How can investors drive up labour standards in the English care sector?

Findings based on study by Dr Caroline Emberson, Dr Subhan Ullah and Nimarta Keswani, October 2024[i]

The adult social care sector is already under stress, with evidence both of problematic labour conditions and a lack of financial sustainability. This research, funded by Friends Provident Foundation, seeks to highlight the role investors can play in helping to improve labour standards throughout this sector which is of large and growing significance to the UK labour market.

Key findings

Due to the complex financial ownership structures within the English social care sector, there is a need to go beyond typical shareholder engagement if labour exploitation problems in the sector are to be addressed.

Our analysis of ethical reporting based on the CCLA modern slavery benchmark scoring system reveals that 48 out of 58 companies (82.8%) of our sample had produced an annual modern slavery statement. While this represents a majority, it also highlights a significant gap, with 17.2% of these major providers failing to meet their legal transparency obligations. Among those reporting, there is also considerable variation in the quality and comprehensiveness of disclosure. On average, companies scored just 36%, with scores ranging from 8% to 73%. Only a few providers demonstrate good practice with just four providers scoring 50% or above, and 37 providers falling in the 25-49% range, indicating substantial room for improvement.

In 55 of the largest 59 care providers in England (where the type of ownership could be identified), the majority of organisations have some form of private ownership. Twenty-three organisations (39%) were privately-owned companies; 11 providers (20%) were owned by private individuals; 9 (16%) were private companies limited by guarantee without shareholders, and a further 9 (16%) were owned by overseas entities. A further 3 organisations were registered societies.[ii] Each of these organisations had complex and multi-tiered links to various types of institutional investor.

Our initial analysis suggests that owners of financial assets such as pension funds, charitable foundations, and other investors may all invest in the English care sector. These investments can be managed directly by the asset owners and/or through investment managers. Some of this money flows into funds (including private equity funds and real estate funds). Money also goes into other investment vehicles like publicly listed real estate investment trusts (REITs).[iii] Ultimately, investments reach the care sector in a variety of ways, including providers of care and care properties. Banks are also involved in the sector through mortgages and business loans.

Yet, due in part to the opacity of these ownership structures, the role investors do – or could – play in addressing poor quality working conditions in the sector has yet to be fully examined.[iv]

Why is this important?

The adult social care sector in England is both important and troubled, socially and financially. There is evidence of a wide spectrum of abuse, including payments below legal national wage levels and more serious forms of exploitation, such as debt bondage, and threats of the withdrawal of sponsorship leading to the risk of deportation.

The social care workforce in England is already very large with around 1.79 million, predominantly female, workers employed in 2022-23. Forecasts suggest that by 2035 a further 490,000 care workers may be required if the demand for care is to be met.[v] Yet low wages and a lack of career progression have led to recruitment difficulties, with an estimated 152,000 vacancies reported in 2022-23.[vi]

The previous government turned to transnational migrant workers to address this shortfall, with 146,477 visas issued to main applicants in 2023 under a 'Health and Care Visa' sponsorship [vii] Commensurate with this expansion of the shortage occupation scheme, however, came a spike in the number of labour exploitation cases reported by care workers to the UKs Modern Slavery Helpline; 918 potential victims were identified in 2023.[viii]

In 2017, the Competition & Markets Authority (CMA) valued the care home sector as worth around £15.9 billion a year and raised serious concerns about its long-term operational and financial sustainability, particularly among those providers of care for local authority-funded placements.[ix] In 2019, research by the Centre for Health and the Public Interest (CHPI) reported a profitability gap between large private equity backed providers and voluntary organisations, raising concerns about profit leakages through rents, dividend payments, net interest payments, 'sale and lease back' property arrangements and directors' fees.[x]

Investors therefore have a key role to play in ensuring the care sector's financial and social sustainability. Given this influential position, they can also demand higher labour standards in the companies they finance.

Recommendations

We make the following recommendations for investors and the UK government:

- **Recommendation 1:** Investors such as private equity companies, publicly listed REITs, and other real estate holders should adopt measures to strengthen investor stewardship, set and monitor labour standards, conduct labour-related due diligence and post-investment monitoring on the companies in whom they invest, and introduce contractual obligations in leases and through red lines related to the quality of care and work.
- **Recommendation 2:** Pension funds, other asset owners, and their investment managers should explicitly expect private equity companies, publicly listed REITs, and other real estate investors to follow recommendation 1.
- **Recommendation 3:** The UK Government should legislate to ensure that care workers in the UK have the right to organise and engage in collective bargaining.
- **Recommendation 4:** The UK Government should ensure that any funding improvements are tied to care quality and minimum safe staffing levels.
- **Recommendation 5:** The UK Government should mandate the disclosure of legal ownership structures and human capital metrics within annual statements prepared in response to section 54 of the UKs (2015) Modern Slavery Act.
- **Recommendation 6:** The UK Government should launch a public inquiry into working conditions within the care sector.

Research overview

Within a mixed methods study, we analysed financial performance and ethical reporting in the care sector.

