



National Audit Office

REPORT BY THE
COMPTROLLER AND
AUDITOR GENERAL

HC 191
SESSION 2012-13

5 JULY 2012

Department of Health

Securing the future financial sustainability of the NHS

Key facts

£2.1bn

total surplus in SHAs, PCTs, NHS foundation trusts and NHS trusts in 2011-12

£1bn

cash given to NHS trusts and NHS foundation trusts in the form of public dividend capital between 2006-07 and 2011-12

34

the total number of NHS trusts (10), NHS foundation trusts (21) and PCTs (3) which reported a deficit in 2011-12

£1.6 billion	total net surplus reported by SHAs and PCTs
£444 million	total net surplus among NHS foundation trusts, including trusts which achieved foundation status during the year
21	NHS foundation trusts in deficit in 2011-12
122	NHS foundation trusts in surplus in 2011-12
£40 million	total net surplus of NHS trusts
10	NHS trusts in deficit in 2011-12
97	NHS trusts in surplus in 2011-12

Summary

1 Between 2011-12 and 2014-15 there will be very little real terms growth in spending on the NHS. The NHS must make up to £20 billion efficiency savings to meet the forecast growth in demand for health services over this period. NHS trusts and NHS foundation trusts face downward pressure on their income with 4 per cent efficiencies built into national tariffs and financial penalties if they do not meet performance standards.

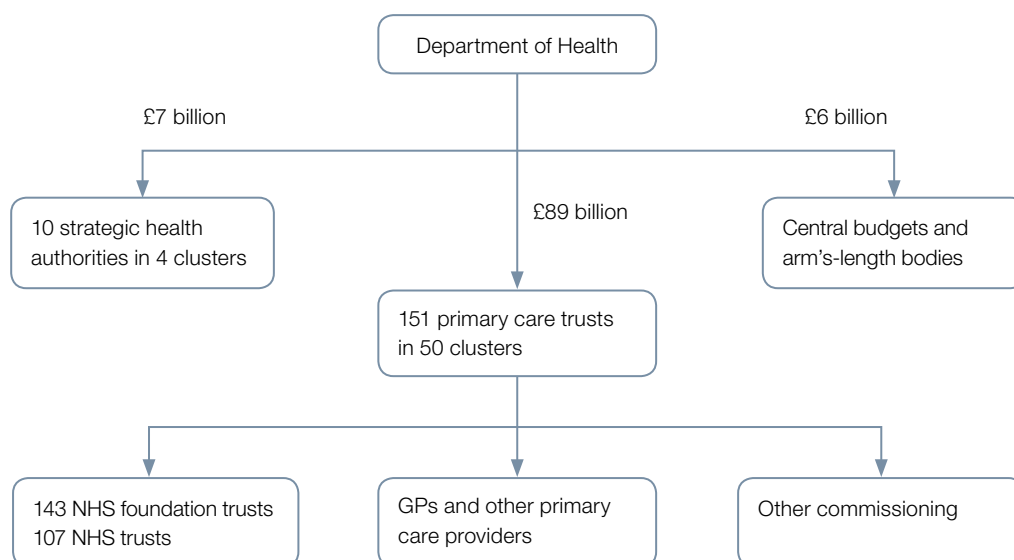
2 **Figure 1** overleaf shows, in a simplified way, how the Department of Health (the Department) funds primary care trusts (PCTs) in England to commission health care services from GPs, hospitals and other providers for their local populations. In 2011-12, as part of the transitional arrangements to implement the Health and Social Care Act 2012, the Department grouped 151 PCTs in England into 50 clusters. There are ten strategic health authorities (SHAs), grouped into four clusters, which performance manage PCTs for the Department. As at 31 March 2012, most tertiary, secondary and community services are provided through 107 NHS trusts and 143 NHS foundation trusts. SHAs also performance manage NHS trusts, while Monitor, an independent regulator, oversees NHS foundation trusts.

3 Implementing measures introduced by the Health and Social Care Act will mean substantial changes to how NHS services are commissioned. PCT clusters managed up to 90 per cent of the NHS revenue budget in 2011-12. Newly created clinical commissioning groups will have their own budgets from 2013-14. From that point the clinical commissioning groups will take over many of the PCTs' commissioning responsibilities. The NHS Commissioning Board will become responsible for commissioning all primary care, overseeing clinical commissioning groups and commissioning specialist services. PCTs and SHAs will cease to exist.

