The Treasury

Budget 2017 Information Release

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THE TREASURY
Kaitohutohu Kaupapa Rawa

Treasury Report: Information on Ministry of Health Budget Package

Date:	9 February 2017	**Report No:**	T2017/143
		File Number:	DH-1-2-3

Action Sought

	Action Sought	**Deadline**
Minister of Finance (Hon Steven Joyce)	Read prior to your meeting with Hon Coleman on 14 February.	Tuesday 14 February
Associate Minister of Finance (Hon Simon Bridges)	None. For information.	Not applicable
Minister Responsible for Social Investment (Hon Amy Adams)	Read prior to your meeting with Hon Coleman on 14 February.	Tuesday 14 February

Contact for Telephone Discussion (if required)

Name	**Position**		**Telephone**	**1st Contact**
[34]	Graduate Analyst, Health	[39]	N/A (mob)	✓
Ben McBride	Manager, Health	[39]	[23]	

Actions for the Minister's Office Staff (if required)

Return the signed report to Treasury.

Note any feedback on the quality of the report

Enclosure: Yes (attached).

Treasury Report: Information on Ministry of Health Budget Package

Executive Summary

This report provides background information about how the budget process for Vote Health has operated (and changed) over the last few years, and provides some high level comments on the Ministry of Health's bids for funding in Budget 17. Information about individual bids can be found in the appendix.

Between 2009 and 2014, Vote Health was managed largely outside the main budget process, with a specific funding allocation (plus retained underspends) controlled by the Minister of Health and no real prioritisation of health sector initiatives against bids from other agencies. Over the last couple of Budget rounds, we have worked to integrate Vote Health into standard budget processes, improve transparency, and strengthen Budget Ministers' decision rights.

The health sector has fixed nominal baselines and genuine cost pressures, so an annual funding increase is more or less inevitable. We have encouraged the Ministry to improve its understanding of sector performance and develop a more granular (bottom-up) understanding of cost drivers, but progress has been slow. The Ministry is seeking new funding for reform in a number of key areas, [33] and [33] We are supportive in principle. However, for [33] the Ministry really needs to do more work on its proposals before seeking funding. Work in the disability area is more advanced, although detailed design work (and a clearer story about baseline cost pressures) is needed.

Recommended Action

We recommend that you **consider** the following speaking points in your discussion with Minister Coleman:

- [40]

- [40]

- How are you managing expectations with DHBs with an unofficial funding signal? Why can't DHBs plan their budgets without a funding signal?

- What progress has been made on developing a social investment approach for the health sector? What does this mean for the separate roles of the Ministry and DHBs? And how will it support other parts of the social sector to improve intractable social problems?

- [40]

- [40]

- Is the Ministry of Health committed to leading a cross-agency process for improving mental health outcomes?

Ben McBride
Manager, Health

Steven Joyce
Minister of Finance

Treasury Report: Information on Ministry of Health Budget Package

Purpose of Report

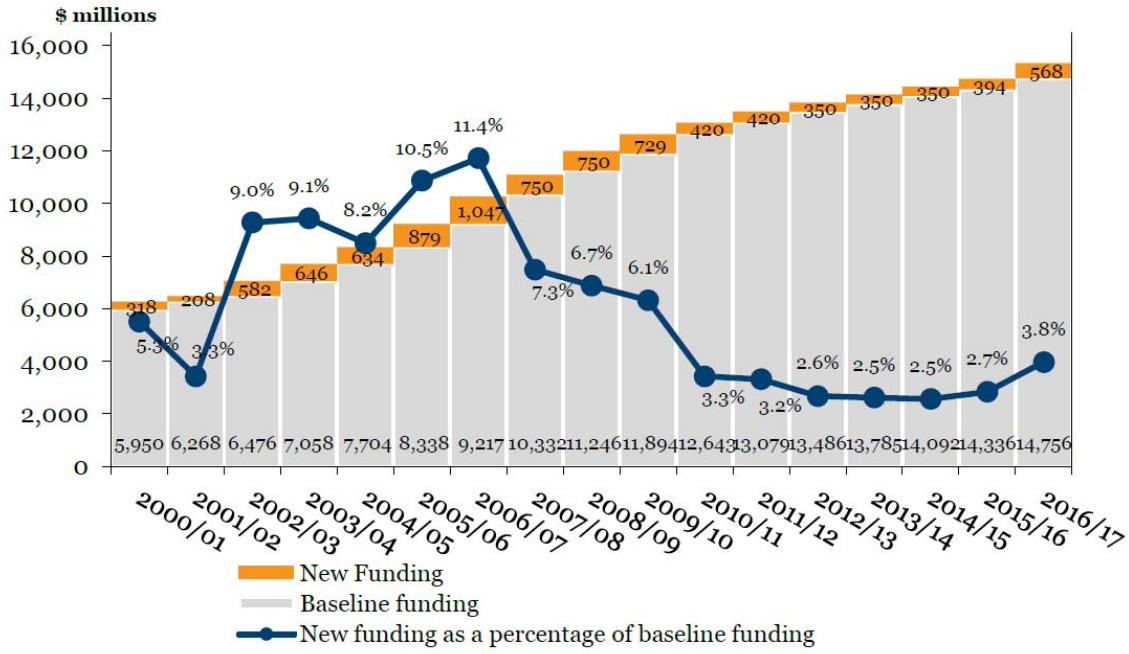
1. You are meeting with Minister Coleman on Tuesday. This report briefs you on the funding arrangements for Vote Health and discusses the Health Four-Year Plan and our views on the initiatives submitted for Budget 17. We will provide you with detailed information regarding the Budget initiatives before your bilateral meetings with Minister Coleman.

