Whittington Health NHS

## Trust Board Meeting

**ITEM: 17**
**DOC: 14**

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| **DATE:** | 28th March 2012 |

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| **TITLE:** | 2012/13 Draft Budget Proposal |

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| **SPONSOR:** Richard Martin, Finance Director | **REPORT FROM:** Jim Davies, Deputy Director of Finance |

**PURPOSE OF REPORT:**

- To provide an update in respect of the 2012/13 budget position for the consideration and approval of the Board.
- To update the Board on the latest Operating Plan submitted to NHS London on the 5th March 2012.

**EXECUTIVE SUMMARY:**

**1. Overview of 2011/12 Position**

1.1. The forecast position for 2011/12 is for the Trust to deliver a surplus of £500k on an IFRS basis (which equates to a surplus of £1,156 excluding IFRS). This has been achieved through robust control of budgets, restraint in the approval of new cost pressures, close scrutiny in the appointment to vacancies and achievement of CIP targets.

**2. Proposal for 2012/13 Budget**

2.1. The key assumptions which underpin the 2011/12 budget position are consistent with Monitor guidance, and the requirements of NHS London. The budget proposal is also consistent with the Trust long term financial model (LTFM) and operating plan submitted to London on the 5th March (attached). The proposal is for an overall planned income position of £277,071k, of which £225,750k is included in respect of North Central London (NCL).

2.2. The overall budget allows for a surplus of £3,120k in an IFRS basis, which is broadly in line with NHS London's expectation of a 1% planned surplus. The equivalent surplus position after excluding the impact of IFRS and for the purpose of the break even target is £3,747k.

2.3. Total CIP within the proposed budget is set at £13,120k, for which schemes have been identified. Schemes and targets have been identified to deliver the £13,120k m target. The majority of the savings will be reflected in base budgets and finance managers are working with budget holders to identify the correct budget location for these. A proportion of the programme relates to trust-wide savings targets, and these will be distributed between budgets and communicated to budget holders as part of the budget sign-off process.

2.4. The agreement of pass through costs in respect of estates and IT is an ongoing piece of due diligence. It has been proposed by the Trust that the agreed outcome represents an adjustment to the 2012/13 SLA once known.

## 3. Key Risks to the Budget Position

3.1. North Central London (NCL) is one of the most financially challenged sectors in the country. Service Level Agreements to date have identified a gap of circa £13.75m between the NCL contract offer and the Trust requirement. While this has not been factored into the budget proposal, this is by far the most significant risk to be flagged within this budget proposal.

3.2. The 2011/12 forecast position used as the basis for developing the budget provides a realistic and reasonable position based on knowledge of activity levels and trends, it should be noted however that activity and income levels have been lower than would have traditionally been expected. Continuation of this trend would present a risk to income levels necessary to cover expenditure budgets.

3.3. Failure to deliver quality and innovation improvements necessary to secure additional CQUIN payments included as part of the overall plan.

3.4. Additional challenges highlighted as part of the detailed assessment of budgets and identification of CIP schemes, including higher than expected;

- Marginal costs / failure to extract marginal costs in line with reductions to activity;
- Incremental Costs;
- Above inflation cost increases e.g. fuel;
- Other unanticipated cost increases;
- A failure to deliver CIP as planned. A failure to deliver the vacancy factor (£1,308k); and
- A failure to identify mitigating actions (£300k) identified relating to new 2012/13 cost pressures

**PROPOSED ACTION:**

**The Trust Board is asked to:**

- **Note:** the forecast position for 2011/12 and the planned achievement of a forecast surplus position of £500k on an IFRS basis (which equates to a surplus of £1,156k excluding IFRS).
- **Agree:** the proposal for the 2012/13 budget position; whilst acknowledging that there are still a number of key risks which have yet to be fully resolved at this stage.
- **Note:** the most significant risk to the budget proposed position is the agreement of the income position.

**APPENDICES:**

Draft Operating Plan submitted to NHS London on 5th March 2012.

**DECLARATION**

In completing this report, I confirm that the implications associated with the proposed action shown above have been considered – any exceptions are reported in the Supporting Information:

Implications for the NHS Constitution, CQC registration
Financial, regulatory and legal implications of proposed action
Risk management, Annual Plan/IBP
Moving Ahead – how does this report support any of the Trust's 5 Strategic Goals

## 4. Overview of 2011/12 Position

The Trust started 2011/12 with the key objectives of delivering a position of £500k on an IFRS basis (equating to a surplus of £1,156k excluding IFRS) and delivering a cost improvement target of some £19.6m.