Analysis of financial statements

Financial statistics for 57 of the 59 largest English care providers monitored by the Care Quality Commission under the Care and Support (Market Oversight Criteria) Regulations 2015 were collated for further examination. For each of these companies, financial data and ratios for the past five years were extracted from the 'Financial Analysis Made Easy' (FAME) database.[xi]

Review of annual statements

In addition, published modern slavery statements for the year 2023-24 were downloaded from each companies' website and coded using the 48 questions detailed in the CCLA Modern Slavery UK Benchmark.[xii]

Case studies and interviews

Six case studies representing different ownership structures and levels of ethical reporting were prepared and suitable investor interventions in each case were discussed with interviewees.[xiii] Eight interviewees were conducted with representatives from two pension funds; a real estate investor; a specialist healthcare private equity fund; two UK trade unions and one global trade union; and a Canadian organisation that supports responsible investing.[xiv]

Results and conclusions

Our research suggests that the English care home market is financed by both UK-based and foreign institutions. Approximately 16% of the care providers in our sample have substantial foreign ownership and such investment is channelled through overseas parent companies. It may be more difficult to hold overseas institutions accountable owing to their distant nature.

Our analysis also shows evidence of financial engineering in the sector, with sell and lease-back arrangements to legally distinct entities. Against this backdrop, there is apparent evidence of financial distress. Approximately 33% of the companies showed current ratios below 1.0 in 2023, suggesting potential liquidity issues in the sector. Furthermore, 44% of the providers had negative profit margins in the same year, highlighting the challenging economic environment in the sector. Solvency ratios have seen decline across many providers, with some ratios dipping below 50%, indicating increased long-term financial vulnerability. Additionally, gearing ratios for 30% of the providers have exceeded 100%, signalling heavy reliance on debt financing, further amplifying future financial risk.

With over 70% of a providers' operating budget allocated to labour costs and limited economies of scale, the level of investment return is linked closely to labour costs.[xv] There was no evidence from the investing institutions we interviewed of any appetite to require companies to increase wage levels above the legal minimum. The gender pay gap also remains a persistent issue in this part of the care sector. Our analysis of the reported figures shows that the average mean gender pay gap across the sampled companies is 5.8%, with a median of 1.9%. However, there is significant variation, with some providers reporting gaps as high as 32%. While the sector employs a predominantly female workforce, men are disproportionately represented in higher-paying managerial roles, contributing to this disparity.

Implications & Recommendations

As one of our interviewees explained, "Care companies end up in these sorts of ESG funds because they're seen as more climate friendly investments". Yet until social issues are given the same weight as environmental concerns, current investment in some parts of the care sector risk being neither financially nor socially sustainable. To address the challenges highlighted by our research, our interviewees recommended the following actions:

Recommendation 1: Investors such as private equity companies, publicly listed REITs, and other real estate holders should adopt measures to strengthen investor stewardship, set and monitor labour standards, conduct labour-related due diligence and post-investment monitoring on the companies in whom they invest, and introduce contractual obligations in leases and though red lines related to the quality of care and work.

Labour-related due diligence processes could include monitoring of care operators to make sure that they meet certain conditions. In one of the organisations we interviewed, the sustainability team had the final say on the inclusion of investments in the portfolio with specific attention paid to human and labour rights issues. In another, due diligence processes are supplemented by relationship building with operating partners. A further interviewee from the private equity sector explained how company engagement programmes were introduced to support the development of appropriate internal management structure and systems for those considered high risk. Where private equity capital was involved, one interviewee reported how, should the board not set and maintain the desired culture and standards, changes could be made to the senior management team. The speed with which such action is possible is evidence of the opportunities offered in private-equity governance.

Real estate investors and REITs can set standards through their contractual obligations and leases, including commitments to fair pay, correct working conditions and adequate training. Where Care Quality Commission inspections have lapsed, regular internal and external auditing can be used to ensure that care quality and labour standards are maintained.

Recommendation 2: Pension funds, other asset owners, and their investment managers should explicitly expect private equity companies, publicly listed REITs, and other real estate investors to follow recommendation 1.

They can set red lines related to social metrics for private equity institutions, negotiate a place on private boards and, with regards publicly-listed companies like REITs, use shareholder engagement and escalation. Social metrics could also be included as part of bond issuance more broadly.

Recommendation 3: The UK Government should legislate to ensure that care workers in the UK have the right to organise and engage in collective bargaining

Our interviewees reported that there is currently no legal right for trade unions to access and organise workers in many parts of the care sector. They believed legislation should be introduced to guarantee trade union access and collective bargaining rights across the care sector. This would enable unions to educate workers about their basic rights and entitlements, which many are currently unaware of due to lack of exposure. Without collective bargaining rights, workers are left without support in negotiating better wages, sick pay, or holiday entitlements.

Recommendation 4: The UK Government should ensure that any funding improvements are tied to care quality and minimum safe staffing levels.

