Review of Sheffield City Council's
Cost of Care Exercise Consultation Report 2017

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Philip Mickelborough

Kingsbury Hill Fox Limited

07941 331322

pjm@kingsburyhillfox.com

www.kingsburyhillfox.com

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Summary

This review is of the consultation report issued by Sheffield City Council following its Cost of Care exercise in 2017.

It is recognised that it is in the interests of care homes and the Council that the commissioners should have an understanding of the actual cost of providing care.

The report is not specific about the sample used for its analysis, but it does appear to be small and unrepresentative.

The analysis used unweighted averages and took no account of resident dependency levels.

Some of the data used in the report appear to be erroneous; in particular the nursing costs.

The method of calculating the notional return on capital is not independent of the operator's personal circumstances.

The Council's plans for the way in which purchases care home places are enlightened but some of its reasoning is based on sub-optimal calculations.

If we were advising the Council we would suggest that the Council:

- repeats the exercise this year or next using an experienced organisation
- undertakes a demand projection using a formula that comprises the separate older age bands to enable the Council and its providers to plan five to ten years ahead
- uses older age bands to obtain a much more accurate comparison of local authority placement practices
- compares Sheffield with its recognised family of local authorities that are similar when 21 relevant factors are taken into account.

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1. The background

Sheffield City Council purchases care home places from independent sector providers, currently paid as one of three care only and two nursing bands. The fees payable for these bands are set by the Council annually.

For 2018/19 the Council has undertaken a "Cost of Care Exercise for Care Homes" in response to feedback from operators of care homes for older people during the 2016/17 fees consultation. The methodology was based on the template described in the January 2017 CIPFA publication *Working with care providers to understand costs - A guide for adult social care commissioners* and was discussed with providers during the summer of 2017. Data were collected from willing care home providers.

The Council published its Sheffield Cost of Care Exercise for Care Homes 2017 Consultation Report in late 2017, with a request for feedback by 9am on 15th January 2018.

An operator of care homes in Sheffield has commissioned Kingsbury Hill Fox Limited to prepare a review of the consultation report to assist in the feedback process.

2. Kingsbury Hill Fox Limited

Philip Mickelborough, who is the driving force within Kingsbury Hill Fox Limited (KHF), has been a consultant in social care for over 22 years. Although he set up KHF in 2001, until earlier this year he did the bulk of his work under LaingBuisson's (LB) name, although he has never been an employee of LB. In spring 2017 he ended his association with LB and has since worked only under the KHF name.

As well as consultancy Philip has written 15 editions of his annual market report on extra care housing, published in July 2017 by KHF as *Extra Care, Assisted Living and Retirement Communities 15th edition Market Report*, his 14 previous editions having been published by LB. LB also published Philip's 12 editions of a similar market report on domiciliary care.

Actual Cost of Care Analyses came to the fore following the Sefton judgement of 2011, when a judge ruled that Councils must take into account the actual costs of providing care locally. Since then Philip has undertaken Actual Cost of Care analyses for Lincolnshire County Council (in 2017 & 2014), Cumbria County Council, Hampshire County Council, Lancashire County Council, Leicestershire Care Association, North Yorkshire Council, Portsmouth City Council, Sefton Council and Southampton City Council.

Before the Sefton judgement Philip undertook Fair Price for Care Analyses, using benchmarked national figures for non-staff costs, for Lincolnshire County Council in 2011, Birmingham City Council, East Midlands Care Association, Gloucestershire County Council, Isle of Man Trading Standards, Lancashire County Council (2004 & 2006), Liverpool Care Association, Norfolk County Council, Plymouth City Council, *re:source* NHS Procurement Hub, St Helens Care Association, Stoke-on-Trent City Council and Wirral Care Association.

Philip's other consultancy has been:

- in strategic planning, benchmarking, market analysis, purchasing strategy, cost analysis, demand projections, acquisitions, due diligence, care tool evaluation and service strategy

- covering domiciliary care (homecare), extra care housing, nursing and residential care homes, supported living, sheltered housing, meals services, health insurance, tele-medicine & telecare, pathology, community health services, medical devices, home-from-hospital and private patient facilities

- for housing, health and care providers in the private and voluntary sectors, financial services (private equity, banking & insurance), acute & community NHS trusts, NHS commissioners, the Tynwald, private medical insurers and local authority social services.

