SECOND EDITION

Calculating a fair price for care

A toolkit for residential and nursing care costs

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The POLICY PRESS

First published in Great Britain in May 2004 by

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Published for the Joseph Rowntree Foundation by The Policy Press

ISBN 1 86134 617 4

British Library Cataloguing in Publication Data
A catalogue record for this report is available from the British Library.

Library of Congress Cataloging-in-Publication Data
A catalog record for this report has been requested.

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The **Joseph Rowntree Foundation** has supported this project as part of its programme of research and innovative development projects, which it hopes will be of value to policy makers, practitioners and service users. The facts presented and views expressed in this report are, however, those of the author and not necessarily those of the Foundation.

Cover design by Qube Design Associates, Bristol
Printed in Great Britain by Hobbs the Printers Ltd, Southampton

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Preface

The text of this report has been structured not only to explain the issues under discussion, but also to offer guidance notes for users wishing to enter local data in the associated toolkit spreadsheet (www.policypress.org.uk/carecost.htm) in order to estimate fair fees for any given locality. Users of the printed report should inspect all highlighted (shaded and boxed) paragraphs. Users of the electronic report may use the hyperlinks to move directly to the relevant cells in the toolkit spreadsheet.

In order to make use of this facility, the Word and Excel files should be placed in the same folder on a PC running a Windows operating system. All of the parameters set in the toolkit spreadsheet may be varied, if desired, to test the effect on calculated fee levels. It is recommended that users save the original before making such modifications. Note that the hyperlinks will no longer work if either of the file names is changed.

Summary

Scope

This report is limited to care home services for older people and people with dementia in England. A similar approach would be equally valid in Wales, Scotland and Northern Ireland, although some costs would differ because of regulatory variances.

Until April 2002, care homes in England were divided under the 1984 Registered Homes Act into 'nursing homes' offering nursing care and 'residential homes' offering residential care. This statutory distinction has disappeared under the 2000 Care Standards Act and all such establishments are now referred to as 'care homes'. Nevertheless, there remains a regulatory distinction between:

- *care homes with nursing*, which may offer either 'nursing care' or 'personal care', and must employ an appropriate level of qualified nursing staff; and
- *care homes only*, which may offer 'personal care' only and do not need to employ qualified nursing staff.

In line with these changes, this report uses the term 'personal care' to refer to what used to be called 'residential care'. Because of the qualified nursing staff input, nursing care is more costly than personal care, other things being equal.

Objective

The principal objective of this report is to provide commissioners of care services, care home operators and others with an interest in the care sector with a transparent and robust means of calculating the reasonable operating costs of efficient care homes for older people and people with dementia in any given locality, and thus determining fee levels necessary to sustain delivery of adequate care services by independent sector providers, now and in the future.

Modification of the 2002 *Calculating a fair price for care* report

This report updates and revises an earlier report published by The Policy Press for the Joseph Rowntree Foundation in June 2002, *Calculating a fair price for care: A toolkit for residential and nursing care costs* (Laing, 2002). Although only two years old, a revision of the original report was considered necessary because of two material changes that have taken place since:

- a significant change in market indicators of the rate of return on capital that is being sought by investors in care homes, from an estimated 16% per annum in 2002 to 14% in 2004;
- changes in costs related to regulatory requirements under the 2000 Care Standards Act implemented in April 2002.

The opportunity has been taken, in this new report, to introduce two further modifications. First, two types of location (provincial and London) are illustrated in Table 1 (on page vii), in order to reinforce the point that 'fair fees' can be expected to vary locality by locality. This is an important point since the single, national average illustration presented in the 2002 report was frequently taken out of context and misquoted as if it applied to all locations.

Second, this revised report calculates both a 'ceiling' and a 'floor' fair fee illustration for each client type in each type of location. The 'ceiling' represents a fair fee for homes which meet physical environment standards for 'new' homes first registered since April 2002, as defined in the *National minimum standards for care homes for older people* (3rd edn, February 2003), and which also pass a locally agreed quality hurdle for other non-physical standards. The 'floor' represents a fair fee for homes that do not exceed the interim physical environment standards for 'existing' homes as defined in the same publication. The 2002 report, in contrast, had calculated fair fees on the equivalent of a 'ceiling' basis only.

Is investment in new care home stock needed?

Investment in new care home stock catering for state-funded clients has virtually ceased in recent years, other than for specific replacement projects (Laing & Buisson, 2003). The recommendations on fee levels contained within this report are based on the premise that a substantial amount of investment in new care home stock will be required to replace stock lost through closures and to meet future demand. It should be noted, however, that there is a contrary view – that the traditional care home sector will continue to contract and that the demand for new facilities in the future will be focused on new models such as 'extra care'. The 'extra care' model of delivering home care services typically to tenants/owners of clustered independent living units is certainly attractive. The issue, however, is whether it can realistically substitute for such a large proportion of traditional care home services as to render further development of care homes unnecessary. Laing & Buisson's view is that this is unlikely, bearing in mind (a) the level of dependency of care home residents now; (b) questions over some home care users' quality of life; and (c) the scale of increase in care services overall required to meet the demands of an ageing population. On this latter point, calculations based on the most recent UK population projections from the Government Actuary show that, if age-specific rates of usage per unit population were to remain as they are now, there would be 1,250,000 older people living in care homes or long-stay hospitals in the UK by the time the older population peaks in 2056, compared with 460,000 in 2003 (Figure 2, page 4). Even with a substantial transfer of demand away from traditional care homes and towards home care and extra care alternatives, therefore, it seems unlikely that further investment in traditional care homes can be avoided.

Care home costs and fair fees

There are four main components of care home costs:

- staffing
- repairs and maintenance
- other non-staff current costs and
- capital costs.

These costs are calculated in the associated toolkit spreadsheet. Because capital costs are assessed to incorporate a reasonable return for investors – including profit – 'fair fees' are identical to the sum of 'reasonable costs'.

Table 1 summarises results from the toolkit spreadsheet calculations when applied to two illustrative types of locality:

a) a low-cost provincial location where care assistant and domestic staff pay rates are close to the National Minimum Wage and where land prices are relatively low;
b) a typical outer London borough or inner home counties location where pay rates are typically about 20% higher than in low-cost provincial locations and land prices may be about three times as high.

The figures in Table 1 represent the gross fee levels, including any Registered Nursing Care Contribution (RNCC) that councils and their NHS partners in each of the two illustrative locality types should aim to pay efficient homes in order to stabilise the market and to ensure an adequate supply of care home places for state-funded clients now and in the future.

In order to establish valid fair fee rates in any *specific* locality, it is essential to enter local data on pay rates and land prices, and to vary any other of the model's parameters if local benchmarks differ from national ones. It may also be necessary to calculate more than one set of fair fee rates within a given social services

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

	Nursing care	Personal care	
	Older people with dementia £ per week 2003/04	Older people £ per week 2003/04	People with dementia £ per week 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	426
	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

Notes: [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 the *National minimum standards for care homes for older people* (3rd edn, February 2003), 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 the *National minimum standards for care homes for older people* (3rd edn, February 2003).

[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 (Laing, 2002).

[d] Projections for 2004/05 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.

authority. Large counties such as Cambridgeshire and Kent, for example, exhibit wide inter-district disparities in pay rates and land values.

The illustrative fair fees in Table 1 are based on costs for homes, which are efficiently configured with regard to staffing. Broadly, they represent the lowest level of cost consistent with meeting minimum staffing levels required by regulators. In practice, 'efficiently configured' means large enough to exploit staffing economies of scale, typically 30 places or more. No allowance has been made for higher costs of smaller-scale homes. The rationale is that Laing & Buisson is aware of no clear evidence that small-scale homes deliver an inherently higher quality for older people or people with dementia. On this premise, there is no case for councils to pay higher prices for small-scale homes – unless specifically justified by some other over-riding factor.

No specific allowance is made in the toolkit spreadsheet for the cost of staff turnover. Many operators argue, however, that staff turnover is unusually elevated in the care home sector because of low pay and minimal employee benefits resulting from the financial stresses to which care homes are subject. The gap in pay and conditions between care homes and other sectors for similarly skilled jobs is likely to remain a potent factor leading to staff turnover in the future, until such time as it becomes affordable for care homes to equalise pay and conditions.

Capital cost adjustment factor

Councils and their NHS partners should not pay physically sub-standard homes at the same rate as for physically good quality homes. If they were to do so, they would find themselves paying fees to sub-standard care homes at a level

that would generate super-profits for them. This is the reason for proposing a range (ceiling and floor) for fair fees for each of the location/client types in Table 1.

The proposal is that councils should apply a *capital cost adjustment factor* such that 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. In addition, in order to avoid paying high fees to homes that provide poor care, it is recommended 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.

What is the upper end of the range of physical standards for which councils should be willing to pay? Ultimately, that is a matter for each democratically elected council. However, there must be a strong presumption that councils, which receive most of their funding from central government, should be prepared to pay a fee which fairly reflects the build/equip costs of any home in their locality which meets the physical environment standards for 'new' homes first registered since April 2002, as defined by the government in the *National minimum standards for care homes for older people* (3rd edn, February 2003). In practice, this means the build/equip costs of a new-build home, estimated at £38,900 per occupied place in the toolkit spreadsheet.

Build/equip costs for a home at the lower end of the acceptable physical quality range are more difficult to derive. Conceptually, they should reflect the current value of the historic bricks and mortar costs of providing capacity (usually by conversion) in homes which do not exceed the interim physical environment standards for 'existing' homes as defined in the *National minimum standards for care homes for older people* (3rd edn, February 2003). These are referred to as 'interim' because they result from a government decision to amend the more demanding physical standards initially introduced in April 2002, for fear of a catastrophic loss of capacity. These amended standards will be subject to further review. For the present, a 'floor' build/equip cost of £9,700 per occupied place is estimated in the toolkit spreadsheet (see 'Capital cost adjustment factor', page 22).

A framework for calculating capital cost adjustments for individual homes is described in 'Capital cost adjustment factor', page 22. It should be noted that *capital cost adjustment factor* could equally be called a 'discount' to be deducted from the upper end of the fair fee range, or a 'premium', and added to the lower end of the fair fee range. The choice of which term to use is presentational. The substance is the same in the fair price model.

The fleshing out of the capital cost adjustment framework in each council area will necessitate decisions on:

- exactly which standards or quality measures are to be used; and
- what weighting should be attributed to each.

This should be a matter for each individual council to decide, in association with local stakeholders.

There will be a cost associated with continuing monitoring of individual homes' compliance with agreed quality standards and ensuring that the process continues to have the confidence of stakeholders. Such 'transaction' costs, although significant, should not be disproportionate in view of the substantial sums of money being spent by councils on care services and the importance of ensuring that the market operates effectively.

The proposed *capital cost adjustment factors* will be important in mitigating the cost consequences of any fair fee policy adopted by councils. On the assumptions used in the toolkit spreadsheet, councils would be justified in paying physically sub-standard homes up to £77 per resident per week less than those meeting national minimum standards for 'new' homes.

Three approaches to making the framework operational are discussed:

- based on compliance of each of the 38 *National minimum standards for care homes for older people*, as evidenced by the latest Commission for Social Care and Inspection (CSCI) report;
- based on quality ratings assessed by an independent third party; and
- development of an in-house methodology for measuring quality.

Each of the options has advantages and disadvantages, which relate to cost, confidence and practicality. Each, however, is equally capable of giving rise to a simple banding system, and each is equally amenable to containment within a budget in a transitional phase, achievable by selection of appropriate triggers and scales for fee increments. Ideally it would be desirable to use CSCI inspection reports, since the regulatory process offers a substantial existing resource that it would be wasteful to duplicate.

Gap between fair fees and fees currently paid by councils

The first 'fair price' report published in 2002 found that in 2001/02 there were substantial gaps in most English localities between fair fee rates and the weekly fees paid by social services (Laing, 2002).

Since then, many local authorities facing capacity shortages have increased their fees by amounts in excess of ordinary inflation and a handful have increased their fees by substantial amounts. Despite the progress that is being made, there were still substantial gaps between fair fee rates and the weekly fees paid by social services in 2003/04.

In brief, the majority of local authorities are willing to pay fees which are close to the rate appropriate for care homes which have not invested in physical amenities over and above the interim minimum for 'existing' homes, incorporated in the revised *National minimum standards for care homes for older people* published in February 2003. But no local authority in England has yet set a baseline fee rate at a level appropriate for care homes which have invested in the more demanding physical standards set for 'new' homes first registered since April 2002. Across England as a whole, the average gap between actual fees paid by local authorities and the fair fee for 'new' homes is calculated at £127 per week for nursing care and £83 per week for personal care of older people.

What would a fully modernised care home sector cost?

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 can be approximated by comparing the England ceiling rates (that is, the fair fees calculated for 'new' homes) with the average gross fees paid by English local authorities. The additional cost to the public sector is estimated at approximately £1 billion per annum at 2003/04 prices and volumes of demand. The beneficiaries of this additional expenditure would be:

- care homes, whose profitability would be raised to reasonable levels;
- state-funded residents, who would have access to fully modernised facilities;
- charities and the relatives and friends of state-funded care home residents, who would no longer need to make third-party top-ups to inadequate local authority fees; and
- privately funded residents who would no longer be asked to cross-subsidise local authority-funded residents.

Future changes in care home costs

It is proposed that each broad cost heading in the toolkit spreadsheet should have a specific inflation factor. These are described in Chapter 4.

There are, however, health warnings. The toolkit spreadsheet should not be over-reliant on inflation factors and benchmarks should be re-examined afresh at intervals to ensure that the toolkit spreadsheet does not diverge from reality.

1

Introduction

Scope

This report is limited to care home services for older people and people with dementia in England. A very similar approach would be equally valid in Wales, Scotland and Northern Ireland, although some costs would differ because of regulatory variances.

Until April 2002, care homes in England were divided under the 1984 Registered Homes Act into 'nursing homes' offering nursing care and 'residential homes' offering residential care. This statutory distinction has disappeared under the 2000 Care Standards Act and all such establishments are now referred to as 'care homes'. Nevertheless, there remains a regulatory distinction between:

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Modification of the 2002 *Calculating a fair price for care* report

The report updates and revises an earlier report published by The Policy Press for the Joseph Rowntree Foundation in June 2002, *Calculating a fair price for care: A toolkit for residential and nursing care costs* (Laing, 2002). Since publication, the original toolkit and report have been widely used by both local authorities and care home providers as a basis for establishing the actual cost of care home provision. Laing & Buisson has itself been commissioned by several English councils to assist in reviewing the reasonableness of baseline fee levels paid to local care home providers. Usually, these projects have been carried out with the cooperation of local provider associations. This has given Laing & Buisson an opportunity to develop and refine the approach and methodology set out in this revised report, and to address the practical issues which have arisen.

