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The future funding of social care in the UK

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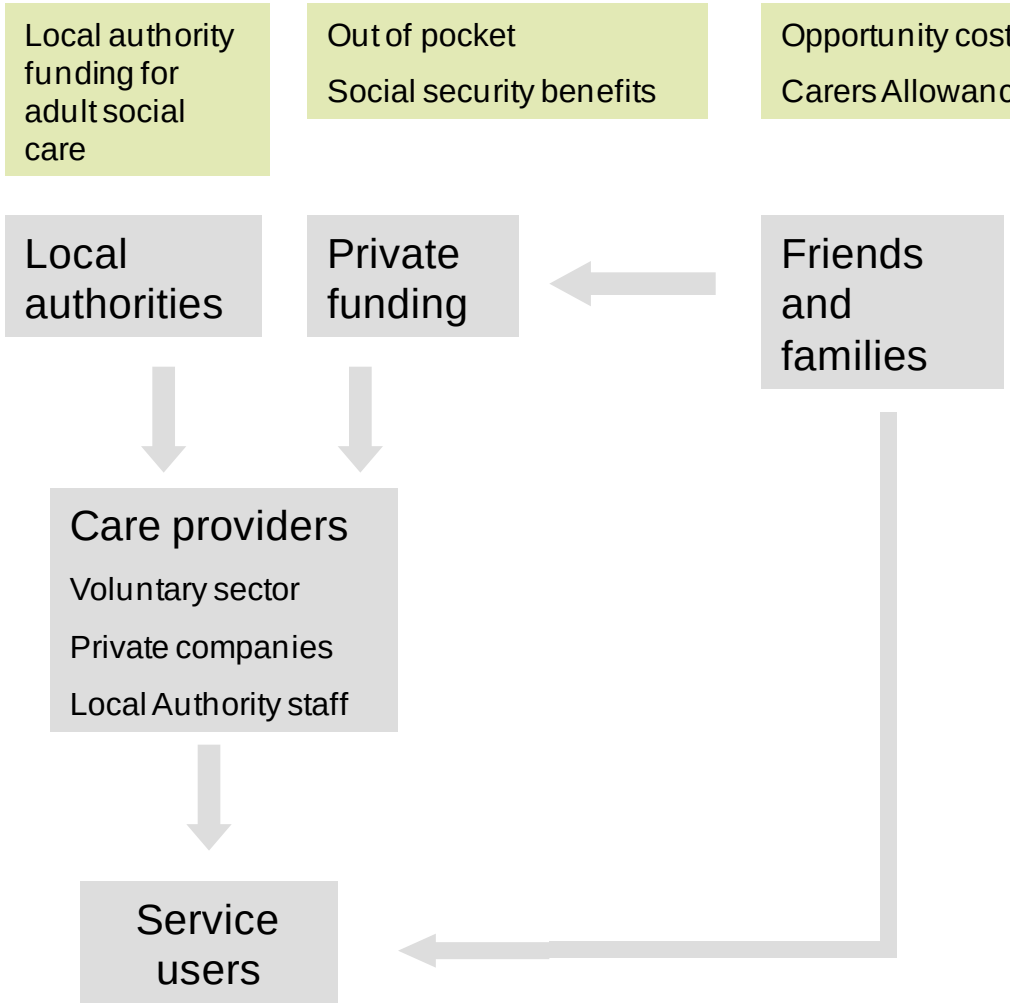
Present system of adult social care



- The UK spends about £19 billion a year adult social care of which £13.4 billion (70%) is in institutional care and £5.7 billion (30%) in home care.
- The public sector accounts for 65% of all expenditure and the private sector 35%. Of private expenditure around 80% is spent on institutional care and 20% on home care.
- The value of informal unpaid care by friends and relatives is estimated to be around £58 billion.
- The total value of LTC is approximately £76 billion a year on this basis.

