Title: Universal deferred payment scheme	Impact Assessment (IA)
IA No: 7084	**Date:** 08/05/2013
	Stage: Final
Lead department or agency: Department of Health	**Source of intervention:** Domestic
	Type of measure: Primary legislation

Summary: Intervention and Options

Cost of Preferred (or more likely) Option				
Total Net Present Value	**Business Net Present Value**	**Net cost to business per year** (EANCB on 2009 prices)	**In scope of One-In, One-Out?**	**Measure qualifies as**
£254m	£0	£0	No	NA

What is the problem under consideration? Why is government intervention necessary?

People who have to pay for residential care (self-funders) often find it difficult to draw on their housing wealth in a timely and flexible manner. Each year, about 35,000 people are at risk of having to sell their home to pay for residential care. This creates anxiety and stress in an already difficult period in people's life.

Private equity release products are often not suitable in these circumstances. Since 2001, local authorities have discretionary powers to defer self-funders' residential care fees against a charge on property. However, provision of these deferred payments is patchy, as local authorities can set their own eligibility criteria and cannot charge interest, thus making a loss on every deferred payment.

What are the policy objectives and the intended effects?

To ensure that no one has to sell their home in their lifetime to pay for care. By placing a clear duty on local authorities to offer deferred payments under certain conditions and setting clear parameters for local implementation, the scheme aims to give homeowners peace of mind and a wider array of choices when going into residential care.

What policy options have been considered, including any alternatives to regulation? Please justify preferred option (further details in Evidence Base)

Two options have been considered:

Option 1 – Do nothing: retaining the current, voluntary local authority scheme. This will not improve access to deferred payments or similar products. A large number of people will remain at risk of having to sell their home.
Option 2 – Universal deferred payment scheme: this is the preferred option. It clarifies the rules that should apply in implementing deferred payments and makes it mandatory for local authorities to give anyone who cannot afford reasonable residential care without selling their home the choice to defer their care fees. It also allows authorities to charge interest.

Will the policy be reviewed? It will be reviewed.					
Does implementation go beyond minimum EU requirements?			N/A		
Are any of these organisations in scope? If Micros not exempted set out reason in Evidence Base.	**Micro** **No**	**< 20** **No**	**Small** **No**	**Medium** **No**	**Large** **No**
What is the CO$_2$ equivalent change in greenhouse gas emissions? (Million tonnes CO$_2$ equivalent)			**Traded:** /		**Non-traded:** **/**

I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.

Signed by the responsible Minister: Norman Lamb MP   Date: 8 May 2013

Summary: Analysis & Evidence   Policy Option 2

Description: Universal deferred payment scheme – FULL ECONOMIC ASSESSMENT

Price Base Year 2010	PV Base Year 2014	Time Period Years 10	Net Benefit (Present Value (PV)) (£m)		
			Low: 68	High: 266	Best Estimate: 254

COSTS (£m)	Total Transition (Constant Price) Years		Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)
Low	Optional		Optional	Optional
High	Optional		Optional	Optional
Best Estimate	/		11	**112**

Description and scale of key monetised costs by 'main affected groups'

Opportunity cost of government provision of deferred payments, net of repayments.
Reduction in these costs as interest will be charged.
Administration costs of operating a deferred payment scheme.

Other key non-monetised costs by 'main affected groups'

Set-up costs in local authorities that have little or no deferred payments at the moment.

BENEFITS (£m)	Total Transition (Constant Price) Years		Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)
Low	Optional		Optional	Optional
High	Optional		Optional	Optional
Best Estimate	/		36	**366**

Description and scale of key monetised benefits by 'main affected groups'

Reduction in anxiety and stress for self-funders going into residential care.

Other key non-monetised benefits by 'main affected groups'

Wider peace of mind benefits to all (potential) self-funders.
Social valuation of financial benefits to homeowners.

Key assumptions/sensitivities/risks	Discount rate (%)	1.5/3.5

Pressures on the housing market, as additional homes remain unoccupied (see p28 -30).
As set out in DH Impact Assessment guidance, this summary sheet does not present financial costs only, but total costs to society including an estimate of the opportunity cost of government spending. For details, please see paragraphs 164 – 171 in the main body of the assessment.
Value of a Quality Adjusted Life Year: £60,000; discount 3.5% (financial costs),1.5% (health benefits)

BUSINESS ASSESSMENT (Option 2)

Direct impact on business (Equivalent Annual) £m: £0m			In scope of OIOO?	Measure qualifies as
Costs: £0m	Benefits:£0m	Net: £0m	No	NA

Evidence Base (for summary sheets)

I - Introduction

1. Each year, approximately 55,000 people in England enter residential care as a self-funder. This means that they have more than £23,500 in assets and therefore, under the current charging rules for residential care, they are liable to pay for all of their residential care fees.

2. However, for many people, the value of their home is a large fraction of their overall assets. For this reason, as many as 35,000 people each year may have to rely on their housing wealth to pay for residential care. For them, it is often difficult to draw on their housing wealth in a timely and flexible manner and they may have to sell their home to pay for care. This creates anxiety and stress in an already difficult period in their life.

3. Since 2001, the Department has promoted a deferred payment scheme, in which local authorities have discretionary powers to defer self-funders' care fees. In other words, the authority pays the self-funder's care fees, but, in exchange, it puts a charge on their property and recovers this charge once the property has been sold.

4. However, the current scheme is discretionary and there is wide variation in both the number of deferred payments offered in local authorities as well as in the eligibility conditions attached to local schemes. Therefore, only about 4,000 people each year take up a deferred payment.

5. The Care Bill contains provisions for a universal deferred payment scheme. All authorities will have a duty to offer deferred payments, with consistent rules for who is eligible, what fees they can defer and for how long. The intention is to give people peace of mind, choice and control when they enter residential care and to ensure that no one has to sell their home in their lifetime to pay for care. This impact assessment (IA) assesses the costs and benefits of the proposed scheme. Where appropriate, the IA discusses the Department's preferred specification of the scheme.

6. However, the details of the scheme will be subject to further consultation in the summer and will be set out in regulation at a later point. As part of the consultation, the Department will seek further evidence on the costs and benefits of the scheme, potential impacts on people sharing protected characteristics (under equalities legislation) and issues for implementation. The costs of the scheme will be kept under review throughout implementation to take into account emerging evidence, for example on demand under a universal deferred payment scheme.

7. The remainder of this impact assessment will
   - Set out the problems faced by people who have to sell their home to pay for care (section II);
   - Present proposals to address these problems through a universal deferred payment scheme (section III);
   - Assess the impacts of the proposals on the availability and number of deferred payments and the resulting costs and benefits, as well as risks (section IV).

II – Background: Description of the problem and reasons for intervention

8. The objective of the proposed universal deferred payment scheme is to ensure that no one has to sell their home within their lifetime to pay for care. This section sets out how many people are at risk of doing so and what negative outcomes they face:
   - Each year, about 35,000 people are *at risk* of having the sell their home to pay for residential care;
   - For practical reasons, they may find it difficult to sell their home quickly;
   - Selling one's home to pay for care causes stress and anxiety for people who are already at a difficult and vulnerable stage in their life.

1. The problem: some people have to sell their home to pay for residential care

1.1 Scope: 35,000 people at risk

9. To estimate the number of people who need to sell their home to pay for residential care we consider the number of people who
   - Enter care each year as self-funders; and
   - Would meet the local authority needs test; and
   - Have savings below £23,500.

10. The Department's social care funding model estimates that, in 2012, approximately 55,000 people[1] entered residential care as a self-funder (see annex A for an explanation of the model). Under the charging rules for residential accommodation (CRAG), they are liable to pay their full residential care fees[2].

11. Under the proposed scheme (as well as under many current local authority deferred payment schemes), self-funders would not be eligible for a deferred payment if they had more than £23,500 in savings. Anyone above this threshold could typically afford to pay for a year of residential care out of their savings, without having to draw on their housing wealth.

12. Excluding this group, the *social care funding model* estimates that about **35,000 people each year are at risk of having to sell their home to pay for care,** either immediately when entering residential care or over the course of their time in residential care. This is about two thirds of self-funders (=35,000/ 55,000).

13. Because the need for care is usually unpredictable while people are in reasonable health, all homeowners who *might* turn out to need residential care in their later life are theoretically at risk of having to sell their home if this happens.

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[1] This estimate is based on figures for 2012. Over time, demand for deferred payments is expected to change in line with the overall self-funder population in residential care. This, in turn, is driven by demography – see section IV.1 for our best estimates of the take-up of deferred payments over time.

[2] This excludes people whose home is occupied by a spouse (or dependent relative), as they are not required to draw on their housing wealth to pay for residential care.

1.2. The problem: difficulties when drawing on housing wealth

14. Self-funders may find it difficult to draw on their housing wealth to pay for care. This is because a house is **a lumpy asset**, which cannot be easily subdivided. As a result, people have to give up ownership of the whole house, even if they only use part of its value to pay for care.

15. In addition, housing wealth is relatively **illiquid**, so that selling one's home is not always possible at short notice. The charging rules for residential care acknowledge this by exempting housing wealth for anyone's first twelve weeks in residential care, providing they meet certain criteria[3], so that people do not have to sell their home in that time.

16. However, in many cases, it is difficult for people to sell their home within twelve weeks. When going into care, people may not be able to put their home up for sale immediately because:
    - Going into care often happens in a crisis with little time to plan the sale;[4]
    - People may not always know whether they will stay in care indefinitely;
    - Putting the house on the market may require preparation (e.g. emptying and preparing the home);
    - The homeowner may lack capacity to manage the property and legal arrangements may be necessary (e.g. giving power of attorney to their children).

17. Then, once the home is on the market, it takes an average of ten weeks to sell. In some regions, the time it takes to sell a house is even substantially longer: 13.6 weeks in the East Midlands and 11.6 weeks in the North West.[5] Finally, after the sale is agreed, it will take some time until it is finalised and money is received. As a result, people will often find it difficult to draw on the value of their home within twelve weeks, even if they want to sell it.

1.3 Negative outcomes: increased anxiety and potential financial loss

18. Given these difficulties in drawing on housing wealth in a flexible and timely manner, self-funders may face a range of negative outcomes:
    - Having to sell one's home, in particular in a rushed way, may add to the anxiety and feeling of loss often associated with this period in life;
    - It may also result in financial disadvantages to the homeowner (e.g. rent foregone).

Additional anxiety/ stress due to having to sell one's home when going into residential care

19. Transition into residential care can be a demanding process for clients and families. Glendinning et al (2008) suggest *"older people often approach services at a time of crisis when they feel vulnerable or unwell and find decision making difficult".[6]* Indeed, a recurrent theme in studies about moving into care is one of "stressful reaction, likened to the experience of loss and grief, (…)

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[3] The authority must have assessed residential care needs and must have less than £23,250 in assets excluding their home.

[4] Glendinning et al (2008): Evaluation of the Individual Budgets Pilot Programme: Final Report

[5] Hometrack 2012: Monthly National Housing Survey, http://www.hometrack.co.uk/hpsurvey/documents/RDHTSurveyDec2012CMS_21122012153607.pdf

[6] Glendinning et al (2008): Evaluation of the Individual Budgets Pilot Programme: Final Report

potentially as traumatic as divorce or death in the family"[7]. Moving into a care home has been associated with what is sometimes called the "relocation stress syndrome" – which involves symptoms such as anxiety, depression, apprehension, loneliness and increased confusion, as well sleep disturbances, weight loss and gastrointestinal upset.[8]

20. In this situation, to sell one's home requires additional decisions and organisational effort and may further contribute to feelings of anxiety and stress. Having to sell one's home is also likely to be a significant source of emotional distress in itself as a home is not only of financial, but also of significant emotional value. In addition, being forced to sell one's home may reinforce feelings of powerlessness and loss of decisional autonomy, which contribute to depression among people in care homes.[9]

Foregone financial benefits

21. Having to sell one's home in a rush may also result in financial losses as people sell their home for a lower price than otherwise possible. For instance, quick sale property agents offer to buy any property as quickly as within a week, but usually pay prices up to 25% below market value.[10] In addition, some people may prefer to keep their property because they expect it to appreciate over time and to generate revenue, e.g. by renting it out or allowing a relative to live there rent-free (with a benefit equivalent to the rent occurring to the relative).

22. It should be noted that these financial benefits fall on the individual taking out the deferred payment. At the same time, there will be corresponding losses to someone else (such as the prospective buyer, who could have acquired the property below market value). Thus, from a societal perspective the *net financial* impact is zero.

23. However, society may have a preference to allow homeowners to fully benefit from their lifetime savings, even if this implies that others will forego the benefits of owning or using their home. Indeed, it can be argued that deferred payments address an underlying distributional problem: while homeowners continue to pay a contribution towards their residential care fees as defined in the charging rules, the deferred payment ensures that they do not face additional dis-benefits such as the loss of their home.

1.4 Reasons for government intervention: no market provision and variable public provision

24. The previous sections have outlined the basic problem: self-funders who go into residential care have to use their housing wealth, which is often illiquid and cannot be drawn on in a flexible way. As a result, they may find themselves forced to sell their home to pay for care. This may lead to additional anxiety and stress in what is already a stressful situation.

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[7] Newson, Pauline 2011: At home then away: supporting new residents as they settle in, in: Nursing & Residential Care 13(1), p32-35

[8] Jackson et al (2000): Bridge of continuity from hospital to nursing home – Part 1: a proactive approach to reduce relocation stress syndrome in the elderly, In Continuum 20(1), p3-8: and: Mallick and Whipple 2000: Validity of the nursing diagnosis of relocation stress syndrome, in Nursing Researcyh 49(2), p97-100

[9] Boyle, Geraldine 2005: The role of autonomy in explaining mental ill-health and depression among older people in long-term care settings, Ageing & Society 25, p731-748

[10] Tornsey, Chris 2012: Quick-sale property firms could cost you thousands, http://www.confused.com/mortgages/articles/quick-sale-property-firms-could-cost-homeowners-thousands-of-pounds

Lack of equity release products for people going into residential care

25. One solution to this problem could be equity release. Equity release is a financial product that allows people to draw on their fixed assets, for instance to pay for (domiciliary) care. However, the equity release market does not offer products aimed at people in residential care to protect them against selling their home.

26. Market research shows that equity release products, as they are currently offered, are "unlikely to be suitable for meeting residential care costs"[11] for a number of reasons:
    - Many people going into residential care would not qualify for equity release products, because their property would not be occupied;[12]
    - Equity release products cap lending at a certain proportion of assets and, therefore, many users would not be able to borrow the cost of an average stay in care.[13] This means that clients would still be subject to the risk of having to sell their home for care;
    - Equity release usually does not offer small and incremental loans (which might be most suitable because length of stay in residential care is uncertain).Instead, typical loans consist of large withdrawals of at least £10,000, which increases the cost of the scheme to borrowers.[14]

27. In addition, there are other well-documented demand barriers to equity release. There remains public mistrust of commercial equity release due to perceptions that it is expensive and due to mis-selling problems in the past. Rightly or wrongly, these may make equity release a difficult option for people moving into residential care. The Government is interested in seeing improvements in the market including more flexible and affordable products to help with care costs. However, its assessment, at this stage, is that equity release is not a general solution for residential care users who have to sell their homes.