Although only two years old, a revision of the original report was considered necessary because of two material changes that have taken place since:

- a significant change in market indicators of the rate of return on capital that is being sought by investors in care homes, from an estimated 16% per annum in 2002 to 14% in 2004;
- changes in costs related to regulatory requirements under the 2000 Care Standards Act implemented in April 2002.

The opportunity has been taken, in this new report, to address in more detail some key issues which were only briefly touched on in the original report – in particular the question of how to ensure that providers of 'sub-standard' homes do not generate super-profits from increases in state-funded fee levels designed to attract investment in high quality facilities and services.

The opportunity has also been taken to present the report as an electronic text document with hyperlinks to the associated toolkit spreadsheet (www.policypress.org.uk/carecost.htm), in order to facilitate navigation to and from the text of the report and the spreadsheet.

Background: threats to market stability

Fees paid by many social services departments throughout the UK are still inadequate to offer reasonable returns to independent sector providers of care homes for older people and people with dementia dependent on state funding. This remains true despite the sometimes substantial increases in fee rates implemented by a minority of local authorities over the last two to three years. At the time of writing in February 2004, many other authorities were actively reviewing their fee rates for the financial year 2004/05 – often with the aid of the 2002 Joseph Rowntree fair price model – and several had agreed in principle with their local providers to move towards fair fee rates over a number of years, recognising that the financial strains of immediate implementation would be too great. But a large number of local authorities continue to maintain fee rates at levels that undermine the stability of their care home markets.

Inadequate fee levels for state-funded clients have been a major factor in the recent years' decline in care home capacity. As well as threatening the stability of local care markets, this has led to reduced local choice for care users, as self-payers (and quasi self-payers with access to top-up funding from families or friends) crowd out wholly state-funded clients and as placements have to be sought out of the local area. This is not just a matter of concern for organisations providing care services. It is a matter of public concern because, for better or for worse, the delivery of residential and nursing care in the UK was largely privatised during the 1980s and early 1990s. Reversing that process is not a realistic option and the UK will remain reliant on private sector provision for the foreseeable future. Care home capacity shortages may also have a knock-on effect on the NHS in the form of 'bed-blocking' – where older people no longer need to occupy a high-cost NHS hospital bed, but cannot be discharged for a variety of reasons, including non-availability of suitable care home places. Delayed discharges in turn may threaten the ability of the NHS to deliver on its ambitious programme of reform to modernise the NHS. It is, therefore, very much in the interests of government, local authorities and the NHS to find a way of promoting a stable and competitive care sector. *Building capacity and partnership in care*, published by the Department of Health in October 2001, acknowledges the problem as follows:

> Providers have become increasingly concerned that some commissioners have used their dominant position to drive down or hold down fees to a level that recognises neither the costs to providers nor the inevitable reduction in the quality of service provision that follows. This is short-sighted and may put individuals at risk. It is in conflict with the Government's Best Value policy. And it can destabilise the system, causing unplanned exits from the market. (DoH, 2001, para 6.2)

The care home sector switched from expansion to contraction mode in the late 1990s. Independent sector capacity peaked at an estimated 457,600 places in April 1997, and by April 2003, had dropped to 418,000, representing a loss of 39,600 places, or 9% of capacity. The main cause has been the closure of small- to medium-sized homes in converted properties, whose owners have taken advantage of elevated residential property values to exit a market in which they were receiving poor returns. Public sector provision has at the same time been declining at a faster rate, although for different reasons. Taking all sectors together, overall capacity peaked at 575,600 places in April 1996, and dropped to 501,900 by April 2001, representing a loss of 73,700 places, or 13% of capacity. All of these figures relate to care establishments for older people, people with dementia and physically disabled people (Laing & Buisson, 2003). Figure 1 shows national trends in demand for and supply of care home places for these client groups, illustrating the reduction in spare capacity in the last seven years.

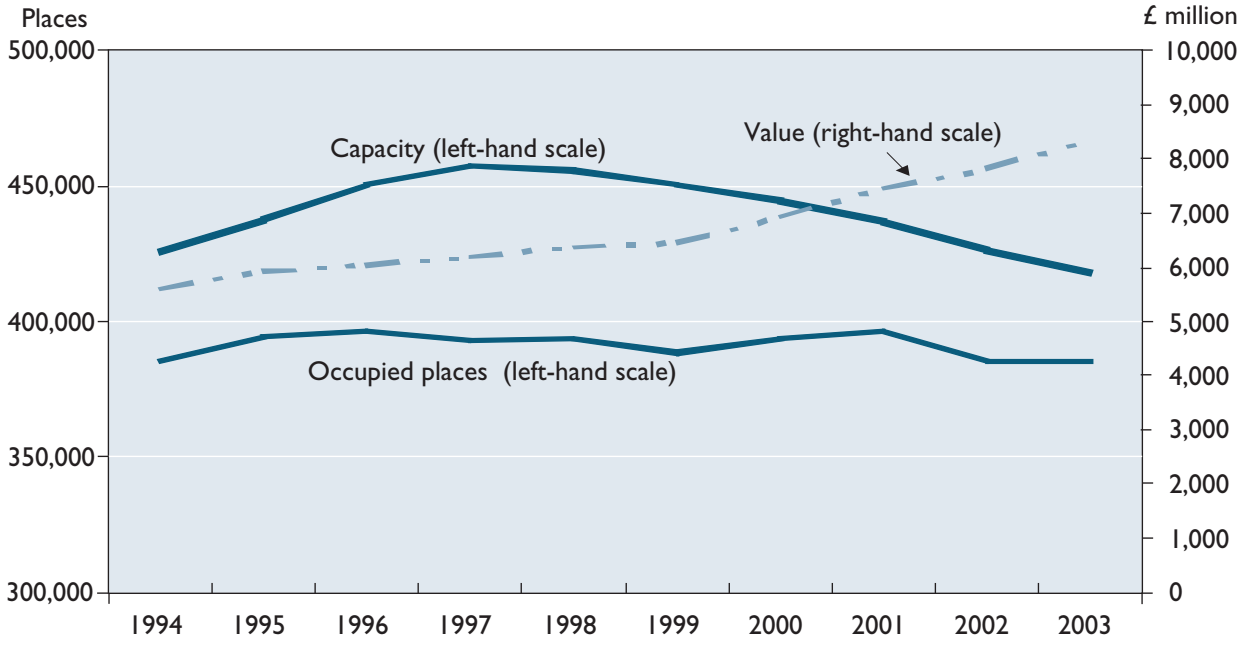
For several reasons, a decline in care home capacity was to be expected, and indeed broadly welcomed. Following the 1993 community care reforms, when local authorities took over

responsibility for most new, state-funded care home placements and for the first time introduced assessment of need, local care commissioners consciously opted to provide home care services for their clients, where practicable, rather than make care home placements. The consequent diminution in overall demand for care home services has meant that less capacity overall is needed. Moreover, there was – and still is – overcapacity in the care home sector in many locations.

However, the process of contraction has been haphazard, rather than planned, leading to a growing number of 'hotspots' where capacity loss has overshot the limited realignment of demand and supply that was ideally required. In these hotspots, care homes are typically running to full capacity. They are in a position to wait for private payers to fill any vacancies at premium rates and this has led local authorities to experience severe problems in making local care home placements, particularly for nursing care and care of older mentally ill people. Hotspots were initially concentrated in the affluent South of England, where land and wage costs are high and there is a strong private pay market. By the beginning of 2004, however, capacity shortages had also emerged in several less affluent areas.

A matter of particular concern is the virtual cessation of investment in new care home stock catering for state-funded clients (Laing & Buisson, 2003), which will be required to replace those homes which have closed or which will close in the near future. The recommendations on fee levels contained within this report are based on the premise that a substantial amount of investment in new care home stock will be required to meet future demand. It should be noted, however, that there is a contrary view – that the traditional care home sector will continue to contract and that the demand for new facilities in the future will be focused on new models such as 'extra care'. The 'extra care' model of delivering home care services typically to tenants/owners of clustered independent living units is certainly attractive. The issue is, however, whether it can realistically substitute for such a large proportion of traditional care home services as to render further development of care homes unnecessary. Laing & Buisson's view is that this is unlikely, bearing in mind (a) the level of dependency of care home residents now; (b) questions over some home care users' quality of life; and (c) the scale of increase in care services overall required to meet the demands of an ageing population. On this latter point, calculations based on the most recent UK population projections from the Government

Figure 1: Capacity and volume of demand, places in residential settings for older people, people with dementia and physically disabled people, independent sector, local authority and NHS providers combined, UK



Source: Laing & Buisson (2003)

Actuary show that, if age-specific rates of usage per unit population were to remain as they are now, there would be 1,250,000 older people living in care homes or long-stay hospitals in the UK by the time the older population peaks in 2056, compared with 460,000 in 2003 (Figure 2). Even with a substantial transfer of demand away from traditional care homes and towards home care and extra care alternatives, therefore, it seems unlikely that further investment in traditional care homes can be avoided.

Objective

The principal aim of this report is to provide commissioners of care services, and others with an interest in the care sector, with a transparent and robust means of calculating the reasonable operating costs of efficient care homes for older people and people with dementia in any given locality, and thus determining fee levels necessary to sustain delivery of adequate care services by independent sector providers, now and in the future.

It is hoped this will act as a guide to commissioners revising baseline fee rates or negotiating them with local providers.

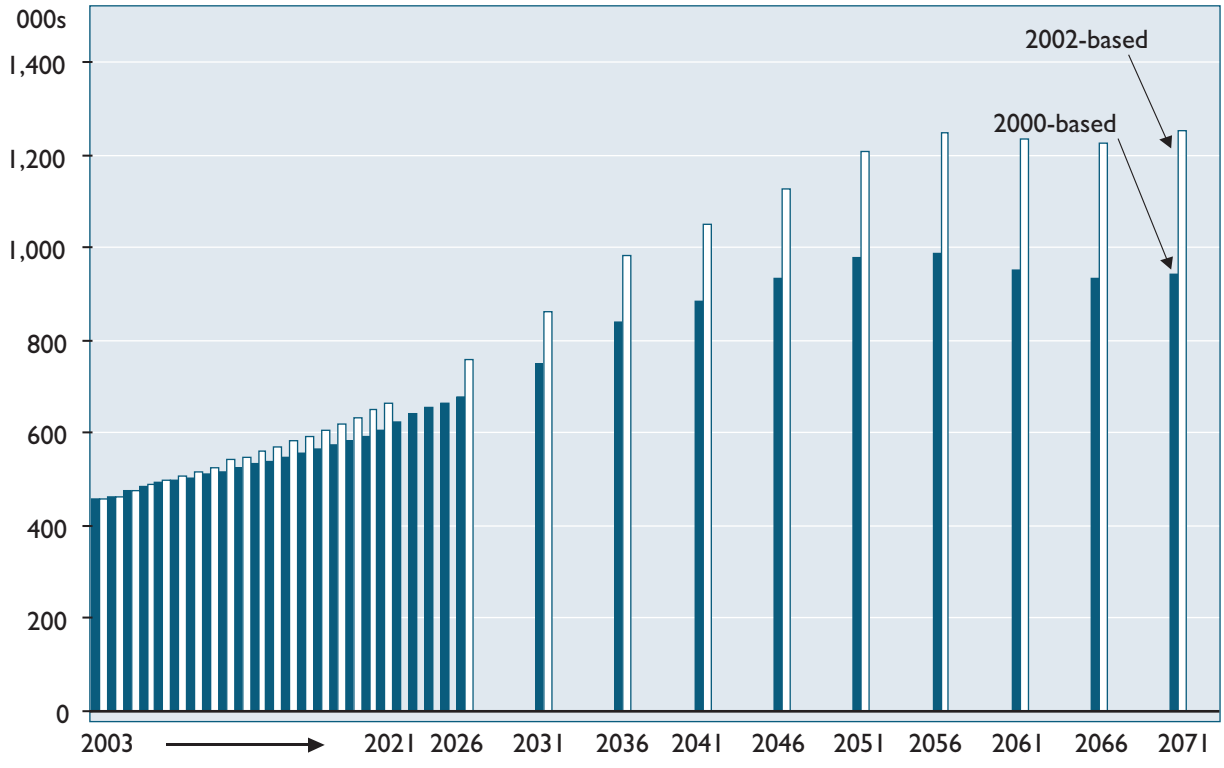
Alongside this report, a toolkit spreadsheet has been prepared, which will allow commissioners and others to enter locally variable components of care home costs, such as pay rates and land prices, so that total costs can be calculated which fairly reflect local market conditions.

Why calculate fees from a cost model using local data?

It is implicit in the aims described above, that:

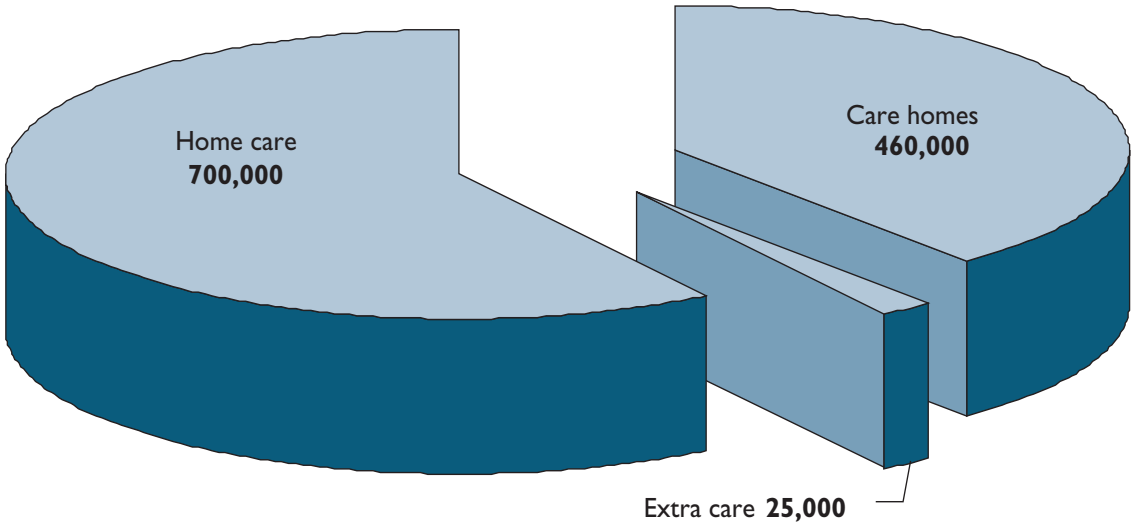
- calculating fee rates from a cost model – rather than tendering or some other negotiating process – is the most practical way of determining fair levels of remuneration for care homes catering for state-funded clients; and
- costs and fee rates should be calculated *locally* rather than nationally.