4 This report looks at the financial sustainability of NHS commissioners, and the NHS trusts and NHS foundation trusts that provide community, secondary and tertiary health care services. If NHS organisations are financially unsustainable this could impact on service delivery and quality. The indicators we used were whether NHS bodies achieved surplus or deficit, what financial support they needed, and measures of debt and liquidity. We examined trends in performance and actions that bodies in the most challenged health economies have taken to address financial difficulties as a way of assessing risks to their future financial sustainability. We have identified risks likely to impact on NHS bodies, but have not made detailed projections of the likely future performance of NHS bodies.

Figure 1
Funding for the NHS in England

The Department of Health funds PCTs to commission healthcare services from GPs, hospitals and other providers



NOTES

- 1 Figures shown are based on 2011-12 plan and rounded to the nearest £ billion.
- 2 At the start of the financial year there were 115 NHS trusts and 137 NHS foundation trusts. At 31 March 2012 there were 107 NHS trusts and 143 NHS foundation trusts.

Source: Department of Health

5 In the medium to long term, achieving financially sustainable health care for local communities is likely to mean changes to where, and how, people access services. Some local commissioners and providers are already developing and consulting on plans to do this. It is important that assumptions about the financial sustainability of providers and commissioners which NHS organisations build into their financial plans take full account of the impact of any financial support received in the past.

Key findings

Indicators of the financial health of the NHS

6 SHAs, PCTs, NHS trusts and NHS foundation trusts reported a combined overall surplus of £2.1 billion in 2011-12. The total revenue allocation for the NHS for 2011-12 was £102 billion. The allocation to SHAs and PCTs for them to commission services was £96 billion.

7 There is a large gap between the strongest and weakest organisations in the NHS. Within the overall surplus there is some financial distress, particularly in a number of provider organisations. This is particularly marked in London. Two trusts, South London Healthcare NHS Trust and Barking, Havering and Redbridge University Hospitals NHS Trust, reported a combined deficit of £115 million. The Royal Marsden NHS Foundation Trust reported a surplus of £20 million. **Figure 2** shows that there were 377 NHS bodies which reported a surplus in 2011-12, and 34 in deficit.

8 In 2011-12 SHAs collectively reported a surplus of £1.06 billion, 51 per cent of the total NHS surplus. Some SHAs have proportionately much higher surpluses than others. The total net surplus for all PCTs rose from £476 million in 2010-11 to £523 million in 2011-12. Of all PCTs, 148 out of 151 reported a surplus in 2011-12. The three that did not are parts of the NHS North Central London cluster, which had a combined deficit of £49 million.

Figure 2

Surpluses and deficits reported by NHS bodies in 2011-12

There were 377 NHS bodies which reported a surplus, and 34 in deficit

	In (deficit)		In surplus		Total	
	Number	(£m)	Number	(£m)	Number	(£m)
Strategic health authorities	0	–	10	1,061	10	1,061
Primary care trusts	3	(49)	148	571	151	523
NHS foundation trusts	21	(130)	116	558	137	428
NHS trusts	10	(177)	97	217	107	40
NHS trusts that became NHS foundation trusts part way through the year	0	–	6	16	6	16
Total	34	(356)	377	2,424	411	2,068

NOTES

- 1 Six NHS trusts became foundation trusts in the course of the 2011-12 financial year. We have included The Hillingdon Hospitals NHS Foundation Trust, which achieved foundation status on 1 April 2011, in figures for NHS foundation trusts for the whole year. The £16 million surplus shown is reported by the Department as £5 million for the period in which they were NHS trusts, and by Monitor as £11 million for the period in which they were NHS foundation trusts.
- 2 Totals may not sum due to rounding.
- 3 Limitations in the data mean that figures for NHS trusts and NHS foundation trusts have to be calculated in slightly different ways. The methodology appendix explains how we have calculated these figures.

