those over SPa) and they had a combined income tax liability of approximately £22bn. Around 83% of this £22bn tax liability is paid by those in

[5] Nor have we considered any potential behavioural responses or allowed for any increased cost of collecting tax receipts. HMRC estimate that in 2018-19 this cost would outweigh any potential yield from increasing the additional rate of income tax (paid only by those with taxable incomes above £150,000) (HMRC 2018).

the top 20% of people by income aged over SPa. Around half of the £22bn income tax liability is paid by those with a higher or additional marginal rate of income tax.

30. Raising income tax rates by 1p in the £ for those aged over SPa could raise an additional £950m revenue upon their existing £94.5bn of taxable income. This would affect all of the 6.8m individuals already paying income tax. Restricting the change to higher and additional tax rates would result in additional income to the Treasury of £200m, affecting around 570,000 taxpayers over SPa.

31. Approximately £145m could be raised by reducing income tax allowances by £100 for the 6.8m taxpayers aged over SPa.

32. Currently, individuals aged over SPa do not pay NI on any earned income. Levying employee NI contributions on the earnings of people over SPa on the same basis as for people under SPa, (i.e. applying Class 1 employee NI rates to employee earnings and Class 2 and Class 4 NI rates to self-employment profits) could affect around 1m individuals. It would result in an average annual NI liability of £1,400 per affected individual in 2014-15, with an aggregate NI revenue of £1.4bn.

33. Rebalancing spending on State Pensions and publicly funded long-term care through annual inflation upratings.

34. Minimum annual uprating of the State Pension is laid down in legislation. The new State Pension must be uprated by at least the rise in average earnings. For some years the basic State Pension, and now the new State Pension, have in practice been uprated by the 'triple lock'. Legislation governing uprating of the parameters of the means tests for long-term care is less prescriptive than for State Pensions. Recent practice for many long-term care parameters has been at best price linking. Capital thresholds have not been uprated at all for some years.

35. The expectation for the lifetime cap on care costs and the daily living cost components of the previously planned reforms was that they would be linked to earnings. This implies that, as we go further into the future, the time it would take to reach the cap would rise faster than if it were linked to prices, as would the portion of care home fees remaining means-tested.

36. Disability benefits (Attendance Allowance and Disability Living Allowance/Personal Independence Payment) also provide help with the costs of disability in old age. These benefits have been uprated by prices in recent years.

37. In previous analysis (Adams et al. 2016b) we investigated the likely effects of a gradual rebalancing of state spending from State Pensions towards long-term care funding for older people through less generous uprating of the State Pensions and more generous uprating of the parameters of the long-term care means tests.

38. In our research we contrasted the effects of introducing the reforms to long-term care then planned for 2020 under a range of different uprating assumptions for State Pensions and the parameters of the long-term care means tests. We found that:

i. By 2030, the savings from uprating the State Pensions by earnings rather than the triple lock would more than pay for more generous uprating[6] of disability benefits and the previously planned cap and associated reforms to the long-term care means tests compared with its cost under expected uprating policy.

ii. More generous uprating of the means tests for long-term care tends to favour those users of home and residential care on lower incomes. While the proposed cap on care costs tends to benefit those on higher incomes and wealth, over time the gap between the gains to those on higher and those on lower incomes would be reduced by more generous uprating.

Acknowledgements

The research underpinning this submission was funded by the Nuffield Foundation but the views expressed are those of the authors and not necessarily those of the Foundation. All responsibility for the analysis reported here rests with the authors.

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Further supporting analysis can be found at http://www.pensionspolicyinstitute.org.uk/casper

[6] Most parameters linked to earnings rather than prices; the cap and daily living allowance linked to prices.