Foreword

Adequate incomes in retirement and the ability to meet the potentially high costs of long-term care in later life are major issues for individuals and for governments worldwide. Changes to the UK state pension system came into force in 2016 and reforms to the English long-term care financing system are planned for 2020. These two sets of reforms were designed largely in isolation from each other.

Which is why this new report is so very welcome. It considers the state pension and long-term care financing systems in tandem and highlights the interactions between the two systems, especially over the long-term.

Through vignettes and aggregate analysis, the researchers have investigated some really pertinent issues such as:

- How important differential uprating rates can be to the overall position of an individual and overall costs;
- The potential for re-balancing public resources between the two systems in light of much public debate in both areas e.g. on the future of the state pension “triple lock”;
- Differences between the systems as applicable in the devolved administrations of Scotland and Wales compared to England
- Considerations when thinking about whether or not the proposed £72,000 cap on long-term care costs should be subject to regional variation or uniform across the country

I am not aware of anywhere else where analysis such as this, all in one place, can be found. We are indebted to the Nuffield Foundation for funding such an important piece of research. I would also like to thank all members of the steering group, who regularly contributed to the research team to help inform and direct their analysis. For anyone involved in policy or decision-making or impacts on private sector institutions in pensions or long-term care, this report is a must read.

Trevor Llanwarne
Interactions between state pensions and long-term care funding reforms

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A Research Report by John Adams, Chris Curry, Ferran Espuny-Pujol, Ruth Hancock, Bo Hu, Derek King, Sarah Luheshi, Marcello Morciano, Timothy Pike, Shamil Popat, Raphael Wittenberg

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Executive Summary

In April 2016 major reforms to state pensions were implemented in Great Britain. Reforms to the English long-term care financing system were also to be introduced in 2016 but have been postponed until 2020. The state pension reforms replace the existing two-tier state pension system with a single tier pension set just above the minimum income guaranteed through means-tested benefits. It affects only people reaching State Pension age from April 2016. The long-term care reforms introduce a cap on lifetime liability for care costs. To reach the cap, people will need to have eligible care needs for a considerable period, typically at least three years.

The primary objective of the state pension reforms is to provide a clearer foundation for private pension saving and reduce reliance on means-tested benefits in retirement by setting the level of the new State Pension (nSP) above the level of the minimum income guaranteed by the means-tested benefit Pension Credit. The long-term care reforms introduce a lifetime limit on individual liability for care costs to provide protection against the risk that care costs could use up nearly all of an individual's savings.

The long-term effects of both sets of reforms will depend on how details of the systems are set in the intervening years, and in particular how components of the systems are adjusted each year – ‘uprated’ – for inflation. This report summarises the findings from a research project which aims to promote informed debate on how the reforms could evolve, highlighting the interactions between the two systems. Amongst other things, the study has analysed the impact of the reforms to 2030 under uprating assumptions consistent with current policy and under alternative uprating assumptions. A separate more detailed Technical Report of the analysis is available.

Public expenditure effects under current uprating policies

- If the triple lock (the highest of growth in earnings, prices or 2.5%) is applied indefinitely, we project that the reformed pension system will cost a similar proportion of gross domestic product (GDP) as the previous system would have until the 2040s, but its cost will then rise more slowly.

- If uprated by earnings, the reformed pension system will cost less than the previous system from about 2030. By 2060, the saving would be equivalent to about 1% of GDP.

- If the long-term care funding system is reformed according to previous government announcements, we project that public spending on long-term care for older people would reach 0.92% of GDP by 2030 compared with around 0.67% in 2015, and 0.86% in 2030 if the current funding system continued.

Gainers and losers from reforms under current uprating policies

- Gains in net income from the pension reforms are small at State Pension age but increase during retirement.

- Home-owners and people on higher incomes tend to gain most from both sets of reforms. Lower income renters can lose more in means-tested benefits than they gain in state pension income.

- People who had care needs in April 2016 are the most affected by the delay in implementation of the long-term care reforms. The cap would have helped to protect the savings of those on modest incomes who are funding their care from their savings.
**Alternative uprating scenarios**

It could be argued that resources for older people should be more focused on the risk of requiring costly care in late old age. We therefore examined a number of more generous uprating scenarios for the reformed long-term care system, some in combination with less generous uprating of the state pension system.

- The more generous care uprating scenarios all increase public spending on long-term care by 2030 but unlike the long-term care reforms themselves, they tend to favour those on lower incomes.
- By 2030, uprating the state pension by earnings rather than the triple lock would go some way to paying for the more generous long-term care uprating scenarios.
- Uprating pensions by prices – although not allowed under present legislation – would more than pay for more generous uprating of the care system.

**Comparisons between England, Scotland and Wales**

The long-term care systems in Scotland and Wales differ from that in England. Scotland has introduced ‘free personal care’. Wales has a similar system to the current English system, but is more generous in some respects, e.g. it has a maximum weekly charge for home care. We therefore examined the effects on individuals of each system and found that:

- The effects of differences in the funding systems depend on the length of time for which individuals need care – especially high intensity home care or residential care.
- It is only for people who need care for long enough to benefit from the cap that the English reforms produce similar reductions in lifetime care costs to a Scottish-style system of free personal care.
- The Welsh system’s maximum weekly charge for home care can be more beneficial than the English reforms for people who need only home care.