Relevant demographic trends (UK)

- The number aged 65+ will increase from to 9.8m in 2009 to 12.4m 2020 and the number aged 80+ from 2.8m in 2009 to 3.6m in 2020
- A female reaching 80 in 2001 had a 2.7% chance of reaching 100 whereas a female of the same age in 2020 has a 12.3% chance
- Male and female life expectancies at age 50 appear to be converging at ~35 years by 2020
- The gap between Healthy Life Expectancy and Life Expectancy is increasing and so potentially more years will be spent needing care

Green/white paper proposals

- **Self funding**: Everyone would be responsible for paying for their own care. The Green Paper rules out this option because ‘people cannot predict what care and support they will need’.
- **Partnership**: Everyone entitled to care would have a proportion of their basic care and support costs paid for by the state. The remainder would be paid for out of pocket.
- **Insurance**: Everyone would be entitled to some support just as with option 2. but there would be additional enabling support based on insurance either state or privately operated.
- **Comprehensive**: Everyone over retirement age who had the resources to do so would be required to pay into a state insurance scheme (suggested range £17k to £20k)
- **Tax funded**: People would pay tax throughout their lives which would be used to pay for all the people currently needing care. This is also ruled out because ‘it places a heavy burden on people of working age’

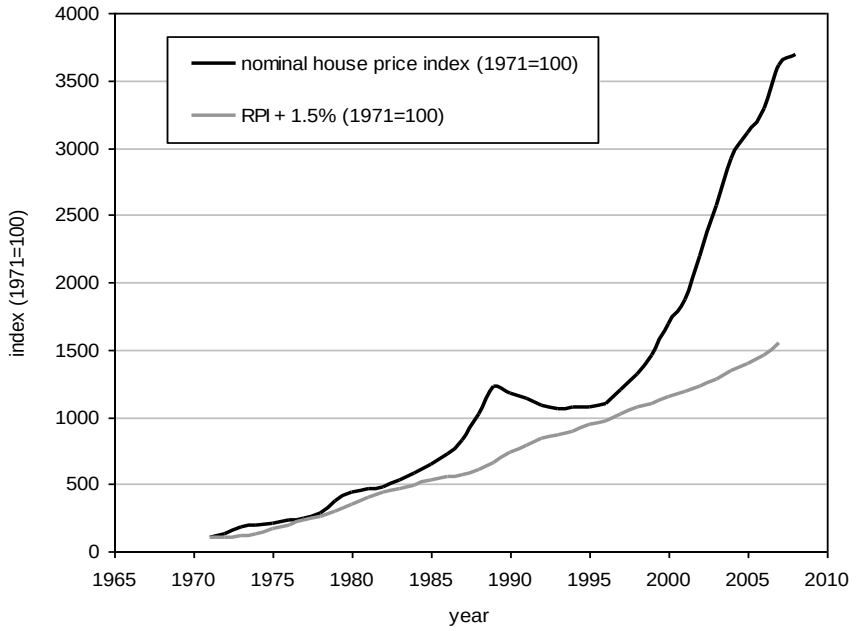
Strategic issues arising

- More older people in frail health needing support
- Insufficient personal income to pay for institutional care
- Taxation route could result in moral hazard (e.g. work disincentives, reduction in informal carers)
- There is crowding out of private finance products due to system complexity and policy uncertainty
- Generally poor planning and ignorance in families (‘the state will look after me’)
- In old age people’s assets generally may be more valuable than their incomes (‘asset rich income poor’)

Income and wealth in UK households age 65+ (based on ELSA)

- The probability of needing LTC in later life is high, but for institutional care it is relatively low (about 35% in the case of females)
- Over twice as many females as males are in institutional care but they are least able to afford it
- Only 400k households out of 6.5m age 65+ households can afford institutional long term care for more than *1 year* on the basis of income, but this increases to 3m if savings are included
- If housing wealth is taken into account then 4.6m households could afford care for more than *1 year*
- Of the 1.8m households that *cannot* afford care for more than one year if housing wealth is included, 0.9m are female only, 0.4m male only, 0.4m couple households and 0.1m other

House prices versus RPI



House prices versus RPI:

Chart shows how house prices have moved relative to the RPI. In 1971 the value of a house would have roughly pay for 3.7 years worth of care. In today's prices it would pay for approximately 8.8 years.