Current public provision of deferred payments is patchy

28. In response to these problems, since 2001, the Department has promoted a deferred payment scheme, in which local authorities have discretionary powers to offer deferred payments (deferrals). In simple terms this involves:
    - The authority is in a situation where it would charge for residential care but the person cannot or does not want to sell their home to pay for this;
    - The authority defers the payment so the person can instead pay later on;
    - In return, the person agrees to a charge on their property to secure the debt;
    - The person then repays the debt once they have sold their property.

29. From 2001 to 2004, the Government also provided a total of £85m of funding to local authorities to facilitate them to offer deferred payments.[15]

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[11] Hosty, Ged 2012: Meeting social care needs, in: Making the most of equity release: perspectives from key players, The Smith Institute, p51-57

[12] Hosty, Ged 2012: Meeting social care needs, in: Making the most of equity release: perspectives from key players, The Smith Institute, p51ff

[13] Products lend a maximum loan to house value (LTV) ratio. For disabled and older clients the terms can be quite favourable, lending up to 50% of housing equity. However, many clients are unable to borrow the cost of an average stay in residential care particularly those with less valuable homes.

[14] Terry, Rachel 2012: Asset-rich, income-poor, in: Making the most of equity release: perspectives from key players, The Smith Institute

[15] Grant allocations of £15m in 2001/2; £30m in 2002/3; £40m in 2003/4.

30. Provision of deferred payments is largely discretionary, in that authorities have powers rather than duties in this area. Department of Health guidance asserts that authorities may be acting unlawfully if they offer no deferred payments at all, but that the decision to offer a deferred payment in any particular case is ultimately a matter for the authority.[16] The Department has issued this guidance partly in response to long-running concerns that authorities were not offering deferrals on the scale the Department had envisaged.[17]

31. However, provision of deferred payments among local authorities is still patchy, with some local authorities providing hundreds of deferred payments and others none at all. In addition, local deferred payment schemes can have very different rules, for instance on loan to value ratios and occupation of the home.

Figure 1 – Number of deferred payments by authority, from a 2012 survey by the Department (DH), the Association of Directors of Adult Social Services (ADASS) and the National Association of Financial Assessment Officers (NAFAO)[18]
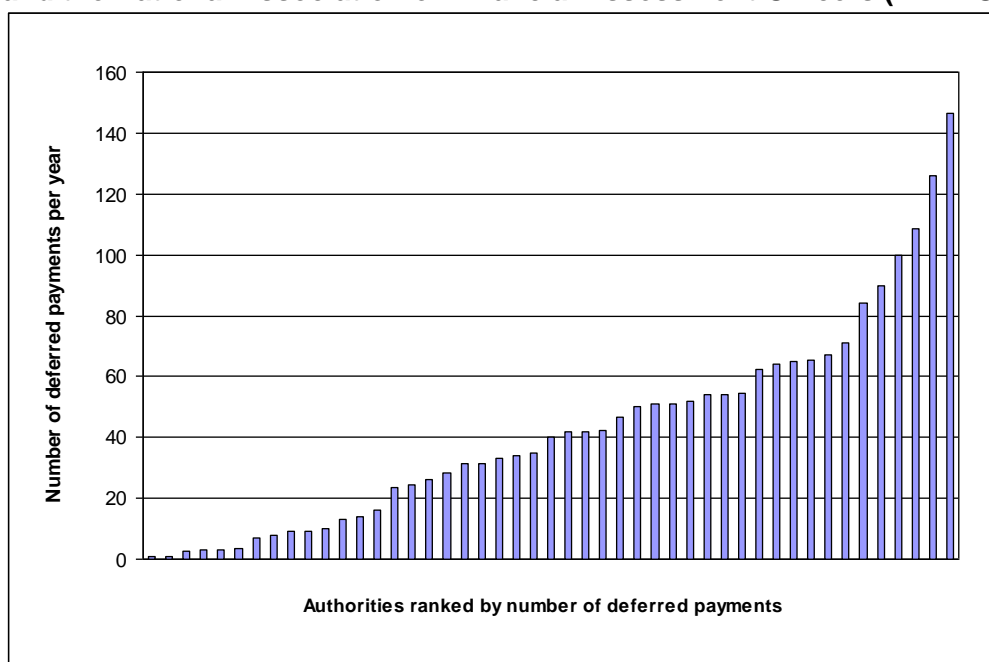
32. Figure 1 shows that there is large variation in the provision of deferred payments. One cause of this variation is that, under the current system, there are disincentives for local authorities to provide deferred payments. In particular, they cannot charge interest on deferrals and, therefore, they effectively make a loss every time they provide a deferred payment.

33. **Variation in local policies**: In 2012, the Department, in collaboration with the Association of Directors of Adult Social Services (ADASS) and the National Association of Financial Assessment Officers (NAFAO), surveyed local authorities about their deferred payment schemes. Responses to the survey revealed considerable variation in the way authorities implement the current

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[16] Local authority circular - LAC DH (2009) 3
[17] Local authority circular - LAC DH (2009) 3
[18] The survey asked authorities about the number of deferred payments ending and beginning in 2011/12. To minimise the impact of random variation in-between years, we have calculated the number of deferred payments per year as the average between those two figures.

discretionary scheme. In particular, a substantial minority of authorities offers deferred payments under conditions which are likely to reduce take-up:

- In nine out of 59 respondent authorities, deferred payments were offered only to people whose home was occupied, either by a relative or by a tenant;
- In 2 local authorities, deferrals were offered only in compelling individual circumstances;
- Some authorities only offered deferred payments to people with liquid assets below a threshold of less than £23,500 (3 local authorities, in one case as little as £4,000).

34. **Variation in local take-up**: To assess the degree to which the offer of deferred payments in each area meets the demand for deferred payments, we calculate the take-up rate in each authority, i.e. the share of new self-funders in residential care who take up a deferred payment in any given year:

> **Take-up rate** = deferred payments / new self-funders in residential care

35. The number of new self-funders in each authority is estimated based on:
- Local authority level data from the Care Quality Commission (CQC) on the total number of care home beds in homes which contain older people;
- An estimate of the occupancy rate in care homes in each English region; [19]
- Data on the number of people in residential care who are supported by their local authority, including those placed by other local authorities from a CQC survey in 2009;[20]
- Data on the number of people supported by continuing health care in residential care, using data from the Department and Laing and Buisson;
- Finally, the estimates are scaled to fit Personal Social Services Research Unit (PSSRU) data on the total number of self-funders at the national level.

Figure 2 – Take-up rate of deferred payments by authority, from the 2012 DH/ADASS/NAFAO survey

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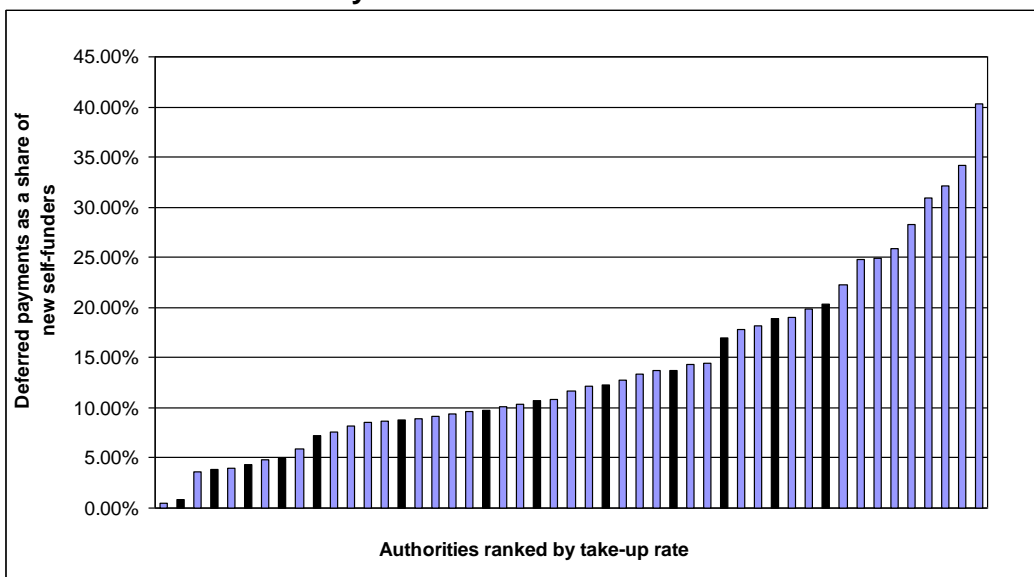
[19] From Laing & Buisson, Care of Elderly People UK Market Survey 2010-11, Twenty-third Edition, London, 2010.
[20] The survey data is uprated to take account of changes in the number of supported residents using information from Personal Social Services Expenditure Return;

36. Figure 2 shows that there is substantial variation in the take-up rate across authorities. This might reflect genuine differences in demand, but it is likely that it also reflects differences in the local offer/supply. The darkly shaded bars in figure 2 represent local authorities with policies that may reduce demand for deferred payments (as defined in para 33) and those authorities have, indeed, less take-up of deferred payments (see also table 1).

Table 1 – Local policy choices and take-up, based on the 2012 DH/ADASS/NAFAO survey

	Proportion of new self-funders in residential care who take-up deferred payments
Authorities with more restrictive policies (13 authorities)	9%
Authorities with no obvious restrictive policies (36 authorities)	14%

As a result, many people still have to sell their home to pay for care

37. Overall, the current scheme did not achieve its objective to "ensure no old person will be forced to sell their home against their will then they go into care"[21]. According to the annual budget survey by ADASS, **approximately 4,000 deferred payments were taken out in 2012**.

38. With about 55,000 self-funders entering care every year, this suggests that, overall, about **7% of self-funders** take out a deferred payment. In light of the variations across local authorities, it appears that the voluntary scheme does not fully meet demand for deferred payments.

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[21] NHS Plan, July 2000

III – Policy proposal – universal deferred payment scheme

1. Option 1- Do nothing

39. Under the do nothing, provision of deferred payment is likely to remain patchy. Neither local authorities nor the private sector would have any incentives to provide more or different offers of deferred payments than at present.

2. Discarded option: voluntary scheme with interest rate

40. The Department has considered modifying the existing, voluntary deferred payment scheme by removing barriers, which currently discourage local authorities from offering deferred payments. In particular, authorities could be allowed to charge interest. Having powers rather than duties, would allow authorities to determine whether to offer deferred payments on a significant scale or not.

41. However, we expect that this would result in continuing local variation, in particular, as some authorities will decide not to promote deferred payments to avoid upfront costs. This would perpetuate the local variability of deferred payments that currently exists, even if backed up by central funding, and thereby would fall short of the policy objective that everyone should have the protection and peace of mind that a deferred payment offers. Wanting these benefits to be universal, the most appropriate approach involves universal duties.

3. Option 2 – a universal deferred payment scheme

42. This is the preferred option. It clarifies the rules that should apply in implementing deferred payments and aims to ensure that a deferred payment is available to anyone who, otherwise, would have to sell their home to pay for care.

43. This section sets out the main components of the proposed policy.

2.1 Eligibility – who can defer and how much?

44. **Eligibility:** Under the policy, there will be a <u>duty</u> to offer a deferred payment to anyone who:
   - Needs residential care and no spouse / dependent lives in their home;
   - Is assessed by the local authority as needing residential care;
   - Has less than £23,250 in savings (i.e. non-housing assets); [22]

45. This makes deferrals an effective extension of the twelve-week disregard allowing homeowners to make use of this initial breathing space and then (in principle) to extend it from week 13 in the form of a deferred payment. As with the twelve-week disregard, this set of rules will target the scheme towards people who need residential care and who have limited liquid assets to pay for care – i.e. those at risk of selling their home in the near future.

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[22] The upper capital limit for the domiciliary care means test is currently £23,250. However over time this is likely to change in line with other parameters in the threshold.

46. People who do not meet the criteria in para 44 at first may nonetheless do so later if their circumstances change, for instance if they deplete their savings.

47. In the summer, <u>the Department will consult</u> on whether, within these criteria, there are occasions when it would be challenging or inappropriate to offer a deferred payment, for example if shared ownership makes the debt hard to secure or recover. In particular, we will consult on how authorities can address these issues to minimise any resulting risks on repayments and the overall costs of the scheme.

48. **Level of care fees**: Under the policy, people can defer appropriate care fees. This means that they can also defer fees which are more expensive than the typical local authority funded care home place (i.e. "top ups" above local authority rate). However, local authorities will have discretion to limit what "top ups" they lend if the amount is excessive in relation to what the individual can afford. The Department will <u>consult on the restrictions local authorities can impose.</u>

49. Under the proposed policy, local authorities can request self-funders to pay part of their care fees out of their income. As a result, people will not defer all of their care costs. However, authorities will allow people to keep additional income to maintain and insure their home. This helps authorities ensure that people only borrow the amount that they need to, while ensuring individuals can maintain their property. Over the summer, <u>the Department will consult</u> on the types of costs associated with maintaining a property to inform what income people retain for this purpose.

50. In addition to the deferred payment, people will also be eligible for means-tested support and for the capped costs scheme. From 2016, financial help for the costs of residential care will be available on a sliding scale to anyone with less than £118k in total assets. This will reduce what care fees the least well off need to defer. The lifetime cost of care will also be capped at £72k, limiting the total amount someone is likely to defer even if they need care for a long time. These entitlements also mean that people will be at a very low risk of negative equity. The funding reform IA contains further details on the 2016 reforms.

2.2 Fees, charges and funding

51. **Admin charges apply:** Local authorities will be able to charge administration fees when people take out a deferred payment. These fees, together with interest payments and central government funding, will contribute to meeting the overall administration costs of the scheme. It has not been decided what level of charges local authorities can charge. This will be set out in regulation.

52. **Interest rates and funding:** As opposed to the current scheme, interest will be chargeable throughout the lifetime of the deferred payment. The regulations will specify a maximum rate, which would be kept under annual review. In addition, loans will be structured to minimize accumulation of interest. Thus, for instance, clients will not take out a lump sum loan on which they will accumulate compound interest. Instead, the total value of their deferral will increase in line with their care costs.

53. Once someone on a deferred payment has depleted their assets below £14,500, they will become eligible for fully means tested residential care and

will stop accumulating further interest payments. This offers protection against negative equity and situations in which users cannot afford interest payments. However, it also means that local authorities will suffer a shortfall in repayments where someone cannot repay all of their interest payments. Local authorities will be able to recoup this cost by charging an overall higher interest rate on all loans. As set out in section IV, page 21, we expect this risk to be low and only result in marginal upwards pressures on interest rates.

54. **As an indication**, the interest rate used in the costs below will reflect local authority borrowing costs with an upwards adjustment to reflect default risk. Given the level of risks involved (see section IV, sub-section 2.1 for a discussion of default risks), we expect that any risk adjustment will be minor. There will be some variation across authorities, reflecting the difference in local default risk, but as an illustration, we estimate the nominal rate will be up to 4% p.a. in 2015/16. In subsequent years, the rate will be revised on an annual basis. As borrowing costs are currently at very low levels, it is likely that, over time, interest rates on deferred payments will rise in line with future increases in headline interest rates.