Source: National Audit Office analysis of audited trust financial data from Monitor and the Department of Health

9 In 2011-12, NHS foundation trusts reported an average surplus of £3.1 million, compared with £2.9 million in 2010-11. NHS foundation trusts, as self-governing institutions, do not have a statutory duty to make a specific surplus in any single year. In 2011-12, 21 NHS foundation trusts finished the year in deficit, an increase from 19 in 2010-11, and had a combined deficit of £130 million. At the end of the year, NHS foundation trusts taken together had a total of £4.0 billion of cash and cash equivalents, £2.2 billion other current assets, and £4.7 billion current liabilities, altogether representing total net current assets of £1.5 billion. Case examples in this study, such as Peterborough and Stamford NHS Foundation Trust, however, show that some NHS foundation trusts are also facing severe challenges.

10 There is a small group of NHS trusts in long-term financial difficulty. By the end of 2011-12, ten trusts reported a combined deficit totalling £177 million, compared with the total £217 million surplus reported by the other 97 trusts.

Financial support given to commissioners and providers

11 The vast majority of PCTs, NHS trusts and NHS foundation trusts reported a surplus in 2011-12. Among those, 51 of the NHS trusts and NHS foundation trusts reported a surplus of less than £1 million. Any assessment of the underlying financial sustainability of the NHS, however, must also recognise that SHAs and PCTs agreed non-recurrent funding to some trusts: direct financial support to increase income; and other non-recurrent funding, including support for transitional costs or business changes. In addition, the Department provided injections of cash to some trusts, in the form of public dividend capital, to strengthen the balance sheet, provide working capital or cover cash shortages resulting from deficits. All financial support is intended to help maintain services for patients, and is conditional on plans for recovery to a more sustainable position.

Direct financial support

12 Without direct financial help some NHS trusts, NHS foundation trusts, and PCTs may not have broken even, would have reported larger deficits, or had smaller surpluses. Had this support not been made available, some of those organisations may have been able to reduce their expenditure further. We estimate that SHAs and PCTs provided £151 million in additional revenue to NHS trusts and £10 million to NHS foundation trusts. **Figure 3** shows that, without 'one-off' direct support, an additional 15 NHS trusts may have posted deficits in 2011-12. We also identified seven PCTs that may have reported a deficit had they not received additional resource allocations directly from their SHA, or benefitted from reallocations between PCTs within the same cluster, totalling £89 million.

Figure 3

Financial support to PCTs, NHS foundation trusts and NHS trusts

Without 'one-off' direct support, an additional 15 NHS trusts may have posted deficits in 2011-12

Change in financial position excluding the effect of direct financial support	Number of bodies which may have moved from surplus to deficit (number)	Potential increase in deficit (£m)	Potential reduction in surplus (£m)
Primary care trusts	7	(82)	(7)
NHS foundation trusts	0	(6)	(4)
NHS trusts	15	(132)	(19)
NHS trusts that became NHS foundation trusts partway through the year	0	0	0
Total	22	(221)	(30)

NOTE

1 Totals may not sum due to rounding.

Source: National Audit Office analysis of audited trust financial data from Monitor and the Department of Health, and information provided to the National Audit Office by strategic health authorities and primary care trusts

Other non-recurrent funding

13 It is difficult to identify the full extent of one-off funding PCTs are giving NHS trusts and NHS foundation trusts. We found that SHAs were aware of most, but not all, of these agreements. To identify the nature and extent of non-recurrent funding, we undertook a census of PCT clusters. Because this was a census of PCTs, rather than provider trusts, it may be more likely to highlight examples where commissioners may be supporting providers, rather than the other way round, and it relies on commissioners' rather than providers' views of what the purpose of additional funding was.

14 We estimate, based on our census of PCTs, that SHAs and PCTs gave NHS trusts and NHS foundation trusts other non-recurrent funding to help them break even, or cover non-recurrent costs, which in 2011-12 totalled at least £274 million.

We cannot identify the extent to which, had commissioners not been able to provide additional funding, trusts could have avoided non-recurrent costs. Facing the same costs, however, without this financial help another 16 NHS trusts and 11 NHS foundation trusts may not have broken even. This sort of funding included:

- funding explicitly to relieve financial pressures, including transitional support (£147 million); and
- funding to help implement business changes (£127 million).

