



IHACPA

# Shadow Pricing Guidelines

June 2024



## **Shadow Pricing Guidelines – Version 4.0 June 2024**

© Independent Health and Aged Care Pricing Authority 2024

This publication is available for your use under a Creative Commons Attribution 4.0 International licence, with the exception of the Independent Health and Aged Care Pricing Authority logo, photographs, images, signatures and where otherwise stated. The full licence terms are available from the Creative Commons website.



Use of Independent Health and Aged Care Pricing Authority material under a Creative Commons Attribution 4.0 International licence requires you to attribute the work (but not in any way that suggests that the Independent Health and Aged Care Pricing Authority endorses you or your use of the work).

Independent Health and Aged Care Pricing Authority material used 'as supplied'.

Provided you have not modified or transformed Independent Health and Aged Care Pricing Authority material in any way including, for example, by changing Independent Health and Aged Care Pricing Authority text – then the Independent Health and Aged Care Pricing Authority prefers the following attribution:

Source: The Independent Health and Aged Care Pricing Authority

# Table of Contents

<b>Acronyms and abbreviations .....</b>	<b>4</b>
<b>Definitions .....</b>	<b>5</b>
<b>1. Executive summary .....</b>	<b>6</b>
<b>2. Assessing readiness for shadow pricing .....</b>	<b>8</b>
<b>3. Commencement of shadow pricing.....</b>	<b>10</b>
<b>4. Monitoring the impact of shadow pricing .....</b>	<b>11</b>
<b>Appendix A: Extracts from the addendum .....</b>	<b>12</b>

# Acronyms and abbreviations

<b>ABF</b>	Activity based funding
<b>IHACPA</b>	Independent Health and Aged Care Pricing Authority
<b>JAC</b>	Jurisdictional Advisory Committee
<b>NEC</b>	National efficient cost
<b>NEP</b>	National efficient price
<b>NHRA</b>	National Health Reform Agreement
<b>NWAU</b>	National weighted activity unit
<b>TAC</b>	Technical Advisory Committee
<b>The addendum</b>	Addendum to the National Health Reform Agreement 2020–25
<b>The NHR Act</b>	<i>National Health Reform Act 2011</i>
<b>The Administrator</b>	Administrator of the National Health Funding Pool
<b>The guidelines</b>	Shadow Pricing Guidelines

# Definitions

<b>Activity based funding</b>	<p>Refers to a way of funding public hospitals whereby they get paid for the number and mix of patients they treat. Activity based funding is underpinned by national classification systems, data collections, costing standards, price weights and efficient costs developed by the Independent Health and Aged Care Pricing Authority (IHACPA), as outlined in the National Health Reform Agreement (NHRA).</p> <p>An activity based funding activity may take the form of a separation, phase, presentation or service event.</p>
<b>Classification</b>	<p>Classifications are comprised of codes that provide clinically meaningful ways of creating a link between patients, their treatments and the costs and resources associated with providing those treatments. This allows hospital and health service provider output to be measured, which is valuable for informing policy decisions, benchmarking and funding of high quality and efficient health care services.</p>
<b>Costing methodology</b>	<p>Costing methodologies are ways to identify and allocate costs. Hospital patient costing focuses on the cost and mix of resources, including services or products, used to deliver patient care, in order to understand the total costs involved in treating a patient. Costing is used to inform the development and refinement of classification systems and provides valuable information for pricing purposes.</p>
<b>Costing study</b>	<p>IHACPA undertakes costing studies in areas where it has identified opportunities for improving the national pricing model or improving the understanding of costs of services. These areas include developing new classifications, major revisions to existing classifications and changes to costing methodologies.</p>
<b>National pricing model</b>	<p>The national pricing model is produced annually by IHACPA and defines the national efficient price, price weights and adjustments based on the cost and activity data from 3 years prior. For more detail, refer to the <a href="#">National Pricing Model Technical Specifications</a>.</p>
<b>Parties</b>	<p>Refers to the signatories to the Addendum to the NHRA 2020–25, being the Australian Government and each state and territory government.</p>
<b>Pricing Authority</b>	<p>The governing body of IHACPA established under the <i>National Health Reform Act 2011</i>.</p>
<b>Shadow pricing</b>	<p>Shadow pricing is undertaken by IHACPA when developing new classifications or implementing significant changes to existing classifications. IHACPA undertakes shadow pricing, with the publication of shadow price weights, to ensure robust data collection and reporting to accurately model the financial and counting impact of changes on the national funding model and minimise the risk of incurring undesirable and inadvertent consequences.</p>

# 1. Executive summary

## 1.1 Background

The National Health Reform Agreement (NHRA), signed by all Australian governments in August 2011, specifies that the Independent Health and Aged Care Pricing Authority (IHACPA) is to develop, refine and maintain systems as necessary to determine the national efficient price (NEP) and national efficient cost (NEC), including classifications, costing methodologies and data collections.

The Addendum to the NHRA 2020–25, signed in May 2020, further defines IHACPA's role in public hospital funding arrangements, in particular, the use of transitional arrangements such as shadow pricing and costing studies when developing new activity based funding (ABF) classification systems or costing methodologies.

