IHACPA

# Understanding the NEP and NEC Determinations 2023–24

March 2023

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# 1. Introduction

The Independent Health and Aged Care Pricing Authority (IHACPA) determines the annual national efficient price (NEP) and national efficient cost (NEC) for Australian public hospital services. IHACPA publishes the NEP and NEC Determinations each year.

The NEP underpins activity based funding (ABF) across Australia for public hospital services. ABF is a way of funding hospitals whereby they are 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.

The NEC determines the Commonwealth Government's funding contribution to local hospital networks for public hospital services that are not suitable for ABF, such as small rural hospitals.

In order to make the NEP and NEC Determinations, IHACPA develops and publishes the annual Pricing Framework for Australian Public Hospital Services (the Pricing Framework), which outlines the principles and policies adopted by IHACPA to determine the NEP and the NEC for that financial year.

IHACPA 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 IHACPA to inform the NEP and NEC Determinations.

## 1.1 About the national efficient price

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 complex 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 0.7726 NWAU which equates to $4,660.
- A coronary bypass (minor complexity) has a weight of 5.4876 NWAU which equates to $33,101.

- A hip replacement (minor complexity) has a weight of 3.9330 NWAU which equates to $23,724.

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 as per the General List of In-Scope Public Hospital Services. It also includes loadings ('adjustments') to the price to reflect legitimate and unavoidable variations in the cost of delivering health care services, including patient factors such as patient complexity, residence and treatment location, and hospital factors such as hospital type, size, and location.

Approximately 493 public hospitals nationwide, including all large metropolitan hospitals, receive funding based on their activity levels.

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 a hip replacement in two different hospitals, which may assist jurisdictions to identify best practice and make funding decisions.

## 1.2 About the national efficient cost

The NEC is used when activity levels are not suitable for funding based on activity, such as for small rural hospitals. In these cases, hospitals are funded by a block allocation based on size, location and the type of services they provide. This type of funding applies to 368 small rural hospitals. Some of these hospitals and services may operate with a mix of block funding and ABF.

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.

The NEC Determination outlines the efficient cost of a small rural hospital, which is the sum of the fixed component and a variable cost component.

IHACPA works closely with its Small Rural Hospitals 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 IHACPA about setting the efficient cost of a small rural hospital.

# 2. Summary of key changes

Based on the principles in the *Pricing Framework for Australian Public Hospital Services 2023–24* (the Pricing Framework), the Independent Health and Aged Care Pricing Authority (IHACPA) has determined the national efficient price (NEP) and national efficient cost (NEC) for 2023–24. Some of the key changes and policy considerations for the NEP and NEC Determinations for 2023–24 are outlined below.

## 2.1 National Efficient Price Determination 2023–24

The NEP for 2023–24 (NEP23) is $6,032 per national weighted activity unit (NWAU).

IHACPA recognises the Australian healthcare system is facing significant and unprecedented challenges arising from the impact of coronavirus disease 2019 (COVID-19) and increased price inflation in the Australian and global economy. In developing the NEP Determination for 2023–24 (NEP23 Determination), IHACPA has aimed to be responsive to these issues and their relevance to pricing model development.

### Impact of COVID-19

COVID-19 has resulted in significant and potentially long-lasting changes to models of care and service delivery in Australian public hospitals. IHACPA notes the importance of ensuring that the impact of COVID-19 is adequately accounted for in the national pricing model.

The NEP23 Determination uses 2020–21 cost and activity data, which includes a full financial year of data impacted by the COVID-19 pandemic response.

In developing the NEP23 Determination, IHACPA has undertaken extensive analysis in consultation with the jurisdictions to understand the impact of COVID-19 on this data.

IHACPA's analysis indicated that in the 2020–21 financial year, there was a reduction in activity in the admitted acute stream and an increase in costs during the Victorian lockdown period spanning August 2020 to October 2020. This pattern of activity and cost is not apparent for the other states and territories for the admitted acute stream or other streams. This indicates that the activity and costs, as reported during the Victorian lockdown period in 2020–21, reflect the higher average cost of care where there is underutilised public hospital capacity, in part due to inflexible costs that do not decrease despite a reduction in activity.

IHACPA has therefore normalised admitted acute activity in Victoria during the lockdown period in order to calculate the NEP23. This normalisation was important to ensure the NEP23 reflects the expected efficient cost of delivering public hospital services in 2023–24, because it is unlikely that the same pattern of cost and activity data arising from the Victorian lockdown period will reoccur in 2023–24.

Additionally, IHACPA's analysis indicated that patients treated for COVID-19 had longer length of stay and increased costs when compared to non-COVID-19 patients in the same Australian Refined Diagnosis Related Group (AR-DRG) end-classes. To address this finding, IHACPA has introduced a COVID-19 treatment adjustment for relevant AR-DRGs to account for the additional costs associated with treating admitted patients for COVID-19.

