The Treasury

Budget 2018 Information Release

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THE TREASURY
Kaitohutohu Kaupapa Rawa

Treasury Report: Further Advice on the PHARMAC Reprioritisation Bid

Date:	19 March 2018	**Report No:**	T2018/635
		File Number:	DH-1-2-3-2-4-2018

Action Sought

	Action Sought	Deadline
Minister of Finance (Hon Grant Robertson)	**Agree** recommendations for implementing the 2017/18 PHARMAC savings proposal	23 March 2018
Associate Minister of Finance (Hon Dr David Clark)	**Agree** recommendations for implementing the 2017/18 PHARMAC savings proposal	23 March 2018

Contact for Telephone Discussion (if required)

Name	Position	Telephone		1st Contact
Hew Norris	Senior Analyst, Health	[39]	N/A (mob)	✓
Carolyn Palmer	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: No

Treasury Report: Further Advice on the PHARMAC Reprioritisation Bid

Executive Summary

In response to Ministers' request at the 13 March bilateral, this report provides more information on the PHARMAC 2017/18 reprioritisation proposal, including related operating costs, and seeks agreement to implement the proposal.

[34]

We have therefore considered three options for implementing this proposal.

	Option	Pros and cons
1	Leave it up to DHBs to decide how the savings are used.	Does not generate savings for the centre and it is unclear how much the savings would be used to strengthen DHBs' relatively weak financial positions (and offset future deficit support needs) or to meet other operating costs in the last month of the year.
2	Same as option 2 plus DHB's 2017/18 deficit support payments are reduced by their level of PHARMAC savings. The reduction in deficit support paid can be carried forward to 2018/19 for reprioritisation in Budget 18.	This would allow funds to be returned to the centre for reprioritisation without any change to DHB appropriations. However, the funds would only be a small fraction of the $22 million savings, around $4-$5 million (the DHBs expected to receive deficit support make up about 20% of the PHARMAC savings). [34]
3	Ministers ask DHBs to use the savings to reduce deficits and meet other expected cost pressures, [38] (**Treasury recommended option**).	While this option does not return savings to the centre, it increases the likelihood that the savings strengthen DHBs' balance sheets, reducing funding requests for deficit support. It also helps DHBs to manage higher than expected cost pressures, [38] which might otherwise result in additional funding requests. Unlike the deficit support option above, there is a much closer alignment between the per DHB PHARMAC savings [38] reducing the risk of concerns being raised by DHBs around uneven treatment.

This report also provides advice in respect of PHARMAC's request for $1.5 million per annum additional operating funding to implement the proposal and whether these costs can be funded from within its baseline or sourced from the 2017/18 Combined Pharmaceutical Budget (CPB) savings for DHBs.

Using CPB funds for PHARMAC operating expenses is not permitted under current practice. The CPB (i.e. pharmaceutical funding for New Zealanders from DHBs' appropriations) is deliberately separate from PHARMAC's operating funding (which is paid from an appropriation managed by the Ministry of Health).

PHARMAC has advised that there is some risk that it may not be able to fully achieve the proposed savings if it does not receive the additional operating funding and it may reduce its resilience as an organisation and reduce or delay its activities in other areas such as achieving its goals to increase health equity.

[34]

The Ministry of Health has already provided advice to the Minister of Health on steps for implementing the early savings proposal. A key step in implementing the proposal is for the Minister of Health to agree for PHARMAC's CPB to be increased from 2018/19 reflecting the inclusion of more hospital medicines.

Recommended Action

We recommend that you:

a **agree** to implement the 2017/18 PHARMAC savings proposal by:

i. Leaving it up to DHBs to decide how the savings are used:

Agree/disagree Minister of Finance	*Agree/disagree* Associate Minister of Finance

ii. Leaving it up to DHBs to decide how the savings are used and reducing DHB deficit support payments to return a small amount of the funds to the centre for reprioritisation:

Agree/disagree Minister of Finance	*Agree/disagree* Associate Minister of Finance

iii. Ministers asking DHBs to use the savings to reduce deficits and meet other expected cost pressures, such as [38]
(Treasury recommended option):

Agree/disagree Minister of Finance	*Agree/disagree* Associate Minister of Finance

b [34]

c **agree** to consider increased operating funding for PHARMAC as part of [33] and [40]

Agree/disagree *Agree/disagree*
Minister of Finance Associate Minister of Finance

d **note** that progressing PHARMAC's proposal also requires the Minister of Health agreeing to a Ministry of Health recommendation to increase PHARMAC's Combined Pharmaceutical Budget from 2018/19.

Carolyn Palmer
Manager, Health

Hon Grant Robertson
Minister of Finance

Hon Dr David Clark
Associate Minister of Finance

Treasury Report: Further Advice on the PHARMAC Reprioritisation Bid

Purpose of Report

1. In response to a request from the 13 March Budget bilateral, this report provides further information on PHARMAC's reprioritisation proposal. In particular:

   a Options to use the $22 million additional savings that PHARMAC has identified it can provide for DHBs in 2017/18.

   b The level of operating cost increase required by PHARMAC to implement the proposal.

2. It also highlights one further action required by the Minister of Health for the proposal to go ahead, being agreement to increase PHARMAC's Combined Pharmaceutical Budget (CPB)[1] from 2018/19.

