NHS
Trust Development Authority

Independent Trust Financing Facility Application

The Acquisition of Barnet and Chase Farm Hospitals NHS Trust by the Royal Free London NHS Foundation Trust

1. Purpose

The purpose of this paper is to provide the committee members with an initial briefing on the proposal for the Royal Free London NHS Foundation Trust ("Royal Free") to acquire Barnet and Chase Farm Hospitals NHS Trust (BCF). This paper sets out:

- some background to BCF and to the Royal Free, as the preferred acquirer;
- a description of the TDA's process as vendor and the governance arrangements, to achieve a solution;
- a summary of the work on clinical quality due diligence;
- a summary of the Heads of Terms negotiated between TDA officers, the Royal Free, NHS England and BCF;
- A value for money and sensitivity analysis of the proposed solution

2. Background

2.1 Transaction

BCF's Board recognised in June 2012, following a "Viability Study", that the Trust would not be financially sustainable on its own. After taking independent advice and after further discussion with NHS London, BCF's Board instigated a procurement process to "find a partner".

Through a competitive two-stage procurement process, the Royal Free emerged as the preferred partner. In November 2012, NHS London reviewed the Strategic Outline Case submitted by the Royal Free and decided to support the proposed acquisition of BCF by the Royal Free, subject to the development and agreement of more detailed business cases. A detailed chronology of the proposed transaction is set out in Appendix 1.

Earlier this year, Monitor's Cooperation and Competition Panel completed its Stage 1 assessment and concluded that the proposed acquisition did not result in significant costs through loss of competition, clearing the way for the transaction.

Following the High Court's rejection of the legal challenge by the London Borough of Enfield on 12 November, the implementation of the *Barnet Enfield Haringey (BEH) Clinical Strategy* is being implemented. Maternity services at Chase Farm Hospital ceased on 21 November and the Chase Farm A&E (and associated emergency care services) closed on 9 December. Local patients requiring emergency care will instead be treated at Barnet Hospital, North Middlesex Hospital or in hospitals in Hertfordshire and Essex. This means that the transaction can proceed on a clear basis, without risk of further legal challenge and based on a definite implementation schedule.

2.2 Barnet and Chase Farm Hospitals Trust

Barnet and Chase Farm Hospitals NHS Trust is a challenged NHS Trust, currently providing services to around half a million people living in north London and parts of Hertfordshire. During 2013/14, BCF has been one of the worst performing NHS Trusts in England in terms of A&E performance (patients waiting more than 4 hours) and Referral to Treatment Time (RTT) for non-emergency, non-cancer patients, with a large backlog of patients waiting over 18 weeks (including a significant number in excess of 52 weeks).

The completion of the implementation of the *BEH Clinical Strategy* on 9 December results in the annual loss of c£xxx income, leading to a forecast deficit for 2014/15 of £xxx pa (over xx per cent of turnover). This is in the context of a planned financial deficit for 2013/14 of £xxx on a turnover of £310m (four months of activity loss).

Alongside the activity and clinical challenges Barnet and Chase Farm requires significant investment in a number of areas to become clinically sustainable and financially viable:

- major investment in its estate, principally at Chase Farm Hospital; to provide both an economically efficient operating model and an environment patients deserve
- new investment in its patient administration, financial and HR systems and processes to make them fit for purpose and contribute to the efficient operating of the site
- a rapid overhaul of its management infrastructure; and
- a cultural shift involving real engagement of senior clinical staff in decision making.

Proposed transactions often result in differing views within a local health system as to whether they are necessary or appropriate; a transaction is often (and rightly) regarded as a strategy of last resort. Unusually in this case, all parties (including all the Trust's main commissioners) are in agreement that the proposed transaction is a necessary step if services are to be provided on a sustainable basis. Finding any form of viable alternative has proved to be very difficult. Only one organisation (the Royal Free) has put itself forward seriously to take on the challenge.

2.3 The Royal Free London NHS Foundation Trust

The Royal Free comprises a major acute hospital (630 beds) located in Hampstead in north London and a network of services provided from other sites across north London and Hertfordshire. The Royal Free has been a successful Foundation Trust since April 2012. Its Standardised Hospital Mortality Index (SHMI) - a key indicator of quality outcomes - is one of the best in England[1]. The Royal Free currently achieves a Continuity of Service Risk Rating (CSRR) of 4 based on a turnover of approximately £580m (2012/13).

