HealthInvestor round table

Living with the living wage:

Can the care sector survive George Osborne's wage commitment?

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Can the care sector survive George Osborne's wage commitment?

George Osborne succeeded in dropping a bombshell on the care sector in the first Conservative Budget for 18 years with the announcement he will introduce the 'national living wage'. From April 2016 the care sector is expected to pay staff aged 25 and over £7.20 an hour, going up to £9 an hour by 2020. It's great news for carers, and long overdue, but given that providers are struggling to make good care and paltry local authority fees add up as it stands, the chancellor's proposition could well prove disastrous.

Staff costs are central to almost all care businesses, and naturally providers are hoping that wage increase costs will be passed on to them via a hike up in local authority fees for services. But no one is holding their breath. There is already a £700 million funding gap in adult social care and calculations by the Local Government Association indicate living wage will cost English councils an extra £330 million next year rising to £1 billion by 2020. In the face of such fearsome figures, what are providers to do?

So far, five of the biggest care home groups in the UK – Four Seasons Health Care, Bupa, HC-One, Care UK and Barchester Healthcare – have lobbied Osborne claiming the care sector is at risk of "catastrophic collapse". Meanwhile the UK Home Care Association told government the "continued supply of state-funded home care will become unviable".

To debate the issue, HealthInvestor and leading law firm Charles Russell Speechlys brought together the leading social care providers, investors and financiers to consider how the sector can survive the introduction of living wage.

Vernon Baxter: Ian, the National Living Wage felt like a very politically-motivated announcement. To what extent did it come out of the blue?

Ian Targett: It did in some respects. If you remember back before the election, Miliband said there was going to have to be a step change in the base rate of hourly wages. And Osborne indicated that he was keen to see wages increase as well. He didn't of course come out and say anything as categorical as this commitment, but it's all part of a project to take the centre ground of politics. Obviously that has to be seen in a context of Labour veering to the left – even before the election and what has followed. It's also part of Osborne's objective to rehabilitate himself personally, so that he's the person that's associated not with swingeing cuts but with getting the economy back on track, getting the public finances in order and then the final pillar of that is essentially spreading prosperity to more people. The judgment was, principally, let's transfer the cost of tax credits effectively onto the private sector, onto employers.

Vernon Baxter: Are you picking up whether or not the Treasury is listening to the concerns raised by the sector about its impact?

Ian Targett: The message is being heard in DH and the Treasury are aware of some of the ramifications of it. There's another part in government that certainly should be aware from a risk management perspective and that is Number 10 and the Cabinet Office. They're absolutely crucial audiences in this because that's part of the nexus of government right at the top that is dealing with policy, spending and then reputational risk issues. How genuinely and sincerely Treasury are listening and whether they're minded to act on it are two separate things. There are also clearly difficulties in putting extra funding in and being sure that it actually ends up reinforcing the care sector.

Michael Lingens: And so, on that score Pete, did you and the other leading sector CEOs get a reply to your letter to the Treasury?

Pete Calveley: We received an acknowledgement that they would organise a meeting, which we've had since. There has been some quite co-ordinated lobbying that's trying to get through to all the different stakeholders Ian mentioned.

My sense is that over time we are being heard. Initially it seemed a little superficial and the ramifications of the risk weren't quite clear to them and they felt, like any other sector, you can either increase your prices or become more productive. Which to be honest in most sectors, with low pay, you can. Other sectors can fix their prices and if everyone's affected they'll all put their prices up and they can all become more efficient. Our main customers are local authorities who fix the prices and have no money. So we can't put our prices up and they can't pay more, currently. Secondly we can't cut our staffing because it's regulated by the CQC.

But the polarisation in the market is not just because of the Living Wage issue. We've had five years of real reductions in fee rates. So over that period, providers have put inflationary increases on to their private pay fees, which has subsidised the below inflationary increases for publicly funded clients. In many parts of the country, the proportion of private pay is below 10%. We have submitted to Treasury as part of our discussions the proportion of each of our homes that would have a margin below a certain amount before the Living Wage is factored in and which become unprofitable on a cash basis if the Living Wage is unfunded. And it was a very significant proportion.

Vernon Baxter: Josie, how difficult is it for government politically and financially to concede ground on an issue like this?

Josie Irwin: It's probably the most difficult negotiating environment at the moment that I've experienced in the last 20 years. Because of the demands and the pressures that are on both the NHS and social care sector, that's a big area of public spending and the government is finding it difficult to square the circles. My concern as a negotiator is about where the money might be found in order to either deal with some of these issues we're discussing this morning. Efficiencies will have to be found somewhere and there will be repercussions in terms of how much nurses and healthcare assistants are paid and what that pay package looks like. We welcome the introduction of the National Living Wage but we do have to be realistic about how that's impacting on social care providers and at the end of the day we want our members to have jobs, and we want them to be paid in those jobs.

Vernon Baxter: Mike, Christie + Co has looked at the nursing sector quite a lot recently – what impact will this have in reality?

