



PAXTON PARTNERS

CHILDREN'S HEALTH QUEENSLAND
FINANCIAL PERFORMANCE IMPROVEMENT REVIEW
FINAL REPORT

Children's Hospital Queensland – Financial performance improvement review

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Disclaimer

The information used in preparing this report was provided by Children's Health Queensland and the Queensland Department of Health.

We did not test or otherwise verify the actual source financial data used for any projection analysis presented in this report. As any projections, assumptions and estimates that relate to the future may be affected by unforeseen events, we express no opinion on the projections or how closely they will correspond with actual results or on the assumptions on which they were based. Furthermore, the scope of our work did not include procedures considered necessary under generally accepted auditing standards for the purpose of expressing an opinion on the projections. Accordingly, we do not express any such opinion.

This report is prepared solely for the purpose set out in the terms of reference of this engagement and is not to be used for any other purpose without Paxton Partners' prior written consent.

During the 2014/15 financial year, Children's Health Queensland (CHQ) went through a major transition to the new Lady Cilento Children's Hospital (LCCH) facilities. The relocation has required significant change management processes to consolidate services from the Royal Children's Hospital (RCH) and Mater Children's Hospital (MCH).

Paxton Partners have been appointed jointly by CHQ and Queensland Department of Health (QDOH) to provide an independent perspective on 2014/15 financial results, and the 2015/16 budget forecast to enable informed discussions on proposed actions to return the Hospital and Health Service (HHS) to a sustainable budgetary position in the short to medium term.

2014/15 Financial Performance

The scope of Paxton Partners review, which commenced in May 2015 included consideration of the likely 2014/15 end of year forecast. At the end of November 2014, prior to the December 2014 opening of LCCH, the CHQ entity had generated a \$7m surplus. However, by April 2015 the result had deteriorated to \$8.3m deficit and by June 2015, the end of year results was a \$17.1m deficit.

QDOH subsequently provided one-off assistance to the entity of \$10m (this was in addition to pre-existing transition grant funding of \$10.4m). With the inclusion of the additional grant, the end of year financial result was a \$7.13m entity deficit.

