



Llywodraeth Cymru  
Welsh Government

# **NATIONAL HEALTH SERVICE FINANCE (WALES) BILL**

**Explanatory Memorandum**  
incorporating the Regulatory Impact  
Assessment and Explanatory Notes

September 2013

# **NATIONAL HEALTH SERVICE FINANCE (WALES) BILL**

## **Explanatory Memorandum to the National Health Service Finance (Wales) Bill**

This Explanatory Memorandum has been prepared by the Department for Health and Social Services of the Welsh Government and is laid before the National Assembly for Wales.

### **Member's Declaration**

In my view the provisions of the National Health Service Finance (Wales) Bill introduced by me on 30 September 2013, would be within the legislative competence of the National Assembly for Wales.

### **Mark Drakeford AM**

Minister for Health and Social Services  
Assembly Member in charge of the Bill

30 September 2013

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## 1. Description

1. The National Health Service Finance (Wales) Bill gives effect to the Welsh Government's proposals in 'Together for Health' to introduce a more flexible finance regime. It provides a new legal financial duty for Local Health Boards to break even over a rolling 3 financial years rather than each and every year. The Bill creates a duty for Local Health Boards to adopt a financial regime to flexibly manage resources, expenditure and approved limits over a rolling 3 year period. This will enable Local Health Boards to focus their service planning, workforce and financial decisions and implementation over a longer, more manageable, period. The intention of the Bill is to allow for better decision making and implementation of optimal solutions in Local Health Boards and remove a significant challenge within the current regime which encourages short term decision making around the financial year.

## 2. Legislative background

2. The National Assembly for Wales has the legislative competence to make provisions in relation to organisation and funding of the National Health Service under Part 4 of the Government of Wales Act 2006 (GOWA 2006). The relevant provisions of GOWA 2006 are set out in section 108 and Schedule 7.

3. Paragraph 9 of Part 1 of Schedule 7 sets out the following subjects on which the Assembly may legislate under the heading of “*Health and Health Services*” and is reproduced below:

*Health and health services*

9 *Promotion of health. Prevention, treatment and alleviation of disease, illness, injury, disability and mental disorder. Control of disease. Family planning. Provision of health services, including medical, dental, ophthalmic, pharmaceutical and ancillary services and facilities. Clinical governance and standards of health care. Organisation and funding of national health service.*

*Exceptions—*

*Abortion.*

*Human genetics, human fertilisation, human embryology, surrogacy arrangements.*

*Xenotransplantation.*

*Regulation of health professionals (including persons dispensing hearing aids).*

*Poisons.*

*Misuse of and dealing in drugs.*

*Human medicines and medicinal products, including authorisations for use and regulation of prices.*

*Standards for, and testing of, biological substances (that is, substances the purity or potency of which cannot be adequately tested by chemical means).*

*Vaccine damage payments.*

*Welfare foods.*

4. None of the provisions of the National Health Service Finance (Wales) Bill fall within any of the exceptions specified in Part 1 of Schedule 7 to GOWA 2006 or applies otherwise in relation to Wales or confers, imposes, modifies, or removes (or

gives power to confer, impose, modify or remove) functions exercisable other than in relation to Wales; or breaches any of the restrictions in Part 2 of Schedule 7 having regard to any exception in Part 3 of that Schedule from those restrictions.

5. Legislative competence to make consequential amendments is provided by section 108(5) (b) of GOWA 2006.

### 3. Purpose and intended effect of the legislation

#### Background

##### Issues

6. The Welsh NHS faces significant service, demographic and financial challenges and given the overall position of public finance, is unlikely to receive material growth in funding over the next few years. The Welsh Government needs to work with the NHS to look at all of the options to identify how resources can be managed optimally. Financial flexibility, through the application of a financial duty over more than one financial year rather than each and every year, could help address the problem.

7. The Welsh Government published 'Together for Health' in 2011<sup>1</sup>. It sets out a clear and ambitious vision for achieving sustainable improvement in the health and wellbeing of the people of Wales and the sustainable transformation of health services to ensure their outcomes compare with the best in the world. 'Together for Health' marked the urgent need to transform the system of health care delivery and reframe the relationship with the people who use the health service. The current planning system has been characterised by the emphasis on annual plans which have focused on delivery of annual service and financial targets.

8. The practical application of the current statutory duties on Local Health Boards is that no flexibility exists at year end and that any overspend, no matter how small, would result in a breach of the Local Health Boards' Statutory Financial Duty. A breach in this duty would also result in the Wales Audit Office giving a qualified regularity opinion on the Local Health Board Accounts and could also potentially place at risk the qualification of the Welsh Government's Accounts.

9. The inflexibility of the current financial regime can distract efforts at year end by focussing on relatively small saving requirements to meet the year end target rather than on the medium term financial strategy and Integrated Plan to deliver the forthcoming financial years. It can also lead to distorted decision making on schemes that require upfront investment to achieve recurring savings, and some schemes can sometimes miss their 'window of opportunity' if not done very early in the financial year.

10. This Bill aims to address this by redefining the statutory financial duty from one year to a rolling three years to support Integrated Medium Term Plans, including Medium Term Financial Plans. The legislation will minimise the risk of short term decision making around the financial year, which may not be in the longer term interests of the organisation. The current financial regime encourages behaviours that are not conducive to securing good value for money.

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<sup>1</sup> <http://wales.gov.uk/topics/health/publications/health/reports/together/?lang=en>

## **Local Health Boards and Financial Planning**

11. Local Health Boards are defined (in accordance with the Office of National Statistics) as “Central Government” bodies for Resource Accounting and Budgeting purposes. They fall under the Welsh Government budgetary and accounting umbrella and they are governed by Annual Resource Limits.

12. Financial duties were placed on Local Health Boards under section 175 of the National Health Service (Wales) Act 2006 requiring that Local Health Boards ‘in respect of each financial year, perform its functions so as to secure that its expenditure which is attributable to the performance by it of its functions in that year (not including its general ophthalmic and pharmaceutical expenditure) does not exceed the aggregate of the amount allotted to it for that year’. A duty under section 176 of the National Health Service (Wales) Act 2006 also requires ‘that the use of its resources in a financial year does not exceed the amount specified for it in relation to that year by the Welsh Ministers’. The National Health Service (Wales) Act 2006 is a consolidation Act which replaced the earlier England and Wales legislation, the National Health Service Act 1977. In the National Health Service Act 1977 the financial duties were set out in section 97, sections 97F, 97G & 97H were inserted into section 97 by the National Health Service Reform and Health Care Professions Act 2002 and applied financial duties and Resource Limits to Local Health Boards in Wales.

13. The requirement for the Integrated Medium Term Plans is not a new requirement, it already exists within the Planning Framework 2013/14 to 2015/16 which was issued to NHS organisations on 8 February 2013 and Model Standing Orders<sup>2</sup> and Standing Financial Instructions issued in July 2012 included the requirement that:

“Local Health Boards will prepare a medium-term service and financial strategy. The medium term plans must reflect longer-term planning and delivery objectives and should be continually reviewed based on latest Welsh Government policy and local priority requirements”

## **England and Scotland**

14. In England, the National Health Service Act 2006 sets out the annual financial duties, similar to those in the National Health Service (Wales) Act 2006. HM Treasury's publication, ‘Improving Spending Control’<sup>3</sup> (April 2012) provides: ‘Good business planning is an essential part of managing spending. Each public sector organisation should plan to use the limited budget that it has to achieve good value for money and ensure that efficient and sustainable choices are made about how public funds are used’. This means keeping an eye on the medium and long term picture, re-assessing risks and evaluating alternative ways of achieving policy objectives’.

15. The Scottish Executive Health Department issued ‘Local Delivery Plan

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<sup>2</sup><http://www.nhswalesgovernance.com/display/Home.aspx?a=427&s=11&m=200&d=0&p=201>

<sup>3</sup><https://www.gov.uk/government/publications/improving-spending-control>

Guidance 2013/14' in 2012<sup>4</sup> that indicates a shift towards better integrated planning and an outcome based approach.

### **National Assembly Committee Recommendations**

16. The National Assembly for Wales Finance Committee<sup>5</sup>, Health and Social Care Committee<sup>6</sup> and the Public Accounts Committee<sup>7</sup> have recommended that the Welsh Government should consider legislative opportunities to support a more flexible planning framework for the NHS, including the management of their finances across financial years.

### **Wales Audit Office Recommendations**

17. The Wales Audit Office Health Finances report published July 2012<sup>8</sup> included the following recommendation:

“R6: The resource accounting regime of the NHS has a short-term focus on breaking even within each financial year. This potentially makes it difficult for NHS bodies to create funds to invest in transformation and change in order to deliver savings in future years. Within the current framework of resource accounting, the Welsh Government should assess the current requirement for health boards to break-even each and every year, and develop options that would enable NHS bodies to invest in new ways of working where these are likely to deliver savings in the future and enable them to break-even over a longer period.”

### **Current Arrangements**

#### **How resources are allocated to Local Health Boards at present**

18. Resources are primarily allocated to Local Health Boards through the issuing of Revenue Allocations (following the approval of the Annual Budget Motion by the National Assembly) which set the Revenue Resource Limits and Cash Limits. Local Health Boards will recognise the Revenue Resource Limit as the limit that expenditure cannot exceed and will, throughout the year, regularly draw down cash, against the Cash Limit, to meet those expenditure outgoings.

