






Calculating the costs of efficient care homes

New research by William Laing of health and community care analysts Laing & Buisson develops a formula published in 2002. This calculated reasonable fees, based on operating costs of efficient care homes for older people in England. Using evidence-based benchmarks, the new research finds:

-  Based on wage and land prices in a typical low-cost location, the study estimates fair fees for operating an efficient care home (meeting all national minimum standards for homes built after April 2002 as defined by the Department of Health). In the latter part of financial year 2003/04, these are: £497 per week for nursing care of older people and people with dementia; £375 per week for personal care of older people; and £399 per week for personal care of people with dementia. Taking account of the October 2004 increase in the National Minimum Wage, corresponding figures for 2004/05 rise to £520, £392 and £417 per week.
-  Costs, and thus fair fees, are higher in more affluent parts of England. For example, the estimated London figure for nursing care of older people and people with dementia is £620 per week (2003/04).
-  Assuming councils continue to 'spot' purchase services, the study proposes a target return on capital of 14% per annum. Under long-term block contracting, rates of return as low as 10% might give investors an incentive to develop and maintain capacity. However, the study concludes this rate of return is unlikely to stabilise the care home market as it is currently structured.
-  To avoid sub-standard homes being paid at the same rate as good quality homes, the study proposes a 'capital cost adjustment factor' proportional to the degree to which each home falls short of the Department of Health's national minimum standards. This would lead to a maximum difference between the upper and lower end of the range of £77 per week in 2003/04 and £80 per week in 2004/05.
-  On the evidence of this study, potentially, the public sector would have to find an additional £1 billion per annum to fund fair fees for a fully modernised care home sector.

Background

Despite recent increases in some areas, fees paid to care homes by most councils in England still offer inadequate returns to operators of care homes catering for older people dependent on state funding. This has led to a decline in care home capacity, destabilisation of local care markets and reduced choice.

Building on a report published in 2002, this study aimed to refine and develop guidance to enable care commissioners to identify the reasonable costs that a typical, *efficient* care home operator may expect to incur, using evidence-based benchmarks. The study specifically rejected an average cost approach on the grounds that average costs include the costs of *inefficient* operators.

The report guides users through the associated toolkit spreadsheet and offers advice on how benchmarks may be modified to reflect local market conditions.

Establishing care home costs

The four principal care home cost categories are: staffing; repairs and maintenance; other non-staffing current costs; and capital costs (including the investor's and operator's return). The toolkit spreadsheet generates costs (fair fees) which are summarised in Table 1.

Staffing

Staffing costs typically absorb 45-60% of care home fees. They include care staff, catering, cleaning and laundry staff and management, administration and reception staff. Costs for each component can be calculated by multiplying the volume of resources required (using benchmark data on the number of staff hours per resident) by weighted average hourly pay rates (taking account of enhancements for unsocial hours) plus on-costs such as employers' National

Insurance, holiday pay, sick pay and employers' pension contributions.

In the case of nursing care for older people and people with dementia, benchmarks of 7.5 qualified nurse hours and 19.5 carer hours per resident per week have been entered in the toolkit spreadsheet. For personal care, the corresponding benchmark is 16 carer hours per resident per week (no nursing staff) for older people and 20 hours per resident per week for people with dementia. These figures still reflect the pre-April 2002 staffing requirements applied by a multiplicity of inspection and registration units for larger scale care homes before implementation of the Care Standards Act. At the time of writing, the Department of Health had not yet issued new guidelines on minimum care staff input requirements.

The toolkit spreadsheet uses a norm of 6 hours of catering, cleaning and laundry staff time per resident per week; this does not vary between homes which offer nursing care and those that do not.

To determine local pay rates care commissioners ideally need to survey actual rates and enhancements paid by local care home providers, distinguishing between public and voluntary sector providers, whose pay rates are typically higher than average, and private sector providers, whose pay rates are typically lower than average. The study proposes that more 'efficient' private sector pay rates be used as benchmarks.

A cost allowance for (typically salaried) management, administration and reception staff is based on norms for a home of approximately 50 beds.

Staff on-costs include:

- Holiday pay under the Working Time Regulations. Full-time staff are entitled to 20 days holiday including bank holidays at full pay, equivalent to an on-cost of 8.3%. Part time staff have the same entitlement pro rata.