Background to Vote Health Funding

Health allocation: Budgets 2009 to 2014

2. Between 2009 and 2014, Vote Health received an annual funding allocation as part of the budget. This was split between a funding increase for District Health Boards (DHBs) and increases for other parts of the Vote. Table 1 provides a summary. (Note that DHBs account for around three-quarters of the Vote Health baseline, so typically receive the lion's share of new funding.)

Table 1: Vote Health funding 2000/01-2016/17



3. [34]

. In late November / early December, the then Minister of Health would bring a noting paper to Cabinet informing Ministers on the baseline increase for DHBs to help them prepare their annual plans. This was communicated as a funding signal, with the final amount confirmed once Cabinet approved the Budget.

4. The way this funding increase is shared between individual DHBs was determined by the Population Based Funding Formula (PBFF), a tool that allocates funding based on the weighted characteristics of the DHBs' populations. The funding signal would not generally be altered later on in the budget process. In other words, the funding signal stuck: the amount signalled to DHBs in November/December, was the same as the amount they received in the Budget.

5. The Minister of Health would then determine what initiatives would be funded with the remaining allocation (typically $100m) as part of the Budget Cabinet paper considered by Ministers in April. This process was outside the main budget arrangements, and therefore health initiatives were not compared with bids from other Ministers. The Minister of Health would separately bring a paper to Cabinet on additional initiatives to be funded from underspends retained within Vote Health, typically within the $50m - $100m range.

6. This arrangement was considered successful in helping the Government build public confidence in its management of the health system. However it existed in a period when other Ministers had to manage with baseline reductions or minimal increases, and where the majority of underspends were returned to the centre. And it also raised questions on the quality of the health initiatives funded, and how they compared to initiatives from other Ministers that missed out on funding.

7. [40]

Budgets 2015 to 2017: Bringing Health into the Budget process

8. Since Budget 2015, the previous Minister of Finance sought to integrate Vote Health into the main Budget process. This included ending the separate allocation, approval by Cabinet of the DHB funding signal, and consideration of health budget bids alongside bids from other social sector agencies. In meetings with the Minister of Health, the Minister of Finance pushed for a greater understanding of underlying cost drivers and a focus on what is being gained from the amount invested.

9. The Ministry of Health has found this process of integration challenging. [40]

Understanding cost pressures

10. The Ministry of Health has mostly used PBFF cost weights and top-down assumptions about wage and price inflation to estimate demographic and other cost pressures facing the health sector. This provides Ministers with contextual information on which to base their decisions, and is better than the earlier rule-of-thumb approach. But it does have drawbacks. First, it tells us relatively little about what is actually going on in the sector – how demographic and other pressures are manifesting themselves and what we should do to manage them. Second, the fact that we generally do not fully fund modelled cost pressures has been interpreted by critics as "underfunding" the

sector, even though public sector agencies generally are expected to manage cost pressures and deliver efficiencies.

11. A key objective for Budget 17 was therefore to move away from an exclusively top-down view of sector pressures, and develop a more granular understanding of cost drivers within the health system. As a starting point, we expected this would include more specific information about changes in (actual rather than modelled) price and volumes. However, progress in this area has been limited and a good understanding of bottom-up cost pressures is still missing. Our understanding is that an exercise aimed at developing a bottom-up understanding of cost pressures was started last year but subsequently abandoned. We think the Ministry will continue to struggle to develop a bottom-up perspective on the health system until it develops a clear outcomes and performance framework, and does a better job of organising and using the data it collects from the sector.