#### **Revenue Allocations**

19. The Welsh Government issues an annual revenue allocation document to Local Health Boards before the start of the financial year to which it relates. Normally this is done as soon after the National Assembly has passed the Annual Budget Motion (usually mid December).

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<sup>4</sup> <http://www.scotland.gov.uk/Publications/2012/12/8405>

<sup>5</sup> <http://www.senedd.assemblywales.org/mgIssueHistoryHome.aspx?Id=1366>

<sup>6</sup> <http://www.senedd.assemblywales.org/mgIssueHistoryHome.aspx?Id=2254>

<sup>7</sup> <http://www.senedd.assemblywales.org/mgIssueHistoryHome.aspx?Id=5801>

<sup>8</sup> [http://www.wao.gov.uk/assets/englishdocuments/NHS\\_Finances\\_167A2012\\_English\\_2.pdf](http://www.wao.gov.uk/assets/englishdocuments/NHS_Finances_167A2012_English_2.pdf)

20. The allocation letter is issued in accordance with section 174 of the National Health Service (Wales) Act 2006. The allocation letter describes the initial Resource Limit for each Local Health Board. It is usually issued under cover of a Ministerial letter to Local Health Board Chairs, with a more detailed covering letter, plus detailed schedules and notes, from the Chief Executive of NHS Wales to Local Health Board Chief Executives.

21. The basis of the Revenue Allocation for each Local Health Board is the recurrent element of the previous year's Revenue Allocation plus or minus any notified changes. Those notified changes could include additional withdrawal and transfer of resources.

22. Not all Welsh Government funding to the NHS in Wales is issued in the initial revenue allocation letter. There are a number of other funding streams that are added to the revenue allocation during the course of the financial year. In addition to the direct revenue allocations, NHS organisations also receive other funding streams for services which are directly invoiced to the Welsh Government.

23. Revenue Allocation to Local Health Boards consists of a Revenue Resource Limit and a Cash Limit. The Cash Limit is not a legal requirement but an administrative cap required by the Welsh Government to ensure compliance with its Ambit. The Resource Limit reflects the total amount "allotted" by the Welsh Government to the Local Health Board (to use section 174/175 of the National Health Service (Wales) Act 2006 terminology). As will be seen below, the Resource Limit is used as the basis of the main statutory duty for Local Health Boards. The Cash Limit reflects the total cash that Local Health Boards can draw down from the Welsh Government against their Resource Limit (section 174 1(b))

24. The main difference between resource and cash limits is usually funding for depreciation and other "non-cash" costs. These are costs incurred by the Local Health Boards and chargeable to their gross and net operating costs, for which they need sufficient resource limit cover, but they do not actually make any cash payments, so they do not require a cash limit cover.

25. Once the initial allocation has been issued to Local Health Boards, it is updated throughout the year (both resource and cash limits) for the issue of in-year funding. The final notified allocation forms the resource limit which is used within the measure to confirm the organisation has met its financial duty of "Achievement of Operational Financial Balance" as detailed in the Statement of Comprehensive Net Expenditure in the statutory Annual Accounts.

### **Capital Allocations**

26. Unlike the revenue allocations, the capital allocations to Local Health Boards and Trusts are not issued through a formal document. Capital allocations will normally consist of:

A discretionary allocation to enable Local Health Boards and Trusts to undertake minor works and equipment replacement; and

An allocation from the All-Wales Capital Programme for approved major capital schemes.

27. Capital allocations will be varied throughout the financial year, and between financial years, to reflect progress against major capital schemes. Allocations are formally notified individually to organisations through the issue of a Capital Resource Limit, which is likely to be amended and re-issued throughout the year as capital allocations are varied in line with progress and updated profiles of major capital schemes. The provisions of sections 175 and 176 apply to both Revenue and Capital Allocations.

### **Purpose of Legislation**

28. The overarching aim of the legislation is to improve the health outcomes of the Welsh population (in the short, medium and long term) by targeting NHS funding towards those services and interventions that provide the best value for money.

29. The purpose of this Bill is to make provision in relation to the financial duties of Local Health Boards in Wales. The Bill provides for each Local Health Board in Wales to secure that its expenditure does not exceed its funding over a period of three years instead of applying to each financial year.

30. Flexibility within a rolling three years period will allow Local Health Boards to focus their service planning, workforce and financial decisions over a longer period and is expected to result in better decision making and optimal solutions by Local Health Boards. It will also remove a significant challenge within the current regime which encourages short term decision making around the financial year end, which may not be in the longer term interests of the organisation. This needs to be supported by a mature and responsive financial framework, function and service that underpins sustainable service transformation.

31. The key change to the existing legislative framework is set out in Section 2 of the Bill. Under this section the financial duties set out in section 175 of the National Health Service (Wales) Act 2006 will be replaced with a duty which requires each Local Health Boards to ensure, in a rolling 3 year period, that its aggregate expenditure does not exceed its aggregate approved limits.. This key financial duty is measured, reported and audited through the Local Health Board's Annual Accounts in the Statement of Net Comprehensive Expenditure and Financial Duty Disclosure Note.

32. Section 176 'Resource Limits for Local Health Boards' is being repealed as it is no longer required. Section 176 introduced the term 'Resource Limits' as part of the Government Resources and Accounts Act 2000. Up to that point, financial transactions within Government departments and the NHS were captured and recorded on a 'cash' basis and following the introduction of 'resource' accounting within the public sector it was necessary to make a distinction between cash based reporting and accruals (resource) based reporting.

33. This distinction is no longer necessary as all 'expenditure' is now recorded and reported on an accruals basis as required under the Government's Financial Reporting Manual. Consequently the provisions within Section 175 which refer to 'expenditure' cover the requirements that were previously contained within Section 176, which referred to 'Resources'.

### **Changes to current arrangements for the financial year end and risks to the Department for Health and Social Services Budget**

34. The change in the Local Health Boards financial duty from an annual duty to a rolling 3 year duty is around the timing, not the totality, of the resource requirements needed to match expenditure over the three years. Regardless of the change to the Local Health Boards financial duty, the Department for Health and Social Services still needs to manage the consolidated NHS Wales and the Department for Health and Social Services resources within its annual Main Expenditure Group budget allocation provided for through the Annual Budget Motion. There has to be sufficient resources available within the Department for Health and Social Service Main Expenditure Group each year to cover all planned expenditure which will include Local Health Board expenditure and Resource Limits, including cover for any flexibility as a consequence of the Bill. It should be noted that this financial flexibility cannot be completely open ended and will need to be managed within this constraint. The resource available within the Department for Health and Social Service budget will be a key limiting factor in the scope of financial flexibility over a rolling 3 year period.

35. The Welsh Government has two major spending controls i.e. Treasury Total Managed Expenditure Limits and the legal budget motion ambit controls voted each and every year by the National Assembly for Wales. The resources allocated to the Department for Health and Social Services (and then to Local Health Boards) or any other Ministerial portfolio, have to be managed within these two control regimes.

36. If a Local Health Board spends or is planning to spend above its resource limits in any one year then there has to be sufficient resources within the annual Welsh Total Managed Expenditure Limits (including the individual resource limit controls) and the resources voted via the Assembly Budget Motion. The legislation could potentially add to the risk that the Welsh Government would breach the Treasury limits and/or legal budget which would have serious consequences for the Welsh Government and the National Assembly for Wales. For example, there would be consequences if Local Health Boards planned or incurred overspends in any one year against their Resource Limits and this could not be offset (by the Department for Health and Social Services in the first instance and then by the Welsh Government as a whole).

37. If the overspend could not be kept within the overall resource limits allocated to the Welsh Government by HM Treasury or voted through the Budget Motion then the Welsh Government accounts would be qualified and any spend would be irregular and need to be regularised through the following:

In terms of an overall budget motion breach this would have to be regularised through a vote procedure by the National Assembly for Wales.

If the HM Treasury limits were about to be breached in any one year then the Welsh Government could apply in advance for contingency funding from the UK Consolidated Fund.

If there was no additional resource provided from the UK Contingency Fund and a breach of allocated Treasury limits occurred then under budgeting guidance the breach would have to be notified to the Chief Secretary to the Treasury (by the First Minister/Minister for Finance); the circumstances of the breach would need to be described and the measures to address this going forward would need to be outlined. Any overspend would probably be recovered by the Treasury from the Welsh Block in the following year.

38. Failure by the Welsh Government to keep within resources each year will also have significant cash implications. Under Resource Budgeting and Accounting, cash generally follows approved resource when it is needed. A significant overspend without approved resource cover would mean that the Welsh Government will not be able to draw down sufficient cash (under Treasury cash limit controls) into the Welsh Consolidated Fund to meet the excess expenditure. This would mean that Welsh public bodies, including the NHS, would not have sufficient cash resources to pay its bills or payroll costs.

#### **Sanctions: financial, legal or other implications of non-compliance**

39. The legislative change to move to a rolling three year financial duty regime will be backed by a requirement, through changes to Directions and Standing Orders and Standing Financial Instructions for Local Health Boards to develop balanced 3 year Integrated Medium Term Service Plans, including balanced Medium Term Financial Plans and have them approved by their Board prior to the beginning of each financial year. The plan would also have to be subsequently approved by the Welsh Government. This requirement would replace the existing narrower requirement for Board approval of annual Local Delivery Plans, including approval of annual balanced Financial Plans prior to the beginning of each financial year. The high level planning process is described further in **Annex 2**.

