

4 December 2009

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To: Minister of Finance

AIDE MEMOIRE: VOTE HEALTH DETAILED EXAMINATION OF BASELINES AND BUDGET 2010 - TREASURY COMMENT

You are meeting with Budget Ministers on Monday 7 December to decide on final Budget 2010 operating allocations to take to Cabinet on 14 December.

Treasury's report for Budget Ministers recommends that

1. the indicative Health allocation of \$300 million be confirmed;
2. the full \$300 million be allocated for DHB funding increases to be signalled before Christmas;
3. a savings target of \$100 million to \$150 million be set for Health's baseline alignment exercise;
4. a \$50 million provision for DHB deficit risks should be the first call for any savings and/or for any increase in the Health allocation;
5. savings above \$50 million be available to fund new policy initiatives and price/volume increases for high-priority Ministry-managed health programmes.

This note gives more information to support those recommendations and to inform any discussion you may have with the Minister of Health:

- our assessment of the Health baseline examination report submitted by the Minister of Health on 30 November; and
- additional information on funding pressures and risks for Health in Budget 2010, and on savings options.

The Ministry of Health's Baseline Examination Report Focuses on Living within \$300m

The Ministry of Health's baseline examination report focuses on managing health pressures and initiatives without exceeding Health's \$300 million indicative operating allocation. It provides options to achieve this through a mix of savings (including policy choices for Cabinet), DHB efficiency gains, and a much more targeted and prioritised approach to funding price/volume pressures for Ministry managed programmes.

The Minister of Health's covering letter does not request an increase in the \$300 million indicative allocation, but it notes that he wishes to discuss the issues raised in the Ministry's report with the Minister of Finance.

DHB Funding Signal – 14 December Cabinet Decision Required

The Minister intends to announce District Health Boards' likely funding for 2010/11 before Christmas. This will inform the preparation of DHBs' District Annual Plans, financial forecasts and capital business plans. The Minister intends to seek Cabinet's agreement to a DHB funding signal on 14 December.

If this DHB funding signal is to be announced before Christmas, it is important to confirm both the size of the Health allocation for Budget 2010, and a clear target for baseline savings that can be used to manage: DHB deficit risks; funding for price and volume pressures in other high priority health programmes; and new initiatives.

The Ministry of Health's Report on Detailed Examination of Vote Health Baselines

The Ministry of Health's submission meets the requirements of the terms of reference agreed by Cabinet. Given the size of Vote Health, the information and analysis provided on a tight timeframe is thorough, and builds on previous Ministry work over the last year.

While the Ministry presents 3 scenarios for managing with a \$300 million allocation, each one comes down to essentially the same choices. Each requires the same level of savings, scaling back of new funding, or increased efficiencies.

The Ministry of Health's report describes options that the Ministry considers will allow:

\$290 million	to increase funding for District Health Boards	delivered as: <ul style="list-style-type: none"> - a full 1.885% demographic adjuster of \$183 million; and - 1.1% or \$107 million to help meet price pressures (full "FFT" price adjustment for DHBs would be 2.27% costing \$220 million)
\$50 million	for a scaled new initiatives package	to deliver Government priorities including med school places, medicines, electives
\$62 million	increases in "highest priority" Ministry-managed programmes	The Ministry has detailed specific price and volume pressures for each non-departmental expense (NDE) programme where it judges funding increases are required to: <ul style="list-style-type: none"> - maintain service coverage (eg: wage pressures in residential care services); - meet contract commitments [<i>deleted – negotiate without prejudice</i>] - meet policy targets (eg: growth toward the 5% population coverage target for "Care Plus" primary care funding).

Managing this package within the indicative allocation of \$300 million would require:

[deleted – negotiate without prejudice] of efficiencies in DHBs	otherwise the \$290 million funding increase will be insufficient to keep DHB deficits inside the forecast track already provisioned within baselines. Increased DHB deficits will then flow back to hit the Government's 2010 operating allowance
\$102 million in ongoing savings within baselines	to fund new initiatives and funding increases for Ministry managed programmes

Key Risks to Managing Within the Health Allocation

Whatever final allocation is agreed, the key risks to Health's ability to manage to the agreed figure and avoid additional costs being charged against the 2010 operating allowance are:

- industrial relations risks – [*information deleted in order to enable the Crown to negotiate without disadvantage or prejudice*];
- implementation risks to DHB efficiencies – DHBs will need flexibility to deliver the estimated [*deleted – negotiate without prejudice*] in efficiency gains. Policy directions that constrain this flexibility or require savings to be reinvested in specific activities will also increase DHB deficits.