Figure 2: Projected[a] numbers of older and physically disabled people living in residential settings, UK (2003–71, all sectors)



Note: [a] Based on applying the 2003 risk of living in a residential setting (Laing & Buisson, 2003) to Government Actuary Department principal projections.

Figure 3: Distribution of formal care services for older people, people with dementia and physically disabled people receiving care, UK (2003)



Limitations of tendering

Tendering processes are well established in local government procurement, which has been the subject of a recent review by Sir Ian Byatt (2001). So why not use a tendering process to establish care home fee levels which are acceptable to both care commissioners and each successful tenderer, rather than seeking to establish a set of baseline fee rates applicable to all local care home providers?

When the community care reforms were implemented in 1993, many local authorities did indeed undertake tendering exercises with local care home providers. In practice, however, the dominant mode of commissioning care home places in most local authorities has become 'spot' purchase under standard terms and conditions at specified 'baseline' fee levels, which may vary within different areas within a large authority's boundaries, and which are typically revised by the local authority at the start of each financial year.

'Spot' purchase remains dominant despite moves among some local authorities towards block contracting, particularly of nursing care places. The dominance of spot purchasing at baseline fee rates is a consequence of certain features of the care market:

- Most important is the choice directive, enshrined in the 1992 National Assistance Act (Choice of Accommodation) Directions. This requires local authorities to allow individuals entering care homes under a local authority contract to go into a care home of their choice, and have their fees topped up by a third party, without unreasonable hindrance by the local authority – provided, among other things, that the individual's choice does not cost the local authority more than it would usually pay for someone with the individual's assessed need. The wording of the choice directive implies that each local authority must have a set of 'baseline' fees, representing what it will usually pay.
- Moreover, client choice limits the opportunities for local authorities to negotiate block contracts that can purport to guarantee a flow of placements to successful tendering parties. In several reports, the Audit Commission has recommended more widespread use of block contracts for care home services. In some cases this could be achieved without infringing the directive on choice by local authorities block contracting with the most popular homes, where they can be confident there will always be an excess of individual demand over places available. But it would be difficult to envisage such block contracts for all, or even the majority, of homes in which a local authority may wish to make placements.
- Another factor militating against use of tendering is the large number of providers that must be successful. Local authorities now pay for over 60% of care home residents nationally. In order to give themselves access

to sufficient capacity, therefore, local authorities typically need to have purchasing arrangements in place with the bulk of care homes operating within their localities. In larger social services authorities, this amounts to several hundred homes. Properly managed tendering processes would have high transaction costs. Moreover, it would be difficult to sustain a genuinely competitive process when there are many legitimate ways in which local care homes could act in concert.

For these reasons, it is likely that 'spot' purchase using baseline fee rates will remain the dominant mode of care home commissioning in the future. Even where the tender route is chosen, care commissioners would still find it useful to have robust information on care home cost structures.

There is a further problem with tendering which relates to the current structure of the market for care services. First, the market is 'imperfect', in the sense that most local authority purchasers occupy a dominant position vis-à-vis providers. Second, the physical environment of most care homes is 'sub-standard' in the sense that they fall short of the physical environment standards for 'new' homes first registered since April 2002, as defined in the *National minimum standards for care homes for older people* (3rd edn, February 2003). Most also fall short of the less demanding physical environment standards set by the *National minimum standards* for existing homes when the Care Standards Act was implemented in April 2002 – which the government shortly afterwards downgraded to 'aspirational' only, in response to fears of a catastrophic shake-out of non-compliant homes. With any degree of excess capacity at all in such a market, a tendering process is bound to generate fee levels which reflect the cost structure of physically 'sub-standard' homes, and which are inadequate to support continuing investment in facilities meeting modern standards.

Local rather than national baseline costs/fees

The case for local rather than national baseline costs and fees is easy to state. Pay rates and land prices are two principal determinants of care home costs and they vary significantly from authority to authority. There can be wide variations between neighbouring authorities in London and other metropolitan areas. There are also many individual social services authorities where cost variances within boundaries are sufficient to justify banding of fee rates by district.

Prior to April 1993, nearly all state-funded placements were funded by Income Support, with a single set of national fee limits other than a weighting for Greater London. With national limits set in line with the lower end of the fee distribution, this gave rise to major inequities (Laing, 2000). Care home residents and their families in more expensive areas of the country typically had to top up their Income Support funding and were often severely financially disadvantaged compared with those in less expensive areas of the country. A significant achievement of the 1993 community care reforms was to eradicate these inequities. Local authorities which took over funding responsibilities assumed at that time an obligation to pay the full costs of care and consequently set baseline fee rates which better reflected local care market conditions.

It would be a retrograde step to revert to a system in which central government set national fee rates, which would be bound to be too high in some areas and too low in others. The framework for care commissioning that was set up in 1993 is a fundamentally sound one, in which individual, budget-capped local authorities seek to obtain best value in the light of local market conditions. The way forward is to address whatever problems have emerged within this local commissioning framework.

The way forward

The issue of inadequate returns to care home providers has arisen since 1993 because of:

- monopsony purchasing power exercised by local authority commissioners;
- lack of skills in long-term market management; and
- more contentiously, inadequate funding from central government.

The first cause is now starting to be redressed, haphazardly, by market forces, as a buyers' market changes into a sellers' market in a growing number of areas. The second can be

addressed in the light of recommendations in *Building capacity and partnership in care* (DoH, 2001). On the third point, central government will have to take a view on whether it is prepared to make available additional funding to carry forward the modernisation of care homes originally envisaged under the Care Standards Act, a modernisation plan which appears now to have been discarded with the relegation of national minimum physical environment standards to 'aspirational' status only.

2

Method for calculating reasonable costs

Costs of care home services

The method adopted in the toolkit spreadsheet builds up total costs from its component parts. The four principal care home cost categories are:

- staffing costs;
- repairs and maintenance costs;
- other non-staff current costs; and
- capital costs.

These costs are calculated in the associated toolkit spreadsheet. Because capital costs have been assessed to incorporate a reasonable return for investors – including profit – 'fair fees' are identical to the sum of 'reasonable costs'.

Conceptual framework

We have interpreted the cost of supplying nursing and personal care services as being the 'reasonable cost' that a typical, *efficient* care home operator would expect to incur. It is important to note that the 'reasonable cost' so defined differs in principle from average costs incurred across all operators, since averages include the costs of *inefficient* operators as well.

We have specifically rejected the option of estimating 'reasonable cost' on the basis of simple averages of costs incurred by all operators, on the grounds that councils would not wish to pay for inefficient modes of operation on a cost-plus basis – unless it were specifically to decide to do so for reasons of service quality, or some other overriding reason.

A relatively non-contentious illustration of this principle of *efficient operator costs* is scale economies in the operation of nursing homes for older people. Staff requirements per bed vary significantly and it seems reasonable to base benchmark costs on an efficient scale of operation – say 30 plus beds – rather than (say) a scale of operation of less than 10 beds, which is wholly uneconomic in terms of staffing costs

Terms and conditions of employment may represent a more contentious illustration. Voluntary bodies and private operators subject to TUPE (Transfer of Undertakings [Protection of Employment]) arrangements typically offer staff higher remuneration (better basic pay rates, bigger enhancements for unsocial hours and more generous additional benefits such as pension contributions) than do other private sector care home operators. This has a major impact on their costs. In some cases we have entered benchmarks in the spreadsheet toolkit that specifically reflect 'more efficient' private sector costs. These benchmarks may, however, be modified in the spreadsheet and the effect of such modifications analysed. For the future, it should be recognised that pay rates in private sector homes in most parts of the country have been constrained in recent years by margin pressures. There exists latent pressure for wage cost inflation, should margin pressure be relieved through higher fee rates in the future.

3

Estimates of reasonable costs by category

Many of the costs of care home operation are dependent on occupancy levels. Nationally, occupancy rates reached a low of around 85% in 1997. They have now recovered to over 90%. This average masks wide variations, with almost a half of care homes running at 95%+ capacity at any one time and about a tenth running at below 75%. A sustainable long-term average occupancy rate in the care home sector is believed to be around 90%

An *occupancy rate* of 90% for 'efficient' homes is assumed in the toolkit spreadsheet. This may be varied if required.

Staffing costs

Staffing is the largest cost item for care homes, typically absorbing 50-60% or more of fees at present. Staffing costs are the product of:

- pay rates and on-costs per hour; and
- staff hours.

Staff turnover costs

No specific allowance is made in the toolkit spreadsheet for the cost of staff turnover. Many operators argue, however, that staff turnover is unusually elevated in the care home sector because of low pay and minimal employee benefits resulting from the financial stresses to which care homes are subject. Staff turnover costs may be incurred under a number of different heads. The largest contribution is likely to result from induction training, where the presence of paid trainees does not count towards the staffing levels required by regulators. Should users wish to make an additional allowance for the cost of staff turnover, it is best done by modifying the training backfill percentage allowance in the toolkit spreadsheet (see 'Training backfill', page 17).

Unskilled staff turnover results from competition for unqualified staff from all sectors of the economy, including retail (for example, supermarkets). The NHS and local authorities are the most important competitors for skilled and qualified staff. Competition from these public sector bodies will increase as care homes progress towards the national minimum standard that 50% of care staff (excluding nurses) should have NVQ Level 2 qualifications or above by 2005, since on gaining their qualification such staff may become potential recruits for the NHS.

Table 2 illustrates how pay rates in the care home sector fall significantly below the NHS by comparing 2003/04 care home pay rates for low-cost provincial locations, drawn from Laing & Buisson survey results, with 2003/04 pay bands in *Agenda for change*, the proposed new pay and grading system for the NHS. The pay advantage of the NHS is in fact substantially greater than the headline figures suggest, since NHS holiday and sick pay entitlements and pension arrangements are substantially more generous. Pay and conditions offered by local authority residential and home care providers are also more generous than those affordable by the private care home sector.

The gap in pay and conditions between care homes and other sectors for similarly skilled jobs is likely to remain a potent factor leading to staff turnover in the future, until such time as it becomes affordable for care homes to equalise pay.

Table 2: Comparative hourly pay rates for certain job types, care homes and NHS *Agenda for change* pay bands, low-cost provincial locations (2003/04)

	Private sector care homes	NHS *Agenda for change* pay bands[a]	
	£ per hour (illustrative)[b]	£ per hour equivalent[c]	£ per annum
Domestic, catering or laundry assistant	4.61	5.35-5.88	Band 1 10,426-11,458
Healthcare assistant (assumed to be NVQ Level 2 or equivalent)	4.89	5.72-7.09	Band 2 11,148-13,832
Nurse (qualified)	9.04-10-64	9.00-11.65	Band 5 7,548-22,710

Notes: [a] Before additions for unsocial hours, high-cost areas and recruitment and retention premia.

[b] Toolkit spreadsheet rate for Monday-Friday daytime, based on Laing & Buisson surveys in low-cost provincial locations (northern England).

[c] 52 weeks @ 37.5 hours per week.

Pay rates

Pay and on-costs per hour are best derived from actual local pay rates, as revealed by surveys of local care providers. The advantages of such an approach are:

- it takes account of local labour market variations;
- it provides a clear focus for debate on what reasonable pay rates are.

The pay rates and on-costs entered in the toolkit spreadsheet have been derived from responses to survey forms mailed to care homes in areas where Laing & Buisson has been commissioned to advise on fair fee rates. They are representative of the *low-cost provincial location* illustrated in Table 1 (p vii). Pay rates for the *outer London and environs* illustration in Table 1 are derived by adding a factor of 20% to pay rates in low-cost provincial locations, derived from information held on Laing & Buisson's database. The survey form is set out in the Appendix.

Care home staff fall into the following categories, for each of which hourly pay or salary rates and on-costs have been collected:

- care staff, comprising qualified nursing staff, senior carers and care assistants, including activities coordinators;
- supernumerary management, administration and reception staff;
- domestic staff (cleaning, laundry and catering staff – excluding chefs/cooks; and
- chefs/cooks.

Maintenance and gardening are assumed to be provided under contract and are included in the 'other non-staff current costs' category.

Staff hours

We believe that the most practical approach to estimating staff hours is by fixing benchmarks for *staff hours per resident per week* (per resident per week) in typical, *efficient* homes catering for each of the client groups. The advantages of such an approach are:

- simplicity, compared with the alternative of using staff/resident ratio benchmarks, which vary according to the time of day;
- *staff hours per resident per week* benchmarks can be selected deliberately to exclude inefficient modes of operation;
- a limited number of benchmarks help to focus debate on key parameters which can then be flexed in the spreadsheet toolkit to illustrate the impact of modifying them;
- the National Care Standards Commission (NCSC), which was responsible for care home regulation between April 2002 and April 2004, stated its intention to set care staffing requirements in terms of hours per resident per week. It is assumed that the Commission

for Social Care and Inspection (CSCI), which assumed responsibility for care home regulation in April 2004, will adopt a similar approach.

Most councils' standard contracts with care homes do not themselves specify staffing requirements. Rather, social services commissioners usually adopt whatever are the regulatory body's (that is, NCSC's or CSCI's) staffing requirements for the time being as appropriate for its contracts with care home operators.

No national staffing guidelines have yet been promulgated, except for those proposed for personal care only in *Care staffing in homes for older people*, published by the Residential Forum in May 2002, and these (as yet) apply only to new homes and homes which have varied their registration since April 2002. The Residential Forum document proposed a range of 16 (low dependency) to 20 (high dependency) care assistant hours per resident per week for older people, plus a formula for a (small) number of staff hours for leisure, social and cultural activities. The document also proposed a formula for calculating staff 'overheads'. Initially, these benchmarks will apply only to new homes, and to homes seeking a variation in registration. As regards staffing requirements for 'existing' (pre-April 2002) homes, which comprise the vast majority, the Department of Health has indicated that for the time being the staffing requirements of the now defunct health and local authority inspection units will continue to apply, and care homes have been instructed not to reduce their staffing levels from those agreed prior to April 2002.

