

Annual statement of reasonable GP fee increases 2009/10 update

May 2009



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WELLINGTON

Level 9, Axon House, 1 Willeston Street
PO Box 587
Wellington 6001
Ph: (64 4) 472 0590
Fax: (64 4) 472 0596

AUCKLAND

Level 17, West Plaza Building
3-5 Albert Street
Auckland 1010
Ph: (64 9) 913 6240
Fax: (64 9) 913 6241

Executive summary

This report presents the 2009/10 update of the annual statement of reasonable GP fee increase. The key points of the report are as follows:

- Primary Health Organisations (PHOs) and their practices use the annual statement to assess whether their proposed fee increases to the patient co-payment will be automatically accepted by their District Health Board (DHB) as 'reasonable' or whether they will need to be referred to a regional fee review committee. Fee increases that are equal to or less than the annual statement of increase will not require referral to a fee review committee.
- The methodology for production of the annual statement was developed in late 2006. The first statement related to the period 2005/06 and 2006/07. Subsequent updates have been developed on an annual basis and have been published by the end of May each year. The same methodology was followed for the production of this year's statement as for previous years.
- The method of calculating annual fee changes includes development of a weighted average of changes to prices of key inputs used to produce the services provided by practices. Specific components from three Statistics New Zealand indices are considered; together, they provide a measure of the extent to which changes in business input costs put pressure on the output prices charged for goods and services within primary health care. The combined impact of changes in these indices suggests an increase in key business input costs; in particular, the labour cost increases for the Health and Community Services remain a strong driver of upward movement, given the high weighting attributed to this component.
- The recommended annual statement of reasonable patient co-payment GP fee increase for 2009/10 is **6.5 per cent** based on a 50/50 capitation/co-payment split.

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1 Introduction

1.1 Purpose of the annual statement

This report presents the 2009/10 update of the annual statement of reasonable GP fee increase.

1.2 Context

1.2.1 Background

In 2006, a project team from LECG was commissioned by DHBNZ to develop a methodology for setting the annual statement of reasonable GP fee increases. The team worked under the guidance of an Advisory Group, involving representatives from DHBs and the primary health care sector. Once the methodology had been developed, LECG produced the first annual statements relating to the 2005/06 and 2006/07 June years. Subsequently, LECG has produced further update reports on an annual basis; DHBNZ commits to publish the statement each year by 31st May.

1.2.2 Application of the annual statement

Primary Health Organisations (PHOs) and their practices use the annual statement to assess whether their proposed fee increases to the patient co-payment will be automatically accepted by their DHB as 'reasonable' or whether they will need to be referred to a regional fee review committee. Fee increases that are equal to or less than the annual statement of increase will not require referral to a fee review committee.

In circumstances where the proposed fee increase is above the level determined in the annual statement, the fee review committee may permit the proposed increase where it views that there is a justifiable rationale, for example, some practice specific factors for which the annual statement methodology does not realistically account.

The annual statement attempts to reflect movement in the drivers of changes in GP fees. It does not attempt to infer or investigate what the absolute or relative level of GP fees should be. Nor does it suggest that fees should increase by the level of the annual statement. The methodology and the subsequent annual adjustment also do not make any inference as to the most efficient way to organise the delivery of care; changing models of care and practice composition are not considered.

2 Recap of methodology

2.1 Indices used

The method of calculating annual fee changes includes development of a weighted average of changes to prices of key inputs used to produce the services provided by GPs.

Three cost inputs are considered as outlined below. Together the three indices provide measures of the extent to which changes in business input costs put pressure on the output prices charged for goods and services.

2.1.1 Labour Cost Index

The price of labour is a major driver of potential changes in operating costs and hence the fees charged by practices. The measure used is the *Labour Cost Index – Salaries and Wage Rates* (LCI), which gives a measure of movements in the cost of labour. The index covers jobs filled by paid employees in all occupations and in all industries except for private households employing staff.

2.1.2 Producer's Price Index

The *Producer's Price Index - Inputs* (PPI-I) is a measure of the change in prices of items such as: materials; fuels and electricity; transport and communication; rent and lease of land; building, vehicles and plant; commission and contract services; business services; and insurance premiums less claims. It excludes labour depreciation costs and GST.

2.1.3 Capital Goods Price Index

The *Capital Goods Price Index* (CGPI) is a measure of the change in the general level of prices for physical capital assets (for example, buildings). It excludes large value items (such as aircraft) and second-hand equipment.