PHARMAC Reprioritisation Bid

3. As we have previously advised [T2018/355], the PHARMAC bid involves:

   a Adding the remainder of hospital medicines to the CPB.

   b Providing savings estimated at $195 million over 4 years (2018/19 to 2021/22) to Vote Health through reduced medicines expenditure in comparison to the current funding trajectory. These savings would be reduced by any increase in operating funding provided to PHARMAC for its increased role to deliver the savings (it is seeking $1.5 million per year).

4. Since submitting its proposal, PHARMAC has identified it can provide additional savings of approximately $22 million in 2017/18 by starting the proposal two months early (in May 2018).

5. The key risk around this proposal is the likelihood of public concerns around a perceived reduction in Government medicine funding and how it may affect access to new products.

Options for Implementing the $22 Million Early Savings Proposal

6. [34]

[1] The CPB is an agreed expenditure level managed by PHARMAC on behalf of DHBs. Hospital cancer medicines are already included along with products including community dispensed medicines, vaccines, and haemophilia treatments.

7. [34]

These options incorporate information from our past report and further information we have become aware of since it was provided to Ministers, including increased DHB funding needs relating to the [38]

8. Under all the options discussed in Table 1, it would be up to PHARMAC and DHBs to organise how the 2017/18 savings would be gained (this is different to the savings from 2018/19 on which would be incorporated in the Budget process through changes to appropriations). We understand from the Ministry of Health that the most likely approach would be for DHBs to invoice the PHARMAC for their hospital medicines spend for May and June this year. The decision for this to occur could be made by the PHARMAC and DHB Boards (without requiring Ministers' approval).

Table 1. Options for using the $22 million PHARMAC savings in 2017/18

	Option	Pros and cons
1	Leave it up to DHBs to decide how the savings are used.	Does not generate savings for the centre and it is unclear how much the savings would be used to strengthen DHBs' relatively weak financial positions (and offset future deficit support needs) or to meet other operating costs in the last month of the year.
2	Same as option 2 plus DHB's 2017/18 deficit support payments are reduced by their level of PHARMAC savings. The reduction in deficit support paid can be carried forward to 2018/19 for reprioritisation in Budget 18.	This would allow funds to be returned to the centre for reprioritisation without any change to DHB appropriations. However, the funds would only be a small fraction of the $22 million savings, around $4-$5 million (the DHBs expected to receive deficit support make up about 20% of the PHARMAC savings). [33]
3	Ministers ask DHBs to use the savings to reduce deficits and meet other expected cost pressures, [38] (**Treasury recommended option**).	While this option does not return savings to the centre, it increases the likelihood that the savings strengthen DHBs' balance sheets, reducing funding requests for deficit support. It also helps DHBs to manage higher than expected cost pressures, [38] which might otherwise result in additional funding requests. Unlike the deficit support option above, there is a much closer alignment between the per DHB PHARMAC savings and [38] reducing the risk of concerns being raised by DHBs around uneven treatment.

9. We recommend option 3 as it helps to partly meet DHBs' additional funding need to support [38] and provides greater certainty around the use of the PHARMAC 2017/18 savings.

10. The use of the PHARMAC 2017/18 savings to offset the [38] could be advised to DHBs' through their letter of expectations, along with their wider funding

package. As the letter of expectations is a public document, this approach would help ensure transparency around the use of the savings.

11. Consistent with our recommended option, we understand that the Ministry of Health is considering submitting a late Budget 18 bid [38] which would be reduced in recognition of the PHARMAC savings in that year.[2]

Actions Required to Implement this Proposal

12. The Ministry has provided separate advice to the Minister of Health[3] on related actions required for PHARMAC's proposal to be implemented. A key Ministry recommendation, which we support, is for the Minister of Health approve the CPB at a higher level of $985 million from 2018/19 to reflect its wider scope (i.e. the inclusion of the additional hospital medicines).

PHARMAC Operating Expenditure

13. PHARMAC's request for $1.5 million per annum additional operating funding, as outlined in is reprioritisation proposal, is not currently included in the draft Budget package[4] and Ministers have requested further information around this element of the proposal:

    a Can the proposal be funded within PHARMAC's operating baseline (i.e. without additional funding)?

    b Could additional operating funding for PHARMAC be sourced from the 2017/18 CPB savings for DHBs?

14. The additional operating costs are mostly related to increased staffing to implement the proposal and realise savings. PHARMAC has advised that there is some risk that it may not be able to fully achieve the proposed savings if it does not receive the additional operating funding to deliver its extended responsibilities.

15. PHARMAC has also advised that using CPB funds for its operating expenses is not permitted under current practice. The CPB (i.e. pharmaceutical funding for New Zealanders from DHBs' appropriations) is deliberately separate from PHARMAC's operating funding (which is paid from an appropriation managed by the Ministry of Health).

16. [34]

[2] We understand from the Ministry that the PHARMAC savings only provide a partial offset for the [38] as they have a different distribution across DHBs.
[3] 'Utilisation of Combined Pharmaceuticals Savings in 2017/18' dated 7 March 2018
[4] This funding is covered by the following Budget 18 bid: 'Implementing Savings in the PHARMAC Combined Pharmaceutical Budget'

[34]

17. [34]

18. [34]

[33]

[34]