

CROWN HEALTH
FINANCING AGENCY
lending, property, advisory

statement of intent 2006/07

30 June 2006

table of contents

Chair's Foreword	2
The Crown Health Financing Agency	4
Part One: Our Contribution to the Sector	6
1.0 Affordable DHB debt	8
2.0 Independent advice improves financial disciplines and DHB performance	14
3.0 Partnership and collective activity improves DHB cost effectiveness	18
4.0 Efficient management of residual AHB assets and liabilities	22
Part Two: Forecast Statement of Service Performance – 2006/07	24
1.0 Output class one: Lending services	25
2.0 Output class two: Property advice and disposal services	27
3.0 Output class three: Financial services	29
4.0 Organisational capability and development	31
5.0 Reporting	33
6.0 Prospective Financial Statements for the Year Ending 30 June 2007	35

chair's foreword

2

INTRODUCTION

The Crown Health Financing Agency (CHFA) is a Crown Entity under the New Zealand Public Health and Disability Act 2000 and is categorised as a Crown agent for the purposes of the Crown Entities Act 2004.

The functional responsibilities for the CHFA include lending, property management and financial advisory services provided to District Health Boards, other health Crown entities, and the Minister of Health.

Under our lending role we have in recent years refinanced the majority of the private sector debt held by the District Health Boards, and are now increasingly involved with lending to new capital investments for the DHBs. As part of this lending role, we engage in rigorous monitoring and assessment of DHB financial performance. As a result we are able to provide Ministers with in depth independent advice on the financial condition of the DHB sector.

Our property services assist DHBs to dispose of surplus properties to release capital funds for reinvestment in the sector. We have developed core competencies in managing and disposing of surplus properties and in advising DHBs on the ownership, occupation and use of their properties.

A new Terms of Reference approved in 2005 has encouraged expansion of our existing services resulting in a wider range of financial advice being provided to DHBs and an increasing involvement in joint DHB projects.

We believe that by encouraging greater collaboration and partnership in the health sector (for example collective procurement) the outcome will be greater efficiency, effectiveness and value for public funding.

The CHFA also continues to manage a range of residual Area Health Board assets and liabilities on behalf of the Government. The remaining residual tasks include the ongoing management of contingent legal liabilities that arise from the previous Area Health Board responsibilities, the long term lease of Tourism and Travel House in Wellington, and the investment of unclaimed patient's funds for the Southland DHB pending a resolution of the future use of these funds.

FUTURE DIRECTION

The CHFA has a successful track record in providing expert lending, property, and financial advisory services to the DHB sector and the Board continues to support the ongoing broadening of these services.

For 2006/07 the Board has placed an emphasis on enhancing existing CHFA services and actively identifying new opportunities to assist the DHB sector to achieve gains in cost effectiveness. This includes developing our networks and relationships across the sector, our performance monitoring and financial analysis, and our capability to deliver expert advice and projects that contribute to achieving a sustainable DHB sector.



ROSS TANNER

Chair

Crown Health Financing Agency

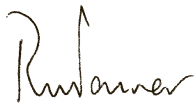
BOARD STATEMENT

This Statement of Intent (SOI) has been prepared to meet the requirements of the Public Finance Act 1989 and the Crown Entities Act 2004 and to give effect to the Minister of Health's ownership expectations for the CHFA.

The SOI outlines for Parliament the nature and scope of the CHFA's functions, what we are trying to achieve, and provides a base against which actual performance can be assessed through the annual report.

The SOI reflects the 'Managing for Results' framework which applies to all Crown Entities from 2006/07. The planning focus places emphasis on identifying our contribution to DHB results.

Part one of the SOI identifies the results that we will pursue in the next three years, the strategies we will use to achieve these results, the measures of success, an assessment of the challenges and risk that we will face and the implications for our required capability. Part two includes the financial and non-financial measures and standards that we aim to achieve for 2006/07.



ROSS TANNER

Chair

Date: 30th June 2006



IAN SLIPER

Board Member

the crown health financing agency

4 The CHFA's objective is to assist District Health Boards (DHBs) to achieve and maintain financial sustainability through the provision of a range of financial services and expert advice.

Our responsibilities are grouped into three distinct 'lines of business' designed to service the lending and property requirements of DHBs and resolve the Crown's obligations in respect of the residual assets and liabilities of the Area Health Boards that existed prior to July 1993. The nature and scope of these functions is covered by a Composite Terms of Reference¹ (most recently updated August 2005).

The CHFA is committed to working in partnership with DHBs, the Ministry of Health, the Treasury, and other stakeholders to achieve the Government's social and financial objectives.

OUR CORE BUSINESS FUNCTIONS

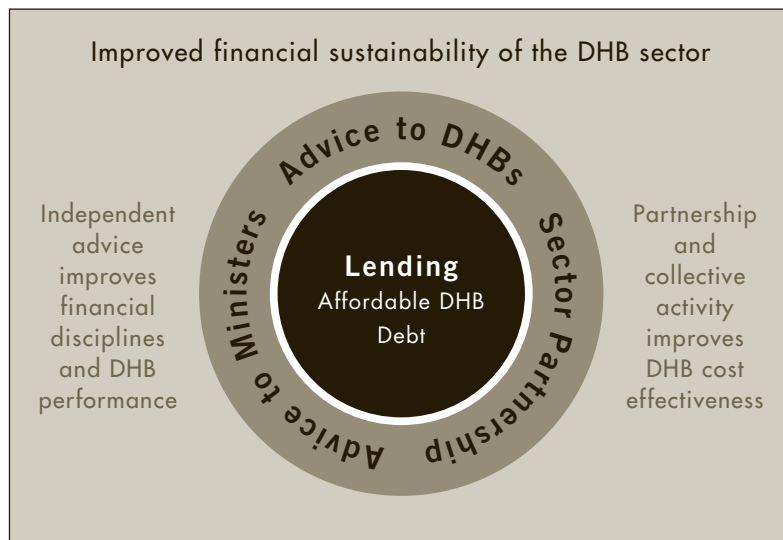
The lines of business undertaken by the CHFA are:

- **Lending:** we are the lender to the DHB sector and provide a range of loan facilities to refinance existing private sector debt or to finance new capital investment.
- **Property:** we assist DHBs with the disposal or acquisition of property to meet future service needs. We also offer advice to DHBs to achieve efficient use of their property estate including ownership, management, occupation and use.
- **Financial services:** we manage a range of residual functions on behalf of the Government, and provide financial and analytical support to DHB efficiency projects and collaborative initiatives.

OUR MANAGEMENT OBJECTIVES

- work in partnership and cooperation with our clients and stakeholders
- understand the needs of our clients
- offer high quality, practical, professional and independent advice
- encourage access to our services through effective work practices
- proactively monitor the financial performance of clients.

RESULTS WE CONTRIBUTE TO



¹ Crown Health Financing Agency Composite Terms of Reference (August 2005)

VALUES

The CHFA will pursue its objectives through demonstrating commitment to its core values:

- **Integrity:** we expect adherence to ethical conduct, open and honest communication and delivering on commitments as the basis for earning and maintaining trust among the Board, staff and stakeholders.
- **Excellence:** we take pride in what we do and challenge ourselves to do better. We continuously seek to improve our business processes, systems and services.
- **Responsiveness:** what we do is driven by the needs of our clients and the expectations of our stakeholders. We are committed to meeting these needs and expectations and our aim is to be accessible and responsive in a professional manner.
- **Teamwork:** we work towards achieving common goals in a spirit of cooperation that is made possible by a team ethic of respect, responsibility and accountability and where support is freely offered to colleagues and others.
- **Courage:** we work in a highly complex sector that requires courage and endurance to achieve results, to challenge the "status quo", to try new things and to learn from our mistakes.
- **Enthusiasm:** we are proactive and passionate about identifying opportunities to contribute to the cost effectiveness and efficiency of the DHB sector. When we identify new opportunities we will respond constructively so as to deliver results that are positive, effective and long-lasting.

part one: our contribution to the sector

6

SECTOR RESULT: IMPROVED FINANCIAL SUSTAINABILITY OF THE DHB SECTOR

The DHB sector has a goal of improving financial sustainability through achieving greater efficiency and value for money.

Financial sustainability requires that revenue is sufficient to meet the cost of service provision, including maintenance and replacement of capital assets required for service delivery.

Enhancing sustainability requires improvements in cost effectiveness, efficiency and value for money.

Achieving financial sustainability will ensure that the sector has sufficient financial resources to support future service needs and infrastructure requirements.

To support this goal the Government has placed an emphasis on:

- identifying and seizing opportunities to improve the cost effectiveness of the DHB sector
- continuing to strengthen relationships
- establishing more coordinated and complementary ways of working across the sector
- disseminating information to achieve shared knowledge.

THE CHFA CAN MAKE A DIFFERENCE BY CONTRIBUTING TO 3 RESULT AREAS AND 1 GOVERNMENT OBJECTIVE:

Result 1:	Affordable DHB debt - DHBs are able to service interest costs and repay debt.
Result 2:	Independent advice improves financial disciplines and DHB performance.
Result 3:	Partnership and collective activity improves DHB cost effectiveness.
Government Objective ² :	Efficient management of the residual assets and liabilities of the former Area Health Boards (AHBs) minimises the cost to the Crown.