55. However, it should be noted that no final decision on the interest rate and funding arrangements has been made. The Department is working closely with stakeholders to finalise its proposals.

2.3 Other policy requirements and local decisions

56. Local areas will likely need to offer support for people taking out deferred payments, alongside the deferred payments scheme, so that it is an effective option for people. We envisage that local authorities and stakeholders will lead on this.

57. The Department will consult on what this support should involve, so are not putting forward detailed proposals in the context of this impact assessment.

58. **Support to homeowners:** It is likely that people using deferred payments will benefit from support to maintain, improve, sell or rent out their home. This will need to reflect local requirements and could be provided by local government, NGOs or the private sector. It would also benefit local areas because it will mean that, in general, homes are less likely to fall into disrepair and are more viable for sale and renting.

59. The Department intends to work with local authorities on a sector-led programme to provide this support. We are not consulting on specific proposals at this stage but are using the consultation to explore what support is required and what best practice already exists.

60. **Information:** People considering a deferral need good information about their financial options and the implications of a deferred payment. Indeed, access to financial advice may be particularly important for people entering residential care (whether they are considering a deferred payment or not).

61. The Department will consult on the issue of what information people require to support financial decisions including deferred payments and who should provide this information.

4. Wider flexibility to offer deferred payments

62. **Deferred payments for domiciliary care:** The proposals allow people to defer residential care fees so that they do not have to sell their home in distress or in their lifetime if they do not wish to.

63. However, local authorities and NGOs have suggested that authorities should have wider powers to defer care fees, for example for domiciliary care. These might be useful to people in a range of situations:
    - To people in residential care who do not meet all of the criteria above;
    - To people in domiciliary care who wish to defer paying their care fees;
    - To people who want to use their housing wealth on additional services that might prevent them from developing care needs or that could help them remain in their home for longer.

64. The Department will consult on how authorities might use these powers before developing detailed proposals. Therefore, the present impact assessment does not discuss this aspect of the scheme.

65. **Deferred payments for younger adults:** At present, deferred payments are only available to older adults going into residential care. However, the Department will consult whether and under what conditions it would be appropriate to extend deferred payments to younger adults in residential care.

66. The cost modelling in this IA does not include any potential costs from any such deferrals. Offering deferred payments to younger adults might result in higher costs as younger adults are more likely to defer payments for longer durations. However, it should be noted that the additional costs would be limited by
    - The total assets of people taking-up deferred payments: no-one will accumulate a deferred payment which will push them below the threshold for means tested support;
    - The cap on total care costs, which limits the care costs anyone has to pay and therefore limits the costs they might need to defer;
    - People on long-term deferrals attempting to rent or indeed sell their homes.

IV – Assessment of impacts (option 2)

67. The objective of the proposed universal deferred payment scheme is to ensure that no one has to sell their home in their lifetime to pay for care. By making it mandatory for local authorities to offer deferred payments under certain conditions and setting clear parameters for local implementation, the scheme aims to give homeowners peace of mind and a wider array of choices when going into residential care.

68. The main impact of the proposed policy is to ensure everyone who needs to sell their home to pay for care will have the option to take up a deferred payment. This section sets out how this is expected to result in
   - Increased take-up of deferred payments;
   - A resulting increase in expenditure to provide these deferred payments and a corresponding increase in repayments;
   - Administrative costs in running the scheme;
   - Benefits to people taking out deferred payments;
   - Risks, in particular potential impacts on the housing market.

1. Increase in the take-up of deferred payments

69. We expect take-up for deferred payments to increase in a universal scheme. We estimate the expected increase in the number of deferred payments by comparing current take-up to an estimate of demand under two different scenarios in the proposed universal scheme.

Do nothing – patchy supply limits take-up of deferred payments

70. According to the ADASS budget survey, there are approximately 4,000 deferred payments every year (based on new deferrals in 2010/11 and 2011/12). This is equivalent to **7% of all self-funders** (=4,000/55,000).

Minimum scenario – all authorities offer deferred payments

71. Compared to the do-nothing scenario, we assume that the universal scheme would ensure that everyone who is at risk of selling their home to pay for care has access to a deferred payment. This means that all local authorities would offer deferred payments, within the policy parameters set out in section III.

72. We know that provision is patchy and that some local authorities do not offer deferred payments at all. At a minimum, under a universal scheme, we expect that the average take-up across England would be similar to the take-up reported in the 2012 DH/ADASS/NAFAO survey, i.e. 14% of all self-funders.[23] As table 2 shows, by 2024/25, this would result in an increase in the number of deferred payments by 6,200 relative to the baseline.

73. The number of self-funders in residential care has been estimated using the Department's social care funding model and takes into account a range of factors such as demography, prevalence of care needs and home-ownership rates (see Annex A for details).

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[23] This estimate excludes authorities with policies that might reduce demands, as set out in para 33.

Table 2 – Deferred payments 2015/16 – 2024/25 (low take-up scenario), estimate based on the DH social care funding model, rounded to the nearest hundred[24]

		15/16	16/17	17/18	18/19	19/20	20/21	21/22	22/23	23/24	24/25
A	New self-funders	62,000	63,000	65,000	68,000	71,000	74,000	77,000	81,000	85,000	88,000
B	Deferred payments (current scheme), =A* 7%	4,300	4,400	4,500	4,700	4,900	5,200	5,400	5,700	6,000	6,200
C	Deferred payments (new scheme), =A*14%	8,600	8,800	9,100	9,500	9,900	10,300	10,700	11,400	11,900	12,300
D	**Additional deferred payments under the new scheme =C-A**	**4,300**	**4,400**	**4,500**	**4,700**	**4,900**	**5,200**	**5,400**	**5,700**	**6,000**	**6,200**

Main scenario – universal scheme increases visibility and take-up

74. However, the scenario outlined in table 2 is based on current take-up in a voluntary scheme. We expect that a universal scheme will enhance the visibility of deferred payments and therefore lead to higher demand.

75. For our main scenario, we assume that total demand for deferred payments, under a universal scheme, will be about 20% of self-funders. This is based on current take-up in a large authority with hundreds of deferred payments, which has a well-developed scheme and where awareness of the scheme is likely to be high. Take-up in this authority is higher than in 80% of authorities in the 2012 DH/ADASS/NAFAO survey.

76. Based on this, we estimate that the universal scheme will increase the demand for deferred payments by up to 11,500 (in 2024/25, see table 3).

77. It should be noted that, under this scenario, we expect that a majority of eligible self-funders do not take-up a deferred payment. As set out earlier, we expect two thirds of new self-funders to be eligible for deferred payments, in any given year. Thus, as an approximation, we expect that **about three in ten eligible self-funders (20%/ 66% = approximately 30%) will take-up a deferred payment**.

78. This may be because some people may prefer alternative arrangements. For example, they may prefer and be able to sell their home before they would

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[24] Due to rounding, figures may not always add up.

need to draw on their housing wealth. Others may prefer to use their liquid savings first and do not stay in care long enough to be forced to draw on their housing wealth (e.g. if they die during their first year in care). Finally, in other cases, deferred payments may also not be appropriate, for example where the property is jointly owned and the joint-owner refuses to have a charge put on the property (or is deceased and the ownership is stuck in probate), or where there is an existing claim on the house from an equity release scheme.

Table 3 – Deferred payments 2015/16 – 2024/25 (main scenario), estimate based on the DH social care funding model, rounded to the nearest hundred[25]

		15/16	16/17	17/18	18/19	19/20	20/21	21/22	22/23	23/24	24/25
A	New self-funders	62,000	63,000	65,000	68,000	71,000	74,000	77,000	81,000	85,000	88,000
B	Deferred payments (current scheme), =A* 7%	4,300	4,400	4,500	4,700	4,900	5,200	5,400	5,700	6,000	6,200
C	Deferred payments (new scheme), =A*20%	12,300	12,600	13,000	13,500	14,100	14,800	15,300	16,200	17,000	17,600
D	**Additional deferred payments under the new scheme =C-A**	**8,000**	**8,200**	**8,400**	**8,800**	**9,200**	**9,600**	**10,000**	**10,500**	**11,100**	**11,500**

Uncertainties around demand

79. There are uncertainties around the estimates above. We base our central estimate on a large authority with high take-up (in the 8th decile of all authorities that responded to the 2012 DH/ADASS/NAFAO survey). We expect that, given the level of take-up (one in five self-funders), awareness of the scheme in the authority in question should be close to universal.

80. However, it is possible that take-up under a universal scheme would increase above this level, even in authorities with currently high take-up. This might be the case, if there still is scope for improvement in frontline delivery in those authorities. On the other hand, it could be that some authorities with lower take-up already meet demand for deferred payments, suggesting that the impact of the universal scheme will be closer to our low take-up scenario.

81. In addition, we propose to introduce interest charges on deferred payments, which may reduce demand for deferred payments. We do not have firm evidence on how interest payments will affect demand for deferred payments.

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[25] Due to rounding, figures may not always add up.

However, we expect that the overall impact of interest charges on demand will be limited, because, for most people, interest charges would be minor when compared to the potential well-being and financial benefits. Table 4 gives an approximation of the interest someone would pay on a deferred payment of different duration, for an average of £20,000 per year. The calculations show that for the majority of people on short loans, interest payments will amount to less than £500.

82. Therefore, we expect that the introduction of interest payments will not reduce overall demand for deferred payments strongly. However, it might encourage some people to repay earlier, unless they have a strong emotional or financial benefit from keeping the property. Given the overall uncertainty, the Department will monitor take-up when the scheme is implemented.

Table 4 – Approximate interest payments over the duration of a deferred payment

A	B	C	D	E
Duration in years	Share of deferred payments with longer duration	Deferred payment (excl interest)	Deferred payment with interest	Interest (=D-C)
1	53%	£20,000	£20,400	£400
2	25%	£40,000	£41,616	£1,616
3	11%	£60,000	£63,681	£3,681

2. Costs

83. This section sets out the costs of the proposed universal scheme compared to a do-nothing scenario, in which the take-up of deferred payments will be unchanged and no interest is charged. Costs include both the inherent cost of providing loans (i.e. deferred payments) as well as the costs of administering the scheme.

84. All costs are in 2010/11 prices, unless indicated otherwise.

85. The modelling takes account of the wider reforms to care funding expected to come into effect in April 2016 – and which are described in detail in the impact assessment on social care funding reform notably:
- A £72k cap on reasonable care costs; and
- Means-tested support for residential care for people with assets of less than £118k.

86. It should be noted that all estimates in the below section are national averages. The costs of deferred payments will vary across regions and the Department will take this into consideration when determining funding for the scheme.

2.1 Total monetised costs of additional deferrals

87. The main financial impact (to government) of providing deferred payments lies in the temporary costs of paying self-funders' care fees for the duration of the agreement. The fees (plus interest) are repaid when the agreement ends with interest with the interest payment representing a cost to the person taking out the deferred payment.

88. This section sets out our estimates for the total volume of deferred payments (and repayments) under the do-nothing and under the proposed universal scheme, as well as under a range of scenarios.

Basic modelling assumptions

89. The Department models the total volume (in monetary terms) of deferred payments based on projections from its social care funding model (explained in Annex A). For each self-funder, the model calculates their deferred payment, using the charging rules for residential care and the proposed eligibility rules for deferred payments. The model then calculates the amount of care fees the individual will defer, taking into account how much they are able to contribute from income. The duration of the deferred payment agreement is determined by the individual's length of stay in residential care and whether they end their agreement before death. Core assumptions used in the model are:
    - The take-up of deferred payments (as set out in section IV, subsection 1 above);
    - The level of deferred payments, i.e. care fees net of any contribution people make towards their care costs from their income;
    - The duration of deferred payments, i.e. the time until loans are repaid;
    - The interest rate;
    - The default rate.

90. **Level of deferrals:** The costs of the deferred payment scheme will depend on the level of care fees people chose to defer. This, in turn, will depend both on the level of care fees they have to pay and the amount they are able to contribute out of their own income.

91. As set out in section III, under the proposed universal scheme, people will be able to defer any reasonable fee (even if this is above the local authority rate in their area). Therefore, we assume that care fees for people taking-up a deferred payment are equivalent to the national average self-funder fee. We also assume that people in the scheme retain £200 per month of their income (including a personal expenses allowance as well as home insurance and maintenance expenditure) and use the remainder of their income to pay for care. Table 5 summarises the resulting estimate of the average weekly value of a deferred payment.

Table 5 – Average weekly value of a deferred payment, in 2010/11 prices[26]

	Assumption	Source	Estimate
A	National average self-funder care fees	Research by PSSRU (as yet unpublished)	£610
B	Average income contribution	Department of Health social care funding model	£220
C	**Average weekly value of a deferred payment**	= A – B	**£380**

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[26] Due to rounding, figures may not always add up.

92. This suggests that the average annual value of a deferral would be about £20,000 (=£380 * 52).

93. **Duration of deferred payments:** The monetised value of deferred payments will depend on their duration, i.e. the time until people repay their deferred payments. We estimate this based on responses to the 2012 DH/ADASS/NAFAO survey (see table 6).

Table 6 – Duration of deferred payment agreements ending in 2011/12, from the 2012 DH/ADASS/NAFAO survey[27]

	Share out of all deferred payments
Less than 1 year	47%
1 to under 2 years	28%
2 to under 3 years	14%
3 years or more	11%

94. It should be noted that the introduction of the proposed universal scheme may affect the duration of deferred payments. For instance, being able to charge interest reduces incentives for local authorities to ensure deferred payments are of short duration. At the same time, interest payments give stronger incentives for individuals to use deferred payments as breathing space only. We also expect that the duration of deferred payments - and in particular the duration of longer-term deferred payments not taken out for breathing space - is most strongly influenced by mortality rather than policy parameters.

95. **Interest rate:** We assume that, under the do-nothing option, no interest is charged, while, under the proposed scheme, authorities will charge an interest rate of 4%. As set out in para 54, in practice, the interest rate will vary across local authorities and over time.

96. It should be noted that the interest rate reflects local authority borrowing costs and therefore, in principle, it allows the scheme to be cost neutral as local authorities are reimbursed for the opportunity cost of making loans.

97. **Care cost price inflation:** The modelling assumes that social care prices will rise at around 2% over headline inflation from 2015/16 onwards.

Default rate

98. We base our central estimates on the assumption that all loans are repaid fully as soon as the deferred payment ends (either at death or because the person in question has sold their house). In practice, there may be a number of reasons why deferred payments are not repaid fully or in a timely manner:
   - **Late repayments**: after someone has died, it will take some time to sell the house and repay the deferred payment;
   - **Default**: the person cannot repay.

99. **Late repayments** will occur where someone dies while their deferred payment is still ongoing and no arrangements have been made to sell the home. In this case, both under the current voluntary scheme and under the proposed

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[27] In the survey, 41 out of 59 respondent authorities provided information on the duration of deferred payments.

universal scheme, interest will accrue until the house is sold and the deferral is repaid.

