

HFMA introductory guide to NHS finance

Chapter 10: How the NHS is financed



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Overview

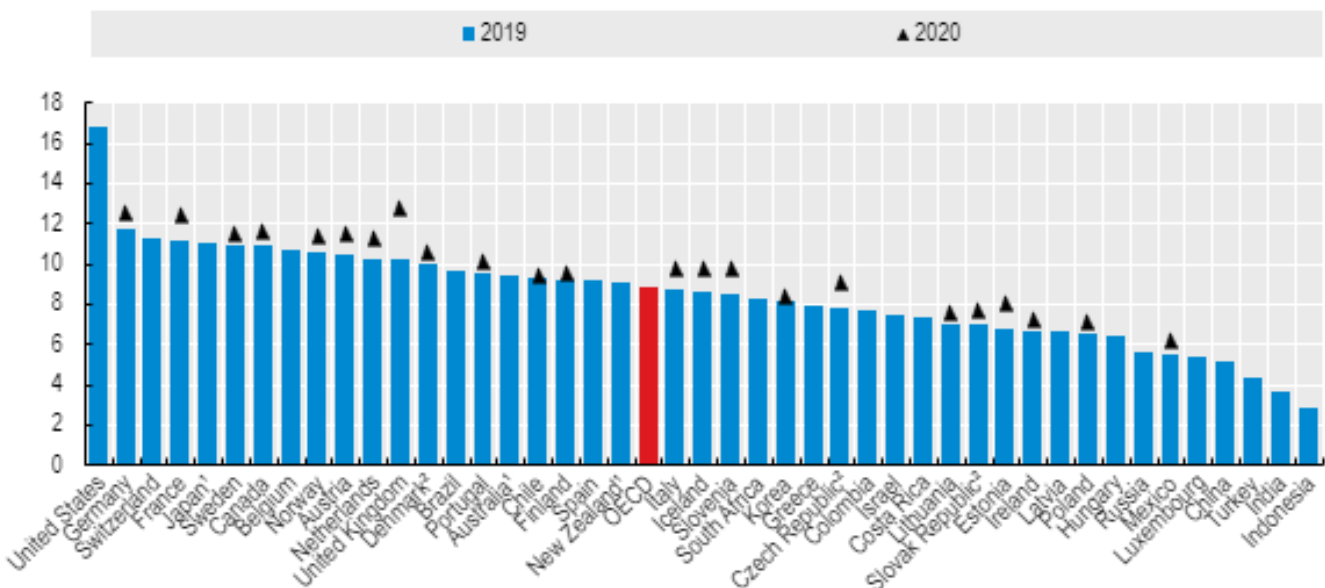
Health spending has always been a topic of political and public interest.

This chapter focuses on how resources are allocated nationally for the NHS and how they are divided up amongst the different areas of health spending. It also gives an idea of the scale of UK spending on health compared with other countries.

10.1 UK spending levels

The Organisation for Economic Cooperation and Development (OECD) health data for 2019 and 2020¹¹⁵ is shown in Figure 1 below. This shows that during 2019, the United Kingdom spent 10.154% of GDP (gross domestic product, or national wealth) on health compared with an average across the 30 OECD countries of 8.84%. Although some countries spend more, 11.7% in Germany and 16.8% in the USA, and have different health systems, UK expenditure on healthcare is broadly in line with other countries and the OECD average.

Figure 2: Health expenditure as a share of GDP, 2019 and 2020



Source: OECD, Health at a glance 2021: OECD indicators, figure 7.1

10.2 The role of HM Treasury

The responsibility for allocating and managing the finances of national government lies with the Chancellor of the Exchequer, who leads HM Treasury. To promote better planning of public spending the Treasury undertakes periodic spending reviews to set 'departmental expenditure limits' (DELs) for each government department. DELs usually cover a period of three years.

¹¹⁵ OECD, *Health at a glance 2021: OECD indicators*, November 2021

The DELs announced in the spending reviews are confirmed twice a year – through the main and supplementary estimates¹¹⁶, where the Government sets out how it will finance its spending commitments and makes any necessary or technical adjustments to its spending plans.

Unusually, in December 2020, the spending review only set out the Government’s departmental spending plans for a single year to 2021/22. Spending reviews usually cover a longer period, and a three-year budget was set in October 2021¹¹⁷.