In this Statement of Intent we focus on our direct contribution to these three sector result areas, and to achieving the Government objective for the residual AHB assets and liabilities.

Indirectly, we contribute to a much wider range of health sector outcomes and Government objectives. While it is important that we continue to contribute to these, this SOI focuses on those key results that we are responsible for.

Part One outlines our contribution to achieving these results in the medium term.

² 'Objective' recognises that not all of our functions, such as managing residual assets, are intended to achieve the sector-level result – the effectiveness of our interventions should not be judged on that basis.

summary of our contribution to sector results

RESULT 1: AFFORDABLE DHB DEBT

Our contribution

- Offering financial products that meet DHB needs
- Providing independent advice to inform investment decisions
- Monitoring DHB financial performance to protect loan quality
- Maintaining DHB debt levels within affordable lending limits
- Employing best practice lending criteria to maintain financial discipline
- Ensuring that debt repayment provides for future asset replacement.

CHFA OUTPUTS

- Lending of term debt
- Financial monitoring
- Independent financial advice.

SECTOR PARTNERS

- DHBs, Ministry of Health, the Treasury, and NZ Debt Management Office.

RESULT 2: INDEPENDENT ADVICE IMPROVES FINANCIAL DISCIPLINES AND DHB PERFORMANCE

Our contribution

- Providing financial and property advice and services assists DHBs to achieve their business objectives
- Maintaining oversight and management of financial risks in the DHB sector
- Providing independent advice that improves the understanding of DHB financial performance.

CHFA OUTPUTS

- Financial advice to DHBs/stakeholders
- Independent policy advice to Ministers on DHB financial performance
- Strategic property advice and surplus property disposal service.

SECTOR PARTNERS

- DHBs, DHBNZ, Ministry of Health, the Treasury, NZ Debt Management Office, Te Puni Kokiri, and the Office of Treaty Settlements.

RESULT 3: PARTNERSHIP AND COLLECTIVE ACTIVITY IMPROVES DHB COST EFFECTIVENESS

Our contribution

- Partnering with DHBs to assist in identifying and implementing opportunities to achieve cost effectiveness
- Enhancing relationships in the DHB sector to support knowledge and information sharing.

CHFA OUTPUTS

- Financial and analytical support for DHB initiatives.

SECTOR PARTNERS

- DHBs, DHBNZ, the Ministry of Health, the Treasury, and other stakeholders.

1.0 affordable DHB debt

THE CHFA CONTRIBUTES BY

Financing

- *CHFA financial products meet DHB needs:* DHBs are able to access a range of financial products with terms and conditions appropriate to their financial circumstances.
- *Independent advice informs investment decisions:* The CHFA participate in the National Capital Committee process³ and provides an independent opinion on the affordability and financial sustainability of DHB capital investment proposals.

Protecting the quality of loans

- *Monitoring of DHB financial performance protects loan quality:* The CHFA independently monitors DHB financial performance to inform advice to Responsible Ministers and to protect the value and quality of loans to DHBs.
- *DHB debt levels are managed within affordable lending limits:* DHB borrowings are managed within agreed lending parameters to maintain affordable debt levels and cash flows.
- *Best practice lending criteria maintains financial discipline:* The CHFA lending practices instil financial disciplines which maintain affordable DHB debt levels and cash flows.
- *DHB debt repayment provides for future asset replacement:* DHB repayment of debt strengthens their financial position to support future replacement of capital assets.

WITH OUTPUTS DELIVERED THROUGH

- lending services.

AND WORKING IN ASSOCIATION WITH

- *DHBs:* DHBs ultimately decide on the service choices for their community and are responsible for operating on a financially sustainable basis.
- *Ministry of Health:* The Ministry of Health has a significant contribution to the performance of the health sector, including allocation of Vote Health funding, maintaining system capacity and providing direction of leadership to the sector.
- *The Treasury:* The Treasury is responsible for providing oversight of the financial and organisational performance of the sector and participate in negotiating Vote Health funding.
- *The NZDMO:* The NZ Debt Management Office provides funding for CHFA loans to DHBs.

³ The National Capital Committee (NCC) leads and facilitates capital investment advice to inform the Ministry of Health's advice to Ministers. The allocation of Crown capital funding is managed via the NCC. Final capital funding decisions rest with Ministers.

FINANCING

CHFA provision of term debt: Debt and equity finance is used to fund capital infrastructure. The mix of finance and the structure of the debt determines the operating cash flows and affordability of the investment.

Independent Advice: The CHFA has a unique position in the sector as the sole provider of term debt. We assess the affordability of investment proposals, structure term debt facilities to support investments,

and provide financing advice to DHBs. Where required we work with DHBs to improve the viability of investment proposals and identify the most efficient financing options.

PROTECTING THE QUALITY OF LOANS

Monitoring DHB financial performance protects the quality of loans: We monitor DHB financial performance against prudent lending criteria to provide an objective assessment of financial health.

Our lending criteria ensure that DHBs minimise borrowing levels and maintain sufficient cash flows to meet the loan requirements. By minimising and encouraging repayment of debt, the sector builds balance sheet provisions for future asset replacement.

1.1 measuring and evaluating sector results**FINANCING: (QUALITY AND EFFECTIVENESS OF PRODUCTS AND ADVICE)**

As at 31st December 2005 DHBs had total assets valued at \$3.92 billion including the infrastructure, clinical equipment and other items that support service delivery. As at 31 March 2006, the CHFA has approved loans totalling \$1,432.8m. Loans actually drawn down amounted to \$912.7m, which is an increase of \$106.5m on outstanding loans as at 31 March 2005 of \$806.1m.

The CHFA has progressively refinanced the majority of DHB private sector debt since 2001. New debt finance is provided for major capital investments including hospital redevelopments and significant clinical equipment.

Assuming that all debt appropriated is drawn, the CHFA loans portfolio is expected to increase to \$1,545m by 30 June 2009. At that date the only remaining private sector debt to be refinanced will be Auckland DHB's bonds of \$120m.

The increase in loan volumes has supported a graduated reduction in our loan administration charge from 0.35% to 0.15%. At 31 March

2006, the average interest rate being paid by DHBs was 6.51%.

At 31 March 2006, the CHFA base interest rate is 24 basis points below the average private bank benchmark, reflecting an estimated saving to DHBs in annual interest costs of approximately \$2.2m. This excludes the difference between bank and CHFA margins (please refer to figure 2 on page 10).

Figure 1: CHFA Total Loans

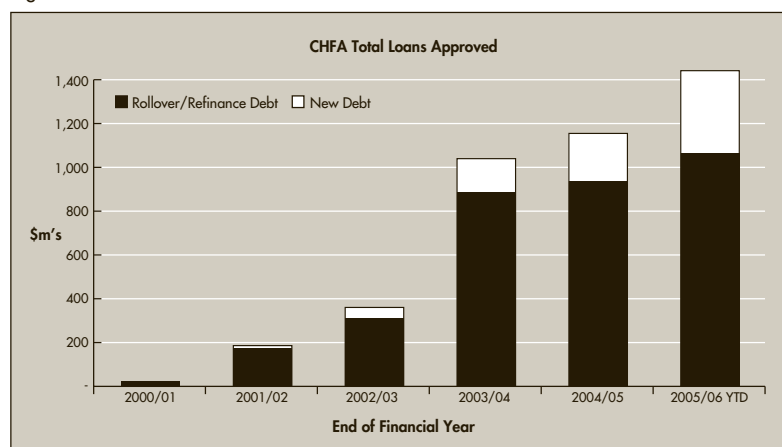
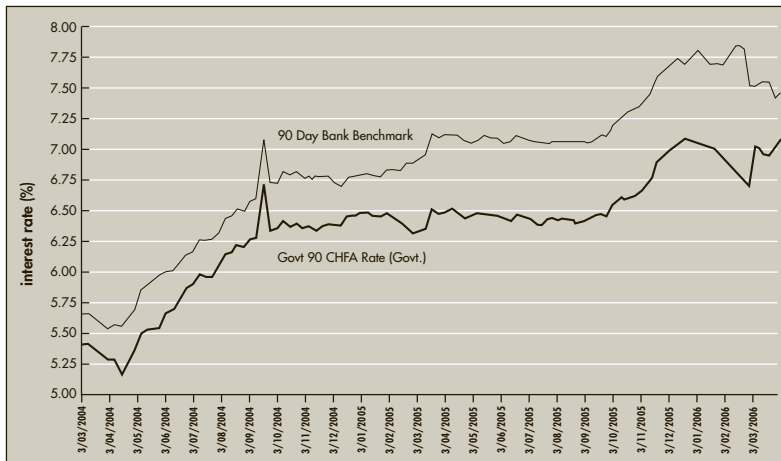


Figure 2: Cost of Finance – 90 day bank benchmark rate v CHFA rate



PROTECTING THE QUALITY OF LOANS

Performance monitoring: The CHFA monitors the financial well-being of DHBs to:

- protect the value of loans
- inform independent advice to key stakeholders
- maintain affordable debt levels and capital investment.

We monitor aggregate sector, individual DHB, and specific investment project performance.

On-going monitoring is supported by DHB financial reporting and regular loan reviews, with performance analysed through our financial models.