Mike Hodges: We were talking about a shortage of qualified nurses earlier in the year, which is one side of the care home sector. The other side is everyone else. The care assistants, the domestics, everyone, which is the engine of those care homes. We've got real pressure points on both sides. Then you have a differential knock on effect above that which hasn't really been spoken about. If you're paid 20p or 30p an hour more than someone below you, will you feel disenfranchised if they just put the base level up and they don't move you? It's a really difficult thing for employers. The other impact is actually lack of investment in the care homes. A lot of care homes that we're seeing now have been starved ▶

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of investment for years. And with a very proactive regulator drilling down on their care they're delivering with the acuity levels of the residents getting higher as well, it really is almost a perfect storm.

Michael Hill: Mike is right, you need to look at the differentials. Because if you've got a 24 year old who manages a 25 year old, who gets a pay increase, and is now paid more than them, what is the 24 year old going to want? They're going to want to have an increase as well.

Michael Lingens: In terms of pricing, is it easier for a specialist provider like CareTech to adjust prices upwards than for example in the elderly sector?

Michael Hill: There are two ways that the price can change. The first is the 1 April annual review. And I'm sure the people around the table will have the same issues and difficulties that we have in that process. Over the previous five years of the last government the thrust of that was negative for the first few years and has only recently come to being slightly positive as an annual review. The only other area is new services. But there's almost certain to be a slowdown on new services because people won't be investing.

Alison Rose-Quirie: I agree and in this sector you're not going to be able to move to the private pay market because there simply isn't one. If you've got severe autism, the likelihood is that you're going to be in care of one sort or another for all of your life. So a number of people that we've got have been there for a long time. And of course the fee rates haven't kept pace with the cost increases, so you're actually looking at legacy fee rates. For us it's not necessarily so much the impact of the National Living Wage, it is the differential. What concerns me is that the Treasury will address the National Living Wage but they won't take into account the differentials.

Vernon Baxter: It would be interesting to hear the perspective from domiciliary care, because clearly that's a sector that's had its run-ins with the government on minimum wage already.

Tim Pethick: We too are caught in the same bind. We can't put our prices up. And as everybody knows, money has come out of home care over the last five years, and there's been an increase in demand for services and that's put significant pressure on prices. Nor can we introduce efficiencies or productivity gains in our cost structure – 75% of our cost structure is our staff cost. Talking to Treasury last week, they've heard the arguments. Interestingly the message I got was they don't necessarily believe it will be as drastic as everybody says. In fact the words they used was 'we've heard it all before in different industries'. So there's a disbelief I think on Treasury's part that actually the consequences are going to be as drastic as potentially they are and I think that's because they don't have a detailed understanding of the issues or the sector. At a high level you can say 'oh we'll just shift people from one home to another home'. It's easy to say that if you take the people out of the equation.

We along with all large providers in the home care sector have been busily handing back contracts over the last 12 months where they're not profitable. And that's accelerating. In our case, it's nearly 40% of our workforce is affected by the National Living Wage. Currently by 2020 it'll be 80% of the workforce. The impact in our business alone by 2020 will be nearly £30 million a year of additional cost. Without some sort of mitigation that's completely unsustainable.

Vernon Baxter: Michael, can you see some of these arguments ending up in court?

Michael Lingens: Under the Care Act, local authorities have wide ranging obligations to promote diversity and quality in the provision of services, which are underpinned by very detailed statutory guidance. I'm reading now from the guidance that took effect in April – 'that [local authorities] should have evidence that contract terms and fee levels for care are appropriate to

provide the delivery of agreed care packages with agreed quality of care and will allow the service provider to pay at least the national minimum wage'. It's pretty clear there that local authorities are between a rock and a hard place. Some local authorities commissioned independent reports on the 'cost of care' in the past, including one from KPMG in Solihull (and more recently Birmingham), that encouraged them to put up their fees by around 15%. But if they haven't got the money, they haven't got the money. Given that the new obligations are so specific, a test case here or there might unlock the logjam.

Aly Kachra: We're in judicial review proceedings against Sheffield City Council at the moment under the pre-Care Act regulations. One of the issues that we've found is that you'll get providers willing to provide care at a certain price as occupancy is the key for them. They're willing to take those risks that other businesses wouldn't take. The judicial review route against a lot of local authorities could be very successful but, from my own personal experiences it's very, very hard to convince a lot of smaller providers that that is a positive way forward.

Pete Calveley: On your point about the smaller providers looking for occupancy in desperation, that always in my view leads to a failure of the service. Because they start taking inappropriate placements that they don't have the skill set to look after. That to me is evidence of the unsustainability of the commissioning.

Aly Kachra: One of the major pieces of work we've done over the last few years in our business is acquiring homes that are struggling. And I wonder how much that's going to be impacted by the Living Wage also because the opportunity to actually recover those businesses, to invest in them, to bring them to a quality sufficient to be able to provide a service is going to be diminished.

David Jones: It's interesting, we're talking about living wage here but there's a lot more pressures in addition to living wage, whether it be the shortage of nurses or agency costs. And then you've got on top of that the regulatory burden so – as Mike said – it does feel like a perfect storm at the moment.

