Placard

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The number of people in care is expected to double by 2035. The UK's population is ageing rapidly. Our society faces stark decisions about how to meet and manage the associated costs.

SOCIAL CARE IN CRISIS: FINDING A COMPREHENSIVE LONGER-TERM SOLUTION

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Permanent solutions are necessary if we are to stem the drain on NHS resources and already-stretched local authority budgets. We cannot resolve these issues simply by throwing cash into a failing system and it is becoming increasingly clear that fundamental reform is needed – perhaps on a scale not seen since the Beveridge report in 1942 and subsequent founding of the modern welfare state.

In this edition of *Placard*, **Sir Steve Webb** (former Minister of State for Pensions and now Director of Policy and External Communications at Royal London) explores possible solutions to the Social Care conundrum, and **Tom Kenny** (Chair of IFoA Health and Care Working Party's Products Research Group) continues the discussion, describing the work of the IFoA's Pensions and Long-term Care Working Party.

ACA Key-point: ***Actuaries could have a role to play in helping government find a solution to social care funding by:***

- ***Developing insurance solutions to social care***
- ***Developing equity release products to enable more individuals to use their housing wealth to fund their social care***
- ***Applying knowledge of demographics and long-term financial modelling to propose alternative funding solutions.***

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Costs are running away

It is estimated[1] that the UK will spend £12.7 billion per year by 2022 on social care and continuing healthcare for the elderly (an increase of 37% versus 2010) but, as individuals, we are doing next-to-nothing to save towards these costs, even though the State will pick up only part of them. While UK adults estimate their elderly care bill to come in at around £550 a week, the true cost is closer to £870 – a gap of £320 per week per adult – according to the Centre for the Modern Family (CMF)[2]. A survey by the CMF found:

One in four people admit they have no idea how they would cover elderly care costs for themselves or a relative, and yet overwhelming evidence suggests we need to. Around four million older Britons – nearly 40% of the over 65s and almost half of those over 75 – currently have a life-limiting and long-standing illness.

42%

42% of people have £2,000 or less in life savings to fall back on, meaning they would only cover the costs of care for a maximum of two and a half weeks in the absence of other support. Instead, half of us expect to be able to rely on a relative even though, for example, we estimate that we could only afford to spend £69 a week on care for our parents.

Raising awareness is vital

Clearly more must be done to raise awareness of the costs of care and to incentivise people to save. Last year's Conservative Party initiatives on residential / at-home care – using the value of our homes, rather than relying on the council to cover the costs of home visits by care workers – highlighted the confusion around this topic. This stems from the common misconception that the State pays for social care needs. Unlike NHS healthcare, social care is means-tested so many have to self-fund costs below a certain threshold or of a specific type.

How sustainable is this? Young people struggle to afford to buy their own homes! Saving to cover unknown, uncertain later-life care costs is understandably therefore not a priority for many in the workforce.

There does, however, appear to be a growing acceptance that individuals would have to be responsible for paying for themselves, with research published by financial services firm Just Group showing that:

– more than half thought the government would pay for their care in 2011, but that this had fallen to less than a third in 2017; and
– approximately one-third of over-45s would be willing to sell their homes if needed.[3]

Funding shortfall is growing

This gap in funding for social care is already a problem. The National Audit Office has warned that one in ten councils will have exhausted their social care reserves within the next three years if the current rate of expenditure continues. Something else garnering a lot of attention in the UK Press is the apparent "postcode lottery" in care services, with the Care Quality Commission saying:

"A quarter (24%) of the social care services in the 10 most deprived areas in England have been deemed to be inadequate or in need of improvement compared with only 15% of those in the 10 richest areas. It means the proportion of inferior services on offer in the poorest areas is far higher than the national average of 20%.

[1] *Source: The Select Committee on Public Service and Demographic Change – Figures are based on a care home without nursing and include daily living costs and top-up care costs*
[2] *Source: The Centre for The Modern Family – The Cost of Care research 2017 – a nationally representative opinion survey of 2,001 UK adults carried out in 2017.*
[3] *Source: www.justgroupplc.co.uk/~/media/Files/J/JJRMS-IR/news-doc/2018/180621-property-and-paying-for-care-double-pages-final.pdf*

Councils in these poorest areas, which have suffered the most from cuts in funding from central government, have been hit the hardest and they also have fewer people paying all of their care costs, putting further strain on the services offered."