**Regional variations within England: should the planned cap on care costs be uniform across England?**

We collated data on regional variations in care home fees, incomes, wealth, home-ownership and disability-free life expectancy. It is clear that the effects of the long-term care reforms will vary regionally. The lower care home fees and lower wealth in more deprived areas raises the question of whether there is a case for the cap to be lower in more deprived areas and higher in more affluent areas. In particular, regional differences in care home fees mean that people in more affluent areas reach the cap more quickly than people in less affluent areas. It could however be argued that uniformity across the country in the level of expenditure on care required before reaching the cap is more important than uniformity in the duration of care before meeting the cap.

The case for a lower cap in more deprived areas and a higher cap in more affluent areas is that:

- Differences in life expectancy with disability suggest that people in more deprived areas may need care for longer periods.
- Difference in care home fees mean that people in more affluent areas reach the cap more quickly than people in less affluent areas.
- Differences in older people’s incomes and savings mean that people in more deprived areas will in general spend-down a higher proportion of their savings before reaching the cap than residents in more affluent areas.
But

- A cap which varies regionally would be complex to administer.
- Uniformity across the country in the level of expenditure on care required before reaching the cap may be regarded as more important than uniformity in the duration of care before meeting the cap or in spend-down of savings.

The choice depends on which dimension of equity is considered more important.
1. **Introduction**

Understanding the interactions between state pension and long-term care reforms is a research project funded by Nuffield Foundation.

In April 2016, major reforms to state pensions were implemented in Great Britain. Reforms to the English long-term care financing system were also to be introduced in 2016 but have been postponed until 2020. The primary objective of the state pension reforms is to provide a clearer foundation for private pension saving and reduce reliance on means-tested benefits in retirement. The long-term care reforms introduce a lifetime limit on individual liability for care costs to provide protection against the risk that care costs could use up nearly all of an individual’s savings.

The combined effects of these two sets of reforms have received little attention despite interactions between them. The long-term effects of both sets of reforms will depend on how details of the systems are set in the intervening years, and on how policies in other parts of the welfare system evolve. This short report summarises the findings from a research project whose aim is to promote informed debate on alternative ways in which the pensions and long-term care financing reforms could evolve, highlighting the interactions between the two systems.

The project has involved researchers from the Pensions Policy Institute, the Personal Social Services Research Unit at the London School of Economics and Political Science (LSE) and the Health Economics Group at the University of East Anglia. The team has already published a series of reports and briefing notes which provide analysis of how the two sets of reforms interact, and of the consequences of detailed aspects of their implementation.

This report provides an overview of the key findings from these other publications. In addition, this report summarises new analysis of the public costs and distributional effects of alternative ways in which key parameters of the new State Pension (nSP) system and planned reformed care funding system might be adjusted each year for inflation (‘uprated’).

A more detailed Technical Report accompanies this summary. The Technical Report covers the analysis of the public costs and distributional effects of alternative uprating policies more fully and provides full details on the methods and assumptions underpinning the analysis.

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1 John Adams, Chris Curry, Sarah Luheshi, Timothy Pike, Shamil Popat
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3 Ruth Hancock, Marcello Morciano, Ferran Espuny Pujol
4 http://www.pensionspolicyinstitute.org.uk/casper
2. Reform Overview

a. The state pension reforms

For people reaching State Pension age from April 2016, a new State Pension (nSP) has replaced the basic State Pension (bSP) and the State Second Pension (S2P) and its predecessor, the State Earnings Related Pension Scheme (SERPS). At £155.65 a week, the full level of the nSP has been set five pence above the minimum guaranteed income for pensioners – known as the Guarantee Credit within the means-tested benefit Pension Credit. Some people retiring from April 2016 will get more than the full level of the nSP – if their accumulated state pension entitlements at the time the nSP was introduced are higher than if the nSP had been in place. People will get less than the full level if they have not made – or been credited with – sufficient National Insurance Contributions.

Savings Credit – a component of Pension Credit – has been removed for people reaching State Pension age from April 2016, on the grounds that the full level of the nSP is above the minimum income level guaranteed through Pension Credit.

The changes do not apply to people who reached State Pension age before the new arrangements were introduced. All pensioners will continue to be able to apply for Pension Credit and means-tested help with their rent and/or council tax. Entitlements to these benefits may be lower than they would have been under the previous system if state pension entitlements exceed what they would have received under the basic State Pension.

Box 1 provides more details of the reformed state pension system.
b. The long-term care reforms for older people

The 2014 Care Act introduced changes to long-term care funding in England. Currently when people need long-term care, their Local Authority (LA) applies a means test to establish how much they must pay towards the cost of that care. Those with capital above an upper threshold have to meet all of their care costs and where care is provided in a care home, the value of a person’s home is usually included in their capital. If their capital is below the threshold they have to contribute to the cost of their care from their income.