40. Under the new planning arrangements there would be a requirement for annual scrutiny and approval of the plans by the Welsh Government's officials to ensure planning is robust and in accordance with policy objectives. As the Department for Health and Social Services will still operate within annual expenditure limits and must manage within the totality of the budget allocated to the Department for Health and Social Services Main Expenditure Group, any flexibility provided and approved for Local Health Boards would need to be managed and approved within these limits. Accordingly this reinforces the requirement for the formal process to review and approve balanced Integrated Medium Term Plans within the Welsh Government.

41. Powers of direction are set out in section 175 (2) and (6) of the NHS (Wales) Act 2006 and these remain unchanged by this Bill.

## **Existing Formal Intervention Powers – National Health Service (Wales) Act 2006**

42. Intervention powers are available to the Welsh Government through the sections 26-28. These powers can be utilised if a Local Health Board is considered to be failing to perform one or more of its functions and can, in certain circumstances, be applied to suspend or remove powers and functions.

### **Accountable Officer Appointment Letter and Memorandum**

43. The Accountable Officer Memorandum, which each Chief Executive receives on appointment together with a letter from the Chief Executive, NHS Wales, defines the responsibility of the Accountable Officer in each NHS organisation for financial management/performance.

44. The Memorandum clearly states that the Accountable Officer of each NHS organisation is directly accountable, for all financial performance issues (and all other performance issues) delegated to the organisation, to the Chief Executive, NHS Wales as Sub Accounting officer for Health and Social Care at the Welsh Government.

45. The Accountable Officer's powers can be removed by the Chief Executive, NHS Wales where the Accountable Officer is not performing the delegated responsibilities.

### **The Delivery Framework Escalation Levels**

46. The Delivery Framework sets out a clear framework for support, escalation and intervention:

Escalation Level	Escalation Action
1.	Local Health Boards/Trusts are responsible for remedial action in response to areas of failure. Welsh Government indicates the additional monitoring requirements. Plans brought forward to redress the position with immediate effect.
2.	Welsh Government instigates Delivery and Support Unit and/or other intervention. Welsh Government and Delivery Support Unit (or other intervention mechanism identified by the Welsh Government) will be actively involved in determining the necessary changes within the Local Health Board/Trust to deliver required outcomes through regular meetings/calls.
3	Issues raised with the Chief Executive of NHS Wales. Meeting required between Local Health Board Chief Executive, NHS Chief Executive Officer and/or NHS Deputy Chief Executive to determine future requirements and actions.
4.	Actions to be determined by NHS Chief Executive which may include the following: Meeting required with Chair, Vice Chair, Chief Executive Officer, Board Secretary and relevant Executives. Introduction of 'special measure' arrangements. Review of executive effectiveness. Review of Board effectiveness. Removal of appropriate funding streams.

Note: **Annex 2** describes the practical application of the delivery framework.

47. To underpin the legislation, the Welsh Health Circular (2007) 049 "Statutory Financial Duty of NHS Trusts and Local Health Boards" will be replaced with a Ministerial Direction setting out the new requirements and escalation levels. These escalation and intervention levels will be in line with that set out in the Delivery Framework.

### **How the Local Health Boards, Wales Audit Office and NHS Trusts are affected**

48. Local Health Boards are directly affected by the legislation as the Bill places a duty on them to break even over a rolling 3 financial years rather than each and every year. The legislation will also impact on the Wales Audit Office who will continue to be required to audit Local Health Board annual accounts and to annually produce a Certificate and Report for each Local Health Board as a result of the duty.

49. NHS Trusts will not be affected as they are covered by Schedule 4 of the NHS (Wales) 2006 Act. The position for NHS Trusts in Wales is different in that they do not operate to a Resource Accounting Regime, and for NHS Trusts the requirement, as set out in Welsh Health Circular (2007) 049, is that 'NHS Trusts should achieve a breakeven position in each and every financial year. Breakeven

should be achieved without the requirement for any additional cash loans or financial support from the Welsh Assembly Government.'

50. This was qualified by the Welsh Ministers by the introduction of a materiality level of the lesser of £0.5m or 0.5% of an NHS Trust's operating income for the year. A Trust is expected to absorb any overspend that is within its materiality limit, within its Income and Expenditure Reserve, or if that is not possible, it must be recovered in the following financial year.

51. The National Health Service (Wales) Act 2006 also provides financial duties for Special Health Authorities. There are currently no Wales only Special Health Authorities, but there are joint England and Wales Special Health Authorities to which the National Health Service Act 2006 applies.

### **Implementation and delivery plan**

52. As part of taking forward 'Together for Health', the Welsh Government has set out a Finance Regime which includes a framework to move from the constraints and limitations of the current annual financial planning cycle to a Medium Term Financial Plans within an Integrated Medium Term Planning framework. Financial flexibility that aligns resources with balanced 3 year plans is a key part of this process and the aim of this Bill is to remove the current legislative constraint on the annual financial duty and replace with an appropriate legislative framework that supports this overall goal of financial flexibility to support sustainable medium term plans.

53. The importance of a strong planning system in NHS Wales is widely accepted and planning requirements have been set out for Local Health Boards and Trusts. The requirements have included the production of a Board agreed Medium Term Plan in March 2013, which articulates how resources (financial, workforce and estate) will be deployed to yield maximum efficiency in order to:

- address areas of local population health need;
- improve quality of care; and
- deliver national priorities.

54. Recent reports by the Public Accounts Committee and Wales Audit Office, both on the maturity of Local Health Boards and more recently on NHS Finances, have pointed to the need to improve the planning system in Wales. Two issues emerge from all assessments:

- the need to strengthen the planning and scrutiny arrangements within Local Health Boards and Trusts;
- and the need, particularly when Local Health Board and Trust arrangements are being strengthened, to ensure that there is adequate national scrutiny, challenge and support.

### **Timescale**

55. It is anticipated that the Bill will gain Royal Assent in January 2014. The Bill will come into force from 1<sup>st</sup> April 2014.

56. The Integrated Planning framework that underpins the change in legislation to a 3 year financial duty and revisions to Standing Orders and Standing Financial Instructions as set out in Annex 3 will need to be in place by the time the new legislation comes into force. The timetable of this planning work will be as follows:

<b>Action</b>	<b>Date</b>
Integrated Planning Framework developed between Welsh Government and NHS	June - September 2013
Integrated Planning Framework signed off	end of September 2013
Integrated Planning Framework issued to NHS	October 2013
NHS organisations develop 2014/15 Integrated Medium Term Plans in accordance with Integrated Planning Framework	October – December 2013
NHS Organisations' Boards sign off plans	January 2014
NHS organisations submit plans to Welsh Government	January 2014
Welsh Government scrutiny process	February - March 2014
Welsh Government approval	Prior to 31 <sup>st</sup> March 2014

### **Transitional Arrangements**

57. For the first two years that the Bill will take effect i.e. 2014-15 and 2015-16, there will not be a formal 'statutory financial duty' test. Consequently the Wales Audit Office will not be required to provide an audit opinion on this, however from 2016-17 onwards the test will apply and consequently be audited. However, the Welsh Government will be agreeing annual resource limits with each Local Health Board. As there will be no actual statutory financial duty test in these years, failure to maintain their costs within the limits that the Welsh Government set will not result in a 'regularity' audit qualification but would result in a substantive narrative report by the Wales Audit Office and possible Public Accounts Committee attendance and any relevant escalation procedures as deemed appropriate under the circumstances.

### **Territorial extent**

58. The Bill applies in relation to Wales.

## 4. Consultation

### **Consultation on proposals for a financial duty over 3 financial years with NHS Organisations**

59. Whilst there hasn't been any formal consultation on the legislative proposal, the issue of the annual statutory duty on Local Health Boards has been the subject of discussion within the NHS and wider stakeholder network. Specifically, a joint Welsh Government and NHS Group was established in 2012 to look at financial flexibility which reported to the NHS Directors of Finance in December 2012. Recommendations of the Group included Financial Flexibility to support Integrated Medium Term Plans, review of legislation to provide additional flexibility whilst ensuring that strong governance and discipline, and brokerage mechanism for NHS bodies to support each other.

60. Work on wider changes to the NHS Finance Regime as referred to in the strategic document 'Together for Health' which included Integrated Medium Term Plans, including Integrated Plans, Financial Flexibility, Resource Allocation, Financial and Delivery Information and Integrated Assurance and Governance, has been presented to, and been supported by, the NHS Chief Executives, Directors of Finance and Directors of Planning Groups. The Financial Flexibility theme included recommendation on seeking changes to the legislative framework for Local Health Board finance.

### **Engagement with Local Health Boards and the Wales Audit Office**

61. Local Health Boards and the Wales Audit Office were consulted to determine the costs and benefits of the legislation. The Wales Audit Office responded to the consultation, along with all 7 of the Local Health Boards.

62. Options on the legislation have been discussed in detail with the Wales Audit Office. The 3 year rolling duty is a retrospective measure and the mechanism and implications for the audit of Annual Accounts has been fully explored and discussed with Wales Audit Office staff.

## **5. Power to make subordinate legislation**

63. The Bill does not contain provisions to make subordinate legislation.

## **6. Regulatory Impact Assessment (RIA)**

64. A Regulatory Impact Assessment has been completed in accordance with Standing Order 26.6 for Bill and it follows at Part 2.