An overview of the Trusts financial performance shows a surplus position of £561k (on an IFRS basis) at Month 11, with forecast surplus for the year in line with the planned (£500k). This position has been achieved through:

- Robust budgetary control and restraint in the approval of new cost pressures;
- Significant progress in delivering the CIP target of £19.6m, of which £19.1m has been delivered, with balance of just £0.5m as yet unidentified;
- The establishment of the Vacancy Scrutiny Panel, which has controlled recruitment to vacancies, and has contributed to under spends against pay budgets in year – which have more than compensated for the shortfall on the CIP achievement.

## 5. Health Economy Context

North Central London (NCL) is one of the most financially challenged sectors in the country. For 2012/13 NCL have indicated a forecast deficit in the region of £100m based on a continuation of unmitigated growth. As a consequence, SLA discussions to date have been extremely challenging. Given that discussions have yet to be concluded, the initial budget has been set at a level which is consistent with the LTFM and latest *Operating Plan* submission (attached).

## 6. Contract Negotiations

Negotiations for the 2012/13 contract have taken place through the traditional contract negotiation process, together with high level chief executive to chief executive discussions. This has been necessary in order to; a) manage the complexity of bringing together an acute contract largely based on PbR, with a predominantly block based community contract; and b) ensure effective risk management for both the Trust and commissioner as part of the ongoing development of the integrated care organisation (ICO).

The current position in terms of contract negotiations with NCL commissioners is that the latest contract offer which the Trust has received is £212.02m which is circa £11.66m below the outturn position included within the offer. This offer as it currently stands would not be financial viable for the Trust. The Trust have however indicated a willingness to work with the commissioners, and have made an initial proposal which effectively accepts the offer of £212.02m as a baseline position, supported by £12.95m of transitional funding, thus taking the Trust proposal for 2012/13 to £225.75m.

The rationale for the Trust offer is to provide financial stability for the next year, and more specific support for additional capital charges linked to the new Electronic Patient Record (EPR) system, the proposed joint acute ward and in establishing appropriate provisions for the restructuring costs necessary for the development of the ICO. The benefit to the commissioner being that the proposed SLA would enable the Trust to develop, transform and support future commissioner QIPP schemes.

Alongside this proposal, traditional negotiations are ongoing, although progress has to date been slow. With effect from Thursday 15th March, formal mediation applies, with any issues unresolved as at the 30th March subject to a formal arbitration process.

## 7. Process of Developing Budgets

In the absence of agreed SLA values, the budget is developed on the basis of on the proposal made by the Trust to NCL of £225.75m. It has been assumed that other contracts will be adjusted for standard tariff deflation and reductions to the MFF as appropriate; together with modest assumptions of growth and QIPP expectations. Clearly the agreement of contracts with a less favourable outcome will present a significant risk to the budget outlined.

The development of the 2012/13 budget has been based on the outputs of the first draft of the long term financial model (LTFM) completed as part of the Foundation Trust application. The budget is therefore consistent with the integrated business plan, and with also with the operating plan submitted to NHS London on the 5th March.

As part of the development of the LTFM and the budget a number of meetings were held with the senior divisional teams in order to agree a number of key assumptions such as; activity projections, cost pressures, the recurrent nature of under / over spends in 2011/12 and CIP.

It was recognised at an early stage due to the constraints of the financial position that any cost pressures / service developments would effectively result in additional CIP requirements. The process has therefore sought to minimise additional expenditure requirements, and it has been agreed by the executive team that cost pressures will be managed through a combination of improved budgetary control, together with limited funding of prioritised pressures. As part of this process Divisions will seek to prioritise pressures, and also improve budgetary control by bringing over spending areas back into line with budget.

## 8. 2011/12 Outturn Position

The figure below provides an overview of the forecast outturn position for 2011/12, showing a total forecast income position of £275,916k, expenditure of £275,416k and a planned surplus of £500k. The figure also highlights the underlying recurrent position as being a £1,574k deficit, with a £2,074k non recurrent surplus making up the overall planned £500k surplus.

**Figure 1: 2011/12 Outturn Position**

| | | Recurrent (£000's) | Non-Recurrent (£000's) | Total (£000's) |
|---|---|---|---|---|
| **2011/12 Forecast Income** | Recurrent income | 275,252 | - | 275,252 |
| | Provision release | - | 820 | 820 |
| | Provision increase | - | (956) | (956) |
| | Non Recurrent Income | - | 800 | 800 |
| | **Total Income** | **275,252** | **664** | **275,916** |
| **2011/12 Forecast Expenditure** | Recurrent expenditure | (294,118) | - | (294,118) |
| | provision release | - | 1,932 | 1,932 |
| | provision increase | - | (2,030) | (2,030) |
| | Non Recurrent Expenditure | - | (800) | (800) |
| | CIP | 17,292 | 2,308 | 19,600 |
| | **Total Expenditure** | **(276,826)** | **1,410** | **(275,416)** |
| **2011/12 Forecast Net surplus/(deficit)** | | **(1,574)** | **2,074** | **500** |