"Average spending by councils on social care fell by 13% between 2009 and 2010 and from 2016 to 2017. Over the same period, about 400,000 fewer older people received social care, as the eligibility criteria were tightened by local authorities trying to cope with the costs".[4]

So what is the UK Government proposing to do to address the current and growing problem? We expect to see a Green Paper on social care for older people in the "Autumn/maybe Winter" of 2018 (already pushed back several times). The anticipated contents of the Green Paper are summarised in Parliamentary Briefing Paper 8002.[5] The Government is intending to look at social care more broadly, and not just how individuals pay for it. It will also include integration with health and other services, carers, workforce and technological developments, among others.

Time for a social insurance scheme?

A recent article in *The Times* notes one of the more radical "social insurance" ideas being discussed by the Department of Health and Social Care and the Treasury, which is for individuals to make a one-off contribution on retirement that would be used to fund social care, or support at home, if needed later in life:

"Younger people would be encouraged to save for the levy, with tax breaks on ring-fenced savings schemes. Those who reached retirement without enough cash could defer payment until after their death, with the money taken from their estate. The idea is not dissimilar to a plan put forward by Labour before the 2010 election, which was denounced as a "death tax" by the Conservatives. Senior Tories now believe it was a mistake to play politics with such an important issue. Some ministers have also become convinced that it would be unfair to increase taxes on the working-age population, which is already struggling with housing costs, when older people have greater assets."[6]

Local councils have clearly been frustrated by the lack of progress on these issues. This has resulted in the Local Government Association (LGA) launching its own version of a green paper: "The lives we want to lead"[7] The LGA highlights that as we are living longer, the current system is under extreme pressure, with adult social care and the service facing an estimated annual shortfall of £3.56 billion in 2025.

Based on the statistics in the LGA's Green Paper, the £3.56 billion shortfall could be met in 2024/25 by:

- Means-testing winter fuel payments (currently free to those over a certain age) [£1.9bn] plus an annual social care premium of £52 per person aged over 40 [£1.6bn];
- Adding 0.8% to the Basic rate of income tax
- Adding 2.4% to the Higher rate of income tax
- Adding 8% to the Top rate of income tax
- 1% National insurance (NI) for those over retirement age [£1.1bn] plus additional 0.24% NI for those under retirement age

Other less-effective suggestions include adding 1% to council tax bills (raising £285m) and / or charging on an affordability basis for accommodation costs for long-term and complex health cases (raising £200m). The LGA's consultation closes on 26 September 2018.

"The ACA's 2018 Pension trends survey found over 40% of employers favour tax changes that encourage social care costs to be met from private pensions, but 52% are 'undecided' on the merits of a compulsory social insurance scheme."

[4] *Source: www.theguardian.com/society/2018/jun/03/data-confirms-postcode-lottery-care-for-the-old*
[5] *Source: https://researchbriefings.parliament.uk/ResearchBriefing/Summary/CBP-8002*
[6] *Source: The Times, 24 July 2018: "At last, a radical solution to the social care crisis" by Rachel Sylvester*
[7] *Source: https://futureofadultsocialcare.co.uk/*

"Two-thirds of employers want social care costs to be met by higher general levels of tax or national insurance"[8]

Media attention

There have been many articles written about the growing trend for pensioners to hoard wealth rather than allow themselves the higher living standards they could afford in retirement. In many cases this is due to retirees having finances locked up in the value of their homes. An article by Paul Johnson, director of the Institute of Fiscal Studies, points out one driver of this failure to spend wealth in retirement *"may be the fear of costs of social care towards the end of life. The combination of a lack of a private insurance market and lack of public provision could lead people to save money just in case. If that is what is happening, it is incredibly inefficient and potentially very damaging to the wellbeing of those concerned…… Which is just another way of saying that the failure of government to deal with social care policy remains staggeringly costly and damaging".*[9]

The long-term care market in the UK has for many reasons been slow to develop. Other countries have been much swifter to develop such models and the UK can look to learn from them. Theresa May has set up a committee to gather evidence from experts which has considered how Germany and Japan have addressed social care issues. A recent article in the *Financial Times*[10] summarised these initiatives:

Japan

- Has one of the world's fastest ageing societies. More than a quarter of the population is aged over 65.
- 28% of workers over age 40 said they were considering quitting their jobs to nurse an ageing relative (according to a survey by Japan's Federation of Trades Unions).
- For the past 17 years, those over 40 pay into an elderly care insurance system, with premiums calculated according to income and where they live. Over 65s have payments deducted from pensions.
- State medical services operate a system of co-payment, whereby individuals bear between 10% and 20% of the cost.
- The above was still considered inadequate and further reforms are being made.

