PENSIONS POLICY INSTITUTE
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Technical Report: Care Funding

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Introduction

The care funding system in England has been widely perceived to need an overhaul. The ageing population means there are more people than ever reaching older ages and in need for care. In September 2021, the Government announced a plan for health and social care in England which would introduce a lifetime cap on personal care costs of £86,000 and increase the thresholds of the means-tested support provided by Local Authorities.[1]

The Association of British Insurers (ABI) wished to understand what care costs those over 65 would face and how they may meet these costs, and asked the PPI to research this.

This paper seeks to examine the impacts of the changes to the social care funding on different groups of people, and identify the population groups whose care costs will be fully funded by the state, partially funded by the state, or self-funded. It also aims to determine the sources of wealth that people may use to meet the costs of care. The report also considers the extent to which additional sources of income or wealth help them meet their care and care-related costs.

Key findings of the report include:

- The care cap could help people reduce their care spending, but only for those that would have otherwise faced catastrophic care costs, such as an intense and long care journey.
- The increased means-test asset thresholds are likely to increase the number of people eligible for means-tested support in paying for care.
- While nobody is likely to be worse off under the proposals, many people who are current recipients of support will see very little change.
- It would take a self-funder over three and a half years of paying for residential care at the average rate of Local Authority arranged care cost to breach the cap, and longer for those receiving means-tested support.
- Only around a quarter of people survive more than three years in a care home.
- An additional income or lump sum could help some people, but for those relying on means-tested support, it would also reduce the amount of Local Authority support received.

[1] HM Government. (2021). Build back better. Our plan for health and social care. Available at: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1015736/Build_Back_Better-_Our_Plan_for_Health_and_Social_Care.pdf

The care funding system is very complex and an individual's possible future position within it depends on many unknown factors, including: the possible extent of care required; the financial position of the person in the future; and their relationship status. All of these factors can have a bearing on the individual's assessed wealth. This makes it very difficult for individuals to plan for care without specialist advice.

Chapter 1: Reforming social care provisions

Social care is the provision of various services that support "people of all ages with certain physical, cognitive or age-related conditions in carrying out personal care or domestic routines", and help "people sustain employment in paid or unpaid work, education, learning, leisure and other social support systems".[2]

Care is provided on either a formal or informal basis. Informal care is generally provided by friends and family who, while typically dedicated and diligent, are not professional carers, for example, those looking after an elderly relative. Formal care is undertaken within the care system by professional carers. The funding of formal care is the focus of this report.

Care can either be provided to people who reside in their own home, i.e. domiciliary care, or in specialist residential care homes and nursing homes. In care homes, the residents face both "care costs" associated with the care they receive, and "hotel costs" covering other associated costs such as accommodation and food.

What is the current situation for individuals in terms of paying for care?

Local Authorities are responsible for the provision of social care for those eligible for support. When a care need arises, individuals, or those acting on their behalf, can ask the Local Authority to undertake an assessment of the care needs. They will also undertake a financial assessment of the individual to establish how much of the care costs fall on them.

NHS data suggests that 552,000 people aged over 65 accessed long-term care support in England during 2020/21. This is around 5.3% of the over-65 population. Current spending on care to support people aged over 65 in care arranged by Local Authorities was around £7.7 billion in 2020/21, of which around £2.2 billion came from payments by the individuals themselves.[3]

In addition, there are people who fund care privately without Local Authority support. These are called "self-funders". This is generally because they have capital and savings above the levels that would grant them Local Authority provision. The data on self-funders is not collected by the Department of Health and Social Care, making it difficult to gauge the number of self-funders. The National Audit Office (NAO) quotes a Figure of 137,000 self-funders aged 65 and over in England living in independent sector care homes, who may be paying a premium of around over 40% on top of Local Authority placement costs.[4] Informal care, which is provided by unpaid carers, such as family members, neighbours, and friends, does not have a spending cost outgo in the same sense as formal care. However, the NAO estimated that in 2016/17 the value of informal care was much larger than formal care. They estimated the value of informal care as being up to £100 billion and that, if informal care were

[2] Commission on Funding of Care and Support (2011)
[3] NHS Digital (2021)
[4] NAO (2021)

not available, the cost of the care that would fall on the state might be around £59 billion, for adults aged 18 and over.[5]

People over State Pension age who do not receive means-tested care support from the Local Authority may still receive some money from the government that is used to pay for care. The main benefit targeted to those who need care is Attendance Allowance, which is at £61.85 or £92.40 a week in 2022, depending on level of need.

The current rules for means-tested support

After assessing a care need, the Local Authority will carry out a financial assessment to determine the financial liability of the Local Authority and the individual in paying for the care.

Eligibility

The individual's savings and assets are measured against an asset threshold, currently set at £23,250. If they have savings and assets over that value, they are not eligible for means-tested support and must pay for the care themselves.

If the individual is receiving care in their home, the value of their home is not included in the asset calculation. If the individual is receiving care permanently in a residential care home, then the value of a property owned by them may be included, if they do not have a qualifying relative, usually a partner or a child, still living in the property.

Amount of support provided

Once an individual is eligible for receiving means-tested support, the Local Authority will calculate how much support is provided. The amount of support is reduced by taking into account:

- savings of between £14,250 and £23,250 (some exclusions apply)
- eligible income, including pensions and some benefits.

[5] NAO (2018)

Addressing the problem of care funding

Dilnot Commission

In 2010, the Government set up the Commission on Funding of Care and Support, ("the Dilnot Commission"), tasked with recommending a sustainable approach to care funding that would best "meet the costs of care and support as a partnership between individuals and the state", while helping people to "choose to protect their assets, especially their homes".[6]

The Dilnot Commission reported in July 2011. They found that the current system was deficient in a number of areas:

- People are exposed to very high care costs with no meaningful way to protect against the risk.
- The current system offers inconsistent services across the country.
- People find the current system confusing and are often unaware of the financial liabilities, believing that the government will provide free care.
- There is inadequate information and advice available to people entering the care system.
- The increase in demand for care services was not matched by an increase in the funding for care.

The Commission concluded that it was very difficult for people to adequately plan or provide for their care needs.

The Dilnot Commission recommended increasing the Upper Capital Limit to £100,000 in 2011 terms, introducing a cap on costs set at £35,000 to protect people from extreme care costs, and standardising contributions to cover living costs in residential care. It also recommended measures to standardise eligibility criteria across England, and that the Government develop an information and advice strategy on how the system works and how to access services, benefits and financial products. The proposed cap included the individual's contribution towards the care costs and the means-tested support received from Local Authorities.

Government response

The Care Act 2014 enacted some of the Dilnot recommendations, including support for carers and a framework of duties for Local Authorities intended to improve standardisation. The care cap and increase to the capital thresholds were included with the intention to implement in 2016.

The Government decided in July 2015 to postpone the introduction of the cap on lifetime social care charges and the more generous means test. In the March 2017 Budget, the Government said that it would publish a Green Paper on social care, in order to allow a public consultation to be held. The green paper was thereafter delayed a number of times.

[6] Commission on Funding of Care and Support (2011)

The 2021 reform

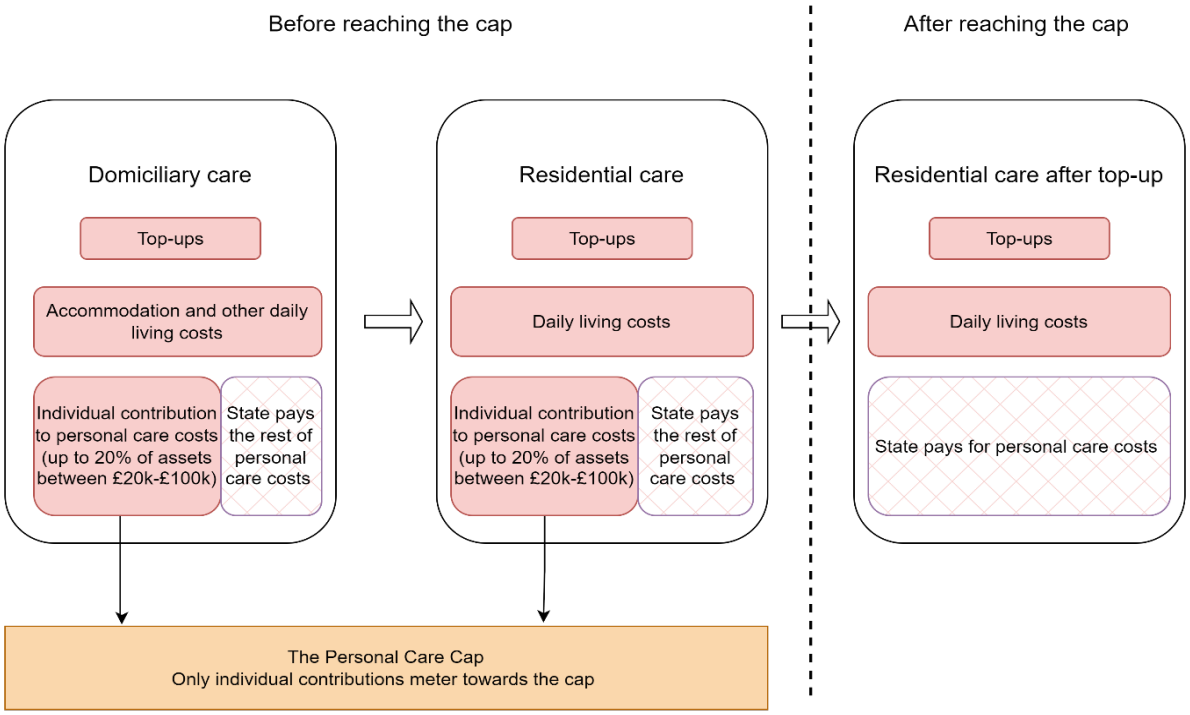
In September 2021, the Johnson Government announced their proposals for care funding, which included:

- A lifetime cap on individual spending on care costs of £86,000
- An increase of the means-test Lower Capital Limit (LCL) from £14,250 to £20,000
- An increase in the means-test Upper Capital Limit (UCL) from £23,250 to £100,000

The cap is not means tested and excludes Daily Living Costs (DLCs) in residential care, which will be set at a notional level of £200/week. The DLCs are the hotel costs associated with providing a residence for the individual. These costs would be required to continue to be met by the individual, with means-tested support if applicable. Unlike the Dilnot proposal, the cap would also exclude any Local Authority financial support. All eligible personal care costs after reaching the cap will be covered by the government.

The reform also removes restrictions on first-party top-ups, allowing those in care to pay extra for services beyond meeting eligible needs, or more expensive providers in locations of choice. Any top-ups before and after the cap will be excluded from the cap and will be covered by the individual.

The reform would also enable self-funders to request their Local Authority to organise their care for them so that they are able to receive care at Local Authority rates. This is an attempt to address the 41% disparity between Local Authority care rates and self-funder care rates.[7]



[7] CMA (2017)

Expanding financial support

The Government does not anticipate any people hitting the care cap until around 2025-26, where they anticipate around 1,000 people to hit the cap, but this number increases to around 74,000 by 2031-32.

The increase in the Upper Capital Limit to £100,000 would bring more people into eligibility for means-tested support. The Government anticipates an additional 50,000 people being eligible for means-tested support as a result of the increased UCL in 2023-24.[8]

While someone can be eligible for means-tested support if they have assets lower than the UCL, the support is tapered depending on the level of assets. Those with assets under the Lower Capital Limit only have to pay from their income and can keep all of their assets. However, those with assets over the LCL would have to pay no more than 20% of their assets between the LCL and UCL per year.

In depth examples of the means test and the interaction of the thresholds are set out in Chapter 2, which examines the impact of the reforms on how individuals might pay for care.

[8] DHSC (2022)

Chapter 2: Impact of care reforms

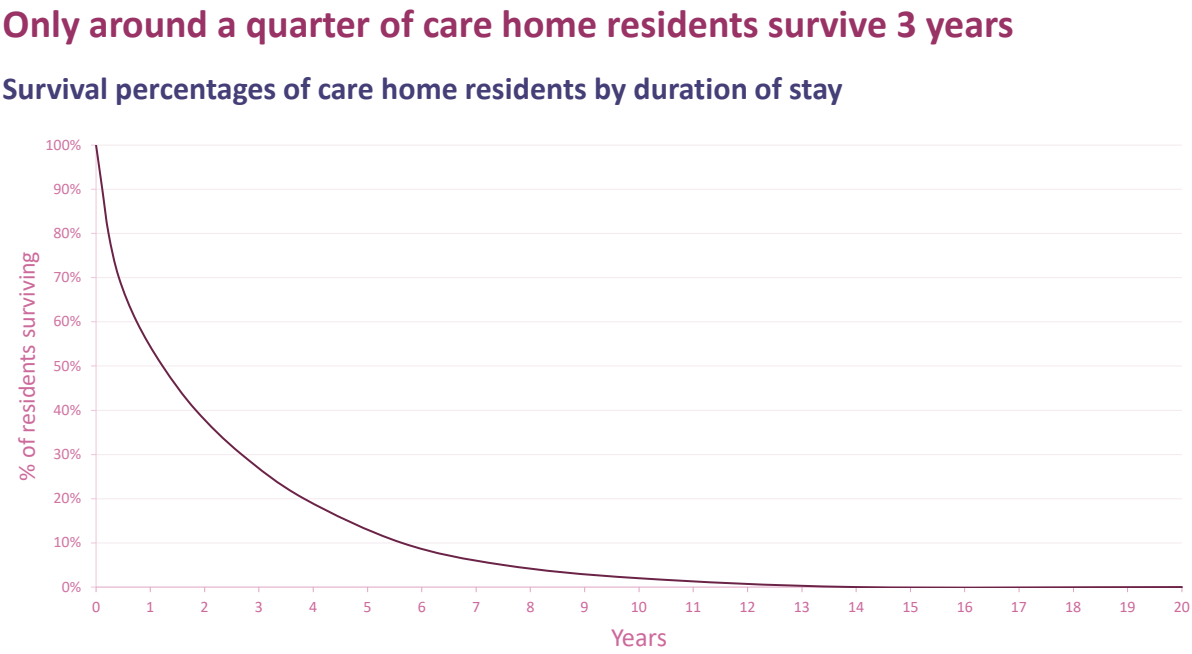
This chapter considers how the reforms work in practice and their impacts on the costs that individuals face themselves depending on their financial position.

Time spent in care homes

The longer someone spends in care, the more their accumulated costs are, which may have an impact on depleting assets. This chapter considers the distribution of time spent in care and the effect that has on asset depletion, and also the likelihood of reaching the new care cap.

Analysis of the survival rate in care homes carried out by the Personal Social Services Research Unit (PSSRU) suggests that many people die quite soon after entering a care home, with only 52% of people being in care for a year, around 27% being in care for over three years and only 12% of people being in a care home for more than five years (Fig 2.1).[9]

Figure 2.1



[9] PSSRU (2011)

The complexity of care costs

The social care system in the UK is devolved to the individual countries. This paper concerns the system in England. In England, social care is not covered by social insurance in the same way as the NHS, and it is not free at the point of use. Instead, there is some government support, such as Attendance Allowance and Funded Nursing Care. Beyond that, people must pay for their own care, but may receive means tested support from their Local Authority which could partially or fully cover the cost.

Care costs vary by the type and extent of care received. Domiciliary care may be charged on an hourly rate and therefore depends on the number of hours per week of care. Staying in a residential care home comes with expenses on top of the care itself, that is the "hotel costs" of the residence this includes the costs of paying for a room and meals. Nursing care in a care home also adds a further expense.

The Government's impact assessment on the proposed reforms set out average costs of care which are used in this report. Average residential care costs for Local Authority arranged care in England are estimated to be around £683 a week, equivalent to £35,500 a year (Fig 2.2).

Fig 2.2 Average Costs of Care in England[10]

Care Type	Cost in 2020/21
Nursing (per week)	£737
Residential (per week)	£683
Home Care (per hour)	£18.34

Understanding the care means test

Analysis in this paper highlights some of the complexities and interactions with the care means test before and after the proposed reforms. It is therefore necessary to have an understanding of the way the means test works and how income and savings are taken into account.

After assessing a care need, the Local Authority will carry out a means test to determine the financial liability of the Local Authority and the individual in paying for the care. The care support and amounts are gender neutral.

Eligibility

The individual's savings and assets are measured against an Upper Capital Limit (UCL), currently set at £23,250. If they have savings and assets over that value, they are not eligible for means-tested support and must pay for the care themselves.

[10] Assumed average costs of care for people over aged 65, DHSC (2022)

If the individual is receiving care in their home, the value of their home is not included in the asset calculation. If the individual is receiving care permanently in a residential care home, then the value of a property owned by them may be included if they do not have a qualifying relative, usually a partner or a child still living in the property.

Amount of support provided

Once an individual is eligible for receiving means-tested support, the Local Authority will calculate how much support is provided. Those with assets under the Lower Capital Limit (LCL), pay only from their income. Those with assets between the LCL and UCL pay from their income and a "tariff income" based on their capital over the LCL.[11]

Not all the income of the said individual goes into care costs. A small proportion of the income is ring-fenced. This income allowance is different depending on whether the person is in domiciliary care or residential care. In domiciliary care, the income allowance is called the Minimum Income Guarantee (MIG) and is currently set at £194.70 a week, in residential care the allowance is called the Personal Expenses Allowance (PEA) and is currently set at £25.65 a week.

The assessed income for care is therefore the eligible income plus the tariff income, less the income allowance. This assessed income level is what the individual would be required to pay towards their care, with the Local Authority providing the balance of cost if necessary.