The reforms, planned to start in April 2020, introduce a lifetime cap on individual liability for care costs. For care in a care home, only the part attributed to care costs attributed to ‘daily living costs’ (sometimes referred to as ‘hotel costs’) does not count towards the cap. To reach the cap people will need to

<table>
<thead>
<tr>
<th>Box 1: Details of the state pension reforms implemented in April 2016</th>
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<tbody>
<tr>
<td><strong>The new single tier state pension</strong></td>
</tr>
<tr>
<td>- The new State Pension (nSP) replaced the previous two-tier system of a flat rate basic State Pension (bSP) and an earnings-related component – the State Second Pension (S2P), or its predecessor the State Earnings Related Pension (SERPS) – for those reaching State Pension age from April 2016.</td>
</tr>
<tr>
<td>- Like its predecessor, entitlement to the new State Pension depends on a person’s National Insurance Contribution (NIC) record. Thirty-five years of NICs are necessary to qualify for a full nSP compared with 30 years under the previous system, and a minimum of 10 years’ contributions is needed to qualify for any amount. Since there is no longer an earnings-related component of the state pension, ‘contracting-out’ is no longer possible.</td>
</tr>
<tr>
<td>- Protection of accumulated state pension entitlements for those under State Pension age: when the new State Pension was introduced, a foundation amount was calculated for each individual, based on their entitlement built up under the previous state pension system. This is then compared to the amount that the individual would have built up if the new State Pension system had been in place. Individuals will then take forward the higher of the two amounts (adjusted for time spent contracted out of the S2P and SERPS) into the new system. If the foundation amount is higher than the new single-tier level, the amount above the single-tier level will be protected and paid on top of the new State Pension.</td>
</tr>
<tr>
<td>- The three main means-tested benefits for pensioners – Pension Credit, Housing Benefit and Council Tax Support continue to be available. People whose state pension income is higher under the new State Pension than it would have been under the previous system will be entitled to reduced amounts of Pension Credit, Housing Benefit and Council Tax Support.</td>
</tr>
<tr>
<td>- Pension Credit aims to ensure that pensioners’ incomes do not fall below a minimum (the Guarantee Credit) and also provides a ‘reward’ through the Savings Credit component. The Savings Credit is being removed for people reaching State Pension age from April 2016.</td>
</tr>
<tr>
<td>- The nSP has been set just above the Guarantee Credit with the intention of reducing the number of pensioners receiving means-tested benefits.</td>
</tr>
<tr>
<td>- Uprating requirements: legislation requires government to uprate the nSP annually by at least the increase in average earnings. The present Government has given a commitment to uprate it by the ‘triple lock’ – the highest of the annual increase in earnings, prices or 2.5%. The standard Guarantee Credit – before any additions e.g. for disability – must be uprated by at least earnings.</td>
</tr>
</tbody>
</table>
have eligible needs for a considerable period (typically at least 3 years, depending on the cost of meeting their care needs).

The long-term care reforms also increase the upper capital threshold for people in residential care. People who are initially not entitled to public support with their care costs may become entitled to some support if their savings fall below the upper threshold even if they have not yet reached the cap.

People with care needs may also be eligible for one of two non means-tested cash benefits for people with disabilities, and to supplements to any means-tested benefits. The treatment of these benefits in the long-term care means test is complex. It is explained along with further details of the current long-term care funding system and the planned reforms in Box 2.
Box 2: Details of the current means test for long-term care and reforms planned for 2020
An individual’s entitlement to state help with the costs of long-term care depends on an assessment of their care needs and on a means test, both of which are administered by a Local Authority (LA).

The current system
- If the individual has capital above an ‘upper capital threshold’, currently £23,250, the individual pays the full cost of their care. For residential care, the value of the home is usually included in capital after the first 12 weeks.
- When capital is below £23,250, the state meets some of the cost depending on the individual’s assessable income.
- Assessable income includes a notional weekly income, known as ‘tariff income’ on capital between a ‘lower capital threshold’, currently £14,250, and the upper capital threshold. The rate of tariff income is £1 for each £250 between the lower and upper capital thresholds. Capital up to the lower capital threshold, and any income from it, is ignored completely in the means test.
- People with capital below the upper threshold are required to put all their assessable income apart from a ‘personal expenses allowance’ of £24.90 towards the costs of care in a care home; or all assessable income above 125% of the Pension Credit standard Guarantee Credit level towards the cost of care at home. (The 25% above the Guarantee Credit level is known as the ‘buffer’)
- People with capital below the upper threshold and receiving LA support will cease when they reach the cap and become entitled to LA support.
- For care at home, assessable income excludes any income from the Savings Credit component of Pension Credit. Assessable income in a care home excludes a small disregard on income from savings which is related to the Savings Credit but not limited to those actually receiving Savings Credit.
- The NHS makes a non means-tested contribution to assessed nursing care needs in a care home.
- A small number of people have their care needs funded fully by the NHS.