## 1.2 Provisions under the addendum

The addendum contains provisions relating to the consultation processes IHACPA is required to undertake with all 9 jurisdictions for proposed changes to the national funding model, with specific reference to processes for changes to classification systems and costing methodologies.

Clause A42 of the addendum states that IHACPA will use transitional arrangements when developing new ABF classification systems or costing methodologies, including shadow pricing classification system changes and pricing based on a costing study, for 2 years or a period agreed with the Commonwealth and a majority of states and territories. This is to ensure robust data collection and reporting to accurately model the financial and counting impact of changes on the national funding model.

Full extracts from the addendum are provided at **Appendix A**.

## 1.3 Purpose

The purpose of the Shadow Pricing Guidelines is to outline the principles and timeframes for commencing shadow pricing and reporting requirements during the shadow pricing period in the development and implementation of new or changed ABF classification systems, to provide clear guidance to jurisdictions.

The guidelines are to be applied in conjunction with the [National Pricing Model Consultation Policy](#), which outlines the principles and consultative processes associated with changes that materially impact the application of the national funding model, including changes requiring shadow pricing and progression from shadow pricing to pricing.

The guidelines do not apply to IHACPA's functions pertaining to the provision of advice to the Australian Government on aged care costing and pricing.

## 1.4 Review

The Pricing Authority and Chief Executive Officer of IHACPA will review the guidelines, including associated documentation, every 3 years or as required.

The guidelines were last reviewed in June 2024.

# 2. Assessing readiness for shadow pricing

## 2.1 Overview

Clause A42 of the addendum states that IHACPA will use transitional arrangements when developing new ABF classification systems or costing methodologies, including shadow pricing classification system changes, for 2 years or a period agreed with the Commonwealth and a majority of states and territories.

As outlined in the [National Pricing Model Consultation Policy](#), IHACPA will undertake shadow pricing for the introduction of new classifications and major structural changes to new versions of existing classifications.

IHACPA undertakes shadow pricing under these circumstances to ensure robust data collection and reporting to accurately model the financial and counting impact of changes on the national funding model and minimise the risk of incurring undesirable and inadvertent consequences.

## 2.2 Principles for commencing shadow pricing

The Addendum does not contain any stipulations requiring the agreement of jurisdictions to commence shadow pricing, however IHACPA will assess readiness for shadow pricing of a new classification or a major structural change to an existing classification in consultation with jurisdictions and other relevant stakeholders.

The following set of principles have been developed to guide the assessment of readiness for shadow pricing for a new or changed classification:

- The new or changed classification and pricing model have been developed in consultation with IHACPA's Clinical Advisory Committee, Jurisdictional Advisory Committee (JAC), Technical Advisory Committee (TAC) and relevant classification development working groups.
- The new or changed classification implements data elements that are currently captured or able to be captured in national data sets (national minimum data sets or national best endeavours data sets) to enable pricing and funding reconciliation.
- The shadow pricing model is based on cost and activity data from an adequate number and range of establishments to provide appropriate coverage of the patient service category and be adequately representative of state and territory costs and activities.
- The available cost and activity data provides adequate coverage of all classification end-classes and there are clear and meaningful strategies to account for any gaps in data.
- The shadow pricing model appropriately accounts for outliers and variation in the underlying data to facilitate pricing model and year-on-year stability.



- The shadow pricing model appropriately accounts for risk and legitimate and unavoidable cost variations, with consideration given to clinical significance, statistical performance and model complexity.
- As part of the progression to shadow pricing, IHACPA will make every effort to minimise undue administrative, financial or operational burdens on the states and territories (such as that associated with dual data collection).

In addition to assessment against the above principles for readiness for shadow pricing, IHACPA will develop and provide states and territories with national weighted activity unit (NWAU) calculators for shadow price weights. States and territories will be able to monitor the impact of shadow pricing on local systems, to provide feedback to IHACPA during the shadow pricing period.

This will facilitate consideration of potential medium and long term impacts on the national pricing model and assist in ensuring that the shadow pricing model is fit-for-purpose.

## **2.3 Consultation process**

IHACPA will consult with jurisdictions through JAC and TAC in assessing readiness for shadow pricing. Proposals to commence shadow pricing will be tabled through JAC and TAC, where IHACPA will provide jurisdictional representatives with updates on classification development, updates on shadow pricing model development, relevant reports and analysis, and IHACPA's rationale to shadow price.

Following consultation through JAC and TAC, feedback from jurisdictions, any additional analysis and the proposal to shadow price will be provided to the Pricing Authority for consideration. Where the proposal is not supported by jurisdictional representatives through JAC, however is approved by the Pricing Authority for progression to shadow pricing, IHACPA will provide the Pricing Authority's rationale to JAC members.

# 3. Commencement of shadow pricing

IHACPA has defined when the 2-year shadow period will commence, in accordance with clause A42 of the addendum. The starting point for the 2-year shadow pricing period will be the commencement of the financial year immediately following the Pricing Authority’s decision to commence shadow pricing or any other date agreed between IHACPA, the Commonwealth and a majority of states and territories.