The means test under the reforms

Under the proposed reforms, the means test is anticipated to work in broadly the same way but with a couple of differences:

- The LCL is £20,000 rather than £14,250;
- The UCL, above which no support is given, is £100,000 rather than £23,250; and
- The introduction of the cap on the total accumulated cost of care a person would pay for care at £86,000

The care cap relates only to the costs towards care paid for by the individual themselves. It does not include payments made by the Local Authority in the case of those receiving means-tested support, nor does it include the Daily Living Costs (DLCs) of residential care. The DLCs, also described as "hotel costs", such as food and accommodation, are set at a notional £200 a week. [12]

The complexities of the means test in practice

The way that paying for care affects people depends on their circumstances. The complexity of whether someone will be paying for their own care depends on both the level of their assets and the level of their income, and, in the case of homeowners, it may also depend on their relationship status at the time they require care.

[11] Tariff income is set at £1 a week for each £250 of assets between the LCL and UCL.
[12] This is a notional level only, not a representative price on the market. The DLCs will be subtracted from the Local Authority rate to determine what counts towards the care cap.

Case study 1: Under the means-test threshold

The care reforms will affect people based on their circumstances. Consider two people with low assets, James and Claudia, requiring care in a residential care home which costs £683 a week.[13] Both of them have £15,000 of assets, but different levels of income; James has £200 a week income and Claudia £800 a week.

When comparing the current system with the proposed reform, those with low assets and low income see little difference. For those with high income and low assets, who are also more likely to self-fund their care costs, the cap offers some benefit depending on the length and intensity of their care journey.

Under the existing rules, James is eligible for means-tested support because his savings are below the UCL of £23,250. However, the Local Authority would not pay the full cost. James would be expected to pay from his income and also a tariff income of £3 a week because his savings exceed the LCL of £14,250 by £750. He would be allowed to keep his Personal Expense Allowance, currently £25.65 a week. So, James would be charged £177.35 a week for his care home, with the Local Authority paying the balance of £505.65 a week. (Fig 2.3)

Under the proposed reforms, James' savings are below the new LCL of £20,000, so he would therefore not be subject to the tariff income. However, he would still have to pay towards his care from his actual income of £200 a week, which will be similarly reduced by the PEA of £25.65 a week. James would be charged £174.35 a week for his care home, with the Local Authority picking up the balance of £508.65 a week. James is £3 a week better off under the care reforms compared to the existing system.

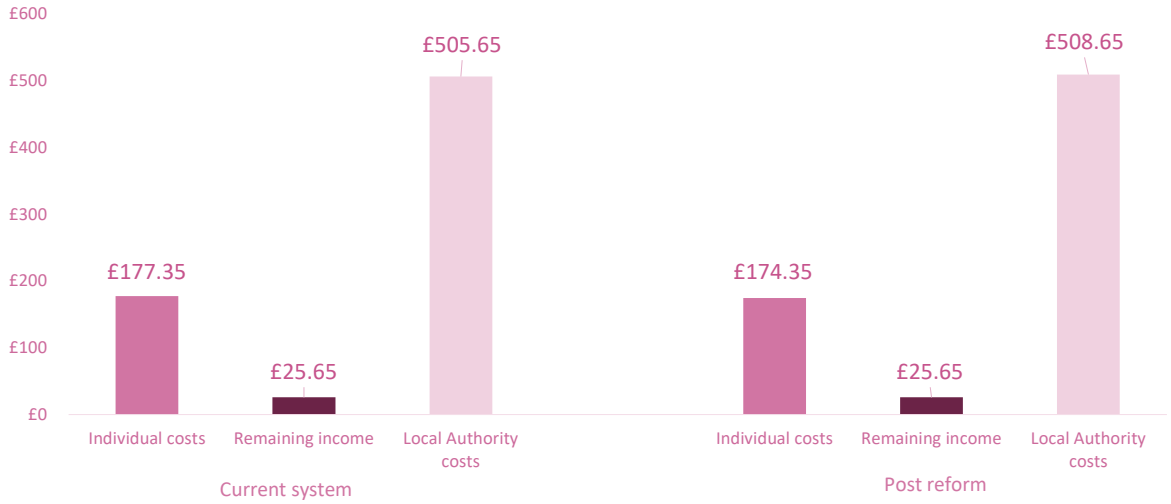
James' payments do not count towards the care cap because in residential care the first £200 of the costs are considered to be DLCs which are not included as care costs within the cap. Therefore, James' payments will never reach the care cap no matter how long he is in residential care.

[13] £683 is the average weekly cost of care in a residential care home arranged by a Local Authority in England, assumed by the government Impact Assessment into the cap DHSC (2022)

Figure 2.3

The reforms have little effect on those already receiving support

Facing care costs of £683 a week (£483 Care, £200 Daily Living), James has an income of £200 a week



Under the existing rules, Claudia is theoretically eligible for means-tested support because her savings are below the UCL of £23,250. However, because her income of £800 a week exceeds the cost of the care home, Claudia would be expected to pay the entire cost of the care home without Local Authority support (Fig 2.4).

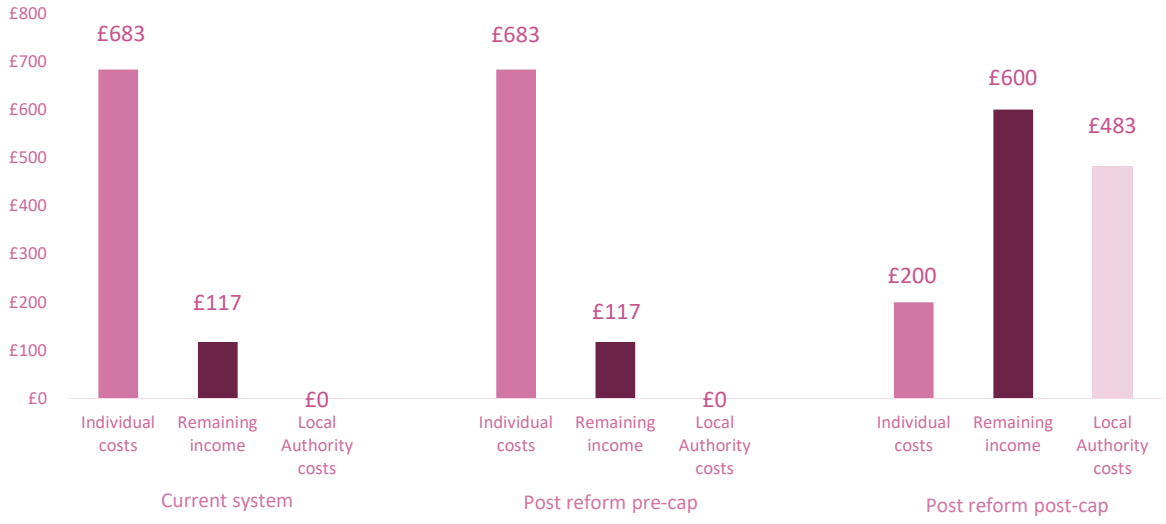
Under the proposed reforms, Claudia would still be in a position where, though her assets are low enough to make her eligible for means-tested benefits, her income is such that she would be required to cover the cost of funding herself. This leaves her in exactly the same position as before the reforms.

However, in paying the full cost of care Claudia is accruing towards the care cap. She would be expected to reach the cap in just under three and a half years. At that point Claudia would no longer have to pay the care element (£483) but would continue to pay the DLCs of £200 a week. This reduces Claudia's weekly care costs. After five years she would have paid accrued costs of £138,000, a saving of just under £48,000 compared to the £177,600 under the current system.

Figure 2.4

The care cap could help those with low assets but high income

Facing care costs of £683 a week (£483 Care, £200 Daily Living), Claudia has an income of £800 a week



The reforms have very little impact on people who receive means-tested support already. The reforms do, however, open up means-tested support to people with higher levels of assets and give self-funders some protection through the cap.

Impact of asset depletion on individuals

The costs of care may also evolve for people as their circumstances change as a result of paying for care. The cost of care can be substantial, so, under the current rules, someone who has significant assets at the time they require care may spend them down substantially and eventually come under the support of the Local Authority as their care costs deplete their assets.

Asset depletion is an issue for those with high levels of assets and low levels of income, and particularly single homeowners. The reform is likely to reduce the scale of asset depletion compared to the current system.

Depletion of assets is a problem for people who start with significant levels of assets, but who do not have an income that will cover the cost of care. Having to pay for care by spending down assets may significantly deplete their savings before they are eligible for care support. This could have a significant impact on their ability to pass on a bequest to their family.

This is particularly an issue for single homeowners who enter residential care. The value of their property will be included in their asset valuation. For many homeowners this is enough to push them over the Upper Capital Limit, moving them out of Local Authority support. If they have no other liquid assets, they may be required to unlock the value in their property

either by selling or releasing equity in some form, such as via a Deferred Payment Agreement with the Local Authority, in order to pay for their care. This will reduce the value of the home that they can leave as a bequest.

Case study 2: Asset depletion for people with low income but with a property

Kasia is 70 years old and has a condition that requires her to move into residential care. Kasia has an income of £200 a week, primarily from her State Pension, she also has savings of £15,000. She is a widow who owns her own home, a flat with the mortgage paid off and worth £80,000. She has no partner or dependent in the home, so the value of the property is included in the assessment of her assets. She therefore has savings and assets of £95,000.

