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The Future of Social Care funding

IFoA Pensions & LTC Working Party
Products Research Group

Tom Kenny (Chair) – Just
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May 2017

The Working Group and the IFoA Support

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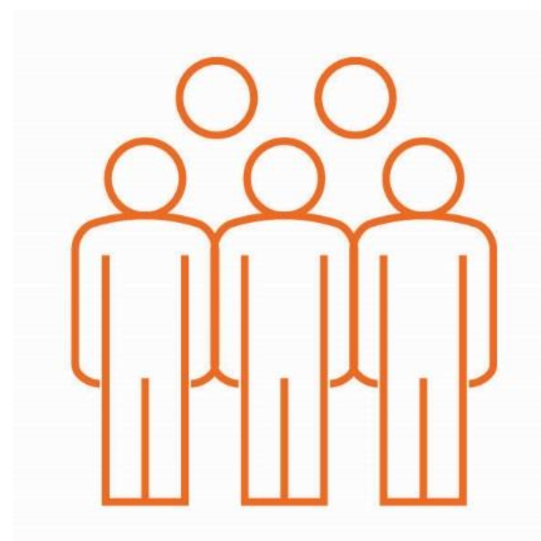

Agenda

- Background on social care funding
- Summary of published results
- Incentive to save - what impact will the new means test have?
- Retirement tool – the final countdown
- Learning from Australia
- Your input required

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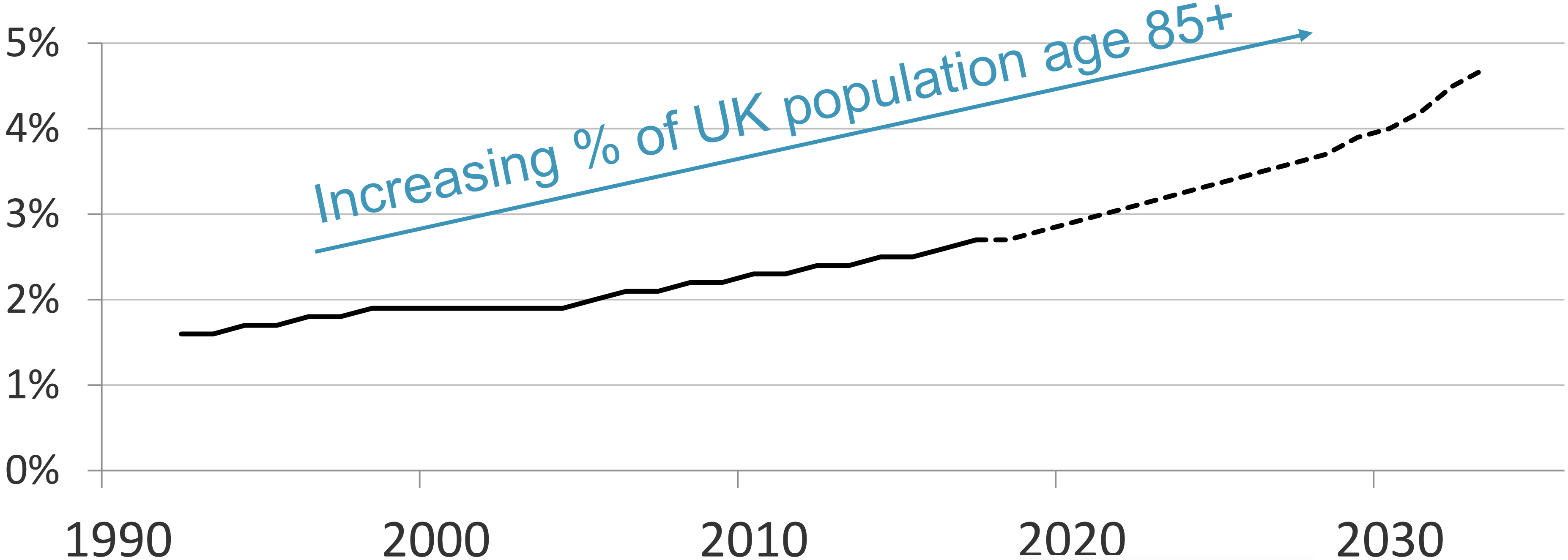
Background on social care funding

A week is a long time in politics…

Changing market dynamics



The political timeline (so far)

July 2011
Dilnot Commission recommendations released

May 2013
Draft Care bill

April 2015
Care Act 2014 comes into force. Implementation of national eligibility threshold and deferred payments schemes

Mar 2017
Spring budget announces social care Green Paper

Mar 2017
Manifestos released with social care high on the agenda

April 2020
Implementation of capped charging system due to come into force

Already a complicated system

- Care act 2014 introduced (in England and Wales only):
  - Deferred payment scheme
  - Care Cap of £72k
  - Increased means testing limits
- Complexity of the system means widespread misunderstanding about split of cost and the support that is available
- Means tested system operated by local authorities, not an extension of the NHS
- Regional variations exist

What's on the horizon?

"You cannot look at this question as simply being about money in the short term.

If we're going to give people the reassurance they need in the long term, it's about finding a way forward that will give a sustainable solution for the future"

"A Labour government would give social care the funding it needs and give a firm commitment to take failed private care homes into public ownership to maintain social care protection"