It is important to emphasise that regulatory requirements for care staffing are the single most important determinant of care home costs. Should CSCI, therefore, adopt benchmarks which are significantly different from those described below, it would be necessary to recalculate 'reasonable costs' and adjust 'reasonable fees' accordingly.

Nursing homes

Care staff: care staffing benchmarks in 2004 have been derived from:

- inspection of written minimum requirements of several former health authority inspection units and discussion with local NCSC regulators of how the requirements are interpreted in practice;
- staff hours reported by care homes responding to Laing & Buisson surveys; and
- national, corporate operator benchmarks, derived from detailed information provided by several major care home groups in late 2003 and early 2004.

The staff benchmarks provided by corporate operators have been given the greatest weight. They are likely to be more reliable than other sources and their portfolios consist almost exclusively of larger-scale (staffing-efficient) homes. Moreover, the figures provided by different groups were remarkably consistent.

None of the sources of information indicated any inherent difference in the number of care hours per resident per week for nursing care of older people as against people with dementia – other than variations in dependency levels, which might be just as great *among* nursing homes catering for older clients only as *between* older clients and clients with dementia. Although there are localities in the UK where regulators have traditionally required higher nursing care staffing for people with dementia than for older people, they are in the minority.

Economies of scale are reflected in both staffing 'ladders' used by regulatory bodies and data on actual staffing levels provided by care homes responding to Laing & Buisson surveys. Typically, an efficient mode of nursing home operation in terms of staff:resident ratios is 30 beds or more.

In the toolkit spreadsheet, benchmarks of 7.5 and 19.5 hours per resident per week have been entered for *nursing* and *other care staff* respectively, making a total of 27 care hours per resident per week. These norms should be kept under continuing review and amended in the toolkit spreadsheet as necessary in the light of further guidance on staffing inputs that may emerge from CSCI.

The total of 27 per resident per week is identical to the benchmark used in the 2002 report. The skill mix, however (the ratio of qualified nursing to total care staff), has been reduced a little in line with recent evidence.

It should be noted that smaller-scale homes may bear much higher staffing costs. In the absence of any clear relationship between small scale and quality, however, there is no case for councils to fund such higher costs.

Catering, cleaning and laundry staff: a figure of 6 hours per resident per week for catering, cleaning and laundry staff was proposed as a minimum standard by the Centre for Policy on Ageing in the first draft of the *National care standards* in 2000, but this was subsequently rejected by the government as too prescriptive. Generally, regulatory authorities do not set any minimum number. Rather, they couch requirements in non-quantitative terms such as 'sufficient' or 'adequate'.

The same benchmark of 6 hours per resident per week was used in the 2002 report, and the benchmark has been confirmed as accurate by several corporate operators during 2003 and 2004, although some consider that it errs, if anything, on the generous side. Corporate operators confirm that the benchmark of 6 hours per resident per week does not vary by registration type (nursing or personal care) or by client type (older people or people with dementia).

Local surveys carried out by Laing & Buisson have provided further confirmation of the total 6 hours per resident per week, together with a breakdown (not available in the 2002 report) between chefs/cooks (1.9 hours per resident per week) and other domestic staff (4.1 hours per resident per week). The breakdown is a useful refinement because chefs/cooks enjoy significantly higher pay rates than other catering, cleaning and laundry staff.

In the toolkit spreadsheet, benchmarks of 1.9 hours per resident per week and 4.1 hours per resident per week have been entered for *chefs/cooks* and *other domestic staff* respectively, in line with national benchmarks. These norms should be kept under continuing review and amended in the toolkit spreadsheet as necessary.

Management, administrative and reception staff: see page 16.

Care homes offering personal care only

Care staff: care staffing benchmarks for personal care have been derived from sources similar to those for nursing care (see 'Nursing homes', page 11), that is, information from corporate operators, local Laing & Buisson 'fair price' surveys and inspection of former inspection and registration units' minimum staffing requirements.

In the 2002 report, a benchmark of 16 care staff hours per resident per week was used for older clients. No specific care staff benchmark was proposed for personal care of people with dementia, although it was noted that some inspection and registration units had specified higher minimum inputs than for older clients; many local authorities pay higher fee rates for dementia; and care staffing levels reported by respondents to Laing & Buisson surveys are typically higher for homes offering personal care to people with dementia than for those catering for older people. This contrasts with nursing care, where the evidence is that staffing is no higher for people with dementia than for older people.

The review of benchmarks in 2003 and 2004 found no evidence of material change since 2002, and the reasonableness of the 16 hours per resident per week was broadly confirmed by the minimum staffing levels published by the Residential Forum (see Table 3). The Residential Forum levels are now part of the national minimum standards for homes newly registered since April 2002, although not for pre-existing homes, which generally operate to less demanding standards.

While not obligatory for existing homes, the Residential Forum benchmarks provide a useful indicator of the additional care staff input (4 hours per resident per week) that may be reasonable to allow for higher dependency clients such as people with dementia.

Table 3: Residential Forum minimum staffing levels for new (first registered after April 2002) homes offering personal care in England

	Hours per resident per week		
a) Basic care hours			
Low dependency	16		
Medium dependency	18		
High dependency	20		
Plus:			
Social, recreation and cultural hours	15 hours/home + 1% of (a)		
Difficulties in providing care	5% of (a)		
Non-care duties	10% of (a)		
	Dependency		
	Low	Medium	High
Total for typical 30-bed home (no difficulties in providing care)	18.3	20.5	22.7

Source: *Care staffing in homes for older people*, Residential Forum, March 2002

A benchmark of 16 *care hours* per resident per week has been entered in the toolkit spreadsheet for personal care of older clients. This is equal to the low dependency basic benchmark proposed by the Residential Forum for newly registered homes.

A benchmark of 20 *care hours* per resident per week has been entered in the toolkit spreadsheet for personal care of clients with dementia (that is, 4 hours more than older clients). This is equal to the high dependency basic benchmark proposed by the Residential Forum for newly registered homes.

These norms should be kept under continuing review and amended in the toolkit spreadsheet as necessary in the light of further guidance on staffing inputs that may emerge from the NCSC or the CSCI when it takes over as regulator in April 2004.

It should be noted that smaller-scale homes may bear much higher staffing costs. In the absence of any clear relationship between small scale and quality, however, there is no case for councils to fund such higher costs.

Catering, cleaning and laundry staff: benchmarks of 1.9 hours per resident per week and 4.1 hours per resident per week have been entered for chefs/cooks and other domestic staff respectively, for homes offering personal care only, whether for older people or those with dementia – that is, the same as for nursing care (see 'Nursing pay rates', page 14).

Management, administrative and reception staff: see page 16.

Staff pay rates and on-costs

A common feature of 'fair price' surveys carried out by Laing & Buisson in different parts of the country is that voluntary sector operators pay higher hourly wage rates than private sector providers to both care and domestic staff. The differential is compounded by higher voluntary sector on-costs in the form of holiday and sick pay and pension contributions (see 'On-costs for hourly paid staff', page 15).

Voluntary sector homes may have more scope to pay higher wages than private sector homes because they have other sources of capital and current funding not accessible to private homes. Whatever the reason, councils will have to take a view on whether they wish in principle to fund

pay rates at the level of a typical voluntary sector provider.

For the purposes of this report, and in line with the principle that council fee rates should aim to cover the costs of *efficient* operators only, it is recommended that voluntary sector pay rates be disregarded, and that private sector pay rates only be used to calculate the reasonable costs of care. All of the pay rates set out below are based on data provided by private sector homes only.

Nurse pay rates

Weighted average nurse pay rates may be calculated from responses to local pay surveys (see the Appendix for the model survey form used by Laing & Buisson). Such surveys should ideally aim to collect differential pay rates for weekend and holiday working. Premiums are typically not paid for evening/weekend working by nurses, although care homes do typically pay double time for bank holiday working.

Laing & Buisson surveys carried out in 2003/04, mainly in the North of England, found an average hourly pay rate of approaching £11 per hour for Level 1 nurses and over £9 per hour for the much smaller number of Level 2 nurses working in care homes. Based on survey data and industry sources, it is estimated that 90% of nurse hours are filled by Level 1 nurses and 10% by Level 2 (enrolled) nurses.

The proportion of nurse hours filled by *Level 1 nurses* is entered at 10% in the toolkit spreadsheet, with the remaining 10% filled by Level 2 (enrolled) nurses.

For the low-cost provincial locality illustration (see Table 1, p vii) weighted average pay rates are calculated within the toolkit spreadsheet at £10.98 per hour for *Level 1 nurses* and £9.33 per hour for *Level 2 nurses*, giving a composite weighted average of £10.81 for all nurses. The figures are based on pay surveys in specific locations in the North of England.

For any given locality, these illustrative pay rates should be superseded by comparable *local* pay rates. There are two ways of doing this – a long way and a short way. Ideally (the long way), a local pay survey should be carried out using the model survey form provided in the Appendix. From the results, the full range of *shift-specific pay rates* can then be entered in the toolkit spreadsheet for both Level 1 and Level 2 nurses. The toolkit spreadsheet will then automatically calculate the composite nurse pay rate through a formula. Alternatively (the short way), a single, composite hourly rate for nurse pay may be estimated on the basis of the best available local information and entered directly in the *composite nurse pay rate cell* in the toolkit spreadsheet, overwriting the formula.

Care assistant pay rates

Weighted average care staff pay rates may similarly be calculated from responses to local pay surveys (see the Appendix for the model survey form). As with nurses, pay premiums for care assistants are typically not paid for evening/weekend working, although care homes do typically pay double time for bank holiday working.

Laing & Buisson surveys carried out in 2003/04, mainly in the North of England, found an average hourly pay rate close to the National Minimum Wage for care assistants with no qualifications, a premium of about 30p per hour for NVQ Level 2 qualified care assistants and a further premium of about 30p per hour for staff classified as senior carers. Based on survey data and industry sources, it is estimated that about 30% of carer hours (excluding qualified nurse hours) were filled by those with NVQ Level 2 or higher at the end of the financial year 2003/04.

Laing & Buisson surveys have found no significant difference in care assistant pay rates between homes offering nursing or personal care or between homes catering for older people or people with dementia.

Based on Laing & Buisson survey material and other industry sources, the proportion of care hours filled by staff with *NVQ Level 2* or above (excluding qualified nursing staff) has been entered in the toolkit spreadsheet at 30%. This parameter should be superseded by local data, where available. The percentage will increase over time. All care homes in England are expected to meet the *National minimum standard* of 50% by 2005.

The proportion of care hours filled by staff designated as *senior carers* has been entered in the toolkit spreadsheet at 15%. All of these are assumed to have NVQ Level 2 or above.

For the low-cost provincial locality illustration (see Table 1), weighted average pay rates are calculated within the toolkit spreadsheet at £4.77 per hour for *care assistants with no qualifications*, £5.00 per hour for *care assistants with NVQ Level 2* and above and £5.30 for *senior carers*, giving a composite private sector weighted average of £4.89 per hour for all (non-nurse) care staff. The figures are based on pay surveys in specific locations in the North of England.

For any given locality, these illustrative pay rates should be superseded by comparable *local* pay rates. There are two ways of doing this – a long way and a short way. Ideally (the long way), a local pay survey should be carried out using the model survey form provided in the Appendix. From the results, the full range of *shift-specific pay rates* can then be entered in the toolkit spreadsheet for each of the three classes of (non-nurse) care staff: care assistants without NVQ Level 2, care assistants with NVQ Level 2, and senior carers. The toolkit spreadsheet will then automatically calculate the composite care staff pay rate through a formula. Alternatively (the short way), a single, composite hourly rate for (non-nurse) care staff pay may be estimated on the basis of the best available local information and entered directly in the *composite (non-nurse) care staff pay rate cell* in the toolkit spreadsheet, overwriting the formula.

Domestic and catering staff

Weighted average domestic staff pay rates may also be calculated from responses to local pay surveys (see the Appendix for the model survey form).

For the low-cost provincial locality illustration (see Table 1) the weighted average hourly pay rate is calculated within the toolkit spreadsheet at £4.70 per hour for *cleaning, laundry and catering staff (excluding chefs/cooks)* and £5.71 per hour for *chefs/cooks*. The figures are based on pay surveys in specific locations in the North of England.

For any given locality, these illustrative pay rates should be superseded by comparable *local* pay rates. There are two ways of doing this – a long way and a short way. Ideally (the long way), a local pay survey should be carried out using the model survey form provided in the Appendix. From the results, the full range of *shift-specific pay rates* can then be entered in the toolkit spreadsheet for *chefs/cooks* and *other domestic staff* (see survey form in the Appendix). Alternatively (the short way), a single, composite hourly rate for (non-nurse) care staff pay may be estimated on the basis of the best available local information and entered directly in the *composite chef/cook pay rate cell* and the *composite other domestic staff pay rate cell* in the toolkit spreadsheet, overwriting the formulae.

On-costs for hourly paid staff

There are four types of employee on-cost borne by care home operators.

Working Time Regulations: under the Working Time Regulations (WTR), full-time staff are usually entitled to 20 days holiday. Part-time staff have the same entitlement pro rata. Some care homes also give their hourly paid staff eight bank holidays in the year as paid holiday, but results from Laing & Buisson surveys in several localities in England indicate that they are in a minority.

A WTR paid holiday on-cost of 8.3% (that is, statutory minimum only) has been entered in the toolkit spreadsheet for both *nurses* and *care, catering and domestic staff*. This represents a downward revision of the 12% (statutory minimum + bank holidays) entered in the 2002 report.

Employers' National Insurance: employers pay National Insurance (NI) contributions of 12.8% of pay above the NI threshold. Because some care home employees work part time, they do not reach the threshold. As a result, average NI paid by employers is below 12.8% of payroll.

Based on data provided by major corporate operators during the 2004 review of the 'fair price' model, NI on-costs of 9.0% for *nurses* and 8.0% for *care, catering and domestic staff* have been entered in the toolkit spreadsheet.

Statutory Sick Pay: evidence from major operators and Laing & Buisson surveys of independent care home providers confirm that nearly all private sector care home operators pay no more than Statutory Sick Pay (SSP) to hourly paid staff. SSP rules are complex, but major corporate groups estimate that SSP adds 2% to their hourly paid wage bill.