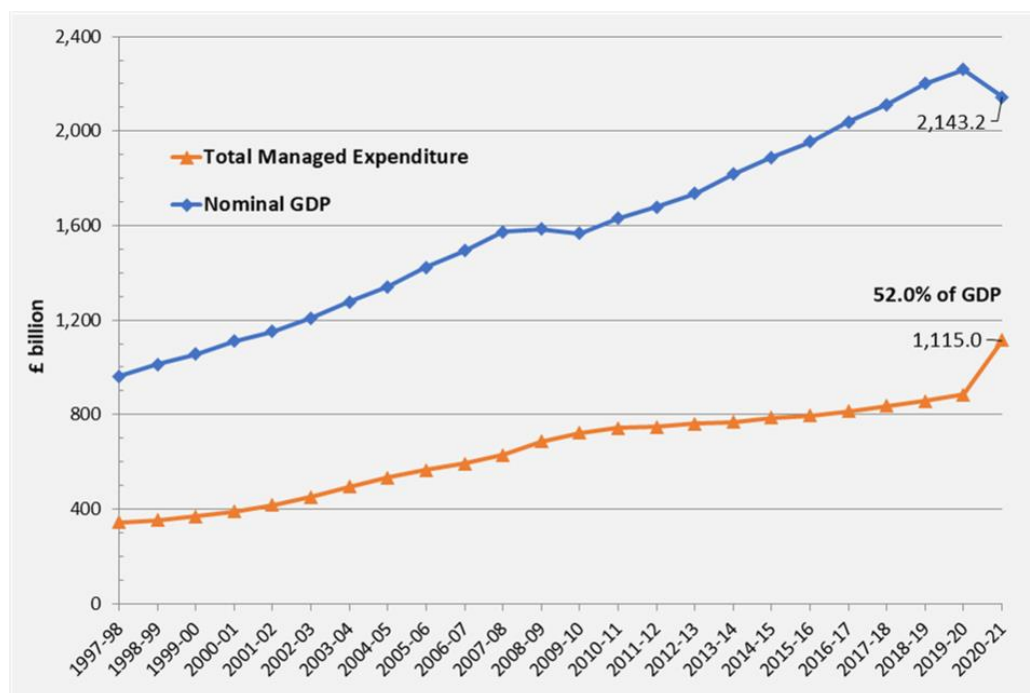
Public expenditure falls into one of two categories:

- DEL spending is expenditure on the running costs of each Government department, for the DHSC this includes the costs of running hospitals, including staff costs, as well as the provision of other healthcare services. Departments are not allowed to overspend the annual DEL set as part of the spending review in a year.
- annually managed expenditure (AME), which is expenditure that cannot reasonably be subject to firm, multi-year limits in the same way as DEL. Examples of such spending are social security benefits which are subject to fluctuation depending on the level of unemployment.

Together, DEL plus AME sum to ‘total managed expenditure’ (TME).

A key issue for any government is the relative level of public spending compared to national wealth (GDP). Relative to GDP (which itself fluctuates from year to year), UK public spending has varied from 35.1% in 1998/99 to a high of 52.0% in 2020/21. This high was due to increased government expenditure due to the Covid-19 pandemic combined with the reduced GDP as a consequence of the pandemic¹¹⁸.

Figure 3: Trends in public spending since 1997/98



Source: HM Treasury, Public spending statistics, February 2022, section 7.1

¹¹⁶ HM Treasury, *Main estimates*, updated May 2021

¹¹⁷ HM Treasury, *Autumn budget and spending review 2021*, October 2021

¹¹⁸ HM Treasury, *Public Spending Statistics releases*, updated February 2022

HM Treasury allocates DELs between revenue and capital spending. Revenue spending is for day-to-day items such as salaries and running costs; capital spending is for buying larger items such as buildings and equipment, which have a usable life of over one year.

HM Treasury's 2021 spending review resulted in the following pattern of allocations of revenue and capital DELs to government departments¹¹⁹:

Table 1: Departmental programme and administration budgets (resource DEL excluding depreciation)