The planned reforms
- To benefit from the lifetime cap on care costs, a person will have to be assessed by a LA, as having eligible care needs. The LA will work out the weekly costs of meeting those needs taking account of local care costs and set a personal budget for the person’s care. It will keep track of the cumulative amount of those costs through the person’s Care Account. For home care users the amount included in the Care Account is not the person’s actual expenditure on care but the personal budget. For people in care homes, the amount included in the Care Account is neither the person’s actual expenditure nor the total home care fee. It is the care home fee covered by the personal budget minus an allowance for the daily living (or ‘hotel’) costs component of the fee. Neither the daily living cost nor any excess of the care home fee above the amount the LA is willing to meet (and has included in the personal budget) counts towards the cap. Until their Care Account reaches the cap, the LA will apply the current means test to determine how much the person must pay towards the cost of their care.
- Progress towards the cap is based on the total costs of individuals’ care needs, not the amount they pay towards that cost. Once the cap is reached, the state will meet the cost of their eligible care needs (calculated as above) without a means test. Daily living costs will continue to be means-tested even after the cap has been reached. The lifetime cap was expected to be £72,000 if implemented in 2016 and the daily living component £12,000 per year or £231 a week.
- The upper capital threshold in residential care will be increased. It was expected to be £118,000 in 2016.
- We assume that since the Savings Credit is removed for those reaching State Pension age from 2016, the disregard of savings income for people in care homes will not apply for people reaching State Pension age from 2016.

Disability Benefits
- People with care needs may also be eligible for one of two cash disability benefits – Attendance Allowance or Disability Living Allowance. Receipt of these benefits can also trigger increases in Pension Credit, Housing Benefit and Council Tax Support through a Severe Disability Addition, currently £61.85 per week which is added to the standard Guarantee Credit level.
- If someone receives help with care home fees from their LA, payments of these disability-related benefits cease. Payments to those initially not receiving LA support will cease when they reach the cap and become entitled to LA support.
- LA’s can include income from disability benefits in assessable income for home care but if they do so must make an allowance for any disability-related expenditure that the person incurs.

Uprating requirements
- Legislation on uprating policy for long-term care is less prescriptive than for pensions.
- Recent practice for many parameters has been, at best, price-linking. Capital thresholds have been unchanged for some years.
- The Government has indicated that the cap on care costs and the allowance for daily living costs in care homes will be linked to average earnings increases.
- Disability benefits have been uprated by price increases in recent years.
c. **Interactions between state pensions and public help with long-term care costs for older people**

If an individual’s net income changes as a result of an increase or decrease in their state pension entitlement, the contribution they are required to pay towards their care costs can change. Thus an increase in state pension income can be wholly or partially offset by an increase in liability for care charges. For those not entitled to public support with their care costs, increases in income can also slow down the rate at which they need to deplete their capital to pay for care.

For people entitled to the Severe Disability Addition in Pension Credit, a full new State Pension will not guarantee that their incomes take them above the level provided by Pension Credit so they may still be entitled to a means-tested supplement to their income.
3. Projected costs of the pensions and long-term care reforms

a. State pensions

The state pension system currently costs about 6.5% of gross domestic product (GDP) and this proportion is set to rise as the numbers of people over State Pension age rises and entitlements increase. Its future cost will also depend to a considerable degree on how it is uprated each year. Legislation requires the new State Pension (nSP) to be uprated by at least the annual increase in average earnings, but the current Government has given a commitment to uprate it by the ‘triple lock’— the highest of the annual increase in average earnings, the Retail Price Index or 2.5% – for the rest of this parliament. If the triple lock is applied indefinitely, the reformed pension system is expected to cost a similar proportion of GDP as the previous system until the 2040s but its cost will then rise more slowly than the basic State Pension. (Chart 1). If earnings uprating is applied, the new State Pension will cost less than the basic State Pension (bSP) from about 2030, and by 2060 the saving would be equivalent to about 1% of GDP.

Chart 1: The new State Pension with triple lock will require a smaller percentage of GDP to pay for it, from around 2046, compared to the basic State Pension

![Chart 1](chart.png)

Note: additional State Pension is the total of State Second Pension (S2P), or its predecessor the State Earnings Related Pension (SERPS)

b. Long-term care costs for older people

At £10.8 billion in 2015, or 0.67% of GDP, the public cost of long-term care for older people is much lower than the cost of state pensions. Its future cost is affected by various factors including: the numbers of older people, particularly those aged 85 and over; disability rates among the older population; the availability of unpaid care from family and friends; the future level of care home fees and the cost of providing care to people in their own homes. Our ‘base case’ (see Box 3) projection is that if the current long-term care funding system remained in place, the public cost of long-term care would rise to £19.6 billion in 2020 (at constant 2015 prices) or 0.86% of GDP (Chart 2).
Public spending on long-term care for older people in England under the current funding system is projected to need to increase by 80% in the next 15 years to keep pace with demographic change, or by over 90% if the reforms are implemented in 2020.

Note: long-term care spending includes NHS-funded care and disability benefits used to pay for care.

If the long-term care funding system is reformed according to previous government announcements (see Scenario 1 in Box 4), we project that public spending on long-term care for older people would reach £20.9 billion, or 0.92% of GDP, by 2030. This is an increase in public expenditure of 93% between 2015 and 2030, as compared with 81% if the funding system is not reformed.

Under the current funding system, private spending on long-term care is projected to increase from £7.9 billion, or 0.49% of GDP, in 2015 to £17.3 billion in 2030 (in constant 2015 prices, or 0.76% of GDP. It is projected to be lower under the reformed than under the current system because the state bears a higher share of care costs under the reformed system. Private expenditure is projected to reach £15.8 billion in 2030 or 0.69% of GDP under the reformed system. This is an increase of 99% between 2015 and 2030 in private expenditure compared with 117% if the funding system is not reformed.

