Written evidence from Department of Health

Ahead of your upcoming evidence session on the Department of Health annual accounts, I am writing to highlight some of our recent analysis that I hope you and the rest of the committee may find useful.

Provider finances

Although the Department contained its spending within its authorised budget in 2016/17 and the NHS broadly delivered financial balance as a whole, the headline figures mask the continued serious financial difficulties within the NHS.

Despite measures to improve NHS finances, including the addition of £1.8 billion in sustainability and transformation funding (STF) and further transfers of funding from capital to revenue budgets, the NHS provider sector reported a net deficit of £791 million in 2016/17, which was £211 million worse than the original target deficit of £580 million. It is also worth noting that because of accounting terms the Department of Health accounts recorded a higher deficit figure than this. The provider sector is already off track for 2017/18 with a deficit of £523m forecast for the full year against an original aspiration that the sector would be in financial balance.

All parts of the NHS are under pressure, but acute hospitals are particularly challenged. Our analysis of the financial data published by NHS Improvement shows that of the 105 providers in deficit, 83 were acute hospitals. With demand for emergency hospital care and workforce pressures both continuing to increase as the NHS heads into winter, is likely that the acute sector will continue to contain the most challenged providers in 2017/18.

The STF has not been enough to bridge the financial gap facing the sector, with some providers also relying on additional loans or running down their financial reserves, our June Quarterly Monitoring Report highlighted. This extensive reliance on additional loans from the Department of Health points to ongoing fundamental problems within the NHS financing regime. Coupled with STF, the introduction of financial control totals and the Controlled Expenditure Process (CEP), there is a sense of layering upon layering of short term financial controls for what is ultimately a structural problem.

Capital funding

The position with capital spending highlights the clear mismatch between planning and reality. NHS trusts submitted initial spending plans worth £4.1 billion but these were reduced to £3.3 billion and then later in the year cut further to £2.9 billion. These cuts were essential as the overall approach to managing the money relies on repeated switches from capital spending to support day-to-day expenditure. In the last year the Department of Health transferred £1.2bn from capital to revenue spending.

Scaling back capital spending has come at a price, with the cost of the backlog of ‘high-risk’ maintenance work increasing from £458m in 2014/15 to £947.1m last year. Our June 2017 survey of trust finance directors also found providers had delayed or deferred capital spending at the end of the last financial year. Once again this is a short-term solution to a long-term problem, and will be a false economy if hospitals are running services from inefficient buildings with equipment that needs replacing. A strategic approach is needed, and we are still awaiting a concrete response to Sir Robert Naylor’s review of the NHS estate to translate the government’s manifesto commitment to deliver ‘the most ambitious programme of investment in buildings and technology the NHS has ever seen’ into reality.
Ultimately, continuing to move money from capital budgets to revenue budgets is not a sustainable strategy.

**NHS Commissioners**

The provider deficit is only manageable because NHS commissioners continue to run substantial underspends. However, in 2016/17 there were the first signs of widespread distress amongst CCGs, with many failing in delivering the target 1% underspend of their allocations. Instead, the difference was made by savings in NHS England itself. This raises two concerns: firstly, that CCGs are now on a downward trajectory; secondly that NHS England’s savings come partly through withholding transformation funding, resources that are needed for the NHS to deliver on the Five Year Forward View.

**Financial sustainability**

While end of year position for NHS providers was better in 2016/17 than in 2015/16, it was worse than originally planned. NHS providers and the central bodies worked incredibly hard throughout 2016/17 and made considerable progress, but this was still not enough to close the financial gaps facing the sector. Balancing the books last year came at a cost – both in terms of the frantic to-and-fro between national and local NHS organisations to contain spending, and a short-term focus on end of year finances at the expense of a long-term strategy, which will be crucial as the NHS now enters its lowest period of funding growth in the current settlement.

The shared planning guidance for 2017/18 again noted the ambition that ‘at national level, the provider sector needs to be in financial balance in each of 2017/18 and 2018/19’. But after just the first quarter, provider deficits for 2017/18 are forecast to be £500 million. In June 2017, our quarterly monitoring report found that 43 per cent of trusts we surveyed were forecasting ending 2017/18 in deficit. Whether or not the Department manages to live within its spending controls this year, 2018/19 looks exceptionally challenging as real terms growth in spending is currently planned to fall close to zero.

I hope this gives you and the committee a useful insight into last year’s annual accounts and the position the provider sector is currently facing.

Please don’t hesitate to contact us should you require any further information.

Yours sincerely

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The King’s Fund