## PART 2 – REGULATORY IMPACT ASSESSMENT

### 7. Options

65. This Regulatory Impact Assessment presents two different options in relation to the policy objectives of the Bill. Each of the options are analysed in terms of how far they would achieve the Welsh Government's objectives, along with the risks, the costs and benefits associated with each option are set out in Chapter 8. All figures have been rounded to the nearest hundred pounds and some of the totals may not sum due to this rounding.

66. The options are whether or not to have a change in the financial duty on Local Health Boards:

**Option 1** – do nothing and use the current legislation providing an annual financial duty, with annual expenditure not to exceed annual resource limit in place, and continue with the issue of directions for integrated medium term planning and medium term financial planning.

**Option 2** – introduce legislation replacing the annual financial duty with a rolling three year financial duty, and continue with the issue of directions for integrated medium term planning and medium term financial planning.

**Option 1 – do nothing and use the current legislation providing an annual financial duty, with annual expenditure not to exceed annual resource limit, and continue with the issue of directions for integrated medium term planning and medium term financial planning.**

67. This option will result in:

The current regime providing the financial duty as an annual duty for annual expenditure not to exceed annual resource limit.

External audit to provide regularity opinion around the annual financial duty – was this duty met or not met (not met - where expenditure exceeded resource limit).

The issue of Local Health Board Standing Orders and Standing Financial Instructions requiring Boards to approve Integrated Medium Term Plans and balanced Medium Term Financial Plans.

The issue of Integrated Planning Framework to include integrated medium term planning and medium term financial planning, and including requirements, guidance, schedules and timetable.

68. Under this option the legislation and audit all focus on the annual requirements, i.e. the short term, not the medium/long term whereas directions, Standing Orders and Standing Financial Instructions focus on the Medium Term plans. This gives a mixed message to organisations, where Medium Term Plans are required by the Welsh Government, but annual financial duty still applies.

69. Local Health Boards in Wales would continue to comply with the current financial duties set out in section 175 of the National Health Service (Wales) Act

2006 which require that, in respect of each financial year, it performs its functions so as to secure that its expenditure, which is attributable to the performance by it of its functions in that year, does not exceed the amount allotted to it for that year. Section 176 of the National Health Service (Wales) Act 2006 also requires that the use of each Local Health Board's resources in a financial year does not exceed the amount specified for it in relation to that year by the Welsh Ministers. This option would include the approach being used in Option 2, for the preparation of Medium Term Financial Plans as part of Local Health Boards Integrated Medium Plans.

70. Option 1 has been discounted because of the mis-alignment of requirements, between the Annual Financial Duty and Medium Term Financial Plan. This option does not offer the financial flexibility from a duty to undertake a 3 year rolling regime and as a consequence would deliver mixed messages to Local Health Boards on their obligations and duties.

71. As options are assessed against the policy goal of financial flexibility to support Integrated Medium Term Plans and Medium Term Financial Plans, the do nothing option is not supported because the current duty continues to place a legislative constraint on Local Health Boards and encourages short term decision making around the financial year, which may not be in the longer term interests of the organisation.

72. The key disadvantages of this option are that:

The legislation and requirements are not aligned, providing inconsistency and confusion for Local Health Boards.

It does not provide the full financial flexibility of implementing both planning requirement change and financial duty change.

It does not strengthen the approach to deliver on the commitments in Together for Health by not supporting the wider approach to the integrated planning process currently being introduced by the Welsh Government.

**Option 2 – introduce legislation replacing the annual financial duty with a rolling three year financial duty, and continue with the issue of directions for integrated medium term planning and medium term financial planning**

73. In summary this option will result in:

Creating a rolling three year financial duty.

External audit providing their regularity opinion around the rolling 3 year financial duty – was this duty met or not met (not met - where aggregate expenditure exceeded aggregate resource limit for the 3 years).

The issue of Local Health Board Standing Orders and Standing Financial Instructions, requiring Boards to approve Integrated Medium Term Plans and balanced Medium Term Financial Plans.

The issue of Integrated Planning Framework to include integrated medium term planning and medium term financial planning, and including requirements, guidance, schedules and timetable.

74. The aim of the Bill is to change the current financial duties of Local Health Boards under sections 175 and 176 of the National Health Service (Wales) Act 2006 to be replaced with a duty which requires each Local Health Board to ensure, in a rolling 3 year period, that its aggregated expenditure does not exceed its aggregated final notified limit in the annual accounts.

**Table 1. Example of 3 Year Rolling Financial Duty**

	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20
<b>Financial Duty Assessment</b>						
3 Year Rolling			X			
				X		
					X	
						X

75. Under the rolling 3 year duty, the first assessment will take place at the end of 2016/17. Illustration of how the new duty will operate:

**Table 2. Local Health Board performance for the 3 year accounting period ending 31 March 2017**

	2014/15	2015/16	2016/17	Aggregate
Net operating costs	X1	X2	X3	X1+x2+x3
Revenue Expenditure Limit	Y1	Y2	Y3	Y1+Y2+Y3
Under/(over) spend against Revenue Expenditure Limit				=(Y1+Y2+Y3) -(X1+X2+X3)

Note: Similar procedure applies to assessment of Capital financial duty

## 8. Costs and benefits

76. This chapter contains an analysis of the costs and benefit of the options detailed in Section 7. **Annex 3** contains the activity needed within the Welsh Government to introduce medium term financial planning for both options. To inform the analysis, Local Health Boards and the Wales Audit Office were contacted and asked to provide their best estimate of the costs for both options and the benefits associated with medium term financial planning.

### Costs

**Option 1 – do nothing and use the current legislation providing an annual financial duty, with annual expenditure not to exceed annual resource limit, and continue with the issue of directions for medium term financial planning.**

77. This option proposes no change to the existing arrangements and consequentially there are no additional costs associated with it.

78. The following paragraphs present a summary of the costs incurred under the current duties and arrangements that the Welsh Government is undertaking to introduce medium term financial planning for Local Health Boards.

79. The Welsh Government considers that the costs associated with this option fall to:

Local Health Boards.

The Wales Audit Office.

The Welsh Government.

### Costs to Local Health Boards

80. Local Health Boards estimate that there will not be a material incremental change in costs moving to a medium term planning arrangement. Given the fast track timescale, Local Health Boards only had limited time to undertake a high level best estimate exercise.

### Cost to Local Health Boards charged by the Wales Audit Office

81. The Wales Audit Office is legally required to undertake an annual audit of accounts for each Local Health Board and charge each Local Health Board accordingly.

82. Wales Audit Office has provided their best estimate of the cost incurred in undertaking this role costs, including the costs of producing a narrative report. The cost for undertaking an annual audit and producing a report is £252,571 per Local Health Board. This represents an annual cost of approximately £1,768,000 for all Local Health Boards.

## Costs to the Welsh Government

**Annex 3** sets out the activities associated with revising, issuing and implementing the Integrated Planning Framework. A Planning Framework is revised and issued on an annual basis to NHS organisations, setting out context and requirements for reflection in organisations' Annual and, since 2013/14, Medium Term Integrated Plans.

83. The costs associated with Option 1 fall into three main categories:

The costs of revising the framework.

The costs associated with the scrutiny of the plans.

The costs associated with the development needs to respond to the framework.

84. The move to Medium Term Integrated Plans requires greater revision and development of the planning framework in 2013-14 than would normally be the case. The process will involve the whole of the Health and Social Services Department and, where necessary other key Departments, for example Local Government and Communities. This engagement is essential to ensure that the framework represents the whole of the Welsh Government's statutory and policy requirements on NHS organisations.

85. The framework is revised and developed over a three month period (July – September) through a project approach and therefore costs are opportunity costs and are estimated based on anticipated contributions from project team members in that time period:

80% of a Grade 6.

10% of x 15 grade 6/7s.

86. On this basis, the estimated one off cost of developing and revising the framework in 2013-14 is approximately £50,000. The Directors will have an overview and steering role as part of this exercise and the opportunity cost associated with their deliberations is included in the above estimate.

87. In terms of scrutiny of plans, there is work underway to secure external capacity to support the scrutiny and review of the integrated plans for this period 2014-15 to 2016-17 (the 2013/14 Medium Term Plans) and January 2014 (the 2014/15 Medium Term plans). The exact scope and remit of the external capacity has yet to be finalised, but it will entail a holistic assessment of plans rather than just financial elements and work that was planned irrespective of the Bill. Estimated costs for the October and January assessments are a one off cost of between £50,000 and £75,000. For the purposes of this RIA, the mid-point of this range is adopted as the best estimate of the cost.

88. The revision of the integrated medium term planning framework will involve building capacity within Local Health Boards. The need to develop planning skill and capacity in Health Boards & Trusts exists irrespective of changes to the financial regime. A package of development opportunities is being developed which will

include some shared learning across NHS Wales organisations as well as learning from other organisations. The exact detail of the learning requirements is still being explored but it is unlikely that it will cost more than £10,000 in facilitation and programme development costs. Use and coordination of existing tools and methods of learning will be utilised and some join up with current development programmes prioritised. Academi Wales are supporting in this regard.

89. For example, a key area of development is with the Boards and their ability to scrutinise. There is already work underway to revise the Board Development programmes, led by Academi Wales and requirements for scrutiny of Medium Term Plans will inform this work. This work will continue irrespective of the Bill.