Financial products for LTC

3 classes of product: 'point of need', 'point of retirement', 'any time'

- Equity release products
- Top up insurance
- Immediate needs annuities
- Accelerated life insurance
- LTC bonds/trust fund
- Disability Linked Annuities

Why LTC bonds?

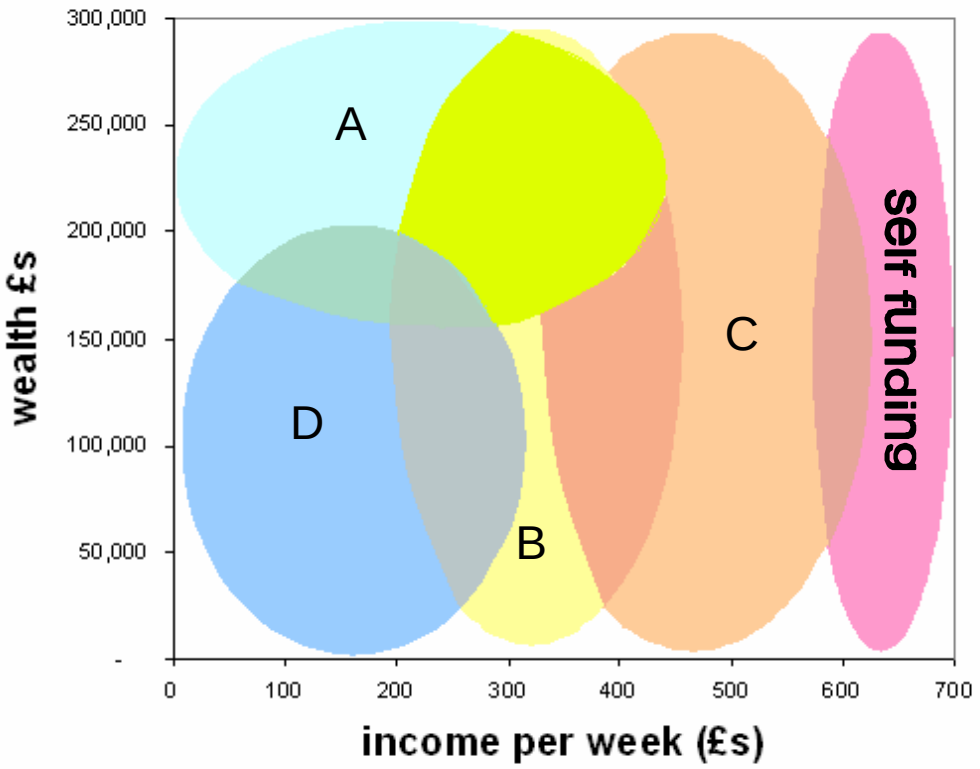
- Large population that cannot afford any LTC
- Like premium bonds but would pay out only if LTC needed otherwise go to estate or pay funeral expenses
- Would pay monthly prizes e.g. like premium bonds
- Would accrue interest just as in a bank
- Experience tells us that people on low income buy premium bonds, lottery tickets etc.
- Would at least be a contribution and would attune the population to saving for care in old age

How do DLAs work?

- Works likes a pension annuity
- But:
  - Higher payments if become disabled
  - Even high payments if go into care
  - Actuarially fair
- It works by trading off competing risks since LTC risk tends to be negatively correlated with longevity risk

What is the market?

