



Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon Kenneth Clarke QC MP
 Secretary of State for Health
 Department of Health
 Richmond House
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3 May 1990

Dear Secretary of State

PUBLIC EXPENDITURE AND THE NHS REVIEW

As you know, I minuted the Prime Minister on 17 April outlining in broad terms the exceptionally difficult background to this year's public expenditure Survey, and the extremely restricted scope for any increases in present programme plans. Aaa

2. I have been looking further at individual programmes, and the prospects for restraining any pressures they might be likely to put upon the Reserves provided in the planning totals. The greatest scope is naturally in the postponement of new policies which might put fresh burdens on the resources available.

3. In your case, of course, there are two outstanding examples of new policies which are at present intended to be introduced next April. Community care is already under discussion in a separate forum, and I do not want to raise it here. But the NHS review is another new policy which is already putting demands on public expenditure.

4. At present, you have some £370 million a year for the NHS reforms. On top of that, I am informed that, if NHS trusts are set up from next April as intended, the interest charges on their capital will add to the planning total (though they will not reduce the PSDR) - possibly around £100 million a year, though that depends on the number of trusts. Some at least of this total of perhaps £500 million a year could be saved if implementation of the reforms were postponed for a while.

5. Moreover, I believe there is a further considerable risk which we are likely to run if implementation goes ahead as planned next April. One of the principal changes will be to fund health authorities as purchasers rather than providers. So if a health authority is an exporter of patients, it will in future have more

to spend on services for its resident population than it has hitherto had to spend on its own hospitals. Conversely, an importing health authority will have less to spend.

6. Next January, you will be giving the health authorities their new budget allocations for 1991-92. Health authorities which are major importers of patients, including those who have major teaching hospitals within their boundaries, will receive smaller - in some cases far smaller - budgets than they are used to receiving. Yet the hospitals within their boundaries will be facing much the same costs, including the pay of doctors and nurses, as before. In principle, of course, those hospitals may expect to receive the missing funds from other health authorities, sending their patients to those hospitals as they have always done. Your Department could perhaps take steps to ensure that that happened, but that would run counter to what, as I understand, health authorities have been told so far about how the new system will work. And the poor information currently available about patients flows and costs, and the further complication of capital charges, may render such an exercise impossible.

7. The danger is that the teaching hospitals may panic. They will face the risk that the exporting health authorities will not send as many patients as before, or may enter into long arguments about the bills for doing so. The hospitals may threaten to begin closing wards straightaway.

8. We could be faced with some very unpleasant headlines, and great pressures to meet the problem by providing more money, even though the problem is merely distributional.

9. It may be that you do not see this as a likely problem. If so, I should be very glad to know how you think health authorities will react next January. But if there is a risk such as I have suggested, it is I believe another powerful reason why we should consider very seriously postponing the reforms.

10. We need not, of course, abandon the switch from provider to purchaser funding, which in principle I support. We could continue with the introduction of contracts, and the associated financial and information systems, but run them on a "shadow" basis only for a couple of years. In that way, health authorities would become accustomed to how the revised budgets would be likely to work in practice, any teething troubles would be overcome, and we should not be so likely to face panic measures, and threats of measures, when the real transition to purchaser funding was made.

11. I should be most grateful if you would give this matter your most serious consideration, and let me know what you think.

12. I am copying this letter to the Prime Minister and the Chancellor.

Yours sincerely
Camps Evans

NORMAN LAMONT

approved by the Chief Secretary
and signed in his absence