Table 7 – Time between the end of a deferred payment agreement and its repayment, based on responses from the 2012 DH/ADASS/NAFAO survey

Authorities with typical repayment	… within three months	… between three and six months	… between six and twelve months	… after more than a year
Percentage of total deferred payments	30%	20%	40%	10%

100. Table 7 shows that the time between the end of the deferred payment and the repayment varies considerably, with only half of all repayments occurring within six months. This has two impacts on the total value of the scheme:
    - Repayments occur later than predicted by the average duration of deferred payments;
    - Repayments are higher than predicted, as more interest accrues.

101. It should be noted that there is a large variation in the average repayment times presented in table 7. The Department will consult about the degree to which this depends on local characteristics outside of the control of local authorities, such as local housing markets, and what can be done to ensure prompt repayment. However, it should be noted that local authorities continue to accrue interest on the outstanding loan.

102. **Default risk**: There is a risk that individuals will not repay part (or all) of their deferred payment. We expect this risk to be small, because deferred payments are secured against property and local authorities will retain the right not to grant a deferred payment in cases they deem particularly risky (for example, where there are competing claims on the property).

103. The main risk of default results from situations in which the debt accrued under the deferred payment is a large proportion of the asset on which it is secured. Under the proposed scheme, if the deferral accounts for all but £14,500 of the person's assets, they become eligible for means tested support and cease to pay interest on their deferral. In such a situation, the local authority foregoes future interest charges on the deferred payment.

104. Secondly, where a deferred payment represents a large share of the asset on which it is secured, there is a risk that large swings in property prices result in negative equity, which makes it impossible to recover all of the outstanding debt.

105. However, we expect that foregone interest and negative equity will not be common. We estimate the average deferral to be £20,000 a year and the average duration of a deferred payment is 1 ½ years. Table 8 shows that the vast majority of houses in England are worth more than is required to pay for 1 ½ years of residential care.

Table 8 – Housing Assets

House value	Proportion of houses sold in England and Wales (Nov 2012) [28]
Under £50,000	1.60%
£50,001 - £100,000	13.20%

106. We assume that the risk of default is small enough that local authorities will be able to manage it, for instance by marginally adjusting the interest rate they charge to reflect local risks.

Modelling the difference between the do-nothing and the preferred option

107. Tables 9 and 10 summarise the volume of deferred payments and repayments under the current voluntary scheme (do nothing) and under the proposed universal scheme. We model two scenarios:
   - A low take-up scenario, in which about 14% of all self-funders take up deferred payments. This is a lower bound estimate, as it does not take into account any increase in take-up due to the increased visibility of a universal scheme. However, this scenario may be appropriate if interest charges substantially reduce demand for deferred payments.
   - A high take-up scenario, in which about 20% of all self-funders take up deferred payments. As argued above, we expect that this scenario is more likely to reflect future demand for deferred payments.

108. Under both scenarios, more deferred payments are taken-up which increases the cost to government of providing those deferred payments. At the same, time, however, the proposals will allow local authorities to charge interest, thereby reducing the costs of deferred payments (compared to the do-nothing).

109. The analysis in this section focuses entirely on new deferrals after 2014/15. Deferrals that have been taken-up before 2014/15 will not be affected by the proposals and the new interest charges will not be applied to them.

110. The usual assessment frame for government policies is ten years (2014/15 – 2024/25 in tables 9 and 10). However, some of the deferred payments that have been taken out in the years preceding 2024/25 will still be ongoing by the end of that year. To fully assess the costs and benefits of the proposed scheme, we need to take into account that these deferred payments will be repaid eventually. Otherwise, we would wrongly imply that all deferred payments which are still outstanding by March 2025 would not be repaid, which is clearly not the case.

111. Therefore, the below calculations take into account all payments and repayments related to deferrals taken out in 2014/15 – 2024/25, including where these occur after 2024/25. It does not take into account any new deferrals occurring after 2024/25, as these deferrals fall outside of the ten year assessment period.

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[28] http://www.landregistry.gov.uk/__data/assets/pdf_file/0020/34706/HPI-Report-Jan-2013.pdf

Table 9 – Volume of deferred payments and repayments (low take-up scenario) in £m, in 2010/11 prices, rounded to the nearest £m[29]

			15/16	16/17	17/18	18/19	19/20	20/21	21/22	22/23	23/24	24/25	After 24/25	TOTAL
Do nothing	A	Deferred Payments (in £m)	27	66	92	110	115	122	129	139	149	157	0	**1,106**
	B	Repayments (in £m)	5	25	54	80	94	104	114	124	133	144	199	**1,077**
	C	Net spent =A-B	22	41	38	30	21	18	15	15	16	14	-199	**29**
Proposed scheme	D	Deferred Payments (in £m)	54	131	184	220	231	244	258	278	298	314	0	**2,212**
	E	Repayments (in £m)	10	51	111	167	196	218	239	259	280	301	425	**2,256**
	F	Net spent =E-D	44	81	73	54	34	26	19	19	18	13	-425	**-44**
ADDITIONAL FUNDING NEEDS = F-C			22	40	35	24	13	9	4	4	3	-1	-225	**-73**

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[29] Due to rounding, figures may not always add up.

Table 10 –   Volume of deferred payments and repayments (high take-up scenario) in £m, in 2010/11 prices, rounded to the nearest £m[30]

			15/16	16/17	17/18	18/19	19/20	20/21	21/22	22/23	23/24	24/25	After 24/25	TOTAL
Do nothing	A	Deferred Payments (in £m)	27	66	92	110	115	122	129	139	149	157	0	**1,106**
	B	Repayments (in £m)	5	25	54	80	94	104	114	124	133	144	199	**1,077**
	C	Net spent =A-B	22	41	38	30	21	18	15	15	16	14	-199	**29**
Proposed scheme	D	Deferred Payments (in £m)	78	188	263	315	329	349	368	397	425	449	0	**3,160**
	E	Repayments (in £m)	15	73	158	238	281	311	341	370	399	431	607	**3,223**
	F	Net spent =E-D	63	115	104	77	49	38	27	27	26	18	-607	**-63**
ADDITIONAL FUNDING NEEDS = F-C			**41**	**74**	**66**	**47**	**28**	**20**	**13**	**12**	**10**	**5**	**-407**	**-92**

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[30] Due to rounding, figures may not always add up.

2.2 Costs of operating the system

112. In addition to the expenditure of allowing people to defer their care fees, there will be additional costs resulting from setting up and operating a deferred payment scheme.

Set-up costs

113. From the 2012 DH/ADASS and NAFAO survey and a previous survey in 2011, we know that at least 70 local authorities already offer deferred payments. While they will face some costs in expanding their activity or adapting their policy to universal scheme, we expect set up costs to be limited in these authorities, as they build on their existing schemes.

114. However, up to 80 local authorities (=152 – approx. 70) currently offer little or only a very limited number of deferrals. These authorities will face a range of costs which may include:
- establish a policy on deferred payments, including a policy on reasonable levels of fees to lend, and risks – such as joint ownership of property;
- write guidance for and provide training to care managers on the new scheme;
- produce information for people who may need a DPA;
- establish and cost an administrative and legal process.

115. We have no information on these costs. However, we are seeking information from local authorities as part of our forthcoming consultation on the cost of designing and implementing a deferred payment scheme.

Administration costs

116. The 2012 DH/ADASS/NAFAO survey asked local authorities to estimate the administrative costs of setting up, monitoring and collecting repayment in a deferred payment scheme. Responses indicated a wide range of costs from £170 to over £1000 (see table 11 for the range of estimates).

Table 11 – Range of administration costs as reported in the 2012 survey

Estimated administration cost per deferred payment	Less than £250	£250 to £500	£500 or more
Number of local authorities	9	8	3

117. Because of uncertainty around the responses (in particular, whether respondents considered all types of cost when responding), we talked, in depth, to a local authority with a large number of new deferrals each year, whose scheme we expect to be in steady state. That authority had reported legal costs of around £375 per deferred payments. In addition, it reported its activity in administering financial assessments and monitoring the scheme (including monitoring the debt, producing annual statements for those with a deferral and collecting repayment). Table 12 summarises the overall costs of administering a deferred payment, assuming on-costs of 30%, adjusting for the higher unit costs in the local authority in question, and deflating from 2012/13 prices to 2010/11 prices.

Table 12 – **Summary of administration costs per deferred payment, in 2010/11 prices and rounded to nearest £10[31]**

A	Legal costs	£350
B	Ongoing monitoring	£70
C	Financial assessments	£70
D	**Total LA staff costs (=A+B+C)**	**£480**
E	Including on-costs (=D*1.3)	£630
F	Land registry fees	£50
G	**TOTAL costs (=E + F)**	**£680**

118. We assume that these costs will rise with inflation. Table 13 estimates the total administration costs of the scheme based on the above assumptions and the number of new deferrals as set out in tables 2 and 3.

Table 13 – Additional deferred payments and administration costs

		15/16	16/17	17/18	18/19	19/20	20/21	21/22	22/23	23/24	24/25
A	Additional deferred payments (14% take-up)	4,300	4,400	4,600	4,800	5,000	5,200	5,400	5,700	6,000	6,200
B	Additional deferred payments (20% take-up)	8,100	8,200	8,500	8,800	9,200	9,600	10,000	10,500	11,100	11,400
C	Additional administration costs at 14% take-up (=A*£680)	2.9	3.0	3.0	3.2	3.3	3.5	3.6	3.8	4.0	4.2
D	Additional administration costs at 20% take-up (=B*£680)	5.4	5.5	5.7	5.9	6.2	6.5	6.7	7.1	7.5	7.8

2.3 Risks and uncertainties

119. The above analysis is subject to a number of uncertainties. This section describes the potential scope and impact of these uncertainties.

Year-on-year variation in demand at local level

120. At the local level, demand for deferred payments varies considerably over time. In the 2012 DH/ADASS/NAFAO survey, the average difference between the number of deferrals that ended in 2011/12 and those that began in 2011/12 was **+/- 28%.** This fluctuation may reflect a variety of factors such as
    - Local housing market conditions (e.g. higher prices may encourage people to sell their home rather than taking out or keeping a deferred payment);
    - Local policy choices regarding the wider social care system, which will affect whether or not people go into residential care (and as a self-funder).
    - Random year-on-year variation, e.g. in the characteristics of each new cohort of self-funders, which may mean that more or less self-funders are eligible for a deferred payment.

121. However, given the overall volume of deferred payments, this variation is modest when compared to local authorities' financial resources. Indeed, for most authorities in the 2012 DH/ADASS/NAFAO survey, year on year variation was less than 5% of their reserves.

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[31] Due to rounding, figures may not always add up.

122. <u>The Department will consult</u> on the risks and costs that annual valuation is variation in demand for deferred payments puts on local authorities.

Risks resulting from empty homes

123. If people take-up a deferred payment rather than selling their home, this may result in a situation where their home is temporarily not occupied. This, in turn, may affect the housing market and result in adverse wider social impacts (through a loss of consumer surplus, where people are priced out of the market and pressure on housing prices). The analysis below estimates these impacts on the housing market. It shows that, at the national level, the impact on the housing market is likely to be relatively small, resulting in about 3,500 unoccupied homes and limited pressure on housing prices, but there could be more significant localised effects, which may affect the balance of costs and benefits.

Quantification of the reduction in housing supply

124. As set out in table 13, we estimate that, by 2015/16, the universal deferred payment scheme will increase the annual flow of new deferred payments by about 8,000. However, not all of these deferrals will result in empty homes.

125. Firstly, about half of all deferrals end within a year. These **short-term deferrals** might end because the person taking out the deferral dies (possibly before they could have sold their home), or because they were taken out as a temporary breathing space by people who then proceed to sell their home. In both cases, we expect that the home would have been empty for approximately the same time, regardless of whether people take out a deferred payment.

126. Similarly, the homes of people who take out **longer-term deferrals** of more than a year also would have been empty for some time at least, even if there were no deferred payments. For example, if they had to sell their home, people might not immediately find a buyer. Sometimes people will also go into care not knowing how long they will stay and therefore, initially, they do not arrange to sell their home.

127. Finally, it is important to consider that not all properties with a deferred payment will be empty. Instead, people in the scheme may wish to ensure that their **property is occupied**, for instance, by renting it out. We estimate that this will be the case for about one third of all properties with a longer-term deferred payment. This estimate is based on responses from nine authorities in the 2012 DH/ADASS/NAFAO survey, which offer deferrals only to people who ensure their home is occupied. Take-up in these authorities was about 7% of all self-funders, i.e. approximately a third of our best estimate for take-up in the universal scheme. However, there is considerable uncertainty around this estimate:
    - In the nine authorities in question, people were obliged to ensure there home was occupied if they wanted to take out a deferred payment. This is a strong incentive for people to do so, e.g. by asking a relative to move in. Fewer homes will be occupied under a universal scheme, under which this specific eligibility condition does not hold.
    - We expect that local authorities will work to encourage people to rent out their homes, thereby increasing occupation rates;
    - People with long-term deferrals are more likely to ensure that there property is occupied (for instance when compared to people who take-out a breathing space loan in view to sell their home).

128. Taking together the assumptions outlined above, we estimate that about 3,000 deferrals each year will result in additional unoccupied properties (in 2015/16).

Table 14 – Number of new deferred payments resulting in empty homes

		2015/16
A	Number of deferrals (annual flow)	8,000
B	… of which short-term deferrals (=A*47%)	3,800
C	Long-term deferrals (=A-B)	4,200
D	.. of which rented out (=C*33%)	1,400
E	**Long-term deferred payments, no occupation (=C-D)**	**2,900**

129. As set out in para 126 and 127, we expect that increases in the number of unoccupied homes will mainly result from longer-term deferred payments. Given the average duration of these deferrals, we estimate that the these will be unoccupied for about two years. Based on this assumption, we expect that the universal deferred payment scheme will reduce the supply of available homes by 5,800 homes in 2015/16 (=2,900 deferrals * 2 years).

Resulting externality

130. Unoccupied homes are more likely to be poorly maintained. The resulting deterioration of the property may, in turn, have negative spill over effects on neighbouring properties and negatively affect their value.

131. Under the proposed scheme, people will retain enough income to maintain their property and they will have support to maintain, do up sell or rent their home. We expect this to reduce the number of long-term empty homes and the problems associated with these (because homes will be adequately maintained). This impact assessment assumes that these policies prevent and offset any externalities linked to empty houses. The proposed consultation in summer 2013 will gather evidence on these issues to inform more detailed policy development.

Wider welfare implications

132. Assuming that the supply of housing is fixed, so that the number of occupied homes, across the country, will fall by 5,800 under the best take-up estimate (less homes will be affected under the alternative, lower scenario). This is equivalent to about 0.03% of about 22 million homes in England.