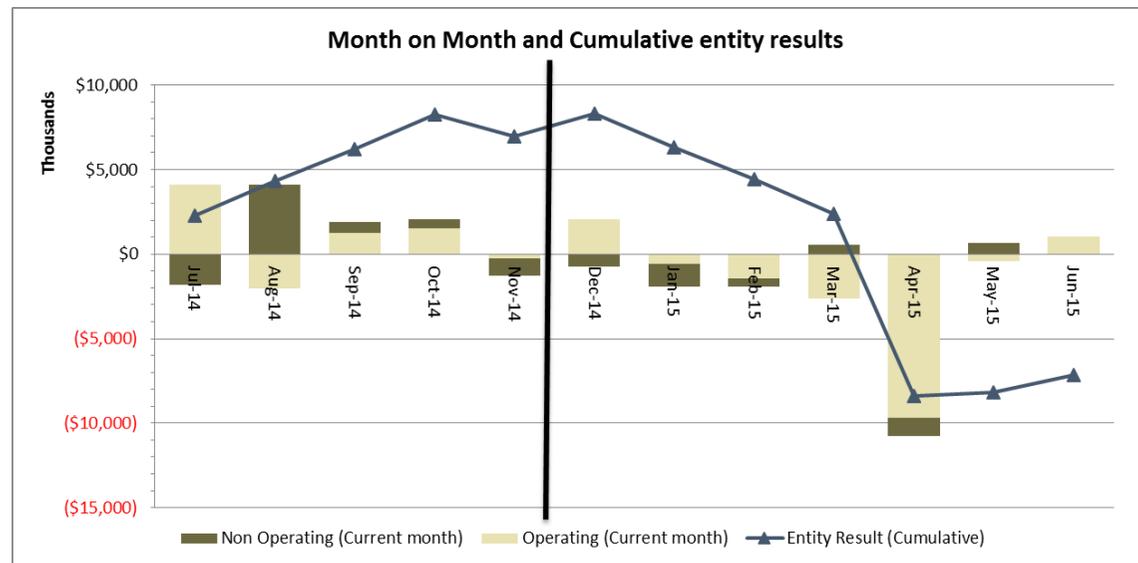


Figure 1 Monthly trend in 2014/15 financial performance

Table 1: 2014/15 overall financial results and indicators¹

	2014 YTD	Dec-14	Jan to June 2015	June 2015 YTD Actuals	Ave. mnth July to Nov 2014	Ave Mnth - Jan to June 2015 (excl Dec 2014)	Difference	
	Nov. Actuals (RCH ONLY)				\$ 000's	\$ 000's	\$ 000's	\$ 000's
Total revenue	140,621	53,902	306,022	500,545	28,124	51,004	22,879	81%
Total Expenditure	136,051	51,858	328,248	516,156	26,496	54,708	28,212	106%
CHQ Operating result (Def) / surp	4,570	2,045	(22,226)	(15,611)	762	(3,704)	(4,466)	0%
Transition / special projects / Trusts	2,396	732	(4,650)	(1,521)	479	(775)	(1,254)	0%
Entity results (Def) / Surp	6,966.6	2,776.6	(26,875.6)	(17,132.4)	1,241.0	(4,479.3)	(5,720.3)	0%
Additional QDOH transitional support funding				10,000				
Reported Entity result (Def) / Surplus				(7,132.4)				

Table 1 highlights the financial year summary:

- If the additional \$10m transitional support grant provided by QDOH is excluded, CHQ incurred a full year entity deficit of \$17.13m.
- The positive financial results reported in the first half year (\$6.97m entity surplus from July to November 2014) were offset by deficits totalling \$26.9m in the second half of the financial year.
- The result included a \$1.5m deficit in the non-operating segment (transitions/special project/trusts) of the organisation which largely related to the cost of transition to the new hospital being higher than the transition funding of \$10.4m provided by QDOH.
- The comparison of average monthly costs pre- and post-transition reflected labour cost increases of 58% (\$12.2m additional labour expenditure per month) and a non-labour cost increase of 138% (an increase of \$7.4m per month)
- With regards to achievement of activity targets, CHQHHS incurred a Queensland Weighted Activity Units (QWAU) shortfall of 2,767 WAU below the total QWAU target of 57,657 (4.8% below target). In terms of ABF related QWAU targets, the shortfall was 2,006 or 3.6% below the 55,405 target, the Public QWAU component of the ABF QWAU target of 47,939 was achieved in full.

¹ The result to June 2015 as reported in the Annual Statements and final activity reports, but excludes any update of CHQ performance from July 2015 for the current financial year. These results exclude any asset impairment or movement in revaluation reserve reported in the annual statement.

Factors contributing to 2014/15 Financial Result (Structural Deficit)

An analysis of the CHQ structural deficit was conducted to assess the effect of any once-off or extraordinary costs incurred during the transition period on the end of year results. The analysis also identified any changes in new recurring fixed and facilities costs which were incurred as a result of the relocation to LCCH. The purpose of the analysis was to understand the extent to which the organisation was faced with ongoing additional unavoidable costs which were not previously incurred at RCH.

The assessment was based on the end of year actual results as a starting point, eliminated any one-off costs and the one-off QDOH transitional support funding, then adjusted for the remaining year effect of new unavoidable costs. The result was an indicative structural deficit in 2014/15 of \$23m on a full year effect basis. The structural deficit result was based on:

- Taking the \$7.1m end of year entity financial result as a starting point;
- *Less* the cost effect of \$7.1m of identified once-off costs incurred by CHQ over and above previous transition funding;
- *Add* once-off additional QDOH transition supporting funding of \$10.9m received in 2014/15;
- *Add* back the any remaining year effect of new recurrent infrastructure and facilities management costs of \$12.2m incurred for new unavoidable costs from the relocation to LCCH to reflect the full year effect in the results.

2015/16 Financial Position

Paxton Partners also worked with the CHQ executive and finance team to assess the current 2015/16 budget forecast and assist in identifying areas to potentially improve the accuracy of the budget process and related assumptions.

Across CHQ, management conducted a zero based budget approach to determine the first full year expenditure budget base for LCCH. At a consolidated level, the total expenditure budget currently amounts to \$653.2m against an expenditure budget of \$659m² (Government revenue from QDOH includes additional funding of \$7.2m to support additional overnight bed capacity and retrieval services, \$5.8m to support additional ICT implementation costs and \$19m of additional transition funding), The budget also includes an undertaking by CHQ management to implement financial improvement strategies totalling \$6.2m.

Based on our understanding of the planned activity plan, bed capacity, demand profile, and with the support of QDOH's provisional transitional funding support of \$19m in 2015/16 and subject to the achievability of budget strategies and revenue targets, the HHS should be in a reasonable position to achieve its break-even operating result budget target (the equivalent of a \$5.8m entity deficit budget forecast before drawing from prior year retained earnings).