Our monitoring reports assess the ability of DHBs to service loans, identify trends in financial health, and provide comparisons of DHB performance.

Loan reviews protect the value of CHFA loans by assessing the ability of the DHB to achieve planned financial performance, and provide confidence in the ability of the DHB to meet debt obligations in the future.

The financial condition rating is based on the ability of individual DHBs and the sector to:

- meet interest costs using funds generated from operations
- appropriately structure their balance sheets
- meet all operating costs and costs of capital
- contribute to capital expenditure from internally generated funds.

DHBs are required to maintain compliance with our lending covenants over an annual period. Where a DHB is at risk of a covenant breach, we will work with them to identify opportunities to improve financial performance.

For the 3 year period to June 2009 we expect DHB performance to be managed within the following loan covenants (please refer to table over):

Forecast financial performance:
The CHFA uses monthly DHB reports and emerging performance trends to provide early warning signals of sector performance to assist the sector to achieve financial targets.

We are continually examining opportunities to strengthen our ability to measure financial performance and enhance the quality of our analysis and reporting.

FINANCIAL RATIO	DESCRIPTION	CHFA COVENANT TARGET
(i) Total Debt (including overdraft and finance leases), to total debt plus equity ratio.	A leverage ratio indicating the extent to which a DHB is financed by debt or Crown equity.	Not to exceed agreed Covenant level, with the CHFA maximum standard criteria currently set at 65%.
(ii) Interest cover i.e. earnings before interest and depreciation but after capital charge, (EBID) to interest.	The EBID ratio identifies the ability of the DHB to service interest charges. The ratio provides a cash-flow focus, after removing non-cash items such as depreciation.	Not less than the agreed covenant level, with the CHFA minimum criteria set at 2.5 times cover.
(iii) Cash flow Ratio (used on an exceptions basis).	The cash flow ratio identifies if a DHB has cash left after funding operating activities. It also takes into account provisions for some non-operating items.	Not less than the agreed covenant level. The standard CHFA criteria is for Net Cash Flow to be greater than or equal to zero.

1.2 opportunities and challenges

FINANCING

Products: We will continue to work with the NZDMO and DHBs to identify opportunities to increase the flexibility of our lending facilities, and to develop new financial products to assist DHBs to manage their cash flows and interest rate risks.

Investment finance: DHBs prioritise capital investments within a fixed capital budget. Priority is given to clinical-need business cases, with lower priority investment being delayed or financed off DHB balance sheets (e.g. leasing). The limited capital for efficiency-based investment proposals can lead to a

transfer of value from the government to the private sector. This presents opportunities for the CHFA to assist DHBs to identify the most efficient sources of non-Government finance.

Debt amortisation: DHBs are generally not repaying term debt. This results in low DHB contributions to asset replacement and higher contributions by the Crown. The CHFA will work with the sector to implement a feasible policy of scheduled debt amortisation to support long-term investment sustainability.

Conflicts of Interest between lending and financial advisory: Potential (but unlikely) conflicts of interest could arise from (i) the CHFA providing financial advice to DHBs and also providing lending to capital investment proposals, and (ii) the CHFA acting as an agent of the Minister and acting as an agent of a DHB.

The CHFA actively manages these potential risks by maintaining an appropriate segregation of duties among staff providing advice and lending services. Where a potential conflict exists, the CHFA will ensure that the Minister is advised of steps taken by the CHFA to manage the risk.

PROTECTING THE QUALITY OF LOANS

The sector is currently performing favourably to plan at a consolidated level; however there are potential issues that could put financial performance at risk over the next three years. Any deterioration may impact on the ability of DHBs to meet loan obligations and sustain capital investment.

Funding growth: Total vote health funding has increased at an average of 7.9% per annum from 2001/02

to 2005/06 – a rate of 5.4% above the average CPI Inflation of 2.5% for the same period. In 2005/06, total budgeted health expenditure was 90% greater than 1995/96. Health expenses as a percentage of GDP are forecast to increase from 5.7% to 6.2% between 2000/01 and 2005/06.

Health spending as a proportion of core Government expenses is forecast to increase from 18.2% in 2000/01 to 20% by 2005/06⁴.

Additional funding has offset cost growth in the sector, potentially masking underlying cost pressures in particular escalating personnel/ labour costs (please refer to figure 3).

Personnel costs: Of all DHB costs, personnel costs have increased the greatest in absolute terms over the last four years (please refer to figure 4). Total DHB personnel costs increased by an average of 7.5% per annum from 2001/02 to 2004/05 – a rate of 5.4% above the labour cost index for the same period. In 2004/05, total personnel costs were 22.6% greater than 2001/02.

In order to maintain financial performance, the sector needs to focus on cost control and implement opportunities to achieve savings. The CHFA will focus on improving our monitoring and advice to identify financial risks and opportunities to achieve immediate and ongoing savings.

Figure 3: Cumulative DHB Funding Growth Since 2001/02

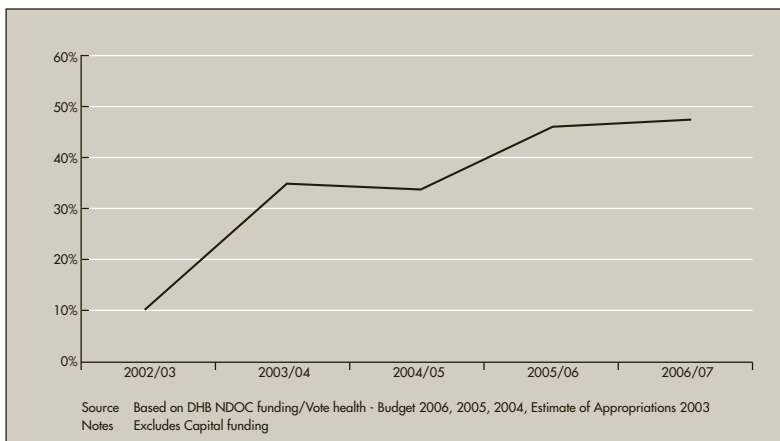
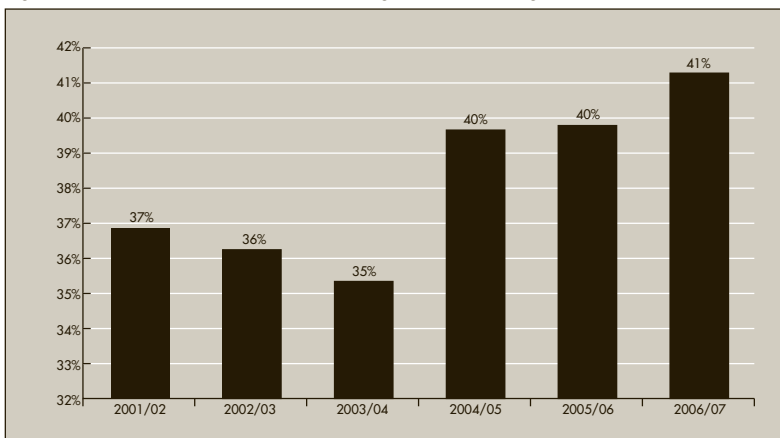


Figure 4: DHB Personnel Costs as a Percentage of DHB Funding



⁴ Source: The Treasury - Budget Economic and Fiscal Update 2005

1.3 our results contribution

	MEDIUM TERM PRIORITIES	BY JUNE 30 2009
1.1	Expand our range of financial products and advice to better meet DHB needs.	Reduce total DHB lease finance costs by introducing an alternative and competitive CHFA lease financing product. Identify alternative financing and ownership arrangements for a range of assets classes to achieve savings for DHBs.
1.2	Expand the coverage of our advice in terms of interest rate risks.	Reduce DHB exposure to cash flow and interest rate risks by expanding financial advice regarding usage of financial derivatives ⁵ and DHB treasury policy.
1.3	Enhance financial disciplines.	Enhance existing lending disciplines including a review of our lending covenants, sector balance sheet structures, and loan amortisation to improve asset provisioning by DHBs.

1.4 maintaining and developing capability

Achieving this result will continue to require a balance of health sector and financing expertise.

Our priorities are to ensure:

- we have the financial and health sector capability to interact effectively with DHBs
- we develop a capability to provide advice on managing DHB interest rate risks
- we are able to analyse sector financial needs to identify suitable financial products that fit DHB business needs
- we retain staff with financial experience for our monitoring and lending functions
- we integrate our practical experience in the health sector with generic financial disciplines to influence the performance of the system
- we develop our performance monitoring to enhance understanding of the drivers of financial performance
- we work with the Ministry of Health and the Treasury to strengthen the linkages between our financial and policy advice.

⁵ Financial derivatives refer to financial contracts that assist an organisation to hedge or manage their cash flow risks associated with fluctuations in interest rates.

2.0 independent advice improves financial disciplines and DHB performance

THE CHFA CONTRIBUTES BY

Advice to clients

- *Financial and property advice and services contribute to achieving DHB objectives:* DHBs receive financial and property services and advice that enhances their financial and operational well-being and assists in achieving their business objectives.

Independent advice to Ministers and stakeholders

- *Oversight and management of financial risk:* Ministers receive frank, timely, accurate and independent advice on the credit worthiness and financial sustainability of the sector. This includes early warning of perceived financial risks and where appropriate, plans to manage those risks.
- *Improved understanding of sector financial performance:* Key decision makers receive timely reports that enhance their understanding of the financial performance of the sector.