Projecting long-term care expenditure further ahead is rather uncertain but demographic pressures are likely to continue to rise. We project that the number of older people unable to conduct at least one personal care task or activity of daily living without help will rise from £1.8 million in 2015 to 2.5 million in 2030, an increase of 44%. It will then continue to rise beyond the period covered by our expenditure projections to £3.1 million in 2040 and £3.6 million in 2050.
4. Gainers and losers from the state pension and long-term care reforms

The state pension reforms affect people reaching State Pension age from April 2016. The long-term care reforms will affect older people who need care for long enough after the reforms are implemented to reach the lifetime cap on care costs. To illustrate the effects of the reforms we considered a number of case studies (‘vignettes’) distinguishing two cohorts:

- those reaching State Pension age (65 for men, 63 for women) in April 2016 who will be affected by both sets of reforms but largely unaffected by the decision to postpone implementation of the long-term care reforms;

- those aged 78 in 2016 and starting to have care needs who would be unaffected by the state pension reforms but have lost out by the postponement of the long-term care reforms.

The vignettes were chosen for illustrative purposes rather than to be representative of the relevant cohorts. Findings presented here concern single people. The majority of older users of care services are single people or widow(er)s, in part because married people often rely on unpaid care from their spouses. Moreover, for married people the means test for long-term care mostly takes account of only the savings and incomes of the individual users. Each vignette was assumed to face the same care trajectory – an extreme trajectory chosen to illustrate the long-term care reforms. Vignettes begin receiving lower rate Attendance Allowance aged 75, start to receive home care aged 78, enter residential care aged 82 and die 4½ years later. More details of the vignettes and the care trajectory are given in the Appendix.

a. People who reach State Pension age from April 2016

Key findings for this cohort were:

- Gains in net income from the pension reforms are small at State Pension age but increase during retirement. This is because the new State Pension (nSP) has to be uprated each year by at least the increase in average earnings whereas under the current system, the second state pension is increased by only price inflation.

- Home-owners tend to gain from both sets of reforms, as do people on relatively high incomes. Home-owners do not received Housing Benefit so do not lose Housing Benefit as a result of higher state pension income. Home-owners are key beneficiaries from the cap on long-term care costs since among care home residents it is mainly (former) home owners who have savings above the threshold for entitlement to LA funding.

- Lower income renters are those more likely to lose out from the pension reforms as they can lose more in means-tested benefits than they gain in state pensions.

- Because they do not lose means-tested benefits, people on low incomes who do not claim their entitlements to means-tested benefits can benefit from the pension reforms. This is also the case for those on low incomes who are excluded from means-tested benefits because they have (quite modest) savings.
Chart 3 shows the net lifetime gains from the pensions and long-term care reforms for each of the vignettes reaching State Pension age in April 2016.\textsuperscript{6}

**Chart 3: Net lifetime gains from pensions and long-term care reforms are highest for high earning/high wealth individuals**

- \textsuperscript{6}We assumed that a small ‘savings disregard’ in residential care which is associated with the Savings Credit component of Pension Credit is removed as a result of the removal of Savings Credit. This explains why it is possible to receive slightly less support for LTC from the combination of pension and LTC reforms.

### b. People aged 78 in 2016

Key findings for this cohort were:

- The delay in implementation of the reforms significantly affects median and high earning vignettes who own their homes.
- Low earning vignettes who rent their home are unaffected.
- Median and higher earning individuals benefit most from implementation of reforms in 2016 and so are affected most by the delay in implementation.
- The effect of the delay on capital depletion is arguably greatest for the median earning vignettes. Compared to higher earners, they currently meet a greater proportion of their care costs by drawing down their capital and would have seen their capital depletion reduced considerably had the reforms been implemented in 2016 (Chart 4). However, the effect of the delay on capital depletion is substantial for both median and high earners.
Chart 4: The single homeowner on median earnings experiences only a slight percentage reduction in cumulative net income as a result of the delay in the reforms but the increase in capital depletion is substantial

5. The costs and distributional effects of alternative policies on uprating the reformed state pension system and the planned long-term care reforms

There has been considerable debate about the merits and affordability of the policy of uprating the new State Pension (or the basic State Pension for those reaching State Pension age before April 2016) by the triple lock. There has been less debate about how the parameters of the long-term care system – whether the current or the reformed system – or indeed the disability benefit system, should be uprated over time. Here we summarise analysis of the projected costs and effects on different income groups of some alternative uprating policies. The focus is on the long-term care system, but taking account of different possible uprating policies for state pensions.

The analysis uses linked simulation models to examine the effects of these alternative scenarios on projected aggregate costs of long-term care and state pensions and the distribution of gains from them that would be experienced by recipients of care. Projections of long-term care and state pension costs are provided up to 2030, by which time recipients of care would be benefiting in full from the long-term care reforms implemented in 2020. All analyses relate to older people and to England. Monetary amounts are expressed at constant 2015 prices. The models use a range of economic and demographic assumptions. Key to the analysis presented here are assumptions on real earnings growth and the triple lock. These are consistent with those produced by the Office for Budgetary Responsibility.\(^7\) Until 2020, growth in earnings and the triple lock are projected to be the same but from 2021, earnings are assumed to grow by 1.8% a year in excess of prices and the triple lock is assumed to average 2.1% a year above prices. The

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\(^7\) They do not incorporate the latest OBR projections published alongside the November 2016 Autumn Statement.
models produce projections under stated assumptions rather than forecasts. The simulation models and assumptions are described in full in our Technical Report.

a. **Uprating scenarios**

Five reform scenarios are compared with our base case (Box 3).