90. The total costs of Option 1 in 2013-14 are estimated to be £1.89m. Of this cost, approximately £122,500 is a one-off cost associated with the move to Medium Term Integrated Plans with the remainder expected to be incurred on an annual basis. These costs will be met from within existing budgets.

**Table 3. Summary of the transitional and recurrent costs incurred in 2013-14 under Option 1**

	£
<b>Transitional Costs</b>	
<b>Welsh Government</b>	
Framework	50,000
External Scrutiny	62,500
Training & Development	10,000
<b>Recurrent Costs</b>	
<b>Local Health Board</b>	
Wales Audit Office	1,768,000
<b>TOTAL</b>	<b>1,890,500</b>

**Option 2 – introduce legislation replacing the annual financial duty with a three year financial duty, and continue with the issue of directions for integrated medium term planning and medium term financial planning.**

91. The following paragraphs summarise the additional costs associated with introducing a three year financial duty.

#### **Costs to Local Health Boards**

92. The Welsh Government, in consultation with Local Health Boards, requested best estimated costs as a consequence of the financial duty over 3 financial years. Each of the 7 Health Boards responded and estimated that with the exception of audit requirements (see below); they will incur **no** additional cost as a result of the move to a three year financial duty. It is anticipated that the expenditure under the current arrangement will not increase because the work to complete an updated Statement and Disclosure Note in the Annual Accounts is not significant and would be accommodated within existing financial accountancy staffing levels.

## Wales Audit Office costs charged to Local Health Boards

93. Wales Audit Office considers that a substantive narrative in the Auditor General Report for the account of each Local Health Board will be necessary as a result of the financial duty over 3 financial years. WAO have indicated that the cost for producing the narrative as part of the annual report for each Local Health Board will be approximately £17,000. This amounts to a total additional cost of £119,000 per annum.

## Costs to the Welsh Government

94. The Welsh Government considers that direct additional costs to introduce a financial duty over 3 financial years would arise from communicating the changes to the law, by revising guidance and carrying out development sessions with Local Health Boards on the arrangements of the new duty.

95. The communications costs associated with this option would be for additional publicity as part of the on-going communications campaign for 'Together for Health'. This would include media relations activities that are estimated to be £500.

96. The Welsh Government would also revise and issue guidance to Local Health Boards, setting out the new duty, which is estimated to be around £2,000. These costs will be met from the Welsh Governments existing budgets

97. The costs set out in the Option 1 are relevant to this option as the work programme will continue regardless of the Bill. Emphasis and content may change but the resources associated with delivering will remain constant.

98. The one off estimated costs for scrutiny only go so far as March 2014 as more detailed assessments are required on longer term scrutiny arrangements of Medium Term Plans.

99. To summarise, there is an additional one-off cost of approximately £2,500 for communications activities and developing guidance under Option 2 and an additional annual cost of £119,000 for the extra audit requirements.

**Table 4. Summary of the transitional and recurrent costs arising from the provisions of the Bill under Option 2**

	£
<b>2013/14 Transitional Costs</b>	
<b>Welsh Government</b>	
Guidance	500
Communications	2,000
<b>2014/15 Recurrent Costs</b>	
<b>Local Health Board</b>	
Wales Audit Office	119,000
<b>TOTAL</b>	<b>121,500</b>

100. Table 5 below, summarises

The existing baseline costs incurred for the financial audit of statutory accounts of Local Health Boards, as set out in option 1.

The existing costs for the planning framework to move from annual to a medium term planning, which the Welsh Government is progressing regardless of legislation as set out in option 1.

The costs to which the provisions of the Bill give rise as set out in option 2.

**Table 5 : Summary of Total Costs (existing and arising from the Bill)**

	£
<b>Existing Baseline Audit Costs</b>	
Wales Audit Office	1,768,000
<b>Existing Planning Framework</b>	
Framework	50,000
External Scrutiny	62,500
Training & Development	10,000
<b>NHS Finance (Wales) Bill</b>	
Cost to which the provisions of the Bill would give rise	121,500
<b>TOTAL</b>	<b>2,012,000</b>

## **Benefits and risks**

**Option 1 – do nothing and use the current legislation detailing an annual financial duty, with annual expenditure not to exceed annual resource limit, and continue with the issue of directions for medium term financial planning.**

### **Benefits**

101. The Local Health Board will continue to operate within a well understood and established financial year end regime.

### **Risks**

102. Local Health Boards continue to make short term decisions towards the end of the year end that may not be in the best interests of the longer term delivery of NHS service.

**Option 2 – introduce legislation replacing the annual financial duty with a rolling three year financial duty, and continue with the issue of directions for integrated medium term planning and medium term financial planning**

### **Benefits**

103. Currently, where decisions are taken at year end, this can stop activity on services and impact on the service delivery to NHS patients. It is considered that the key benefit of this option would be that by removing the year end focus this should lead to better service, workforce and financial planning through aligning the timing of the resource requirements with the service change and service transfer time-scales.

104. The implementation of the Integrated Planning Framework and Standing Orders and Standing Financial Instructions does provide benefit over the historical arrangements for Annual Plans and Annual balanced Financial Plans. However this option is still constrained by the annual financial duty and this statutory duty requirement is likely to outweigh the potential benefits of medium term planning, particularly in the second half of any financial year.

105. The benefits of amending the statutory constraint each year would be to potentially to avoid the automatic consequence of an audit qualification should Local Health Boards expenditure exceed its Resource Limit.

106. The benefits for Option 2 also include behavioural change and create a culture that improves the use of medium term financial planning and reduces the costs associated with meeting compliance.

107. This should result in much of the benefits of aligning timing of resources to profiled service plans in Local Health Board and remove a significant challenge within the current regime which encourages short term decision making around the financial year, which may not be in the longer term interests of the organisation.

108. In responding to the consultation, Local Health Boards identified a number of benefits that they expect to be realised as a consequence of the new duty and the medium term financial planning arrangement:

Ability to 'invest to save' by strategic overspends in one year to generate savings in years two and three.

Ability to focus on a longer planning horizon, rather than always being focused on the next twelve months.

Integrated Medium Term Plans will support the development of longer term service plans which could provide sustainable services and financial sustainability where implementation is longer than the annual financial cycle. More joined up rather than reactive decision making.

Will allow better quality delivery plans to be developed annually.

Reduces the risk of investment decisions being made where the key criteria is time i.e. End of year capital.

More realistic timescale to enable improved integration with workforce and ICT plans and their delivery.

More realistic timescales related to quality improvements and realising the benefits of improved efficiency and productivity

Better alignment with planning and financial cycles of other partners e.g. Local Government.

Would support the development of a performance management system/set of measures which is more stable and offers consistency and continuity over a strategic period.

Provides a clearer, more uncomplicated story for staff and the public about direction of travel which can be supported with coherent plans to get there.

Recruitment strategies and workforce redesign which may have front loaded premiums to deliver downstream financial and service efficiency would be supported within a longer integrated planning framework.

## **Risks**

109. Failure by the Welsh Government to keep within resources each year will have significant resource and cash implications. The main risks are set out in paragraphs 34-38. Under Resource Budgeting and Accounting, cash generally follows approved resource when it is needed. A significant overspend without approved resource cover would mean that the Welsh Government will not be able to draw down sufficient cash (under Treasury cash limit controls) into the Welsh Consolidated Fund to meet the excess expenditure. This would mean that Welsh public bodies, including the NHS, would not have sufficient cash resources to pay its bills or payroll costs.

## **Summary and preferred option**

110. Flexing the annual financial duty to three years will allow Local Health Boards to focus their service planning, workforce and financial decisions over a longer period and is expected to result in better decision making and optimal solutions. This needs to be supported by a mature and responsive planning, financial and

governance framework, function and service that underpins sustainable service transformation.

111. There is a variety of evidence to support financial flexibility and medium term financial planning, which includes:

Sir Michael Lyons enquiry into Local Government, 'Place-shaping: a shared ambition for the future of local government'.<sup>9</sup> "The inflexibility of the current funding system inhibits local responsiveness. In addition to my detailed analysis and recommendations on local government finance I make recommendations on other ways of improving financial flexibility, by enabling resources to better reflect local priorities and to support partnership working." An article, published in Transformations in Business and Economics<sup>10</sup>, entitled 'Multi-year Budgeting as an Element of Institutional Reforms: The Experiences of European Union Countries versus Its Present-Day State in Poland' presents the importance of multi-year budgeting as part of institutional reforms of modern public finances.

The Audit Commission. Improving medium-term financial planning: a practical guide for primary care trusts, Briefing paper<sup>11</sup>, May 2008. This guide is based on a review of Primary Care Trust local delivery plans and Medium Term Financial Plans.

The Audit Commission also published a discussion paper, World class financial management: discussion paper. 15 November 2005<sup>12</sup>. In responding to the challenge of improving financial management, this paper set out to stimulate debate across public services and among finance professionals about what standards of financial management the public sector should aspire to over the longer term.

112. Recent evidence to support the use of integrated planning arrangements can be found in the Healthcare Inspectorate Wales and the Wales Audit Office report 'An overview of Governance Arrangements - Betsi Cadwaladr University Health Board', published June 2013<sup>13</sup>.