Philip has been a non-executive director of Life Opportunities Trust since February 2014, an independent sector care body providing registered residential care, supported housing and domiciliary care & support to people with learning disabilities in Hillingdon, Hertfordshire and Westminster. He has also been a Magistrate (JP) on the Wiltshire bench since 2007.

3. Alignment of interests

In our experience it is in the care home operators' and the local authority commissioners' interest that the actual cost of providing a care home place should be known. This is why most of our Actual Cost and Fair Price analyses over the last 15 years have been undertaken with the full support of providers and commissioners.

For commissioners, this is because:

- commissioners require a sustainable care home market so that they are able to place the older and vulnerable people they are responsible for

- councils are under extreme financial pressure, and will not release extra funding to commissioners without strong evidence that it is necessary

- knowing and taking into account the actual cost of care protects the council from legal action by operators

- paying a fee that reflects actual costs reduces the likelihood of a two-tier care home market developing, with some homes providing second-rate care only for supported residents and others providing better-resourced care only for self-funders.

Care home operators benefit from local authorities knowing the actual cost of care as that increases the likelihood of councils paying a fee that reflects the cost of providing that care, and reduces the need for top-ups and for the cross-subsidy by self-funding residents.

The Sheffield City Council document *Report Supporting The Recommendations for Care Home Fee Uplifts Sheffield City Council 2017/18* strongly suggests that the commissioners recognise the needs of care homes and the inadequacy of the fees it paid in 2016/17.

4. The Council's methodology

We commend the commissioners for approaching the issue of setting its fee level by consulting with and seeking information from care home operators about their actual costs; it offers many advantages over a policy of taking the previous year's fees and uplifting them by a set amount or percentage.

In accordance with the advice in the CIPFA document, the commissioners started the cost process early and should reach an agreement by the start of financial year 2018/19; this is good as we have frequently been called in by other local authorities to advise on fees just before or after the relevant year starts.

Although the documents we have seen suggest that the commissioners genuinely do wish to understand the costs of care and pay a fair rate, for reasons we will address we do not feel that the commissioners have been as successful in understanding the actual costs of care as they might have hoped.

5. The response and the data sources

From the Sheffield City Council document *Report Supporting The Recommendations for Care Home Fee Uplifts Sheffield City Council 2017/18* we learned that there were 82 independent care homes in the City providing 3,768 beds in total, of which 18 were voluntary/not for profit homes.

For the analysis some information was provided by nine sources, relating to care homes or care home groups, out of the 12 that originally expressed an intention to participate. As we interpret the commissioners' report, the data used to calculate fees were taken from five operators that provided full accounts; three provided information that was used to calculate residential costs and two provided information for nursing costs (although the report is ambiguous and there may have been only four operators). We have concerns that:

- the report does not tell us how many care homes are represented by the five operators, although it has been suggested to us that they represent only nine homes, a sample of only ten per cent
- the report does not tell us how many beds were represented by those five operators, and therefore what they represented as a percentage of the 3,768 beds, but we are sceptical that the sample was adequate for an accurate analysis
- the report does not say whether the figures reported by the five respondents related solely to care homes within Sheffield; if they include the costs for care homes outside Sheffield the costs reported will not be local costs and so may be a poor guide to costs within the City.

The report states that subsequent reminders were issued by email and letter to those who had volunteered to participate but no further information was received. It does not say whether these were directed at only the three operators that had no responded at all, or whether efforts were made to improve the response from the six homes that provided information deemed inadequate by the commissioners.

The *Report Supporting The Recommendations for Care Home Fee Uplifts Sheffield City Council 2017/18* states the following:

> "*The providers range from small, long established operators with a single care home in a converted property, to large national organisations that run many purpose-built care homes – typically focused on areas of the city where land costs are lower. Approximately 33% of the current care homes in Sheffield are operated by large national organisations; however there are a growing number of more local organisations who have multiple care home ownership. Such a diverse range of ownership, brings with it different business models, some operate with significant debts whereas others may have very little. National providers will cross-subsidise across their homes to manage local variations in demand and profitability, these larger providers can also exploit economies of scale. "*

This confirms our view that the sample would not have been representative of the diverse range of ownership.