WITH OUTPUTS DELIVERED THROUGH

- lending services
- property services
- financial advisory services.

AND WORKING IN ASSOCIATION WITH

- *DHBs:* DHBs are autonomous and independently responsible for their own financial performance. DHBs will decide whether to adopt our advice and recommendations. We are reliant on our ongoing relationship with DHBs to provide advice on key issues in the sector.
- *Ministry of Health:* The Ministry's role in terms of improving DHB financial performance includes (but is not limited to) monitoring the financial and non-financial performance of the health system and individual DHBs against the objectives agreed with Government. The Ministry plans and maintains nationwide frameworks and specifications for services. This includes an overview of nationwide planning for capital development.
- *The Treasury:* The Treasury also monitor and advise on the performance of the health sector, and have a significant involvement in reviewing operating and investment performance.
- *Office of Treaty Settlements (OTS) and Te Puni Kokiri (TPK):* OTS and TPK are responsible for managing the Crown's Maori Protection Mechanism and Sites of Significance processes when DHBs wish to dispose of surplus properties.

FINANCIAL ADVICE

The CHFA's financial advice contributes to achieving DHB efficiency and cost-effectiveness objectives. DHBs are able to access our financial advice to enhance their financial and operational well-being.

PROPERTY ADVICE

The CHFA property disposal services and strategic advice assists DHBs to efficiently dispose of surplus properties to achieve a more productive property estate. Our property advice adds value to the marketability of each property and to the disposal process through

minimising delays associated with the land disposal process.

The property disposal service allows DHBs to sell properties to the CHFA and release capital for immediate reinvestment in more productive assets. Capital proceeds are maximised by achieving high sale prices and reducing disposal costs.

We also offer specialist property advice to DHBs who do not have access to in-house expertise. Our advice assists DHBs to achieve cost effective property solutions including ownership, management, occupation and use of properties.

It is not mandatory for DHBs to use our property services. Our property services compete on the basis of our experience in the health sector and understanding of their estate needs.

INDEPENDENT ADVICE TO STAKEHOLDERS

The CHFA is an independent advisor to the Minister of Health and Minister of Finance on the financial sustainability of the sector. Our advice enhances the awareness and understanding of potential operating risks and the required financial disciplines that influence sector performance.

2.1 measuring and evaluating sector results

FINANCIAL ADVICE

The performance of our financial advice is measured on a project basis and reported quarterly. For each project the CHFA estimates the resulting savings or gains in cost effectiveness (where appropriate).

During 2005/06 the CHFA provided a range of financial advice. For example, in 2005/06 we advised Waikato DHB on the ownership and financing options for a car park on their Hamilton site. Our analysis identified a range of options to maximise the value of the investment to the DHB.

PROPERTY ADVICE AND SERVICES

The performance of our property services is measured on an individual project basis against

the client's business objectives and is reported on a quarterly basis.

Since December 2001, the CHFA has disposed of \$17.6m of surplus DHB property, either through purchasing and on selling the property, or by the CHFA acting on behalf of the DHB. A further \$14.7m of property has been purchased by the CHFA and is currently being cleared for resale.

For property disposal projects, the CHFA quantifies the holding and processing costs, final sales price, and the total capital returned to the DHB. The performance of property advisory services is measured following the implementation of our advice based on the gains in cost effectiveness.

INDEPENDENT ADVICE ON THE FINANCIAL PERFORMANCE OF THE SECTOR

Monitoring of DHB financial performance against our lending covenants informs advice to Responsible Ministers and key stakeholders. Regular advice is provided through our quarterly report and as required for specific issues.

Our reports and advice are provided to enhance understanding of the drivers of DHB financial performance.

The performance of our advice can be measured by the accuracy of our reporting and through feedback from stakeholders (based on completeness, accuracy and stakeholder satisfaction).

2.2 opportunities and challenges

16

FINANCIAL ADVICE

DHBs seek our advice when accessing Government finance. In this capacity we advise individual DHBs and the National Capital Committee. Our generic financial advice and expertise can be applied to both public and private source of finance to achieve more efficient financing decisions (e.g. DHB car parking buildings) and reduce interest rate risks.

There are opportunities to engage earlier with DHBs in the development of business cases, and to work more closely with DHB financial forums to provide independent advice on a range of financing issues.

PROPERTY ADVICE AND SERVICES

Availability of surplus property:

The CHFA is currently negotiating with three DHBs to purchase surplus property with an estimated value of \$9.75m. Previous consultation identified that DHBs have a number of properties that may in future be declared surplus. These properties are likely to be of less significant size and value, with more significant properties likely to be identified following hospital redevelopments.

FUTURE PROPERTIES

Disposal challenges: Compliance with the transfer and protection mechanisms is a key challenge to the disposal process. Processing delays increase property holding costs and diminish the capital available for reinvestment. The CHFA will continue to work with Te Puni Kokiri and the Office of Treaty Settlements to streamline disposal processes.

The disposal of surplus properties is becoming increasingly difficult. Due to the specific location, size and other characteristics, future surplus properties may also be of a 'less saleable' nature (with premium surplus properties having previously been identified or disposed of).

In addition, significant gaps in the ownership history of properties and changes in the state of the real estate market will continue to add further complexity to the disposal of property.

Property acquisition and planning: There is significant opportunity to promote the use of our property expertise to advise DHBs on future planning, sale, and acquisition of property.

INDEPENDENT ADVICE TO MINISTERS AND STAKEHOLDERS

Understanding DHB performance:

To provide early warning of perceived financial risks it is important that we continue to expand our understanding of the drivers of DHB performance. This includes maintaining a sound understanding of sector risks, funding policies, contracting arrangements, and DHB cost structures.

2.3 our results contribution

	MEDIUM TERM PRIORITIES	BY JUNE 30 2009
2.1	Complete the disposal transactions of existing holdings of surplus properties.	Disposal of existing property holdings releases \$14m for reinvestment by DHBs and the CHFA. Sales prices and holding costs will meet the budgeted targets for each property.
2.2	Continue to provide DHB property advice and services that release further capital or improve the cost effectiveness of DHB property decisions.	Further property disposal transactions release \$9m of capital for reinvestment by DHBs and the CHFA. Other property advice will improve the cost-effectiveness of DHB property decisions as measured against the DHBs' status quo property arrangements.
2.3	Continue to provide financial advice to DHBs to assist in meeting their business objectives.	Advisory projects successfully achieve the desired outcomes as agreed with the DHB. Examples of outcomes include improved financial management, cost savings, or more cost effective financing decisions.
2.4	Enhance our analysis of sector trends and financial forecasting to deliver forewarning of significant sector risks and opportunities.	Ministers have access to regular reports that provide forewarning of significant risks and opportunities to achieving financial targets. Stakeholders receive relevant, informed and timely reports on key financing issues that impact on sector financial performance. Ministers and stakeholders are satisfied with the completeness and quality of our financial advice as determined by regular feedback from Ministers and stakeholders.

2.4 maintaining and developing capability

Achieving this result will continue to require capability in financing, property, and health sector experience. Our priorities are to ensure:

- we have financial expertise and awareness of DHB business needs to deliver credible advice and services to DHBs and participate constructively to the debate on achieving DHB financial sustainability
- we enhance our understanding of the drivers of DHB performance and our capability to advise DHBs and stakeholders
- we retain commercial expertise to deliver effective property solutions and advice that meet DHB service and business needs
- we develop our capability to work with other Government agencies to increase the efficiency of statutory property disposal processes
- we develop our capability to focus on 'big picture' sector issues to inform advice to stakeholders.

3.0 partnership and collective activity improves DHB cost effectiveness

THE CHFA CONTRIBUTES BY

- *Partnering with DHBs will assist in achieving cost effectiveness:* Through establishing partnerships and collective activity, the CHFA, DHBNZ and individual DHBs focus on identifying opportunities to achieve cost savings that sustain and improve financial performance.
- *The relationship between CHFA and DHBs supports knowledge and information sharing which improves DHB performance:* Enhanced sector relationships will support information sharing, and provide opportunities to identify best practice and improve DHB performance.

WITH OUTPUTS DELIVERED THROUGH

- lending services
- financial advisory services.

AND WORKING IN ASSOCIATION WITH

- *DHBs, DHBNZ:* The CHFA work in partnership with DHBs and existing networks (including regional and national forums) to identify and establish collaborative initiatives.
- *The Ministry of Health:* The Ministry is responsible for monitoring collaborative initiatives in the sector.

We have previously signaled our willingness to work in partnership with DHBs and DHBNZ to assist them to achieve their business goals. The CHFA offers financial and analytical support to DHB initiatives, efficiency projects and the development and implementation of collaborative initiatives.

PARTNERSHIPS AND COLLECTIVE DHB ACTIVITY

Partnership with DHBNZ: There is strong alignment between DHBNZ and the CHFA to see DHBs improve performance through collective activity. Recognizing this alignment, DHBNZ and CHFA have agreed to a Memorandum of Understanding to support the relationship and shared understanding⁶.

The CHFA is interested in building relationships with the DHB sector and participating in initiatives that deliver cost savings to the sector. CHFA is in a position to work with DHBNZ to support and participate in sector-wide projects.