Germany

- The number of people aged 67 and over is expected to rise to 21.5m by 2040 (42% higher than in 2013).
- 2.9m Germans needed care at the end of 2015 (8.9% higher than in 2013).
- Medical care costs were €344bn in 2015, or €4,213 per person (42% higher than in 2013).
- The Government social care insurance system was introduced in 1995.
- The national care insurance fund, funded from pay deductions with employer matching, took in €31bn and spent €29 bn in 2015 while increasing reserves to €8.3bn.
- Care spending has risen sharply – 56% more in 2015 versus 2005.
- Pay deductions have been increased this year by 0.2%, to 2.55% of income.
- Any shortfall in costs still needs to be made up by self-funding / family support.
- Three quarters of those needing care are looked after in their own homes (an aim of the reforms).
- Someone with dementia being cared for at home now receives €1,298 pm (€609 more than under the old system).

[8] *ACA 2018 Pension trends survey*
[9] *The Times, 11 June 2018, Article by Paul Johnson*
[10] *Source: www.ft.com/content/3507b50c-0276-11e7-ace0-1ce02ef0def9*

Funding social care costs is, of course, a sensitive and complex issue. There are many wider issues at play here – such as questions around fair pay in the social care sector, and the interaction of funding and care provision with existing healthcare or retirement benefits. The 2017 election debate has helped to publicise the problem and we welcome the fact that it has begun to feature strongly on the political and social agenda.

ACA Key-point: ***The ACA hopes the upcoming Green Paper on social care policy will be radical and balanced in looking to a range of long-term funding reforms to support our ageing population. Whatever the approach, it must look to deliver an integrated savings policy for later life – factoring in that younger generations have much lower savings and no 'generous' defined benefit pensions to fall back on. It must also offer genuine incentives to those who can afford to save whilst also providing an underpin that secures a good standard of care for all.***

This Autumn's Green Paper on social care policy, and the public consultation that follows, will no doubt spark some healthy debate! However, we hope that sustained political appetite for reform with appropriate support from healthcare professionals and interested parties from the financial community (including actuaries) means it won't fizzle out.

IS IT TIME FOR THE CARE PENSION?

Sir Steve Webb, former Minister of State for Pensions and now Director of Policy and External Communications at Royal London

There are many things that could happen to us in our life which could cause us to incur unexpected and potentially 'catastrophic' costs, ranging from our house burning down or us needing complex, specialist medical treatment. In response, we do not each individually save enough money on the off-chance that we have to rebuild our house or pay for brain surgery – we get together and take out home insurance or we pay taxes and are covered by the NHS.

However, as the 'Dilnot' Commission into the funding of long-term care pointed out, the risk of facing catastrophic later life care costs remains the 'last big unpooled risk'. Whereas health needs are covered by the NHS, help with social care is only available free of charge to those with very limited resources. Anyone else has to meet their own care costs and with typical weekly costs for nursing or residential care approaching £1,000 per week, the total bill can quickly mount up. And yet there is virtually no functioning market for care insurance, with the one exception of 'immediate needs' annuities which are bought for a lump sum on admission to a care home.

In a recent Royal London Policy Paper – 'Is it time for the care pension?' – I examine the supply and demand reasons why care insurance products are largely unavailable and suggest one way in which such products might be brought back onto the market.

Confusion abounds

On the demand side, there are a number of reasons why people are reluctant to buy care insurance. First, people are fundamentally confused about what the State will provide in the event of a care need arising. The general public does not make the distinction between 'health care' and 'social care' and there is a widespread (though incorrect) assumption that you will be looked after in your hour of need. There is therefore little appetite to take out private insurance if you think the government will pay in any case.

A second demand-side barrier is the assumption that 'it will never happen to me'. The majority of us probably will not face an extended period in residential care in later life. Unless you have first-hand experience of residential care, perhaps through a family member, you may also have little idea just how quickly the bills can mount up.

No meaningful tax breaks

A third demand-side issue is the lack of incentives to take out care insurance. Someone taking out a pension gets up-front tax relief on the contributions plus the benefit of a tax-free lump sum. By contrast, despite the fact that those who take out care insurance are potentially relieving the state of a future burden, there are no meaningful tax breaks for care insurance.

An issue that straddles the demand and supply side of this market is that such products are generally 'sold not bought', and the appetite of financial advisers to promote freestanding care insurance has been limited. Where such products existed in the past they had to be sold as a separate product by advisers with specialist qualifications. With a limited market and the option of selling other products that are easier to sell, it is easy to see why the number of people going out and selling care insurance was limited.

