

Treasury Report: Vote Health Budget Meeting 22 March 2010

Date:	19 March 2010	Report No:	T2010/440
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Action Sought

	Action Sought	Deadline
Minister of Finance (Hon Bill English)	Read this briefing prior to your meeting with the Minister of Health 8.00am Monday 22 March 2010	Monday 22 March 2010
Associate Minister of Finance (Hon Simon Power)	Read this briefing	Monday 22 March 2010
Associate Minister of Finance (Hon Steven Joyce)	Read this briefing	Monday 22 March 2010

Contact for Telephone Discussion (if required)

Name	Position	Telephone		1st Contact
[withheld - privacy]	Senior Analyst, Health	[withheld - privacy]	[withheld - privacy]	✓
Claire Douglas	Manager, Health	[withheld - privacy]	[withheld - privacy]	

Minister of Finance's Office Actions (if required)

If the Minister of Finance agrees, forward a copy of this report to the Minister of Health.

Enclosure: No

Treasury Report: Vote Health Budget Meeting 22 March 2010

Draft Agenda

You are meeting the Minister of Health at 8.00am on Monday 22 March 2010 to discuss Budget 2010 for Vote Health. The following agenda items are proposed:

1) Operating - Baseline Alignment Proposal and Finalising Budget Allocations:

- a) Confirm the profile of new funding already agreed
(The Health BAP assumes an additional \$12.4 million is available in outyears).
- b) Ensuring DHB deficits and other risks are managed within Vote Health
 - i) The Health BAP proposes no increase in DHB deficit provisioning or risk reserves, but signals that risks are unlikely to be managed within current risk reserves
 - ii) Discuss any further increase in the Health allocation and its application
(Treasury recommends any increase be applied to risk reserves)
 - iii) Discuss further options for savings and reprioritisation during 2010/11 to manage risks and pressures in Vote: Health
(Treasury recommends a target for additional savings options to match any increase in the Health allocation).

2) Capital:

- a) Note the available funding in the current Health Capital Envelope.
- b) Confirm a nil additional capital allocation.

Recommended Action

The Treasury recommends that Budget Ministers:

Operating

- a **note** that the Vote Health Baseline Alignment Proposal (BAP) balances over the forecast period, but does not balance in outyears as it assumes an *ongoing* increase of \$12.400 million per year from a *time-limited* increase in the Health allocation earlier agreed by the Minister of Finance;
- b **confirm** that the additional operational funding agreed to date for Health in Budget 2010 is \$400 million ongoing, plus \$91.362 million spread over the next four years only;
- c **note** that notwithstanding ongoing efforts to constrain costs and strengthen financial disciplines on DHBs, there remains a significant risk that DHB deficits and other cost pressures cannot be managed within Vote Health's baselines and budget allocation;
- d **note** that the Health BAP proposes savings averaging \$33.962 million per year in Ministry managed spending for reprioritisation to higher priorities in Budget 2010 (0.2% of total Health baselines, and 1.3% of Ministry-managed spending);
- e **note** that Budget Ministers have agreed to consider allocating some additional funding for Vote Health in Budget 2010, [*deleted – free and frank*];
- f **agree** to increase the Budget 2010 Health allocation by \$10 million per year, with the following impact on the Health package as submitted in the BAP:

\$ million	2010/11	2011/12	2012/13	2013/14	Outyears	4-Year Total
Budget Allocation agreed by Cabinet	400.000	400.000	400.000	400.000	400.000	1,600.000
08/09 Under-spends (phasing to 2013/14 as in Health BAP)	34.900	22.528	17.104	16.830	-	91.362
Additional funding [<i>deleted – free and frank</i>]	10.000	10.000	10.000	10.000	10.000	40.000
Total funding increase for Health	444.900	432.528	427.104	426.830	410.000	1,731.362
Plus Savings identified in BAP	31.907	33.575	34.646	35.720	33.059	135.848
Total funding for Budget 2010	476.807	466.103	461.750	462.550	443.059	1,867.210
Less Total BAP spending proposals	466.807	456.103	451.750	452.550	445.459	1,827.210
Less BAP shortfall	-	-	-	-	12.400	
Additional balance available	10.000	10.000	10.000	10.000	(2.400)	40.000

- g **agree** that this additional funding be added to the Health Services Funding Risk Reserve, with expenditure against the risk reserve subject to the existing requirements for joint Ministerial approval;

Agree/disagree.

- h **invite** the Minister of Health to explore further savings and reprioritisation options at least matching any increase in the Health budget allocation, to manage risks and funding pressures with the agreed funding for Vote Health over the course of 2010/11 without recourse to further funding from the centre;

Agree/disagree.