These projects also assist the CHFA to enhance skills, knowledge, and capability to deliver well-informed independent advice.

The CHFA and DHBNZ prioritise projects in consultation with DHBs to identify projects that offer returns to the sector in terms of potential savings and/or added value, and where the sector has signaled a readiness and willingness to participate in the project. Projects commonly involve encouraging collective procurement and information sharing.

⁶ Memorandum of Understanding between the Residual Health Management Unit and DHBNZ (2004).

Partnership with DHBs: DHBs also directly engage the CHFA to access advice and support for individual or cross-DHB projects. Such projects commonly lead to lending solutions, efficiency gains, or information sharing aimed at achieving improved cost effectiveness. These projects are commonly initiated by the DHB, and reflect their current priorities, and the challenges and opportunities that they face in achieving their financial objectives.

To date, DHBs have been successful in establishing collective projects including shared services and buying groups. Through building on existing relationships and partnerships, there is potential to fully utilise their strong bargaining position.

KNOWLEDGE AND INFORMATION SHARING

The CHFA has identified the need for greater information sharing on supplier performance and pricing to reduce variation across the DHB sector.

We are keen to assist DHBs to establish protocols to promote information sharing on products, services, prices and supply sources to support price benchmarking and greater collaboration. We will work with DHBNZ and the Ministry of Health to ensure alignment between the various 'benchmarking-type' work streams.

3.1 measuring and evaluating sector results

PARTNERSHIPS AND COLLECTIVE DHB ACTIVITY

During 2005/06 the CHFA actively pursued opportunities to assist DHBs to achieve greater efficiencies in procurement. For example the CHFA provided analysis of potential savings in vehicle fleet ownership, management, procurement, disposal and financing. The CHFA is also providing project management resource to DHBNZ's 'value from insurance' collective risk management project aimed at improving the efficiency and cost effectiveness of risk management and insurance in the sector.

For each project the CHFA sets measurable performance targets in terms of cost savings, effectiveness, quality and timeliness to evaluate success in meeting project objectives. In implementing the managing for results framework, the CHFA will focus on developing processes to enhance our capability to identify and monitor the effectiveness of projects over the next 3 years.

KNOWLEDGE AND INFORMATION SHARING

The performance of information-sharing activity can be measured through monitoring the ongoing cost and price savings that are achieved through more structured information sharing arrangements and improved contracting practices.

3.2 opportunities and challenges

20

PARTNERSHIPS AND COLLECTIVE DHB ACTIVITY

The identification and prioritisation of opportunities for collective projects with DHBNZ will be managed through their Service Framework Group. In the medium term, the CHFA will continue to work with DHBNZ to continue and build on existing projects.

In addition, the CHFA will work directly with DHBs where appropriate to identify opportunities for the CHFA to provide analytical support to achieve projects that DHBs identify as priorities to their work programme.

The most significant challenge in establishing collective activity is achieving shared understanding of the costs and benefits (and respective allocation) and gaining credible support to achieve the savings in the short term.

A common challenge is that coordinated buying groups can struggle to develop specifications that address all of the needs and wants of all DHB members. Similarly there are situations for some goods and services where a 'one-size-fits-all' approach is not appropriate, and the benefits of collaborative purchasing may be outweighed by the increased costs associated with coordination and inflexibility. In such situations it is important to recognise a range of coordination options to achieve savings.

Other challenges associated with establishing DHB buying groups include losing local responsiveness to DHB needs, and potential for disproportionate allocation of benefits and costs associated with the collaborative purchasing ventures.

KNOWLEDGE AND INFORMATION SHARING

At present there are limited mechanisms to allow DHBs to share information on supplier performance. This may result in duplication of research costs, multiple assessments of the same supplier, and limited knowledge of supplier capability.

To support greater collaborative purchasing, DHBs could develop protocols for sharing supplier performance information and identify opportunities to develop common information collection standards.

3.3 our results contribution

	MEDIUM TERM PRIORITIES	BY JUNE 30 2009
3.1	Develop a procurement strategy for non-Pharmac ⁷ consumable goods.	Work in partnership with DHBs, DHBNZ and other sector stakeholders to develop a procurement strategy for non-Pharmac consumable goods. The strategy will identify opportunities, and provide structure and direction for future collective procurement initiatives.
3.2	Continue to project manage the implementation of the DHBNZ 'value from insurance' project.	Continue to work with DHBNZ to implement any future phases of the 'Value from Insurance' project and subsequent enterprise risk management projects (e.g. DHB captive). The initial insurance project will achieve cost savings of greater than \$3m, and more efficient insurance coverage and risk management (measured against previous policy coverage).
3.3	Develop a fleet management strategy for DHB vehicle fleets.	Develop a fleet management strategy for vehicle ownership, management, procurement, disposal and financing which achieves ongoing savings of greater than \$1m per annum.
3.4	Encourage information sharing on supplier performance.	Information sharing protocols are developed in partnership with DHBs which increases the transparency of supplier performance and contract prices.

3.4 maintaining and developing capability

Achieving this result will require developing our ability to identify opportunities in the sector and our capability to assist DHBs to implement projects. Our priorities are to ensure:

- we continue to strengthen our relationships and networks in the DHB sector
- we are able to analyse sector needs and opportunities and to develop solutions that meet DHB business objectives
- we have analytical capability and capacity to assist DHBs to implement initiatives
- we develop our working relationship with existing DHB groups to support the implementation of initiatives.

As a small organisation of 8 full time staff we are constrained in the number of activities that we can participate in at any one time. This constraint will require ongoing prioritisation of projects to ensure the most effective use of our resources. To maintain our capability, we also need to carefully manage appropriate succession planning for core roles.

⁷ Pharmac is responsible for managing Government expenditure on pharmaceuticals, purchasing hospital pharmaceuticals on behalf of DHBs, therapeutic devices and some related consumables.

4.0 efficient management of residual AHB assets and liabilities

In addition to the three key result areas, the CHFA is responsible for achieving the Government's objective of efficiently managing claims against the former Area Health Boards, and other residual assets and liabilities to minimise the total cost to the Crown.

The CHFA is responsible for:

- *Residual Contingent Liabilities:* As the legal successor to the former Area Health Boards (AHBs), the CHFA manages claims arising from acts or omissions of the former AHBs pre-1993 to achieve timely and appropriate compromise, settlement or defence of the claims.

- *Residual Property Liabilities:* The CHFA manages the sub-letting of the residual lease on Tourism and Travel House (Wellington) to reduce the overall cost to Government.
- *Residual Assets (Patient Trust Funds):* The CHFA is the constructive trustee of some Southland DHB unclaimed patient funds pre 1993.

4.1 measuring and evaluating sector results

RESIDUAL CONTINGENT LIABILITIES

In managing contingent liabilities the CHFA is responsible for settling proven claims at the lowest possible cost to the Crown and in such a way as to manage the risk of creating a precedent for other litigation.

Some 370 claims or notifications have been vested in the CHFA since establishment. Many of these were subsequently confirmed by the instigation of legal action against the Crown during the earlier years of our operation. The CHFA continues to receive claims relating to pre-1993 including the Greenlane Heart Library and the psychiatric hospital patients' claims. As at 31 March 2006, the number of active claims has been reduced to three. The CHFA monitors and reports annually on the total cost of claims settled. The total costs include legal costs, administration and compensation to claimants.

RESIDUAL PROPERTY LIABILITIES

At establishment in 1993, the CHFA assumed responsibility for two long-term property leases.

The residual lease for Tourism and Travel House (Wellington) remains under our management until 2012. As at 31 March 2006, 100% of the lease space has been sublet, and we hold verbal or written agreement to subleasing 62% of the total lease space through to the expiry of our lease. The CHFA monitors the total cost to the Crown on an annual basis and comparative lease rates.

RESIDUAL ASSETS: PATIENT TRUST FUNDS

In April 2001, the Minister of Health assigned to the CHFA the function of being the constructive trustee of some Southland DHB unclaimed patient funds accumulated prior to 30 June 1993, pending the determination of disposal. The CHFA manages the trust funds to protect and increase the total capital.

With the accumulation of interest, the Southland DHB unclaimed patient fund stands at \$0.49 million. The Public Trustee was requested by the Solicitor-General in 2002 to determine an appropriate scheme for these funds. Southland DHB and the Public Trustee are currently agreeing the terms of an appropriate Trust Deed.

4.2 opportunities and challenges

By 30 June 2006, the only Residual functions managed by the CHFA will be those relating to the management of the head lease at Tourism and Travel House and the residual claims portfolio.

The number of active claims has been reduced to the psychiatric hospitals and Greenlane heart library claims filed late in 2004. Initial discussions have been held with the Ministry of Health in respect of the future management of the claims portfolio.

4.3 our results contribution

	MEDIUM TERM PRIORITIES	BY JUNE 30 2009
4.1	Proactively effect the settlement of residual claims.	Resolve all three of the existing active residual claims.
4.2	Prudently manage and invest Southland DHB patient trust funds.	All unclaimed Southland Patient Trust funds are transferred to an approved scheme by July 2007.
4.3	Proactively manage the tenancy risk at Tourism and Travel House.	Renegotiate lease agreements through to 2012 for 100% of tenancies to reduce the total lease risk to the Crown. The cost to the Crown is less than 20% of the total head lease and operating costs.