	2020/21 £bn	2021/22 £bn	2022/23 £bn	2023/24 £bn	2024/25 £bn
Health and Social Care	136.3	147.1	167.9	173.4	177.4
Education	66.8	70.7	77	79.2	80.6
Home Office	12.9	13.7	15.2	15.6	15.7
Ministry of Justice	8.2	8.4	9.3	9.8	10.1
Law Officers' Departments	0.6	0.7	0.8	0.8	0.8
Ministry of Defence	30.6	31.5	32.4	32.2	32.4
Single Intelligence Account	2.3	2.2	2.3	2.4	2.5
Foreign, Commonwealth and Development Office	9.7	7.3	8.5	7.9	7.8
DLUHC Local Government*	5.3	8.5	11.7	12.1	12.8
DLUHC Housing and Communities	2.3	1.9	2.2	2.2	2.1
Department for Transport	3.6	4.4	7.8	6.8	5.7
Business, Energy and Industrial Strategy	2.1	2.3	2.6	2.7	2.6
Digital, Culture, Media and Sport	1.4	1.4	2.1	1.6	1.6
Department for the Environment, Food and Rural Affairs	4.1	4.1	4.5	4.4	4.3
Department of International Trade	.05	0.5	0.5	0.5	0.5
Department of Work and Pensions	5.7	5.6	7.6	7.2	6.9
HMRC	4.2	4.2	5.2	4.9	4.7
HM Treasury	0.3	0.2	0.3	0.3	0.3

¹¹⁹ HM Treasury, *Autumn budget and spending review 2021 (tables E2 and E3)*, October 2021

	2020/21 £bn	2021/22 £bn	2022/23 £bn	2023/24 £bn	2024/25 £bn
Cabinet Office	0.7	0.5	0.6	0.6	0.5
Scotland	30.3	31.6	35.0	35.7	36.3
Wales	12.5	13.5	15.1	15.4	15.6
Northern Ireland	11.9	11.7	12.9	13.2	13.4
Small and Independent Bodies	2.2	2.1	2.4	2.5	2.4
UK Shared Prosperity Fund			0.4	0.6	1.3
Reserves and adjustments		10.7	11.0	10.9	10.3
Ringfenced Covid-19 funding	121.2	69.8			
TOTAL DEL	475.8	454.7	435.2	442.5	453.7

Source: Autumn budget and spending review 2021, HM Treasury

Table 2: Total department capital DEL

	2020/21 £bn	2021/22 £bn	2022/23 £bn	2023/24 £bn	2024/25 £bn
Health and Social Care	8.6	9.4	10.6	10.4	11.2
Education	4.7	5.6	6.3	7.0	6.1
Home Office	0.8	0.9	1.0	1.0	0.8
Ministry of Justice	1.1	1.4	1.7	2.2	1.4
Law Officers' Departments	0.0	0.0	0.0	0.0	0.0
Ministry of Defence	11.7	14.4	15.6	15.8	16.2
Single Intelligence Account	0.6	0.9	1.0	1.2	1.2
Foreign, Commonwealth and Development Office	2.8	2.4	2.6	3.5	4.0
DLUHC Housing and Communities	9.0	7.8	8.9	6.9	6.8
Levelling up fund		0.2	0.9	1.4	1.4
Department of Transport	16.9	18.8	19.5	19.9	20.5

	2020/21 £bn	2021/22 £bn	2022/23 £bn	2023/24 £bn	2024/25 £bn
Business, Energy and Industrial Strategy	18.8	15.6	17.0	20.8	21.2
Digital, Culture, Media and Sport	0.5	0.8	0.8	1.1	1.1
Department for the Environment, Food and Rural Affairs	0.9	1.6	2.2	2.9	2.7
Department of International Trade	0.0	0.0	0.0	0.0	0.0
Department of Work and Pensions	0.3	0.3	0.6	0.5	0.4
HMRC	0.5	0.6	0.7	0.6	0.5
HM Treasury	0.0	0.0	0.0	0.0	0.0
Cabinet Office	0.2	0.5	0.4	0.5	0.5
Scotland	5.2	5.2	5.6	5.6	5.5
Wales	3.3	2.4	2.6	2.6	2.6
Northern Ireland	1.7	1.7	1.8	1.9	1.8
Small and Independent Bodies	0.3	0.4	0.5	0.5	0.6
UK Shared Prosperity Fund			0.0	0.1	0.2
Reserves		7.5	4.9	3.8	3.7
Funding for leases reclassification exercise (IFRS 16)		1.5	1.5	1.5	1.5
Adjustment to classification changes		-1.1			
Temporary Covid-19 funding	5.8	0.5			
Total capital DEL	93.7	99.3	106.8	111.5	111.9

Source: Autumn budget and spending review 2021, HM Treasury

The financial position in England, including separate lines for the costs of Covid-19, is summarised in the table that follows:

Table 3: Department of Health and Social Care funding

	2020/21 £bn	2021/22 £bn	2022/23 £bn	2023/24 £bn	2024/25 £bn	Average annual real terms growth 2021/22 to 2024/25
Resource DEL	136.3	147.1	167.9	173.4	177.4	4.1%
of which NHS England and Improvement	125.9	136.1	151.8	157.4	162.6	3.8%
DHSC capital	8.6	9.4	10.6	10.4	11.2	3.8%
TOTAL DEL	144.9	156.4	178.5	183.8	188.6	4.1%
Ringfenced Covid-19 funding	47.4	33.8				
total DEL including ringfenced Covid-19 funding	192.3	190.3	178.5	183.8	188.6	

Source: HM Treasury, Autumn budget and spending review 2021

Funding for health services in other UK nations is included in the separate Northern Ireland, Scottish and Welsh block grants. Any changes in planned spending in the NHS in England are matched by relative increases within these block grants through an allocation process called the Barnett formula¹²⁰. However, the individual administrations may spend less or more than these amounts on health services depending on their own priorities.

10.3 The role of the Department of Health and Social Care

The Department of Health and Social Care decides how the funding it receives from HM Treasury is allocated in England. Health and social services in Northern Ireland, Scotland and Wales are the responsibility of the devolved administrations (see chapters 20 to 22).

Most of the total NHS settlement (see table above) is allocated to NHS England and NHS Improvement which keeps around 20% for its own commissioning responsibilities and running costs and allocates the rest to clinical commissioning groups (CCGs).

The Department retains part of the allocation to meet:

- its own running costs
- the costs of various central health and miscellaneous services – for example, some centrally administered services and projects managed centrally for the benefit of the NHS (such as clinical negligence); a range of statutory and other arm's length bodies funded centrally (for

¹²⁰ House of Commons Library, *The Barnett formula*, January 2020

example, the NHS Business Services Authority and Health Education England – see chapter 3 for details)

- the costs of public health spending – this is covered by a separate ring-fenced budget (from the Department of Health and Social Care’s allocation) that is passed to and managed by local authorities and Public Health England (an executive agency within the Department – see chapter 3).

10.4 The role of NHS England and NHS Improvement

NHS England and NHS Improvement is responsible for using the funding it receives from the Department to deliver the *NHS Mandate*¹²¹ (the mandate) that it agrees annually. In practice this means that NHS England and NHS Improvement’s allocation must fund the costs of:

- directly commissioning activities – including the primary medical services provided by GPs, dentists, community pharmacists and opticians; specialised services; offender and military healthcare
- CCG allocations that fund the services they commission including elective and emergency hospital care, community care and mental health services (see chapter 5 for more information on the role of CCGs)
- the running costs for NHS England and NHS Improvement itself¹²², its regional teams, local professional networks, clinical senates, and networks
- running CCGs (known as the ‘running cost allowance’)
- some services that are commissioned by local authorities.

For 2021/22 the total revenue budget allocated to NHS England and NHS Improvement to deliver the mandate was £144.4 billion. Performance against that mandate will be published in the 2021/22 annual report and accounts.

The 2020/21 NHS England annual report and accounts¹²³ sets out the performance against the mandate for that year.

¹²¹ Department of Health and Social Care, *NHS mandate 2021/22*, March 2021

¹²² NHS England and NHS Improvement is the operational name of NHS England, Monitor and the NHS TDA. Each body has its own funding and set of accounts, so the funding from the Mandate only covers the running costs of the NHS England part of NHS England and NHS Improvement, the other parts are funded directly by the DHSC. Operationally, the three bodies are managed as one and costs are apportioned when the statutory accounts are prepared.

¹²³ NHS Commissioning Board, *Annual report and accounts 2020/21*, January 2022

Table 4: Revenue departmental expenditure limit 2020/21

	Plan £bn	Actual £bn	Underspend against plan £bn	
Direct commissioning		28.2	27.1	1.1
NHS England administration, central programmes and other		19.4	15.3	4.1
CCGs		101.9	101.7	0.2
Total		123.4	122.4	5.4

Source: NHS Commissioning Board, *Annual report and accounts 2020/21*¹²⁴

10.5 CCG allocations

CCGs received five-year allocations in January 2019, covering the periods 2019/20 to 2023/24¹²⁵. These allocations were based on the five-year funding settlement for NHS England and NHS improvement announced by the Prime Minister in June 2018¹²⁶. Allocations were firm for 2019/20 – 2021/22, with the following two years issued as indicative for planning purposes.

The *Autumn budget and spending review* set out the resource limits for the Department of Health and Social Care to 2024/25, these were confirmed in the *Spring statement* in March 2022.

