Independent Hospital Pricing Authority

Understanding the NEP and NEC 2018-19

March 2018

IHPA

Understanding the NEP and NEC 2018-19 – March 2018

Contents

Introduction

The Independent Hospital Pricing Authority's (IHPA) key role is to determine the annual National Efficient Price (NEP) and National Efficient Cost (NEC) for Australian public hospital services. IHPA publishes the NEP and NEC Determinations every year.

The NEP underpins Activity Based Funding (ABF) across Australia for public hospital services. ABF is a way of funding hospitals whereby they get paid for the number and mix of patients they treat. ABF is intended to improve the value of the public investment in hospital care and ensure a sustainable and efficient network of public hospital services.

In order to make these Determinations, IHPA develops and publishes the annual *Pricing Framework for Australian Public Hospital Services*. This document is crucial as it outlines the principles and policies adopted by IHPA to determine the NEP and the NEC for each financial year.

IHPA consults with all stakeholders, including state and territory governments, the Commonwealth Government and the general public, prior to finalising the Pricing Framework each year.

The Pricing Framework is released prior to the NEP and NEC Determinations to provide transparency and accountability by making available the key principles and policies adopted by IHPA to inform the NEP and NEC Determinations.

About the National Efficient Price (NEP)

The NEP is based on the average cost of an admitted acute episode of care provided in public hospitals during a financial year. Each episode of patient care is allocated a National Weighted Activity Unit (NWAU).

The NWAU is a measure of hospital activity expressed as a common unit, against which the NEP is paid. It is a point of relativity for the pricing of hospital services, which are weighted for clinical complexity. The 'average' hospital service is worth one NWAU. More intensive and expensive activities are worth multiple NWAUs, and simpler and less expensive activities are worth fractions of an NWAU.

The price of each public hospital service is calculated by multiplying the NWAU allocated to that service by the NEP.

For example:

- A tonsillectomy has a weight of 0.7158 NWAU which equates to $3,588.
- A coronary bypass (minor complexity) has a weight of 5.1572 NWAU which equates to $25,848.
- A hip replacement (minor complexity) has a weight of 4.0509 NWAU which equates to $20,303.

The NEP has two key purposes:

1. To determine the amount of Commonwealth Government funding for public hospital services.
2. To provide a price signal or benchmark about the efficient cost of providing public hospital services.

Each NEP Determination includes the scope of public hospital services eligible for Commonwealth Government funding on an activity basis (detailed in a document released by IHPA called the 'General List of In-Scope Public Hospital Services'). It also includes loadings to the price ('adjustments') to reflect legitimate and unavoidable variations in the cost of delivering health care services, such as location of patient residence and patient complexity.

The NEP is used by jurisdictions as an independent benchmarking tool to measure the efficiency of public hospital services in their state or territories. For instance, it is possible to compare the cost of the hip replacement in two different hospitals, which may assist jurisdictions to identify best practice and make funding decisions.

About the National Efficient Cost (NEC)

The NEC is used when activity levels are not suitable for funding based on activity such as small rural hospitals. In these cases, services are funded by a block allocation based on size, location and the type of services they provide. This type of funding applies to approximately 400 small rural hospitals.

The NEC also applies to public hospital services or functions that are not yet able to be described in terms of 'activity' such as teaching, training and research.

Some of these hospitals and services may operate with a mix of block grant and ABF.

The NEC Determination provides a set dollar amount that represents the average cost of block funded hospitals across Australia. Hospitals are assigned to a size-locality-type grouping and mean expenditure is calculated for groupings.

IHPA works closely with a Small Rural Hospital Working Group, which includes representatives from states and territories, small rural hospitals, and peak healthcare bodies and associations. The working group provides vital guidance and advice to IHPA about setting an effective cost for block funding.

The key difference between the NEP and the NEC is that in relation to the NEC the states and territories manage the total block funding amount provided to hospitals. This is determined through service level agreements that are made between the states and territories and the Local Hospital Networks.

Summary of key changes

Based on the principles in the *Pricing Framework for Australian Public Hospital Services 2018-19*, IHPA has determined the NEP and NEC for 2018-19.

National Efficient Price 2018-19

The NEP for 2018-19 is $5,012 per NWAU.

The NEP has been impacted by a number of methodological improvements. The improvements with material impacts on the NEP for 2018-19 are as follows:

Pricing and funding for safety and quality

Sentinel events

The June 2017 Addendum to the National Health Reform Agreement states that public hospital episodes that include a sentinel event will receive zero funding on or after 1 July 2017 across all relevant episodes of care (all streams) in both ABF and block funded hospitals. IHPA implemented this approach for NEP17, with this carried through to NEP18.

Hospital acquired complications

The June 2017 Addendum to the National Health Reform Agreement states that IHPA is to implement the agreed funding approach for hospital acquired complications (HACs). HACs are complications which occur during a hospital stay and for which clinical risk mitigation strategies may reduce (but not necessarily eliminate) the risk of that complication occurring. The list of HACs which are subject to the funding approach was determined a Joint Working Party including the Australian Commission on Safety and Quality in Health Care, IHPA and clinicians.