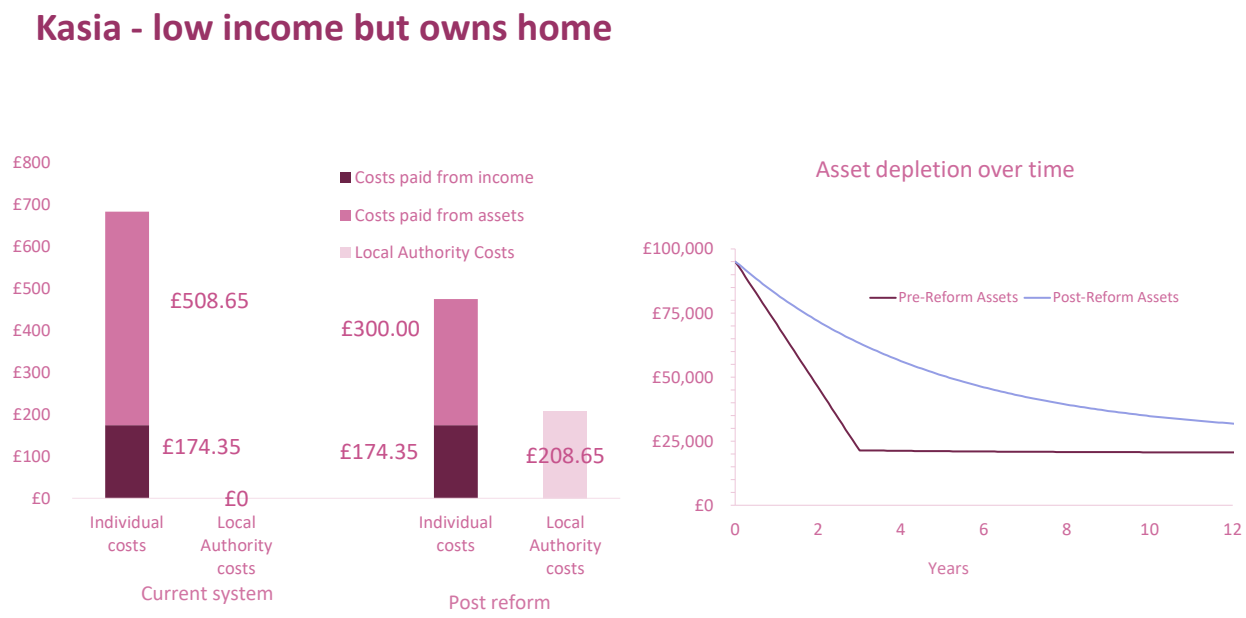
The Local Authority has arranged a place in a care home for her which costs £683 a week, including £200 hotel costs.

Asset depletion under current rules

Under the existing rules, she is not eligible for means-tested support because her savings and assets are above the UCT of £23,250. This means that Kasia would be required to pay the full cost of care herself without receiving any support from the Local Authority until the value of her assets falls below £23,250. This will mean that Kasia must unlock the value in her house, which is likely to require her to sell her house to cover the costs.

Over a period of three years, the cost to Kasia would amount to around £106,500 in current earnings terms, which Kasia would have to meet through a combination of her £200 income and spending down her assets. However, at the end of the three years the value of her assets would have depleted to the level of the UCL. At that point she would become eligible for Local Authority support and reduces the costs on Kasia.

Figure 2.5



Asset depletion under proposed reforms

Under the proposed reforms, Kasia's savings of £95,000 are below the new UCL of £100,000. She would therefore be eligible for means-tested support from the Local Authority, subject to the tariff income. However, as with the current rules, she would still have to pay towards her care from her pension income, of £200 a week.

The tariff income would be £300 a week ([£95,000 - £20,000] / 250 = £300), giving her a total notional income of £500 a week. Taking account of the PEA of £25.65 a week gives a chargeable income of £474.35 a week.

This does not cover the full cost of the care home, so Kasia would be required to pay the £474.35 and receive support from the Local Authority to cover the balance of the cost of care of £208.65 a week.

Over a period of three years, the total cost to Kasia would amount to around £64,200 in current earnings terms, which is around £42,300 less than the cost before the reforms of £106,500 for the three years. Over the three years, Kasia accrues £33,000 of charges towards the cap. However, at the end of the three years her assets have depleted by around £30,000. This reduces her tariff income and increases the Local Authority balancing payment. It also slows the accrual of charges towards the cap, to an extent that Kasia would continue to pay out her income and deplete her assets, but would not be expected to ever reach the cap (Fig 2.5).

Asset depletion is likely to be reduced by the reforms. People who would be required to spend down their assets to meet care costs under the current system, i.e. those who have to self-fund but cannot meet the costs from their income, are more likely to be eligible for Local Authority support.

How long individuals would need to be in care to reach cap: Domestic and residential

The amount of time taken to reach the care cap and therefore not be subject to further personal care costs is dependent on the cost of care.

Domiciliary care

Domiciliary care includes a carer regularly visiting a person's home to help perform various household tasks, or personal care and activities. Generally, the weekly spend on domiciliary care is lower than that on residential care. This means that it will take longer before the care cap is reached. The spend on domiciliary care in the table below is assumed to be £250 a week, that is around 13 and a half hours of care at the average hourly rate in England of £18.34.

Figure 2.6[14]

Progress to the cap depends on income and savings

Progress to the cap at various levels of income and savings in *domiciliary* care, at a cost of £250 a week

Income (£pw)	No savings	£25k savings	£50k savings	£100k savings	£150k savings
100	*	*	29y 1m	10y 5m	6y 8m
200	*	*	12y 3m	6y 5m	6y 8m
300	17y 5m	13y 7m	7y 3m	6y 5m	6y 8m
400	8y 5m	7y 6m	6y 8m	6y 8m	6y 8m
500	6y 8m	6y 8m	6y 8m	6y 8m	6y 8m

* will not reach care cap within 30 years

In domiciliary care, the individual has more living expenses to cover than the person in residential care, and therefore have a higher income disregard. In assessing the means-tested support in domiciliary care, the disregard on individual income is called the Minimum Income Guarantee (MIG). The MIG is currently set at £194.70, compared to the Personal Expense Allowance of £25.65 a week.

On a spend of £250 a week, a person who is paying for the care themselves without Local Authority support might be expected to reach the care cap after 6 years and 8 months of

[14] PPI calculations

receiving care. Those who receive means-tested support from the Local Authority would not be expected to reach the cap as quickly, for example someone with £25,000 of savings and a weekly income of £300 a week would cover around £125.30 of the cost of care and receive Local Authority support of around £124.70. They might reach the care cap after around 13 years and 7 months (Fig 2.6).

Residential care

For those in residential care, the costs are higher. A self-funder paying residential care costs of £683 a week reaches the cap around 3 years and 6 months. Those who receive Local Authority support are likely to have longer until they reach the care cap because the Local Authority payments towards care are not counted towards the cap. This means that people with lower incomes and savings are not likely to reach the care cap no matter how long they spend in care (Fig 2.7).

Figure 2.7[15]

Progress to the cap depends on income and savings

Progress to the cap at various levels of income and savings in *residential* care at a cost of £683 a week

Income (£pw)	No savings	£25k savings	£50k savings	£100k savings	£150k savings	>£200k savings
100	*	*	*	*	*	3y 6m
200	*	*	*	*	5y 0m	3y 6m
300	*	20y 8m	13y 8m	6y 4m	3y 8m	3y 6m
400	10y 6m	9y 1m	6y 10m	4y 2m	3y 6m	3y 6m
500	6y 5m	5y 10m	4y 9m	3y 6m	3y 6m	3y 6m

* will not reach care cap within 30 years

Regional differences in the cost of care

The analysis in this paper assumes that the cost of care costs is £683 a week for residential care. That figure is an estimate of the average cost of Local Authority arranged care in England,[16] but the care costs vary across the country. The higher the cost of care the quicker the individual will reach the care cap. Costs in London and the South West tend to be higher

[15] PPI calculations
[16] DHSC (2022)

than other parts of England (Fig 2.8), leading to them reaching the care cap faster than those in other parts of the country.