Public dividend capital

15 Four NHS foundation trusts and 17 NHS trusts have received public dividend capital totalling just over £1 billion between 2006-07 and 2011-12, to provide working capital (cash).

The Department gives revenue public dividend capital to ensure they have sufficient cash to pay creditors and staff. Public dividend capital is not accounted for as income, so does not affect whether a trust reports a surplus or deficit. South London Healthcare NHS Trust, and its predecessors, have needed a total of £356 million public dividend capital support over the last six years, and not paid any back. Public dividend capital issued to NHS trusts and NHS foundation trusts by the Department in 2011-12 totalled £253 million, a sharp increase from the £76 million public dividend capital paid in 2010-11.

Risks to the future sustainability of local health economies

16 The relationships that commissioners and SHAs have with providers in need of financial support, and the level of support offered, vary across the country.

Some PCTs have had limited ability to support providers because of pressure on their own financial resources.

17 Only two PCTs now have historic debt from overspending in previous years.

The total amount of outstanding debt at the end of March 2012, for these two commissioners, was £21 million. The Department expects existing PCT clusters to have cleared all legacy debts during 2011-12 and 2012-13, so as not to pass liabilities to the new clinical commissioning groups.

18 NHS foundation trust margins are being squeezed. A key measure of underlying financial performance is the 'earnings before interest, tax, depreciation and amortisation' (EBITDA) margin. The EBITDA margin fell from an average of 7.8 per cent in the first quarter of 2008-09 to 6.1 per cent at the end of 2011-12. Monitor scored three NHS foundation trusts with a financial risk rating of 1 and six with a rating of 2. The average financial risk rating has dropped from 4.1 in the first quarter of 2008-09 to 3.4 in 2011-12.

19 At the end of the 2011-12 financial year, Monitor, the financial regulator of NHS foundation trusts, assessed 11 out of 143 NHS foundation trusts as in significant breach of their terms of authorisation wholly or partly for financial reasons. Monitor scores foundation trusts on a five-point scale, and judges a rating of 3 (or higher) to be the minimum acceptable level of financial performance. This does not map directly on to snapshot financial risk ratings.

20 NHS foundation trusts in difficulty may need the Department to provide working capital because commercial banks withdraw facilities. One of the terms under which commercial banks may provide working capital facilities is that NHS foundation trusts maintain a Monitor risk rating of 3. Trusts rated 1 or 2, however, are likely to be those most in need of cash support.

21 The Department has given working capital loans to NHS trusts and NHS foundation trusts, and as at 31 March 2012 there was £236 million outstanding. Trusts have taken out loans to improve their liquidity, sometimes because of a poor cash position. The Department will only issue loans when it is confident trusts will be able to repay them from future surpluses, and interest is charged on the outstanding balance.

22 Some PCTs have agreed to make advance payment of amounts due to trusts under contracts during the year. Some trusts have needed to do this to help them manage cashflow, and allow them to pay creditors.

23 In addition, PCTs waived fines for providers, for example for failing to achieve acquired infection targets; or made local agreements for the amount paid to providers for emergency admissions and readmissions. The PCTs we spoke to explained that rather than levy penalties, they expected trusts to use the money saved to improve their performance in these areas. Commissioners also agreed payments to reflect increased work where measures to reduce referrals or emergency admissions had not been in place.

24 Among NHS trusts aspiring to NHS foundation trust status there are around 40 trusts that remain on course, but a larger group which are failing to meet milestones and are postponing application dates. At the end of September 2011, there were 19 trusts due to submit their foundation trust application to the Department before the end of 2011-12. At the end of March 2012, ten of these were rated as 'red risk' because of the danger that they will not stay on the forecast trajectory towards foundation trust status. A further nine with later application dates are also 'red risks'. Our report in October last year, *Achievement of foundation trust status by NHS hospital trusts*, showed that at least 20 NHS trusts were not financially sustainable in their current form.

25 It is not yet clear whether clinical commissioning groups and the NHS Commissioning Board will agree to provide financial support to providers, in the way that SHAs and PCTs have done.

