



HEALTH REPORT

Subject: FUNDING ALLOCATIONS FOR OPERATIONAL AND CAPITAL EXPENDITURE IN BUDGET 2006

Date: 20 March 2006 **File Ref:** FN20-06-7-14

Attention: Hon Pete Hodgson

PURPOSE OF HEALTH REPORT

This report meets the report back requirement requested at the meeting of the Minister of Health with the Minister of Finance on the Budget 2006 Vote Health funding. The Ministry does not have an agreed position with Treasury over the extent to which Vote Health can pre commit funding from the 2007/08 and 2008/09, indicating the budget allocations. Treasury and the Ministry have both put forward suggestions which include access to some of the 2007/08 and 2008/09 funding.

This report sets two options for the allocation of the increase in Vote Health operating funding for 2006/07 based upon a number of options originally considered. One of the options is the Treasury preferred option, the other is the Ministry preferred option. The report considers the capital allocations and the associated impacts on the operational expenses. Further, the paper considers the need to access additional funding in 2007/08 and 2008/09 to ensure a fully funded budget allocation in out years whilst retaining a \$45 million risk reserve.

TIMING IMPLICATIONS

Priority:	Routine	Semi-Urgent (5 Days)	Urgent (3 Days)	24 Hour
		X		

EXECUTIVE SUMMARY

The options presented demonstrate that the operational funding in Vote Health can be managed within the allocation if a decision is taken to access an element of the indicative funding in 2007/08 and 2008/09 and

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However, the restraint required is not considered to be overly severe and options exist to allow

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The Ministry and Treasury have not reached agreement over the extent of access to pre commit the indicative funding in 2007/08 or 2008/09. The difference between the two options peaks at \$41.705 million in 2009/10, although the allocation of funds is significantly different. It is suggested that you agree to the Ministry of Health figure and as the individual items are approved via subsequent Health Reports, that the Treasury comments be addressed at that time. To the extent that you agree to scale back funding for the individual items, then the access to the indicative funding can be reduced.

A number of the initiatives are at an advanced stage of being developed and costings prepared. However, some require further work. It is the ones that have further work pending, that Treasury identify could be scaled back. To scale them back now could cause problems in 2006/07 depending on the final funding requirements for the initiatives.

It is further assumed that bids for further capital for Vote Health will be submitted for Budget 2007.

There are significant capital pressures throughout the Health Sector (DHBs, Ministry and Crown Entities). As in previous years, the Capital funding ambitions of the Sector outstrips the amount of funding available, even prior to the need to fund

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Reflecting these ongoing pressures, the Ministry and DHBs have developed processes for reviewing the strength of business cases. This paper outlines some of the options for managing the most immediate capital pressures that you might wish to pursue after receiving advice from the Ministry and DHBs through those processes. It demonstrates that work on

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projects should be progressed through development of business cases that fit the available Budget 2006 operating funds, which will be determined by this paper.

The option to transfer one off funding (operational) to the Capital envelope to advance Sector Capital projects is recommended. The extent of that transfer will be dependent on which Capital projects are approved.

In this report "Health Sector" refers to the Ministry, DHBs and other Crown Entities.

RECOMMENDATIONS

The recommendations are that you:

- (a) **Agree** with option 2 (the details of which are in Appendix '2') as the operational funding allocation; and Yes/No
- (b) **Agree** to seek the Minister of Finance's agreement to the following level of pre-commitments against the indicative Health operating allocations in Budget 2007, 2008 and 2009: Yes/No

\$ million	2005/06	2006/07	2007/08	2008/09	2009/10 & out-years
Pre-commitment	-	-	50.0	65.0	77.0

- (c) **Note** the Treasury preferred budget package option (Appendix 1) requiring the pre-commitment shown in the following table and the Treasury comments on the operational funding allocation; Yes/No

\$ million	2005/06	2006/07	2007/08	2008/09	2009/10 & out-years
Pre-commitment	-	-	23.774	31.635	35.295

- (d) **Note** that Treasury suggest that pre-commitments against future Budgets could be reduced to nil by further scaling of initiatives Yes/No

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- (e) **Note** that funding will have to be prioritised between pressures in the Health capital budget as capital pressures exceed funding available; Yes/No