Table 1: Summary of costs (fair fees) calculated from the toolkit spreadsheet

	Nursing care		Personal care	
	Frail elderly and dementia £ per week	Frail elderly £ per week	Dementia £ per week	
	2003/04	2003/04	2003/04	
a) Low-cost provincial location				
Ceiling ^a	£497 ^c	£375 ^c	£399	
Floor ^b	£420	£298	£322	
b) London and environs				
Ceiling ^a	£620	£474	£503	
Floor ^b	£543	£397	£425	
	Projection 2004/05 ^d	Projection 2004/05 ^d	Projection 2004/05 ^d	
a) Low-cost provincial location				
Ceiling ^a	£520	£392	£417	
Floor ^b	£441	£312	£338	
b) London and environs				
Ceiling ^a	£642	£488	£519	
Floor ^b	£562	£409	£439	

a The upper end of the range (ceiling) represents a fair fee for homes meeting physical environment standards for 'new' homes first registered since April 2002, as defined in *National minimum standards for care homes for older people*, 3rd Edition February 2003 (Department of Health), and which also pass a locally agreed quality hurdle for other non-physical standards.

b The lower end of the range (floor) represents a fair fee for homes which do not exceed the interim physical environment standards for 'existing' homes as defined in *National minimum standards for care homes for older people*, 3rd Edition February 2003 (Department of Health).

c Corresponding national average 'ceiling' fair prices in 2001/02 were calculated at £459 for nursing care and £353 for residential care of frail older people in the 2002 report.

d Projections for 2004/5 were calculated by applying the inflation factors as set out in the toolkit spreadsheet, including 7.8% for low-paid care and domestic staff in the low-cost provincial location (in line with National Minimum Wage increases to be implemented in October 2004) compared with 5% for low-paid staff in London and its environs.

Table 2: Fair fees for nursing care in financial year 2003/04

	Nursing care for older people or people with dementia		Residential care for older people		Residential care for people with dementia	
	£ per week		£ per week		£ per week	
	a) Low-cost provincial location	b) Outer London and environs	a) Low-cost provincial location	b) Outer London and environs	a) Low-cost provincial location	b) Outer London and environs
Cost heads						
A) STAFF, INCLUDING ON-COSTS						
Qualified nurse staff	97	117	0	0	0	0
Care staff	113	136	93	112	116	139
Domestic staff	36	43	36	43	36	43
Management / admin. staff	31	37	31	37	31	37
Agency staff allowance – nurses	2	3	0	0	0	0
Agency staff allowance – carers	2	2	1	2	2	2
Training ‘backfill’ (cover for staff on training)	3	4	2	2	2	2
Total staff	£284	£341	£162	£195	£186	£223
B) REPAIRS AND MAINTENANCE						
Maintenance capital expenditure	13	13	13	13	13	13
Repairs and maintenance (revenue)	6	6	6	6	6	6
Contract maintenance of equipment	2	2	2	2	2	2
Total repairs and maintenance	£21	£21	£21	£21	£21	£21
C) NON-STAFF CURRENT COSTS						
Food	17	17	17	17	17	17
Utilities	12	12	12	12	12	12
Handyman / gardening (on contract)	6	6	6	6	6	6
Insurance	4	4	4	4	4	4
Medical supplies (inc. equipment rental)	3	3	3	3	3	3
Registration fees (inc. Criminal Records Bureau checks)	2	2	2	2	2	2
Recruitment	2	2	2	2	2	2
Direct training expenses	2	2	2	2	2	2
Incontinence products	0	0	0	0	0	0
Other non-staff current expenses	7	7	7	7	7	7
Total non-staff current expenses	£55	£55	£55	£55	55	55
C) CAPITAL COSTS						
Land	33	99	33	99	33	99
Buildings and equipment meeting national minimum physical standards for ‘new’ homes first registered since April 2002	103	103	103	103	103	103
Total capital costs	£136	£203	£136	£203	£136	£203
Fair price for homes meeting all standards for ‘new’ homes in National minimum standards for care homes for older people, 3rd Edition February 2003 (DH)	£497	£620	£375	£474	£399	£503
Maximum capital cost adjustment factor for homes not meeting physical standards for ‘new’ homes	-£77	-£77	-£77	-£77	-£77	-£77
Fair price for homes which do not exceed the interim physical standards for ‘existing’ homes in National minimum standards for care homes for older people, 3rd Edition February 2003 (DH)	£420	£543	£298	£397	£322	£425