<table>
<thead>
<tr>
<th>Box 3: Base case projections</th>
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<tbody>
<tr>
<td>Our base case projections assume that:</td>
</tr>
<tr>
<td>• The state pension reforms are in place for those reaching State Pension age in 2016 and the new State Pension (nSP) and basic State Pension (bSP) are uprated by the triple lock indefinitely.</td>
</tr>
<tr>
<td>• State Second Pension/State Earnings Related Pension for those who reached State Pension age before April 2016 is uprated by prices.</td>
</tr>
<tr>
<td>• The current long-term care funding system continues indefinitely with most components uprated by prices (the NHS contribution to nursing care in nursing homes is linked to earnings).</td>
</tr>
</tbody>
</table>

All the scenarios replace the current long-term care system with the planned reforms from 2020 (Box 4). The Government previously indicated that under the reforms, the cap on care costs and the daily living costs would be linked to earnings, while other components of the system would continue to be uprated according to general price movements. This is what is assumed for Scenario 1.

The alternative scenarios have been selected to illustrate some possible routes to shifting some public spending from pensioners in general to pensioners with care needs and to demonstrate the effects that changing state pension uprating can have on long-term care costs.

Scenario 2 uprates the cap and daily living costs in line with prices as for other long-term care and disability benefits parameters. Uprating the cap and daily living costs by prices rather than earnings is more generous than linking them to earnings. The cap is reached sooner because it is lower than it would be if linked to earnings and because the part of care home costs that is treated as eligible care costs is higher. The part that remains means-tested after reaching the cap is smaller. The triple lock is applied to pensions in this scenario.

Scenario 3 links state pensions and long-term care and disability benefits parameters to earnings growth apart from the cap and allowance for daily living costs which as in Scenario 2 are price linked. Scenario 4 links state pensions to the Consumer Price Index (CPI), links most long-term care and disability benefits to earnings but as in Scenarios 2 and 3, the cap and daily living costs are price-linked. A low cost 5th Scenario links state pensions to CPI and uprates long-term care and disability benefits as in Scenario 1. Box 4 summarises the uprating scenarios.
b. **Aggregate costs of uprating scenarios**

Chart 5 summarises the effects of the alternative scenarios on public and private expenditure on long-term care for older people by 2030. Scenarios 1-4 all increase public expenditure and reduce private expenditure as compared with the base case. In Scenario 1, implementation of the long-term care reforms on the uprating basis announced by the Government would lead to additional public expenditure in 2030 of £1.3 billion at 2015 prices above continuation of the current system (the base case). Scenario 4 generates the highest projected public expenditure on long-term care at £23 billion compared with £19.6 billion under the base case. Under Scenario 4, public expenditure on long-term care in 2030 is projected to correspond to 1.01% of GDP compared with 0.86% under the base case. The growth between 2015 and 2030 in public spending on long-term care is projected to be around 80% under the base case (Chart 2) but would grow by 112% under Scenario 4. Projected public expenditure on long-term care under Scenario 5 is a little higher than under the base case despite the same assumptions on uprating of long-term care parameters. This is because the state pension is assumed to be linked only to prices under Scenario 5, leading to lower incomes of care users, a consequent reduction in what they pay towards their care, and an increase in what the state pays.

**Box 4: Uprating Scenarios**

Scenario 1:
- Long-term care reforms implemented in 2020
- nSP and bSP uprated by triple lock
- cap and daily living costs uprated by earnings
- other components of the long-term care and disability benefits systems are uprated by prices, except the NHS contribution to nursing costs in care homes is earnings linked.

Scenario 2:
- As Scenario 1 but
  - the cap and daily living costs are uprated by prices

Scenario 3:
- As Scenario 2 but
  - long-term care parameters and disability benefits are linked to earnings
  - nSP and bSP uprated by earnings

Scenario 4:
- As Scenario 3 but
  - nSP and bSP uprated by prices

Scenario 5:
- As Scenario 1 but
  - nSP and bSP uprated by prices
Chart 5: By 2030, the most generous long-term care uprating scenario increases public expenditure on long-term care for older people by £3.4 billion (17%) compared with the base case.

Notes: (1) Long-term care public expenditure includes NHS-funded care and disability benefits used to pay for care. Private expenditure includes payments from users from their other sources of income including their state pensions. (2) Scenarios are described in Box 4 on page 16.

Chart 6 compares the additional public spending (as against the base case) on older people’s long-term care under each scenario with the changes (again as against the base case) in spending on state pensions and means-tested benefits. The net effect of Scenarios 1 to 3 is to increase overall public spending across these three areas whereas Scenarios 4 and 5 decrease it considerably as a result of uprating state pensions by only prices. The net effect is shown by the line on the chart while the effect for each of the three areas is shown by the bars.

Chart 6: By 2030, the less generous pension uprating reduces public spending far more than the more generous uprating of long-term care increases it.