The Royal Free is a teaching organisation hosting a major campus of University College London (UCL) Medical School. The Royal Free is a founder member of the UCL Partners academic health science network, collaborating with UCL, Queen Mary's and four other NHS Trusts in north and east London.

The Royal Free's Integrated Business Plan (IBP) for the acquisition of BCF sets out a transformation agenda, positioning the Royal Free at the centre of a managed care network. This will involve the Royal Free reaching agreements with its commissioners to, for example, invest heavily in a programme of service redesign with its clinical commissioning groups (CCGs); implement GP referral protocols, reducing demand on hospital-based care; manage a range of community hospital services complementary to its referral base; invest in the redevelopment of Chase Farm Hospital site as a high quality outpatient and elective hospital with an urgent care centre; maximise the use of Edgware Community Hospital.

3. The Vendor process

The TDA set up a governance process in line with the principles laid out in the Accountability Framework including:

- a Transaction Board, meeting fortnightly, chaired by The London Delivery and Development Director, involving all key stakeholders;
- three workstreams – a Finance Group, Transactions Group and Clinical Quality Oversight Group – reporting to the Transaction Board;
- Deloitte (Finance) and Hempsons (legal) appointed as advisors; and
- a programme plan agreed with the Royal Free,

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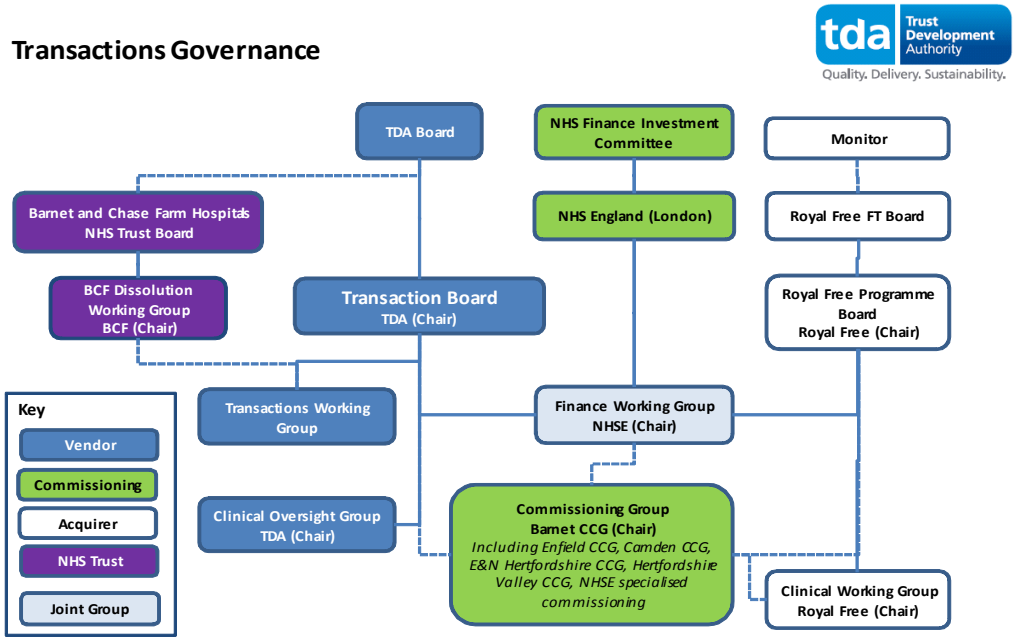
[1] Dr Foster, Hospital Guide, November 2012

A schedule of the governance arrangements is shown below:

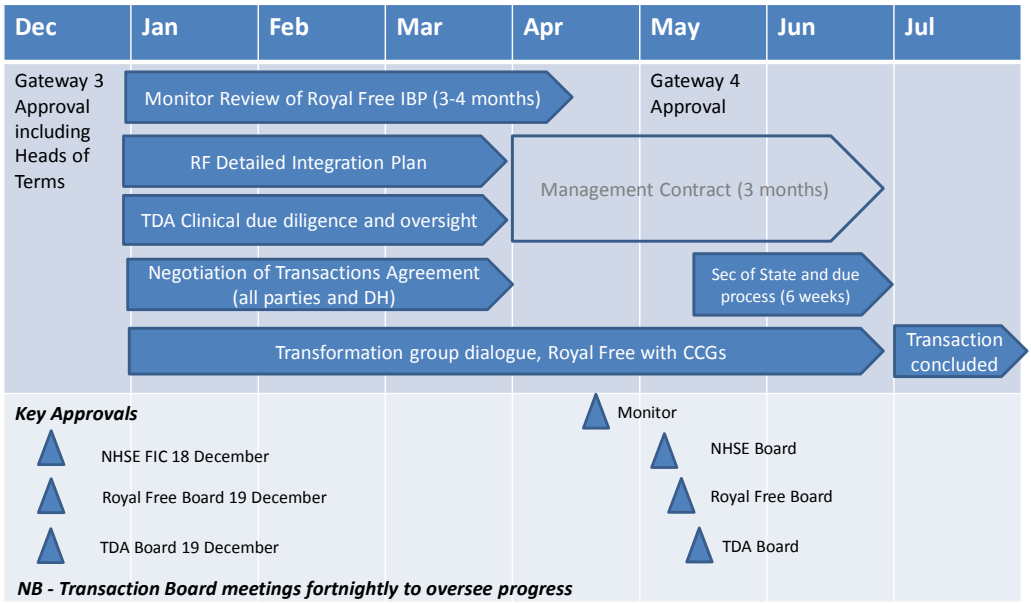
Transactions Governance



Note
The Transaction Board aligns programme governance to the TDA's published Accountability Framework. The diagram illustrates the governance arrangements between stakeholder organisations , however this does not in any way reduce the independent statutory authority of stakeholder boards.

Key milestones and outline timetable for the programme are shown in the diagram below

BCF Acquisition, Overview of Key Milestones



4. Clinical Quality Due Diligence

The TDA's Accountability Framework outlines the approach to discharging responsibilities to provide assurance of the clinical quality due diligence processes that have been undertaken, in order to advise and provide assurance to the TDA Board, as 'vendor', that there is no reason on the grounds of risk to quality to prevent the transaction going ahead. The clinical quality assurance of 'sender' and 'receiver' includes:

- Quality Assurance of 'receiver' and 'sender - The identification of significant risks to clinical quality in both parties. This includes: Monitor Governance Risk Rating for NHS Foundation Trust, CQC briefings of compliance, CQC Intelligent Monitoring Reports, analysis of quality indicator information from the TDA Business Intelligence Unit, and outputs from the TDA's ongoing oversight meetings with BCF.
- Quality Assurance of the Quality Due Diligence process undertaken by the 'receiver' organisation - This has included a review of the draft Clinical Due Diligence undertaken by the Royal Free and review of the Royal Free's draft IBP.
- Quality Assurance of the Transition and Handover Process, which will be undertaken between gateway 3 and gateway 4 - This is a significant programme of work in the period up to handover.

5. Financial assessment

The Heads of Terms, to be signed by the TDA, the Royal Free, BCF and NHS England, includes some key terms around the financial support for the transaction:

- xxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxx xxxxxxxxxxxxxxxx

- xxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxx xxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxx xxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxx xxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxx xxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxx

- xxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxx xxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxx

As part of its IBP, the Royal Free has submitted a Monitor-compliant Long Term Financial Model (LTFM), setting out a detailed financial plan for the next 5 years. This has been subject to relevant due diligence and challenge.

Table 1 – Summary of financial support

	TABLE REDACTED		

6. Value for Money

To establish whether the proposed merger transaction demonstrates Value for Money a Do Minimum comparator has been constructed (a Do Nothing option would not allow for a clinically viable organisation).

A description of the Do Minimum comparator (including methodology, assumptions and sensitivity testing) is contained in Appendix 2

The outcome of the value for money modelling is summarised in the table below:

Table 2 – Value for money assessment

Option	**Net Present Cost (£m)**	**Equivalent Annual Cost (£m)**	**Rank**
Do Minimum	XXXX	XXXX	2
Transaction	XXXX	XXXX	1

Note: the VFM assessment takes no account of any non-financial benefits of the transaction over Do Minimum

Sensitivity tests were undertaken on key assumptions and this showed that the outcome is not sensitive to plausible changes in the main assumptions driving the conclusion. Therefore we should have a high degree of confidence that the value for money test for proceeding with the transaction, against the (simplified) Do Minimum benchmark is robust.

