

HINCHINGBROOKE ONE YEAR OF CIRCLE



HSJ Local Briefing is our new in-depth analysis of the key issues facing the NHS's major health economies

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In brief

Issue Hinchingsbrooke Health Care Trust became the second NHS hospital to be franchised to a private company when Circle began running the hospital last February. This analysis explores the lessons learned from the last year and the future prospects for the hospital franchise model.

Context A year into the franchise experiment, senior health figures are questioning the viability of using the model more widely in hospitals. They cite austerity and the need to reduce activity in hospitals as key drivers. Failure by Circle would deal the model a potentially fatal blow. It faces a tough challenge. Its savings plan, which is intended to clear a £40m debt, was criticised as "over ambitious" by the public accounts committee this month. Unions continue to call for Circle to leave.

Outcome Circle's ambition to clear the trust's debt are unlikely to materialise. Even the company admits it may not pay off the debt. Clinical improvements have been made since Circle arrived but it remains to be seen whether standards can be maintained while driving through large efficiencies.

It appears likely Circle will continue to run the trust, rather than withdraw when it has an opportunity. If it were to leave, questions about the future viability of Hinchingsbrooke's services are likely to arise.

The hospital franchise model is not dead, but appetite is diminishing in the short term.

Background

Hinchingsbrooke Health Care Trust became the second ever NHS hospital to be franchised to a private company in November 2011 when ministers signed a 10-year deal with Circle.

Events at the Cambridgeshire hospital will have a profound impact on the private sector's role in providing NHS services and in particular on the future of the hospital franchise model.

A combination of economic and political drivers has seen appetite for the model drop off dramatically in the last 12 months.

The model must deliver value for money for the NHS and private sector, a balancing act previous public-private arrangements have failed to achieve.

Private finance initiative (PFI) deals have left a string of trusts – not least Peterborough and Stamford Hospitals Foundation Trust, which is just 24 miles from Hinchingsbrooke – with serious financial problems.

Moreover, the debate around the private sector profiting from the NHS will always be ideologically and emotionally charged.

In addition to a difficult backdrop, the challenge facing Circle is huge for two other broad reasons.

First, its business plan proposed unprecedented savings for a NHS trust which the public accounts committee last month dismissed as "over ambitious".

Secondly, the broader environment has become increasingly challenging for private providers looking to run full-service hospitals under a franchise model.

Commissioners are trying to take activity out of acute hospitals; tariffs are being ratcheted down; and there is uncertainty over public sector pay. Required efficiencies savings are drastic.

Circle took over the hospital in February 2012. This briefing considers the lessons from its first year and the future of the franchise model.

The hospital

Hinchingsbrooke is a small district general hospital with a turnover £107m and serves a 160,000 population.

A National Audit Office report, The franchising of Hinchingsbrooke Health Care NHS Trust, said it was in financial turmoil because of a series of "management errors including: payment by results submission inaccuracies; and miscalculating the demand for a new private finance initiative treatment centre".

When Circle took over it had £39m of accumulated debts and an estimated structural annual deficit of up to £4m.

Stephen Dunn, director of policy and strategy at NHS Midlands and East, which played a key role in the deal, said despite the financial problems, "the hospital was not a failing trust".

"The hospital provides great quality services to the local people," he added.

However, the trust had some substantial clinical challenges, including issues with waiting times, colorectal services and cancer services.

The debt is unlikely to be paid off

Circle's business plan projects it will achieve £311m savings over the 10-year life of the franchise – an unprecedented sum which would leave the hospital debt-free if it was successful.

Circle's proposed savings represent over 5 per cent each year over the contract. An essential element of the projected savings is an assumed annual 4.3 per cent efficiency saving from year four onwards.

Cost saving plans include job cuts; increasing private patients; changing nurse to bed ratios and streamlining A&E.

The public accounts committee's Report on the Franchising of Hinchingsbrooke Health Care NHS Trust and Peterborough and Stamford Hospitals NHS Foundation Trust, published on 7 February, said Circle had submitted "overly optimistic and unachievable savings projections".

The NAO report said Circle had not fully specified "how it would achieve these savings [and] most of the savings are expected to be made in the later years of the 10-year franchise".