- (f) **Agree** that the Yes/No

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projects are prioritised ahead of the rest of the capital pressures in the health sector, and that the NCC will be asked to provide objective advise on the strategic business cases for

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projects;

- (g) **Agree** that the National Capital Committee will be asked to provide objective advice on the strength of the business cases for other Health Sector capital pressures Yes/No

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- | | | |
|-----|---|--------|
| (h) | Agree that the National Capital Committee be asked to provide advice on relevant changes in service delivery in relation to capital investment, where this might assist you in managing capital pressures; | Yes/No |
| (i) | Note that officials have also identified a range of options for managing capital pressures, including the transfer of one off operating funding from the Health Services Funding NDE to the capital envelope | Yes/No |
| | [Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials], | |
| | and decisions on these options should be taken after receiving and considering NCC advice on business cases and an assessment of your priorities and risks for the portfolio; | |
| (j) | Note that the options available to manage capital pressures demonstrate that Ministers of Health and Finance will be able to take decisions to provide capital funding for | Yes/No |
| | [Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]; | |
| (k) | Agree that officials should prepare business cases for | Yes/No |
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| | projects that are consistent with the available operating funding agreed in recommendation (a) above, and the available capital funding; | |
| (l) | Agree that the Ministry will respond to the Treasury comments in this paper, in the subsequent individual health reports on initiatives as the approval to release funds is requested; | Yes/No |
| (m) | Agree that to the extent that any funds for initiatives in 2007/08 and 2008/09 as per recommendation (b), are not required, then the funds are not available for other initiatives; and | Yes/No |
| (n) | Note that Treasury will provide separate advice on the extent of pre-commitment to Vote Health Funding in 2007/08 and 2008/09 | Yes/No |

to the Minister of Finance;

- (o) **Sign** this paper and forward it to the Minister of Finance. Yes/No

Karen O Poutasi (Dr)
Director-General of Health

MINISTER'S SIGNATURE:

DATE:

REPORT

Background Information

This report focuses on two options based upon a range considered for the allocation of Operational funding and the consequences for capital investment from the Budget 2006 Bilateral.

The key constraints are:

1. New capital available of \$146 million
2. New operating funding available of \$750 million in Budget 2006 and indicative allocations of \$750 million in Budget 2007 and Budget 2008.

The approach adopted has been to:

1. Scale back capital funding requests to allow a greater allocation to be applied to

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2. Identify the impacts of the scaling back capital requests on the DHB Sector and how those impacts can be managed
3. Factor into the operating allocation the flow on impacts of

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4. Flat line (where possible) existing initiatives for operational funding and capture future increases against indicative \$750 million in each of 2007/08 and 2008/09
5. Set aside a risk reserve of \$45 million in each year (free and un-committed)
6. Explore the opportunity to re-phase/rescale the existing operational allocations
7. Identify a range of options for the Minister under the above parameters
8. Identify the impact of decisions against future indicative dollars available for operational allocations. To ascertain the extent of available funding to cover other pressures and the extent to which the Health Capital Budget could be increased by an operating to capital transfer.

Summary of Options					
No	Options	Risk Reserve & Unallocated	Capital	Maximum Pre-commitment of Operational Funding	Comments
1	Appendix 1 Treasury Option	Risk reserve \$45m pa, [Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials].	[Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials].	\$35.3m	Significantly scale back various initiatives. Reduces funding available for other capital projects and a pre-commitment of funds
2	Appendix 2 Ministry preferred option [Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]. extra savings of \$10m taken up	Risk reserve \$45m pa. [Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials].	[Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials].	\$77.0m	[Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]. and a pre-commit of funds and all planned 2006/07 initiatives go ahead
	Other options considered				
3	[Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials].	Risk reserve \$45m pa. [Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials].	[Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials].	\$42.9m	Greater uncertainty over longer term intentions to fund capital projects

		ministers and officials].			
4	[Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials].	Risk reserve \$45m pa. [Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials].	[Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials].	\$51.1m	[Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials].
5	[Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials].	Risk reserve \$45m pa. [Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials].	[Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials].	\$76.7m	[Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]. but not all potential operational funding savings are taken up
6	[Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials].	Risk reserve \$45m pa. [Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials].	[Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials].	\$129m	Not affordable from Capital funding unless a significant number of Sector projects are delayed/ stopped. Relatively significant pre-commitment of operational funding.