133. In addition, in reality, the supply of housing is not fully inelastic. Any reduction in supply will be partially mitigated through an increase in prices: where fewer houses are available in an area, some people will be willing to pay higher prices for access to the remaining housing stock, which, in turn, makes it more interesting for sellers or property owners to provide housing. There are about 710,000 empty homes in England[32] - even if only 0.8% of these were brought into the market in response to the new unmet demand, this would be sufficient to balance the reduction in housing supply due to deferred payments.

134. This reduction can result in three separate impacts, which are explained, in more detail, in Annex B:
   - A loss of consumer surplus as some people are unable to find accommodation at the price they are willing or able to pay;
   - Price pressures in the housing market, which might increase prices/rents resulting in a transfer of wealth from buyers/renters to sellers/landlords;
   - Rent (or equivalent income) foregone to people taking out a deferred payment.

135. **Loss of consumer surplus**: as a result of the reduction in available housing stock, some people will be unable to find accommodation at the price they are willing to pay. Therefore, they lose out on the benefit of that accommodation (net of the rent they would have paid).

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[32] http://www.emptyhomes.com/statistics-2/empty-homes-statistice-201112/ ; *Often they are rented homes that have fallen into disrepair; sometimes the owner has inherited the property. In many cases the owner lacks the funds or the skills to repair and manage the property.*

136. However, this effect is likely to be small: a reduction in the housing stock by 6,000 homes is equivalent to a shift in the total supply of housing by 0.027%. Given the responsiveness of demand and supply to prices, we expect this to generate only a similarly small shift to prices. People who are priced out of the market by this small shift in prices will have had little net benefit from their accommodation (once rent is taken into account).Annex B calculates the corresponding loss of consumer surplus to be, in total, as little as **£20,000 per year**.

137. In practice, supply will respond to fill the gap created by 6,000 homes taken off the market. Thus, some of the resulting excess demand will translate into higher prices, some of it will be addressed by an increasein houses supplied by other home owners/landlords. We estimate that, overall, **the number of occupied homes will fall by 3,500** (see Annex B).

138. **Impact on market rents:** The reduction in housing supply might increase prices/rents in the housing market. In Annex B, based on estimates for the demand and supply elasticities for housing, we estimate that prices could increase by up to £3.85 per year per household. Across 22 million households in England, this effect could add up to about £85m, which are transferred from home sellers/renters to home owners/landlords. A priori, this transfer of wealth is neutral from a social perspective. However, taking into account the differences in income between landlords and renters, in particular, we estimate that these transfers result in a reduction of social welfare by **£13m per year**.

139. However, it should be noted that this impact is contingent on price pressures being passed on to consumers. Given the size of the effect, which amounts to about £0.3 per household per month, rents may not be adjusted to pass on this potential increase.

140. **Foregone rental income**: As 3,500 less homes will be occupied, their owners forego any rental income they could have earned on them. This adds up to **£42m per year** (=3,500 homes * £12,000 per year). The social welfare effect of this reduction in rental income is uncertain. In particular, as people *decide not to rent* out their house, they must value doing so more than the rent they forego. Therefore, arguably, the benefit of not having to rent out their home outweighs any loss in rental income. However, there is a risk as people may misjudge their own utility or not take into account the utility of rental income to others (such as their family). In practice, local authorities will offer support in renting out the property and people's families are likely to be involved in the decision-making and, indeed, the management of the rental process.

141. **Local variation**: It should be noted that the above discussion treats the housing market as one coherent market for the whole of England. In reality, there are many local housing markets and both the incidence of deferred payment and the underlying structure of the local housing market will differ.

142. Local variation could mean that in many areas the impacts on the housing market could be very small, but also means it is possible that in some local areas there could be more significant impacts on housing shortages and prices. In such areas, the negative impacts on the housing market could substantially affect the balance of the costs and benefits generated by deferred payments.

143. The Department will consult to understand to what extent deferred payments could have a significant local impact on housing markets, and how this issue could be addressed. Local areas that support people to rent out or sell their properties are likely to see fewer empty homes and this support could mitigate local impacts on the housing market. The Department will work with the sector to develop such a support programme.

3. Benefits

144. As set out in tables 2 and 3, we expect that the introduction of a universal deferred payment scheme will lead to an increase in the number of deferred payments by about 8,000 in 2014/15 and around 11,000 in 2024/25. This section discusses the expected benefits generated by deferred payments:
   - Reduction in stress and anxiety for those who go into residential care as self-funders and will not have to sell their home as a result of the universal deferred payment scheme;

- Peace of mind for anyone who may be at risk of having to sell their home in the future;
- Financial protection for homeowners.

3.1 Improved well-being through a reduction in anxiety and stress

145. The main benefit of deferred payments lies in the reduction of anxiety for those who otherwise would have to sell their home. As set out in section II, the stress of moving into a care home has been associated with a range of symptoms such as:
- Anxiety
- Depression
- Loneliness and increased confusion
- Sleep disturbances
- Weight loss
- Gastrointestinal upset

146. Having to sell one's home, in a rush, when going into residential care, is a source of further stress and anxiety, which may reinforce these symptoms and thereby reduce people's quality of life. The proposed deferred payment scheme will prevent people from suffering this additional stress and anxiety, and thereby, will improve their quality of life.

147. There is no quantified information on the prevalence of given levels of anxiety in people who go into care homes or on the specific impact of having to sell one's home in that situation. Therefore, we cannot easily monetise these benefits. However, we illustrate the potential value of the reduction in anxiety and stress, by creating a **central scenario** describing the approximate well-being impact of deferred payment and making a number of assumptions:
- Firstly, we assume that anyone who takes out a deferred payment will benefit, to some extent, from a reduction in anxiety.
- Secondly, we assume that the positive impact on their quality of life can be represented by a move on the EQ-5D quality of life scale from "no anxiety" to "moderate anxiety". This translates to a quality of life improvement of 0.071. It should be noted that this is an estimate for the average self-funder and will vary for individuals depending on a) their attachment to their home and b) their overall health state and level of anxiety.
- Finally, we expect this improvement occurs once for each deferred payment and has an average duration of 1 year.

148. Taken together, the above assumptions suggest that each deferred payment improves the well-being of the person taking-up the deferral by about 0.071 quality-adjusted life years (QALYs) per deferred payment. As the QALY is valued at £60,000, this suggests an expected monetised benefit of **£4,260 (=0.071 * £60,000) per recipient**.

Sensitivity analysis – duration of benefits

149. The above estimate is sensitive to the assumptions used. In particular, for our central estimate, we assume that a reduction in anxiety occurs, on average, for approximately one year after someone has taken-up a deferred payment.

150. However, in practice, for some people, the impact of a deferred payment may be limited to the transition period only, as people settle into their new environment and become more able to deal with the prospect of selling their home. For others, selling one's home may be a dreadful prospect even as they settle into residential care. In particular, their ability to cope and actively manage any sale may decline with their health state. As a result, their benefit from the deferred payment is not limited to the first year.

151. As sensitivity analysis, we vary the duration of the quality of life improvement caused by deferred payments. As a lower bound, we estimate that the quality of life improvement set out above, will persist for about half a year. This takes into account that it may take that long for many people to sell their home (including the twelve-weeks disregard) and to settle their anxiety afterwards. The resulting **lower bound** quality of life improvement would be **£2,130 (=£4,260/2) per deferred payment**.

152. As an upper bound, we assume that the reduction in anxiety is felt throughout the whole duration of the deferred payment, as, arguably, not having to sell one's home will generate peace of mind throughout the whole stay in care. Given an average duration of a deferral of about 1 ½ years, this suggests an upper bound value benefits of **£6,390 (=£4,260 *1.5)** per deferred payment.

153. **Alternative example**: It should be noted that this range does not take into considerations other sources of uncertainty, such as the intensity of the anxiety felt. Those who feel the least benefit from a deferred payment may not take them out, in the first place. However, one might consider that there are different degrees of impact among those who take-up a deferred payment:
    - Some people will only feel the indicated reduction in anxiety (a quality of life impact of 0.071) for a limited time – assumed to be three months after the twelve-weeks disregard ends (which would be the time it takes to settle the sale, during which their savings would be at risk). The total quality of life loss is 0.018 (=0.071 for 3 months);
    - For others, however, the anxiety may be more severe initially, especially where they are already in a fragile state. Therefore, we assume that it can be represented by a move from "moderate to "severe" on EQ-5D which translates into a quality of life loss of at up to 0.434 if they do not already score "severe" on another dimension. We assume that this state would last for about six months, resulting in a quality of life loss of 0.217.

154. An average quality of life loss of 0.071 (as in our central scenario) would require at least 25% of all people taking-up deferred payments to fall into the second group. To match our lower bound scenario (equivalent to a quality of life loss for 6 months), only about 9% of deferred payments would need to be taken-up by people with more severe anxiety.

3.2 Wider peace of mind benefits

155. The above analysis assumes that deferred payments improve the well-being of those taking out a deferred payment. However, in practice, peace of mind benefits may extend beyond this group. Firstly, the availability of deferred payments may reduce worries and anxiety even for those self-funders who do not take-up a deferred payment in the end, but who are at risk of having to sell their home. In addition, peace of mind benefits may also extend to those who are not currently at risk of going into residential care, at all. Indeed, knowing that the deferred payment scheme is available and that there is no need to sell one's home within one's lifetime may provide reassurance to anyone who may be at risk of needing residential care, at any point in the future. This has not been quantified.

3.3 Value of financial protection

156. As set out in section II, being able to keep one's home may result in financial benefits to some people, as they avoid a distressed sale or continue to benefit from rental income. These benefits fall on the individual in question, while, at the same time, there will be corresponding losses to someone else (such as the prospective buyer, who could have acquired the property below market value). Thus, from a societal perspective the *net financial* impact is zero.

157. However, it could be argued that society, due to considerations of fairness and justice, prefers to allow people to get the full benefit out of their lifetime savings, even if this means that someone else foregoes corresponding benefits. This has not been quantified.

5. Net present value calculations

158. This section summarises the costs and benefits (relative to the do-nothing scenario) which have been identified in the preceding sections and calculates the net present value of the proposals (from a societal perspective).

159. The main monetised impacts of the proposed policy include changes to:
    - Net costs of providing deferred payments, i.e. the difference between loans and repayments. This includes both the additional expenditure due to more deferred payments, and the additional income due to the interest rate. It should be noted interest payments on deferred payments are a financial benefit to government, but a loss to people taking out a deferred payments;

- The administration costs of providing a deferred payment scheme;
- The well-being benefits to recipients due to reduced anxiety and stress.

Scenarios for net present value calculations

160. To account for uncertainty, tables 15 -17 present a range of scenarios:
     - scenario 1: high take-up of deferred payments (by 14% of self-funders) and low benefits (of £2,130 per deferral);
     - scenario 2: low take-up (14%) and high benefits (£6,390 per deferral);
     - scenario 3: high take-up (20%), average benefits (£4,260) - we expect this to be the most appropriate representation of costs and benefits.

Distribution of costs

161. Calculations in this impact assessment include the full social value of the proposals, including the opportunity cost of public funding (exchequer funding).

162. It should be noted that the social valuation of costs and benefits may differ depending on whom these costs and benefits fall on. However, for some of the costs and benefits identified in this impact assessment, it is currently not possible to say with certainty who will bear them. For the purpose of this impact assessment, it is assumed that all public sector costs will be covered by Department of Health funding, rather than raised by taxation or borne by local authorities. This is a cautious assumption for the purposes of this impact assessment and is **subject to spending review decisions**, as well as subsequent funding decisions.

163. Therefore, tables 15 - 17 are subject to uncertainty with regard to who bears the identified costs. **For illustration purposes**, tables 15-17 assume that the total costs of deferred payments net of repayments will be financed out of central funding and that government will bear all administration costs. These are conservative assumptions: administration fees paid by people taking-up deferred payments will result in less costs to government. Who bears any of the identified costs is contingent on assumptions about the source of funding. In particular, at this moment, no decision has been made on
     - the duration of Department of Health funding to local authorities;
     - how costs fall on Department of Health or wider government budgets – this is subject to the spending review (even though, for this impact assessment, it is assumed they fall on the Department of Health);
     - the scope of administration fees, which will be paid by those taking up a deferred payment.

Opportunity cost of Department of Health funding

164. In particular, the below calculations of the social value of costs and benefits need to take into account the **opportunity cost of Department of Health funding,** wherever public expenditure is involved. To the degree that funding comes out of the Deparment of Health's budget, as an approximation, we expect that its opportunity cost lies in foregone expenditure in the National Health Service (NHS) – even though it is not possible to specify where exactly it would have been spent.

165. This implies that the foregone spending would have observed the same budget constraint that apllies for NHS spending, as defined by the National Institute for Health and Clinical Excellence (NICE). The National Institute for Health and Clinical Excellence (NICE), estimates that an increase of expenditure of £20-£30,000 will on average force the NHS to make economies (e.g. on staff or on drugs or on procedures) that will lead to a loss of a quality adjusted life year (QALY). Therefore, we compare the benefits of a policy with the costs, in terms of the health benefit, that could have been generated through funding to the NHS (at a rate of £25,000 per QALY). At the same time, the Department of Health assigns a value of £60,000 to a QALY, consistently with similar valuation of policies that mitigate mortality or morbidity risk by other government departments, based upon studies of what members of the public are on average willing to spend to reduce their own mortality risk, or to improve their own health outcomes.

166. A policy proposal that costs £25,000 to the NHS is therefore presented with an opportunity cost of £60,000 on the assumption that it would force an economy that would displace a QALY, and therefore lead to a drop in overall health benefits that would be valued by the public at £60,000. As a result, as an approximation, the true opportunity cost of funding in the health and social care system is assumed to be £2.4 for every £1 lost (=£60,000/£25,000).

Discounting

167. Future expenditure and benefits are worth less to society than costs or benefits of equal size which occur today. Therefore, to calculate the net social value of the proposals, we discount future costs and benefits.

168. As per Green Book convention, monetary costs and benefits are discounted at 3.5% (in real terms) per year, which is approximately 5.5% in nominal terms. It should be noted that we expect a nominal interest rate of 4% to be charged on deferred payments. As a result, if a loan of £100 is made, government foregoes alternative expenditure worth £100. If the loan is repaid after a year, the total repayment will be £104, which can be spent by government. However, to society, the value of this expenditure will be less than the original cost of £100, as future expenditure is discounted at 5.5%, resulting in a present value of only £98.6 (=£104/1.055).

169. This is the approach used in tables 15 -17 which treat all public sector costs as Department of Health costs. To the degree that local authorities can fund the scheme out of borrowing, the scheme can be considered cost-neutral, because the interest rate charged by local authorities (assumed to be 4%) would reimburse them for their own costs of borrowing. The net present value of the financial impact of individual loans would be zero. However, as set out above, no decision has been made about the duration of Department of Health funding for the scheme, so that it is assumed, for the purposes of this impact assessment that costs fall on the Department.

170. A different discount rate is used for health and well-being benefits. This is because the value of a quality-adjusted life year (QALY) is expected to increase in line with GDP, i.e. at 2% per year. Thus, by using a constant value of a QALY of £60,000 in 2010/11 prices, we implicitly discount health benefits at a rate of 2% pa. We correct for this by discounting all health and well-being benefits in tables 15 -17 at a rate of 1.5% pa.