In paragraph 70 of this report it states "As an immediate challenge, further work is required by the Health Board to fully integrate and deliver service, workforce and financial plans. Whilst the Operational Plan refers to an integrated approach, in reality individual plans are not always fully integrated or affordable. Furthermore, the financial implications of service changes and

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<sup>9</sup><http://webarchive.nationalarchives.gov.uk/20100407205427/http://webarchive.org.uk/wayback/archive/20070428120000/http://www.lyonsinquiry.org.uk/index.html>

<sup>10</sup> 9(2), pp. 418-431. 2010. <http://www.transformations.khf.vu.lt/20b>

<sup>11</sup> <http://archive.audit-commission.gov.uk/auditcommission/subwebs/publications/studies/studyPDF/3439.pdf>

<sup>12</sup> <http://archive.audit-commission.gov.uk/auditcommission/audit-regime/support-guidance/pages/worldclassfinancialmanagementdiscussionpaper.aspx.html>

<sup>13</sup> <http://www.assemblywales.org/bus-home/bus-business-fourth-assembly-laid-docs.htm?act=dis&id=247493&ds=7/2013>

priorities need to be considered and built into the Operational Plan at an early stage, with a clear assessment that the proposed plans are affordable.”

The report’s recommendations 21 & 22 are also relevant, setting out that “The Board must take action to fully integrate and deliver service, workforce and financial plans and must prepare and approve sustainable service and financial plans before the start of the 2014-15 financial year that clearly demonstrate how financial pressures will be managed and addressed.”

113. Whilst the Welsh Government is already using powers of direction to introduce integrated medium term planning, including medium term financial planning, it is evident that its main weakness is that this is seen as supplementary to the main requirement of Annual Delivery Plans, Annual Financial Plans and Annual Financial Duty. In order for the medium term financial planning to work and for NHS patients to benefit from a more sustainable service, Local Health Boards’ financial duty and planning requirements must change from an annual basis to a medium term basis covering at least 3 years.

114. The Welsh Government considers that Option 2, the placing of a rolling 3 year financial duty on Local Health Boards, will provide a financial regime that flexibly manages resources, expenditure and approved limits over a 3 year period as part of a medium term financial planning arrangement.

## 9. Competition assessment

115. The competition filter is required to be completed if the legislation affects business, charities and/or the voluntary sector. The policy may have an indirect impact on businesses or contractors that provide services to the NHS. This impact is consequential and difficult to quantify. Local Health Boards anticipate that the ability to provide more sustainable services will result from a longer term approach to procurement and retention of staff.

116. The table below summarises the competition filter results.

Question	Response
<b>Q1:</b> In the market(s) affected by the new regulation, does any firm have more than 10 percent market share?	No
<b>Q2:</b> In the market(s) affected by the new regulation, does any firm have more than 20 percent market share?	No
<b>Q3:</b> In the market(s) affected by the new regulation, do the largest three firms together have at least 50 percent market share?	No
<b>Q4:</b> Would the costs of the regulation affect some firms substantially more than others?	No
<b>Q5:</b> Is the regulation likely to affect the market structure, changing the number or size of businesses/organisation?	No
<b>Q6:</b> Would the regulation lead to higher set-up costs for new or potential suppliers that existing suppliers do not have to meet?	No
<b>Q7:</b> Would the regulation lead to higher on-going costs for new or potential suppliers that existing suppliers do not have to meet?	No
<b>Q8:</b> Is the sector characterised by rapid technological change?	No
<b>Q9:</b> Would the regulation restrict the ability of suppliers to choose the price, quality, range or location of their products?	No

### Specific Impact Assessments

117. Impact assessments were completed as part of this RIA. There were no negative differential impacts identified from the review of impact assessments.

118. The Welsh Government is bound by the Equality Act 2010, and the Wales-Specific Equality Duties Regulations, the Human Rights Act 1998 and the European Convention on Human Rights. An **equality impact assessment** on the NHS Finance (Wales) Bill found no negative impacts. Where NHS service provision becomes more sustainable as a consequence of better planning and decision making, it will have a positive impact on all NHS users.

119. As part of the policy impact screening, consideration has been given to the five headline indicators in the Welsh Government's **Sustainable Development Scheme**. The Local Health Boards have identified that Integrated Medium Term Plans will support the development of longer term service plans which could provide sustainable services and financial sustainability where implementation is longer than the annual financial cycle. This could encourage more efficient use of resources by enabling Local Health Boards to enter into longer term supply contracts. This may also result in longer term contracts with energy suppliers, including the potential to invest to save in more resource efficient equipment. A more sustainable approach to service provision could also impact on staff turnover by reducing the need for Local Health Boards to utilise short or fixed term employment contracts because of financial flexibility.

120. A **rural proofing** screening assessment found that where Local Health Boards in rural areas procure services for NHS delivery, the procurement arrangements will be more sustainable as Local Health Boards will take longer term decisions for their organisations as a consequence of the duty.

121. The Welsh Government's Welsh Language Scheme requires that an assessment of the impacts of the Bill on the **Welsh Language** be carried out. The revisions to directions, guidance, circulars and provision of training prepared as a result of the Bill will need to be assessed and produced bilingually in line with the Welsh Government's Welsh Language Scheme.

122. Section 1(1) of the **Rights of Children and Young Persons (Wales) Measure 2011** provides that from the beginning of May 2014 the Welsh Ministers must have due regard to the requirements of Part 1 of the Convention, articles 1 to 7 of the Optional Protocol on armed conflict (except article 6(2)) and articles 1 to 10 of the Optional Protocol on the sale of children, child prostitution and child pornography.

123. Section 1(2) of the Measure states that from the beginning of May 2012 until the end of April 2014, the Welsh Ministers must have "due regard" to the requirements of Part 1 of the United Nations Convention on the Rights of the Child ("the Convention") and the Protocols when making any decision about provision proposed to be included in an enactment, as is the case here.

124. While there are no provisions within this legislation that specifically apply or do not apply to children, it is expected that allowing Local Health Boards financial flexibility over a 3 year period and enabling them therefore to plan more effectively should have positive benefits for sustainable service provision, which would of course benefit children as NHS service users.

## **10. Post implementation review**

125. The effectiveness of the legislation will be monitored by the Welsh Government through the on-going administration and integrated performance management of the new planning, delivery and financial regime. The Wales Audit Reports will be used to measure the impact the regime is having on fiscal management. Data will be collected from Local Health Boards on any costs and benefits as a result of the financial duty and planning framework and the effect on NHS patients through improved services.

## Annex 1 – Definition of Terms

<b>Definition</b>	<b>Meaning</b>
3 year period	A rolling 3 financial year period, the first of which commences on 1/4/2014 and ends on 31/03/2017.
Financial year	12 month period ending 31 March
Expenditure/Resource	These words should be used interchangeably throughout this EM. Expenditure is a reference to the use of resources through their expenditure, consumption or reduction in value.
Approved limits	The “control total” – currently defined and formally issued by Welsh Government as “Resource Limits”.
Financial Regime	The formal document that sets out the various finance, planning and governance themes and work to underpin Together for Health. This included Integrated Plans, Financial Flexibility, Resource Allocation, Financial and Delivery Information and Integrated Assurance and Governance.
Integrated Medium Term Plan	3 year integrated plans to include clinical, service, quality, workforce, financial, capital plans.
Integrated Planning Framework	Welsh Government issued document setting out NHS Wales planning cycle, planning assumptions, statutory requirement on NHS organisations and policy requirements.
Local Health Board Standing Orders	Formal governing documents, including a range of other framework documents setting out the arrangements within which the Board, its Committees, Advisory Groups and NHS staff make decisions and carry out their activities - its 'ways of working'.
Standing Financial Instructions	A component element of the Standing Orders that sets out the regulation of the financial proceedings and business.

Revenue Allocation	The main funding allocated by Welsh Ministers to enable Local Health Boards, and through Local Health Boards the NHS Trusts, to provide healthcare services for the resident population.
Revenue Resource Limit	The quantum of revenue resources issued to Local Health Boards as notified by Welsh Government.
Achievement of Operational Financial Balance	Achievement of Operational Financial Balance as defined and measured as per the Local Health Board Manual of Accounts.
Capital Resource Limit	The quantum of capital resources issued to Local Health Boards as notified by Welsh Government.
Resource Budgeting and Accounting	The accruals based accounting framework applicable to “Central Government” bodies as defined by the Office of National Statistics.
Delivery Framework	The Delivery Framework sets out a clear framework for service requirements, support, escalation and intervention.
Ministerial Direction	The NHS (Wales) Act 2006 provides for Welsh Ministers to give directions to NHS bodies on the way in which they are established, regulated and how they should exercise those functions that have been delegated to them. Directions can be issued by way of statutory instrument (i.e. regulations, orders, etc.) or by letter or other form of written instruction or may be issued as guidance. NHS bodies have a legal duty to comply with any direction issued by Welsh Ministers. Directions will usually be issued to NHS bodies under cover of a Ministerial Letter.

## Annex 2 – The Practical Application of the Duty

1. To illustrate how the legislation will be applied, the following key milestones take place as part of the Local Health Boards' planning framework:

- Initially, the Welsh Government, as part of the planning round, would issue Resource Planning Assumptions and initial baseline Revenue Resource Requirement figures for the Local Health Board to take into account in developing and finalising its Integrated Medium Term Plan and Medium Term Financial Plan.
- The Integrated Medium Term Plan and Medium Term Financial Plan will be developed in line with the issued Integrated Planning Framework, Delivery Framework and available resources.
- The Local Health Board should develop, finalise and approve an Integrated Medium Term Plan, including a balanced Medium Term Financial Plan, for submission, after Board approval, to Welsh Government prior to the beginning of the first year of the plan period.
- The Welsh Government would formally review and approve the balanced plan.
- The Welsh Government would action the requested and approved financial flexibility, detailed in the approved plan, between years through Recoverable Revenue Resource Limit Adjustments
- If the Welsh Government were not to approve the plan, then escalation and intervention powers would come into force and could eventually result in there being no flexible resource available to Local Health Boards. Access to Recoverable Revenue Resource Limit would be subject to approval of submitted plans, therefore if the plan is not approved the Local Health Board would be unable to access the Recoverable Revenue Resource Limit flexibility.