The difficulty the commissioners had in obtaining adequate information does not surprise us. Experience has taught us that providers are usually reluctant to disclose confidential financial information to their major customer. One of the main reasons why we are commissioned to undertake these analyses is that we can guarantee that the councils will not have access to any individual care home's information, and a major aspect of generating a good response is to reassure operators of the confidentiality of their figures.

6. The analysis

6.1 Weighting

The analysis has taken the figures from three residential care operators and averaged them; the figures from a small local private operator has been given the same weight as those from a large national one which may have many more beds in the City. Similarly, the nursing figure is an unweighted average of two operators.

Our practice is to weight the figures for each operator by the number of that operator's beds in the City, so giving more importance to operators with many beds than to those with only a few, bringing the weighted average closer to the actual costs across the City. We accept that the commissioners may not have been given sufficient information to do this, but without weighting the results have less validity.

6.2 Resident dependency levels

Nor has any account been taken of the resident mix in the homes analysed:

- residents with dementia usually require more care than frail older people
- residents admitted under NHS Continuing Care criteria usually require more nursing and more personal care
- residents with high dependency needs require more care than low-dependency residents.

Care homes in practice cannot allocate their care costs between types of residents, but we always ask for a resident breakdown so that we can determine whether the care homes are typical in their resident mix. The commissioners' report does not address this.

6.3 Allowing for inflation

Care assistant and domestic staff wages have been affected by the increase in National Living Wage (NLW) and we consider it reasonable to inflate their wages by this amount.

The change in nurses' wages is much less affected by the rise in NLW; in our experience care home operators have tended to compress wage differentials rather than maintain actual or relative differentials. Nurses' wages are affected more by the shortage of nurses, so severe that we know of many care homes that are converting from nursing care to care only because they cannot staff their homes. A higher rate for nurse wage inflation might be more appropriate, although we are unable to put an objective figure on what it should be.

The job of a care home manager has become much more bureaucratic due to CQC requirement, and we are aware from many sources that despite annual salaries that are rising faster than inflation, the role of care home manager is one which appeals to so few people that the sector is struggling to find the right calibre of staff. Although we understand the commissioners' wish to apply the same two per cent rise that they have 'enjoyed', the reality is that care home managers' salaries will have risen by more than this figure. As a guide, it is estimated that managers' salaries rose by 50 per cent between 2006 and 2016, a simple average of five per cent per annum.

7. Specific costs

We have not commented on all the costs reported in the table in the report, but only where we have some observation to make.

7.1 Nursing costs

The two nursing providers reported nursing costs of £106 and £58 per resident per week.

Both of these are substantially less than we would expect; £150 or more would be normal and we do not believe the reported figures represent the actual costs per nursing resident per week (prpw). We suggest there may be two explanations for this discrepancy:

- the care homes may have reported only the nursing costs that exceed the NHS Funded Nursing Care allowance, meaning that actual costs are £150-£155 higher than those reported

- most nursing homes accommodate a mixture of nursing and care only (residential) residents; the total nursing costs may have been divided by the total number of residents, instead of by the number of nursing residents.

Whichever explanation, or both, is true, the nursing figure cannot be considered to reflect the cost of providing nursing care.

7.2 Personal care staff

The largest single cost head, personal care staff, appears low to us when compared with other analyses we have undertaken. Nevertheless the figures are not sufficiently low to be considered necessarily outlying or erroneous.

In our Actual Cost of Care analyses we ask about hourly pay rates, skill mix (qualifications) and weekly care hours; this methodology gives a more accurate estimate of care costs.

The figures for domestic and cleaning staff appear higher than we would expect, so it may be that some of the work that would be carried out by care workers is being done by domestic staff.

7.3 Other costs

The figures reported by the care homes in the "Other costs" give no cause for comment, other than that some of them appear lower than we would expect. If these are the reported costs, however, they are the figures that should be used.