Some interviewees reported that parts of the sector were in a weak and precarious position. Revenue is limited due to the current levels of local authority funding which, in some cases, fails even to cover operating costs. One interviewee believed that standards could be improved through a revised funding offer tied to a stricter regulatory regime, including the stipulation of minimum staffing ratios.

Recommendation 5: The UK Government should mandate the disclosure of legal ownership structures and human capital metrics within annual statements prepared in response to section 54 of the UKs (2015) Modern Slavery Act.

Interviews with trade union representatives highlighted the lack of transparency around the ownership structures and financial practices of many care providers. Several of our interviewees believed that increased public disclosure and scrutiny, as has been introduced in the United States, could lead to a greater focus on issues such as labour rights, not seen currently as financially material. System-wide disclosure about employment was described as 'very patchy' with basic detail related to staff turnover levels difficult to obtain. Other human capital metrics such as levels of absenteeism and employee wellbeing surveys could also usefully be included. Though disclosure does not necessarily change practices, it opens the possibilities for further conversation.

Recommendation 6: The UK Government should launch a public inquiry into working conditions within the care sector.

The regulatory gap that exists between the Gangmasters and Labour Abuse Authority, who have no remit to license care providers, and the Care Quality Commission, whose inspections focus primarily on care quality, means that the labour conditions of care workers may not currently be adequately monitored.

The inquiry should examine alternative funding models for social care. The existing economic model risks perpetuating the prioritisation of investors' interests over the remuneration of frontline staff. It should also review international examples such as policies introduced in other countries to increase public disclosure requirements for care home ownership; and address the broader issue of unregulated terms and conditions that leave workers vulnerable to unfair treatment and exploitation.

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[i] https://www.nottingham.ac.uk/research/beacons-of-excellence/rights-lab/research-projects/analysing-financial-structure-transparency-and-accountability-in-the-care-market-in-england.aspx

[ii] More detail of the ownership relations for each of these companies can be found via the link to our published database: https://www.nottingham.ac.uk/Research/Beacons-of-Excellence/Rights-Lab/Documents/Database.xlsx

[iii] As publicly listed legal entities, regular shareholder engagement is appropriate for the management of REITs.

[iv] If you are interested in engaging in further research in this area, please contact Dr Emberson at: caroline.emberson@nottingham.ac.uk

[v] Skills for Care (2021) The state of the adult social care sector and workforce in England. Available at: https://www.skillsforcare.org.uk/adult-social-care-workforce-data-old/Workforce-intelligence/publications/national-information/EARLY-RELEASE-The-state-of-the-adult-social-care-sector-and-workforce-in-

England.aspx#:~:text=Our%20forecasts%20show%20that%20i. (accessed 03 October 2024).
[vi] Skills for Care (2023) The state of the adult social care sector and workforce in England: Key findings 2022/23. Available at: https://www.skillsforcare.org.uk/Adult-Social-Care-Workforce-Data/Workforce-intelligence/publications/national-information/The-state-of-the-adult-social-care-sector-and-workforce-in-England.aspx (accessed 17 September 2024).
[vii] Home Office (2024) Why do people come to the UK? To work. Available at: https://www.gov.uk/government/statistics/immigration-system-statistics-year-ending-december-2023/why-do-people-come-to-the-uk-to-work (accessed 17 September 2024).
[viii] Unseen (2024) Annual Assessment 2023: Working towards a world without slavery. Available at: https://www.unseenuk.org/wp-content/uploads/2024/05/Unseen-Helpline-Annual-Assessment_2023.pdf (accessed 17 September 2024).
[ix] Competition & Markets Authority (2017) Care homes market study: Final report. Available at: https://www.gov.uk/cma-cases/care-homes-market-study (accessed 17 September 2024).
[x] Kotecha, V. (2019) Plugging the leaks in the UK care home industry: Strategies for resolving the financial crisis in the residential and nursing home sector. Available at: https://chpi.org.uk/papers/reports/plugging-the-leaks-in-the-uk-care-home-industry/ (accessed 17 September 2024).
[xi] A dashboard of the key financial indicators related to each company can be found here: https://www.nottingham.ac.uk/Research/Beacons-of-Excellence/Rights-Lab/Documents/Dashboard.xlsx
[xii] The CCLA (2023) Modern slavery UK benchmark permits the evaluation of statements based on conformance with the requirements of section 54 of the Modern Slavery Act 2015; the disclosure of information outlined in the Home Office Guidance on Modern Slavery and the degree to which companies report of 'finding', 'fixing' and 'preventing' modern slavery. The scorecard used is available at: https://www.ccla.co.uk/documents/ccla-modern-slavery-uk-benchmark-2023/download?inline (accessed 17 September 2024).
[xiii] Case studies were selected to provide examples of large
not-for-profit or employee-run providers; large for-profit (private equity owned or
backed) providers; and large-for-profit (non-private equity) providers.
[xiv] Though attempts were made to negotiate access, it did not prove possible to interview representatives either from a bank or REIT.
[xv] Competition & Markets Authority (2017) Care homes market study: Final report. Available at: https://www.gov.uk/cma-cases/care-homes-market-study (accessed 17 September 2024).