The HAC Adjustment reduces the level of funding a hospital receives for an admitted acute episode of care where a HAC takes place on or after 1 July 2018. If more than one HAC is present, the larger of the adjustments applies. The reduction in funding is equivalent to the additional costs of providing hospital care due to the occurrence of the HAC.

The HAC Adjustment includes a comprehensive risk adjustment model, which accounts for the increased likelihood of some patients of experiencing a HAC. In the case where a HAC is experienced by a patient considered to be of low risk then funding for that episode is reduced by the full incremental cost of the HAC. Where a patient is determined to be of high risk of experiencing a HAC, then the funding for that episode is reduced by a proportion of the incremental cost of the HAC. The preventability of the complication was also considered by the Joint Working Party in determining the HAC list.

The intention of the HAC Adjustment is to provide a financial incentive for hospitals to reduce the rate of HACs and the funding approach will complement existing measures by Australian governments to improve safety and quality in health care.

Patient Remoteness Treatment

IHPA recognises that there are legitimate costs incurred by some hospitals due to circumstances outside of their control such as geographic area. IHPA has introduced a ‘Patient Treatment

Remoteness Area Adjustment' which provides an additional treatment-based loading to account for the costs of care for admitted acute episodes in remote hospitals which is not otherwise accounted for through the patient-based adjustment. The loading better accounts for the higher costs of care associated with treatment in remote areas.

Multidisciplinary case conferences where the patient is not present

Multidisciplinary case conferences have become a more common and important aspect of clinical care. Increased complexity and specialisation in health care has driven the need for more formalised mechanisms for multidisciplinary collaboration where often the patient is not present.

IHPA has created two non-admitted classes for multidisciplinary case conferences where the patient is not present which will allow for specific reporting of this activity and to provide data collection to support the pricing of the services in future years. Shadow price weights have been included in the NEP Determination to foreshadow the specific pricing of these services in 2019-20.

Indexation of cost data

The cost data used to develop NEP18 is sourced from the NHCDC for 2015-16. To account for the three year time lag between the costing data and the price, IHPA indexes the cost data using a pre-determined indexation methodology. IHPA has reviewed the indexation methodology in preparation for NEP18, and has decided that its approach to indexation is appropriate.

Back-casting

As with previous years, the Pricing Authority has recalculated ('back-cast') NEP17 to incorporate the most up-to-date cost data and to take account of methodological changes introduced in NEP18 which impact on the ability to compare the NEP between years. IHPA is required to back-cast the previous year's NEP under Clause A40 of the National Health Reform Agreement.

Back-casting is important to ensure the calculation of Commonwealth funding is not adversely impacted by changes in the calculation of the NEP over years. Under the National Health Reform Agreement, the Commonwealth funds 45 per cent of the efficient growth in public hospital services which are funded on an activity basis.

The Pricing Authority has recalculated NEP17 using more up to date cost data than was available when NEP17 was initially calculated. This is allowed for in the National Health Reform Agreement (Clause A40).

The back-cast NEP17 shows an increase of 1.6% between NEP17 and NEP18, which is the basis for Commonwealth growth funding for 2018-19.

NEP17	Back-cast NEP17	NEP18
$4,910	$4,933	$5,012

National Efficient Cost 2018-19

The NEC for 2018-19 is $5.171 million.

The NEC18 has seen a significant improvement in data robustness due to the results of IHPA's collaborative work with the Australian Institute of Health and Welfare to review expenditure that is in-scope under the National Health Reform Agreement. These improvements have meant that IHPA is able to reflect the true cost of block funded hospitals better.

Support for innovative funding models

IHPA recognises that service delivery models are not static and innovative models of care offer the potential to provide more effective health services. The Pricing Guidelines outline the policy objectives to guide IHPA's work and reference fostering clinical innovation whereby "the pricing of public hospital services should respond in a timely way to introduction of evidence-based, effective new technology and innovations in the models of care that improve patient outcomes".

IHPA will consider jurisdictional proposals to block fund patients to support the introduction of new innovative funding models on a case-by-case basis. For 2018-19, the Pricing Authority has determined that enrolled chronic care patients in the capitation funding model in Victoria ('HealthLinks: Chronic Care') will be block funded to support the introduction of this program.

Back-casting

Commonwealth funding for block funded hospitals is based on growth between NEC17 and NEC18. In order to calculate this growth, a back-cast NEC17 has been calculated to place it on the same basis as NEC18. The back-cast NEC17 figure is $5.025 million, indicating growth of 2.9% from NEC17 to NEC18.

More information

For more information about IHPA, Activity Based Funding or the NEP and NEC Determinations, please visit www.ihpa.gov.au or contact enquiries.ihpa@ihpa.gov.au.

Independent Hospital Pricing Authority

Level 6, 1 Oxford Street
Sydney NSW 2000

Phone 02 8215 1100
Email enquiries.ihpa@ihpa.gov.au
Twitter @IHPAnews

www.ihpa.gov.au

IHPA