There are a number of zero figures reported, implying a cost of less than 50 pence prpw, and these appear unlikely to reflect the actual costs. Some of these are for cost heads that could not be that low. There are two likely explanations:

- the operators left this question blank, perhaps because the information was not readily available, and a blank response has been mistaken for a zero response, giving a final figure that is low
- these costs have been included in other costs heads, giving a final figure that does reflect these items.

8. Corporate overheads

Corporate overheads are a difficult factor in calculating costs on a per resident per week basis. They can represent:

- the costs of operating and managing a large number of individual care homes; to an extent these are offset by the economies of scale that a large group may achieve
- the central purchasing of what are actually individual care home costs, such as insurance, training, marketing or recruitment.

Without knowing the make-up of the reported costs we cannot comment on how reasonable they are. The commissioners' model uses a figure of 7.5 per cent for corporate overheads; if this refers to true corporate overheads (the first bullet point above) then we regard this as generous.

9. Rent/mortgage costs

9.1 Return on capital value/mortgage payments

The Council’s model uses reported figures for rent and mortgage interest.

In our view the allowance made for the operator’s capital tied up in the home, or the cost of financing its purchase, should not depend on the personal circumstances of the operator. The return should be the same whether the operator bought the home in the 1980s and has no debt, or whether he bought it last year with a 100 per cent mortgage. This is discussed in Section 9.2 below.

In our Actual Cost of Care analyses we calculate a cost per resident per week from the estimated capital employed using a rate of return of around seven per cent. This national figure comes from the percentage of the capital value that an operator would have to pay to rent a care home, or that a care home building's owner could charge when letting it to an operator. The seven per cent represents the current rate at which a leasing deal would be agreed, and is derived mainly from deals that have taken place in the south, but we have no reason to believe they would be different in Sheffield.

This method generally gives a figure that is higher than some operators pay in bank interest and lower than others do.

9.2 Why not use the actual figures provided for mortgage and bank interest?

Some may question why we do not use the actual figures provided for mortgage and bank interest. This is because we consider that the return should be independent of the capital structure; why this is so can be illustrated by some examples:

> *two brothers operate identical homes purchased with identical mortgages. They both receive a legacy from an aunt; one uses this to pay off part of his care home mortgage and the other uses the money to pay off the mortgage on his own house. Would anyone say that the Council should pay a higher fee to the latter owner because his care home mortgage is higher?*
>
> *Or a further example: neither of the above brothers receives their expected legacy, their aunt having spent all her money on care home fees. One operator has to take out a second mortgage on his care home to pay off his ex-wife as part of a divorce settlement. Once more, would anyone say that the Council should pay a higher fee to the divorcee because his mortgage is higher?*
>
> *A third example might help: a man bought his care home in the 1980s and has paid off his mortgage. The Council takes this into account and pays a low fee that reflects the absence of financing costs. One day he sells the home to another man who buys it with a 100 per cent mortgage. Under such an arrangement the new owner would be able to claim a much higher fee from the Council for exactly the same service in order to cover his mortgage costs.*

So in our view the degree of mortgage indebtedness should not affect the indicative cost of providing care; that is personal to the operator and not to the cost of care. The method we have described above effectively assumes that all the homes are 100 per cent mortgaged or leased, and that banks must be paid their interest. If they are not 100 per cent mortgaged, the return on capital represents the owner’s opportunity cost of selling the assets and investing the capital from the sale elsewhere.

10. Return on business activity

The return on capital brings the total cost/fee up to break-even level. A care home receiving this would cover its costs and be able to pay the rent or pay the bank the interest on a loan to purchase it.

There is a need for a further return, one on the business activity (or revenue cost), and this profit is needed for a range of reasons including:

- to compensate the care home operator for the time he takes running the home
- in the case of a charitable organisation, to enable it to produce a surplus to expand its services
- to reward the operator for the risk he takes in running a business rather than parking his money in a long-term investment
- to enable the operator to pay off some of the principal of the loan taken out to buy the home
- to reassure the bank or other lenders that the interest payments are well covered and their loan is secure.