While this forecast position provided a realistic and reasonable position based on activity levels and trends, it should be noted that activity and income levels during 2011/12 (as at the Month 10 position) have been lower than would have traditionally been expected, and as a result the trust has under performed against contracts. If this is a continuing trend this represents a risk to the organisation of lower levels of income to support infrastructure and other operating costs. While this position will continue to be monitored, it needs to be flagged as a risk.

As outlined above, the key risks in respect of the acute contract to this positions are outlined as follows:

- NCL Commissioner intentions, and specifically the risk that contract values are subject to significant further reductions.
- Fluctuations in the levels of activity and associated income

## 9. 2012/13 Draft Budget Position

The starting position for the 2012/13 draft budget position is the 2011/12 forecast outturn position, which is adjusted for non recurrent items, and 2012/13 adjustments. The composition of the 2012/12 budget is summarised as follows:
The recurrent position is illustrated as follows:

**Figure 2: 2012/13 Draft Budget Proposal**

| | Income £000 | Expenditure £000 | Surplus/ (Deficit) £000 |
|---|---|---|---|
| **2011/12 Forecast Outturn** | **275,916** | **275,416** | **500** |
| Non Recurrent | (664) | | |
| Market Forces Factor (MFF) | (2,200) | | |
| Haringey Children's Service FYE | 1,543 | | |
| Inflation | (4,144) | | |
| CQUIN | 1,570 | | |
| Net Commissioner Adjustment | 7,100 | | |
| Income Phasing | (2,300) | | |
| Other | 250 | | |
| Non Recurrent | | (898) | |
| Planned Provision Increase | | 3,000 | |
| Marginal Costs | | (483) | |
| Incremental Costs | | 1,499 | |
| Non Recurrent CIP in 2011/12 | | 2,308 | |
| Vacancy Factor | | (1,308) | |
| *Subtotal* | | *1,000* | |
| Agreed Cost Pressures | | 2,023 | |
| Additional 2012/13 Cost Pressures | | 1,700 | |
| 2011/12 Reserves Made Recurrent | | (400) | |
| Mitigating Actions | | (300) | |
| *Subtotal* | | *1,000* | |
| Inflation | | 2,125 | |
| Contingency | | 1,300 | |
| Haringey Childrens Service FYE | | 1,000 | |
| Increased Capital Charges | | 600 | |
| Other | | (511) | |
| CIP | | (13,120)* | |
| **2012/13 Budget** | **277,071** | **273,951** | **3,120*** |

* While the Trust have plans to deliver £13,120k CIP, within the Operating Plan there is a presentational requirement to show "new" CIP only **and not** the full year effect of 2011/12 schemes. Within the operating plan the CIP is presented as £11,630k "new" CIP, with the remaining being shown as "old year" CIP carried forward in the underlying position.

** The draft budget proposal of £3,120k is on an IFRS basis, the equivalent value excluding IFRS is £3,747k.

The key assumptions behind the each of the proposed budget adjustments are outlined as follows;

**Income Assumptions**

- *Non Recurrent Income*: The figure of £664k relates to the net non recurrent income included in the 2011/12 forecast outturn (figure 1), but which is not applicable for the 2012/13 budget position.
- *MFF*: The figure of £2,200k represents the expected reduction to MFF income as part of the national rebasing exercise. Further guidance has been received which indicates a higher figure, there is therefore a risk that MFF income may reduce further.
- *Haringey Children's Service FYE:* The figure of £1,543k represents the full year income position for Haringey Children's service, this adjustment to the SLA and budget is necessary as income in 2011/12 does not reflect the full year position ( services transferred to the Whittington in May 2011).
- *Inflation:* The figure of £4,144k relates to the standard tariff deflator, which is applicable to NHS Payment by Results (PbR) and non PbR services.
- *CQUIN:* The figure of £1,570k relates to additional CQUIN income anticipated, in line with the operating framework which set out a 1% increase in amounts payable under CQUIN.
- *Net Commissioner Adjustment:* The figure of £7,100k reflects net additional funding requested from NCL as part of the contract negotiations. The purpose of this adjustment is to support;
    - Additional capital charges associated with the new EPR system and joint ward. The capital charge element relates to two years worth of funding, and hence there is also an income phasing adjustment of £2,300k which effectively transfers this value to 2013/14.
    - Support the establishment of provisions to resource anticipated restructuring costs.
- *Income Phasing*: As highlighted above, transitional support requested for capital charges relates to more than one year, and this effectively a phasing adjustment between 2012/13 and 2013/14.
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**Expenditure Assumptions**