Fig 2.8 Average care costs in the England[17]

Region	Average weekly cost of care
North East	£656
North West	£598
Yorkshire and The Humber	£642
East Midlands	£634
West Midlands	£627
East of England	£713
London	£793
South East	£741
South West	£795
England (total)	**£683**

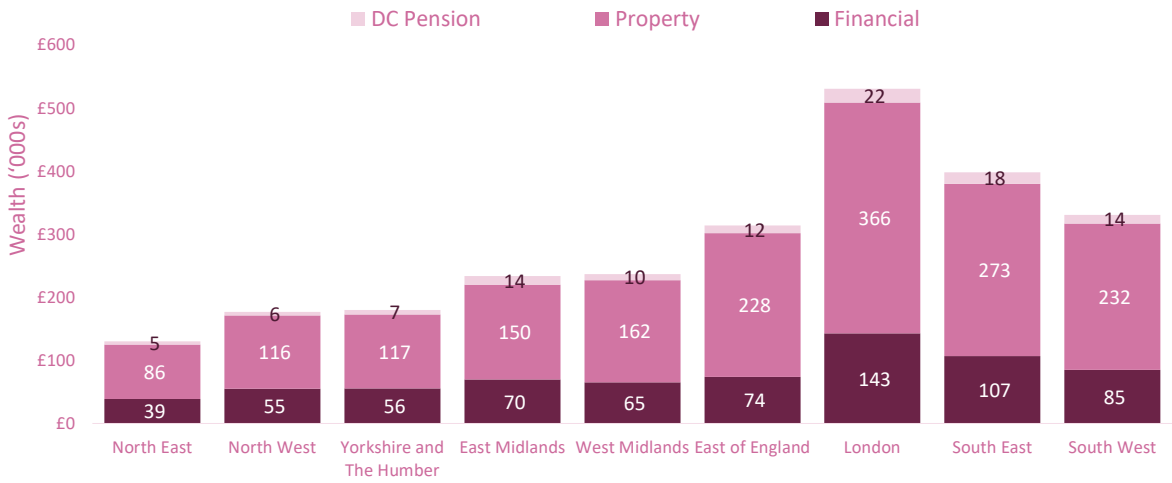
These regional disparities mirror regional wealth disparities, so are also likely to mirror people's ability to pay for care. Sources of wealth used to pay for care are also likely to be different throughout the country (Fig 2.9).[18]

[17] DHSC (2022)
[18] PPI analysis of the Wealth and Assets Survey Round 7

Figure 2.9[19]

People over 65 have more wealth in London and the South of England

Wealth of current people aged over 65 by location and source (£'000s)



Sources of wealth to cover the costs

Housing wealth forms the largest portion of their wealth for more than 60% of current pensioners. When housing wealth is disregarded, only around 20% of people would have assets over the Upper Capital Limit. The rest would be entitled to some Local Authority support. Nearly half of current pensioners have financial assets of a value below the Lower Capital Limit and would thus only have to pay from their income (Fig 2.10).

The value of the house will likely be such that the individual will either be exempt from means-tested support (if the property takes their assets to over £100,000) or subject to tariff income to the extent that they must draw down on their assets. For example, £70,000 of assets would lead to a tariff income of £200 a week.

Liquidity of assets may affect people's ability to pay for care. Financial assets are likely to be easier to access than property wealth, which may have to be sold or entered into an equity release agreement. This could be a particular issue for those in residential care who have property but no spouse or partner living in the property, because property values are likely to be their main asset.

[19] PPI analysis of the Wealth and Assets Survey Round 7

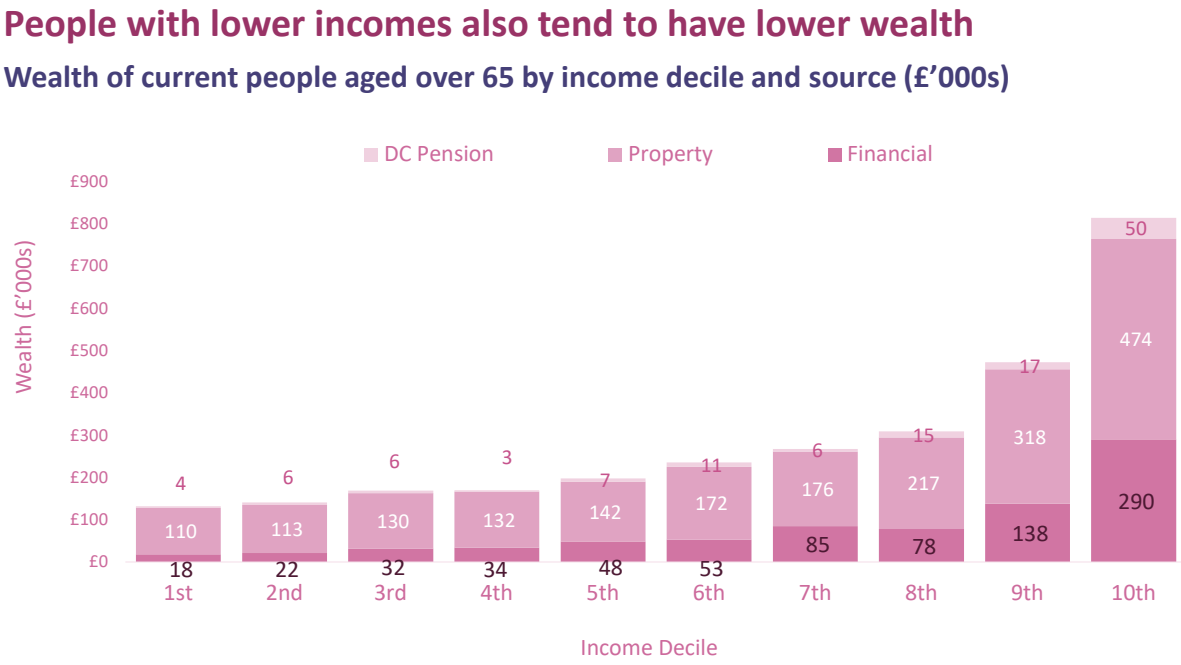
Figure 2.10 Financial assets by percentile with tariff income required[20]

Percentile	Non-residence wealth	Tariff income (£ a week)
10	£150	0
20	£1,500	0
25	£3,000	0
30	£5,000	0
40	£10,600	0
50	£20,500	3
60	£36,800	68
70	£64,000	176
75	£86,100	265
80	£115,000	N/A (self-funding)
90	£234,205	N/A (self-funding)

Taking into account housing wealth would increase the proportion of people who would be required to make significant payments towards their care from their assets. But because the assets that have put them in that position are housing assets, they may find difficulty in meeting the payments without drawing money from their property (Fig 2.11). Defined Contribution pension wealth could be a source of wealth to pay for care for some people. However, for many people their pension may have been used to purchase a guaranteed income products and is not therefore available.

[20] PPI analysis of Wealth and Assets Survey Round 7

Figure 2.11[21]



Presenting those percentages as average levels of wealth for each income decile shows that those with lower incomes also tend to have lower wealth (Fig 2.11). Although these wealth amounts could end up being used to pay for care, they do not necessarily directly translate into the assessed level of capital assets. For example, pension wealth is not included in the assessment, and whether housing wealth is considered depends on the circumstances.

The distribution of wealth among current pensioners skews to the younger pensioners. People between age 65 and 79 have higher levels of wealth, and are more likely to have some accessible pension wealth (Fig 2.12). Whereas people aged over 80 have negligible levels of accessible pension wealth, as the rules in place at the time they retired required them to purchase guaranteed income products. Those with more accessible wealth are more able to pay for top-ups as this pension wealth has not yet been transformed into guaranteed income. People over age 80 also tend to have lower levels of financial and property wealth than younger pensioners (Fig 2.13).

[21] PPI analysis of the Wealth and Assets Survey Round 7

Figure 2.12

People with lower incomes also tend to have lower wealth

Wealth of current people aged 65 to 79 by income decile and source (£'000s)