Note: Figures may not add because of rounding

- Employers' National Insurance (NI) contributions amount to 12.8% of gross pay above the (NI) threshold. Because many care home employees work part-time, the average NI paid by employers is lower. Based on group operator norms, NI on-cost benchmarks of 9% for nurses and 8% for carers and catering, cleaning and domestic staff have been adopted.
- A sick pay on-cost of 2% is assumed, based on private sector group operator norms. Nearly all private sector care home operators pay no more than Statutory Sick Pay (SSP) to hourly paid nursing, care assistant and domestic staff. Voluntary sector operators and private sector operators subject to TUPE (which protects employment rights) frequently have more generous sick pay arrangements.
- Based on almost universal private sector practice, zero has been adopted as the benchmark for the employer's pension contribution on-cost for hourly paid care and domestic staff.
- An allowance is, however, made for employers' pension contributions for management and administrative staff, which increases their aggregate on-cost to 30% in the toolkit spreadsheet.

Non-staffing current costs and maintenance

This category includes costs such as utilities, provisions, registration fees, grounds maintenance and maintenance capital expenditure (the latter in place of depreciation). Typically, they absorb 10-15% of care home fees. They can be calculated fairly readily on a 'per resident' basis, with relatively little regional variation. In the study, benchmark data from major care home operators have been used.

Capital costs

Capital costs, including the investor's and operator's return, account for the balance of care home fees. The study emphasises the importance of using a simple formula which can be applied regardless of the capital structure of any home. To do otherwise would lead to a hopelessly complex requirement for commissioners to understand and allow for the intricacies of different capital funding structures.

Assuming most homes continue to 'spot' purchase services, the study proposes a target return on capital of 14% per annum. Under long-term block contracting, rates of return as low as 10% might be sufficient to give investors an incentive to develop and maintain capacity. However, the study concludes that a rate of return at this level is unlikely to stabilise the care home market as it is currently structured.

Summary of care home costs

Table 2 summarises the estimated reasonable costs incurred by efficient providers of nursing care for older people or people with dementia in 2003/04. Projected costs for 2004/05 are provided in the toolkit spreadsheet.

Capital cost adjustment factor

Paying physically sub-standard homes at the same rate as physically good quality homes would risk generating super-profits for sub-standard homes. To avoid this, the study proposes that councils apply a capital cost *adjustment factor*: fees payable to each individual home would reflect the degree to which that home meets or falls short of the upper end of the range of physical standards for which the council is willing to pay. The study also proposes that homes of a physically high standard should also surmount a quality hurdle relating to non-physical standards in order to qualify for payment at the upper end of the fee range.

A framework for calculating capital cost adjustments for individual homes is described in the main report. On the assumptions used in the toolkit spreadsheet, the maximum capital cost adjustment factor (i.e. the maximum differential between 'floor' and 'ceiling' fees) would be £77 per resident per week.

Affordability of reasonable fees

The potential additional cost to the public sector of an England-wide commitment to pay a fair price for a fully modernised care home sector is estimated at approximately £1 billion per annum at 2003/04 prices and volumes of demand.

About the project

Much of the benchmark data entered in the toolkit spreadsheet was based on discussions with chief executives and finance directors of leading companies representing a significant proportion of the care home sector in England during the latter part of 2003. Other benchmark information, including pay rates in low cost areas, was derived from surveys of large and small care homes carried out by Laing & Buisson in the north of England in financial year 2003/04.

How to get further information

Further information may be obtained from the author William Laing, Laing & Buisson, 29 Angel Gate, City Road, London EC1V 2PT. Tel: 020 7833 9123; email william@laingbuisson.co.uk.

The full report, **Calculating a fair price for care: A toolkit for residential and nursing care costs** by William Laing, is published for the Foundation by The Policy Press (ISBN 1 86134 617 4, price £11.95). An electronic version of the report (using Word and Excel) with links to its accompanying datasheet is available free of charge from.