Capital

i **note** that \$211.172 million is available for new capital projects within the existing Health Capital Envelope, including \$6.672 million the Minister of Health proposes to transfer from his available operating allocation;

j **agree** that no additional capital allocation be made for Vote Health in Budget 2010;

Agree/disagree.

k **note** that ongoing work to establish the National Capital Investment Committee and a new capital process for Health will enable better planning and prioritisation of capital investment in the Health sector in future years;

l **note** that Treasury will work with Ministry of Health officials to ensure any changes required to the Health budget package are reflected in final financial recommendations for Cabinet;

m **agree** to refer a copy of this briefing to the Minister of Health.

Agree/disagree.

Claire Douglas
Manager, Health
for Secretary to the Treasury

Hon Bill English
Minister of Finance

The Vote Health Baseline Alignment Proposal

Confirming Funding Already Available – Balancing Outyears

1. Cabinet has agreed a Budget 2010 allocation of \$400 million per year for Health.
2. The Minister of Finance has since agreed to support additional one-off funding of \$91.362 million to be spread over four years (equal to Health's 2008/09 non-departmental underspend).
3. The Minister of Health has proposed ongoing savings and reprioritisation in the BAP averaging \$33.962 million per year over the forecast period.

Table 1: Summary of Vote Health Baseline Alignment Submission

\$million	2010/11	2011/12	2012/13	2013/14	Highest outyear
Funding					
Budget 2010 Allocation	400.000	400.000	400.000	400.000	400.000
08/09 Underspends	34.900	22.528	17.104	16.830	-
Savings and reprioritisation (0.2% of current baselines)	31.907	33.575	34.646	35.720	33.059
TOTAL	466.807	456.103	451.750	452.550	433.059
Expenditure Proposals					
DHB funding increases (3.6% increase as earlier agreed)	350.000	350.000	350.000	350.000	350.000
Ministry-managed programmes (2.2% increase overall - targeted to priority programmes)	59.340	59.340	59.340	59.340	59.340
Government commitments	16.789	24.235	25.306	26.380	23.719
Initiatives from 08/09 underspend	34.900	22.528	17.104	16.830	12.400
Increase to risk reserve	1.787	-	-	-	-
Transfer to fund Bowel Cancer outyear	3.991	-	-	-	-
TOTAL	466.807	456.103	451.750	452.550	445.459
BALANCE	-	-	-	-	(12.400)
% New Funding	93.16%	92.64%	92.33%	92.11%	89.80%
% Re-prioritisation	6.84%	7.36%	7.67%	7.89%	7.42%
% Unfunded	-	-	-	-	2.78%

4. The Vote Health BAP balances across the forecast period, but spending proposals exceed the allocation by \$12.4 million per year in outyears. This is because it assumes ongoing funding in outyears for (largely discretionary) initiatives that the Minister of Health proposes to fund over the next four years from time-limited funding: electives (\$10 million per year); breast reconstruction (\$2 million per year); and cochlear implants (\$0.4 million per year).
5. As a first step in Monday's discussion, we recommend that Ministers confirm the current budget parameters to ensure any changes are made from a clearly agreed starting point: a budget allocation of \$400 million per year ongoing, plus time limited funding of \$91.362 million spread over the next four years.
6. Without further changes in funding, Health will therefore need to scale back initiatives of find additional savings of \$12.4 million per year from 2014/15 onward.

Ensuring DHB Deficits and Other Risks are Managed within Vote Health

7. As the Health BAP makes clear, volatility in DHBs' operating deficits is the largest fiscal risk in the vote. DHBs will need to achieve significant efficiency gains and savings relative to past performance to reduce their aggregate deficits as required to stay within the declining track of budgeted deficit support, while also managing wage pressures (from progression under existing collective agreements and any increases in collective agreements renegotiated this year). The BAP proposes no increase in the current provisioning for deficit support.

Table 2: DHB Deficits – Forecast and Provisioning

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

8. *[information deleted in order to maintain the effective conduct of public affairs through the free and frank expression of opinions]*

9. Current Health baselines also include a general risk reserve in the Health Services Funding appropriation. Use of this funding requires joint agreement of the Minister of Finance and the Minister of Health for which the Ministry of Health must demonstrate that it is a prudent use of the risk reserve given the known risks to be managed. No significant change to current risk reserve levels is proposed in the BAP.