4.4 maintaining and developing capability

To achieve this objective we will need to access additional funding to defend and settle claims against the Crown. The CHFA has had the ability to fund the cost of defending claims from our reserves.

However our reserves will be depleted during the 2007/08 year and it is anticipated that based on information currently available, additional funding will be required at that time.

part two: forecast statement of service performance – 2006/07

24

OUTPUT CLASS NAME	VALUE 2006/07 (\$000 GST EXCL.)		
	(1) LENDING	(2) PROPERTY	(3) FINANCIAL SERVICES
Appropriation	965	0	706
Other Income	69	315	172
Total Income	1,034	315	878
Operating expenditure	915	228	2,501
Surplus/(Deficit) ¹	119	87	(1,623)

This section of the Statement of Intent outlines the financial and non-financial measures and standards that we aim to achieve for 2006/07 and which contribute to achieving our results.

Note (1): The deficit in the Financial Services output class relates to costs of specific residual functions and a shortfall in Appropriation below CHFA's baseline funding level.

This deficit is currently funded from CHFA equity subject to agreement with the Ministry of Health.

1.0 output class one: lending services

1.1 background

The CHFA is the lender to the DHB sector and provides a range of term loan facilities similar to those available from private banks. Loans are provided to refinance existing private sector debt or to finance new capital investments.

As at 31 March 2006, the CHFA has established lending relationships with all 21 DHBs. At the same date, loan approvals amounted to \$1,432m. The CHFA is forecasting its loan portfolio to increase to \$1,545m by June 2008.

1.2 organisational responsibilities

The Terms of Reference require the CHFA to approach its lending responsibilities "applying normally accepted lending criteria" recognising that DHBs are "required to operate on a sustainable financial basis whilst delivering a high standard of services" and are "taking all appropriate steps within their control to achieve and sustain this condition". The specific responsibilities of the CHFA are to:

- provide term loans to DHBs and other clients in the health sector through the provision of a range of financing products.
- assess DHB credit worthiness utilising normally accepted lending practices.
- provide appropriate lending advice.
- report to the Ministers of Health and Finance on the credit worthiness and financial sustainability of DHBs from an independent lender's point of view and provide early warning of perceived financial risks and mitigation strategies.
- protect the value of the loans and manage risks.
- support the Crown's objective of providing Crown sourced term debt to DHBs. To this end the CHFA is to manage the process of the conversion of existing private sector term debt into public sector debt; overall relationship with the private sector banks; lending of Crown term debt to DHBs; and risks associated with Loans to the DHBs.
- administer loans on behalf of the Crown as instructed by the Responsible Ministers.

1.3 output performance (including results contribution)

This class of outputs involves provision of term debt facilities, monitoring of DHB performance, and provision of independent

financial advice. The output class contributes to achieving all three of our key result areas (please refer to table on page 26).

2006/07 performance measures: lending services

26

LINK TO KEY RESULTS		DESCRIPTION	STANDARD AND PERFORMANCE TARGET
Financing	CHFA financial products meet DHB needs.	Refinance of existing CHFA loans and private debt.	(1.1) All loan terms and condition are agreed with the DHB 30 days prior to the expiry date of an existing facility.
		Provide long-term finance for new capital projects.	(1.2) For new loan facilities, all terms, and conditions are negotiated with the DHB within 90 days of the loan being approved by the CHFA. The DHB is able to draw down the loan on the requested date.
		Meet DHB long-term financing needs.	(1.3) DHBs are satisfied with our lending products and administrative performance as demonstrated by an annual survey of DHB opinion.
Protecting the quality of loans	Monitoring of DHB financial performance protects loan quality.	Monitor and report on the credit worthiness and financial sustainability of DHBs against normally accepted lending practices.	(1.4) Loan quality is demonstrated by DHBs successfully meeting the CHFA lending covenants with no defaults on interest payments. (1.5) Loan quality and credit assessment is monitored through the loan application process, annual loan review and monthly monitoring of covenants. (1.6) Monthly monitoring of loan covenants and conditions identifies covenant breaches or loan quality risks. Covenant breaches are reported to the CHFA Board with recommendation for action to protect loan quality on a quarterly (or exception) basis.
Independent advice to Ministers and stakeholders	Oversight and management of financial risk.	Provide early warnings of perceived financial risks and plans to manage those risks.	(1.7) Ministers are provided with timely reports on a quarterly basis. Other ad hoc advice will be delivered within agreed timeframes. (1.8) The Minister will be formally requested on a regular basis to indicate his level of satisfaction with the overall quality of the advisory outputs produced.
	Improved understanding of sector financial performance.	Key decision makers receive timely reports that enhance their understanding of financial performance.	(1.9) Stakeholders receive timely and accurate advice within agreed timeframes.
Advice to DHBs	Financial advice contributes to achieving DHB objectives.	DHBs receive financial advice that enhances their financial and operational well-being and assists in achieving their business objectives.	(1.10) DHBs receive timely and accurate advice within agreed timeframes. (1.11) DHBs will be formally requested on a regular basis to indicate their level of satisfaction with the overall quality of the advisory outputs produced.

2.0 output class two: property advice and disposal services

2.1 background

27

The CHFA assists health sector clients with the disposal of surplus property assets, and offers strategic property advice intended to maximise the use of existing DHB land holdings, and to plan future DHB property needs.

The property unit is focused on the effective and efficient disposal of properties declared surplus within an overall objective of maximising the return to the health sector. It also offers strategic property advice covering acquisition, development

(including physical works and subdivisions), leasing, site planning, construction, and use of property holdings.

The property function is required to achieve a break-even financial result. Funding is provided by way of risk sharing with clients in the disposal process, income earned from the provision of advisory and agency services, and capital funding through a revolving line of credit provided by Westpac Banking Corporation.

2.2 organisational responsibilities

The CHFA provides strategic property advice to health sector clients and offers a property disposal service which may be on the basis of:

- *Purchase of client property:* The purchase and disposal of surplus health sector properties.
- *Property disposal:* The provision of advice to health sector clients on the disposal of surplus properties.
- *Other property advice:* The provision of strategic advice in relation to the ownership, management, occupation and use of properties.

2.3 output performance

Contribution to results: Clients receive well founded and independent property-related services and advice that enhances their financial and operational well-being and assists in achieving their business objectives.

2006/07 performance measures: property advice and disposal services

28

LINK TO KEY RESULTS		DESCRIPTION	STANDARD AND PERFORMANCE TARGET
Advice to Clients	Property advice contributes to achieving health sector objectives and financial performance.	Property disposal service.	<p>(2.1) Total holding and disposal costs are maintained within budgeted targets as agreed for each property.</p> <p>(2.2) All transactions comply with legislative and legal requirements as assessed through independent due diligence audits.</p> <p>(2.3) Properties are disposed within the timeframes agreed with the DHB.</p>
		Property advice.	<p>(2.4) Property advice assists DHBs and other health sector clients to identify opportunities to achieve a more efficient property estate by achieving cost savings and/or cost effectiveness gains as measured against status quo property arrangements.</p> <p>(2.5) Clients receive timely and accurate advice within agreed timeframes.</p> <p>(2.6) Clients will be formally requested on a regular basis to indicate their level of satisfaction with the overall quality of the advisory outputs produced.</p>

3.0 output class three: financial services

3.1 background

When established in 1993, the CHFA assumed a number of statutory functions. At the time there was an expectation that these functions would all be of a relatively short duration. In the event, some of the functions involved have proven to be

more complex and costly than originally envisaged; however, the CHFA continues to be responsible for them and their resolution. The CHFA also provides financial advisory services to DHBs.

3.2 organisational responsibilities

Residual Services: As the legal successor to the former Area Health Boards, the CHFA is responsible for managing all residual assets and liabilities of the former Area Health Boards vested in the CHFA including:

- *Residual contingent liabilities:* As at 31 March 2006, the number of active claims has been reduced to three. In managing these contingent liabilities, the CHFA is responsible for settling proven claims at the lowest possible cost to the Crown and in such a way as to manage the risk of creating a precedent for other litigation.

- *Residual assets (including property leases):* The CHFA is responsible for managing the residual long-term property lease for Tourism and Travel House (Wellington) until expiry in 2012.
- *Patient trust funds:* The CHFA is the constructive trustee of some Southland DHB unclaimed patient funds pre 1993.

Financial advisory services:
The CHFA also provides financial advisory services to DHBs to assist them to achieve their business goals and objectives.

3.3 output performance

Management of residual assets and liabilities: The provision of residual management services contributes to achieving the Government objective of efficiently managing down residual assets and liabilities in relation to the former Area Health Boards.

Financial advisory services:
The provision of financial advisory services contributes to achieving greater DHB collaboration and improving cost effectiveness.