In alignment with the annual NEP and NEC determination development cycle, IHACPA will communicate its intent to shadow price to broader stakeholders through the public consultation process to develop the [Pricing Framework for Australian Public Hospital Services](#) and communicate decisions on shadow pricing through the pricing framework.

The timeframes for assessing readiness for shadow pricing are outlined in **Table 1**.

**Table 1: Timeframes for proposal, consultation and commencement of shadow pricing**

Process	Process details	Timeframe
Public consultation on IHACPA’s intent to shadow price	30-day public consultation period through the consultation paper on the pricing framework	May to June of the current year
Assessment of readiness for shadow pricing	Incorporation of stakeholder feedback to the consultation paper and additional consultation where required	July to October of the current year
Proposal for shadow pricing tabled at JAC and TAC	2-week JAC and TAC consultation period	No later than 31 October of the current year
Pricing Authority approval	Incorporation of feedback from JAC and TAC	November of the current year
Notification to health ministers of intent to progress to shadow pricing	45-day ministerial comment period for the draft NEP determination, which will provide detail on the new or changed classification that is being shadow priced	December of the current year
Stakeholder notification of progression to shadow pricing	Stakeholders are notified of the final decisions around shadow pricing through the publication of the pricing framework	December of the current year
Provision of shadow price weights	Shadow price weights and associated NWAU calculators are published alongside the final NEP determination.	By 31 March of the following year
Commencement of shadow pricing	IHACPA and jurisdictions begin monitoring the impact of shadow pricing.	From 1 July of the following year

# 4. Monitoring the impact of shadow pricing

The publication of the annual NEP determination will include shadow price weights and NWAU calculators for new or changed classifications that are being shadow priced. Groupers for new or changed classifications that are being shadow priced will also be made available to the states and territories upon request. Where feasible, the calculations for shadow priced classifications will be incorporated into the [IHACPA data submission portal](#).

Where the implementation of groupers for shadow pricing new or changed classifications represents an undue administrative burden on the states and territories, IHACPA will support jurisdictional evaluation of the shadow pricing period through the provision of impact analysis through JAC and TAC. This may include analysis of the potential impact of shadow pricing on the other patient service categories, and assessment of the shadow pricing model against the existing pricing model.

Further information on the NEP determination, shadow price weights and NWAU calculators can be found on the [IHACPA website](#).

# Appendix A: Extracts from the addendum

Clause	Detail
A37	All parties will participate in the development of parameters of the national funding model each year, through the IHPA <sup>1</sup> process outlined in clauses B21 to B40, including efficient price, classifications and cost weights. This process will rely on transparent sharing of analysis, commissioned costing data, and shadow pricing and reporting (where appropriate) to support robust decision making.
A42	<p>The IHPA will use transitional arrangements when developing new ABF classification systems or costing methodologies, including shadow pricing classification system changes and pricing based on a costing study, for two years or a period agreed with the Commonwealth and a majority of States to ensure robust data collection and reporting to accurately model the financial and counting impact of changes on the National Funding Model.</p> <ol style="list-style-type: none"> <li>a. Where a jurisdiction participates fully in the shadow pricing, including the provision of the best available data over the shadow period to support the implementation of the new ABF classification systems or costing methodologies, the Parties agree there will be no retrospective adjustments to the National Funding Model, excluding adjustments to Commonwealth contributions as a result of service volume reconciliations as set out in clauses A63, A65 and A73.</li> <li>b. Business rules will be developed by the national bodies in consultation with Parties, addressing significance of changes, process and consultation around retrospective adjustments where appropriate. <ol style="list-style-type: none"> <li>i. If the national bodies consider there is a potential need for a retrospective adjustment to the national funding model, national bodies will communicate, consult and collaborate with Parties. The national bodies will hold a consultation period of 45 days to allow Parties an opportunity to provide submissions on the matter.</li> <li>ii. Within 45 days following the jurisdiction 45-day consultation period, national bodies will prepare a report to the Council of Australian Governments Health Council, advising them of the national bodies' decision and the nature and circumstances of the recommended adjustment to the national funding model.</li> <li>iii. Once the report is provided to the Council of Australian Governments Health Council, the national bodies will incorporate the decision regarding the retrospective adjustment into the national funding model and provide parties with an updated report on funding entitlements from the national model.</li> <li>iv. When providing payment advice to the Commonwealth Treasurer following the six-month or annual reconciliation, the Administrator will include a section that notes any matters or concerns raised by State Ministers in the 45-day consultation period in the formation of that advice.</li> </ol> </li> </ol>

<sup>1</sup> On 12 August 2022 amendments to the NHR Act came into effect changing the Independent Hospital Pricing Authority's name to the Independent Health and Aged Care Pricing Authority (IHACPA) and expanding its role to include the provision of costing and pricing advice on aged care to the Australian Government.



Independent Health and Aged Care Pricing Authority

Eora Nation, Level 12, 1 Oxford Street  
Sydney NSW 2000

Phone 02 8215 1100

Email [enquiries.ihacpa@ihacpa.gov.au](mailto:enquiries.ihacpa@ihacpa.gov.au)

[www.ihacpa.gov.au](http://www.ihacpa.gov.au)