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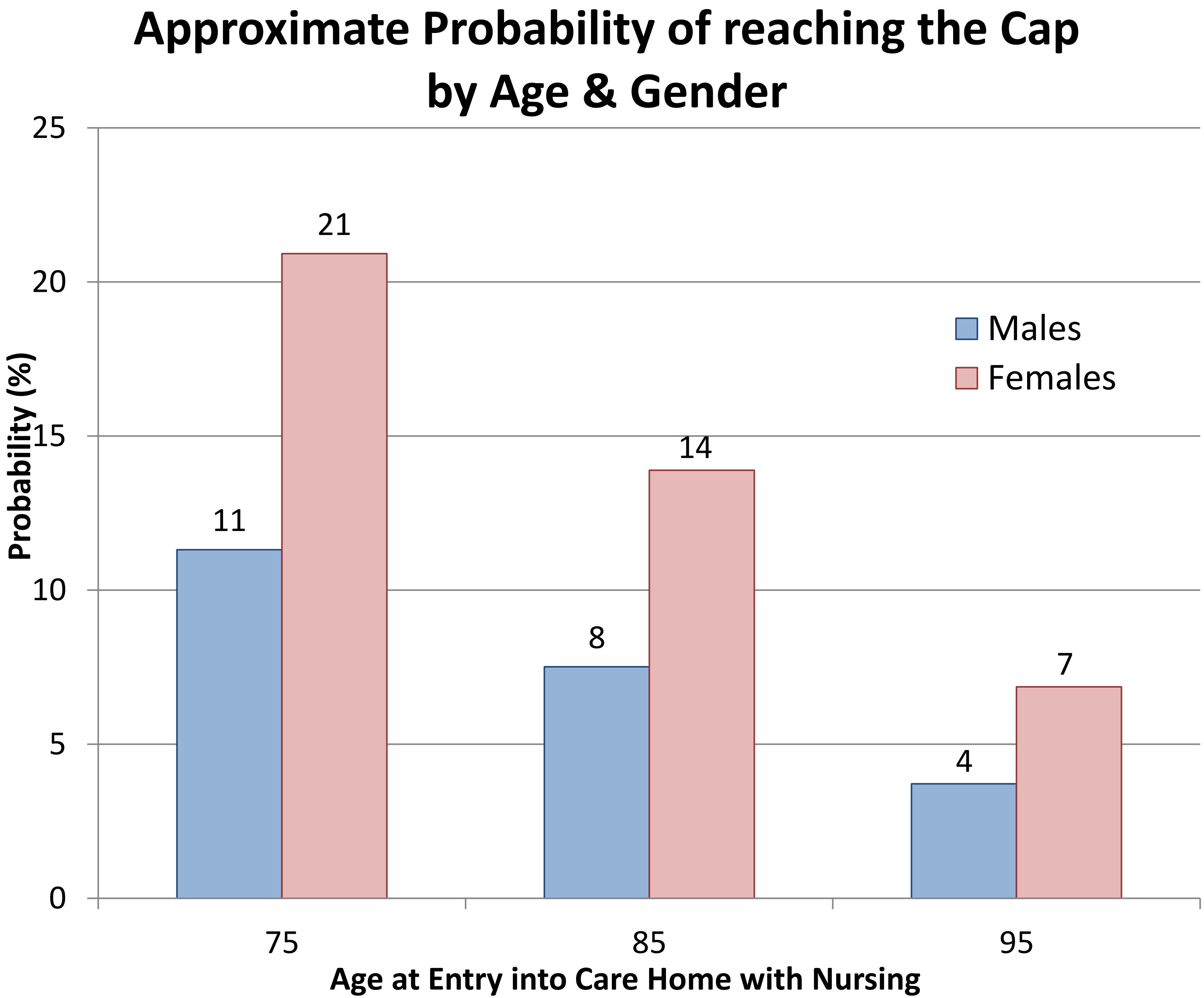
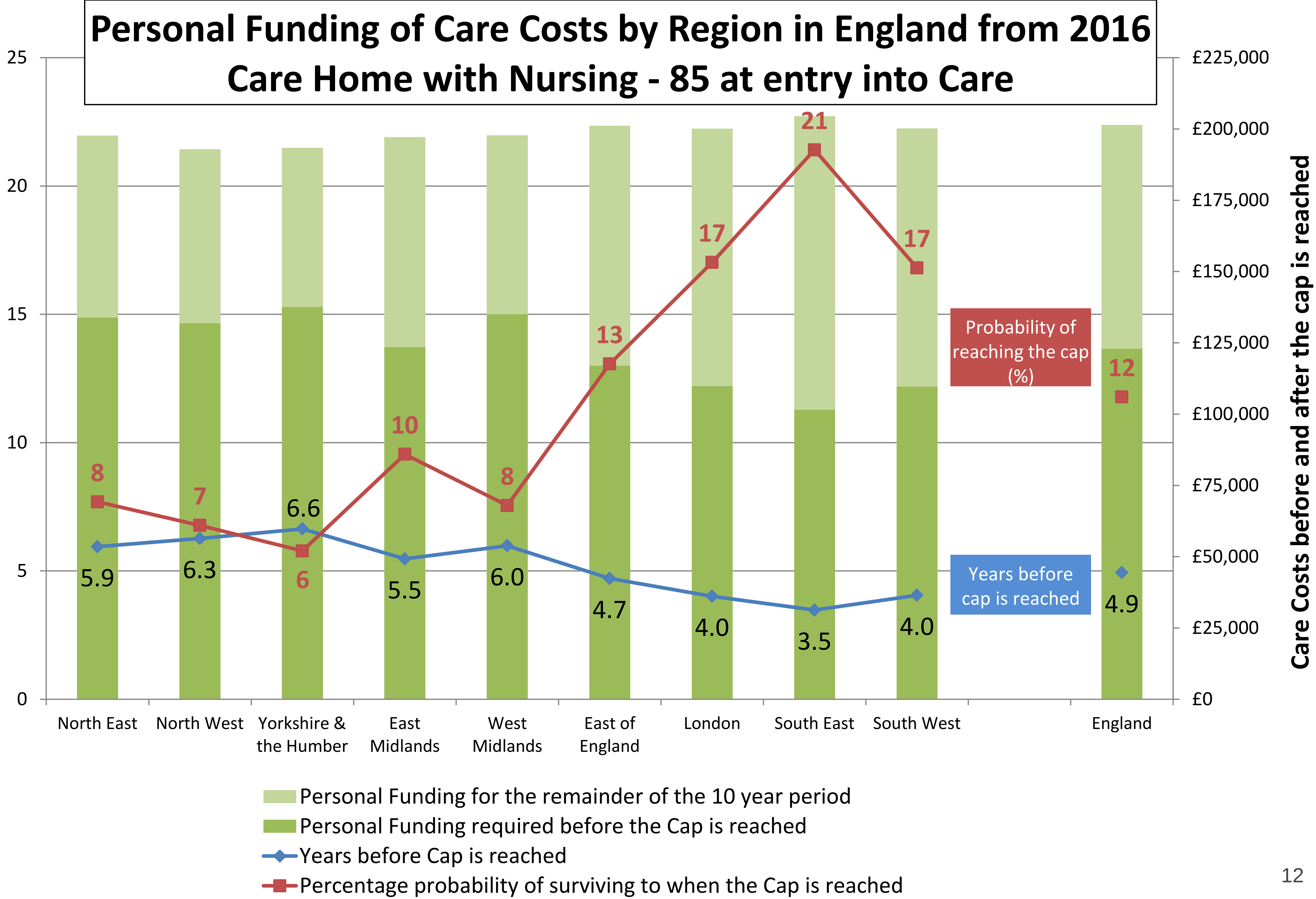
Published results

Products research group


Approximate Probability of reaching the Cap
by Age & Gender
Probability (%)
25
20
15
10
5
0
21
11
14
8
7
4
Males
Females
75
85
95
Age at Entry into Care Home with Nursing



Personal Funding of Care Costs by Region in England from 2016
Care Home with Nursing - 85 at entry into Care
25
20
15
10
5
0
£225,000
£200,000
£175,000
£150,000
£125,000
£100,000
£75,000
£50,000
£25,000
£0
Care Costs before and after the cap is reached
8
7
6
10
8
13
17
21
17
12
5.9
6.3
6.6
5.5
6.0
4.7
4.0
3.5
4.0
4.9
Probability of reaching the cap (%)
Years before cap is reached
North East
North West
Yorkshire & the Humber
East Midlands
West Midlands
East of England
London
South East
South West
England
Personal Funding for the remainder of the 10 year period
Personal Funding required before the Cap is reached
Years before Cap is reached
Percentage probability of surviving to when the Cap is reached

Possible product innovations

Care ISAs

Variable annuities

Income drawdown

Equity release variations

Pre-funded protection

Disability-linked annuity

?