2006/07 performance measures: financial services

30

LINK TO OBJECTIVES/ KEY RESULTS		DESCRIPTION	STANDARD AND PERFORMANCE TARGET
Residual AHB Assets and Liabilities	Efficient management of residual AHB assets and liabilities.	Residual Contingent Liabilities.	(3.1) Status of all contingent liabilities are reviewed quarterly to the board.
		Residual Property Liabilities (Tourism and Travel House).	(3.2) Sub-letting of Tourism and Travel House achieves recovery of 80% of total Crown costs of the head lease. (3.3) Agreements are in place by 30 June 2007 for sub-tenancies through to 2012 covering at least 50% of the total Crown costs.
		Residual Assets (Patient Trust Funds).	(3.4) Patient trust funds distributed by 30 June 2007. (3.5) Prudent investment and management increases total trust funds by 5% by 30 June 2007.
Advice to DHBs	Partnership and collective activity improves DHB cost effectiveness.	CHFA partnerships with DHBs assist in achieving cost effectiveness.	(3.6) CHFA undertakes at least 2 efficiency-type projects in partnership with DHBs by 30 June 2007. (3.7) Terms of reference for each project will specify the cost savings and/or cost effectiveness targets and will be reported quarterly.
		Knowledge and information sharing.	(3.8) Potential opportunities for sharing procurement information and expertises are identified by 31 December 2006, with a project being accepted by a DHB by 30 June 2007.

4.0 organisational capability and development

Over the next 3 years we will develop our capability to manage for results and the required implications for planning, management and monitoring. To ensure that we attract and retain productive and talented staff to support achieving our results, we will implement our 'good employer' obligations and continue to promote equal employment opportunities.

MANAGING FOR RESULTS

In 2005/06 we adopted the 'managing for results framework' into our strategic planning processes. 2006/07 represents a continuation of our existing strategic direction, functions and responsibilities and we will continue to implement our strategic plan to achieve our key results covered in Part One, pages 6 to 23.

Adopting the management framework: In 2006/07 we will continue to implement the framework to cover the full management cycle including implementation, delivery and review – in particular we will update our planning and reporting processes to ensure that our monitoring and evaluation processes support achieving our key results.

By August 2006, we will have internal work plans for 2006/07 that identify the staff results to support our planning results, including appropriate milestones to support monitoring and performance reviews.

Monitoring performance: We are committed to monitoring and reviewing our performance continually. This will include seeking regular feedback from the Minister of Health and our clients to assess our ability to meet expectations.

Result indicators: The series of result indicators outlined on pages 6 to 23 will support monitoring progress towards achieving our key results. These indicators represent a starting point using currently available information – during 2006/07 we will enhance and develop the set of result indicators to support the evaluation of our performance.

Capability indicators: At present we undertake an annual survey of stakeholders/clients to seek feedback on our performance and to support us in assessing progress against our management objectives. We will also share good practice experience with like organisations. In 2006/07 we will continue to develop and improve our capability indicators and look for opportunities to share good practice experience with other organisations.

Our capability priorities for 2006/07 are to:

- invest in the capability of our people
- enhance the effectiveness of our services
- build on our existing relationships.

INVEST IN THE CAPABILITY OF OUR PEOPLE

Success in achieving our key results depends on maintaining and developing our people and making full use of their capabilities.

CHFA capability development is an ongoing priority. In 2006/07 we will:

- maintain financial and health sector capability to interact effectively with DHBs
- retain staff with financial experience for our monitoring and lending functions
- maintain financial expertise and awareness of DHB business needs to deliver credible advice and services to DHBs
- retain commercial expertise to deliver effective property solutions and advice that meet DHB service and business needs.

32

In 2006/07 we will undertake a review of our capability to identify specific gaps and will ensure that personal development plans are in place by August 2006 to address those gaps. During 2006/07 we will also develop a common approach to learning and development for the CHFA to ensure that development programs focus on enhancing employee knowledge in the areas of health sector issues, finance and financial services, property, and project management.

Development programs will also focus on developing leadership, communication and relationship management.

As a small organisation of 8 staff a key challenge is managing work scheduling, annual leave, succession planning and cover for core roles. As such, we are keen to recruit an additional full time staff member to support our existing functions, and to help us give effect to our strategic direction. This additional resource will be funded from within our existing appropriation.

ENHANCE THE EFFECTIVENESS OF OUR SERVICES.

The CHFA will maintain suitable quality control procedures including internal peer review, consultation and routine checks for compliance with CHFA procedures. All analysis and advice outputs will comply with the CHFA's quality standards.

2006/07 performance measures: organisational capability and development

DESCRIPTION	STANDARD AND PERFORMANCE TARGET
Managing for Results	<p>(4.1) Internal work and performance plans are in place by August 2006 and are consistent with CHFA key results, including appropriate milestones.</p> <p>(4.2) By 30 June 2007, new key result and capability indicators will be developed for implementation in 2007/08 to support monitoring of results.</p>
Invest in the capability of our people	<p>(4.3) Maintain low-staff turnover of no more than 1 person per annum.</p> <p>(4.4) Staff are positive about career opportunities, professional growth and job satisfaction as determined by an annual survey of the CHFA's work environment completed in December 2006.</p> <p>(4.5) Personal Development Plans are in place by August 2006 which are consistent with the CHFA key results and capability development needs.</p>
Enhancing our effectiveness	<p>(4.6) Internal/external audits reflect that policies, procedures and business systems are appropriate and being complied with at audit or following spot checks.</p> <p>(4.7) Average audit rating greater than 3 [acceptable] achieved following audit in October 2007.</p>

5.0 reporting

The following information will be provided to the Responsible Ministers and to the Ministry of Health

5.1 lending

Quarterly as at 30 June, 30 September, 31 December and 31 March, and within 45 business days of the end of each quarter, reports on the CHFA lending function, matching performance against the targets set. The quarterly report will encompass the following:

- current loan applications
- all loan approvals
- details of loan transactions to date

- general comment on CHFA's view as to the financial sustainability of DHBs, including where appropriate specific case-by-case comment
- where considered appropriate, alert Responsible Ministers to any emerging problems and/or risks (actual or potential) to the value of the Crown's Loans to Clients and advise of CHFA's plans to manage those risks.

On dates to be advised by Treasury, the CHFA will provide to the Ministry of Health and Treasury forecast cash flows relating to the Refinancing of DHB private sector debt and the rollover of CHFA loans on a monthly basis for the first two years and annually for the three out-years.

5.2 property

Quarterly as at 30 June, 30 September, 31 December and 31 March, and within 45 business days of the end of each quarter, reports on the property portfolio function matching performance against benchmark standards.

The quarterly report will encompass:

- property currently under negotiation for purchase by the CHFA
- property held by the CHFA identifying the estimated time of disposal for each property held
- estimated total realisable value for the property portfolio held by the CHFA

- property sold by the CHFA during the period and cumulatively since beginning the activity in terms of value and location
- details of any identified issues and risks
- the costs incurred in holding and selling the property
- details of Other Advisory Services provided.

5.3 financial services (including residual functions)

Quarterly as at 30 June, 30 September, 31 December, and 31 March, and within 45 business days of the end of each quarter, reports on:

- Contingent Liabilities - The status and estimated liability for damages or other monetary awards
- Residual Assets - The management status and plans for disposal of all assets vested in the CHFA
- Patient Trust Funds - The balance of funds held and current investment strategy
- Details of any Financial Advisory Services provided.

5.4 financial

By 31 May 2007, the CHFA will prepare and deliver to its Responsible Ministers, its draft Statement of Intent in accordance with the Crown Entities Act for the 2007-2008 year.

By 31 August 2007, the CHFA will have completed its annual accounts for external audit.

CHFA will supply the Ministry of Health and/or the NZDMO and/or the Treasury, as applicable, with:

- quarterly financial reports: consisting of consolidated statements of financial performance, financial position and contingent liabilities in an agreed form within 45 working days of the end of such quarter to which the report relates.
- summary financial information: in an agreed form for inclusion in the Crown's accounts as at 30 June in each year, no later than such dates as are specified by the Treasury.
- an annual report: in accordance with the Crown Entities Act or Public Finance Act (as applicable).

5.5 other

The CHFA will also provide:

- any information that the Responsible Ministers might request.
- a quarterly report to the Responsible Ministers on progress made towards achieving the performance measures noted in Section 4 of this Statement of Intent.
- a quarterly report to the Responsible Ministers on its strategic initiatives and/or DHB projects.