The above table summarises the options that were considered by officials. Option 1 (Treasury preferred) and option 2 (Ministry preferred) are the focus of the report.

Managing pressure on the Health Capital Budget

The following table outlines the funds in, and key pressures on, the health capital budget.

	\$m
Total funds available to Health Capital Budget, including \$146m in Budget 2006	\$836.377
Less, funding approved by Ministers that is likely to be required ¹	608.749
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- Capital and Coast building cost escalation	43.000
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Remaining Health Capital Budget	165.928
Pressures on remaining Health Capital Budget	
Projects from 2005 Capital allocation round	75.964
Ministry led sector information Projects [Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]	62.850
[Information deleted in order to enable the Crown to carry out commercial activities without disadvantage or prejudice]	16.000
[Information deleted in order to enable the Crown to carry out commercial activities without disadvantage or prejudice]	63.600
[Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]	53.800
Other – DHB projects yet to be considered by NCC	116.700
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Total known pressures on remaining Health Capital Budget	577.914
Short fall between known pressures and remaining Health Capital Budget	(411.986)

Refer appendix 3 for details.

The table above shows that there is likely to be \$165.928 million remaining in the Health Capital Budget that could be applied to new capital initiatives. There are \$577.914 million of known projects that will be “bidding” for these funds. In addition, there are a range of capital projects for which we do not have good information, but which may require funding – such as seismic upgrades in response to new building regulations. We are also aware of a large number of capital projects that have been flagged by DHBs through the recent asset management plans exercise as wanting funding in future years.

While the level of pressure compared to available funding appears significantly out of balance, it is normal and reflects the nature of the health sector.

¹ Includes \$27.440m for additional Pandemic Supplies that the Cabinet Policy Committee considered on 15th March 2006.

As the NCC consists of people from DHBs and is chaired by the Ministry of Health, it is effectively the Health Sector being asked to manage itself, which encourages buy-in to decisions. The NCC provides advice to the Ministry of Health, and Joint Ministers are asked to make final decisions on the allocation of Health Capital Budget after hearing NCC (advice on the quality of business cases), Ministry and Treasury advice. (Appendix 4 gives further back ground on the capital envelope in Vote Health).

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As per the Budget 2006 Health Bilateral paper, NCC will be asked to objectively consider all the capital projects in the health sector (as to the quality of the business case), that have not previously been approved by Joint Ministers, including

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(Strategic business plans only). As per the Bilateral paper, we recommend that you also ask NCC to provide any advice on changes to service delivery that might assist you in managing capital pressures.

In budget 2005 it was agreed by Ministers of Health and Finance to bring together all Health Sector Capital into one envelope. Prior to this, the Ministry managed a pool of funds for whole of Sector projects and the NCC gave advice only on DHB capital projects.

In addition to the advice that NCC provides, officials are aware of a range of options for you to manage the known capital pressures. Some examples of these options are outlined below.

The key message is that, if joint Ministers agree, there are sufficient options available to provide

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It is recommend that officials begin to develop business cases for these projects that reflect the available operating funding and the likely available capital funding.

Some of the options for managing Health Sector Capital pressures:

Saving (if applicable)

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[Information deleted in order to enable the Crown to carry out commercial activities without disadvantage or prejudice]

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Total \$310.6M

Other considerations in managing these pressures:

- In addition to these options, you may wish to transfer some one off operating funding from the Health Services Funding NDE to the Health Capital Envelope. Operating to capital swaps are discussed elsewhere in this paper. The transfer of such funds would allow some key projects to proceed. The Ministry estimates it would have up to

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available for transfer to capital.

- It will also be possible to seek further capital funding in Budget 2007, in order to further progress

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plus any other Health Sector projects.

- Entities in the Health Sector seeking funds from the Health Capital Envelope are required to maximise their own funding contributions to the project. Following business case reviews, it may be that some entities are able to meet a larger portion of the cost and reduce their request for capital.