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Changes to means testing

Encouraging savings for care

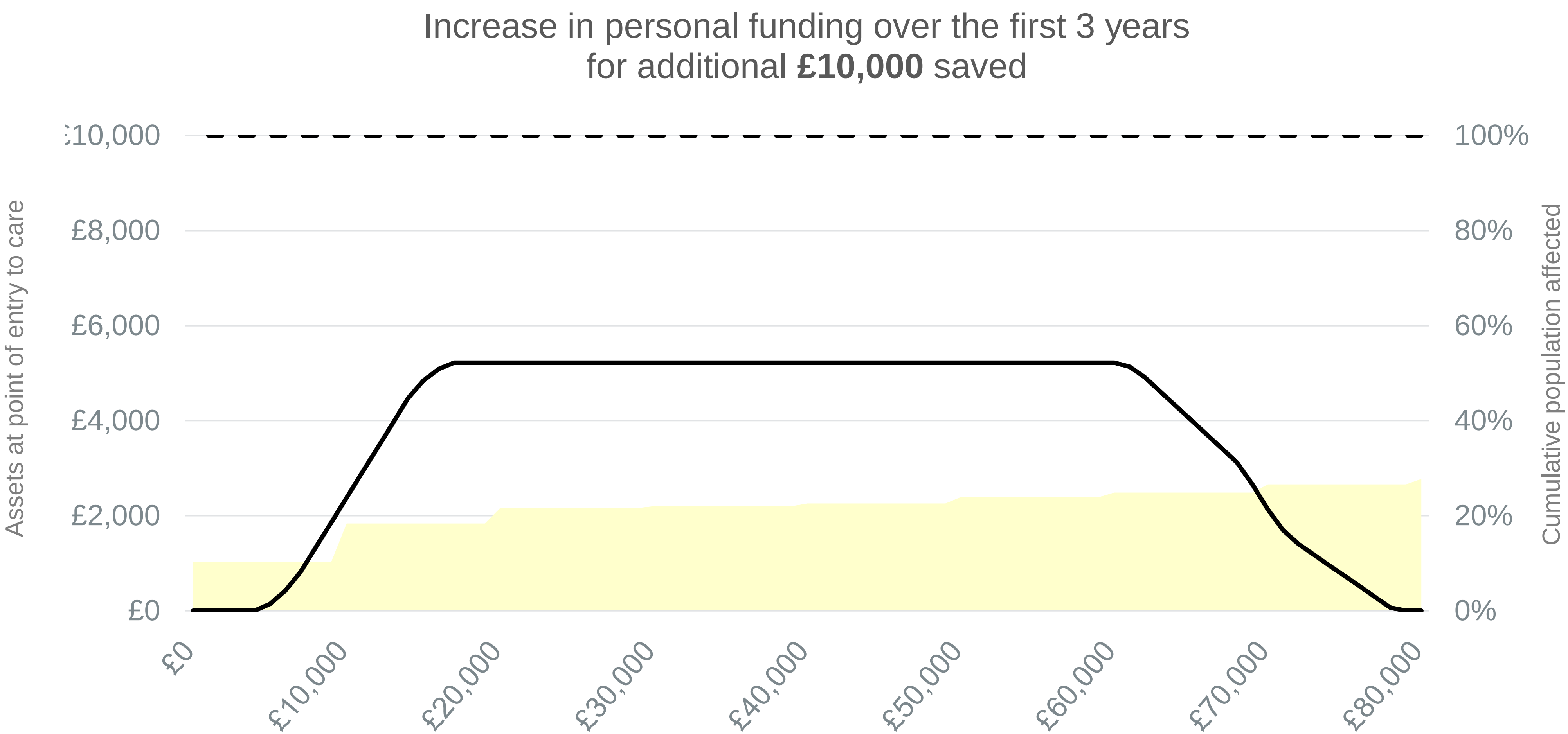
One of the major challenges to address is the incentive to save for potential future care costs. In our analysis we found:

1. The current means testing system is a **disincentive to saving**
2. Means testing thresholds as set out in ‘the Act’ provide a greater level of reward for savers than the existing thresholds, and may increase the level of saving for care, but they **could still act as a barrier**
3. Additional money put aside could lead to an increase in the amount that the individual has to contribute to their care costs with **no change in the cost or quality** of care received

Scope of means testing investigation

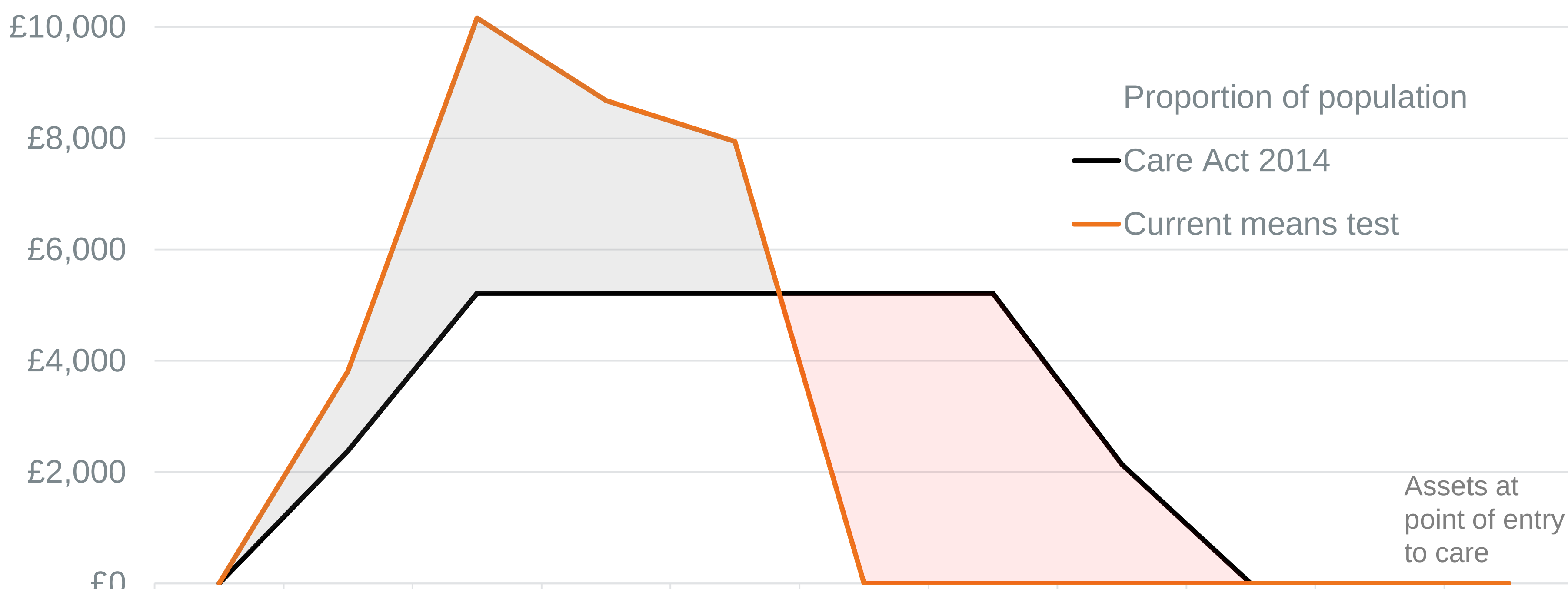
- Our **aim** was to analyse the impact of the new means test limits on incentivising saving towards long term care, extending our scope in 2 ways:
  - expand our analysis to understand the impact on savers of a range of **different levels of means testing thresholds**
  - overlay the results with **population data** to understand the current population dynamics and who will benefit/lose out from changes to the current thresholds