Based on almost universal private sector practice, an SSP on-cost of 2% has been entered in the toolkit spreadsheet for both *nurses* and *care, catering and domestic staff*.

Employers' pension contributions: evidence from major operators and Laing & Buisson surveys of independent care home providers also confirm that nearly all private sector care home operators currently do no more than offer stakeholder pension arrangements as required by law, with no employer's contributions, to hourly paid nursing, care assistant and domestic staff. Such pension contributions that they offer are restricted to management and administrative staff (see the next section).

Voluntary sector operators frequently have more generous pension arrangements.

Based on almost universal private sector practice, a zero employer's pension contribution on-cost has been entered in the toolkit spreadsheet for both *nurses* and *care, catering and domestic staff*.

Management, administrative and reception staff

This is an element of cost where there are economies of both small scale and large scale. For very small homes, no management costs may appear in the home's accounts. A management cost may be imputed, however, and this may be reflected in a higher return on capital norm for smaller owner-managed homes (see 'Target return on capital, small owner manager', page 21). The accounts of medium and larger-scale homes run by owner/managers may also have no specific management costs allocated. Again, a management cost may be imputed, and the normal practice of valuers is to deduct a reasonable estimate of management costs from profits when calculating the value of such a home as a multiple of profits.

In fact, the great majority of homes responding to Laing & Buisson 'fair price' surveys in different localities in England state that they employ a manager, whose costs must be spread across all residents. In line with the principle that councils should only pay for efficient modes of delivery, it is clear that the management cost allowance should be based on larger-scale homes, although the choice of exactly what scale is ultimately arbitrary.

Other management costs include administrative, accounts and reception functions at the individual home level, as well as deputising for the home manager. The way in which homes are staffed to cover these functions varies widely. Some homes employ a deputy manager, some of whose time may be spent providing 'rostered' care. Others do not. Some homes employ a receptionist, while others do not. Corporate providers interviewed in 2003/04 said that they spent on average a further £11 per week on other management, administrative and reception staff costs.

Based on £30,000 per annum spread over 50 residents, a *manager's salary* cost of £13 per resident per week before on-costs has been entered in the toolkit spreadsheet.

Based on major corporate group norms, a further £11 per resident per week before on-costs for *other management, administrative and reception staff pay* has been entered in the toolkit spreadsheet.

An on-cost allowance of 30% for all *management, administrative and reception staff* has been entered in the toolkit spreadsheet, to allow for enhanced benefits, particularly pension contributions, over and above those available to hourly paid staff.

Agency staff

Agency usage is very variable. The majority of care homes do not use any agency staff at all in

any one week, but a small minority may fill a large proportion of their shifts, 20% or even more, with agency staff, and this can have a major impact on overall costs. Over large portfolios, agency usage may be in the order of 5% of staff hours, although information is not wholly reliable. Agency usage is largely restricted to nurses and other care staff. Use of domestic agency staff appears to be minimal.

The question is, what level of agency usage, if any, should be allowed for in a typical *efficient* home? The 2002 report argued the case for allowing nothing at all, for two reasons:

- First, the norm is zero agency usage, in the sense that most homes do not use agency staff, or if they do, only occasionally; and the minority of homes that rely heavily on agency staff may do so for reasons which do not in principle justify reimbursement by councils. For example, heavy agency use may arise from poor management or from inappropriate location.
- Second, agency usage is one response to an inability to fill shifts from employed or bank staff. Another response is not to fill the shift and possibly seek an exception to the home's staffing notice from the regulatory body. When the 2002 report was written, information available to Laing & Buisson showed that care home groups often paid fewer staff hours than they budgeted for, and the savings were broadly similar to the excess costs from agency usage. This was a major factor in the decision not to make any allowance for agency staff costs.

A significant change arising from implementation of the Care Standards Act in April 2002, however, calls for a review of the original approach. Since April 2002, it has become potentially a criminal offence for care home managers to breach *National minimum standards*, for which managers may be in danger of losing their registration and their ability to continue to work in the industry. Under these new conditions, unforeseen staff absences are less likely to remain unfilled and more likely to result in agency usage.

An agency usage allowance of 2.5% of *nurse shifts* and 1.5% for *care assistant shifts* has been entered into the toolkit spreadsheet.

The benchmark of 1.5-2.5% is intended to represent a reasonable level of agency usage across an efficient portfolio of homes, in order to provide the flexibility to ensure that resident care is not compromised even when unplanned absences occur at short notice. Most corporate care home groups report actual agency usage at a significantly higher level, with 5% or more of shifts filled by agency staff across their portfolio for both nurses and care assistants.

An 'agency premium' of 100% has been entered in the toolkit spreadsheet for both *nurses* and *care assistants*, in line with national sector norms.

Training backfill

In line with English *National minimum standards*, the backfill costs of a minimum of 3 days of paid training per employee need to be added to staffing costs. Other direct training and recruitment costs are incorporated in 'Other non-staff current costs', page 34.

A *training backfill* on-cost of 1.2% (3 days as a percentage of 241 working days in the year) has been added to staffing costs in the toolkit spreadsheet, amounting to £3 per resident per week.

Training costs may rise as a result of staff turnover. If local staff turnover is elevated for reasons that are beyond the control of care home operators, there may be a case for the training backfill on-cost percentage to be increased in the toolkit spreadsheet (see 'Staff turnover costs', page 9).

Group overheads

This category of expense, consisting of head office and regional office costs, is borne only by care home groups. It typically absorbs around 4-5% of fees for an efficiently run group. This expense should be ignored for the purposes of estimating what fee rates councils should pay. Group overheads are best regarded as portfolio management costs which corporate investors are prepared to absorb within their gross rate of return (see 'Capital costs', page 18).

Expressed in another way, there is no reason why corporate operators should receive a special allowance for employing staff and other resources to manage their portfolios, while independent operators do not.

No allowance is made for group overheads in the toolkit spreadsheet.

Repairs and maintenance costs

This section revises the 2002 report format in the light of information received during the 2003/04 updating exercise.

Data collected from several major corporate providers of care homes for older people during late 2003 indicate a UK average spend of about £21 per resident per week. Since the cost head is relatively small, it is not essential to supersede this with local data in the toolkit spreadsheet. Should users wish to do so, however, regional variances in building costs can be obtained from the Royal Institution of Chartered Surveyors (RICS).

A total of £21 per resident per week has been entered in the toolkit spreadsheet for *repairs and maintenance* covering both the current and capital accounts. The main component is £700 per year for maintenance capital expenditure, based on estimates by corporate groups of expenditure over the lifetime of a care home. To avoid double counting, no allowance has been entered for the non-cash item of depreciation.

Other non-staff current costs

Basic non-staff current costs are based on norms reflecting the experience of several major corporate providers of care homes for older people, gathered during late 2003. The two largest items are food and utilities. There is a range of smaller items, but not all corporate groups classify cost heads in the same way. Corporate norms provide the best available indication of the costs borne by larger-scale, *efficient* homes. Since these costs are relatively invariable throughout the country, there is no need to supersede them with local data.

In the toolkit spreadsheet, £55 per resident per week has been entered for *non-staff current costs*.

A number of modifications have been made under this heading since the 2002 Joseph Rowntree report, including:

- repairs and maintenance paid as revenue items have been moved into the 'Repairs and maintenance' category (see above);
- insurance costs have been revised upwards in line with substantial premium increases;
- specific items have been added for recruitment and direct training expenses;
- as before, no cost allowance has been made for incontinence products, on the grounds that this is an NHS responsibility. It is recognised that this is a contentious point, but the sums of money involved are relatively small.

Capital costs

An adequate return on capital for care home operators is the key to achieving a stable independent sector of sufficient size and appropriate quality to meet the commissioning needs of councils and their NHS partners. On the assumption that new and/or replacement care home capacity *is* required (see 'Background', page 2), councils throughout the country need to set fee rates such as to (a) incentivise existing operators to continue to offer services and to upgrade their physical assets where they are below *National minimum standards* for newly registered homes; (b) attract investment in new care home capacity to replace that which is being lost through home closures; and (c) compete with private payers and residents funded by other public sector agencies for available care home places.

It is desirable to have one simple formula for return on capital, which can be applied regardless of the capital structure of the home. To do otherwise would lead to a hopelessly complex requirement to understand the intricacies of different capital funding structures.

Target return on capital

Our conclusion is that councils should ideally set 'spot purchase' fees at levels sufficient to offer

providers a return on capital of 14%. This compares with the figure of 16% recommended within the 2002 report. Long-term block contract commissioning offers scope for a lower target rate of return.

The background to the proposed 'spot' return of 14% is as follows, looking in turn at the main types of capital structure found in the for-profit sector, as well as the voluntary, not-for-profit sector.

Independent owners funded by a mixture of equity and debt: despite the expansion of corporate operators, Laing & Buisson data show that 68% of privately owned care home places nationally remained in the hands of independent (non-group) operators in 2003. The definition of a 'group' is any individual, partnership or company that operates three or more care homes. Care home groups, so defined, own the remaining 32%. Independent operators, therefore, are the dominant source of care home supply and are likely to remain so for the foreseeable future.

For most of the last 20 years *good quality* care homes have been bought by independent operators at a 'profit purchase' multiple of about 6-6.5 times sustainable Earnings Before Interest, Tax, Depreciation, Amortisation and Rent (EBITDAR) at the level of the individual home (that is, excluding any corporate overheads). In the last two years (between 2002-04) the EBITDAR multiple has risen to about 7-7.5 (or 7.25 as the mid-point in this range) for *good quality* homes catering for a state-funded clientele (that is, homes which among other things meet all the room size and single/sharing ratio standards incorporated in the *National minimum standards for care homes for older people* introduced in April 2002, and subsequently relegated to 'aspirational' only). Homes with a predominantly privately funded clientele may attract a yet higher multiple because the quality of their future earning streams is perceived as better. The reasons for the general rise in care home EBITDAR multiples may include the continuation of a low interest rate environment and a perception among investors of better prospects for the care home sector.

A 'profit purchase' multiple of 7.25 implies that purchasers are willing to invest in *good quality* care homes in the expectation of a return of 14% (that is, the reciprocal of 7.25). It comes as close as possible to an objective, market-related norm for expected rate of return.

The return of 14% is a 'blended' rate. The owner (equity investor) seeks a much higher return on capital, about 25-30%, and achieves this by leveraging with bank finance.

The gross return on capital of 25-30% sought by the equity investor compensates him/her for:

- opportunity cost of not investing in alternative, non-risk securities such as gilts;
- risk;
- time and energy spent overseeing the business.

There are at present few, if any, areas of the country where it is possible to earn a blended 14% return on new developments for older people or people with dementia costing around £50,000 per bed including land costs (see 'Land costs', page 22) from spot purchase fees on offer from local authorities. This is believed to be the major reason why few new care homes are currently being built for older clients who are state-funded, despite acute shortages of supply in some areas.

Groups funded by a mixture of equity and debt: care home groups operate in the same market as independent operators and the rates of return they seek are comparable. Despite the well-publicised financial stress suffered by the care home sector, there remains an appetite for investment in the acquisition of existing care home businesses, if not in developing new care homes. The explanation for this is that care home values have declined along with declining profits, and investors can still buy assets that offer a 14% EBITDAR yield at the individual home level. In other words, financial stresses have not reduced the percentage yield for investors making acquisitions, although they have certainly kept the perceived risk profile of the sector high, thus reinforcing the need for a relatively high EBITDAR yield of around 14% for a property-based business.

Care home groups may derive their equity funding from private investors, including the group's principals, or from private equity and venture capital companies. Like independent operators, groups seek to leverage their equity with debt finance. The structure of debt and equity may be more complex, but the essential features are the same. Like independent operators, active corporate purchasers in the market at present are typically seeking to buy good quality homes, at a multiple of about 7-7.5 times sustainable earnings at the home level. To the extent that purchase multiples stretch upwards, it reflects an expectation that sustainable profits are likely to grow in the next few years.

Like independent operators, care home groups are rarely able to justify development of new care homes for a 'spot purchased' state-funded clientele in the current climate, although they may be able to justify the addition of new capacity to existing care homes, where land costs are zero, and they may be able to develop entirely new care homes on the basis of block contracts.

Unlike independent operators, larger corporate groups must bear an additional cost in the form of head office and regional office overheads. These represent costs over and above management and administration at the level of the individual home. Typically, such overheads absorb around 4-5% of gross fee income for an efficiently run group, which is equivalent to around 3% of the capital value of a typical good quality portfolio. These additional group overheads can be ignored by councils for the purposes of setting a fair price for care. Such overheads should be viewed as portfolio management costs. Equity providers are either prepared to operate on a lower blended return on capital than independent owners (3 percentage points lower, that is, 11%), or they expect to recoup at least part of the diminution in return from better financial engineering, higher leverage, lower interest rates from providers of debt or improvements in operational profitability. In these ways, venture capital companies can still realistically seek to achieve a return on their equity capital of 25-30% per annum.

Sale and leaseback: sale and leaseback funding became a major driver of acquisition and development activity at the end of the 1990s, but it evaporated in the early months of 2000 with the withdrawal from new business of NHP plc and other sale and leaseback providers.

The fundamental reason for the (temporary) demise of sale and leaseback was reduced profit margins of care home operation, which in turn reduced 'rent cover' (the ratio of a home's operating profit to its rent commitment) to dangerously low levels. Although there is little or no new sale and leaseback business being transacted at present, over £1 billion of care home assets throughout the UK remain subject to sale and leaseback arrangements. Some of the operators remain distressed, and there have been several bankruptcies. The homes themselves, however, continue to operate since they are predominantly good quality physical assets with few alternative uses.

Sale and leaseback is a mechanism for separating the property element from the operating element of care home provision. It is widely used in other sectors of the service economy, including hotels and pubs. The rationale of sale and leaseback was and is that care homes represent an important class of asset which should attract property investors at relatively low rates of return, although not as low as commercial property or office space. Sale and leaseback allows operators to borrow 100% of the capital cost of care homes and thus develop their businesses from a low (arguably too low) equity base. The strategy of NHP was to generate a continuing flow of new capital from 'securitisation' of its rental streams on the Eurobond market. Essentially NHP would spend its available cash on care homes, rent them to operators and then sell the rental stream to bond holders, giving NHP the cash to start the process again. The attraction of bond holders as an ultimate source of funding was and is that they will accept a relatively low yield in return for having the first claim on secure rental streams. NHP itself makes its return from any surplus remaining after paying bond holders and its own operating costs. In the event, NHP ceased to seek new business in 2000 because the squeeze on care home margins prevented it from achieving its target profitability.