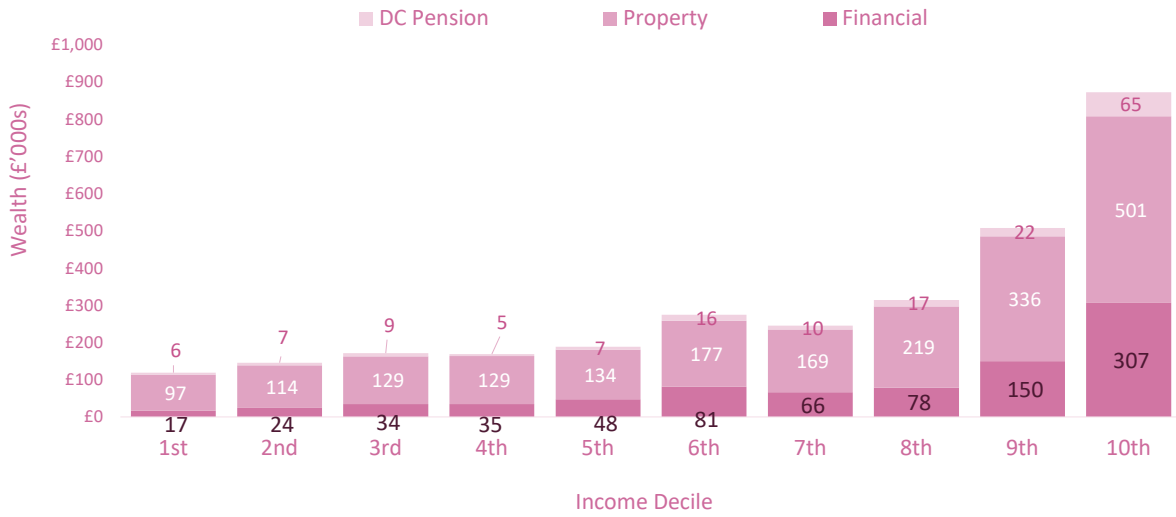
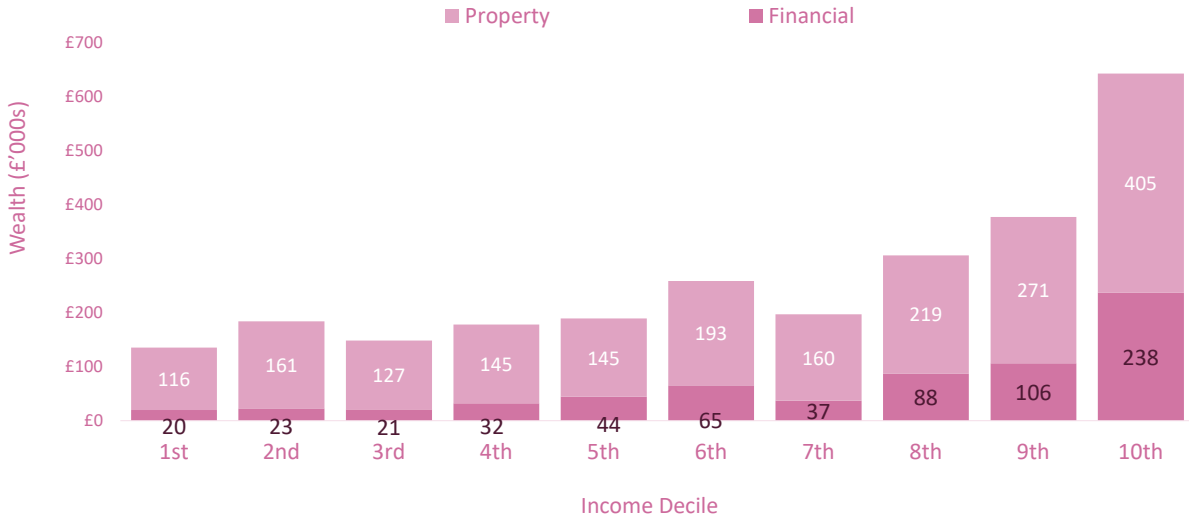


Figure 2.13

People with lower incomes also tend to have lower wealth

Wealth of current people aged over 80 by income decile and source (£'000s)



Chapter 3: Additional income and wealth

Insurance and long-term savings products may help people to pay for care

Insurers used to provide "pre-funded" insurance specifically for long-term care, a product where people would pay single or regular premiums in return for cover against the possibility of needing long-term care benefits sometime in the future. They would typically pay out a cash benefit if the customer had a care need, based on activities of daily living. While some of these policies are still in payment, they are no longer generally sold. The products were introduced in 1991. Data from The Association of British Insurers (ABI) shows that there were 45,000 in force in 2010 and 24,000 in 2018. Multiple factors contributed to this decline, which coincided with mooted reform of the state offer.

In recent years, providers have developed similar products with a care 'rider': whole of life or critical illness policies, which pay out early if a care need arises. No data is available on sales of these products, but based on wider life insurance market data, numbers are likely to be in the hundreds per year.

Immediate needs annuities (INA) are a long-standing option for customers at the point of need, guaranteed to cover care home fees for the rest of the policyholder's life. An INA is a form of purchase life annuity, bought with money that has already been taxed. Purchase life annuities only account for hundreds of policies a year

The possibility of an unknown and potentially very large cost of care could lead people to seek out a product to reduce their risk. Typically, in such circumstances insurance products provide a risk mitigation measure for individuals.

This report considers two sets of scenarios, analysing the effect of receiving or having a) extra income and b) an extra lump sum. The analysis is product neutral – the extra lump sum or income could have come from savings, property or another source, but it could also be thought of as the pay out of an insurance product upon a care need being identified.[22]

Extra income or capital has an effect on the means test assessment, as a person's affordability increases. For example, a person with an income of £200 a week, who now has an extra income stream of £100 a week would be assessed as having £300 a week under the means test.

Income product interaction with the reforms

Recall two of our individuals from Chapter 1, James and Claudia. Both have assets of £15,000. James has an income of £200 a week while Claudia has an income of £800 a week. If they were each to have an additional £200 a week the effect is rather different for each.

[22] This is not a product analysis, the costs of purchasing such a product are not taken into account.

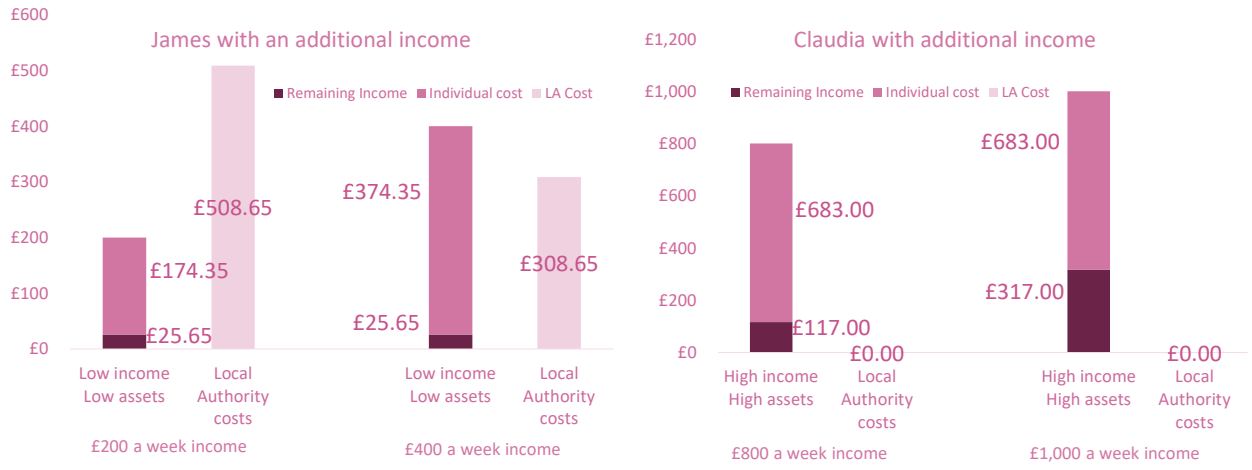
For James, without the additional income his income and assets mean he must pay £174.35 a week towards his care and has only £25.65 income left over, his Personal Expenses Allowance (PEA). But, with the additional £200 income, James must pay £374.65 a week towards his care and, again, is left with only £25.65 income to spend as he wishes. The product simply increases his spend on a pound for pound basis and reduces the cost to the Local Authority. James therefore sees no benefit personally from the additional income (Fig 3.1).

For Claudia, the situation is different; she already has an income that covers the total cost of her care, the additional income is not spent on care but increases her remaining income. This could give her the ability to pay for top-ups, such as a more comfortable room or other amenities.

Figure 3.1[23]

For people receiving LA payments, additional income may simply reduce their support

Care costs for James and Claudia with additional incomes of £200 a week



Where additional income is likely to reduce the Local Authority support then the individual does not get the full benefit of the product. They are essentially sharing the benefit of the additional income with the Local Authority. In the case of James, the Local Authority gets the full benefit, with their outgo reducing by the amount of pay-out and James seeing no improvement in his financial situation.

The proportion of benefit received by the individual compared to that received by the Local Authority depends on the financial situation of the individual.

If without the additional income, one receives Local Authority support, then some of that support will likely be withdrawn when their income is increased. The less support one receives from the Local Authority, the more of the additional income benefits them directly.

[23] PPI calculations

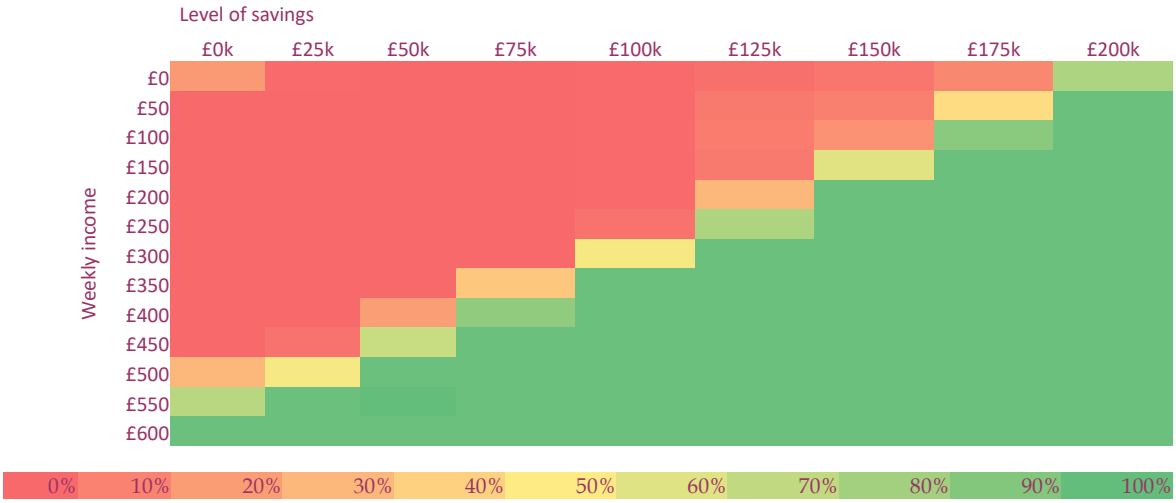
It is those who would have otherwise have to pay the entire cost themselves that see a full benefit.