Circle maintains the terms of its contract incentivise it to make the savings and pay off the trust's debt. However, analysis shows the deal does not force Circle to pay off the debt.

The company remains adamant it will strive to clear the debt but admitted to HSJ it may not happen.

"If we deliver all the plans in our tender, it pays off the historic deficit. If we use all our best efforts but the world changes, ten years is a long time, and we only get half way through that, then we will have paid off a big chunk of the [historic] deficit," said Circle chief executive Steve Melton.

As revealed by HSJ, the deal is structured so that the first £2m of any year's surplus goes to Circle. The company takes a quarter of surpluses between £2m and £6m, and a third of surpluses between £6m and £10m.

Any surplus which does not go to Circle would go to the NHS, and used to make contributions to pay down the debt.

It would be unrealistic for Circle to have pay off the entire £40m before making a profit. But the deal structure suggests Hinchingsbrooke's debts will not be cleared in 10 years.

Put simply, Circle could take a £2m profit each year and not pay down the debt – although it would have to be running a surplus to achieve this.

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Financial performance in 2012-13

The trust is currently forecasting a £3.7m deficit for Circle's first year in charge having planned to "more or less break even" in November 2011.

A variety of reasons – including a higher than anticipated deficit when the company arrived – have been put forward by the company.

The company has to pay any deficit accumulated during the contract up to a cumulative total of £5m. If the trust incurs further losses on Circle's watch, either party can terminate the deal, requiring Circle to pay a £2m termination fee to Hinchingsbrooke.

This year's deficit means it is likely the company will have to pay nearly three quarters of the £5m in the first year of the contract alone.

Unison, a long-standing critic of the franchise deal, has raised concerns that Circle will walk away from the deal imminently – an accusation the company rejects.

While the company remains wedded to the notion it will not need to break its agreed limit, HSJ understands the wording of the contract allows the company to put more money in.

Hitting the £5m mark would trigger discussions between the Circle and the NHS but, should both parties agree, further Circle money could be injected.

Senior health experts told HSJ Circle had too much invested in Hinchingsbrooke both financially and in reputation. Walking away would raise fundamental questions about its future.

Circle's finances

The amount Circle has raised from investors shows the size of what is at stake for the company. Its holding company, Circle Holdings, is listed on the London Stock Exchange AIM sub market.

Last June, it raised £47.5m by allocating around 67.9m shares to institutional investors. Company documents warned it would have risked "insolvency of all or part of the Group" if it had failed to do so.

This was apparently a very unlikely scenario. Investors would have been sounded out before such a share offer was put together to make sure there were sufficient takers. However, the warning is a reminder that Circle's environment, where substantial sums are raised from international investment vehicles and hedge funds, is very different to the UK public sector.

The company posted a pre-tax loss of £32.9m on revenues of £74.6m in 2011 and pre-tax losses of £38.8m on revenues of £76.4m in 2010.

However the company told HSJ it was still forecasting positive earnings before interest, taxes, depreciation and amortisation – an operating profit – by 2014.

The company said its current predicament of raising money from backers and posting losses is a development phase which will pay off in the long term.

The company's financial prospects were given a significant boost this month when it announced it had secured a further five-year contract to provide services at the Nottingham NHS treatment centre, worth £22m-£42m a year.

The contract win was a critical development for the company but failed to have a substantial impact on its share price.

Circle's share price dropped by around two thirds from over 180p to 65p a share over the last 12 months, including a sharp drop in June 2012 (see chart).

Its then chief executive Mr Parsa said that big dip was due to the company's decision to raise money upfront, but that he was confident it would recover in the long term.

HSJ understands the company does have further income-earning projects in its pipeline which will be unveiled in the coming few months.

Clinical improvements and the Circle model

Despite the financial issues at Hinchingsbrooke, there is evidence of improved clinical performance.

The trust received a clean bill of health from the Care Quality Commission in December for the first time since its inspections began. Circle said it had prioritised fixing quality issues over financial first.

On arriving at Hinchingsbrooke the company said it identified colorectal services, cancer surgery and accident and emergency waiting times as not fit for purpose.