Although bond holders will accept low rates of return, securitisation is a complex piece of financial engineering requiring payment of very substantial fees. For this and other reasons, NHP set its rent at 10.8% of lending. In other words, care home operators which opted for sale and leaseback needed to achieve a 10.8% return (on historical capital costs) plus (say) a further 3% to cover group overheads to make a total of 13.8% before breaking even. It is easy to see, therefore, how some highly geared operators got into difficulties.

Publicly quoted companies: from a peak of 20 a decade ago, the number of UK publicly quoted care home groups has fallen to just four. Only one of these, Care UK, is a substantial operator and it differs from most care home groups in that it describes itself as an 'outsourcing company' and seeks long-term (as opposed to 'spot') contract business from local authorities and the NHS.

The principal motivation for seeking stock exchange quotations a decade ago was the personal enrichment of principals. The stock exchange initially placed a high valuation on what was viewed as an exciting new sector, but disenchantment soon set in with poor profit performance, and share prices fell below net asset values. Most commentators see little prospect for the foreseeable future of a resurgence of stock exchange quoted care home groups. In any case, the stock market is generally not comfortable with gearing ratios of more than 50%, which puts stock market listed care home companies at a disadvantage to private companies able to operate at much higher gearing ratios. The return on capital requirements of the stock market, therefore, are not relevant councils' fee setting.

Small owner manager: small, owner-managed homes, up to, say, 10 beds, are the only exception in principle to the benchmark of a 14% return, or a profit purchase multiple of 7.25 on top quality assets. This is because, at a very small scale of operation, business oversight is in practice inseparable from the home management and administration function. Valuers do not, therefore, typically impute a cost of management when calculating value. Rather, they allow a lower profit purchase multiple, say, 5 for a small home meeting all standards, which implies a higher target blended rate of return of 20%. This difference, however, should in principle wash out in the allowances for management and return on capital.

Not-for-profit providers: there is no reason in principle why voluntary sector or not-for-profit providers should seek a lower rate of return on investment than for-profit providers. They may indeed be obliged under their charitable objects to seek the best return on their capital available for investment.

Based on the foregoing, a target rate of *return on capital* of 14% has been entered in the toolkit spreadsheet.

Capital value of care homes

If commissioners are to attract investment in new care home capacity they will need to offer a reasonable rate of return (that is, 14% for spot purchase) on the cost of new development, made up from building/equipment costs and land costs.

Building and equipment costs

Industry sources indicate that at 2003/04 prices a fully equipped, new-build care home with 40-45m^2 gross space per bed (including common parts) can be delivered as a design and build turnkey project at £35,000 per bed. These costs can be assumed to be constant throughout England as a whole. This is because there is only a handful of active, specialist care home builders, which tend to operate nationwide at prices which do not vary greatly by geography.

A sum of £35,000 per bed has been entered in the toolkit spreadsheet as the *capital cost of buildings and equipment* for care homes meeting physical environment standards for 'new' homes first registered since April 2002, as defined in the *National minimum standards for care homes for older people* (3rd edn, February 2003). This is equivalent to £38,889 per resident at 90% occupancy.

The same building and equipment cost should in principle be allowed for *any* care home, whether new build or not, which meets the same standards. The rationale for this is that councils and their NHS partners must not only attract new capacity but also incentivise operators of existing stock to remain in operation and to upgrade facilities if necessary to meet the highest physical standards for which commissioners are willing to pay.

Land costs

Land price data from all areas of the country is collected by the Inland Revenue and collated in *Property Market Report*, published twice yearly by the Estates Gazette.

A minimum of three quarters of an acre is required for a 50-bed care home. On this basis, the land cost per care home bed and per resident can be calculated at three quarters of the cost per acre of suitable development land, divided by 50 and adjusted for occupancy.

For the low-cost provincial locality illustration (see Table 1) *land costs* of £750,000 per acre have been entered in the toolkit spreadsheet. This is equivalent to £11,250 per bed or £12,500 per resident at 90% occupancy, assuming a 14% return on capital. This is the single most highly variable parameter in the cost model. For any given locality, the illustrative land cost of £750,000 per acre should be superseded by comparable *local* land costs. Costs in London, its environs and other high priced areas throughout the country may be three times as high and sometimes much higher still.

Depreciation

The accountancy profession's standard is to depreciate buildings at 2% over 50 years. Equipment is depreciated over variable but much shorter time periods. Land is not depreciated.

There are sound accounting reasons for depreciating buildings, but in reality the value of buildings may rise over time and the effect of annual depreciation allowances are often reversed through periodic revaluations of property assets to create revaluation reserves.

From the perspective of local authority purchasers, making allowances for both deprecation and maintenance capital expenditure would be double counting.

In the toolkit spreadsheet, an allowance for *maintenance capital expenditure* has been entered. No allowance has been made for depreciation.

Capital cost adjustment factor

It would not be appropriate for councils and their NHS partners to pay physically sub-standard homes at the 'fair' rate established for physically good quality homes. If they were to do so, they would find themselves paying fees to sub-standard care homes at a level that would generate super-profits for them (contrary to Proposition 3, page 23). This is the reason for proposing a *range* (ceiling and floor) of fair fees for each of the location/client types in Table 1 (p vii).

The proposal is that councils should apply a *capital cost adjustment factor* such that 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. In addition, in order to avoid paying high fees to homes that provide poor care, it is recommended 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.

What is the upper end of the range of physical standards for which councils should be willing to pay? Ultimately, that is a matter for each democratically elected council. However, there must be a strong presumption that councils, which receive most of their funding from central government, should be prepared to pay a fee which fairly reflects the build/equip costs of any home in their locality which meets the physical environment standards for 'new' homes first registered since April 2002, as defined in the *National minimum standards for care homes for older people* (3rd edn, February 2003). The appropriate 'ceiling' is best represented by the build/equip costs of a new-build home, estimated at £35,000 per place, or £38,900 per

occupied bed at 90% occupancy in the toolkit spreadsheet.

Build/equip costs for those homes at the lower end of the acceptable physical quality range, which are acceptable to councils making placements, are more difficult to derive. Conceptually, they should reflect the current value of the historic bricks and mortar costs of providing capacity (usually by conversion) in homes that do not exceed the interim physical environment standards for 'existing' homes as defined in the *National minimum standards for care homes for older people* (3rd edn, February 2003). These are referred to as 'interim' standards because they result from a government decision to amend the more demanding physical standards initially introduced in April 2002, for fear of a catastrophic loss of capacity. These amended standards will be subject to further review. The build/equip cost 'floor' is estimated in the toolkit spreadsheet by assuming that the floor value of such homes as going concerns is £20,000 per registered place (or £22,200 per occupied bed at 90% occupancy in a typical low-cost provincial location). If the assumed land value of £12,500 per occupied bed is deducted, this gives a floor build/equip cost of £9,700 per occupied bed. Although this method is based on what may be viewed as ultimately arbitrary assumptions, the result is believed be reasonable and to reflect market realities.

This in turn allows the difference between the floor and ceiling build/equip costs to be calculated at £29,200 per occupied bed. Application of the return on capital benchmark of 14% per annum then gives a range of £77 per resident per week between the floor and ceiling capital cost per resident per week. This £77 represents the maximum *capital cost adjustment factor* to be applied to individual homes.

It should be noted that the *capital cost adjustment factor* could equally be called a 'discount' to be deducted from the ceiling of the fair fee range, or a 'premium' to be added to the floor of the fair fee range. The choice of which term to use is presentational. The substance is the same in the fair price model.

The proposed *capital cost adjustment factor* will be very important in mitigating the cost consequences of 'fair price' policies adopted by councils, by ensuring that sub-standard homes do not obtain super-profits.

The fleshing out of the capital cost adjustment framework in each council area will necessitate decisions on:

- exactly which standards or quality measures are to be used; and
- what weighting should be attributed to each.

This should be a matter for each individual council to decide, in association with local stakeholders.

There will be a cost associated with continuing monitoring of individual homes' compliance with agreed quality standards and ensuring that the process continues to have the confidence of stakeholders. Such transaction costs, although significant, should not be disproportionate in view of the substantial sums of money being spent by councils on care services and the importance of ensuring that the market operates effectively.

A proposed framework for calculating *capital cost adjustment factors* is described below. It is based on the following propositions:

1. Councils should be prepared to pay the full cost of providing care of an acceptable standard in any home which meets the physical environment standards for 'new' homes first registered since April 2002, as defined in the *National minimum standards for care homes for older people* (3rd edn, February 2003), for example, single rooms with a minimum of 12m^2 of usable space excluding en-suite facilities.
2. Councils should not pay for standards higher than national minimum standards.
3. Councils should not pay fees that are likely to generate super-profits for care homes. (This proposition applies equally to homes which may be highly rated on 'soft' quality criteria but which have not invested in their physical environment up to post-April 2002 standards.)
4. All homes should be expected to score highly on 'soft' quality criteria, most of which do not impose a cost burden on the home, and this should be viewed as a precondition for unlocking their capital cost entitlement as calculated through the *capital cost adjustment factor*.

To make the framework operational, councils will require:

- evidence of the degree to which each home complies with relevant quality standards;
- a scoring and weighting mechanism to allow raw data on compliance to be translated into fee entitlements.

There are essentially three routes that councils could follow, or a mix from all three:

- make use of ratings of compliance with each of the 38 *National minimum standards* contained within the most recent inspection reports for each home published by the CSCI on its website www.carestandards.org.uk;
- make use of quality ratings assessed by an independent third party; or
- develop an in-house methodology for measuring quality.

In each case, we recommend a two-step process in which increments in fee entitlement are related to compliance with physical standards, which are the main generators of care home costs, and these increments are 'unlocked' by meeting non-physical standards, which do not necessarily impose any costs on care homes.

Option 1: CSCI inspection reports: several actual *worked examples* in Sheet 1 (Parameters and assumptions) of the toolkit spreadsheet illustrate how the *capital cost adjustment factor* would be calculated for a sample of homes, using CSCI inspection reports. The steps are as follows:

- List out all of the *environment standards*, that is, standards 19-26 for care homes for older people.
- Ascribe a *Relative Importance Weighting* (RIW) to each of these environment standards. As an illustration, in the worked examples, we have given *standard 23* (minimum room size and single/shared room ratios) the highest RIW of 10 because the nature of personal living space is (probably) highly valued by residents and (more importantly) the provision of good sized, mainly single rooms adds significantly to capital costs. For the purposes of illustration, other environmental standards have been given an RIW of 2, indicating lower relative importance. Each of the RIWs could be varied and any national minimum environment standard felt to be irrelevant could be made not to count at all in calculating the *capital cost adjustment factor* by giving it a zero RIW.
- Assess the *Per Cent Compliance* with each of the environment standards. Evidence of compliance with national minimum standards can most easily, transparently and economically be derived from the latest inspection report for the particular home. Reports for most homes in England are now published on the CSCI website. There is then the issue of translating this evidence into a scale. Any compliance scale chosen will ultimately be arbitrary, but the calculation should ideally be as transparent and non-subjective as possible. In the toolkit spreadsheet illustration, the CSCI scale of 1 (does not meet standard), 2 (partly meets standard), 3 (meets standard) and 4 (exceeds standard) have been translated as 0%, 50%, 100% and 100% compliance respectively (note that Standard 4 would be assessed as no more than 100%, in line with Proposition 2, page 23 above). A scale such as this would ensure that homes which met none of the environment standards would be given a zero environment score, meaning that they would be entitled to no more than the relevant 'floor' fee rate, that is, £77 less than the 'ceiling' fee rate in the 2003/04 toolkit spreadsheet (see Table 1, p vii).

As the user of the toolkit spreadsheet fills in all of the RIW and Per Cent Compliance cells, the spreadsheet calculates the *weighted average compliance with post-April 2002 environment standards* for the illustrative examples.

The next step is to repeat the process described above by listing out the *non-environment national minimum standards* (1-18 and 27-38) and filling in the RIW and the Per Cent Compliance cells. As this is done, the spreadsheet calculates the *weighted average compliance with non-environment quality standards*. The spreadsheet then multiplies the weighted average compliance with non-environment quality standards by the weighted average compliance with post-April 2002 environment standards, in order to derive a *combined compliance* factor, from which in turn is derived *combined non-compliance* factor. This is then applied to the *maximum capital cost*

adjustment factor (£77 per week in the toolkit spreadsheet) to give the *capital cost adjustment factor* for the particular home.

The advantages of the CSCI inspection report option are:

- the 38 standards against which homes are assessed are national standards derived from a massive three-year process of expert reports and consultation;
- inspection reports are a readily available, transparent and 'free' resource;
- inspection reports should be updated by the CSCI at least once and usually twice a year;
- there is an existing statutory requirement on homes to pay for inspections, set at £72 per registered place per year from April 2004.

However, there are currently practical disadvantages to the CSCI inspection report option:

- Inspectors' ratings may not be viewed as objective and may not have the confidence of care home operators. In particular, it is widely believed that there is substantial inter-inspector variation within any single CSCI area. It is also believed that the rigour with which 1, 2, 3 and 4 compliance ratings are applied may vary widely throughout England. It is possible, therefore, that a subsequent move to harmonise ratings may have a significant knock-on effect on individual homes' *capital cost adjustment factors* without any material change having taken place in their quality.
- Individual reports frequently do not assess all standards. This may give rise to bias, or a perception of bias, where the *capital cost adjustment factor* has to be based on an incomplete set of standards.
- Until recently, reports have frequently taken several months to be published.
- The timing and flow of new assessments could not easily be planned, since they are at the discretion of the regulator (CSCI). Multiple inspections in the course of the year may lead to frequent requests for reassessment of *capital cost adjustment factors* based on new evidence.
- An important practical disadvantage is that the degree to which a given home meets standard 23 (minimum room size and single/sharing ratios) cannot be 'read' directly from individual inspection reports. This is because reports for homes first registered before April 2002 are based on the relatively undemanding interim physical environment standards for 'existing' homes as defined in the *National minimum standards for care homes for older people* (3rd edn, February 2003), rather than the more demanding standards for 'new' homes first registered after April 2002. In the illustrative worked examples in the toolkit spreadsheet, compliance with standard 23 for 'new' homes has been estimated on the basis of evidence available from inspection reports, but in practice it would have to be validated by other evidence, possibly a visit to the home by a council official. It will be necessary, therefore, for councils to complement the CSCI report-based approach by developing an in-house tool (see Option 3, below) for measuring how far this key physical environment standard is met.
- A potential issue for the future is that CSCI may set up a lighter touch regulatory regime for homes which have provided other evidence of quality. In one way this could simplify the process of quality monitoring, since the fact of being subject to a lighter touch could be regarded as evidence of full compliance with non-environment quality standards. But councils would still have to develop an in-house tool (see Option 3, below) for measuring how far physical environment standards were met.