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The Treasury is proposing an alternative budget package where operating funding sufficient to match a higher level of

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initiatives is allowed for. Effectively Treasury is suggesting an additional capital spend in the order of

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above the Ministry's suggested

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To achieve the Treasury option, significant limits would be placed on operational funding of 2006/07 initiatives (appendix 1).

Appendix 3 lists the individual capital projects to be considered for funding. To allow the following projects to go ahead, the Ministry would require

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to be transferred to capital from the Health Services Funding NDE and the use of remainder of the Capital Envelope (\$165.928 million Capital Envelope, giving a total

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This would leave no flexibility to carry out other capital projects, although further one off funding could be transferred from the Health Services Funding NDE if the Sector were able to fund any associated operating funding from within existing baselines.

\$

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Total **267.314M**

The use of one off funding to transfer to capital funding is subject to Cabinet approval.

Timing of Capital Allocation Process and Budget announcements

We respect that you will want to make announcements on new spending at the time of Budget 2006. The recommendation that you delay making decisions on the allocation of capital until after you have received NCC advice on business cases may restrict these announcements. However, we believe there will be announcements to be made around:

- the total capital funding being made available to the sector

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You should also note that:

- you will have the opportunity to announce significant capital spends later in the year once final decisions are made
- The Government has invested heavily in Health Sector capital in recent years and several new facilities will be opened during the next year.

Savings in Operating Funding

The initiative allocations, originally proposed in the January budget templates, have been reviewed in all cases by the relevant Deputy Director General.

The following savings have been identified:

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These savings have been reflected in Appendix 2.

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Additional Flexibility

Additional flexibility arises as a result of underspending in the current financial year on both NDE and DE. On reviewing past figures it is estimated that approximately \$40 million will be available to top up the funding in 2006/07 in the Health Services Funding NDE.

The above can be used for one off operating expenditure or for transfer to the Capital envelope for the Sector to use. If it is used by the Ministry of Health as oppose to the Sector for Capital funding then operational funding for on going operating expenditure will also be required.

None of the above has been factored into the options suggested or recommended.

What counts against the \$750 million Allocation and Capital

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It is usual policy to fund all associated flow-on costs for decisions made and announced by Government. Initiatives announced as part of Budget 2006 cannot commit further spending against future budgets (except where this is appropriated now or disclosed as a charge against future budgets). Some programmes may be amenable to phasing or piloting with further extensions under active consideration for future budgets. For example,

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Flatlining (where possible) the operating initiatives in appendix 2 enables these to be funded within the agreed allocation for Budget 2006 and the previously indicated level of pre-commitment against future Budget allocations. Any future operating funding for these initiatives can be treated as a risk and funded in future budgets, provided that these decisions are stand-alone from those made in Budget 2006.

In terms of future commitments and managing within the \$750 million indicative allocations, the most significant items to impact this are the FFT and demographic figures. Inflation and its impacts on the FFT are forecast to track lower over the next few years based on the Treasury's half yearly economic and fiscal update forecasts released in December 2005. This could potentially reduce demands on the \$750 million indicative funds by \$50 million ongoing in 2007/08 and a further \$80 million ongoing in 2008/09.

Why have a \$45 million risk reserve?

The \$45 million risk reserve appears as an ongoing reserve that it could be argued the Vote can not afford. However, there are likely to be decisions made where on going funding (not a rising profile) are required

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To that end, those decisions could not be made without funds existing in out years to cover these decisions.

The use of the indicative allocation rather than actual appropriated dollars would restrict future decisions and announcements to annual allocations only.

Requesting \$100 million in 2007/08 and \$200 million in 2008/09 as appropriations and a charge against the indicative allocation for those years

Appendix 2 shows the impact of savings and the shortfall to be covered if part of the suggested indicative \$100 million and \$200 million are to be accessed. \$76.7 million would be the actual needed as a pre-commitment. Accessing funding for operational expenditure was discussed at the Bilateral. This allows all the original initiatives to proceed,

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The call on the indicative allocation for 2007/08 and 2008/09 is not excessive and significantly lower than originally suggested.