From the perspective of product providers, care insurance is a challenging market. Future care costs are hard to estimate and this is an area heavily influenced by changes in regulation and public policy. Guessing the extent of State support for care in future decades is challenging, and regulatory changes such as the national living wage or rising building standards for care homes can have a big impact on the cost of providing care.

In addition, future medical advances could have big and unpredictable consequences. In a positive scenario we could have medical breakthroughs which tackle the diseases which leave us needing prolonged later life care and medical intervention, and this could reduce the amount that people need to spend in later life. On the other hand, we may find new ways of keeping people alive which mean that stays in residential and nursing care could be significantly extended. If policies are taken out decades ahead of the onset of care, the pricing of such policies would be exceptionally difficult.

New opportunities

Recent changes in pension provision do however provide an opportunity for providers to innovate and offer new ways of pooling the risks of catastrophic care costs.

Until relatively recently, most people reaching retirement did so with an 'income for life', either in the form of a Defined Benefit (DB) pension or through an annuity bought with a Defined Contribution (DC) pension pot. However, the death of DB provision in the private sector and the growth of auto-enrolment into predominantly DC provision is likely to change this situation. More people are likely to reach retirement with an un-annuitised DC pension pot, and DB to DC transfers are adding to the numbers who reach retirement with an investment pot rather than a pension.

This provides the opportunity to look at existing decumulation products such as 'drawdown' accounts to see if a care insurance could be grafted on. This could either be in the form of a lump sum policy bought at retirement or a regular premium insurance taken from the drawdown account throughout retirement. I suggest that this might be marketed as 'inheritance insurance', helping to ensure that people can pass on the value of a family home in full in the event that substantial care costs were to arise. One advantage of grafting this feature onto drawdown accounts is that these are products with which advisers are already familiar and discussing with clients, and this would simply be an additional product feature.

"Three-quarters of employers say social care costs borne by individuals should be capped"[11]

Policy changes to grow market

Whilst such products could, in principle, be introduced today, there are two policy changes which I believe would help such a market to grow. The first would be a favourable tax treatment, so that withdrawals from the drawdown account to pay for care insurance would be tax free. This would increase the attractiveness and affordability of the policy to consumers. Second, providers would value an overall 'cap' on any individual's lifetime exposure to potential care costs. This would help to ensure that major genetic or medical advance or major changes to the social care system did not expose providers to an open-ended liability.

Time ripe for the 'care pension' concept

There are many questions of detail which would need to be resolved, and this approach is clearly only one part of a complex jigsaw of responses to the social care funding crisis. But after two decades in which multiple expert reports and policy reviews have failed to turn into practical solutions, the 'care pension' concept could make a valuable contribution to ensuring that fewer people in the future are exposed to the risk of catastrophic care costs.

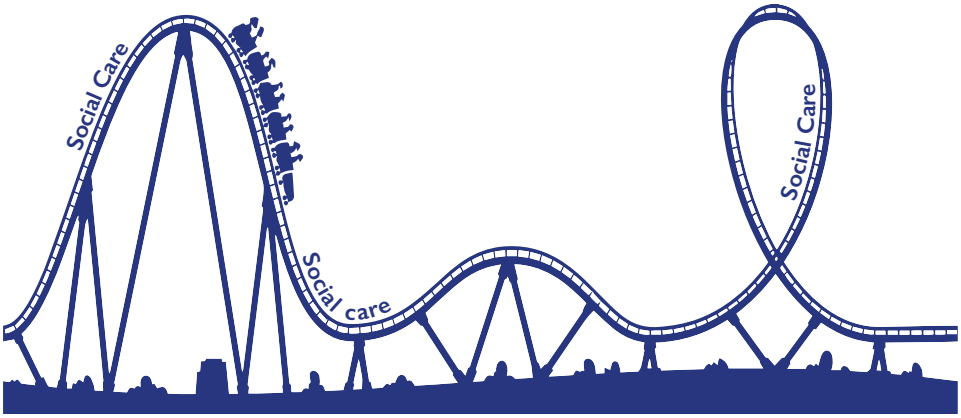
DOES THE GOVERNMENT CARE ABOUT LONG TERM CARE?

Tom Kenny,
Chair of IFoA Health and Care Working Party's Products Research Group

It was a rollercoaster of policy messages and media statements from the government in 2017 on adult social care. We had the excitement of announcements that they were going to make the tough decisions of government and finally lay out a plan for social care funding, including the announcement that there would be a green paper published in 2017. We then had the confused messages and media frenzy that was produced by the Conservative general election manifesto, and reference made to a 'dementia tax'.