Notes: (1) Long-term care public expenditure includes NHS-funded care and disability benefits used to pay for care. Private expenditure includes payments from users from their other sources of income including their state pensions. (2) Scenarios are described in Box 4 on page 16.
c. Distribution of gains by income group from long-term care reforms under different uprating scenarios

The distributional effects of the scenarios are investigated by examining how average gains from the long-term care reforms vary across quintiles (fifths) of the income distribution for the relevant age group. These effects are shown for recipients of residential or home care aged 65 and over in 2030. Gains are calculated by comparing an individual’s net income, after meeting care costs, under each scenario with their net income under the base case.

All income groups gain from the long-term care reforms. Even people with low incomes can benefit from the introduction of the cap on care costs if they would otherwise be disqualified from help with residential care costs by their housing wealth – within the lowest income group around two-thirds are owner-occupiers.

Chart 7: Expressed in absolute terms (£s per week), gains from the long-term care reforms are largest for higher income care users but more generous uprating narrows the gap between the gains for those on high and low incomes

Users of residential care or home care aged 65+, 2030

Expressed in absolute (£s per week) terms, the gains from the planned long-term care reforms are largest for those on higher incomes as they stand to gain most from the introduction of the cap (Chart 7). A different picture emerges if gains are expressed as a percentage of income (Chart 8). These percentages vary less by income than the absolute amounts and, for Scenarios 2-4, are highest for the lowest income group. Although the absolute gains are smaller in the lower part of the income distribution, they represent larger proportions of income and so may be of considerable value to the recipients.

Gains are larger for Scenarios 2-4 than for Scenario 1. Their distributional effects are also different. For example, under Scenario 1, the average gain in the highest income group is 2.4 times that in the lowest income group (£43 compared with £18). This compares with
1.5% higher under Scenario 4. The scenarios which uprate long-term care parameters more generously are particularly beneficial for those on lower incomes.

Chart 8: Expressed as percentages of income, gains vary less by income and for two scenarios are highest for the lowest income group.

Users of residential or home care aged 65+, 2030

Note: Scenarios are explained in Box 4 on page 16
6. Long-term care funding for older people - a comparison between England, Wales and Scotland

The long-term care funding systems in Wales and Scotland differ from that in England, Scotland has a policy of ‘free personal care’. Wales’ system has a similar structure to England’s but is more generous in various ways (Box 5). To illustrate the effects of the differences between the systems, including both the current and planned reformed English system, we used vignettes who reached State Pension age in 2016. All would therefore retire under the reformed Great Britain-wide state pension system.

<table>
<thead>
<tr>
<th>Box 5: Long-term care funding in Scotland and Wales</th>
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<tbody>
<tr>
<td>• In Scotland, personal care at home is not charged for and there is a non means-tested subsidy for care in a care home of £171 per week in 2015 prices. Means tests apply for the rest of the care home fee and for ‘domestic’ help at home.</td>
</tr>
<tr>
<td>• Scotland has higher upper and lower capital thresholds than those currently in force in England.</td>
</tr>
<tr>
<td>• Wales has set the upper and lower capital thresholds to be the same so no tariff income is generated.</td>
</tr>
<tr>
<td>• Wales has a maximum weekly charge of £60 for home care and also uses a higher ‘buffer’ for assessing user charges for home care.</td>
</tr>
</tbody>
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The main findings from this comparison are:

• Compared with the current English system, a Scottish style system of ‘free personal care’, the Welsh system, and the reforms due to be implemented in England in 2020 are all more generous.

• The benefits of implementing these systems in England would go to people who are not eligible for state support with their care costs – or eligible for support with only part of those costs under the current English system.

• The benefits of a Scottish style free personal care system depend on the level of non means-tested state contribution to care home fees.

• The comparisons of the different funding systems depend on the length of time for which individuals need care – especially high intensity home care or residential care.

• The Welsh system, which has a maximum weekly charge for home care, can be more beneficial than the English reforms for people who need only home care.

• It is only for people who need care long enough to benefit from the cap on care costs that the English reforms produce savings in lifetime care costs similar to a Scottish-style system of free personal care.
7. **Regional variations within England: should the planned cap on liability to meet care costs be uniform across England?**

While the case for introducing a cap rests mainly on efficiency, the question of whether the cap should be uniform across the country or variable between regions or areas raises issues of equity.

The case for a lower cap in more deprived areas and a higher cap in more affluent areas is that:

- Differences in expectation of life with disability suggest that residents of more deprived areas may need care for longer periods toward the end of life.
- Differences in care home fees mean that people in more affluent areas reach the cap more rapidly than people in less affluent areas.
- Differences in older people's incomes and savings mean that people in more deprived areas will in general spend-down a higher proportion of their savings before reaching the cap than residents of more affluent areas.

The case for a single uniform cap across the country is that:

- A cap which varies by area would be complex to administer if people move area while receiving care.
- Uniformity across the country in the level of expenditure on care required to be met by the care user before reaching the cap may be regarded as more important than uniformity in duration of care before meeting the cap or in spend-down of savings.

The choice between a uniform cap across the country or a cap which varies by region or local area depends on which dimension of equity is considered more important.
8. **Summary and conclusions**

Our analysis has shown that the way in which the state pension and planned long-term care reforms evolve over time can make substantial differences to their effects.