Impact of new means test limits (Care Act 2014)



Impact of change in upper capital limit

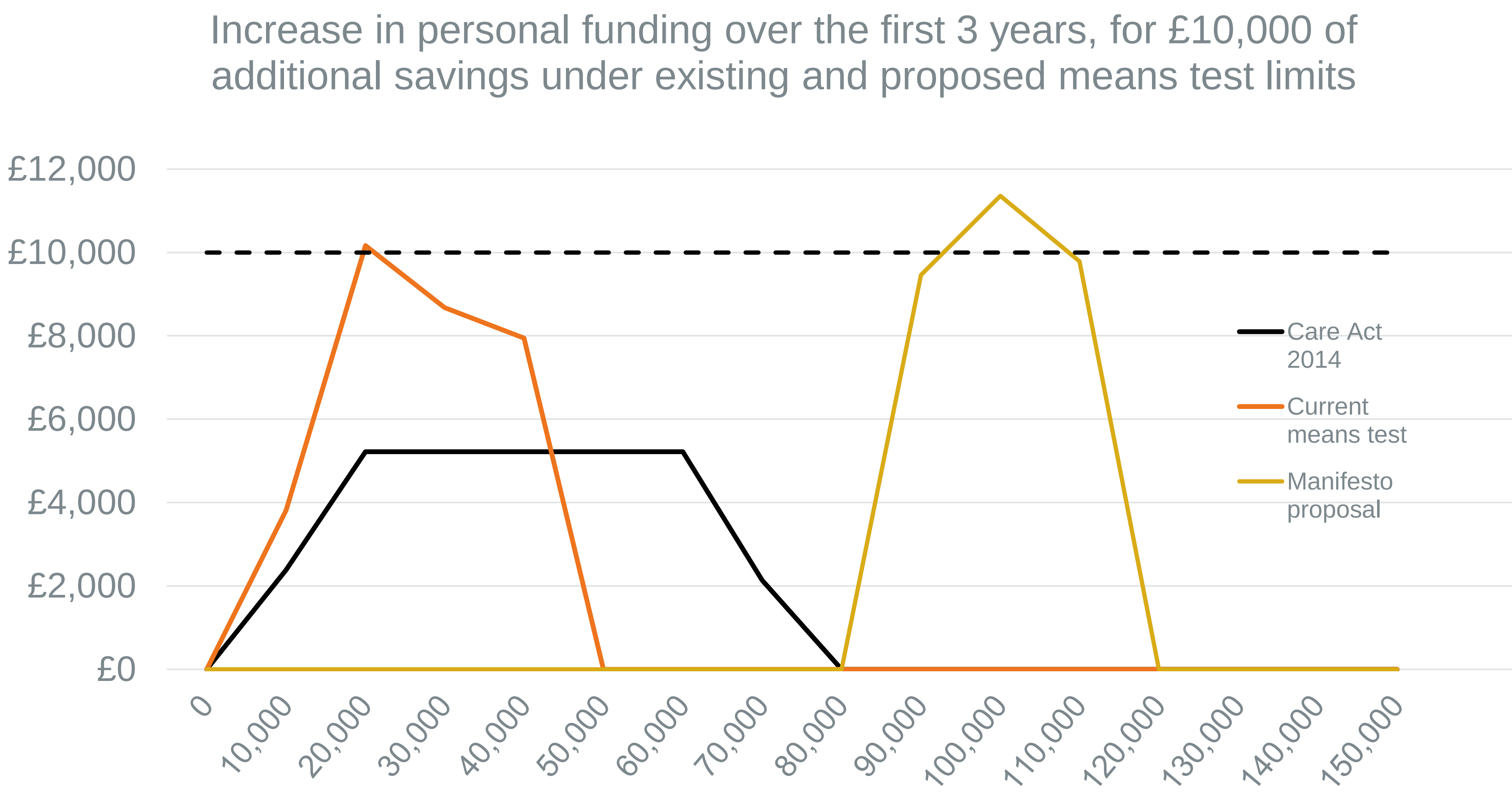
Increase in personal funding over the first 3 years, for **£10,000** of additional savings under existing and proposed means test limits



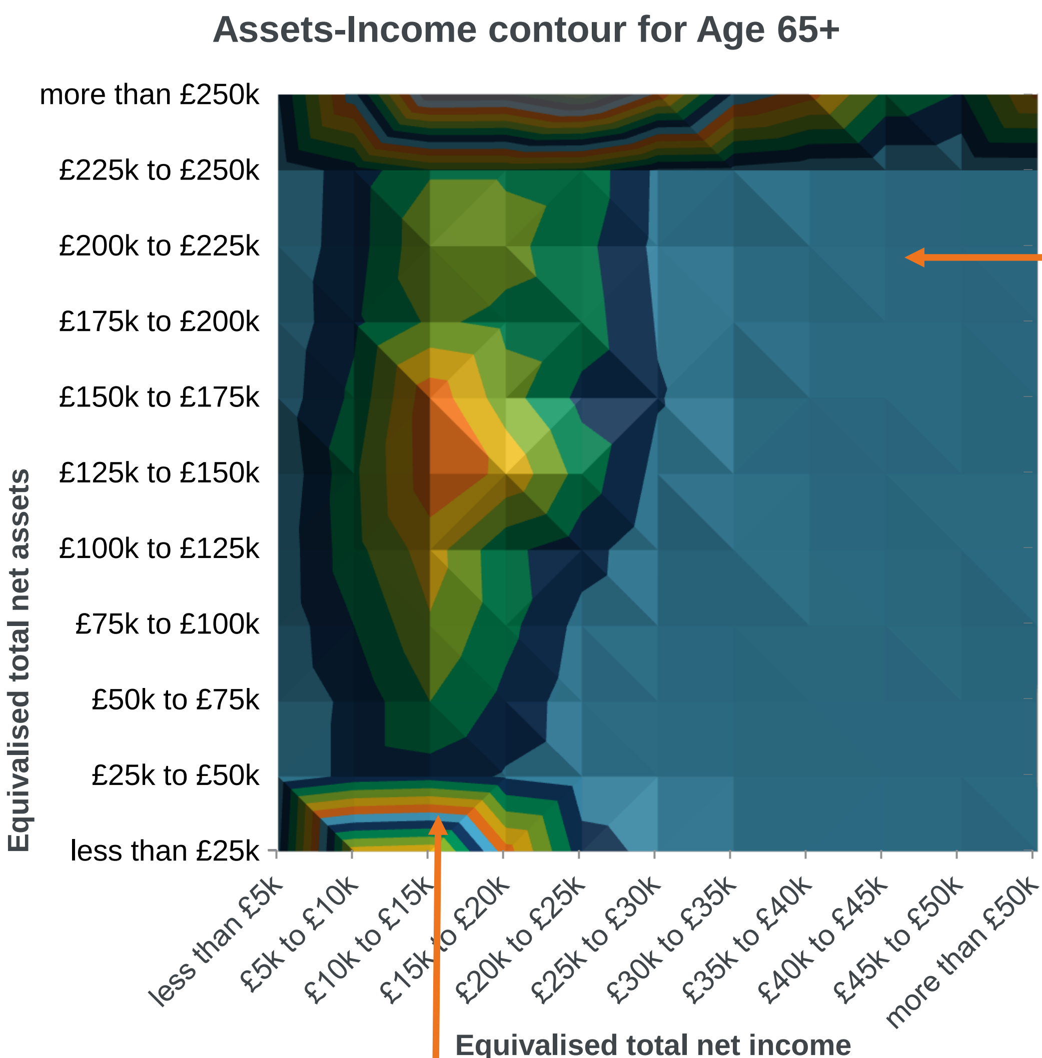
	0	10,000	20,000	30,000	40,000	50,000	60,000	70,000	80,000	90,000	100,000
Proportion of population	10.3%	8.0%	3.3%	0.4%	0.6%	1.3%	1.0%	1.7%	1.1%	2.3%	2.3%