We are now in the second half of 2018 and the Green Paper is now going to be published 'later' in 'the autumn/winter'. The Health & Care minister has made a statement that there will be a cap on care costs, but it is still unclear what form this will take. It is clear that making changes to social care funding is politically difficult, but there are really only three choices: increase government funding through taxation; increase private funding or reduce the quality of care being provided by the State.

[11] *ACA 2018 Pension trends survey*



In the General Election, there was widespread concern by the over 65's that they might need to use their home to pay for their care – the message that most people who have sufficient assets currently have to pay for their care seemed to get lost. This highlighted the clear lack of understanding of the current system among the general public, referred to by Sir Steve Webb in his article, and the widespread belief that they shouldn't pay for it. In the same way that middle-aged adults often avoid later life conversations with their parents, the policymakers of our country need to stop avoiding this difficult issue, and we urgently need to have cross-party agreement about who should pay and then simply get on with making the change to our social care system.

What is the Care Cap?

Under the Care Act 2014, a cap on social care costs of £72,000 was legislated for. Once the cap is reached the state pays for care costs – this is typically reached after 5 years under the £72,000 cap. However, the cap only includes the local authority rate, so doesn't include accommodation costs (aka 'Daily living costs') or any top-up costs[12] above the local authority rate. This means that individuals can typically expect to spend over £240k after 6 years.

The Health and Care Working Party of the Institute and Faculty of Actuaries (IFoA) has been undertaking research since 2013 analysing the impact of the Care Act and the potential pension and insurance products that could be used to help fund long term care (LTC). The results of this research were published in 2014 ('How can pensions help meet consumer needs under the new Social Care regime') with a follow-up paper in 2016 ('The Future of Social Care Funding – Who Pays').

Key findings were:

- Pensions savings are unlikely to be sufficient on their own to enable someone to meet their LTC needs.
- There is no single product that ideally solves the LTC problem for everyone. Prefunding has its challenges, particularly if there are no incentives or nudges to encourage prefunding.
- In addition to pension products, Immediate Needs Annuities, pre-funded protection and equity release type products could be part of the solution to increasing private funding of LTC.
- There is significant regional variation in the way the care cap potentially benefits individuals with significant variations in the expected personal costs and the likelihood of reaching the cap by region.
- The means test as currently applied creates significant disincentives to save, in some cases saving additional money leads to an individual being in a worse position overall as the reduction in State benefits received exceeds the money saved. The new means test under the Care Act would reduce the level of disincentive significantly.

[12] *Top-up costs are common among self-funders as there is currently a significant differential in the fees self-funders pay for care vs the fees local authorities pay for exactly the same standard of care in the same care home – self-funders are currently subsidising local authority funded individuals in care.*

More recently, the Health and Care Working Party supported the joint publication of a paper in November 2017 with Independent Age and the IFoA on the social care system ('Will the cap fit?'). A key recommendation in the paper suggested that the government should consider resetting and reframing the cap ('all-inclusive cap') to be at a level which would kick in after around 3 years (typical life expectancy for someone with high care needs e.g. in residential care or nursing care); and to include all care costs including Daily Living Costs and typical top-up costs. The idea behind the proposal was to create a simpler care system that individuals can understand, so that they can potentially take actions to protect themselves against the average cost of care in retirement.

What else is the working party looking at?

The working party has several strands of research and activity in progress at the moment, including:

1. Analysing different means test limits and cap levels to understand the varying impacts on individuals.

2. Development of a Retirement and LTC projection tool to be hosted on a consumer advice website to enable the general public to better understand their potential care costs and how it could affect the money they have available in retirement, and what they may have left in the form of inheritance.

3. Australia has been making similar changes to their social care system as the UK over the last few years, so we are undertaking a comparison between the UK and Australia to see if there are any lessons that can be learnt.

4. Data – there is a general lack of publicly available data on long term care to support detailed research and modelling. We are looking to help local government develop a framework for collecting and publishing anonymised data that can be used to support LTC modelling, which can inform public policy, but also support product development in the insurance industry.

Let's hope 2018/19 are years in which government policy on social care becomes clearer, and we can get off the social care policy rollercoaster!

***Placard* is the periodic discussion paper of the Association of Consulting Actuaries. Please note that the views expressed in this publication are the views of the individual authors.**

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