Table 15 – Scenario 1: high take-up, low benefits – all costs and benefits in £m and 2010/11 prices

		15/16	16/17	17/18	18/19	19/20	20/21	21/22	22/23	23/24	24/25	Repayments after 24/25*	TOTAL
COSTS													
A	**Set-up costs**						**UNQUANTIFIED**						
B	**Administration costs**	5	6	6	6	6	6	7	7	7	8		**64**
C	**Net funding requirement for additional deferred payments taken out between 2015/16 and 2024/25 (=outgoing payments minus repayments, see table 10)**	41	74	66	47	28	20	13	12	10	5	-407	**-92**
D	**TOTAL (=B+C)**	46	80	72	53	34	27	19	19	18	12	-407	**-28**
E	**Including opportunity cost of public funding (=D*2.4)**	**111**	**192**	**173**	**127**	**82**	**64**	**46**	**45**	**43**	**30**	**-978**	**-66**
BENEFITS													
F	**Financial transfer to individuals (=C)**	41	74	66	47	28	20	13	12	10	5	-407	**-92**
G	**Reduction in anxiety and stress**	17	17	18	19	20	20	21	22	24	24		**203**
H	**TOTAL (=F+ G)**	**58**	**92**	**84**	**66**	**47**	**40**	**34**	**34**	**34**	**29**	**-407**	**111**
Net value													
I	**Net value (=H-E)**	**-53**	**-100**	**-88**	**-61**	**-34**	**-23**	**-13**	**-11**	**-9**	**-1**	**570**	**177**

Net present value **	£68m

* This column includes all outstanding repayments on deferred payments which have been taken out until the end of 2024/25, but are repaid later. The government/local authorities will receive additional repayments after 2024/25 (see row C), which is a cost to individuals (row F).
**This is the sum of the discounted net value of benefits minus costs; discounted at 3.5%pa, or 1.5% for the well-being benefits in row G.

Table 16 – Scenario 2: low take-up, high benefits – all costs and benefits in £m and 2010/11 prices

		15/16	16/17	17/18	18/19	19/20	20/21	21/22	22/23	23/24	24/25	Repayments after 24/25*	TOTAL
COSTS													
A	Set-up costs						UNQUANTIFIED						
B	Administration costs	3	3	3	3	3	4	4	4	4	4		35
C	Net funding requirement for additional deferred payments taken out between 2015/16 and 2024/25 (=outgoing payments minus repayments, see table 10)	41	74	66	47	28	20	13	12	10	5	-407	-92
D	TOTAL (=B+C)	44	77	69	50	31	24	16	16	14	9	-407	-57
E	Including opportunity cost of public funding (=D*2.4)	105	186	166	120	75	57	39	37	34	21	-978	-138
BENEFITS													
F	Financial transfer to individuals (=C)	41	74	66	47	28	20	13	12	10	5	-407	-92
G	Reduction in anxiety and stress	27	28	29	30	31	33	35	36	38	40		328
H	TOTAL (=F+ G)	68	103	95	77	59	53	47	48	49	44	-407	236
Net value													
I	Net value (=H-E)	-37	-83	-71	-43	-16	-3	8	11	14	23	570	373

Net present value **	£266m

* This column includes all outstanding repayments on deferred payments which have been taken out until the end of 2024/25, but are repaid later. The government/local authorities will receive additional repayments after 2024/25 (see row C), which is a cost to individuals (row F).
**This is the sum of the discounted net value of benefits minus costs; discounted at 3.5%pa, or 1.5% for the well-being benefits in row G.

Table 17 – central scenario: high take-up, mid-estimate benefits – all costs and benefits in £m and 2010/11 prices

		15/16	16/17	17/18	18/19	19/20	20/21	21/22	22/23	23/24	24/25	Repayments after 24/25*	TOTAL
COSTS													
A	Set-up costs						UNQUANTIFIED						
B	Administration costs	5	6	6	6	6	6	7	7	7	8		64
C	Net funding requirement for additional deferred payments taken out between 2015/16 and 2024/25 (=outgoing payments minus repayments, see table 10)	41	74	66	47	28	20	13	12	10	5	-407	-92
D	TOTAL (=B+C)	46	80	72	53	34	27	19	19	18	12	-407	-28
E	Including opportunity cost of public funding (=D*2.4)	**111**	**192**	**173**	**127**	**82**	**64**	**46**	**45**	**43**	**30**	**-978**	**-66**
BENEFITS													
F	Financial transfer to individuals (=C)	41	74	66	47	28	20	13	12	10	5	-407	-92
G	Reduction in anxiety and stress	34	35	36	37	39	41	43	45	47	49		406
H	TOTAL (=F+ G)	**75**	**109**	**102**	**84**	**67**	**61**	**55**	**57**	**58**	**54**	**-407**	**314**
Net value													
I	Net value (=H-E)	**-36**	**-83**	**-71**	**-42**	**-15**	**-3**	**9**	**11**	**15**	**24**	**570**	**380**

Net present value **	£254m

* This column includes all outstanding repayments on deferred payments which have been taken out until the end of 2024/25, but are repaid later. The government/local authorities will receive additional repayments after 2024/25 (see row C), which is a cost to individuals (row F).

**This is the sum of the discounted net value of benefits minus costs; discounted at 3.5%pa, or 1.5% for the well-being benefits in row G.

V – SUMMARY AND CONCLUSION

171. This impact assessment has discussed the problems and poor outcomes faced by self-funders who are at risk of having to sell their home to pay for residential care. As it is difficult to draw on housing wealth in a flexible and timely manner, self-funders face the risk of having to sell their home to pay for care. This creates anxiety and stress in an already difficult period in people's life. In addition, society may have a preference to allow homeowners to fully benefit from their lifetime savings, even if this implies that others will forego the benefits of owning or using their home.

172. Since 2001, the Department has promoted a deferred payment scheme, in which local authorities have discretionary powers to defer self-funders' care fees. However, provision is patchy as local authorities have wide discretion about who is eligible for a deferred payment and cannot charge interest on deferred payments, thus making a loss on every deferred payment. The Department proposed a universal scheme, in which it is mandatory for local authorities to offer deferred payments under certain conditions and setting clear parameters for local implementation, the scheme aims to give homeowners peace of mind and a wider array of choices when going into residential care. This is expected to substantially increase the take-up of deferred payments, resulting in larger expenditure on deferred payments and peace of mind benefits to people going into residential care. At the same time, the proposed scheme will allow local authorities to charge interest on their deferred payments, thereby reducing the costs (to government) of the scheme.

Total monetised costs and benefits

173. Table 17 summarises our best estimates the total costs and benefits of the proposed scheme. These include costs to government as well as benefits to people taking out deferred payments.

174. **Costs to government**: It is estimated that the additional **administration costs** linked to the increase in deferred payments will sum up to **£64m over ten years** (sum of row B in the table).

175. As more deferred payments are taken-up up, the costs to government of providing those deferred payments increases relative to the do-nothing (with lower take-up). At the same, time, however, the proposals will allow local authorities to charge interest, thereby reducing the costs of deferred payments (compared to the do-nothing). We estimate that the proposed changes will reduce government costs of deferred payments by **£92m** over ten years (=sum of row C).

176. However, most of the additional interest income falls on later years, while most of the additional costs fall on earlier years. We adjust for this by discounting costs and cost savings at 3.5% (in real terms) per year when calculating the present value of costs and benefits.

177. In addition, as set out in paras 169-171, the total social value of these costs includes the opportunity cost of government funding, which means that both expenditure and income is valued at a higher rate than its nominal cash value (see row E).

178. Taking into account the discount rate as well as the opportunity cost of government funding, the present value of government savings is estimated at £15m over ten years, while the opportunity cost of the additional administration expenditure is valued at £127m. Thus, over ten years, we estimate the present value of additional government expenditure to be £112m.

179. **Benefits to individuals**: Individuals' financial costs and benefits are the mirror image of government's costs: outgoing deferred payments are individuals' receipts, while individual's repayments are income to government. As a result, we estimate that individuals' **net repayments will increase by £92m** over ten years (=sum of row F). This reflects the higher interest rate charged under the proposed scheme. However, as deferred payments are received in earlier years, while repayments are made in later years, the **present value of the net cost to individuals** is estimated at a lower value of about **£6m** .

180. In addition, individuals benefit from reductions in anxiety and stress (see row G). The present value of these well-being benefits is estimated at £372m over ten years (at a 1.5% discount rate, see para 175).The total present value of benefits **is thus estimated at £366m** (=£373m - £6m)..

181. **Net present value:** Taking together the above calculations, we estimate the net present value of the proposed policy to be about **£254m over ten years** (=£366m -£112m).

Equality impact

182. The Department conducted an engagement exercise over Autumn 2011 with care users and members of the care sector on reform of social care, including proposals for universal deferred payments.

183. The engagement found support for deferred payments; a workshop on social care funding involving representatives from local authorities and disabilities groups note that *"Universal deferred payments would give people additional choices and flexibility in meeting their care costs and there was strong support for them."*[i]

184. Deferred payments will be subject to eligibility criteria, notably whether someone needs residential care and whether they have limited liquid assets. Beyond this the scheme will not actively discriminate on the basis of equalities characteristics such as old age, gender, sexual orientation, belief or socio-economic status. However it is likely there will be a differential level of uptake of deferred payments across different population groups. This is discussed below.

185. The take up of deferred payments should reflect the **makeup of people in care homes** – as such we expect they will cater main to disabled and older people, predominantly women.[ii]

186. A detailed equalities analysis based on available research is below: [iii]

187. **Disability:** People in residential care almost exclusively have a disability or mental impairment. A 2004 study attributes residency to the following conditions in order of priority: Incontinence; dementia; stroke; heart disease; arthritis; diabetes and endocrine; depression; fractures; lung and chest disease; cancer; epilepsy and Parkinson's disease.[iv]

188. Deferred payments will help this group arrange appropriate care and support without selling their home at the same time.

189. **Age:** Residential care users are predominantly older people. A 2006 census of UK homes found that 92% of residents are aged over 75, and 60% are over 86.

190. **Gender:** 78% of residents are female. This is generally accepted to reflect two factors: i) increased longevity amongst women is associated with a higher prevalence of age-specific disability; ii) women are more likely to survive male spouses and have less access to informal care.

191. Deferred payments may particularly benefit **lower and middle socio-economic groups**, specifically homeowners with limited income and savings to fund their care. This is the group likely to be at greatest risk of selling their home to pay for residential care.

192. We note that authorities have, to date, been less willing to offer a deferred payment to credit risks including those with pre-existing debts or charges on their property or whose home is co-owned. These groups will probably tend to belong to lower social economic groups. The department is consulting on how to ensure these groups can safely have a deferred payment.

193. Deferred payments may benefit **carers** by allowing them to live in the residents home (with the residents consent of course). This will particularly help carers who whose right to live in the home

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[i] *Caring for our Future,* Workshop on Funding Reform held 22 November. A summary can be found at: http://caringforourfuture.dh.gov.uk/2011/11/23/22-november-workshop-summary/

[ii] Statistics for Gender, Age and Disability are drawn from *Care of Elderly UK Market Survey,* 2011-12, Laing and Buisson (2012)

[iii] Statistics for Gender, Age and Disability are drawn from *Care of Elderly UK Market Survey,* 2011-12, Laing and Buisson (2012)

[iv] Summarised in Laing and Buisson (

is not already guaranteed under CRAG (i.e. those who are not spouses or civil partners or included in the list of relatives in the guidance).[v]

194. Deferred payments will not differentiate based on **sexual orientation or transgender status..** It is possible there will be differential levels of take-up between heterosexual/non-trans people and LGB or transgender people but the evidence for this is unclear:
   - There is not hard evidence for the proportion of LGB or T individuals in residential care
   - All things being equal, one would expect this to reflect that the older population at large.
   - There are grounds to expect a *higher* representation of LGB or T individuals in residential care:
       o Older LGB and T individuals may be less likely to have children, and
       o Are more likely to live alone or to experience isolation
       o This factors may mean that LGB and T individuals are more likely to need residential care because they have less access to informal care.
   - However, some studies suggest LGB and T individuals tend to delay using residential care because of concerns about discrimination in care.

195. **Race:** Deferred payments will not differentiate between users based on race, but it may be the case that certain ethnic groups are less likely to take-up a deferred payment or may be less likely to qualify.

196. The Joseph Rowntree Foundation note that the proportion of the minority ethnic population living in care homes is smaller than the white population living in care homes, and that older people from ethnic minorities are more likely to have be living in larger households and a household with one or more carer.[vi]

197. Based on this, it may be the case that the white population is more likely to use residential care and therefore to use a deferred payment.

198. **Belief:** Deferred payments may be compared to a loan. The departments proposals include allowing authorities to charge a rate of interest that is sufficient to cover their own borrowing costs.

199. Interest is currently only charged on deferred payments when repayment occurs more than 56 days after the person dies and some authorities also apply administration charges.

200. We note that the payment of interest and charges on deferred payments may present a barrier to Muslim care users. This is because of the tenets of Shariah (Islamic law), which prohibits the payment of interest.

201. The Department plans to review practice in this area and will discuss the issue of interest and charges with Muslim groups. The consultation asks for evidence of equalities impacts and specifically in relation to this issue.

202. **Socio-economic status:** Deferred Payments will benefit homeowners with limited income and savings to fund their care, who would otherwise face selling their home when faced with residential care fees.

203. The consultation notes that authorities have, to date, been less willing to offer a deferred payment to certain groups, including those with pre-existing debts or charges on their property or whose home is co-owned. This is because authorities are concerned they will have difficulty recovering the deferred payment. These groups will probably tend to belong to lower social economic groups.

204. The department is consulting on how to ensure these groups can receive a deferred payment. It will take into account the impact on specific groups as part of this process and would be interested in hearing views from those concerned.

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[v] The CRAG rules recognise that a resident may wish for their carer to live in their home, and gives Councils the option to reduce social care charges so as to prevent the home being sold (in effect treating the carer in the same way as a spouse, civil partner or dependent relative. However, there is limited use of these powers based on a 2007 FOI survey. Guaranteeing the availability of a deferred payment will allow carers to live in the resident's home if this is what both parties would like.
[vi] *Changes in communal provision for adult social care: 1991-2001,* Joseph Rowntree Foundation (2006)

205. **Summary of analysis:** Deferred payments benefit people in residential care and their families. The population using care is almost exclusively disabled (physically or mentally) and is predominantly female and aged 75+.

206. Deferred Payments will predominantly benefit homeowners with low income and / or savings, who tend to belong to lower and middle socio-economic groups.

207. Deferred payments will not differentiate on the basis of race, however ethnic minorities are less likely to use residential care and because of this may take up fewer deferred payments.

208. Deferred payments will not differentiate on the basis of faith, however charging of interest may pose a barrier to faith groups who have objections on religious grounds. This is an issue we will discuss with Muslim Groups.