Treasury considers the Ministry of Health's assessment of [deleted – negotiate without prejudice] in realisable DHB efficiencies to be at the upper limit of what is achievable and realisable in Budget 2010. We consider a DHB funding increase of \$300 million to be the minimum prudent level. Even if the full \$300 million indicative allocation is committed to the DHB funding increases the Minister of Health wishes to signal before Christmas, we recommend that further provision should be made (whether funded from savings or from changes to the Health allocation) for industrial relations risks and risks to DHBs deficits.

- We will advise further on budgeting options for this risk provision (eg: as a tagged central contingency or as an increase in the appropriated DHB deficit track).

Ministry of Health Budget 2010 Scenarios

(scenarios differ only in the sequence and source of funding for each component)

Funding for	\$m	Funded from	\$m
DHB Resourcing	290	Health Allocation	300
- Amount required for deficits to remain within forecast track, [deleted – negotiate without prejudice] is realised in operating efficiencies.			
New Initiatives	50	Savings	102
- Scaled package for policy priorities		- Reprioritisation, scaling new initiatives and funding increases, or further DHB efficiencies	
Ministry NDE programmes	62		
- Targeted volume/price increases for priority programmes managed by Ministry of Health			
Total	402		402

Treasury Option

Funding for	\$m	Funded from	\$m
DHB Resourcing	300	Indicative Health Allocation	300
Provision for risk to DHB deficits	50	First call on savings (or any Health allocation increase)	50
- if efficiencies realised are below [deleted – negotiate without prejudice] and/or IR costs exceed plan			
New Initiatives and Ministry NDE programmes (balancing items)	50-100	Further savings	50-100
Total	400-450		400-450

Savings Options

The Ministry has identified savings options well in excess of the \$102 million required to fund its budget scenarios. This gives Ministers a range of options for reprioritisation.

The Ministry's report doesn't present these options in a way that allows choices to be easily quantified and seen as a menu to achieve any given savings target:

- Some options avoid cost increases, but don't deliver savings against current baselines (e.g.: no price increase to primary health capitation subsidies);
- Some options save DHBs money but don't free up funding in baselines. Some may be double counted in expected DHB efficiencies [deleted – confidentiality of advice].
- Some options are costed as "all or nothing" savings [deleted – confidentiality of advice], while others are costed as incremental options [deleted – confidentiality of advice]
- At this stage, Ministers don't need to make specific savings decisions. But a savings target for Health to work to would help to crystallise the choices needed to fund priority risks and pressures in 2010. The Minister and Ministry of Health can then work on more detailed

savings options and policy recommendations for Cabinet as they complete the Health baseline alignment exercise due to Budget Ministers in March.

This table summarises the savings options identified. Ballpark ranges in each area are sketchy at this stage. The key point is *these options will exceed the amount required to fund the proposed health package*. They provide considerable choice for Ministers.

Potential Health Savings Options

Area	Ballpark Range	Details – options include:
Primary Care	<i>[deleted – confidentiality of advice]</i>	<i>[deleted – confidentiality of advice]</i> Change PHO Management Fees (up to \$33m)
<i>[deleted – confidentiality of advice]</i>	<i>[deleted – confidentiality of advice]</i>	<i>[deleted – confidentiality of advice]</i>
<i>[deleted – confidentiality of advice]</i>	<i>[deleted – confidentiality of advice]</i>	<i>[deleted – confidentiality of advice]</i>
<i>[deleted – confidentiality of advice]</i>	<i>[deleted – confidentiality of advice]</i>	<i>[deleted – confidentiality of advice]</i>
<i>[deleted – confidentiality of advice]</i>	<i>[deleted – confidentiality of advice]</i>	<i>[deleted – confidentiality of advice]</i>
MoH Mental Health Programmes	\$4m-\$7m	Ministry In-Depth Review identified \$4m of “low-risk” and \$3m of “medium risk” options
<i>[deleted – confidentiality of advice]</i>	<i>[deleted – confidentiality of advice]</i>	<i>[deleted – confidentiality of advice]</i>
MoH Public Health	\$14m-\$40m	Ministry In-Depth Review identified \$14m of “low-risk” and \$11m of “medium risk” options. Other public health options identified are up to \$15m.
<i>[deleted – confidentiality of advice]</i>	<i>[deleted – confidentiality of advice]</i>	<i>[deleted – confidentiality of advice]</i>

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