Option 2: Quality ratings assessed by an independent third party: a variety of quality assurance programmes are in use within the care home sector. Most, however, are not specially designed for care homes and deal with only a small sub-set of care home attributes. These include Investors in People and ISO 9002. Although useful indicators of quality, they are not suitable for calculating capital cost adjustment factors as described above.

The best known independent organisation to specialise in the care home sector and offer an assessment of quality across a comprehensive range of care home attributes is Brighton-based RDB Star Rating, whose ratings were in use in Blackpool, Sefton, Redcar/Cleveland, Lancashire, St Helens, Brighton & Hove and Wigan at the beginning of 2004. There is a considerable amount of overlap between RDB and national minimum standards. RDB's star rating

assessments are based on an inspection of documents and interviews with managers, other staff and residents. Star ratings do not cover the physical environment of the home – that is covered by a separate 'crown' system. It is possible, therefore, for a home in a modest building to receive a 5-star rating. Homes must, however, receive at least a 4-star rating before being eligible for a crown rating. This principle is fully in line with the framework proposed above, whereby achievement of 'soft' quality standards is to be viewed as a precondition for unlocking a home's entitlement to higher fees by virtue of compliance with physical environment standards.

The advantages of the RDB star rating and crowns option are:

- RDB ratings may inspire more confidence among care home operators than NCSC inspections;
- being specifically designed for the purpose, RDB ratings will always be based on RDB's full set of quality attributes;
- reports are likely to be made available soon after completion; and
- the timing and flow of new assessments can be planned.

The disadvantages of RDB star rating and crowns are:

- cost: accreditation fees range from £1,250 to £3,000 depending on size and client group, although there may be some opportunities for mitigation via grants from various sources;
- a possible disadvantage is that the RDB crown system may not exactly match varying degrees of compliance with national minimum standards for newly built homes, as recommended in Proposition 1, page 23.

The principal disadvantage of the RDB option is its additional cost. In the future, it may be that an RDB star rating, or similar, will be acceptable as an alternative to a CSCI inspection, but that is not on the government's immediate agenda.

In other localities where RDB star ratings are used, it is the care home that pays. This seems to set appropriate incentives, since care homes which cannot realistically expect to gain higher fees will not incur the expense of seeking a star or crown rating, and the accreditation costs for care homes which successfully apply will be recovered from higher fees. It is understood that in areas where star ratings are used to trigger local authority fee premiums, typically about one third of homes pay for a star rating, although the incentives to participate would be significantly higher with a possible extra £77 per week on the table. The maximum premium triggered by a star rating in areas where it was used in 2003/04 was about £20 per week.

Option 3: Development of an in-house tool for measuring quality: the third option is for councils to develop their own in-house tool for measuring quality and paying quality premiums up to £77 per week. Councils could choose to use a mix of national minimum standards and local standards, and the process could be identical to that described for Option 1 (CSCI inspection reports) – except that *locally defined standards* would be used in place of, or in addition to, national minimum standards.

The advantages of such an approach would be:

- it is potentially simpler than Option 1 (CSCI inspection reports) and less susceptible to bias from an incomplete set of measurements;
- the timing and flow of new assessments can be planned;
- it is less expensive than Option 2 (independent third party) although not necessarily less expensive than Option 1.

Whether or not an in-house tool would command the confidence of care home operators would probably depend on their degree of involvement in the development of the tool.

Summary of options for calculating *capital cost adjustment factors:* each of the options has advantages and disadvantages, which relate to cost, confidence and practicality. Technically, however, each of the options discussed is equally capable of giving rise to a simple banding system, and each is equally amenable to containment within a budget in a transitional phase, achievable by selection of appropriate triggers and scales for fee increments.

Ideally it would be desirable to use the CSCI inspection report option, since the regulatory process offers a substantial existing resource which it would be wasteful to duplicate.

Summary of care home costs and fair fees

Tables 4-6 illustrate the reasonable costs incurred by efficient providers of nursing and personal care for older people and people with dementia in 2003/04, and the corresponding range of fair fee levels for purchasers.

Two sets of illustrative figures are given for each client group, reflecting two types of location at opposite ends of the range of wage costs and land prices:

a) low-cost provincial location in the North, Midlands or extreme South West of England; and
b) high-cost location in outer London and its environs.

These are illustrative figures only. In order for commissioners to estimate reasonable costs and fair fees in their own areas, it is essential that they substitute *local* wage rates and land prices in the toolkit spreadsheet and if necessary adjust the *nurse* and *care assistant hours per resident per week* benchmarks to reflect their own service specifications and/or the requirements of local regulators. The illustrative data inserted in the toolkit spreadsheet represent actual figures for a low-cost provincial location in which Laing & Buisson carried out a full fair price exercise in 2003/04.

In each of the illustrative cases in Tables 4-6, a range of fair fees is identified. At the higher end of the range is the fair fee appropriate to a care home which has invested in providing a physical environment which meets national minimum standards for 'new' homes first registered after April 2002, and which also passes a quality hurdle for other non-physical standards (see 'Capital cost adjustment factor', page 22). At the lower end of the range is the fair fee appropriate to a care home which does not exceed the interim physical environment standards for 'existing' homes incorporated in the revised *National minimum standards* published in February 2003. The difference between the top and the bottom of the range, equal to £77 per week according to the assumptions built into the toolkit spreadsheet, represents the maximum capital cost adjustment factor for homes which fail to meet the more demanding standards for 'new' homes ('Capital cost adjustment factor', page 22).

Gap between fair fees and fees paid by social services

The 2002 report found that in 2001/02 there were substantial gaps in most English localities between fair fee rates and the weekly fees paid by social services.

Since then, many local authorities facing capacity shortages have increased their fees by amounts in excess of ordinary inflation, and a handful have increased their fees by substantial amounts. Laing & Buisson's analysis of the 2003/04 round of fee revisions found that 23% of local authorities (excluding Scotland) had increased some or all of their baseline fees by more than 10% and another 30% had increased some or all by between 5-10%. Some local authorities have also acknowledged that their baseline fees are unsustainably low and have agreed with their local provider associations that while they cannot afford to pay fair fees immediately, they will seek to move towards fair fees over a period of years.

Despite the progress that is being made, there were still substantial gaps between fair fee rates and the weekly fees paid by social services in 2003/04. In order to provide some quantification of the gap, English councils' baseline fee rates set at the outset of financial year 2003/04 (collated annually in *Community Care Market News*) have been compared with the 'fair fee' rates derived from the toolkit spreadsheet. Baseline fees are those rates that are declared by each social services authority as the basis for spot purchasing with local care homes. Where they are banded, the highest baseline fee rates have been used for comparison. To simplify the task, the comparison has been confined to the 84 social services authorities for which 2003/04 baseline fee rates were available in the North, North West, East Midlands, West Midlands and South West of England. These regions are relatively

Table 4: Fair fees for nursing care in financial year 2003/04

	£ per resident per week, 2003/04	
Nursing care for older people or people with dementia	**a) Low-cost provincial location**	**b) Outer London and environs**
Cost heads		
a) Staff, including employers' on-costs		
Qualified nurse staff cost per resident (excludes supernumerary managers)	97	117
Care assistant staff cost per resident (including activities)	114	136
Catering, cleaning and laundry staff cost per resident	36	43
Management/administration/reception staff cost per resident	31	37
Agency staff allowance – nurses	2	3
Agency staff allowance – care assistants	2	2
Training backfill	3	4
Total staff	**£285**	**£341**
b) Repairs and maintenance		
Maintenance capital expenditure	£13	£13
Repairs and maintenance (revenue costs)	£6	£6
Contract maintenance of equipment	£2	£2
Total repairs and maintenance	**£21**	**£21**
c) Other non-staff current costs at home level		
Food	17	17
Utilities (gas, oil, electricity, water, telephone)	12	12
Handyman and gardening (on contract)	6	6
Insurance	4	4
Medical supplies (including medical equipment rental)	3	3
Registration fees (including Criminal Records Bureau checks)	2	2
Recruitment	2	2
Direct training expenses (fees, facilities, travel and materials) net of grants and subsidies	2	2
Incontinence products	0	0
Other non-staff current expenses	7	7
Total non-staff current expenses	**£55**	**£55**
d) Capital costs		
Land	33	99
Buildings and equipment meeting national minimum physical standards for 'new' homes first registered since April 2002	103	103
Total capital costs	**£136**	**£203**
Fair price for homes meeting all standards for 'new' homes in the *National minimum standards for care homes for older people* (3rd edn, February 2003)	£497	£620
Maximum capital cost adjustment factor for homes not meeting physical standards for 'new' homes	–£77	–£77
Fair price for homes which do not exceed the interim physical standards for 'existing' homes in the *National minimum standards for care homes for older people* (3rd edn, February 2003)	£420	£543

Table 5: Fair fees for personal care (for older people) in the financial year 2003/04

	£ per resident per week, 2003/04	
Personal care for older people	**a) Low-cost provincial location**	**b) Outer London and environs**
Cost heads		
a) Staff, including employers' on-costs		
Qualified nurse staff cost per resident (excludes supernumerary managers)	0	0
Care assistant staff cost per resident (including activities)	93	112
Catering, cleaning and laundry staff cost per resident	36	43
Management/administration/reception staff cost per resident	30	37
Agency staff allowance – nurses	0	0
Agency staff allowance – care assistants	1	2
Training backfill	2	2
Total staff	**£162**	**£195**
b) Repairs and maintenance		
Maintenance capital expenditure	13	13
Repairs and maintenance (revenue costs)	6	6
Contract maintenance of equipment	2	2
Total repairs and maintenance	**£21**	**£21**
c) Other non-staff current costs at home level		
Food	17	17
Utilities (gas, oil, electricity, water, telephone)	12	12
Handyperson and gardening (on contract)	6	6
Insurance	4	4
Medical supplies (including medical equipment rental)	3	3
Registration fees (including Criminal Records Bureau checks)	2	2
Recruitment	2	2
Direct training expenses (fees, facilities, travel and materials) net of grants and subsidies	2	2
Incontinence products	0	0
Other non-staff current expenses	7	7
Total non-staff current expenses	**£55**	**£55**
d) Capital costs (14% return on capital)		
Land	33	99
Buildings and equipment meeting national minimum physical standards for 'new' homes first registered since April 2002	103	103
Total capital costs	**£136**	**£203**
Fair price for homes meeting all standards for 'new' homes in the *National minimum standards for care homes for older people* (3rd edn, February 2003)	£375	£474
Maximum capital cost adjustment factor for homes not meeting physical standards for 'new' homes	–£77	–£77
Fair price for homes which do not exceed the interim physical standards for 'existing' homes in the *National minimum standards for care homes for older people* (3rd edn, February 2003)	£298	£397

Table 6: Fair fees for personal care (dementia) in the financial year 2003/04

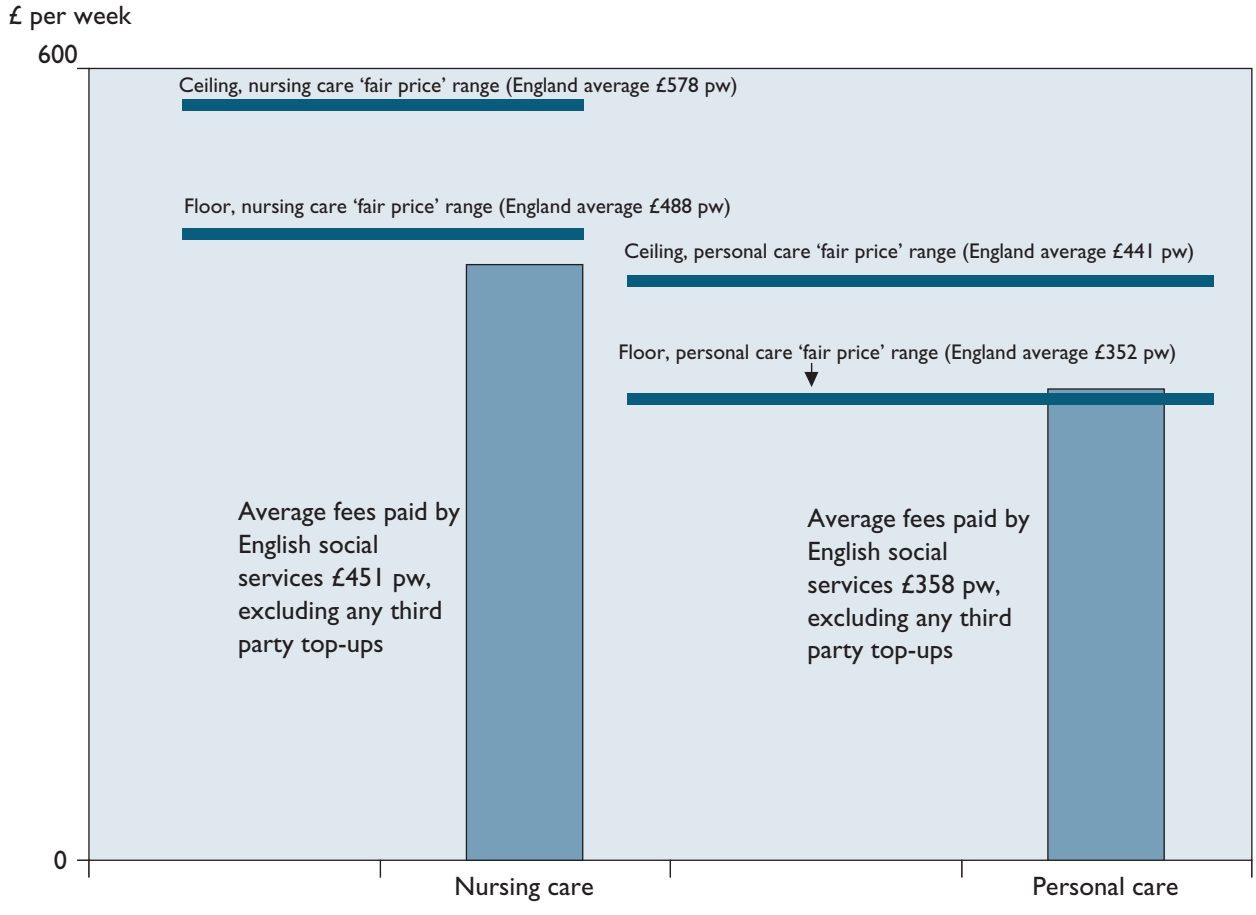
	£ per resident per week, 2003/04	
Personal care for people with dementia	**a) Low-cost provincial location**	**b) Outer London and environs**
Cost heads		
a) Staff, including employers' on-costs		
Qualified nurse staff cost per resident (excludes supernumerary managers)	0	0
Care assistant staff cost per resident (including activities)	117	139
Catering, cleaning and laundry staff cost per resident	36	43
Management/administration/reception staff cost per resident	30	37
Agency staff allowance – nurses	0	0
Agency staff allowance – care assistants	2	2
Training backfill	2	2
Total staff	**£186**	**£223**
b) Repairs and maintenance		
Maintenance capital expenditure	13	13
Repairs and maintenance (revenue costs)	6	6
Contract maintenance of equipment	2	2
Total repairs and maintenance	**£21**	**£21**
c) Other non-staff current costs at home level		
Food	17	17
Utilities (gas, oil, electricity, water, telephone)	12	12
Handyperson and gardening (on contract)	6	6
Insurance	4	4
Medical supplies (including medical equipment rental)	3	3
Registration fees (including Criminal Records Bureau checks)	2	2
Recruitment	2	2
Direct training expenses (fees, facilities, travel and materials) net of grants and subsidies	2	2
Incontinence products	0	0
Other non-staff current expenses	7	7
Total non-staff current expenses	**£55**	**£55**
d) Capital costs (14% return on capital)		
Land	33	99
Buildings and equipment meeting national minimum physical standards for 'new' homes first registered since April 2002	103	103
Total capital costs	**£136**	**£203**
Fair price for homes meeting all standards for 'new' homes in the *National minimum standards for care homes for older people* (3rd edn, February 2003)	£399	£503
Maximum capital cost adjustment factor for homes not meeting physical standards for 'new' homes	–£77	–£77
Fair price for homes which do not exceed the interim physical standards for 'existing' homes in the *National minimum standards for care homes for older people* (3rd edn, February 2003)	£322	£426