² The \$5.8m difference between the CQH Revenue and expenditure budget will be drawn from previous years retained surpluses to fund part of the costs to support the increase in beds over the year.

Table 2 2105/16 CHQ budget position

2015/16 CHQ budget position	Total \$ 000's
Total forecast income	\$ 653,252.3
Total forecast expenditure	\$ 665,220.7
Budget gap	(\$ 11,968.4)
Financial improvement strategies	\$ 6,250.0
Proposed 2015/16 CHQ entity P&L forecast	(5,800.0)
Drawings from previous year's retained earnings	\$ 5,800.0
Grand total	0.0

Other aspects of the review

Benchmarking

A high level benchmarking analysis against comparable paediatric specialist hospitals across Australia - using peer comparison data provided through Children's Healthcare Australasia – was also undertaken. Cost comparison data by Diagnosis Related Group (DRG) was only available for 2013/14 financial year and therefore not considered useful for the purposes of this review. However other efficiency and effectiveness measures were available up to March 2015, with LCCH data represented from December 2014 to March 2015.

It was noted that the data used in this analysis has been affected by the impact of the LCCH transition period to the new hospital. Indicatively, CHQ management has suggested that since March 2015, performance and activity has improved and returned to reasonable peer comparative levels.

With the support of QDOH, CHQ will undertake a more detailed and longer term benchmarking analysis with other Australian tertiary-quaternary paediatric hospitals as a way of assessing appropriate comparable efficiency and effectiveness measures. This will be undertaken with support of the Independent Hospital Pricing Authority (IHPA) and Children's Healthcare Australasia (CHA).

CHQ Financial governance and accountability framework

A significant challenge for the CHQ leadership team has been the re-establishment of a service-wide financial governance and accountability framework, particularly in the light of management's initial emphasis on commissioning the new site from two existing organisations, the early focus on patient quality and safety considerations, human resources, change management issues and challenges in managing cultural differences between RCH and MCH.

CHQ is re-establishing a more balanced approach to management accountability across the organisations key strategic and operational management domains. The CHQ Performance management framework (PMF) is currently being rolled out across the organisation as a key management accountability and monitoring

framework aimed at setting key performance goals and targets across all divisional teams in the organisation. The PMF attributes CHQ's financial, activity, workforce, quality and safety, and other operational metrics to each division in line with organisational goals.

The framework has been well structured and if implemented as intended will provide a significant step towards enhancing governance accountabilities across the organisation.

Supported by the introduction of improved organisation wide management reporting and analytical support functions by Finance, if the management framework is implemented as expected, the plans established by CHQ management to enhance financial and operational governance accountability across the organisation will be a positive and critical step towards ensuring the organisation is able to return to its previous sustainable financial position.

Preliminary 2015/16 results

As at the end of September 2015, the year to date operating result reflected a \$1.2m deficit. After including Trusts, Research and specific projects the entity result was a \$2.9m deficit

The deficit result has been largely attributed to significant increases in variable costs (labour and non-labour) resulting from higher than expected patient activity in the first quarter of the financial year with LCCH delivering an additional 4% of patient activity above projected YTD targets.

However, CHQ management have estimated that a further \$1.6m in ABF WAU revenue could be taken up in YTD results relating to additional Commonwealth growth funding contributions to reflect the additional ABF activity delivered over the year to date target levels. In real terms, the adjusted CHQ year to date results should reflect at least a break even underlying operating result to the end of September (compared to the current reported result of \$1.2m operating deficit). On an entity basis, the result would fall within year to date budget forecasts.

QDOH have also recently announced additional funding (\$7.2m) to the 2015/16 budget to support capacity for 331 beds (on average³) across the hospital being an increase of 31 on existing bed numbers. This increase in beds will support the achievement of planned activity and support good patient flow across the hospital care streams. A further \$20m recurrent funding on a full year effect basis is being funded by QDOH to support this capacity. Extra funding has also been provided to support the implementation of clinical information systems across LCCH and enable a more sustainable and responsive paediatric retrieval service to be put in place.

Taking into account the current underlying position and factoring in the provision of additional QDOH funding to increase current bed capacity and patient throughput, CHQ is well placed to achieve a break even position in 2015/16.

³ Throughout any given year, there will be times when the physical bed capacity of 359 beds could be occupied and at times less than 331 beds would be required to be occupied.