In March 2022¹²⁷, NHS England and NHS Improvement issued one-year allocations to integrated care boards (ICBs) for 2022/23 and also set out a revised allocation methodology that will be applied for that period¹²⁸. Prior to ICBs being established through the *Health and Care Act*, these allocations will be applied to the CCGs which will become the ICB.

Once a CCG has been notified of its allocation for the forthcoming period, it plans how to use the funding across the full range of services that it commissions with the overall aim of improving the health and wellbeing of its population. A CCG commissions services from a range of providers including NHS trusts and foundation trusts, the private and voluntary sectors (see chapter 16 for more on commissioning).

10.6 NHS trusts and NHS foundation trusts

Funding secondary care

The majority of community, acute, specialist and mental healthcare in England is provided by NHS trusts or NHS foundation trusts. These trusts meet the costs of providing healthcare services (staff salaries are normally the largest element) and receive income from CCGs (and for some services, from NHS England and NHS Improvement) via contracts that specify the quantity, quality, and price of services to be provided. Each CCG (or NHS England and NHS Improvement) is responsible for meeting the cost of services provided to its population in line with the contract's terms. CCGs, NHS

¹²⁴ NHS Commissioning Board, *Annual report and accounts 2020/21*, January 2022

¹²⁵ NHS, *Allocations 2019/20 to 2023/24*, January 2019

¹²⁶ UK Government, *Prime Minister sets out 5-year NHS funding plan*, June 2018

¹²⁷ NHS England, *Allocation of resources 2022/23*, April 2022

¹²⁸ NHS, *Technical guide to integrated care board allocations 2022/23 to 2024/25*, April 2022

England and NHS Improvement, and providers are responsible for ensuring that patient treatments are clinically appropriate and provided in a cost-effective way.

Trusts also receive some income from other sources such as private patient income, hosting services, car park receipts, leasing of buildings and research and development. For many teaching hospitals, the latter can be significant.

Many trusts also have access to funds donated by members of the public on a charitable basis. However, these can be used only for the purpose for which they were given – for more about charitable funds see chapter 19.

Funding research and development

NHS funded research is overseen by the National Institute for Health Research (NIHR). The NIHR is funded by the Department of Health and Social Care to improve the health and wealth of the nation through research and is headed by the chief scientific adviser and director of science, research, and evidence. The NIHR is a virtual organisation hosted by NHS providers, universities, and life science organisations. Its day-to-day operations are run through six coordinating centres that allow the NIHR to commission and fund research, provide facilities and people within the clinical research network and support those who are carrying out, training, and participating in research.

Funding for NHS bodies can come through the NIHR Central Commissioning Facility that supports various research programmes, as well as a service to support those applying for the research programmes. The following schemes are also managed by this facility:

- applied research collaborations (ARCs) that support applied health and care research that meets the needs of local populations and increases the rate at which research is implemented into day-to-day practice. There are 15 ARCs in England that share £135m investment announced in July 2019.
- clinical research facilities (CRFs) for experimental medicine. CRFs are purpose-built, cutting edge facilities with specialist clinical, research and support staff in 28 NHS hospitals where universities and NHS organisations can work together on dedicated programmes of patient-orientated experimental medicine research. In February 2022, CRFs were awarded £161m to be shared by 28 organisations over five years.
- biomedical research centres (BRCs) – that are collaborations between universities and NHS organisations to translate lab-based breakthroughs into potential new treatments, diagnostics, and medical technologies. The 20 BRCs received £816m from 1 April 2017 to be spent over 5 years.

The NIHR clinical research network coordinating centre manages the clinical research network that comprises

- 15 local clinical research networks (LCRN) covering all of England
- 30 clinical research specialties
- national specialty leads.

NHS bodies and individuals can access funding from the various work streams depending on whether they are one of the lead organisations or undertake work in a particular area of research.

Funding clinicians' training

In addition, some trusts get substantial sums through placement fees for undergraduate healthcare professionals as well as salary and training costs for post graduate healthcare professionals. These funding flows are governed by Health Education England (HEE) via a system of education tariffs¹²⁹.

10.7 Primary care services

Most primary care services are provided by independent contractors such as general medical practitioners (GPs), general dental practitioners (GDPs), pharmacists and ophthalmic practitioners. Whilst they are an integral part of the NHS, these contractors operate as small businesses that contract with the NHS to provide primary care services. Contracts are designed to reward the quality of treatment.