The DHB funding signal

12. Giving DHBs an early (pre-Christmas) funding signal has some advantages. It can help to manage expectations within the sector, and gives DHB management certainty about their short-term funding path. However, it does mean that Ministers are asked to pre-commit a large slice of the Budget operating allowance before bids from other agencies have even been submitted. This makes it difficult to assess competing priorities and consider trade-offs.

13. In practice, the usefulness of the early funding signal has been undermined in recent years because it has subsequently been adjusted. In both Budget 15 and Budget 16, the funding signal was revised upwards late in the budget process, essentially to achieve a particular headline allocation for Vote Health. In Budget 16, the Minister of Finance agreed with the Minister of Health not to seek Cabinet agreement to a formal funding signal before Christmas: DHBs were instead given an informal signal. This year, no funding signal has been given to DHBs, although they have been told to assume the same nominal funding increase as in Budget 16 for planning purposes. The Ministry of Health would now like to firm up this guidance: you should receive a separate note from them about this shortly.

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[40]

Budget 2017

Overall objectives

17. Over last couple of years, we have focused on trying to get better information about cost drivers, and encouraging the Ministry to think more strategically about risks and value for money. So the priorities have been:

    - a better understanding of cost pressures
    - stronger performance and accountability frameworks, supported by effective use of health data
    - rebalancing resources towards primary and community care
    - more effective working relationships between the health sector and other social sector agencies.

Vote Health budget bids

18. The Ministry of Health have requested over [in operational funding over four years, with bids in both Track 1 and Track 2. [33] in capital funding has also been requested.

19. The Ministry has submitted one Track 1 bid proposing to increase access to contraception for low income women. This bid stacks up well against social investment criteria and is well developed. It is supported by evidence. The Ministry of Social Development has been involved in the development of the implementation and evaluation plan.

20. Treasury comments (and preliminary funding recommendations) on individual bids within track 2 are provided in the appendix. The Track 2 bids are organised according to the five priority budget areas identified in the Four Year Plan. These are discussed below. In areas where the Ministry is seeking significant increases in funding, we think that Ministers need to challenge the Ministry on what level of change are they seeking.

[33]

[33]

Mental Health

26. The centrepiece of this package is the bid for a cross-sector mental health contingency fund (within Vote Health) that can be drawn down to commission mental health services. Again, we recognise the need for reform (and additional resources) in this area, and the need for a much broader cross-sector focus; but this is another example of the Ministry bidding for funding without being able to explain what it wants to do with it. There is no information about what the new commissioning model would look like, what the current capacity of the sector is, or how the Ministry would strike a balance between primary/community and specialist services.

27. We do not support a contingency fund within Vote Health. We think proposals for reform need to be worked up though a cross-agency process (involving Education, Social Development, ACC and the Justice sector). There are linkages with and between a number of Track 1 bids. Funding decisions is this area may be better left until Budget 18; or at least deferred and managed through a centrally held contingency fund (controlled by Finance Ministers). In the past, mental health services have tended to be a poor cousin of health/hospital expenditure, to the extent that funding has had to be ring-fenced to be protected. It is therefore not surprising that services are not currently well placed to respond to demands from other parts of the social sector.

[33]

Disability

29. Proposals for disability reform are better developed, based on the Enabling Good Lives principles and two demonstration projects, although detailed design work still needs to be done. The Ministry of Health has been signalling financial pressures in this area for a couple of years, but has yet to clearly to articulate the extent of these or how they have arisen [34] . We are not unsympathetic to the request for new funding, but we do think it is important to get a comprehensive sense of existing and short-term funding pressures at the same time as considering medium-term reform. There are also linkages with Terranova. We sent you a separate note on all of this at the end of last week.

Screening and Prevention

30. The Screening and Prevention package includes bowel and [33] . While there is clear intervention logic for these initiatives the Ministry has provided little information on implementation and the capacity of the sector to take on these new services (other than bowel screening). [34]

System Funding

31. This is basically an assortment of other bids for funding (DHB cost pressures, PHARMAC, [33] , electives, organ donation, workforce development, and the DHB capital investment pool). The largest item is DHB cost pressures. DHBs have fixed nominal baselines but growing populations, so annual funding increases are justified. However, as discussed above, we would like to see more detailed information from the Ministry to support the annual bid for funding. How much do they really know about actual (bottom-up) cost drivers in the system?

32. The DHB capital investment pool bid, seeking [33] billion over four years, does not require outyear funding at this time, leaving a [33] million bid in 2017/18. Discussions with the Ministry and DHBs are on-going, to test the likelihood of investment-ready business cases emerging in 2017/18. The Ministry also needs to clarify how much of the DHB capital pool allocation from Budget 14 remains unused. It is currently estimated at about $100 million, but we need a precise figure before agreeing to new funding.