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Budget 2006 Operational Initiatives

Commentary on the above initiatives has been included in Health Reports 200616 (2006 Budget Initiatives – Vote Health and the Joint Treasury/Health Report – 2006 Vote Health Budget Package – Bilateral Briefing). Treasury has commented below on each initiative, however, the Ministry has not responded to each item. The Ministry has provided advice on the initiatives and flexibility of them to allow for re-phrasing in earlier reports and briefings. The Ministry will respond to the Treasury comments in its subsequent individual Health Reports as the approval to release funds is requested.

In its Budget 2006 initiatives template the Ministry has requested \$7 million in 2005/06 to cover the Residential Care Loans write off. Without such an appropriation the Ministry would have to absorb the write off from its appropriations and so reduce the funding available for Health Services Funding NDE carry forwards or potential transfers to the Capital funding envelope.

The above item was not discussed at the Budget Bilateral, although it was in the Bilateral paper. No specific recommendations referred to it. To absorb the write off would reduce underspends available from

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The Ministry has issues with the principle that is applied here, in that write off of Crown debt is not leading to health gains and is an additional cost applied to the Vote above the original requirements.

Treasury comments

Treasury analysis shows that a credible Vote: Health package is possible without pre-committing more than \$35.3 million per annum in 2009/10. This package allows:

- Lower pre-commitments against future indicative Vote: Health operating allocations
 - More flexibility in future years

Room for greater investment in [Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]

- → Ensuring sufficient funding to achieve goals

- A focus on better value for money
 - Which leads to a smaller number of initiatives, done well
 - Informed by Government priorities represented in the Speech from the Throne and agreements with support parties

- Full-funding of initiatives
 - Minimising unexpected constraints on future allocations

Treasury recommend the following package

	Balanced Package Amount				
	2005/06	2006/07	2007/08	2008/09	2009/10 & out-years
\$ millions					
Balance of Health Funding Package surplus/(deficit)	74.365	10.293	(48.431)	(33.311)	(33.311)
New funding for Budget 2006	-	261.000	261.000	261.000	261.000
PHAS funding	49.361	34.480	34.480	34.480	34.480
<i>less</i> \$45 million risk	-	(45.000)	(45.000)	(45.000)	(45.000)
Funding available for new initiatives in Budget 2006	123.726	260.773	202.049	217.169	217.169
<i>less</i> Commitments & Service Delivery Risks	(7.000)	(121.474)	(132.218)	(132.218)	(132.218)
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<i>less</i> Scaleable and Phaseable – Treasury Supported	-	(36.426)	(38.893)	(38.782)	(31.900)
Remaining Allocation / (pre-commitment) Treasury package	116.726	79.871	(23.774)	(31.635)	(35.295)

Treasury notes that pre-commitments against future indicative Vote: Health operating allocations could be further reduced to nil,

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a) Commitments and service delivery risks

These are high priority initiatives that represent either existing commitments or areas where there is a genuine risk of service failure. Treasury supports fully funding these initiatives.

Initiatives in this category are:

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- Development of Trans-Tasman Therapeutic Regulator – Medsafe delay ongoing operating

[Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]

- Environmental Science and Research (ESR) laboratory and surveillance capability

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- Forecast Funding Track (FFT) and demographics (including savings)

b)

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c) Scaleable and phaseable – value for money

These are initiatives that in Treasury's view represent good value for money and should be funded, but which could be scaled back or phased.

Initiatives in this category included in the Treasury package at full cost are:

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- Meningococcal transition 2006/07 to 2008/09

Initiatives in this category included in the Treasury package at a scaled back cost are:

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- Funding for the parts of Healthy Eating Healthy Action (HEHA) implementation that represent good value for money

This option reduces pre-commitments in out-years

One purpose of this paper is to inform the decision on an appropriate level of pre-commitments. Too high a pre-commitment will significantly reduce your ability to manage Health pressures within the indicative \$750 million per annum allocations for Budget 2007 and Budget 2008.