### Year 1

2. Using the planning framework milestones, for the Example Local Health Board, the following scenarios explain what will happen at the end of Year 1:

**Table 1: Example Local Health Board - Approved Plan & Year 1 Expenditure in line with Plan**

	2014/15	2015/16	2016/17
Baseline Revenue Resource Requirement	£1,000 m	£1,000m	£1,000m
Board Approved Planned Expenditure	£1,005 m	£998m	£997m
Planned Under / (Over)spend against Revenue Resource Limit	(£5m)	+£2m	+£3m

3. In reviewing and approving the Integrated Medium Term Plan, and Medium Term Financial Plan, the Welsh Government will need to fully understand and have confidence that the Local Health Board can manage the scale of movement in expenditure levels between the years (in this case the £7m reduction between £1,005m in 2014/15 and £998m in 2015/16)

**Table 2: Example 1-, the result of the Welsh Government approving the Medium Term Financial Plan**

	2014/15	2015/16	2016/17
Baseline Revenue Resource Requirement	£1,000m	£1,000m	£1,000m
Recoverable Revenue Resource Limit	£5m	(£2m)	(£3m)
Adjusted Revenue Resource Limit	£1,005m	£998m	£997m

4. Using the Example Local Health Board the results of potential year end outturns are illustrated and detailed in the following scenarios:

**Scenario 1 - 2014/15 Actual Spend £1,005m**

2014/15 Actual Spend £1,005m

- actual spend is within Year 1 Adjusted Revenue Resource Limit – reported as underspend against Revenue Resource Limit in the 2014/15 Annual Accounts’ Statement of Comprehensive Net Expenditure.
- 3 Year Rolling Financial Duty not considered in 2014/15.

5. The Welsh Government would ensure that the appropriate transparent disclosure notes would be included within the organisation’s Annual Accounts to reflect:

- That the Welsh Government had approved the Local Health Board Balanced Medium Term Financial Plan.
- The link between the approved balanced Medium Term Financial Plan and Year 1 Adjusted Revenue Resource Limit.
- The actual performance against Year 1 Adjusted Revenue Resource Limit.
- The actual performance in line with balanced Medium Term Financial Plan.

6. In this scenario, the Wales Audit Office would not be required to review and report on Financial Duty in Year 1, although they will issue narrative report.

**Scenario 2 – Approved Plan & Year 1 Expenditure not in line with Plan**

2014/15 Actual £1,006m Expenditure against Year 1 Adjusted Revenue Resource Limit of £1,005m

2014/15 Actual Spend

£1,006m

- actual spend is **not** within Year 1 Adjusted Revenue Resource Limit – reported as **overspend** against Revenue Resource Limit in the 2014/15 Annual Accounts' Statement of Comprehensive Net Expenditure.
- 3 Year Rolling Financial Duty not considered in 2014/15.

7. Appropriate transparent disclosure notes would be included within the organisation's Annual Accounts to reflect:

- That the Welsh Government approved the Local Health Board balanced Medium Term Financial Plan.
- The link between the approved balanced Medium Term Financial Plan and the Year 1 Adjusted Revenue Resource Limit.
- The actual performance against Year 1 Adjusted Revenue Resource Limit.
- The actual performance is **not** in line with balanced Medium Term Financial Plan.
- Disclosure on the reason why performance is not in line with the approved plan and set out actions to recover performance within years 2 and 3.

8. The Wales Audit Office is not required to review and report on the Financial Duty in Year 1. However they will provide narrative report, referencing the disclosure note on performance as not in line with plan, and the potential impact on the 3 year rolling financial duty, when it is measured at end of 2016/17.

9. The Welsh Government would consider if action is necessary under the formal escalation process and which forms part of the delivery framework described in paragraph 46.

### ***Scenario 3 – Plan Not Approved by the Local Health Board***

10. A Local Health Board may be unable to finalise a balanced Medium Term Financial Plan and get Board approval, for submission to Welsh Government.

11. The Board responsibility for presenting and approving the plan is set out in Ministerial Directions issued by the Welsh Government and will be included within the Board's Standing Orders and Standing Financial Instructions. If the Direction is not met, then the following applies:

- The Board will be in breach of their own Standing Orders if plan not finalised and approved.
- The Chair has personal responsibility to ensure that matters reserved for the Board are dealt with by the Board in a timely manner and in line with Standing Orders.
- The Chief Executive has personal responsibility to ensure that the plan is presented in a timely manner to the Board for approval.

12. Where the above requirement has not been met, the initial escalation will be direct to the NHS Wales Chief Executive who will determine actions which may include the following:

- A meeting is required with the Chair, Vice Chair, Chief Executive Officer, Board Secretary and relevant Executives.
- The introduction of 'special measure' arrangements.
- A review of executive effectiveness.
- A review of Board effectiveness.

13. The Welsh Government will ensure these actions include a strict timetable with weekly monitoring, and further escalation and intervention as appropriate, including up to intervention powers set out in section 28 of NHS (Wales) Act 2006.

**Scenario 4 – Plan Not Approved by the Welsh Government**

14. The approved plan may not be in place because Local Health Board may submit a balanced plan but the Welsh Government, following review, may not approve the plan.

15. Using the Example Local Health Board, where the Welsh Government approval is not given, for this scenario:

**Table 3: Scenario 4**

	2014/15	2015/16	2016/17
<b>Local Health Board submitted balanced Medium Term Financial Plan</b>			
Baseline Revenue Resource Requirement	£1,000m	£1,000m	£1,000m
Board Approved Planned Expenditure	£1,005m	£998m	£997m
Planned Under / (Over)spend against Revenue Resource Limit	(£5m)	+£2m	+£3m

16. The Welsh Government not approving the Medium Term Financial Plan would lead to:

**Table 4: Scenario 4,**

	2014/15	2015/16	2016/17
Baseline Revenue Resource Requirement	£1,000m	£1,000m	£1,000m
Recoverable Revenue Resource Limit	-	-	-
Adjusted Revenue Resource Limit	(£1,000m)	£1,000m	£1,000m

17. The powers of intervention that are available to the Welsh Government through the National Health Service (Wales) Act 2006 as detailed in Delivery Framework, circulars and letters, would apply here. The escalation, to level 1 to 4 will be subject to the assessment of the state of the submitted plan, and on the judgement of necessary action to deliver a robust and appropriate balanced plan. Welsh Government would:

- Confirm with Local Health Board that plan not approved.
- Confirm that, pending resubmission and approval of a balanced 3 year plan that the Year 1 Revenue Resource Limit would remain as £1,000m.
- Require Board to resubmit balanced 3 year plan within a month.
- Detail any specific requirements highlighted in the review of the original submitted Local Health Board plan and any recommendations for support.
- Detail any specific requirements relating to the Year 1 plan pending resubmission and approval of balanced 3 year plan.

18. Performance against Year 1 Revenue Resource Limit will be assessed through both monthly Quality and Delivery Meetings, as per the Delivery Framework, and through the monthly Financial Monitoring Returns. The Local Health Board Chief Executive, as the Accountable Officer, would regularly update the NHS Wales Chief Executive where there were concerns on delivery against the Year 1 Revenue Resource Limit and set out actions and timescales for corrective action.

19. If a review of a resubmitted plan led to Welsh Government approval, the actual performance would be covered by Scenarios 1 and 2 above. If the resubmitted plan was not approved Welsh Government, then it would escalate in line with existing escalation and intervention powers until balanced plan was submitted and approved.

20. Further escalation and intervention powers that would take effect as a consequence of Welsh Government not approving the plan would be:

- Escalation from support to intervention, where action will be subject to assessment of how close or far the Local Health Board is from an approvable balanced plan.
- That the Local Health Board is to resubmit plan by end of May 2014.
- Confirmation that the resources available would be limited to baseline Revenue Resource Requirement,
- That the Welsh Government would highlight the continued non compliance of Board and Board members, including impact on the Chair's position and Chief Executive position, as Accountable Officer.

21. If escalation and intervention has not succeeded at this point, then the next iteration of the submitted plan is not approved and further action is taken:

- The NHS Wales Chief Executive will determine actions and intervention, including any recommendations to Minister regarding powers available to the Welsh Government through the NHS (Wales) Act 2006, S26-28.



## Year 2

26. As part of the Local Health Boards planning framework, health boards will be required to submit and obtain approval for a three year rolling plan every 12 months. In each year the timetable and process will be identical to that which is laid out at the beginning of this annex.

27. Consequently, the second medium term plan covering the period 2015-16 to 17-18 will be submitted for approval to the Welsh Government by the end of January 2015. The process and implications of various year end outturn scenarios will result in the same outcomes as the examples shown within pages 37 to 42 above.

28. As the new statutory duty will be based on a three year rolling retrospective test, the Wales Audit Office will not be conducting a formal statutory financial duty test again at the end of the 2015-16 financial year.