- Less than 30% of those 85+ have assets of less than £80,000

What might the future hold?



Population dynamics



Median assets of £200,000 for those 65+ reducing to £170,000 for those age 85+

- Polarised results driven by home ownership
- Relatively high proportion of asset-rich homeowners
- Total net income clustered around £10-£20,000 p.a.

Median income of £16,000 for those 65+, reducing to £13,000 for those age 85+

Summary of findings

- The current means testing system can cause a disincentive to save with an effective ‘tax rate’ of over 100% for some people!
- Under the Care Act 2014, those with few assets on entry to care have a higher disincentive to save
- There is less/no disincentive to save for:
  1. Those with high assets on entry to care
  2. Those with high income in retirement
- Individuals could put money aside into means testing exempt products to reduce their income in retirement and protect their assets eg income bonds, funeral plans, trusts

Recommendations

- Removal of biases in the means testing system that penalise less wealthy savers
- Introduction of new categories of financial products that allow
  - savings to be exempt from the means test up to a specified threshold, for example
    - savings from pensions ring-fenced for care costs
    - care savings accounts
  - if they do not need to be used then given exemption for Inheritance Tax

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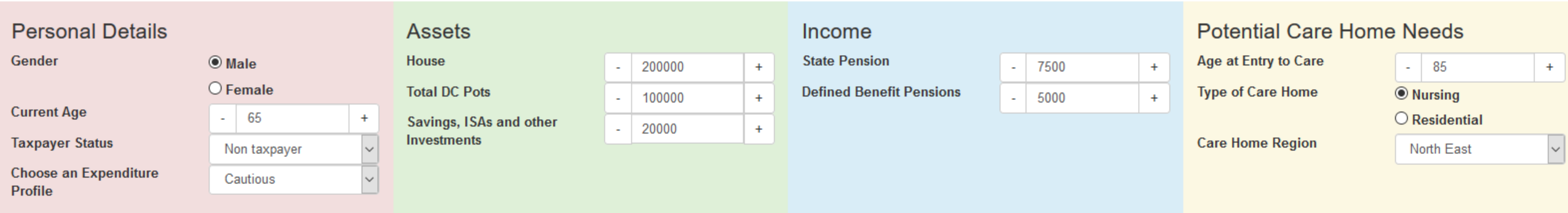
The Final Countdown!

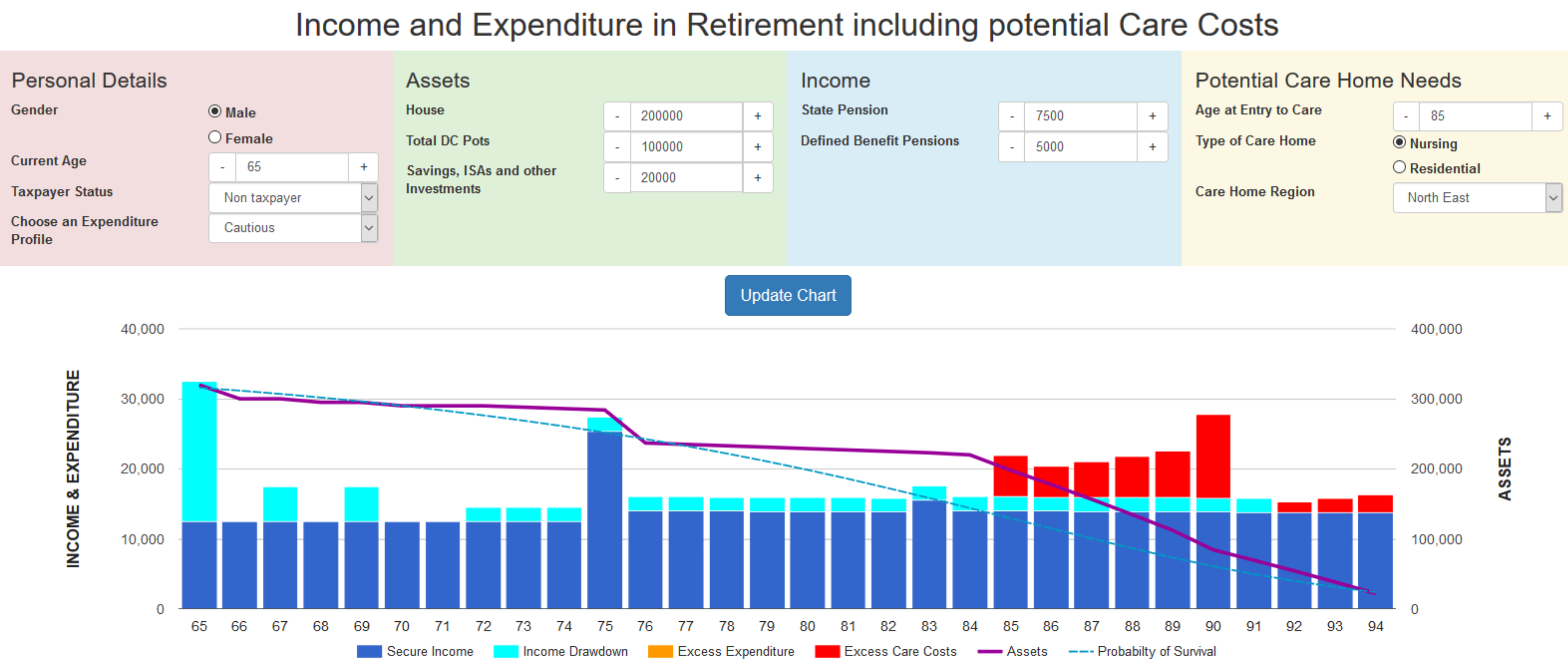
Helping people manage money in retirement

- Developing a straightforward interactive web-based tool to
  - help guide people to manage their income and assets in retirement
  - and, equally importantly, manage their expenditure in retirement
  - in the expectation that care provision may well be needed in later life
- The model is in development
  - aiming to make available later this year
  - show snapshots of the model today
- It’s The Final Countdown for their money in retirement