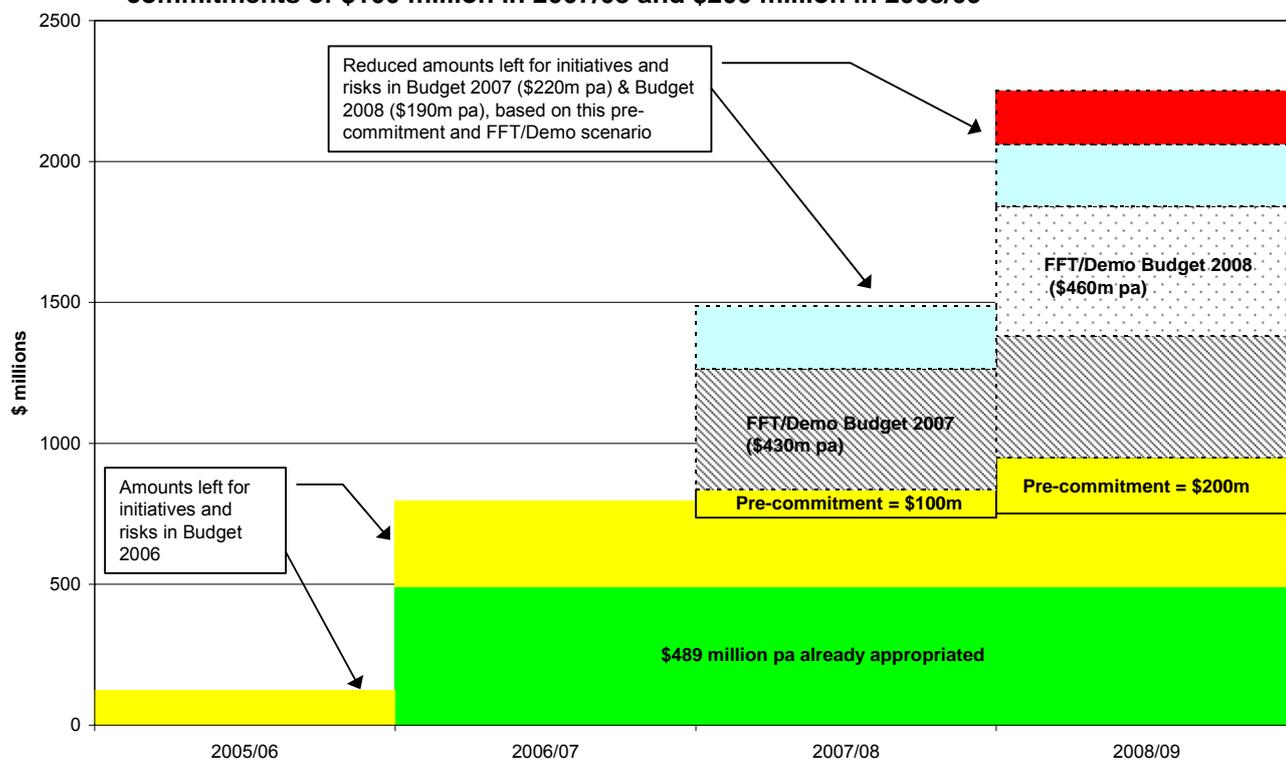
Treasury recommends keeping pre-commitments against Budget 2007 to no more than \$35.295 million per annum in 2009/10. Pre-commitments reduce flexibility, as illustrated by previous Health Funding Package commitments which have created a major difficulty in producing a balanced package for Budget 2006.

Vote: Health faces a number of risks during the 2006/07 fiscal year that may not be able to be managed out of the Vote: Health risk contingency. Over-spends on the contingency may result in further commitments against future budgets.

When considering the level of pre-commitments, forecast funding for FFT and demographics needs to be taken into account. The fiscal context is tightening and

there are *significant* Vote: Health pressures that are not addressed in Budget 2006. If inflation (say) were to continue at the level used for the 2006/07 FFT/demo calculation, automatic adjusters could account for \$430 million and \$460 million of Budgets 2007 and 2008 respectively².

Figure 1: Budget 2006 operating allocations for Vote: Health – showing the impact of pre-commitments of \$100 million in 2007/08 and \$200 million in 2008/09



There is also a risk that new initiatives in Budget 2006 that are not fully funded will reduce future spending options. Initiatives advanced in Budget 2006 should be complete in the sense that their benefits should not be contingent on funding extensions in future budgets. For this reason, Treasury's proposed package suggests scaling those initiatives for which this can be done without reliance on later funding. This principle applies to both capital and operating expenditure.