The heat map (Fig 3.2) shows how much of the additional income actually goes to improve the individual's financial position, as opposed to reducing the Local Authority spending for each combination of income and wealth. The chart considers the impact of an additional income of £100 a week. The outcome is expressed as a colour on the heat map, the red colours show that people with corresponding income and wealth do not get much of a net gain because the additional income simply reduces the local authority financial support. The green colour suggests that the additional income is a substantial net benefit. As the map shows, the outcome is heavily dependent on the level of income and assets the individual is assessed as having.

Figure 3.2[24]

Additional income may reduce LA benefit for many people

Net benefit of an additional £100 a week to people in residential care for 5 years



Mapping the financial situation of current pensioners on to the heat map shows that around 38% of current pensioners would have a net benefit of more than two-thirds of the total payments (the green squares on the heat map), 2% would have a net benefit of between one-third and two-thirds, and 60% would see net benefit of less than a third of the additional income (the red squares on the heat map).

[24] PPI calculations

Lump sum product interaction with the reforms

To look at the impact of a lump sum, recall our two examples James and Kasia. James has an income of £200 a week and assets of £15,000; Kasia also has an income of £200 a week but has assets of £95,000 consisting of £15,000 savings and a property worth £80,000. If they were each to have a product that pays a lump sum the effect is rather different for each.

For James, without the lump sum, his income and assets mean he must pay £174.35 a week towards his care, and has the PEA of £25.65 left over. But, with the £75,000 lump sum, James has assets of £90,000, leading to a tariff income of £280 a week, so he must pay £454.65 a week towards his care and, again, has just the PEA of £25.65 left over. The lump sum leads to an increase in James' spend and reduces the cost to the Local Authority. The cost over three years to James without the lump sum is £27,200, compared to a cost of around £61,800 with the lump sum.

However, James may see an improvement in his finances. This is because, despite paying more towards his care, he is also left with some of the lump sum he was given, which he could use to top-up for care beyond eligible needs, a more comfortable care arrangement or just leave some as part of his inheritance. The lump sum increases James' costs by £34,600, but also increases his net position by £40,400, 54% of the value of the lump sum. The net difference in his financial position depends on the time spent in care (Fig 3.3).

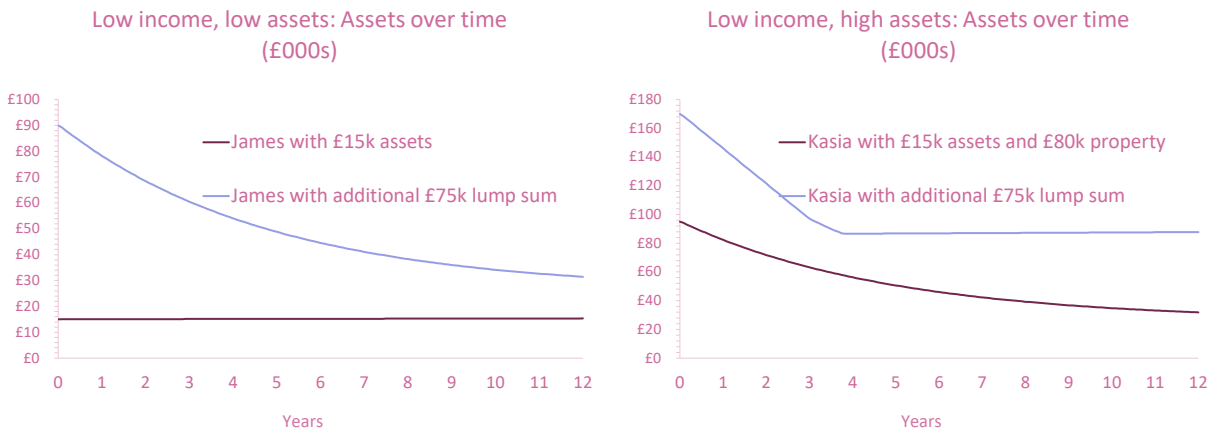
For Kasia, the situation is different; without the lump sum she already has assets of £95,000 that mean she is eligible for means-tested support, but must pay a tariff income of £300 a week in addition to her income. This leads to a cost of £474.35 a week to pay, for which she may deplete her savings and have to sell or in some other way unlock the value in her home. With the additional £75,000 lump sum her assets are £170,000. This is above the Upper Capital Limit for the means test, meaning she would not be eligible for Local Authority support and would have to finance the full cost of the care home of £643 a week herself. The higher outgo would deplete faster than without the lump sum. However, the lump sum gives her more liquid assets to use to make the payments before she would have to consider selling her home.

In paying for the full cost of care, the care cap would be reached in just under three and a half years, which would stop the requirement for Kasia to pay for her care and leave her paying for the Daily Living Costs (DLCs), which would largely be met by her regular income. Kasia's assets would not be expected to drop below £80,000 (Fig 3.3). The lump sum would increase her outgo but may give her a way to make the payments and avoid ever having to sell her house.

Figure 3.3[25]

Additional lump sum product would affect people differently

Level of assets over time for James and Kasia in residential care



The effect of a lump sum may be more time dependent than an income. The lump sum payment is made all at once and is spent down. A longer period of time in care could mean more spending down of the lump sum, and a lower financial benefit of the lump sum. However, as in Kasia's case, the care cap being reached stops the depletion of assets and serves to slightly improve the financial outcome over time.

Like the additional income scenario, a lump sum is more likely to lead to a positive net financial position if it does not reduce the individual's support from the Local Authority. People who are not means-test supported, and therefore paying for their own care, may see the greatest benefit from a lump sum product. A lump sum may be used to protect other assets, for example providing a liquid asset to pay for care costs without having to sell a property, allowing for example, for a home to be left in a bequest.

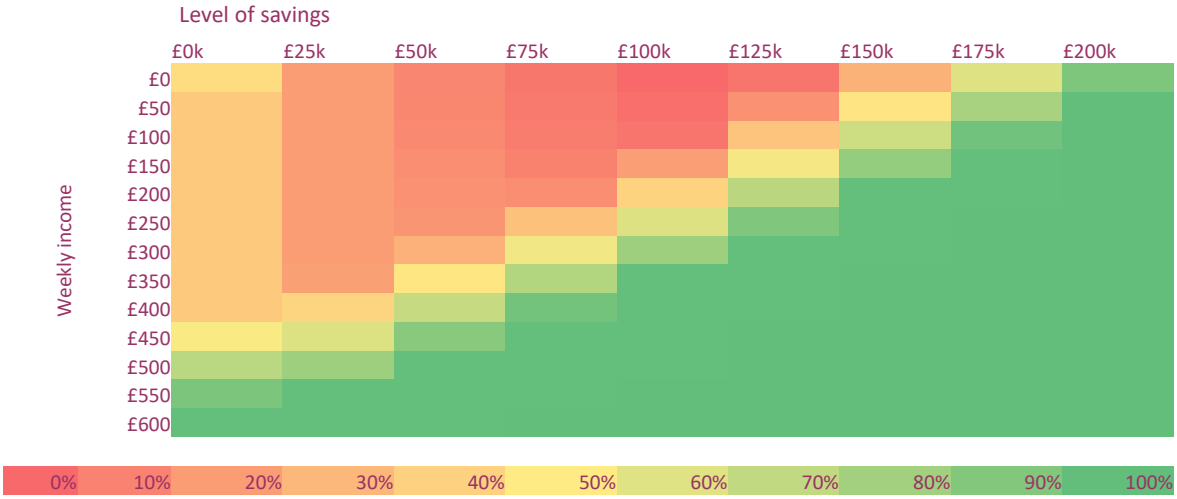
The heat map shows how much of the financial position has improved after five years of residential care as a proportion of the amount of the lump sum for each combination of income and wealth. The chart considers the impact of a lump sum of £75,000 and five years in residential care.

[25] PPI calculations

Figure 3.4[26]

A lump sum payment could help some people pay for care

Net benefit of a £75k lump sum to people in residential care for 5 years



Mapping the financial situation of current pensioners onto the heat map shows that around 43% of current pensioners would have a net benefit of more than £50k, 46% by between £25k and 50k, and 11% by less than £25k.

Some products may not be suitable for everyone

Paying for products that provide an additional income may not be suitable for everyone. If the extra income or lump sum simply replaces or reduces the support they receive from the Local Authority, they are not likely to have a worthwhile benefit from it. The people who may be able to benefit are likely to be those who would have low or no Local Authority support, who could use products to improve access improvements to their care and/or protect their assets.