Table 3: Health Services Funding Risk Reserve

[deleted – negotiate without prejudice]

10. *[information deleted in order to maintain the effective conduct of public affairs through the free and frank expression of opinions]*

11. The Health BAP signals the risk that the Minister of Health could seek more funding from the between-budget general contingency over the course of the year should these risks eventuate:

48. *In previous years the Health risk reserve has been set at a level sufficient to provision for known fiscal risks during the Budget process and the expectation on Health was that it would manage within its available funding. However the Budget 2010 allocation has not provided sufficient funding to increase the risk reserve above its present level given the funding required for DHBs and the Ministry to maintain the coverage and quality of their frontline care and support services.*

49. *Currently there is unallocated funding of [deleted – negotiate without prejudice] remaining in the risk reserve. While history has shown that not all fiscal risks materialise in a given year, based on the risks outlined in the table above, it is estimated that a risk reserve of between [deleted – negotiate without prejudice] would enable Health to manage within its available funding without recourse to the between Budget contingency.”*

Options for Additional Funding for Vote Health in Budget 2010

12. Budget Ministers have indicated they wish to consider an increase in the Health allocation for Budget 2010, in light of forecast savings in Vote: ACC and recognising some downstream pressures on Vote Health from current changes in the management of ACC programmes and entitlements.
13. In considering additional funding for Health in Budget 2010, Ministers should note that there is little rationale for relating any aggregate level of new funding in Budget 2010 to the hypothetical amount the system would receive under a formulaic “inflation plus demographics” (FFT/Demo) increase of 4.155%:
 - DHBs have already been told their funding increase will be \$350 million or 3.6%;
 - Across-the-board increases for Ministry managed programmes were ended in Budget 2009, and the Health BAP proposes to sustain current services with a 2.2% overall increase. Increasing Ministry managed programmes by full FFT/Demo while holding DHBs to a lower track would be difficult to justify;
 - Using a full “FFT/Demo” adjustment as the baseline for comparison assumes no scope for efficiencies, contradicting the government’s general approach to state sector management the expectations already signalled to the Health sector;
 - Such funding adjusters relate to current funding streams and the presumed cost of sustaining current services, but any additional funding provided to Health is likely to be committed to new activity.
14. The Treasury recommends that any further increase in Health’s 2010 budget allocation should be applied to increase the Health Services Funding risk reserve. This will assist the Minister of Health to manage the risks and pressures outlined above without recourse to the general contingency, and will ensure that any further spending proposals are subject to a risk analysis and joint Ministers’ agreement.

Proposed Savings and Reprioritisation

15. The Health BAP proposes savings and reprioritisation within baselines averaging \$33.962 million over the next four years. This is a relatively modest level of savings compared to the overall Vote (0.2%) and compared to the more “discretionary” non-DHB components. Only one option requiring a Cabinet policy decision is proposed (a paper will be submitted soon proposing \$2.19 million in savings from primary care funding streams).
16. A broader range of savings options were identified for consideration during last year’s line-by-line review, in-depth reviews of specific programme baselines, and the detailed examination of the Vote reported last November.
17. The Health BAP does not identify any further savings options that may be considered if necessary to manage the risks and pressures on the Vote over the course of the year, given the stated inadequacy of current risk reserves.
18. *[information deleted in order to maintain the effective conduct of public affairs through the free and frank expression of opinions]*

Proposed Allocation of Remaining 2009/10 Risk Reserve

19. A set of proposals for spending the balance of the 2009/10 risk reserve was included in the Health BAP. These proposals total \$31 million. Decisions on these proposals can be made by the Ministers of Health and Finance under existing cabinet delegations and do not require to be included in the Budget package. The Treasury has requested further information from the Ministry of Health on the outstanding risks to be managed, and will prepare a separate paper for joint Ministers decisions on these proposals.

Capital funding for Vote Health

20. There is **\$204.5 million** in the existing Health capital envelope (of which \$39.9 million will be required for Auckland and Waitemata elective theatres). The BAP proposes to increase the capital envelope by a further \$6.672 million¹. With this change, there is \$171 million available in baselines for capital projects approved in 2010.

Baseline Funding	\$m
Capital Envelope (unallocated to specific projects)	\$204.500
Added from 2008/09 Underspends	<u>\$6.672</u>
	\$211.172
Less projects likely to be/already agreed by Ministers	
Auckland & Waitemata Elective Theatres Proposals	<u>\$39.900</u>
Remaining Baseline Funding	<u>\$171.272</u>

21. *[information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials].*
22. Treasury has recommended that Budget Ministers agree a zero allocation of additional capital for Health in Budget 2010. This is based on the competing capital priorities across government, and an assessment that the existing Health capital envelope of \$171.272 million should be more than sufficient for 2010, given:
- Central funding for Health capital averaged about \$140 million over the last decade;
 - In only three of the last ten years have capital approvals exceeded the amount already available;
 - The Ministry of Health's criteria (low risk/high certainty, few service planning issues, immediate safety, government priorities) and
 - Recognising the embryonic state of the new capital process.
23. Once the new capital process is in place and functioning effectively, higher health capital spends may be appropriate in Budget 2011 and 2012. Considerable further work is also required to develop advice for Ministers on the desirability and feasibility of long term funding signals and/or long term capital budget tracks. This will include more work on how a fully sustainable funding track could be defined.

¹ This is from the \$91.362 million of operating funding over four years the Minister of Finance has agreed to support in light of Health's 2008/09 underspends.