The Budget Strategy Cabinet paper has indicated that the Government's capital budget is expected to significantly tighten in Budgets 2007 and 2008. The total allowance for Budget 2007 is currently set at around \$500 million over 2007/11. This compares with \$2.1 billion agreed for Budget 2006. This has particular relevance to

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Providing better value for money

² These amounts include a 0.5% discount similar to that offered by the Minister of Health as part of FFT/demo calculations for Budget 2006; Treasury does not know whether the Minister intends to continue with these discounts i.e. FFT/demo could be even higher.

Initiatives with merit that would benefit from further work, and are amenable to phasing and scaling:

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Healthy Eating Healthy Action

The underlying objectives addressed by most of the proposals within this initiative are strategically important to achieving the Government's health goals. However, some proposals have no plan for how they will spend funding, some probably represent low-value for money because they duplicate services (e.g. breastfeeding initiatives), and some have no clear rationale (e.g. a tripartite agreement coordinator). The initiative also calls for an additional 11 Ministry of Health policy analysts, which Treasury considers could be met from existing Ministry resources.

Treasury's proposed package scales back this initiative to exclude funding for under-developed or low value-for-money components.

Initiatives recommended for deferral or not supported:

[Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]

Breast screening age extension

Cabinet has directed that costs for this initiative be met from within baselines. CAB Min (04) 6/6 and SDC Min (04) 2/2 'noted that the costs will be met within existing Vote Health funding baselines.'

Treasury does not support funding this initiative in Budget 2006.

Commentary on capital processes

There is a difference of view between Treasury and the Ministry of Health on the appropriate role of the National Capital Committee. The Ministry of Health view is that the National Capital Committee should not be asked to provide the Minister of Health with a prioritised ranking of all capital projects.

The Treasury acknowledges that we are asking the NCC to undertake a difficult task. However, the NCC is the group that is best placed to advise Ministers, and the better the understanding that the NCC has of the tightness of the capital budget facing the Minister of Health, the better they will be able to communicate this to their colleagues in DHBs.

Ministers still retain decision making rights. The NCC formally provides its advice to the Ministry of Health, and is highly dependent on Ministry advice in making its own decisions. But the Treasury and the Ministry have the opportunity to comment on NCC advice when it is provided to Ministers.

The National Capital Committee's Terms of reference include to:

- provide strategic policy advice regarding capital investment and timely recommendations to the Ministry on capital projects that require ministerial approval.
- develop and keep current a Capital Investment Framework for managing the capital budget envelope
- consider wider matters and advise on the incentives, policies and structures that affect the Government's capital ownership objectives.

NCC has ranked projects by priority in the past. At the NCC's December 2005 meeting, the value of the business cases bidding for funds was greater than the actual amounts available in the Health Capital Budget. The NCC were presented with a ranking of the business cases. The committee noted this ranking and undertook a discussion of it. As the total value of the business cases (of a standard able to be recommended to Ministers for funding) was less than the budget constraint, the ranking did not have to be formally agreed and advised to Ministers.

This is consistent with recommendation (u) from the Budget 2006 Health bilateral draft minutes which states:

“agreed that in order to ensure that Vote Health capital pressures can be defensibly and appropriately changed to accommodate the constraints on capital funding, that the National Capital Committee (NCC) be requested to give objective advice on overall Health capital priorities (including revisiting the 2005 allocation round) at the April 2006 NCC meeting;”

Treasury recommends that NCC be asked to provide you, through the Ministry, with an objective prioritised ranking of all Health Sector capital pressures, and where relevant, advice on changes in service delivery that to assist you in managing the capital pressures. All capital pressures

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should be put on the table for this process in order to demonstrate to ensure its integrity, and gain buy-in from the wider sector.

It is standing process for all capital spending from the Health Capital Budget to undergo the NCC prioritisation process (as laid out in the National Capital Investment Guidelines published by the Ministry of Health), except in cases of urgency (e.g. pandemic preparedness). We suggest that you discuss any change in this policy with the Minister of Finance.