26 Of the primary care trust clusters responding to our census, 51 per cent said they were very or quite concerned about the financial sustainability of their providers. The challenges faced by any one trust are determined by local circumstances. PCTs and SHAs that we spoke to highlighted a common set of problems from their perspective:

- Provider trusts will have to achieve higher levels of efficiencies than they have previously managed.
- In the past, some large annual increases in income have allowed provider trusts to stay in surplus by growing income rather than focusing on cost reduction, but the potential to do this is now limited.
- Contractual rules are now making it much more difficult for providers to improve their finances by increasing activity.
- Some hospitals cannot afford private finance initiative commitments, or commitments limit the scope to reduce services. Some trusts will face increased pressure as the amount of tapered private finance initiative support they receive, agreed as part of the original business case, reduces. Based on responses to our census of PCTs, we estimate that this totalled at least £61 million in 2011-12. The Department has announced that six NHS trusts and one NHS foundation trust will receive central support to offset the cost of 'unaffordable' private finance initiative schemes, from 2012-13 onwards.
- Commissioners must improve their financial position and make efficiencies, which reduces their ability to manage the local health economy to support providers (although local policy on this varies).

27 No NHS trust or NHS foundation trust has yet been placed in a 'failure regime'. The Health and Social Care (Community Health and Standards) Act 2003 gave Monitor the power to replace members of NHS foundation trust boards, which it has used on occasion, or dissolve an NHS foundation trust, which it has not. Amendments in the Health Act 2009 created the option for the Secretary of State to appoint a special administrator to take over a failing NHS trust.

Conclusion on value for money

28 Funding for the NHS will not substantially increase, in real terms, over the next three years. The NHS delivered a surplus of £2.1 billion in 2011-12 but within this there is significant variation in financial performance. At the moment some organisations in difficulty have been given additional financial support through both direct financial support and additional non-recurrent funding. It is hard to see that this approach will be a sustainable way of reconciling growing demand with the scale of efficiency gains required within the NHS. Without major change affecting some providers the financial pressure on them will only get more severe.

29 For value for money to be delivered in future, two things are required: first, careful management of the risks created by transition to a new commissioning model; and second, a coherent and transparent financial support mechanism is needed which outlines when trusts should be supported, or allowed to fail.

Recommendations

- a** The Department should implement a framework for local health economies to ensure that non-recurrent support to financially weak providers or commissioners is transparent. This should be incorporated into the standard reporting mechanisms being developed for the new health system. At present, the extent to which PCTs and providers are reliant on one-off financial support, particularly through additional non-recurrent funding, is not always visible.
- b** The Department, in line with the new Health and Social Care Act (2012), should publish guidance on assistance to both NHS trusts and NHS foundation trusts around both the provision of non-recurrent support and issuance of public dividend capital. The Department should also decide when providing public dividend capital to NHS trusts or NHS foundation trusts, in what circumstances, if ever, it will expect repayment.
- c** The Department will need to make available additional working capital for NHS trusts in the pipeline if they are all to have sufficient liquidity to become an NHS foundation trust. The Department should also introduce a central working capital fund that NHS foundation trusts can access as an alternative to commercial facilities. This would reduce the costs that NHS foundation trusts pay for commercial working capital facilities, and prevent NHS foundation trusts from having their working capital facilities withdrawn when they have financial difficulties.
- d** The Department should explain how it will ensure the financial stability of local providers should clinical commissioning groups get into financial difficulty. Clinical commissioning groups will be progressively authorised to take on commissioning responsibilities for NHS trusts and NHS foundation trusts from late 2012. In a few areas they will face a difficult financial situation at both provider and commissioner level.
- e** The Department should use, where appropriate, the failure regime measures currently available to it for those NHS trusts in the pipeline that cannot achieve foundation trust status. Some providers may be too financially weak to be viable as merger partners and other alternatives to long-term financial support need to be found.
- f** Monitor should publish detailed guidelines explaining how, in practice, the failure regime for NHS foundation trusts which are not sustainable long term will be activated and executed. The Health and Social Care Act 2012 introduces a failure regime for NHS foundation trusts, giving Monitor the opportunity to address the small number of NHS foundation trusts that have spent years in significant breach of their terms of authorisation because of their finances.