Appendix 1 – Chronology

Milestone	Date	Methodology	Outcomes
NHS London-led Feasibility Study into the viability of BCF as an FT and the future of Chase Farm Hospital	December 2011	Option appraisal work, looking at feasibility of Chase Farm Hospital transferring to North Middlesex University Hospital NHS Trust (NMUH) and options for BCF as a trust going forward	Letter to the Secretary of State - no real advantage to separating Chase Farm from BCF Trust. An indication that BCF had no long term future as a standalone trust / FT
NHS London-led Viability Study covering BCF and NMUH trusts ["TDA Gateway 1"]	May 2012	More extensive options appraisal work into the future of BCF as a potential FT, modelling a range of alternative organisational configurations that might generate a more sustainable long-term solution	BCF clearly not sustainable or viable as a future FT. NMUH probably would be viable as a FT. Royal Free likely to offer the best merger / acquisition solution.
BCF Board considers conclusions of the Viability Study ["TDA Gateway 2"]	June 2012	Further financial analysis by Deloitte at request of the Trust CEO	Decision by the BCF Board to "seek a partner" in order to become a sustainable organisation. Trust issues an open invitation to partner with 46 NHS organisations within 25 km of its sites.
Recommendation of the BCF Programme Board to work with the Royal Free as "Preferred Partner"	September 2012	A competitive, 2-stage procurement. University College London Hospitals NHS FT and Barnet Enfield and Haringey Mental health NHS Trust initially indicated interest, but withdrew before submitting a Final Offer. Royal Free determined to be "above the line" by the BCF-led Programme Board panel	Decision to work with the Royal Free in producing a Strategic Case for acquisition.
Decision by NHS	November	Detailed review of the	A letter from NHS

London to support the acquisition of BCF with the Royal Free as Preferred Partner	2012	Strategic Outline Case submitted by the Royal Free, including an LTFM, outline programme and identification of potential synergies.	London confirming the decision, anticipating an Outline Business Case from the Royal Free in February 2013 and a completed transaction January 2014.
TDA Gateway 3	November 2013	Joint development by the TDA of a Heads of Agreement, Business Case and LTFM with the Royal Free	28 November TDA Board. Recommendation to BCF Trust to consult on its dissolution.
TDA Gateway 4	March 2014 (tbc)	Assurance report on the Final Business Case and Transactions Agreement	[Special March Board meeting leading to recommendation to Secretary of State]

Appendix 2 – Do Minimum methodology

1. Methodology

The Do Minimum comparator has been constructed in a simple and straightforward way; if the test provided evidence that the value for money difference is relatively small between the two option then the comparator would need to be reworked in more detail to provide greater accuracy. If however, the value for money gap is significant e.g. not switched by any of the sensitivity scenarios – then we can confidently assume that the approximation is sufficiently accurate for the purposes of establishing a clear decision between the options.

The value for money calculations have been modelled over a 30 year period and at a discount rate of 3.5% in accordance with the Treasury Green Book. Real cashflows have been modelled, based on nominal cashflows deflated for an assumed general inflation rate of 2.5%. This methodology has been applied to both the Do Minimum option and the Transaction Option to generate a NPC on a genuine like for like basis.

2. Do Minimum Assumptions

This option assumes that the transaction does not go ahead, and the Barnet and Chase Farm sites do not have significant investment in them.

The ongoing Trust deficit has been used as a proxy for the cost to the tax payer of the Do Minimum option under consideration, and is the starting point for the comparison. Under a scenario where a Trust continues to operate at a loss, without prospect of improving sufficiently to enable it to ever reverse that situation, the taxpayer would, in theory, have to contribute additional cash to fund that gap.

Clinical Services: It is assumed that the "post-BEH" configuration of services (i.e. current services) will be maintained, at existing levels and split, as now, between the two main hospital sites. As it is likely that over the next 5 years commissioners will want to change this in some way, the Do Minimum does not pre-empt any such future decision-making.

Similarly it is assumed that current quality standards will be maintained, not improved or degraded. It is assumed that levels of performance can be delivered to national standards.

Capital Costs: The capital cost of this scenario assumes that the Chase Farm site can be run on the current infrastructure, with minimal capital being expended to maintain that infrastructure, and make necessary improvements to maintain minimum acceptable clinical standards.

Investment agreed as part of the BEH strategy goes ahead as planned. The backlog has two elements – the Cyril Sweett survey backlog plus additional backlog as identified by BCF.

Land sales as set out in the BEH strategy also proceed as planned.

Ongoing Deficit Support: The deficit support modelled is based on the deficit forecasted by BCF for the five years until financial year 2018/19, with the final deficit amount extrapolated over the remaining 25 year period.

