

Independent Hospital Pricing Authority

Understanding the NEP and NEC 2020–21

March 2020



IHPA

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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 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.

In order to make these Determinations, IHPA develops and publishes the annual [Pricing Framework for Australian Public Hospital Services](#) (the Pricing Framework). 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

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 0.7398 NWAU which equates to \$3,936.
- A coronary bypass (minor complexity) has a weight of 5.3468 NWAU which equates to \$28,445.
- A hip replacement (minor complexity) has a weight of 3.7733 NWAU which equates to \$20,074.

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 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.

Approximately 480 public hospitals nationwide, including all of the 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 the hip replacement in two different hospitals, which may assist jurisdictions to identify best practice and make funding decisions.

About the national efficient cost

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 373 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 funding and ABF.

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

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 efficient cost of a small rural hospital.

Summary of key changes

Based on the principles in the Pricing Framework for Australian Public Hospital Services 2020–21 (the Pricing Framework), IHPA has determined the national efficient price (NEP) and national efficient cost (NEC) for 2020–21.

National efficient price 2020–21

The NEP for 2020–21 is \$5,320 per national weighted activity unit (NWAU).

Some minor methodological improvements have been made to the NEP for 2020–21.

IHPA has incorporated an adjustment for non-admitted specialised paediatric services. The adjustment for a hospital acquired complication (HAC) has also been extended to include 'fourth degree perineal laceration during delivery' in line with Version 2.0 of the HAC list.

The NEP Determination 2020–21 also uses the Australian Bureau of Statistics' 2016 Australian Statistical Geography Standard Remoteness Area classification.

Back-casting

As with previous years, the Pricing Authority has recalculated ('back-cast') NEP19 to incorporate the most up-to-date cost data and to take account of methodological changes introduced in NEP20 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 (NHRA).

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 NHRA, 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 NEP19 using more up-to-date cost data than was available when NEP19 was initially calculated.

The back-cast NEP19 shows an increase of 2.1 per cent between NEP19 and NEP20, which is the basis for Commonwealth growth funding for 2020–21.

NEP19	Back-cast NEP19	NEP20
\$5,134	\$5,210	\$5,320

National efficient cost 2020–21

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

For 2020–21, the total modelled cost for block-funded hospitals up to 3,500 national weighed activity unit (NWAU) comprises a fixed cost of \$2.040 million and the variable cost of \$5,687 per NWAU. An additional loading of 39.1 per cent is applied for 'very remote' hospitals.

In addition, the NEC 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.

IHPA 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 IHPA's work and reference fostering clinical innovation whereby the pricing of public hospital services respond in a timely way to introduce evidence-based, effective new technology and innovations in the models of care that improve patient outcomes.

With this in mind IHPA will continue to block-fund patients on a trial basis in hospital avoidance programs that have been approved on the General List of In-Scope Public Hospital Services.

The NEC also includes costs for the CAR-T (Kymriah®) treatment in 2020–21 for New South Wales and Victoria, as agreed with the Commonwealth in 2019.

Back-casting

The back-cast NEC 2019–20 for the purpose of estimating Commonwealth growth funding estimated between 2019–20 and 2020–21 is the sum of the fixed component and the variable component.

The fixed component is determined as:

- \$1.954 million for hospitals with an annual NWAU(19) less than or equal to 176.
- \$1.954 million less 0.029 per cent per-NWAU(19) for hospitals with an annual NWAU(19) greater than 176, with an additional loading of 39.1 per cent for 'very remote' hospitals.

The variable component of the efficient cost is determined as \$5,448 per-NWAU(19) for hospitals with an annual NWAU(19) greater than 176.

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.

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