Again, an example might help:

> *a man applies for a job, and at the interview asks what the compensation package is. The reply is that the employer will pay a relocation package, all his daily travelling expenses, will pay for lunch and give him an allowance for ironing his shirts and cleaning his suits. It is more than likely that the applicant would say this break-even package is not enough; he would like a salary too, to compensate him for his time and the stress of the job.*

In our Actual Cost of Care analyses we are sometimes asked to include a figure for profit. In these cases we use a percentage of the business activity component of the cost, at a variable rate that is derived from the prices at which groups of care homes are being bought and sold by corporate providers. This is the level of return that would entice a large corporate provider to open a new care home to satisfy any unmet demand.

The actual percentage varies but is substantially higher than the 2.5 per cent suggested by the commissioners in their model.

There are, however, arguments for councils to offer a return on business activity that is less than the full percentage:

- a council's primary aim may not be to entice new corporate providers into the market but to ensure that its current provider market survives and if necessary expands capacity by extensions to satisfy future increases in demand
- private operators benefit in the long term from the capital appreciation of their property asset, a factor that is not factored in by corporate providers and their shareholders.

11. Other factors

11.1 Quality of care

In most of the Actual Cost of Care analyses we undertake providers tell us that the fees that their local authorities pay are constraining the quality of care that they can offer; that although the homes are managing on the fees paid they are not delivering the level of care that residents deserve.

It is for the commissioners to decide whether they are willing and able to pay for better care, or whether they are content with a service that is acceptable to CQC. While higher fees would allow an operator to pay better wages or employ more staff, it is not proven that paying higher fees will increase the quality of care provided.

11.2 Supply, demand and occupancy rate

The CIPFA document referred to above states that:

> *"The market in the city has remained fairly stable over the previous 12 months, however there continues to be a significant demand for places and the occupancy of care homes remains relatively high. If the demand increases or the capacity reduces there is a risk there will be insufficient places at the right quality and price for the people who need them."*

We are informed that occupancy rates in Sheffield care homes are now in the mid-90 per cent range. This is high by national standards, and in our view above the long-term sustainable level.

When there is a shortage of supply care home owners will naturally prefer full-price self-funding residents over supported ones unless substantial top-ups are available; the commissioners may find it difficult to place their less wealthy clients in any care home.

12. The Council's plans for purchasing

12.1 Simplifying fee structure

The commissioners suggest replacing the three care only and two nursing fee bands with one band for each. While we do not know the providers' views on this, we recognise the advantages of a system that is:

- simpler
- avoids having to assess unstable residents on or just before admission, knowing that admission itself may change their care needs
- eliminates the need to re-assess residents during their stay
- eliminates the need to make subjective judgements on care homes.

The disadvantage for providers, as far as we can see, is that some providers may 'cherry-pick' the least dependent residents leaving others with more expensive ones.

12.2 Reducing placements

The commissioners recognise that they made more care home placements (both residential and nursing) per 100,000 population in 2016-17 compared with other councils in the Yorkshire and Humber region. Only two out of 13 comparator councils made more placements.

While we fully agree that alternatives to care homes, such as extra care and intensive homecare, should be used where possible, we have two comments on the commissioners' calculation:

- we would not use the general population as the comparison group; we would use a method comprising the separate age bands 65+, 75+ and 85+ to obtain a much more accurate comparison of placement practices

- we would not compare Sheffield with its 13 geographical neighbours, but would use its recognised family of local authorities that are similar when 21 relevant factors are taken into account.

13. The way forward

If we were advising the Council we would suggest that the Council:

a) repeats the cost of care exercise this year or next using an experienced organisation that:
    - can guarantee that the care homes’ data will be kept confidential and not disclosed to the Council
    - has the resources to chase up non-responders and clarify all ambiguities, query outlying figures, correct errors and enquire about missing pieces of data
    - will enquire about costs in greater depth than the CIPFA template
    - will give all care homes in Sheffield the opportunity to contribute to the analysis
    - can give participating care homes a confidential comparison of their costs with the City averages, so that they can see where their costs are high and take measures to control them

b) undertakes a demand projection using a formula that comprises the separate age bands 65-74, 75-84 and 85+ to enable the Council and its providers to plan five to ten years ahead

c) uses more specific age bands to obtain a more accurate comparison of local authority placement practices

d) compares Sheffield with its recognised family of local authorities that are similar when 21 relevant factors are taken into account.

Kingsbury Hill Fox Limited is one of the organisations that could do all of these, and has done so for many local authorities.