Income and Expenditure in Retirement including potential Care Costs



- Capture some key data to initiate the model
- Personal Details
  - include a number of Expenditure Profiles – we'll start with a 'Cautious' profile
- Assets
  - includes any DC pots as well as property and savings
- Income
  - includes state pension, DB pensions and annuities
- Potential Care Home Needs
  - care fees depend on needs and vary within region



- Model displays projected income and assets including
  - excess expenditure and care fees over income
  - probability of survival
- User can add/delete events – as shown on next slide
  - e.g. one-off or regular drawdown, annuity purchase

Income and Expenditure in Retirement including potential Care Costs

Personal Details

Gender (●) **Male** ( ) **Female**

Current Age - 65 +

Taxpayer Status Non taxpayer

Choose an Expenditure Profile Cautious

Assets

House - 200000 +

Total DC Pots - 100000 +

Savings, ISAs and other Investments - 20000 +

Income

State Pension - 7500 +

Defined Benefit Pensions - 5000 +

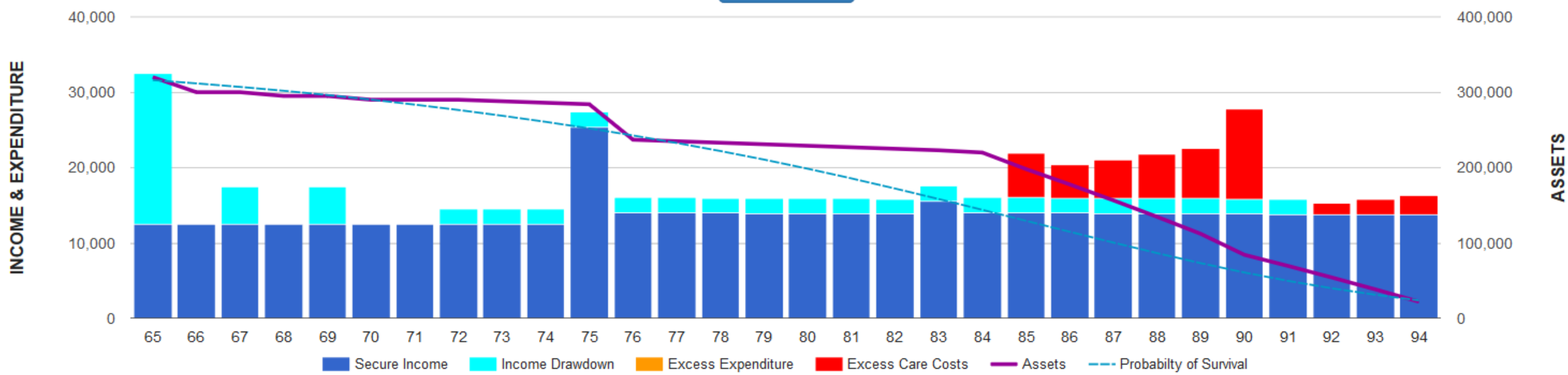
Potential Care Home Needs

Age at Entry to Care - 85 +

Type of Care Home (●) **Nursing** ( ) **Residential**

Care Home Region North East

Update Chart

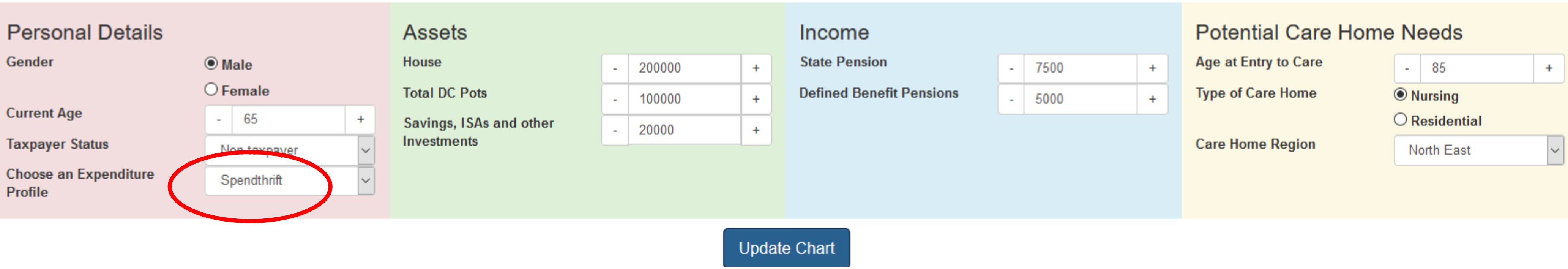


List of Events

Add new event | Delete selected event

Age at Event	Type of Event	Amount	£/%	Repeat?	Period (Years)
65	One-Off Drawdown	20000	£	N	0
67	One-Off Drawdown	5000	£	N	0
69	One-Off Drawdown	5000	£	N	0
72	Regular Drawdown	2000	£	Y	20
75	Annuity Purchase	45000	£	N	0
83	Annuity Purchase	6000	£	N	0

Income and Expenditure in Retirement including potential Care Costs



- Changing the Expenditure Profile to ‘Spendthrift’
  - reflects extra expenditure in early phase of retirement
  - but assets run out after about 6 years of care home fees

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Learning from the land down under

Why Australia?

MINIMUM ADDITIONAL LEVEL OF INCOME AND/OR GUARANTEED LEVEL OF INCOME + BROADLY CONSTANT REAL INCOME FOR LIFE + FLEXIBILITY = CIPR

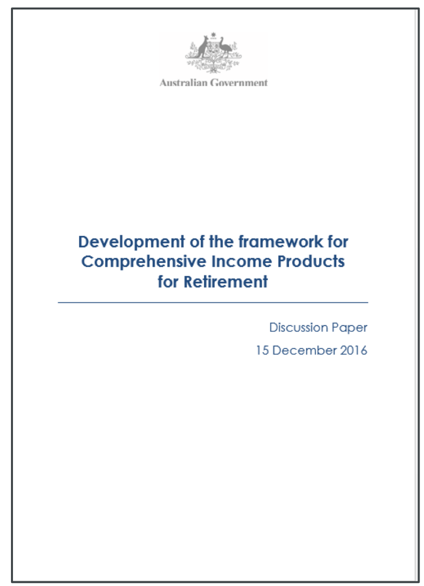
Australian Government
Department of Human Services

Why Australia?

- Australia has many parallels with the UK in terms of demographics and post-retirement funding systems
- Limited research completed in recent years comparing the UK and Australian systems
- Several recent and planned legislative and regulatory changes relating to post-retirement funding

Minimum annual retirement contribution levels

Year	Australia	UK
2017-18	11.0%	2.0%
2018-19	11.5%	5.0%
2019-20	12.0%	8.0%


Australian Government

Development of the framework for Comprehensive Income Products for Retirement

Discussion Paper

15 December 2016

Why Australia?