Advice and guidance are likely to be important as a result of the complexity around who might or might not benefit from any products. Additionally, the potential suitability will, in part, be based on unknown future circumstances, including the future financial position of the individual, the relationship status of the person (which affects whether the home is taken into account), and the severity of any care need.

The data analysis suggests that around a third of current pensioners may see a financial benefit from a product that provides cash or an income in the case of a care need. These tend to be the people who have income and wealth such that they would not be interacting with the Local Authority's means-tested support. It is also possible that some of these people have

[26] PPI modelling

enough wealth such that they are not too concerned about the cost of care home provision to the extent that they feel the need to insure against it. The market may be people who have wealth that they wish to protect from being used to pay for care.

Chapter 4: Future care interaction

Current pensioners compared with Gen X

Analysis of what the reform means for pensioners has been based on the data on current pensioners. This chapter considers how the next generation approaching retirement will likely meet their costs of care based on the income and asset projections, and how an additional income or capital would benefit them if they need care.

Financial position of Generation X is different from that of current pensioners

Previous PPI research has shown that Generation X will reach retirement with lower levels of Defined Benefit (DB) income than current pensioners and more Defined Contribution (DC) savings on average. There may be a higher prevalence of private pension saving as a result of automatic enrolment, however Generation X individuals will not benefit from full working lives of automatic enrolment. The higher likelihood of having DC pensions may mean they have more easily accessible funds, that they could use to top-up for care of their choice.

They were found to be more likely to reach retirement in rented accommodation or with an outstanding mortgage.[27] With housing being the key source of wealth, the increasing rate of renting at old age means fewer Gen X can rely on housing wealth to get the care they may want.

State pension for the Generation X individuals is assumed to be at the level of the full new State Pension (nSP). This is higher than the state pension of some of the current pensioners who retired under the old basic State Pension (bSP) system. The bSP is lower than the nSP and, while it had an additional element of State Second Pension (S2P), accrual of contribution years had more exceptions, leading to more people being unable to accrue the full level. State pension is therefore likely to be higher for Generation X than for current pensioners.

Generation X are therefore more likely to have lower levels of average private pension and housing wealth than the current generation of pensioners. This, in turn, means that if they require care they are more likely to be reliant on means-tested Local Authority support.

How might savings income levels affect outcomes for Gen X

Slightly fewer people in Generation X may get the full benefit of an income or lump sum product than those in the current generation of pensioners (Fig 4.1)

[27] PPI (2019)

Figure 4.1 Proportion of people benefiting from income and lump sum products after five years in residential care

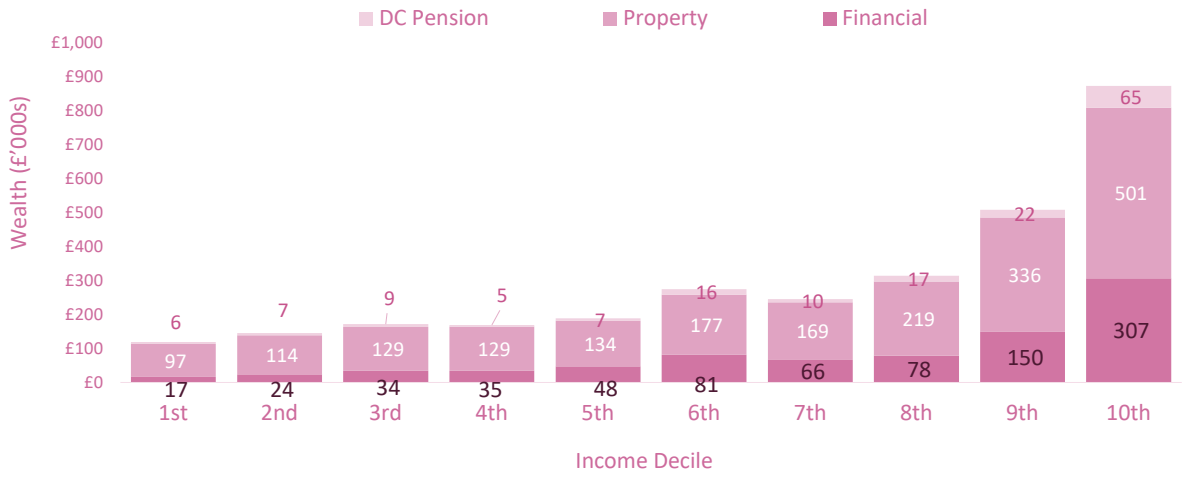
	75k lump sum		£100 a week income	
Proportion of net value individual in financial improvement to individual	Current pensioners	Gen X	Current pensioners	Gen X
Less than 33% of value	11%	24%	60%	68%
between 33% and 67%	46%	40%	2%	3%
over 67% of value	43%	35%	38%	29%
Full value	37%	28%	37%	29%

Projecting Generation X households to retirement suggests that Generation X individuals are less likely to see full value from income or lump sum products than current pensioners, reflecting the likely different financial situation that Generation X will be in in retirement. If Gen X have lower private pension incomes and lower levels of home ownership, then they may be expected to be more reliant on the Local Authority for care support. This could mean that fewer will have the level of assets that put them in the group that could benefit from a care insurance product (Fig 4.2).

Figure 4.2

People of Generation X may have low levels of pension and property wealth

Projected wealth of Generation X people at state pension age by income decile and source (£'000s)



This outcome should be caveated, however, in that, while the analysis does take account of future pension savings, the increase in value of current financial wealth, and assumes that those with mortgages will have paid off their mortgage, it does not take into account the possibility of inheritance of assets.

Technical appendix

Modelling the costs of care

Assumptions

Costs of care are assumed to be at the levels set out in the impact assessment. £683 a week for residential care. This is the Department of Health & Social Care (DHSC) estimate of the average weekly cost of care in England. The weekly cost of domiciliary care is assumed to be £250 a week; this assumes around 13 and a half hours of care.

Pre-reform thresholds and allowances are in line with Department for Work & Pensions (DWP) rates. Post-reform thresholds and allowances are at the levels set out by the Government in their policy documents.

	Pre-reform	Post-reform
Lower Capital Limit (LCL)	£14,250	£20,000
Upper Capital Limit (UCL)	£23,250	£100,000
Tariff rate	£1 a week per £250 over LCL	£1 a week per £250 over LCL
Cap	-	£86,000

Earnings and Consumer Prices Index (CPI) growth are assumed to increase in line with Office for Budget Responsibility's (OBR) assumptions. Long-term economic growth rates:

Earnings growth: 3.8%

CPI: 2%

Post-retirement investment growth: 4%

Rates and thresholds are assumed to increase in line with earnings. This is in line with Impact Assessment assumptions. Care costs are assumed to increase in line with earnings growth. Income up to the level of the Guaranteed Credit (GC) level in retirement is assumed to increase in line with earnings growth. Retirement income over the GC level is assumed to increase in line with growth in CPI.

Calculations

Costs of care are modelled in a monthly cashflow model, allowing for income, income disregard, and tariff income from assets. These are compared to the cost of care to calculate an individual cost and a Local Authority cost in a month. A running total of individual care costs is maintained. In the case of residential care, it is assumed that the first £200 a week (in

current earnings terms) is the Daily Living Costs (DLC) and therefore excluded from care costs. An indicator compares the individual care costs with the care cap. Once the care cap is reached, the individual no longer faces care costs but is subject to daily living costs as appropriate.

Current and future pensioners

Current pensioners

Mapping the current over-65 populations and projected Generation X is done using the Wealth and Assets Survey.

For the current over-65 population, the assets considered are net financial wealth, net value of property (excluding main residence), and net value of the main residence (if using for residential care and individual is single). Pension wealth is excluded, as it is from the means test. Physical wealth, the value of possessions such as car etc, is also excluded.

In the case of a couple, the amount assigned individually to each is half of the household level. This mirrors the way that income and assets are assigned in the Local Authority assessment.

Data cuttings are then done on an individual basis using the individually assigned assets and income.

Projecting Generation X

To project Generation X to retirement, the starting point is the Wealth and Assets Survey data on income, employment, pension contributions, current assets and home ownership.

Income in retirement: Individuals are assumed to be eligible for the full rate of the new State Pension (nSP). For those in employment and making pension contributions, it is assumed that those contributions continue up to their State Pension age, at which point they retire and take their pension at a sustainable rate of 3.5% of the fund. They are also assumed to take a lump sum which is added to their assets.

Housing wealth: Those who are currently homeowners with a mortgage are assumed to have paid off their mortgage by retirement, so the net value of the property at retirement is the value of the property. House values are assumed to increase in line with earnings growth. Those who are not already homeowners are assumed to remain renters throughout their lives.

Financial wealth: Financial assets are assumed to increase in line with pre-retirement investment returns, that is 1.5% above the rate of earnings growth.

Having calculated the projected pension and assets at retirement, they are discounted to current earnings terms to compare to the current pensioners and the current rates and thresholds of care.

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