Contact for telephone discussion (if required)

Name	Position	Telephone Direct Line After Hours	Suggested First Contact
Paul Helm	Chief Financial Officer	[Information deleted to protect the privacy of natural persons, including deceased people]	1
[Information deleted to protect the privacy of natural persons, including deceased people]			2
Debbie Chin	Deputy Director General Corporate & Information Directorate		3

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Appendix 3 - Health Capital Budget - Pressures

	TOTAL	Comments / Notes / Mitigation strategies
Required reserved funding [Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]	[Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]	[Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]
Capital and Coast DHB escalation	(43.000)	This will be required in order for the project to be completed. Cabinet has agreed that Ministers can approve up to \$43M for Capital and Coast DHB escalation.
Ministerial priority DHB projects [Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]	[Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]	
Total	(6.200)	
TOTAL	(61.700)	
PROPOSALS WITH - BUSINESS CASES COMPLETED AND FUNDING RECOMMENDED BY THE NCC AND MINISTERIAL PRIORITY PROJECTS		
2005 capital allocation round - NCC		

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Total

(5.564)

2005 allocation round projects that are recommended for reconsideration

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[Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]

Total NCC	(70.400)		
TOTAL NCC AND MINISTERIAL PROJECTS	(75.964)		
MINISTRY LED SECTOR INFORMATION PROJECTS			
[Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]	[Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]		
TOTAL MINISTRY LED SECTOR INFORMATION PROJECTS	(62.850)		
DHB and NZBS PROJECTS - 2006 Allocation Round Projects that cannot all be postponed without considerable difficulty or operating cost impact			Amounts are what DHBs indicate is required from Health Capital Budget
[Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]	[Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]		[Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]
[Information deleted in order to enable the Crown to carry out commercial activities without disadvantage or prejudice]	[Information deleted in order to enable the Crown to carry out commercial activities]		[Information deleted in order to enable the Crown to carry out commercial activities without disadvantage or prejudice]

	without disadvantage or prejudice]	
[Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]	[Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]	[Information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]
Subtotal	(53.800)	
Total	(133.400)	
Pending 2006 allocation round projects that could be delayed		
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Total	(116.700)	
Uncertain future capital requirement		
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Appendix 4 Health Capital Envelope Background Information

During the last eight years investment in hospital infrastructure has been at the highest level for a generation. This investment has not been matched by capital investment in other areas of health. It is likely that business cases for IT projects in the Health sector will demonstrate considerable benefits and strong value for money. However, in order to progress IT business cases, in the tight fiscal environment it is likely that a lower level of Government funding for DHB capital projects than in recent years will result. The diverting of capital from DHB projects towards sector wide Ministry led projects must be done in a sustainable way that enables essential DHB work to proceed and reasonable capital 'shocks' to be managed. The contribution of operating carrying forward transfer to capital, will assist with Sector Capital projects. If this is achieved Health will be able to deliver on its obligation to manage within its available capital funding. This appendix proposes how this can be achieved.

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Opportunity to encourage improved implementation of SPNIA

A key objective of the new Service Planning and New Health Intervention Assessment; framework for collaborative decision-making (SPNIA) is that health service planning for major capital developments be improved. SPNIA is in its implementation phase, a pause in new major capital projects will allow SPNIA to become fully operational and mean that the next phase of major capital investment is able to be better informed as regards ideal service configuration.

Engagement and support from DHBs

Engagement and support from DHBs for the change of direction will significantly reduce risk and assist the Minister of Health to achieve his objectives. The Minister's requirement to change the emphasis in capital expenditure and the strong constraint on capital from the Crown has been raised with DHBs, both across the sector and in detail with the DHBs most affected. The response of DHBs has been mature, constructive and understanding.

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DHBs also expend over \$200 million per annum for depreciation that is applied to capital investment as the expense is a non-cash item. They can therefore still continue with much significant and urgent capital investment.

Ministers should therefore note that notwithstanding that the strategic change of direction required is substantial and swift, that it is a change that the Ministry and, in particular DHBs, can deliver with the assistance of the NCC. The speed and degree of the change that is defensible will be clearer following the April 2006 NCC meeting. As discussed below involving the NCC need not cause any delay, but should give Ministers greater confidence in Health capital processes.

Improve capital decision making processes

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The normal deadline for business cases being put to NCC, is 31 August each year with final funding decisions following review of business cases in September and October. The NCC advises the Ministry on business case quality and prioritisation of projects that require funding from the health capital budget.

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