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The Baroness Barran MBE
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Dear Diana,

I'd like to thank you for the interesting debate on Clauses 14 and 15 of the Children's Wellbeing and Schools Bill. These will, respectively, introduce a financial oversight scheme to increase financial and corporate transparency among the most 'difficult to replace' providers and their corporate owners; and take a power to impose, through regulations made in the future, a cap on the profits of non-local authority Ofsted-registered providers of children's homes and independent fostering agencies (to be extended to supported accommodation).

I committed to write to the House to address the questions you raised about the operation of the scheme.

The challenges facing the placements market for fostering, supported accommodation and children's homes are myriad and complex. In 2022, the Competition and Markets Authority (CMA) found that the children's social care placement market was dysfunctional. It found that the largest private providers were making profit margins significantly above what would be expected in a well-functioning market.

This Government is committed to addressing these issues so that local authorities can find homes that meet the needs of children in their care and secure value for money. This includes ensuring that we have the right homes in the right places; a more diverse market of providers; are enabling local authorities to shape the market, negotiate effectively and achieve value for money; and that we are improving the quality and stability of the market (including through the introduction of the financial oversight scheme). We are taking forward both legislative and non-legislative measures to achieve these objectives, and we will be providing further information as policy development continues.

To help deliver this there will be £560 million capital investment over 2026-30. This will include funding to refurbish and expand children's homes, and renovating and expanding foster carer homes, in order to help fix the placements market.

We have also set out in our Command Paper, Keeping Children Safe, Helping Families Thrive, our intention to work with providers, investors, and the sector at large to support them with innovative funding mechanisms – for example, social financing models like social outcomes partnerships – to break down barriers to setting up new residential care.

In relation to your specific questions on the Financial Oversight Scheme you asked whether providers might seek to restructure themselves to avoid falling within the entry criteria for the Scheme. We are aware that registered providers might seek to avoid the eligibility criteria for the Financial Oversight Scheme. We are currently working to design the eligibility criteria which will be specified in regulations, but like the Care Quality Commission market oversight scheme conditions, it is possible to reduce the risk of evasion by setting a number of different conditions. Should our analysis indicate that providers are undertaking such behaviour we will take that into account in determining whether this can be considered a failure to comply with the scheme.

The Department will have the power to issue civil monetary penalties. These could apply to any level of a provider's organisational structure, up to the parent company, that has failed to comply with the requirements of the Scheme. Furthermore, if providers do not comply, Ofsted could independently decide to utilise their existing enforcement powers to cancel or suspend registration of a provider in relation to some or all of their individual establishments or agencies. Finally, if there is any evidence of evasion, the regulations containing the oversight conditions can be amended.

Providing local authorities with advance warning that there is a real possibility a provider might close for financial reasons will support them to meet their statutory duties and find alternative placements. If a large or 'difficult to replace' provider failed financially, it could lead to them closing their doors suddenly, causing huge disruption to children who could lose their home. Without the Scheme in place, local authorities would be more reliant on readily available or emergency placements that may be 'spot purchased', expensive, and possibly unsuitable for children. This would therefore place additional resource burdens on them.

More widely, as part of our efforts to reshape the market we are providing additional support to local authorities in commissioning as well as forecasting, and market shaping.

You also asked about how we have engaged with the sector in designing and developing the Scheme and how contingency planning will work given the current market conditions. We have undertaken significant stakeholder engagement to support the development of the Financial Oversight Scheme to ensure that it is proportionate and not overly burdensome on providers. This includes discussions with the Department's Market Interventions Advisory Group (which includes representatives from across the sector) and our provider sub-group which has local authority, charity and private provider representatives. We have also worked with provider membership associations throughout.

To reduce unnecessary administrative burdens where possible and to ensure providers are prepared, we will continue this work with them in the run up to launch of the Financial Oversight Scheme to support them to understand the new requirements. Once the Scheme is up and running, we will seek provider views and feedback at regular intervals to ensure any burdens are reasonable and appropriate.

In relation to the impact of the scheme on the market, we are committed to taking a measured approach to implementing all of our reforms. We are acutely aware of the importance of not destabilising the market by doing too much too soon, at the risk of causing significant disruption to the care of our most vulnerable children and young people. It is important we can respond to ongoing changes in the dynamic children's social care market. That is why we are setting the detailed entry criteria for the Scheme in secondary legislation, which we will lay before Parliament in due course.

You also asked about the IT system that will be needed to support the implementation of the Scheme. The Department is confident that it has the resources to develop the new IT systems successfully and it has been funded as part of the 2025/26 budget. We are learning lessons from similar programmes and undertaking extensive engagement with users to develop an effective product that meets the objectives of the scheme. Similarly, we will ensure we have the financial expertise needed to undertake the analysis of providers' financial data, and will be bringing additional expertise into the Department to support this.

We are working closely with the Care Quality Commission to learn lessons from their similar market oversight scheme covering adult social care providers, including both the impact this has had on their market and the expertise needed to develop and operate effective schemes.

We will be able to share details on the launch date of the scheme in due course. As you will appreciate this is in part determined by the progress of the Bill through the House.

I also wanted to address your additional question, following the debate on Thursday, asking if the Department has commissioned or carried out the relevant analysis which would give the Government a full and accurate picture of profitability and ownership in this sector.

Regarding profitability, we believe that the CMA report (2022) and the Local Government Association report (undertaken by Revolution Consulting) (2023) provide strong and recent evidence for the need for these new powers.

The CMA estimated operating profit margins for large providers (between 2016 and 2020) were 22.6% for children's homes; 19.4% for Independent Fostering Agencies and 35.5% for Supported Accommodation. The LGA's 2023 report, which covered large providers who were collectively responsible for around a fifth of placements in children's homes and slightly over half of fostering placements, showed similar findings on profit making in the market. These two studies focused on larger providers, and their scope was limited due to issues with gaining access to, and drawing reliable conclusions from, data sets. Analysis by Teneo of the 2021/22 financial reports of children's home providers indicates that larger players tend to have greater EBITDA margins. Companies with annual revenues above £100m tend to have almost 10%-point greater average profit margins than smaller providers (c. 17% vs c. 7%). However, excessive profit making can occur no matter the size of the provider and it would be wrong, and unfair, to limit any future profit cap to providers of a particular size.

As I have already said, these reports provide strong and recent evidence in support of this legislation. One of the safeguards within the legislation is that regulations may only be made if the Secretary of State is satisfied it is necessary to do so, having regard to the public interest that these services represent value for money. We have been clear that this clause provides important backstop powers to ensure that government can take action, if needed, to end profiteering. We will only use these powers if necessary, if our other market intervention measures don’t have their intended effect. In order to make this value for money determination, the Secretary of State would of course take into account a range of information, including evidence as to whether our other interventions have been successful, and additional evidence about the state of the market at the time.

Please also be assured that a full consultation, including with local authorities and providers’ representatives, including on the appropriate level for any cap, would need to take place before this power was used.

Regarding ownership, the Financial Oversight Scheme will help build a picture of ownership as its aim is to increase the financial transparency of ‘difficult to replace’ placement providers. We will publish a list of the providers who are on the Scheme. This will increase transparency to the sector and support local authorities with their local sufficiency and contingency planning.

Thank you again for taking the time to engage on these matters. I hope these further details have been useful and I will place a copy in the House libraries.

Yours sincerely,

Jacqui Smith

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