The adjusted nominal recurrent forecast deficit for 2014/15 (based on BCF revisions to initial forecast) is £xxxxx.

The deficit forecast has been based on the Monitor assumptions of 2.1% inflation, 1.9% income deflator, 4% recurring CIPs and a £1m recurring QUIPP per annum.

Management: The Trust currently operates with a high level of interim management and a Do Minimum option would assume consolidation of posts into a substantive structure. BCF would continue to be governed by an independent NHS Board. The reduction in cost due to this consolidation has been assumed to be incorporated in the delivery of the CIP programme.

Transitional Funding: Transitional funding has been agreed as part of the implementation of the BEH strategy. It has been assumed that this will be received as set out in the approved FBC.

NHSE Call to action: There is an adjustment to income from financial year 2015/16 for the effect of NHSE's Call to Action initiative on the provision of secondary care. NHSE has estimated this as £xxx over the combined RF and BCF entities. This has been reduced by 50% to take account of associated marginal cost reductions. Of the rebated total it has been assumed that the BCF proportion of the total is 45%.

Transaction Support Funding: Under this scenario, there is no additional support funding requirement.

3. Transaction Option – New Hospital at Chase Farm

This assumes that the transaction takes place, and that the Chase Farm site has a new build hospital as part of the overall rationalisation and restructuring required to address inefficiencies.
The capital expenditure falls in years 3 and 4 of the evaluation timescale and the benefits start to take effect in year 5. This is however only a part-year effect, and as a consequence the combined organisation retains a deficit at the end of year 5. However, the trajectory is towards breakeven and the assumption is that there is no ongoing deficit beyond the evaluation horizon.

Capital Costs: The capital cost of this scenario assumes that a new build of £xxxm on the Chase Farm site.

£m	Barnet	Chase Farm	Total
Capital			
Disposals		REDACTED	
Net Total			

Ongoing Deficit Support: None.

Transitional Funding: Transitional funding has been agreed as part of the implementation of the BEH strategy. This funding has been modelled through the combined organisation LTFM and is therefore included in the Additional Funding Support.

NHSE Call to action: There is an adjustment to income from financial year 2015/16 for the effect of NHSE's Call to Action initiative on the provision of secondary care. NHSE has estimated this as £xxx over the combined RF and BCF entities. This has been reduced by 50% to take account of associated marginal cost reductions. Of the rebated total it has been assumed that the BCF proportion of the total is 45%.

Additional Support Funding: This is based on the funding request extracted from the combined organisation LTFM and covers the following areas:

- Deficit support
- CSRR support
- Integration costs
- Capital (net of depreciation)
- Liquidity

The total support modelled is £xxx.

4. VFM comparison

The outcome of the value for money modelling is summarised in the table below:

Option	Net Present Cost (£m)	Equivalent Annual Cost (£m)	Rank
Do Minimum	REDACTED		2
Transaction			1

The summary table shows that the Transaction has the lower Net Present Cost and therefore offers the best value for money solution. The Transaction eliminates the ongoing deficit at Barnet & Chase Farm, which the Do Minimum option fails to do. This is a large contribution to the lower Net Present Cost benefit of the preferred option.

Also note that this analysis does not include any non-financial benefits that may arise from the transaction e.g. through better leadership, governance, clinical engagement.

5. Sensitivity Testing

In order to test the sensitivity of the value for money decision to the key assumptions within the model we have flexed these assumed values to determine at what point the VfM decision changes i.e. the switching point.

Sensitivity Test 1 – Reduced deficit at BCF under the Do Minimum Option
The deficit in every year was reduced to a constant real amount such that the switching point was achieved. The deficit was £xxx per annum for every year of the evaluation period. Given that the best current estimate by the Trust is for a deficit of £xxx, with a predicted increase year on year, this reduction of 48% seems unlikely.

Sensitivity Test 2 – Reduced capital funding under the Do Minimum Option
Reducing the capital requirement under the Do Minimum option to zero does not cause the outcome of the appraisal to change – the Transaction remains the preferred option.

Sensitivity Test 3 – Increased support funding under Transaction
In order for the Do Minimum Option to become better value for money than the Transaction, the total support funding requested (currently £xxx) would have to increase by 175% (i.e. almost triple in value) to £xxx.

This demonstrates that the value for money gap between the two options is not likely to be sensitive to any changes in support funding.

These results show that the value for money decision is not sensitive to the assumptions made and we can have a degree of confidence that for the purpose of this exercise it is based on reliable modelling.