NHS England and NHS Improvement, and CCGs under co-commissioning arrangements, pay primary care service providers according to nationally negotiated contracts – although local enhanced services to cover specific needs of patients in the area are negotiated locally. For example, GP practices receive a global sum to cover the provision of core services to their registered patient list and additional 'quality' payments for achieving goals set out in the quality and outcomes framework (QOF).

The interface between primary and secondary care is not always clear and is becoming more blurred as services become more integrated. GPs with specialist interests are increasingly playing a significant part in delivering patient care outside of the traditional hospital routes. On the other hand, some NHS providers are now employing GPs and are providing primary care services in the community to the local population.

See chapter 7 for more on primary care services.

10.8 What is the money spent on?

The Department of Health and Social Care publishes consolidated accounts for the whole of the NHS in England each year.

According to the 2020/21 accounts¹³⁰, staff costs account for 37% of operating expenditure for the DHSC as a group. Nearly all (94%) of the staff costs are incurred by NHS provider bodies. For NHS provider bodies, 64% of operating costs relate to staff costs.

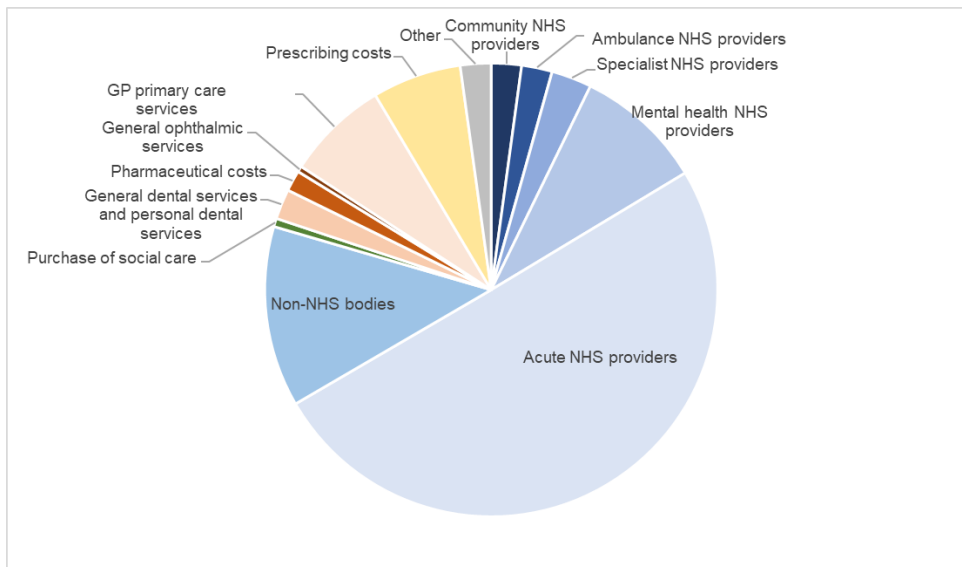
In 2020/21 the DHSC passed over 80% of its voted funds to NHS England and NHS Improvement for it to meet the requirements of the NHS Mandate. This percentage is usually over 90% but the impact of Covid-19 meant that the DHSC purchased more services and supplies directly.

Analysis of NHS England's annual report and accounts 2020/21, supplemented by information from the consolidated provider accounts for the same year, reveals that approximately 67% of commissioner's expenditure is on secondary care, while 18% is spent on primary care.

¹²⁹ DHSC, *Education and training tariff guidance and prices for 2021/22*, July 2021

¹³⁰ DHSC, *DHSC annual report and accounts 2020/21*, January 2022

Figure 4: Analysis of NHS England expenditure on goods and services by category 2020/21



Key learning points

- The UK spends just over 10% of GDP on health – around the OECD average.
- The government and HM Treasury determine how much money each government department receives based on spending reviews.
- Money is allocated for both day-to-day (revenue) and capital spending.
- The Department of Health and Social Care decides how the budget is used with over 80% of the revenue budget going to NHS England and NHS Improvement.
- The Department keeps some money for central services and arms' length bodies such as Public Health England and Health Education England.
- NHS England and NHS Improvement allocates the bulk of the money it receives to CCGs but keeps some to fund its own direct commissioning functions and running costs.
- NHS and foundation trusts receive the bulk of their income via contracts with CCGs and NHS England and NHS Improvement; other sources include income from research and development.
- Primary care services are provided predominantly by independent contractors who receive income via contracts agreed with NHS England and NHS Improvement.

Additional HFMA resources

The HFMA maintains a directory of resources which provides links to other HFMA outputs such as briefings and webinars across a range of subjects. It also highlights e-learning courses that are available. [The directory of resources can be found here.](#)