## Classification system updates

For NEP23, IHACPA will price admitted acute care using the new Australian Refined Diagnosis Related Groups Classification (AR-DRG) Version 11.0 and the International Statistical Classification of Diseases and Related Health Problems, Tenth Revision, Australian Modification, Australian Classification of Health Interventions, Australian Coding Standards Twelfth Edition.

IHACPA will also use the Tier 2 Non-Admitted Services Classification Version 8.0 to price non-admitted services for the NEP23 Determination. This includes the pricing of four new classes for '20.58 Long COVID', '40.65 Violence, abuse and neglect services', '40.66 Genetic counselling' and '40.67 Long COVID'.

Community mental health care services will continue to be block funded for 2023–24 while a third year of shadow pricing is undertaken using the Australian Mental Health Care Classification (AMHCC) Version 1.0. This will provide additional time for IHACPA to work with jurisdictions and stakeholders to ensure robust transition arrangements and risk mitigation are in place to support activity based funding using AMHCC Version 1.0 to commence in 2024–25.

The NEP23 Determination uses the Australian National Subacute and Non-Acute Patient Classification (AN-SNAP) Version 4.0 to price admitted subacute and non-acute services, and also includes shadow price weights using AN-SNAP Version 5.0 for admitted subacute and non-acute services. This represents the second year of shadow pricing for AN-SNAP Version 5.0.

## Back-casting

As with previous years, the Pricing Authority has recalculated ('back-cast') the NEP Determination 2022–23 (NEP22) to incorporate the most up-to-date cost data and to take account of methodological changes introduced in NEP23 which impact on the ability to compare the NEP between years. IHACPA is required to back-cast the previous year's NEP under clause A41 of the Addendum to the National Health Reform Agreement 2020–25 (the Addendum).

Back-casting is important to ensure the calculation of Commonwealth funding is not adversely impacted by changes in the calculation of the NEP over the years. Under the Addendum, the Commonwealth funds 45 per cent of the efficient growth in public hospital services which are funded on an activity basis with a growth cap of 6.5 per cent a year.

The Pricing Authority has recalculated NEP22 using more up-to-date cost data than was available when NEP22 was initially calculated.

The back-cast NEP22 results in an increase of 3.8 per cent between NEP22 to NEP23, which is the basis for Commonwealth growth funding for 2023–24.

| NEP22 | Back-cast NEP22 | NEP23 |
|---|---|---|
| $5,797 | $5,813 | $6,032 |

## 2.2 National Efficient Cost Determination 2023–24

The efficient cost of a small rural hospital is the sum of the fixed cost component and the variable cost component.

For 2023–24, the total modelled cost for block-funded hospitals up to 175 NWAU 2022–23 (NWAU(22)) comprises a fixed cost of $2.169 million and the variable cost of $5,984 per NWAU(22). An additional loading of 48.3 per cent is applied for 'very remote' hospitals.

In addition, the NEC Determination covers some services in public hospitals that do not meet the technical requirements for applying activity based funding. Usually this means that they cannot be counted and/or costed. For example, teaching, training and research and some non-admitted mental health services are instead provided a block-funding amount.

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

With this in mind, IHACPA will continue to block-fund programs that have been approved by the Pricing Authority for inclusion on the General List of In-Scope Public Hospital Services.

The Addendum contains provisions around specific arrangements for high cost, highly specialised therapies recommended for delivery in public hospitals by the Medical Services Advisory Committee. In 2023–24, the following high cost, highly specialised therapies are recommended for delivery in public hospitals, based on advice received from the Commonwealth:

- Kymriah® – for the treatment of acute lymphoblastic leukaemia in children and young adults.
- Kymriah® or Yescarta® – for the treatment of diffuse large B-cell lymphoma, primary mediastinal large B-cell lymphoma and transformed follicular lymphoma.
- Qarziba® – for the treatment of high risk neuroblastoma.
- Luxturna™ – for the treatment of inherited retinal dystrophies.
- Tecartus® – for the treatment of relapsed or refractory mantle cell lymphoma.

### Back-casting

The back-cast NEC Determination 2022–23 for the purpose of estimating Commonwealth growth funding between 2022–23 and 2023–24 is the sum of the fixed component and the variable component.

The fixed component is determined as:

- $2.108 million for hospitals with an annual NWAU(22) less than or equal to 175.
- $2.108 million less 0.029 per cent per NWAU(22) for hospitals with an annual NWAU(22) greater than 175, with an additional loading of 48.3 per cent for 'very remote' hospitals.

The variable component of the efficient cost is determined as $5,815 per NWAU(22) for hospitals with an annual NWAU(22) greater than 175.

# 3. More information

For more information about the Independent Health and Aged Care Pricing Authority, activity based funding and the National Efficient Price and National Efficient Cost Determinations for 2023–24, please visit www.ihacpa.gov.au or contact enquiries.ihacpa@ihacpa.gov.au


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