## Year 3

29. For the period 2016-17 to 2018-19 health boards will be required to submit approved plans before the end of January 2016. Once again the timetable, process and implications of various year end outturn scenarios will be the same as described above with the ***exception of where actual expenditure falls above that which was planned and approved over the previous three years.***

30. At the end of the financial year 2016-17 the Wales Audit Office will for the first time and each subsequent year thereafter perform its statutory financial duty test. This test will be undertaken to ensure that the aggregate expenditure over the three previous financial years i.e. 2014-15, 2015-16 and 2016-17 does not exceed the total aggregate amount approved by the Welsh Government for that period.

31. Where the aggregate expenditure over the three year period does exceed the aggregate approved expenditure limit, the annual accounts for 2016-17 would receive a ***regularity audit qualification*** and Wales Audit Office will include a full narrative report within the accounts setting out the circumstances and reasons for the qualification.

32. The specific circumstances that led to the breach of the financial duty and an assessment by the Welsh Government of the ability of the health board to recover the position would determine the action that would be taken in accordance with the framework for support, escalation and intervention as described on page 15.

NOTE: As Welsh Health Circular (2007) 049 "Statutory Financial Duties of NHS Trusts and Local Health Boards" will need to be revoked and a new Direction/Circular issued, an updated Protocol for Escalation & Intervention will need to be included as an Annex. The rewritten Annex will need to reflect that the Protocol for Escalation & Intervention will be in context of reviewing and approving the Integrated Medium Term Plan 2014/15 to 2016/17, not just the balanced Medium Term Financial Plan 2014/15 to 2016/17. This escalation and intervention protocol would be a common protocol for:

- Delivery Framework
- Integrated Planning Framework
- Financial Duties.

## Annex 3 – Summary of Cost Type

### Cost Type Analysis for additional work identified as necessary as a consequence of the Bill

Relevant activity can be: 1. already planned / underway;  
2. need additional work / resource required as a result of the Bill; or  
3. both.

Number	Activity	Activity already planned / underway for integrated medium term planning (YES/NO)	Additional work / resource required as a result of NHS Finance (Wales) Bill (YES/NO)	Cost Type	Cost period: One off cost Annual Cost On-going Cost
1	Revision of Local Health Board Standing Orders ○ Revising a limited number of paragraphs	Y	Y	Administration	One off cost
2	Revision of Local Health Board Standing Financial Instructions ○ Revising a limited number of paragraphs	Y	Y	Administration	One off cost
3	Revision of Trust Standing Orders ○ Revising a limited number of paragraphs	Y	Y	Administration	One off cost
4	Revision of Trust Standing Financial Instructions ○ Revising a limited number of paragraphs	Y	Y	Administration	One off cost
5	Revision of Local Health Board Manual For Accounts	Y	Y	Administration	One off cost

Number	Activity	Activity already planned / underway for integrated medium term planning (YES/NO)	Additional work / resource required as a result of NHS Finance (Wales) Bill (YES/NO)	Cost Type	Cost period: One off cost Annual Cost On-going Cost
	<ul style="list-style-type: none"> <li>○ Review &amp; update Statement of Net Comprehensive Expenditure and one Disclosure Note</li> </ul>				
6	Revision of Trust Manual For Accounts <ul style="list-style-type: none"> <li>○ Review &amp; update Statement of Net Comprehensive Expenditure and one Disclosure Note</li> </ul>	Y	Y	Administration	One off cost
7	Revision of Local Health Board Summarised Accounts	Y	Y	Administration	One off cost
8	Revision of Trust Summarised Accounts	Y	Y	Administration	One off cost
9	Revision of Welsh Health Circular (2007) 049 Statutory Financial Duties of NHS Trusts and Local Health Boards <ul style="list-style-type: none"> <li>○ Rewrite and reissue of whole document</li> </ul>	N	Y	Administration	One off cost
10	Revision of 2013/14 Revenue Allocation Letter <ul style="list-style-type: none"> <li>○ Review in case any change required</li> </ul>	Y	Y	Administration	Annual Cost
11	Scrutiny of Integrated Medium Term Plans (IMTP) External capacity being	Y	Y	External Resource	Initially one off but will include on-going cost

Number	Activity	Activity already planned / underway for integrated medium term planning (YES/NO)	Additional work / resource required as a result of NHS Finance (Wales) Bill (YES/NO)	Cost Type	Cost period: One off cost Annual Cost On-going Cost
	<p>considered for October 2013 assessment of 2013-14 IMTP  External capacity being considered for January 2014 assessment of 2014/15 IMTP  Longer term scrutiny arrangements to be clarified</p>				
12	<p>Revision of 2013/14 Financial Monitoring Returns</p> <ul style="list-style-type: none"> <li>○ Review but unlikely to materially change in year</li> </ul>	Y	Y	Administration	Annual Cost
13	<p>Revision of 2013/14 Delivery Framework</p> <p>Review but unlikely to materially change in year</p>	Y	N	Administration	Annual Cost
14	<p>Revision of Integrated Medium Term Planning Framework, Guidance &amp; Templates 2014/15 to 2016/17, including Medium Term Financial Planning Framework, Guidance &amp; Templates 2014/15 to 2016/17</p> <ul style="list-style-type: none"> <li>○ Programme in place to develop framework</li> </ul>	Y	N	New Guidance and skills/capability development	One off cost but review of plans likely to lead to update of framework for following year's planning submission
15	Revision of NHS Wales Delivery Framework 2014/15 onwards	Y	N	Administration	Annual Cost

Number	Activity	Activity already planned / underway for integrated medium term planning (YES/NO)	Additional work / resource required as a result of NHS Finance (Wales) Bill (YES/NO)	Cost Type	Cost period: One off cost Annual Cost On-going Cost
	<ul style="list-style-type: none"> <li>Programme in place to develop framework</li> </ul>				
16	<p>New - Performance Monitoring Returns 2014/15 (assumed these will be required to support performance management and monitoring of delivery of Integrated Medium Term Plans)</p> <ul style="list-style-type: none"> <li>Requirement to be assessed</li> </ul>	Y	N	Administrative Compliance / Escalation	On-going
17	<p>Revision of Capital Guidance Requirement to be assessed</p>	Y	Y	Administrative	One off cost
18	<p>Revision of relevant Ministerial Directions</p> <ul style="list-style-type: none"> <li>Direction to include updated Financial Duty direction and Integrated Planning direction</li> </ul>	N	Y	Administrative	One off cost
19	<p>Produce guidance for new financial regime (non-statutory)</p> <ul style="list-style-type: none"> <li>To be included as part of annual update of</li> </ul>	Y	Y	New Guidance	One off cost
20	<p>'Up-skilling' WG staff – awareness raising and training</p>	N	Y	skills/capability development	One off cost

Number	Activity	Activity already planned / underway for integrated medium term planning (YES/NO)	Additional work / resource required as a result of NHS Finance (Wales) Bill (YES/NO)	Cost Type	Cost period: One off cost Annual Cost On-going Cost
21	Communications with Local Health Boards and Wales Audit Office	N	Y	Administrative	On-going

## Annex 4 – Explanatory Notes

### Introduction

1. These Explanatory Notes relate to the National Health Service Finance (Wales) Bill introduced into the National Assembly for Wales on 30 September 2013.
2. They have been prepared by the Welsh Government’s Department for Health and Social Services in order to assist the reader of the Bill and to help inform debate on it. They do not form part of the Bill and have not been endorsed by the National Assembly for Wales.
3. The Explanatory Notes should be read in conjunction with the Bill. They are not meant to be a comprehensive description of the Bill. Where an individual section of the Bill does not seem to require any explanation or comment, none is given.
4. The Bill creates a duty for Local Health Boards to adopt a financial regime to flexibly manage resources, expenditure and approved limits over a rolling 3 year accounting period instead of each financial year. The purpose of the Bill is to enable Local Health Boards to focus their service planning, workforce and financial decisions and implementation over a longer, more manageable, period.
5. Sections 2(1) to 2(3) inclusive of the Bill, detail the specific changes to the National Health Service (Wales) Act 2006 required to move from an annual financial duty to a financial duty which is measured over a three year period. An illustration of the periods to which it will apply are identified in **Table 1**. An illustration of how the financial duty will operate is set out in **Table 2**.
6. Section 2(4) repeals s176 of the National Health Service (Wales) Act 2006. Section 176 requires Local Health Boards to maintain their resource expenditure within resource limits. This requirement is now contained within section 175.

**Table 1 - Illustration of how the financial duty is assessed over a rolling 3 year accounting period**

	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20
<b>Financial Duty Assessment</b>						
3 Year Rolling			X			
				X		
					X	
						X

The first assessment of the financial duty will take place at the end of 2016/17. (This table shows the first four 3-year accounting periods only).

**Table 2 - Illustration of how the financial duty in section 175 as amended will operate**

**Local Health Board performance for the 3 year accounting period ending 31 March 2017**

	2014/15	2015/16	2016/17	Aggregate
Net operating costs	X1	X2	X3	X1+X2+X3
Expenditure Limit	Y1	Y2	Y3	Y1+Y2+Y3
Under/(over) spend against Expenditure Limit				=(Y1+Y2+Y3) -(X1+X2+X3)

Where a Local Health Board has not spent in excess of its expenditure limit (determined by the Welsh Ministers) in the rolling 3 year accounting period it will be assessed as having met its financial duty.