**Public expenditure effects under current uprating policies**
- If the triple lock is applied indefinitely, we project that the reformed pension system will cost a similar proportion of gross domestic product (GDP) as the current system until the 2040s but its cost will then rise more slowly.
- If uprated by earnings, the new State Pension (nSP) will cost less than the previous system from about 2030. By 2060 the saving would be equivalent to about 1% of GDP.
- If the long-term care funding system is reformed according to previous government announcements, we project that public spending on long-term care for older people would reach 0.92% of GDP by 2030 compared with around 0.67% in 2015, and 0.86% in 2030 if the current funding system continued.

**Gainers and losers from reforms under current uprating policies**
- Gains in net income from the pension reforms are small at State Pension age but increase during retirement.
- Home-owners and people on higher incomes tend to gain most from both sets of reforms. Lower income renters can lose more in means-tested benefits than they gain in state pension income.
- People who had care needs in April 2016 are the most affected by the delay in implementation of the long-term care reforms. The cap would have helped to protect the savings of those on modest incomes who are funding their care from their savings.

**Alternative uprating scenarios**
More generous uprating scenarios for the reformed long-term care system, in combination with less generous uprating of the state pension system would focus resources for older people on those at risk of costly care in late old age.
- The more generous care uprating scenarios all increase public spending on long-term care by 2030, but, unlike the long-term care reforms themselves, they tend to favour those on lower incomes.
- By 2030, uprating the state pension by earnings rather than the triple lock would go some way to paying for the more generous long-term care uprating scenarios.
- Uprating pensions by prices – although not allowed under present legislation – would more than pay for more generous uprating of the care system.

**Comparisons between England, Scotland and Wales**
- The effects of differences in the long-term care funding systems in England, Scotland and Wales depends on the length of time for which individuals need care – especially high intensity home care or residential care.
- It is only for people who need care for long enough to benefit from the cap that the English reforms produce reductions in lifetime care costs similar to a Scottish-style system of free personal care.
- The Welsh system’s maximum weekly charge for home care can be more beneficial than the English reforms for people who need only home care.
Regional variations within England: should the planned cap on care costs be uniform across England?

The lower care home fees and lower wealth in more deprived areas raises the question of whether there is a case for the cap to be lower in more deprived areas and higher in more affluent areas. In particular, regional differences in care home fees mean that people in more affluent areas reach the cap more quickly than people in less affluent areas. It could however be argued that uniformity across the country in the level of expenditure on care required before reaching the cap is more important than uniformity in the duration of care before meeting the cap.
List of other project publications


## Appendix: Vignette descriptions

<table>
<thead>
<tr>
<th>Vignette</th>
<th>Description</th>
</tr>
</thead>
</table>
| Single male, low earner | Career: Retired aged 55 (early retirement due to ill health)  
Earning distribution: Low earner (30\textsuperscript{th} Percentile)  
Home:  
· Renter (£141 pw in 2016 prices, converted to 2015 prices)  
· Income linked council tax liability from ELSA  
Other financial wealth – Income linked from ELSA (£1,000 in 2016 prices) |
| Single female, low earner | Career: Career break aged 30 to 41, retirement aged 63  
Earning distribution: Low earner (30\textsuperscript{th} Percentile)  
Home:  
· Renter (£141 pw in 2016 prices, converted to 2015 prices)  
· Income linked council tax liability from ELSA  
Other financial wealth – Income linked from ELSA (£1,000 in 2016 prices) |
| Single male, median earner | Career: Retirement aged 65  
Earning distribution: Median  
Home:  
· Home owner (£300,000 in 2016 prices)  
· Income linked council tax liability from ELSA  
· Income linked house price  
Other financial wealth – Income linked from ELSA (£8,000 in 2016 prices) |
| Single female, median earner | Career: Retirement aged 63  
Earning distribution: Median  
Home:  
· Home owner (£300,000 in 2016 prices)  
· Income linked council tax liability from ELSA  
· Income linked house price  
Other financial wealth – Income linked from ELSA (£8,000 in 2016 prices) |
| Single male, high earner | Career: Retirement aged 65  
Earning distribution: High Earner (70\textsuperscript{th} Percentile)  
Home:  
· Home owner (£400,000 in 2016 prices)  
· Income linked council tax liability from ELSA  
· Income linked house price  
Other financial wealth – Income linked from ELSA (£40,000 in 2016 prices) |
| Single female, high earner | Career: Retirement aged 63  
Earning distribution: High Earner (70\textsuperscript{th} Percentile)  
Home:  
· Home owner (£400,000 in 2016 prices)  
· Income linked council tax liability from ELSA  
· Income linked house price  
Other financial wealth – Income linked from ELSA (£40,000 in 2016 prices) |
Figure A1: The projected pathway of gross care costs and Attendance Allowance (AA) assumed within the vignettes: cohort reaching State Pension age in 2016

Note: If eligible for state help with residential care costs, the care home fee is taken to be the LA rate (lower than the fee they would pay as self-funders) but payment of Attendance Allowance ceases.
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Editing decisions remain with the authors who take responsibility for any remaining errors or omissions.

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