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Monitor
Independent Regulator
of NHS Foundation Trusts

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To: Foundation Trust Applicants
Foundation Trust Unit
Foundation Trust Network
Foundation Trusts

Dear Colleague,

Re: Update to Monitor's financial assumptions

Context

Monitor's financial assumptions are used by Monitor to assess applicant trusts for foundation trust status and for risk rating certain investments and transactions undertaken by existing NHS foundation trusts. They are not intended to provide a basis for commercial decision making by or between providers and commissioners within the NHS, including contract negotiations. However, existing NHS foundation trusts may find it useful to consider these assumptions as part of their own annual planning rounds.

As new evidence comes to light and policy develops, it is important for this to be reflected in the financial assumptions to ensure good decision making both by trusts and by Monitor's Board. As a consequence, following the publication of the Operating Framework for the NHS in England 2012/13, and other new evidence on the financial condition of the sector, Monitor's Board has decided to update the financial assumptions to reflect more recent evidence of the continuing pressures on NHS funding.

Our financial assumptions are determined using an evidence-based methodology. They are represented as an estimate of the efficiency requirement for trusts over the next five years. This efficiency requirement reflects the overall pressure on the service based on expected growth in demand for NHS services (e.g. due to an ageing population, inflation and rising drug costs), against which there will be only limited growth in funding. When the efficiency requirement is applied to individual trusts, we also consider whether local health economy circumstances could mean that either more optimistic or pessimistic assumptions should be made.

Methodology

As a regulator we use two scenarios as the starting point to assess trusts for foundation trust status, an 'assessor case' and a more challenging 'downside case'. The assessor case reflects our central estimate of the expected pressures and risks to providers' income and costs. The downside case builds on the assessor case but reflects a more pessimistic view of the expected pressures and risks. There are separate sets of assessor and downside assumptions for acute and non-acute providers (i.e. ambulance trusts, mental health trusts and community trusts) due to differences in pressures and risks.

Our assumptions on income pressures are consistent with guidance in the Operating Framework regarding the change in tariff for 2012/13 and beyond. Our assumptions about cost pressures are based on careful consideration of the likely pay and non-pay pressures in the NHS, including the latest economic forecasts published by the OBR, historic trends in NHS pay and prices, and stated government policy on public sector pay.

Whilst the assumptions are first applied generically to all applicants it is recognised that individual providers will face their own specific circumstances and will, to some extent, be able to mitigate the risks (and therefore part of the required efficiency requirements). Where mitigating actions are backed up by careful and evidence based planning we will consider offsetting our assumptions with their impact.

Efficiency Requirement

The table below details the implied sector-wide efficiency requirement facing providers based on these updated assumptions; we anticipate that these levels of recurrent efficiencies will be required from all providers.

Table 1: Sector-wide efficiency requirements

		2012/13	2013/14	2014/15	2015/16	2016/17
Acute	Assessor	4.5%	5.0%	5.0%	4.2%	4.2%
	Downside	5.25%	5.5%	5.5%	5.0%	5.0%
Non-acute	Assessor	4.5%	5.0%	5.0%	4.2%	4.2%
	Downside	5.0%	5.5%	5.5%	4.7%	4.7%

In addition, for acute trusts we consider the impact of tariff income levers as described in the Operating Framework and Payment by Results Guidance for 2012/13. These include:

- Tariff rules relating to the non-reimbursement of emergency readmissions within 30 days of discharge following an initial episode of elective care.
- The 30% 'marginal tariff' for non-elective procedures.
- Tariff flexibility that allows providers and commissioners to agree in exceptional circumstances variations from tariff prices below the national published price.

Monitor will consider the impact of tariff income levers in line with the policy adopted by a trust's commissioners. Depending on local circumstances and actions being taken by the trust, the impact of the tariff income levers could be significant, and based on evidence for the acute sector as a whole, could increase the overall efficiency challenge by 2% (non-recurrently). For an individual trust, evidence indicates that this additional challenge could be more or less than 2% and this risk could be managed to a lesser or greater extent by each trust. Consequently, we will assess and apply the additional pressure from the tariff income levers non-recurrently on a case-by-case basis to reflect the circumstances of individual trusts.

It is important to note that Monitor will consider evidence provided by trusts to support assumptions made in relation to tariff income levers, for example where providers can show that they have plans in place to reduce emergency readmissions and/or non-elective activity growth, or providers can demonstrate that there is an integrated and planned approach across a local health economy to address the risks of patient readmissions.

The non-acute downside efficiency is lower than the acute efficiency downside from 2015/16, based on evidence that acute trusts are experiencing greater financial pressures than the non-acute sector.

Implications

These assumptions reflect Monitor's current view of the likely sector-wide impact of the operating environment and specific risks facing acute and non-acute providers and are consistent with maintaining the current "bar" for achieving foundation trust status. We recognise the scale of the productivity challenge that these revised financial assumptions imply. However, it is important that the assumptions reflect the current policy framework and economic outlook, which continues to be challenging. The assumptions recognise that cost improvement programmes will need to be delivered on an even more ambitious scale going forward. To ensure quality is not compromised, it will be important for trusts to look at new ways of working and new ways of delivering services as they seek to address these challenges. In some areas service reconfiguration is likely to be necessary to ensure healthcare provision remains financially viable and safe.

These updated assumptions will come into effect for all foundation trust authorisations and transaction risk rating decisions from 1 May 2012 onwards. We will allow additional time for applicants currently with us for assessment should they request it in order to provide the evidence required to meet the revised assessor and downside cases.

It remains important for trusts to plan effectively and to challenge financial plans and forecasts in light of these updated assumptions. Applicants should continue to develop mitigation plans to address our downside scenario, including developing plans to respond to the impact of the non-elective cap and readmission penalties. In developing such plans applicants will need to pay careful attention to ensure that they can be delivered whilst maintaining quality.

Applicant trusts should contact Miranda Carter (Miranda.Carter@monitor-nhsft.gov.uk) for further information.

Yours sincerely

David Bennett
Chairman and Interim Chief Executive

CC: SHA Provider development leads
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