homogeneous as regards costs and conform to the 'low-cost provincial location' illustration in Tables 4-6.

For nursing care, the results of the comparison show that 69 of the 84 authorities offered maximum baseline fee rates that were lower than the bottom end of the fair fee range as calculated by the toolkit spreadsheet. None of the authorities offered baseline fees that reached the upper end of the fair fee range. Fee gaps were less marked for personal care of older people. Only 35 of the 84 authorities offered maximum baseline fee rates that were lower than the bottom end of the fair fee range as calculated by the toolkit spreadsheet. Again, none of the authorities offered baseline fees that reached the upper end of the fair fee range for personal care of older people. In the more affluent parts of England, gaps between baseline fee rates and fair fees also appear to be less marked, because more local authorities have been forced to respond to acute care home shortages. But this is difficult to quantify because costs (from which fair fees are calculated) are not homogeneous across the more affluent South East of England. There are some caveats to this analysis. For example, local authorities may in practice pay higher fees than their declared baseline fee rates. Nevertheless, there can be little doubt that there is a real and substantial gap between fees paid by most local authorities and 'fair' fees that would be generated by the toolkit spreadsheet.

The same conclusion can be drawn from Figure 4, which uses different sources for social services fees, found in local government returns to central government. In summary, the majority of local authorities are willing to pay fees which are close to the rate appropriate for care homes which have not invested in physical amenities over and above the interim minimum for 'existing' homes

Figure 4: Gap between fair fees and average fees paid by local authorities (England averages), care homes for older people (2003/04)



Sources: Average fees paid by social services were calculated by dividing 'expenditure on other providers' of care home placements for older people reported in 'Detailed personal social services expenditure by council' (www.publications.doh.gov.uk/public/pss_stat.htm#0203) by the number of supported residents reported in *Community care statistics: Supported residents (adults) England* (DoH, 2003)

incorporated in the revised *National minimum standards for care homes for older people* published in February 2003. For these homes the fee gap may be small. But no local authority in England has yet set a baseline fee rate at a level appropriate for care homes which have invested in the more demanding physical standards set for 'new' homes first registered since April 2002. For these good quality homes, the fee gap (that is, the difference between a fair fee and what the local authority is willing to pay) averaged about £80 per week for personal care and about £130 per week for nursing care across England in 2003/04, according to the data from which Figure 4 is derived.

In essence, the conclusion to be drawn is that the fees that are typically on offer from local authorities are fairly close to being adequate for unmodernised care home stock. But they are wholly inadequate to fund a modernised care home sector meeting the physical standards set by the government for new homes registered after April 2002.

Fair price ranges were calculated from the toolkit spreadsheet using estimates of England average costs.

What would a fully modernised care home sector cost?

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 can be approximated by comparing the England ceiling rates (that is, the fair fees calculated for 'new' homes) with the average gross fees paid by English local authorities, both sets of figures being taken from Figure 4. The additional cost to the public sector is calculated at £1 billion per annum at 2003/04 prices (Table 7). This figure is an approximation based on imperfect information, as described above. It is of the same order of magnitude as the corresponding figure calculated in the 2002 report, but the two should not be compared since they are not derived in the same way.

The beneficiaries of this additional expenditure would be:

- good quality care homes, whose profitability would be raised to reasonable levels;
- state-funded residents, who would have access to fully modernised facilities;
- charities and the relatives and friends of state-funded care home residents, who would no longer make third-party top-ups to inadequate local authority fees; and
- privately funded residents who would no longer cross-subsidise local authority-funded residents.

Table 7: Estimated cost to the public sector of increasing local authority fees for older care home residents in England to levels sufficient to reimburse the reasonable costs of care homes meeting physical environment standards for 'new' homes first registered since April 2002[a]

	Nursing care	Personal care	Total
a) Reasonable costs at England average prices and 14% return on capital (from Figure 4)	£578 pw	£441 pw	
b) Average fees paid by local authorities, UK 2003/04 estimate	£451 pw	£358 pw	
c) Difference (a-b)	£127 pw	£83 pw	
d) Number of English local authority supported residents[b]	74,000	126,000	200,000
Total cost of funding the difference (c x d x 52)	£489m per annum	£554m per annum	£1,033m per annum

Notes: [a] As defined in the *National minimum standards for care homes for older people* (3rd edn, February 2003).

[b] *Community care statistics: Supported residents (adults) England* (DoH, 2003)

4

Future changes in care home costs

Proposed method and health warnings

This chapter proposes a method for adjusting fees in line with cost inflation.

The proposal is that each broad cost heading in the toolkit spreadsheet should have a specific inflation factor, using information and indices set out below.

There are, however, health warnings.

All inflation indexes are historic. Therefore, if a council is seeking to set fee rates for the coming financial year in advance, it will need to project forward the relevant indices on the best available information and subsequently adjust them to re-establish a correct baseline on which the subsequent year's inflation factors are to be applied.

There is the potential for index-based cost projections to diverge from reality. Therefore, it will be desirable at regular intervals (say, every three years, or earlier if there is a significant material change such as new regulatory staffing guidance) to recalibrate the benchmark figures that have been entered in the toolkit spreadsheet. This will correct for two sources of divergence:

- where the prices of care home inputs diverge from the best available inflation index (for example, where the National Minimum Wage has a specific impact on pay rates for low-paid staff);
- where the volume of inputs changes (for example, a material change in *National minimum standards* applied by the CSCI, or some material alteration in councils' service specifications).

Staffing costs

Many long-term contracts for nursing and personal care throughout the country now build in two or more inflation factors to reflect changes in broad groups of costs. Most frequently, a wage index is applied to the bulk (50-70%) of the baseline fee and Retail Price Index (RPI) for the remainder. Although this does not capture all of the variation in rates of change in cost, it addresses the primary concern of care home operators – that use of RPI alone is bound to reduce their margins over a period of time, because labour is such a large component of cost and because labour efficiency savings are generally denied by regulatory controls on labour inputs. The particular wage index typically used in many such long-term contracts is the Office for National Statistics (ONS) average earnings index for health and social work, on the grounds that this may be expected to reflect movements in public and private pay rates most closely aligned with care home staff costs. The Index is published as series S56 in *Labour Market Trends* by the ONS.

In the absence of any other data series more closely aligned with care home staff costs, we recommend that the Council use the *Average Earnings Index for Health and Social Work* as a measure of staff cost inflation, as indicated in the toolkit spreadsheet.

However, this should be superseded where there are other, more relevant measures of staff cost inflation. In October 2004, for example, the adult rate of the National Minimum Wage will increase from £4.50 per hour to £4.85 per hour (up 7.7%). The young worker rate will increase from £3.80 per hour to £4.10 per hour (up 7.9%).

For the low-cost provincial locality illustration (see Table 1, p vii), where low pay tracks the National Minimum Wage, it would be necessary to enter a *National Minimum Wage inflation factor* in the toolkit spreadsheet specifically for non-nurse care staff and domestic staff.

In the past, the National Minimum Wage has been increased significantly every two years, with a pause in between. If this pattern continues, the inflation factor for low-paid staff in 2005/06 may be lower than average earnings inflation for the economy as a whole.

Councils should also be aware of another factor that may push pay rates for hourly paid care home staff ahead of average wage inflation adjusted for the National Minimum Wage. This is the fact that pay rates in the care sector have been held back by the financial stress experienced by operators. It is likely that any reduction in financial stress (for example, from councils paying higher fees) will trigger pressure for pay rises.

Repairs and maintenance costs

The Royal Institution of Chartered Surveyors (RICS) publishes two sets of indexes, each with a regional breakdown:

- *All-in Tender Price Index* (measures changes in tender prices per unit of building work – £ per m^2);
- *General Building Cost Index* (measures changes in material costs and wage rates in the building industry).

The two series should in theory converge in the long term. Both are available in the *Quarterly Review of Building Prices* published by RICS on a £320 annual subscription.

It is recommended that the RICS *General Building Cost Index* should be used as the inflation factor for repairs and maintenance in the toolkit spreadsheet since it is less subject to year-on-year fluctuations caused by the level of demand in the economy for building services.

Other non-staff current costs

It is recommended that the *Retail Price Index* should be used in the toolkit spreadsheet as the inflation factor for other non-staff current costs.

It is recognised that some specific items may be subject to higher inflation rates, for example, registration fees in 2004/05. But the sums involved are relatively small compared with the overall upward fee realignments proposed in this report.

Capital costs

The RICS *General Building Cost Index* (see above) is entered in the toolkit spreadsheet as the inflation factor for the buildings and equipment element of capital costs.

No inflation factor is entered for the land element of capital costs. It is recommended that a revaluation of land be part of less frequent general recalibrations of the toolkit spreadsheet (see 'Proposed method and health warnings', page 33). Meanwhile, changes in land prices should be monitored.

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Appendix:
Care home costs survey

1. Hourly rates you are currently paying to directly employed and bank staff

Grade	Shift	Average hourly pay rate[a] (£ per hour) Daytime	Night (waking)
Care assistant (No NVQ qualification)	Monday-Friday		
	Saturday		
	Sunday		
	Bank Holiday		
Care assistant (NVQ Level 2 or above)	Monday-Friday		
	Saturday		
	Sunday		
	Bank Holiday		
Senior carer	Monday-Friday		
	Saturday		
	Sunday		
	Bank Holiday		
Nurse (Level 1) (only homes providing nursing care)	Monday-Friday		
	Saturday		
	Sunday		
	Bank Holiday		
Nurse (Level 2) (only homes providing nursing care)	Monday-Friday		
	Saturday		
	Sunday		
	Bank Holiday		
Domestic and catering staff (excluding chefs/cooks)	Monday-Friday		
	Saturday		
	Sunday		
	Bank Holiday		
Chefs/cooks	Monday-Friday		
	Saturday		
	Sunday		
	Bank Holiday		

Note:[a] **Hourly pay rate** means gross hourly pay to the employee. Do *not* include NI. Do *not* include any holiday pay allowance.

2. Agency staff

During the last week, what percentage of shifts were filled by agency staff? (*tick one per category*)

a) Nurses (only homes providing nursing care)

None ❑ 1-2% ❑ 3-4% ❑ 5-9% ❑ 10-14% ❑ 15-19% ❑ 20-29% ❑ 30-39% ❑ 40-49% ❑ 50% + ❑

b) Care assistants and senior carers

None ❑ 1-2% ❑ 3-4% ❑ 5-9% ❑ 10-14% ❑ 15-19% ❑ 20-29% ❑ 30-39% ❑ 40-49% ❑ 50% + ❑

c) Domestic staff

None ❑ 1-2% ❑ 3-4% ❑ 5-9% ❑ 10-14% ❑ 15-19% ❑ 20-29% ❑ 30-39% ❑ 40-49% ❑ 50% + ❑

3. Staff turnover

What percentage of your staff do you estimate leave in the course of a year? (*tick one*)

Less than 5% ❑ 5-9% ❑ 10-14% ❑ 15-19% ❑ 20-29% ❑ 30-39% ❑ 40-49% ❑ 50% + ❑

4. Staff hours

Please state the total number of paid 'rostered' hours worked by all employed and agency staff in each grade during ONE WEEK.

[Guide: for example, a 40-bed residential home might enter 700 against care assistants, 100 against senior carers, 0 against nurses, 160 against domestic staff and 80 against chefs/cooks.]

Grade	Paid 'rostered'[a] hours per week
Care assistants	
Senior carers	
Nurses (only homes providing nursing care)	
Domestic and catering staff (except chefs/cooks)	
Chefs/cooks	

Note: [a] That is, excluding supernumerary management or training hours.

5. Sick pay

Do you offer Statutory Sick Pay only? YES ❑ NO ❑

If NO, please describe your sick pay benefits for different staff grades:

6. Holiday pay

Do you offer holidays in line with Working Time Regulations only YES ❑ NO ❑

If NO, please describe your additional holiday benefits for different staff grades:

7. Pension contributions

What employer's pension contributions, if any, do you offer staff?

Describe

8. Manager's salary

What is the salary of the manager/matron of the home? £ ____ per annum

What is the salary of the deputy or assistant manager (if any)? £ ____ per annum