We will focus on relevant learnings from the Australian system comparing four aspects:

- post-retirement demographics
- funding of care
- insurance and other product solutions
- recent and planned government legislative and regulatory changes

Post-retirement demographics

- Ageing population
  - age 65+ projected to increase from 14% to 22% in 2061
  - age 85+ expected to more than double to 5%

Table 1: Old age dependency

Year	Japan	USA	China	Australia	UK	Thailand
1990	17%	19%	8%	17%	24%	7%
2010	36%	19%	12%	20%	25%	12%
2030	57%	32%	25%	31%	34%	26%
2050	82%	34%	40%	36%	39%	44%

Source: US Census Bureau

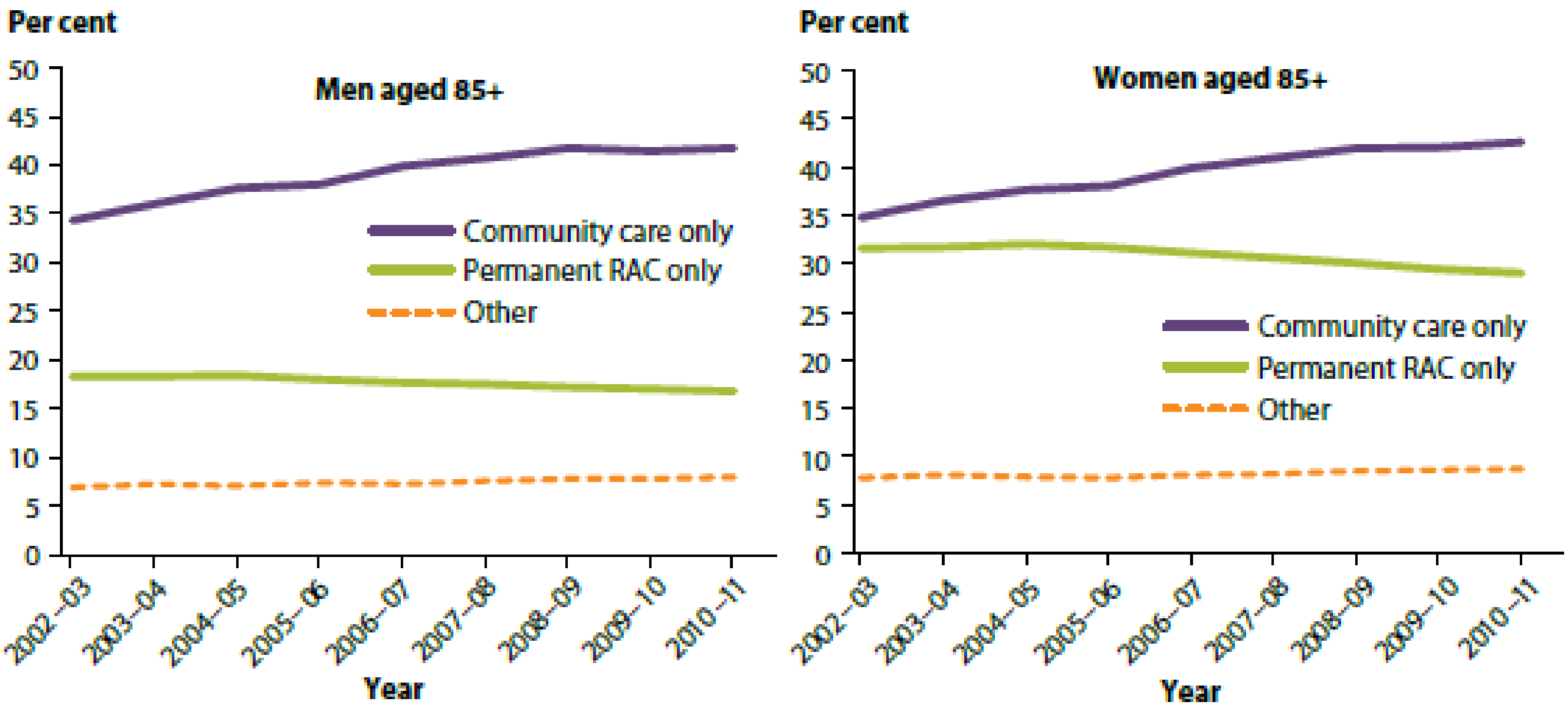
- Life expectancy (M/F) at age 65 increasing (Source: OECD)

	2010	2014
Australia	18.9/21.8	19.4/22.2
UK	18.2/20.8	18.8/21.3

Funding of care in Australia

- National information centre launched in 2013
- Caps apply (figures at 20 March 2017)
  - Annual cap of $26k and Lifetime cap of $63k
- Means tested care fee - need an aged care assessment
  - All assets are included
  - Property disregard applies
- Basic daily fee pegged to Age Pension + accommodation payment (upfront bond or ongoing) + extra services fees

Funding of care in Australia



Note: 'Other' includes use of respite RAC only, or use of combinations of permanent RAC, respite RAC and community care. Figure excludes ACAP and TCP use.

Source: AIHW 2014b: Figure 2.8.

Figure 6.3.1: Rates of use of aged care services by sex for people aged 85 and over, 2002–03 to 2010–11