CROWN HEALTH FINANCING AGENCY - PROSPECTIVE FINANCIAL STATEMENTS

6.0 prospective financial statements for the year ending 30 june 2007

35

PROSPECTIVE INCOME STATEMENT (EXCL GST)	2006/07 Full Year \$000 Planned
Crown funding	1,671
Interest received	240
Total Revenue	1,911
Finance Costs	(30)
Other operating expenditure	(3,348)
Total Expenditure	(3,378)
Surplus/(Deficit) before Other Income and Expenses	(1,467)
Surplus/(Deficit) on property transactions	87
ROBOC Income	408
Depreciation	(38)
Total Other Income and Expenses	457
Surplus/(Deficit)	(1,010)

PROSPECTIVE STATEMENT OF CHANGES IN EQUITY (EXCL GST)	2006/07 Full Year \$000 Planned
Shareholders interest at start of period	6,894
Surplus/(Deficit) for the period	(1,010)
Transfers to MOH of ROBOC	(408)
Shareholders interest at end of period	5,476

CROWN HEALTH FINANCING AGENCY - PROSPECTIVE FINANCIAL STATEMENTS

36

PROSPECTIVE BALANCE SHEET (EXCL GST)	2006/07 Full Year \$000 Planned
Crown Equity	5,476
Current Assets:	
Bank	2,648
Contingent Liability Settlement Fund (CLSF)	2,856
Receivables	-
Prepayments	-
Properties intended for sale	12,382
	17,886
Current Liabilities:	
Creditors	272
Property Loans	12,382
	12,654
Net Working Capital	5,232
Non Current Assets :	
Fixed Assets	244
Advances to DHBs	1,213,140
	1,213,384
Non Current Liabilities:	
Advances from NZ Debt Management Office	1,213,140
Net Assets	5,476

CROWN HEALTH FINANCING AGENCY - PROSPECTIVE FINANCIAL STATEMENTS

37

PROSPECTIVE CASH FLOW STATEMENT (EXCL GST)	2006/07 Full Year \$000 Planned
Operating Cashflows	
Cash was provided from	
Crown Agencies and other income sources	2,829
Cash was provided to employees, suppliers	(4,181)
	(1,352)
Investing Cashflows	
Cash was provided from sale of assets	5,729
Cash was provided to purchase of assets	(3,885)
	1,844
Financing Cashflows	
Cash was provided from borrowings	3,840
Cash was provided to repayment of borrowings and distributions to Ministry	(5,429)
	(1,589)
Net increase/(decrease) in cash held	(1,097)
Add Opening cash balance	3,745
Closing Cash Balance	2,648
Made up from:	
Balance Sheet Cash	2,648

CROWN HEALTH FINANCING AGENCY - SIGNIFICANT ACCOUNTING POLICIES FOR THE YEAR ENDING 30 JUNE 2007

6.1 significant assumptions

38

6.1.1 PURPOSE

Purpose of statements

The prospective financial statements have been prepared for the purposes of reporting in the annual Statement of Intent and should not be relied on for any other purposes

6.1.2 BASIC ASSUMPTIONS

Bases of assumptions made, uncertainty and material effect

Certain assumptions in the preparation of the prospective statements have been made. These assumptions have been made to the best of our knowledge and based on best information available at the time. Were there is uncertainty and/or the potential for material effect on the prospective statements, further comment is made on these specific issues later in this section

6.1.3 FUNDING

Ministry of Health

The Ministry will provide funding of \$1.671m for the year ended 30 June 2007, to meet operating expenditure not funded from CHFA's equity reserves. The Ministry has confirmed funding at this level.

6.1.4 LENDING

DHB Loans

The budgeted loan balances at year end have a neutral effect in the Balance Sheet, being recognised as an asset in respect of the DHB loans and a liability in respect of Treasury advances. The interest paid and received is also neutral.

The timing of DHB draw downs is uncertain and values are based on the best estimate of anticipated draw downs.

6.1.5 SURPLUS DHB PROPERTY DISPOSAL

Financial Breakeven Objective

Anticipated property sales for the year are budgeted to make a surplus. However, uncertainty about unanticipated property transactions and timing of these transactions, together with a brought forward deficit position, is anticipated to negate this surplus, resulting in a breakeven position as required in accordance with the Property Disposal Terms of Reference.

6.1.6 CONTINGENT LIABILITIES SETTLEMENT FUND

Purpose of fund

The balance of this fund is held as a provision against claims covered in the Statement of Contingent Liabilities. In the event of such claims being paid, this fund would be reduced or exhausted. IF the funds are insufficient to meet costs awarded, CHFA will be reliant upon the Ministry of Health for further appropriation to settle the claims. Officials have been alerted accordingly.

6.1.7 CREDITORS AND DEBTORS

Creditors and Debtors have been budgeted as payable/receivable within 30 days.

6.2 statement of accounting policies

6.2.1 STATUTORY BASE

Pursuant to the Health Sector (Transfers) Amendment Act 2000, the Crown Health Financing Agency (CHFA) was established on 1 July 1993, continues under section 57 of the NZ Public Health and Disability Act 2000 and operates as an independent Crown agent for the purposes of the Crown Entities Act 2004.

With effect from 1 July 1993, CHFA assumed responsibility for all Area Health Board assets and liabilities that did not vest in District Health Boards (formerly Crown Health Enterprises) or other transferees. In addition CHFA manages lending to District Health Boards (DHBs) and provides assistance and advice to the sector in respect of property matters. Both activities are undertaken in accordance with the Terms of Reference approved by the Responsible Ministers.

The prospective financial statements have been prepared in accordance with part 4 of the Crown Entities Act 2004, the Public Finance Act 1989, and section 67 of the New Zealand Health and Disability Act 2000.

6.2.2 MEASUREMENT SYSTEM

Generally accepted accounting practices recognised as appropriate for the measurement and reporting of results and financial position on an historical cost basis has been followed.

Note, the financial reporting standard about preparing prospective financial statements (FRS-42) says that the (prospective) forecast

statements for an upcoming financial year should be prepared using the same standards as the statements at the end of that financial year.

The prospective (forecast) financial statements in this SOI have been prepared in accordance with NZ GAAP. However, from 1 July 2007 a new set of accounting standards will be used in New Zealand called the New Zealand Equivalents to International Financial Reporting Standards (NZIFRS). This means that the financial statements at the end of the financial years 2007/08 and 2008/09 will be prepared in accordance with the new NZIFRS but the prospective (forecast) statements in this document are prepared using the previous standards (NZ GAAP).

6.2.3 GOODS AND SERVICES TAX

The financial statements have been prepared exclusive of goods and services tax (GST), with the exception of accounts payable and accounts receivable, which are stated GST inclusive.

6.2.4 REVENUE RECOGNITION

Funding, interest and other revenue are recognised when earned and is reported in the financial period to which it relates.

6.2.5 INTEREST ON BORROWINGS

All interest costs have been accrued on a monthly basis.

6.2.6 TAXATION

CHFA is a public authority in terms of the Income Tax Act 1994 and consequently is exempt from income tax.

6.2.7 PROVISIONS

ROBOC: A provision for the distribution of receipts on behalf of the Crown is made on a monthly basis. Receipts on behalf of the Crown represent rental income from tenants of Tourism and Travel House. CHFA has a lease obligation for five floors of Tourism and Travel House until 2012. Space not occupied by CHFA is sub-leased with this rental being returned to the Crown.

6.2.8 INVESTMENTS

Investments are stated at the lower of cost and net realisable value.

6.2.9 FIXED ASSETS

All items of property, plant and equipment are initially recorded at cost and depreciated. Initial cost includes the purchase consideration and those costs directly attributable in bringing the asset to the location and condition necessary for its intended use.

6.2.10 DEPRECIATION

Depreciation is calculated on a straight-line basis to allocate the cost amount of an asset, less any residual value, over its useful life.

The estimated useful lives of property, plant and equipment are as follows:

- Leasehold improvements
12.5 years (8%)
- Plant and equipment
8.3 years (12%)
- Office equipment, furniture and fittings
2.8 – 3.6 years (28% - 36%)

6.2.11 ACCOUNTS RECEIVABLE

Accounts receivable are stated at expected realisable value after providing for doubtful and uncollectible debts.

6.2.12 STATEMENT OF CASH FLOWS

Cash is defined as cash balances on hand, held in bank accounts, demand deposits in which CHFA invests as part of its day-to-day cash management.

Cash flows are derived from:

- Operating activities, which includes cash received from all income sources of CHFA and records the cash payments made for the supply of goods and services.
- Investing activities are those activities that relate to the acquisition and disposal of non-current assets and money market investments.

- Financing activities comprise the change in equity and debt capital structure of CHFA.

6.2.13 FINANCIAL INSTRUMENTS

CHFA is party to financial instruments as part of its normal operations.

These financial instruments include bank accounts, short-term deposits, debtors, creditors and loans. All financial instruments are recognised in the prospective statement of financial position and all revenues and expenses in relation to financial instruments are recognised in the prospective statement of financial performance.

Except for loans, which are recorded at cost, and those items covered by a separate accounting policy, all financial instruments are shown at their estimated fair value.

As a guardian of public money, CHFA must be risk averse and seek to minimise exposure arising from its treasury activity. CHFA is not authorised to enter into any transaction that is speculative in nature.

6.2.14 PROPERTIES INTENDED FOR SALE

Property intended for sale is stated at acquired cost plus all recognised revenue and expenditure associated with that property. Revenue consists of rental income earned during the holding period. Expenditure relates to all holding costs e.g. maintenance, interest and rates etc.

When an unconditional contract for the sale of a property exists, and as soon as the total profit can be estimated reliably, the profit is recognised.

6.3 statement of commitments

Crown Health Financing Agency has the following commitments at 30 June 2007:

6.3.1 CAPITAL

Nil

6.3.2 OPERATING LEASE COMMITMENTS

Less than one year	459,000
One to two years	459,000
Two to five years	1,377,000
Over five years	115,000
	<u>2,410,000</u>

Operating lease commitments are in respect of the lease of five floors of Tourism and Travel House. The lease expires in 2012. This Statement of Commitments excludes cancellable contracts.

6.4 statement of contingent liabilities

Crown Law Office's estimate of CHFA's liability as at 30 June 2006 (based on claims received at that date) arising from legal proceedings and disputes by third parties, is

assessed at \$15,216,000. It should be noted however, that CHFA is aware that there are potentially further claims in respect of the past treatment of psychiatric patients.