In January 2012 – before Circle took over – the trust had fallen below the 95 per cent standard for four hour waits in A&E and, according to Mr Melton, there "was a very live debate about" whether Hinchingsbrooke should offer a full A&E service. The trust has since significantly improved A&E waiting times performance.

In March 2012, a review by the Royal College of Surgeons highlighted "serious failings within the colorectal service" which were first flagged in June 2011.

Circle brought in a leading colorectal surgeon from its Nottingham hospital, as well as other clinicians, and has been credited by NHS Cambridgeshire with "transforming" the quality of care.

The company attributes clinical success to its decision to implement the "Circle operating model". That is, in summary, putting more clinicians in leadership roles.

Hinchingsbrooke now has seven clinicians on its executive board. There was just one before, the medical director.

The decision has gone down well

with commissioners.

Speaking on behalf of NHS Cambridgeshire, Abby Richardson, a GP and vice-chair of Hunts Care Partners, a local commissioning group, told HSJ that Circle had provided "greater clinical engagement and leadership" in negotiations with commissioners and would have a positive on patient care.

Unions reject claims of greater staff engagement. They highlight results of a recent staff survey which showed the trust has seen a "minor but consistent deterioration" in staff morale since it was taken over.

Circle said the results were "unquestionably disappointing". The Royal College of Nursing has said morale was "extremely low" and staff "angry and bewildered".

If Circle left Hinchingsbrooke

The unions want Circle to leave Hinchingsbrooke – but this would raise fundamental questions about the future of its services.

Well placed observers said the hospital would be unlikely to shut, but it would be likely to see some services downgraded. This may be seen as helping the trust itself – and nearly Peterborough and Stamford Hospitals Foundation Trust, which is also heavily in debt – to become stable.

NHS Midlands and East policy director Stephen Dunn warned last year that without Circle, the hospital "might have to close".

He wrote that, had Circle not taken over Hinchingsbrooke, "services might have been cut, the hospital might have had to close, or an £80m subsidy might have needed to support the existing management".

Future of the hospital franchise model

Senior sources told HSJ that Whitehall's interest in franchising

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acute trusts to either the private sector – or to NHS foundation trusts – had waned dramatically over the last 12 months.

There has been considerable interest in the model in recent years and particularly when Andrew Lansley was health secretary. However, the complexity of the model has raised concerns, as have the political challenges and lack of evidence that it will deliver sustainable solutions.

The Treasury's decision, revealed by HSJ, to place plans by the George Eliot Hospital Trust to tender for a private management franchise on hold until it has carried out a full review may be an indication of the new climate.

Treasury officials will be likely to bear in mind the public accounts committee's criticisms of Circle's business plan for Hinchingsbrooke as they carry out their enquiries.

The broader economic and policy environment has also become increasingly challenging for private providers who may want to run a franchise.

Future of the hospital franchise model

Commissioners are stepping up efforts to reduce hospital activity; tariffs continue to be cut; and there is uncertainty over public sector pay. As a result the requirement for efficiency savings in the NHS is drastic.

Bill Morgan, a special political adviser to Mr Lansley when he was health secretary and now a senior adviser at MHP Health Mandate, told HSJ: "The idea that there are lots of private sector companies in the UK able and willing to take on hospitals which are in serious difficulty, it's just not true."

Circle remains adamant it is still looking for further opportunities at full service hospitals but it appears the view across much of the market is shifting.

Conclusions

Circle is just one year into a 10-year project: any overarching judgement about its success or failure would be premature.

However, some early conclusions can be drawn.

- Circle is unlikely to clear the trust's deficit. The company itself acknowledged it may not pay down the debt.
- The company can take heart from clinical improvements, although whether it can maintain standards while driving through searing efficiencies remains to be seen.
- Union fears that Circle will walk away appear premature. The company's entire brand and considerable finance is staked on Hinchingsbrooke. Failure by Circle at Hinchingsbrooke would raise fundamental questions about the viability of both the company and Hinchingsbrooke's status as a full-service hospital.
- The franchise model may not be dead, but diminishing appetite from both the public and private sector suggests its use will be limited in the short and medium term.