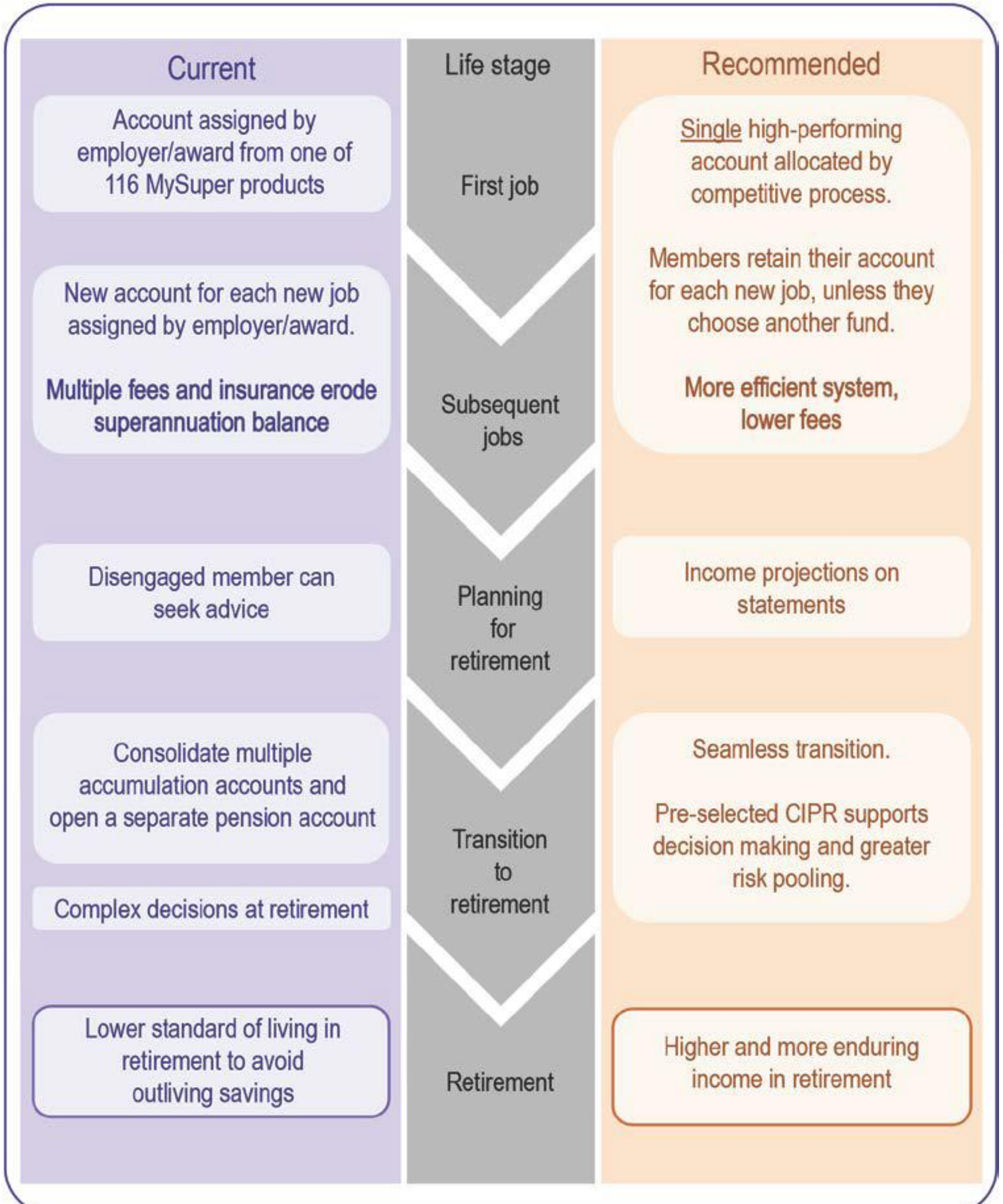
Legislative and regulatory environment

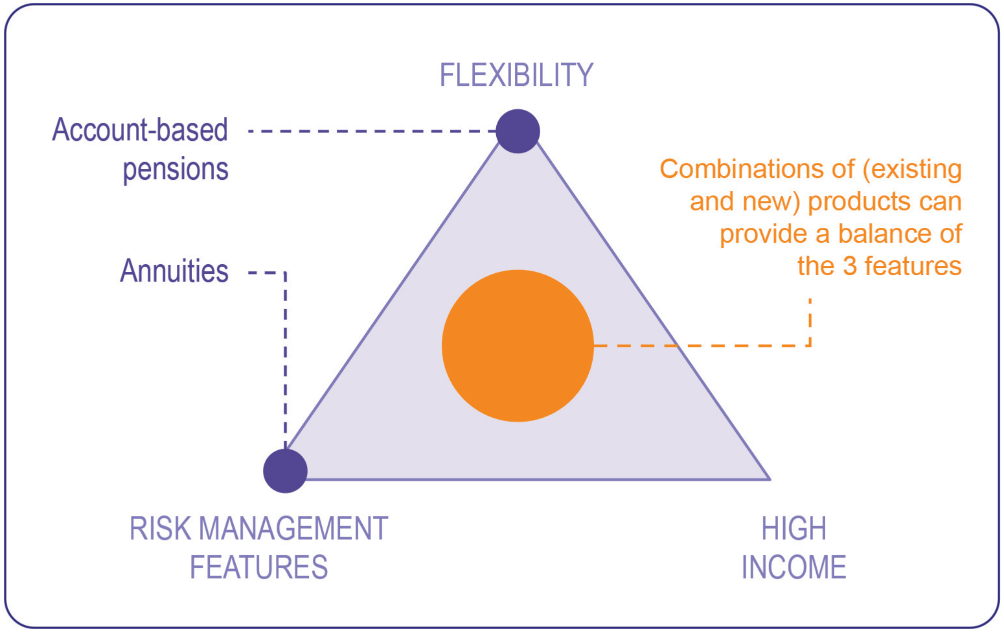
- Several key regulatory changes expected to encourage market for annuity-type products in Australia:
  - Government enshrined objective of superannuation to provide income in retirement to substitute or supplement the Age Pension
  - "CIPRs" (Comprehensive Income Products for Retirement) framework
  - Removal of impediments to deferred and group/pooled annuity products
  - Consultation on CIPR and MyRetirement products ends on 9 June 2017

Legislative and regulatory environment

PROBLEMS SEEKING TO BE ADDRESSED	OBJECTIVES OF CIPRS PRODUCTS AND THE CIPRS FRAMEWORK
Individuals are **self-insuring against longevity risk** and may be living more frugally in retirement than they need to	**Increase individuals' standard of living** by facilitating risk pooling – providing security of income for life and the potential for higher income in retirement
Individuals face **a lack of diversity and choice** in retirement income products, in particular an absence of products that efficiently manage longevity risk	**Increase the availability and choice** of products that efficiently manage longevity risk
The superannuation system is **not achieving its objective efficiently** due to its over-reliance on account-based pensions	**Increase the efficiency of the superannuation system** so that it can better meet its proposed objective
Individuals face **complex financial decisions**, a lack of guidance and behavioural biases at retirement but many are unlikely to seek financial advice	Empower trustees to provide members with **an easier transition into retirement**

Legislative and regulatory environment





Products

- Annuity market different direction of travel:
  - annuitisation levels 3% in Australia but rising
  - 75% in UK (pre-2014) and now 30% UK (Q3 2016)
- Retirement and care annuities now widely available on platforms and via industry superannuation funds
- Growing equity release market
- Deferred annuities likely to become popular
- Growing market for care insurance
  - Challenger's CarePlus annuity sales AUD 90m 1H17, +100% vs 2H16

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Over to you

Discussion points

1. What do you think will be in the Green Paper?
2. If the means test threshold changes to be £100k including property how will consumers behaviour change? What can insurers react?
3. What should change in the social care funding system?
4. How are pensions freedoms going to affect social care funding?
5. What are the barriers to product innovation in the LTC market?

Questions

Comments

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Appendix 1: Assumptions underlying the model

- Illustrations in the pack, unless stated otherwise, are based on:
  - Assumptions underlying our care cap model:
    - care costs based on Laing & Buisson report
    - survival rates based on PSSRU/BUPA Report on Length of Stay in Nursing Homes in England (2011)
    - all amounts inflated by 3.5% per annum
    - as cap increases, the percentage of the cap achieved remains constant
    - individuals choose to continue to make top-up payments even after cap is reached
  - Means testing model :
    - Income of £12,000 on entry to care equal to the personal expense allowance
    - Results focus on the impact of surviving 3 years in LTC

Appendix 2: Regional variations

Scotland:
- Free personal care for over 65s and free nursing care for all (at local authority rates).
- National deferred payment system.

Regional variation in level of provision (eligibility criteria) and costs
- across jurisdictions
- within some jurisdictions

Northern Ireland:
- Means tested benefits – lower limit is £14,250 and upper limit is £23,250

England:
Care Act 2015 proposals relate to England.
- New Charge Cap
- New deferred payment system.

Wales:
- Means tested benefits at single ‘capital limit’ of £24k
- Greater integration of health and social care system