Pete Calveley: The CQC have just released figures of home closures or de-registrations. There's been over a thousand homes de-registered over the last two and a half years. Which is a huge number. Not a thousand beds, a thousand homes.

Aly Kachra: The CQC play a major part in this as well. I don't know what other people's experiences are of inspections over the last sort of 12 months under the new regime, but a lot of ours point towards staffing levels, and there's a lot of observation work from the CQC and a lot of that tends to conclude that staffing levels may not be sufficient.

Alison Rose-Quirie: It's not only the staffing ratios, it's also the staff training. The only people who are getting funded now for residential placements are the increased acuity and increased complexity cases, and of course the CQC are then coming in and judging you on how you deliver that service. But we haven't had the time or the resources to actually bring the staff up to be trained sufficiently to deal with the challenging behaviour. So you've got a huge mismatch there and I think the pressures from CQC are just going to make things worse. There are some local authorities that we're talking to now that are starting to realise their responsibilities under the Care Act and they are starting to talk about giving a premium onto the fee rate to address things like staff training. So I think there are some green shoots in terms of local authorities' attitudes.

Tim Pethick: There's no doubt there are a number of local authorities who are stepping up to the mark and increasing rates in an unprecedented way. Equally there are a number of local authorities who would love to do something about it but just can't. And I think that's the real issue. There's a huge number of local

authorities that would be prepared to do something but just don't know how. They can't balance the books. So it's not a lack of willingness or a lack of understanding of the issues. It's simply a lack of money.

Vernon Baxter: I'm interested whether or not the group thinks the National Living Wage will act as a catalyst or a hindrance to the wider goal of integrating healthcare and social care?

Pete Calveley: What tends to catalyse public sector organisations is cost impacts to themselves. The Living Wage, we're all aware, is probably not such a big issue for local authorities and NHS bodies. When there's no driver from that and the problem sits with the private sector largely, then I don't see that catalysing behavioural change or organisational structural change.

David Jones: My worry is a lot of people are hanging their hat on something being said on 25 November which is going to solve the problem and actually, although I'm sure we'll have a statement, it'll be something quite broad, quite woolly.

Pete Calveley: They will say something about social care but even if there is a real intent we won't know what that means unless they describe the vehicle of delivery because we don't get our settlements until April, May, June, October. So by which time the cost has come in and we don't know how much we're going to get to fund it.

Vernon Baxter: So what's it going to take before action has to be taken?

Tim Pethick: I don't think a spectacular collapse will necessarily mean action because I think government will inevitably point their finger at the private sector operators and say well you got it wrong. I don't think there's any general acceptance that it's the marketplace environment that's creating these issues. I think they perceive it as greedy private sector operators who are cutting corners and cutting costs and getting it wrong.

Pete Calveley: Genuinely, we hope we've made our case. I agree with you, you can be cynical, but genuinely there is a case to be made.

Tim Pethick: There's no doubt there's a genuine case. We've provided figures in confidence as well. There's certainly no notion that this is crying wolf in reality. The perception is disconnected to the reality of the situation. What we've got to do is get those two things in the same place before we're going to get any sort of real change or engagement. It seems to me all roads lead to the NHS – that's the fundamental backstop. Once the care sector starts collapsing, inevitably the NHS is going to have to pick up the cost of that. ■

The above is an edited transcript and is not reported verbatim. The panel met in central London on 15 October 2015.

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THE FINAL WORD

The background to the living wage debate in our sector is that, while the living wage may be a 'good thing' in policy terms for low paid employees, the cost increases which will result for most operators come on top of many years of public sector fee levels remaining flat or declining in real terms. Coupled with staff shortages and excessive agency fees and a regulatory environment that is (rightly) trying to drive up the quality of care, these extra staffing costs might drive some operators out of business.

The lobbying efforts of the 'big 5' residential care home operators may be getting through to the Treasury, especially as they have shared profit margin details that show that in some parts of the country where there is a greater reliance on public sector funding, many homes will simply become unprofitable.

It is also worth saying that the picture is a bit more differentiated across the sector. Wage levels are already high in the south east and operators who have a high proportion of private pay customers or who provide a high degree of care specialism (such as in the high acuity learning disability and mental health areas) may have some flexibility to adjust fee levels. This market polarisation is reflected in M&A activity and pricing. But the picture is looking bleak for those operators (including one or two of the very large ones) who rely heavily on local authority and NHS funding or who have very high staffing costs (such as the domiciliary care operators). What will it take for the government to listen? Perhaps it will be the reputational risk to government of a string of business failures, especially if these back up on to the NHS, which is already struggling to cope. Or possibly some successful judicial reviews under the Care Act that will encourage local authorities to re-prioritise spending or pass the pressure back up the line to central government. But all this will take time and even if the Chancellor makes some gesture to the sector in the CSR on 25 November, the mechanism for delivering extra funds quickly to social services budgets is uncertain.

Although the phrase is sometimes over-used, many parts of the sector are looking at a 'perfect storm'. ■

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