- *Non Recurrent Expenditure:* The figure of £898k relates to the net non recurrent expenditure included in the 2011/12 forecast outturn (figure 1), but which is not applicable for the 2012/13 budget position. This excludes non recurrent CIP, which is included separately as part of the 2012/13 target of £13,120k.
- Planned Provision Increase: As highlighted above the figure of £3,000k is included to support the establishment of provisions to resource anticipated restructuring costs.
- Marginal Costs: The figure of £483k reflects a reduction to marginal costs which is largely based on projected reductions associated with metrics and KPI's included within the activity plan. The reduction is based on the assumption that a reduction to activity in this way will facilitate the extraction of variable costs e.g. drugs and clinical consumables.
- Incremental Costs: The figure of £1,499k reflects the anticipated increases to salary costs as a result of upward movements on the agenda for change pay scale.
- Non Recurrent CIP in 2011/12: The figure of £2,308k relates to CIP achieved non recurrently in 2011/12, which therefore needs to be added back into the 2012/13 position. Within the plan this is partly mitigated by a £1,308k vacancy factor, which assumes continued management / review of vacancies in 2012/13. This leaves a net pressure of £1,000k included within the plan.

- Agreed Cost Pressures: The figure of £2,023k includes agreed cost pressures which are summarised in the following figure.

**Figure 3: Summary of Agreed Cost Pressures**

| Description | 2012/13 £000 |
|---|---|
| **General Cost Pressures** | |
| Agency Worker Regulations | 300 |
| Medical Staff Cover | 840 |
| Pay Award for Low Paid Staff (<£21,000) | 341 |
| Carbon Allowances | 120 |
| IHSS Contract | 126 |
| Above Inflation Increase - Fuel | 100 |
| Above Inflation Increase - CNST | 196 |
| **Total Cost Pressures** | **2,023** |

- Additional 2012/13 Cost Pressures: The figure of £1,700k relates to additional cost pressures identified following discussions with budget holders. This is partly mitigated by reserves held in 2012/13 which can be allocated on a recurrent basis (£400k), and the assumption that the pressures can be partly mitigated (£300k). This leaves a net pressure of £1,000k included within the plan.
- Inflation: The figure of £2,125k relates to standard inflation applied across non staff expenditure. 2012/13 is the second year of the pay freeze, so there is no allowance for pay awards, with the exception of increase for lower paid workers (staff earning below £21,000) which is included as part of the cost pressure and is included in figure 3 (above).
- Contingency: The Trust is requires to set aside 0.5% of income as a contingency. The £1,300k included therefore reflects the establishment of a contingency reserve. A number of financial cost pressure risks have been identified and will be subject to further review and scrutiny.
- Haringey Children's Service FYE: The figure of £1,000k has been included in respect of the full year expenditure position for Haringey Children's service, this is corresponding adjustment to the expenditure position to match the full year income adjustment ( services transferred to the Whittington in May 2011). The next iteration of the LTFM will review the full year effect funding requirement as an upward pressure is likely to be required.
- Increased Capital Charges: The figure of £600k relates to additional capital charges in respect of the new EPR and Joint Ward.
- CIP: The figure of £13,120k reflects the agreed cost improvement target for 2012/13.

## 10. Summary of Key Risks and Opportunities

The purpose of this paper has been to outline a proposed budget and to identify key risks, the key risks being:

- NCL Commissioner intentions, and specifically the risk that contract values are subject to significant further reductions, the gap between the respective positions of NCL and the trust currently stands at circa £13.75m.
- Failure to deliver quality and innovation improvements necessary to secure additional CQUIN payments included as part of the overall plan.
- The 2011/12 forecast position used as the basis for developing the budget provides a realistic and reasonable position based on knowledge of activity levels and trends, it

should be noted however that activity and income levels have been lower than would have traditionally been expected. Continuation of this trend would present a risk to income levels necessary to cover expenditure budgets.

- Additional challenges highlighted as part of the detailed assessment of budgets and identification of CIP schemes, including higher than expected;
  - Marginal costs / failure to extract marginal costs in line with reductions to activity;
  - Incremental Costs;
  - And above inflation cost increases e.g. fuel;
  - Other unanticipated cost increases; and
  - A failure to deliver CIP as planned.
  - A failure to deliver the vacancy factor (£1,308k).
  - A failure to identify mitigating actions (£300k) identified relating to new 2012/13 cost pressures.