209. There are no grounds for a differential impact on sexual orientation, marriage or civil partnership.

Protected Group	Specific Impact	Mitigation Action
Age	Deferred Payments will predominantly benefit older people and their families	
Disability	Deferred Payments will almost exclusively benefit people with disabilities and their families	
Gender reassignment	Non-trans people may be more likely	

Deferred Payments will not differentiate on this basis.

210. Table 17 provides an overview of our overall equalities analysis.

Table 17 – Overview of equality analysis

	to enter residential care and take up deferred payments than trans people	
Pregnancy and Maternity	n/a	
Race	The white population is more likely to use residential care / deferred payments than ethnic minorities.	
Religion or belief	Muslims and other faith groups may object to charging of interest	We will consult with religious groups to understand how we could address any such concerns.
Sex	Women are more likely than men to use residential care / deferred payments	
Sexual Orientation	People from the LGB community may be more likely to enter residential care and take up deferred payments than people from the heterosexual community.	
Marriage and Civil Partnership*	n/a	
Socio-Economic Status**	Deferred payments benefit homeowners with low income and savings who face selling the home. This group is potentially more likely to have pre-existing charges or to co-own their property, potentially making it more difficult to access a deferral	We are consulting on how best to resolve this type of situation and wish to take on board comments from those affected.

* Only needs to be considered with regards to the first aim of 'Eliminating discrimination, harassment and victimisation'.
** Not required by the equality duty but voluntarily considered by DH

Specific impacts

211. The Department has further considered the following specific impacts.

212. **One in, two out:** The impacts presented in this impact assessment do not fall under the one in, two out rule as deferred payments do not involve new burdens on business or civil society.

213. **Sunset clause:** As above, the obligation to include a sunset clause does not apply as deferred payments do not involve new regulation on business or civil society.

214. **Micro enterprise exemption from regulation**: Deferred payments do not involve new regulation on business or civil society.

215. **Small Firms Impact Test:** Deferred Payments do not affect small firms. We discuss regulatory impacts below relating to equity release providers, which are exclusively larger businesses.

216. **Competition:** The Government does not consider a deferred payment to be a financial product. The deferred payment has a very specific purpose – it helps people who would otherwise need to sell their home to pay for residential care to delay the need to do so. This need is not catered for by existing financial services. Insurance-based products do not delay the need to sell the home (because they involve a large upfront premium) and equity release is not a suitable option for people who move into residential care, as providers condition access to equity release on the home being occupied (as outlined in section II of this impact assessment).

217. Moreover, as outlined in section III, the Department thinks that people should receive an overview of their financial options, including full information about all alternatives to a deferred payment, so that they can chose the option which fits their needs best. The Department will develop this support to homeowners in conjunction with the care sector.

218. On this basis, we do not anticipate competition impacts.

219. **Environmental and sustainability impacts**: Paras 116 – 119 outline the potential risk that some (though not all) deferred payments may lead to situations where homes are not occupied and are poorly maintained (which in the most serious cases could lead to environmental and sustainability impacts). However, as noted the scheme will include proposals to support people to maintain, sell or rent their property to mitigate these issues. This impact assessment assumes these policies prevent and offset these impacts. The consultation will gather evidence on this

220. **Human rights:** There will no negative impact on human rights.

221. **Justice system impacts:** Deferred Payments has no implications for the justice system.

222. **Rural proofing:** Deferred Payments will be available regardless of local authority area and there is no reason to expect an inequitable impact on rural residents.

Annex A: Modelling of Social Care Funding Reforms

A1. On this basis, we do not anticipate competition impacts. The costs presented in this Impact Assessment are projections of the likely costs. They are based on a series of assumptions about future trends in relevant factors, including demography, the prevalence of disability and unit costs of care services.

A2. It should be noted that the costs have been estimated on the basis of national average data, and so are unlikely to fully reflect the variation in social, economic and demographic conditions in individual local authority areas.

A3. This annex provides further information on the modelling and analysis used to estimate the costs of the reforms.

Older Adults

A4. The increased public expenditure due to the increased state support for older adults due to the cap and extended residential care means test are modelled using the DH social care funding model. *The model does not make forecasts about the future*. It makes projections on the basis of specific assumptions about future trends.

A5. The DH social care funding model is an excel based micro-simulation model which runs using VBA code. DH analysts designed and developed the model to analyse different funding reform options, including changes to the social care means test and the implementation of a capped cost system. The key outputs of the model are total public spend on older adult social care and the distribution of spend by income and wealth of the different reforms. The model also allows the impact of different reforms to be analysed at an individual level.

Figure A1: Older adults modelling architecture


DH social care funding model architecture
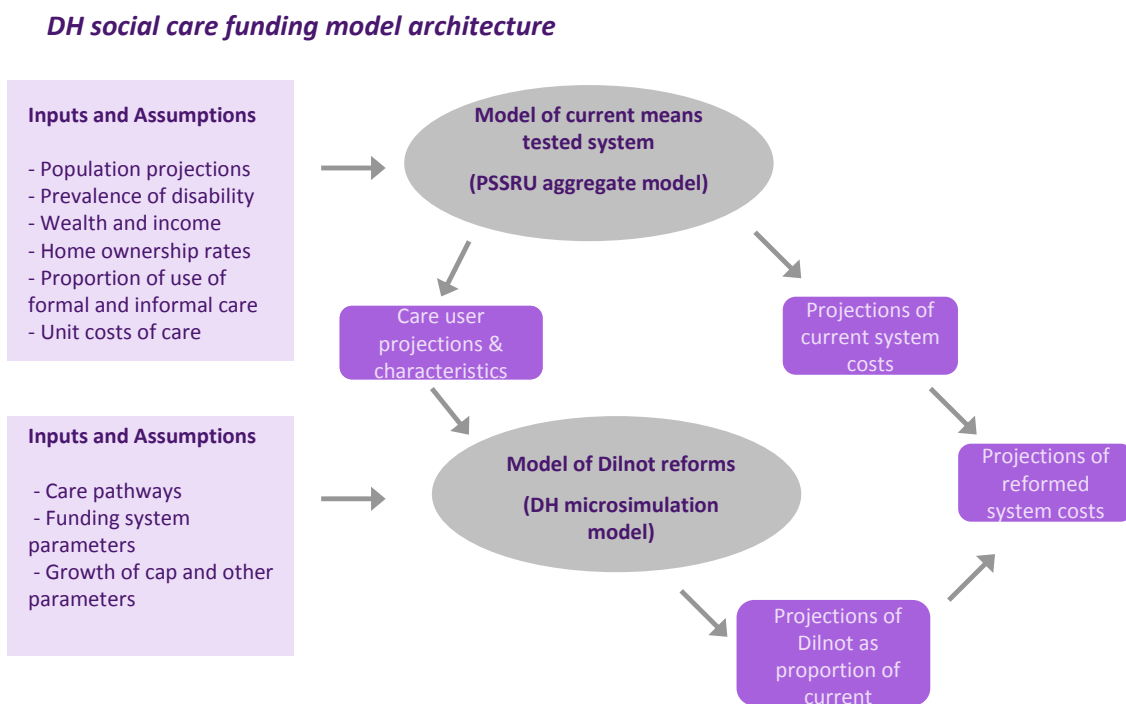
A6. The DH model fits into a modelling architecture where the DH model takes inputs from the Personal Social Services Research Unit (PSSRU) aggregate model on the future projections of the number of care users and their characteristics and the projected costs of the current system. This forms the baseline onto which the % increase in costs for the reformed system estimated by the DH model is applied to produce the final cost estimate.

A7. The DH model is a cross-sectional model that retro speculatively simulates uncompleted care journeys of a representative cross section of care users in the cross-sectional month being

modelled. It independently models October in the years 2010/11 to 2025/26. These yearly mid point estimates are multiplied up to produce year estimates.

A8. The base sample used in the model is the ADL (activity of daily living) disabled 65+ population from wave 4 of the English Longitudinal Study of Ageing (ELSA)[vii]. It models 5 care settings separately; nursing homes, residential homes and 3 levels of home care (low, medium and high intensity).

A9. For each care setting the model runs a representative sample through an individual care pathway model. The representative sample is generated by weighting the sample for each year and care setting using weights derived from outputs from the PSSRU aggregate model of the number and characteristics of care users.

Figure A2: VBA structure of DH social care funding model
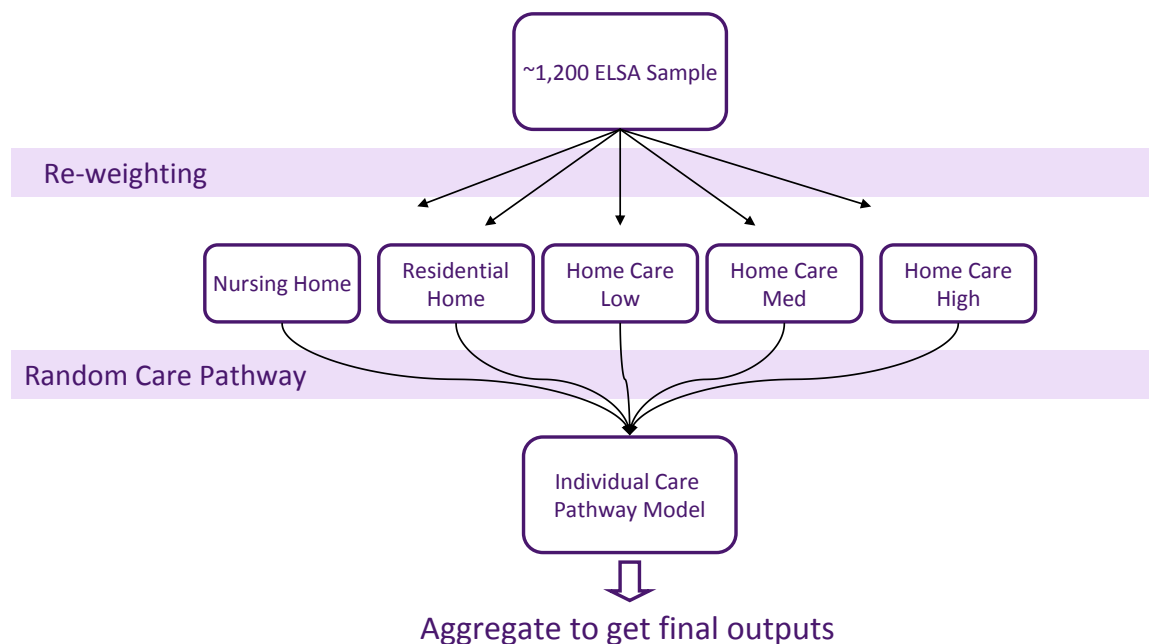
A10. Each individual in the sample is randomly assigned an uncompleted care pathway from a derived distribution of all uncompleted care pathways. The survey data used to derive the distribution is length of stay in (BUPA) care homes (PSSRU) [viii], Admissions to care homes and home care survey 2005 (PSSRU) [ix] and 2006 User Experience Survey[x]. Monte-carlo methods are used to average out the variation in outputs resulting in the random selection of care pathways.

A11. The individual care pathway model computes the state and private spend for each month of the care pathway, this is dependent on the individuals characteristics (income, wealth, household type, housing tenure) and the funding system being modelled. The quantities of the cross-sectional month are aggregated using the weights to produce population level estimates.
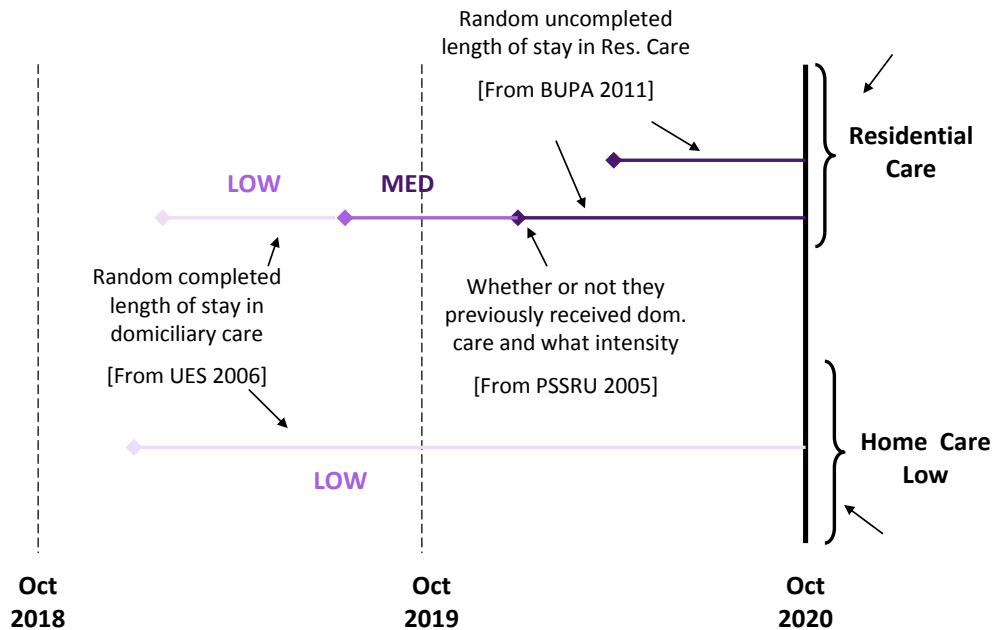

[vii] http://www.ifs.org.uk/ELSA

[viii] PSSRU DP 2769 – Jan 2011 – Commissioned by BUPA

[ix] PSSRU DP 2265/3 – July 2006

[x] User Experience Survey 2006

Figure A3: Modelling of uncompleted care journeys

Each person in care at the cross section is assigned a randomly assigned uncompleted care pathway

Random uncompleted length of stay in Res. Care

[From BUPA 2011]

LOW   MED

Residential Care

Random completed length of stay in domiciliary care

[From UES 2006]

Whether or not they previously received dom. care and what intensity

[From PSSRU 2005]

Home Care Low

LOW

Oct 2018   Oct 2019   Oct 2020

Assumptions in the PSSRU aggregate model

A12.   The majority of the assumptions are relevant to the projections of future costs for the current system, as well as projected the increased spend of the reformed system. From the interaction with the PSSRU aggregate model these assumptions follow through into the projections of cost of the reforms.

The key assumptions in the PSSRU aggregate model are:

KEY ASSUMPTIONS OF THE BASE CASE OF THE PSSRU MODEL
- The number of people by age and gender changes in line with the Office for National Statistics (ONS) 2008-based population projections.

- Marital status changes in line with GAD 2008-based marital status and cohabitation projections.

- There is a constant ratio of single people living alone to single people living with their children or with others and of married people living with partner only to married people living with partner and others.

- Prevalence rates of disability by age group (65-69, 70-74, 75-79, 80-84, 85) and gender remain unchanged, as reported in the 2001/2 General Household Survey (GHS) for Great Britain.

- Home-ownership rates, as reported in the 2001/2 Family Resources Survey (FRS), change in line with projections produced by the University of East Anglia.

- The proportions of older people receiving informal care, formal community care services, residential care services and disability benefits remain constant for each sub-group by age, disability and other needs-related characteristics.

- Health and social care unit costs remain constant in real terms to 2015 and then rise by 2% per year in real terms (but non-labour non-capital costs remain constant in real terms).