Income-wealth map and market penetration



Key

A= Equity release

B= top up insurance

C= DLA

D= LTC bonds

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Something for everybody……

Means testing

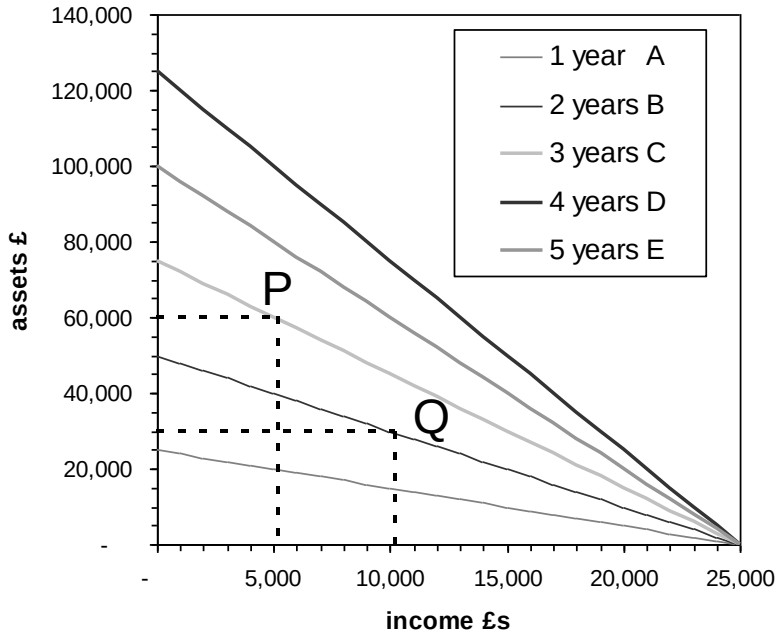
- Complex to understand
- Disincentive to save and crowds out private finance solutions
- Unfair because people just above the threshold have no state support or limited means to insure against risk
- Its not what people want (Green Paper consultation)

Principles on new form of means testing

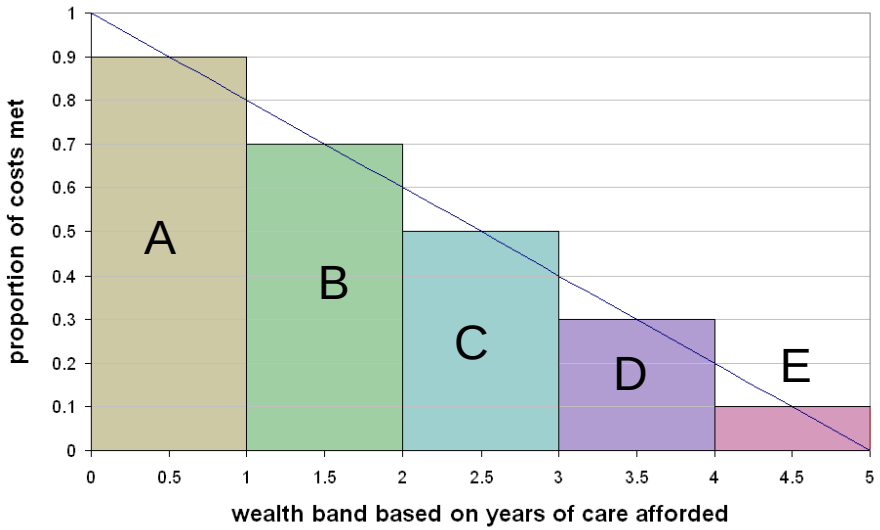
- All people should receive something unless they are self-funders
- It should be based on income and assets
- It should not dis-incentivise people to save
- It must be fair and transparent!
- It should be affordable in terms of public expenditure

Means testing or wealth testing?

Stage 1



Stage 2



1. People are placed into 'wealth bands' according to the years of LTC they can afford based on both income and assets.
2. People needing LTC receive a proportion of their LTC costs based on which band they are in as shown in example

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Example

- Assume that the value of the state pension and other benefits is worth £10k per year and that care costs £25k a year
- Based on the rates shown a person in each band would receive:
  - A: £13.5k (£25k-£10k) x 0.9 shortfall £1.5k
  - B: £10.5k (£25-£10k) x 0.7 shortfall £4.5k
  - C: £7.5k (£25k-£10k) x 0.5 shortfall £7.5k
  - D: £4.5k (£25k-£10k) x 0.3 shortfall £10.5k
  - E: £1.5k (£25k-£10k) x 0.1 shortfall £13.5k
  - >E nothing

Rates are illustrative only and actual rates would need to be affordable in public expenditure terms

And finally…the suggested role of the state

To:

- Provide regulation
- Provide incentives for people to take them up e.g. through the tax system
- Clarify the role of the state in terms of the state entitlement people can expect based on a unified assessment system
- Make it easier to get financial advice and direction at points of need or contact
- Covering risks that the market cannot handle
- Improve the quality and efficiency of care services

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END

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Article forthcoming in The Economic Journal:

"Paying for long term care with private finance"