Annex B - Social welfare effects of empty homes

B1. Under the central take-up estimate in this impact assessment, the offer of deferred payments is expected to result in about 6,000 homes being withdrawn from the housing market (by 2015/16), as their owners take out a deferred payment *and* decide not to rent out their property (see table 3 in the main body of the assessment for estimates).

B2. This Annex sets out the potential welfare implications of this reduction in housing supply. It should be noted that the calculations in this Annex operate under a number of simplifying assumptions:
- The housing market in England can be thought of as one unified market. In reality, there are many local housing markets, in which demand and supply elasticities, as well as the incidence of deferred payments will vary;
- Supply of housing is inelastic (this assumption is relaxed later on in this Annex);
- The housing market works in a frictionless manner, so that even small price pressures are passed on to consumers (the impact of this assumption is discussed below).

Impact of a reduction in supply under inelastic supply

B3. Figure B.1 demonstrates the impact of a reduction in the supply of housing, under the – simplifying - assumption that supply for housing is perfectly inelastic in the short run. In the figure:
- D is the demand for housing (and the marginal benefit of housing)
- S and S' are the supply for housing before and after the introduction of universal deferred payments (assumed to be perfectly inelastic otherwise)
- p and p' is the market price before and after the change.

Figure B.1 – Empty homes resulting from supply shock (inelastic supply)
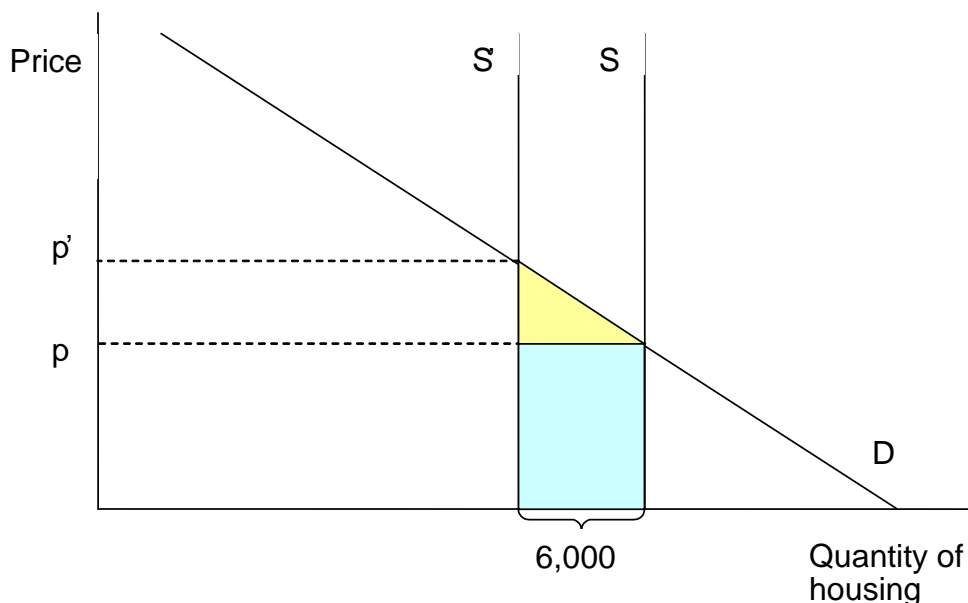
B4. If supply is perfectly inelastic, in the short run, the number of occupied homes will decrease by 6,000 because of the additional deferred payments taken out. This reduction will have three major impacts:
- A reduction in consumer surplus as some people are priced out of the market and lose the use value of accommodation (minus the cost, e.g. the rent) – this is the yellow triangle;
- Prices in the housing market (i.e. house prices and rents) will increase and, as a result, there is a transfer of wealth from buyers/renters to sellers/landlords – this is the rectangle to the left of the yellow triangle.
- A loss of producer surplus: rent (or equivalent income) foregone to people taking out a deferred payment.

B5. In a first step, we quantify these welfare effects under the assumption of inelastic supply, before relaxing that assumption.

B6. **Loss of consumer surplus:** The loss of consumer surplus associated with the reduction in available housing is equal to the area of the yellow triangle. As we can see from the above figure, the size of this area will be determined by the gradient of the demand curve, i.e. the price elasticity of demand. The more elastic the demand for housing, the less housing prices will need to rise to squeeze out the excess demand resulting from the reduction in supply.

B7. We estimate the relevant elasticity of demand to be around -0.5[xi]. This suggests that a 1% increase in prices will, all other things being equal, reduce the quantities of housing demanded by 0.5%.

B8. A reduction in the housing supply by 6,000 homes is equivalent to a shift in supply by 0.027% (as there are about 22m households in England)[xii]. With an elasticity of demand of -0.5 and based on our assumption of perfectly inelastic supply, this can be expected to push up prices by 0.055% (=0.027%/0.5*1).

B9. Assuming an average rent of £1000[xiii] per month, or £12,000 per year, this would result in a small increase in housing prices per household of approximately £6.5 per year. Based on this, we can calculate the loss in consumer surplus as the area of the yellow triangle:

Consumer surplus loss = ½ * change in quantities * change in prices
= ½ * 6,000 * £6.5 = **£20,000 per year**

B10. **Effect on market rents and transfer:** In figure B.1, the reduction in housing supply leads to an increase in annual housing prices by £6.5 per year. Across the 22m households in England, this is a transfer of £144m per year from renters/sellers to landlords/ buyers. However, as will be set out below, the actual increase in prices will be mitigated as supply is not perfectly inelastic. Instead, part of the excess demand will be met by an increase in the number of houses supplied, so that the over all increase in prices will be less than indicated.

B11. **Foregone rental income:** Finally, as 6,000 homes are taken off the market and not rented out, their owners forego the potential income from renting (or, indeed, selling them). At a rent of £12,000 per year, this is a total reduction in rental income of £72m per year. The social welfare effect of this reduction in rental income is uncertain:
- As people decide not to rent out their house, they must value doing so more than the rent foregone, so that, arguably, they do not lose out;
- However, there is a risk that they misjudge their own utility;
- People in residential care may value the additional income generated from renting less because they have little consumption use out of it. Its value to their family may be higher, so that there could be an externality imposed where homes go unrented. However, in practice, the risk of this externality is often mitigated because people's families are likely to be involved in the decision-making and, indeed, the management of the rental process. Maintaining one's assets for one's heirs is one likely motive of people taking out a deferred payment, so that people may well factor in their families interests when making the decision whether or not to rent.

Calculating the shift in prices and quantities under elastic supply

B12. The above presentation is limited by the assumption that supply is perfectly inelastic. In reality, however, the supply for housing is likely to be at least somewhat elastic, as higher prices attract both more building activity (in the medium run), but also set incentives for landlords to ensure their property is let out.


[xi] This is at the higher range of what is identified in the literature: Ermisch et al 1996 estimate it to be: –0.35 while King 1980 estimates it to be –0.5.
Ermish et al: 'The Price Elasticity of Housing Demand in Britain: Issues of Sample Selection', Journal of Housing Economics, Vol. 5, pp.64-86.
King 1980: 'An Econometric Model of Tenure Choice and Demand for Housing as a Joint Decision', Journal of Public Economics, 14, 137-159.
[xii] DCLG English Housing survey 2010/11: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/6739/2173283.pdf
[xiii] This is above the average rent in England GBP731, as shown here: http://www.lslps.co.uk/documents/buy_to_let_index_feb13.pdf. However, we take £1,000 per month to be a cautious approximation of the equivalent price of the average household, to take into account that owned property may well be bigger, and therefore on average more expensive than the average rented property.

Figure B.2 – Empty homes resulting from supply shock (elastic supply)
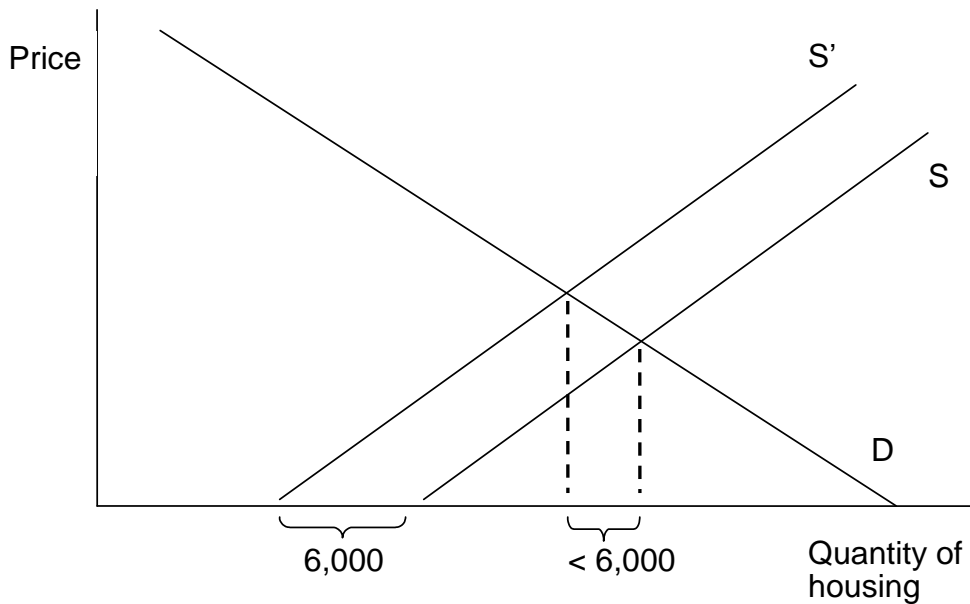
B13. As a result, as figure B.2 shows, the final reduction in the number of available homes resulting from the introduction of universal deferred payments will be less than 6,000 and, consequently, the increase in market prices will be less than indicated above.

B14. We estimate that the elasticity of supply ranges between 0.28[xiv] and 0.45[xv] and, as our central estimate, take it to be about 0.35. The overall effect on prices will depend on the interaction of demand and supply elasticities.

B15. We can estimate this impact by calculating approximate inverted, linear demand and supply curves:

Quantity demanded (in million homes) = X – a * p (price in £ per year)
Quantity supplied (in million homes) = Y + b * p (price in £ per year)

Where:
- X and Y are the quantities demanded/supplied (in millions) if the price of housing is zero;
- a and b are the slope coefficients of demand and supply.

B16. For the demand curve, we know that:
- Given a demand elasticity of -0.5, a 1% change in prices (£12,000*1%= £120) will lead to a 0.5% change in quantities demanded (£22m * 0.5% = 0.11m)
- Therefore the slope of the inverted demand curve is:
  a = change in quantity/ change in price = 0.11/ 120 = 0.000917
- At a price of £12,000, the quantity demanded is 22 (million). This allows us to solve for
  X = 22 + 12,000*0.000917 = 33
- This gives the inverted demand curve: D = 33 – 0.000917*p

B17. For the supply curve, we know that:
- Given a supply elasticity of 0.35, a 1% change in prices (£12,000*1%= £120) will lead to a 0.35 change in quantities supplied (£22m * 0.35% = 0.077m);
- Therefore the slope of the inverted demand curve is: a = change in quantity/ change in price = 0.077/ 120 = 0.000642;

[xiv] Levin and Price 2009: Understanding the Drivers of the Price Elasticity of House Supply and the role of Real Interest Rates and Cyclical Asymmetries
http://www.gwilympryce.co.uk/housing/Levin_&_Pryce%20_HousingSupply.pdf

[xv] OECD 2011: Housing markets and structural policies in OECD countries, Economics Department Working Paper No.836

- At a price of £12,000, the quantity supplied is 22 (million). This allows us to solve for Y = 22 - 12,000*0.000642 = 14.3
- This gives the inverted supply curve: S = 14.3 + 0.000642*p

B18. Equilibrium is given where Demand = Supply, i.e.:
- 33 – 0.000917*p = 14.3 + 0.000642*p
- 18.7 = 0.001558*p
- p = 18.7/0.001558 = 12,000

B19. As 6,000 houses are taken off the market, the supply curve shifts to the left by 6,000 units of housing, which can be described by a reduction in Y by 0.006 (million homes). The new supply curve is thus:

S' = 14.294 + 0.000642*p

B20. The new equilibrium is where S' = D:
- 33 – 0.000917*p = 14.294 + 0.000642*p
- 18.706 = 0.001558*p
- p= 12,003.85

B21. The new equilibrium price is thus: £12,003.85 per year. In other words, taking into account supply and demand elasticities, we expect an increase in average prices/ rents by £3.85 per year.

B22. The resulting quantity of homes can be estimated by inserting this result into the demand curve:
- D = 33 – 0.000917*£12,003.85 = 21.996470 or 21,996,470 homes.

B23. In other words, the number of homes falls by 3,530 (=22,000,000 – 21,996,470) rather than 6,000 as estimated under the assumption of inelastic supply.

Welfare effects under elastic demand and supply

B24. **Effect on market rents and transfer:** Prices are estimated to increase by £3.85 per household per year. Using the same line of reasoning as in para B10, this results in a transfer of about £85m per years from buyer/renters to sellers/landlords (=£3.85* 22m). From a societal perspective, this transfer is a priori neutral. However, to the degree that homeowners and landlords are more wealthy than renters and buyers, there may be a loss of social welfare resulting from a transfer to these groups.

B25. This is particularly the case in the private rental market (17% of all households[xvi]), while it may or may not be the case in the owner-occupier segment of the market (66% of the market), depending on individual circumstances. Indeed, in some cases, the buyer may very well be more wealthy/ have more income than the seller (e.g. where people scale down because they cannot afford to maintain the larger property or because they need to access the wealth stored in the house).

B26. We approximate the potential welfare loss by assuming that, in the private rental sector any increase in rents is a transfer from a group in the second income quintile (renters) to a group in the top quintile (landlords). Using Green Book equity weights for these income groups[xvii], this suggest a social welfare loss of about **£13m per year** (=£85m * 17% * (1.3- 0.4), where the latter term is the difference between the suggested equity weights for these groups).

B27. However, it should be noted that this welfare loss will only occur under the condition that markets function in a frictionless enough way to pass on this small, one-off supply shock. As with other goods, suppliers of housing factor in "menu costs" and wider pricing strategies when deciding whether or not to adjust prices. For instance, rents are typically adjusted in steps of £10s per month, while the price pressure resulting from 6,000 empty homes is thought to result in an

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[xvi] English Housing Survey 2010/11: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/6739/2173283.pdf
[xvii] http://www.hm-treasury.gov.uk/d/green_book_complete.pdf, p94

average increase in prices of about £0.30 per month, suggesting that the price pressure may not be passed on to consumers.

B28. **Effect on rents foregone:** Elastic demand also suggests that the overall volume of rents foregone is less than predicted, when considering inelastic supply. While about 6,000 homeowners take their home off the market as a result of deferred payments, other landlords (or sellers) fill some of the supply shortage by putting previously unused properties on the market. As a result the total rent foregone adds up to **£42m** per year (=3,500 homes * £12,000 per year). As above set out above, the social welfare effect of this reduction in rental income is uncertain as people *decide* not to rent out their house, they must value doing so more than the rent foregone.