2.2 Annual statement calculation

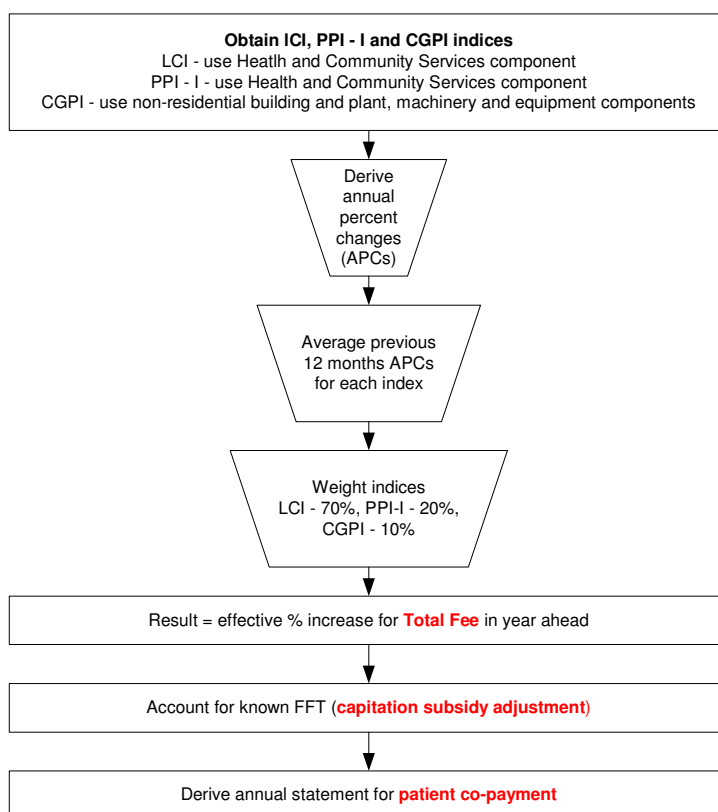
As described in previous reports, the process of calculation takes place sequentially (see Figure 1 below).

The first step involves processing of the Health and Community Services components of the labour cost and the producers price-inputs indices as well as the relevant components of the CGPI. We determine the annual percentage change for each index and average these over the previous 12 months.

Following this, we apply the agreed weightings to the respective indices. These weightings remain unchanged from those utilised in previous years: 70 per cent labour (LCI); 20 per cent other inputs (PPI-I); and 10 per cent for capital (5% for each component of CGPI).

Using this weighted average we calculate the first step in a two-stage process. In the first instance, we assess the effect of input cost changes on total fees (i.e. GP fees in the absence of capitation payments). From this, we use the known Future Funding Track adjustment (FFT) to derive the reasonable level of co-payment increase.

Figure 1: Schematic of calculation process



3 Changes in indices

3.1 Source of data

The most recent releases for the relevant indices, published by Statistics New Zealand in May 2009 for the March 2009 quarter, have been utilised to generate this annual statement. The relevant files can be accessed directly from the Statistics New Zealand website¹.

3.2 Overview of trends across indices

A summary of movements in relevant indices is provided below in Table 1.

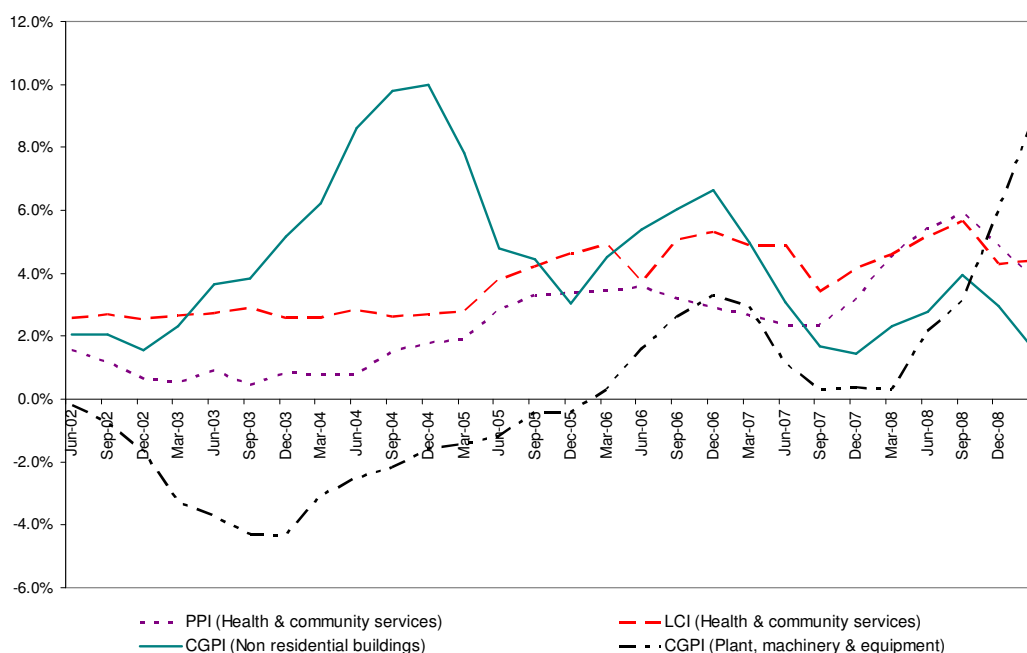
Table 1: Index movements to March 2009			
Index	Change from previous quarter (from Dec 09)	Percentage change from same quarter previous year (from March 08)	Average of annual percentage change²
PPI Inputs Health and community services	0.6%	3.8%	5.0%
LCI Health and community services	1.1%	4.4%	4.9%
CGPI Non-residential buildings	-0.4%	1.5%	2.8%
CGPI Plant machinery and equipment	2.7%	9.0%	5.1%

¹ <http://www.stats.govt.nz>

² This figure is the average of the annual percentage changes for each of the four quarters for the previous fiscal year. For example, for this 2009/10 update report, the figures provided in relation to each index above represent the average of the annual percentage changes for Jun 08, Sep 08, Dec 08 and Mar 09. These figures are used to derive the weighted average annual change, which is effectively the percentage increase allowable for the total fee in the year ahead, prior to adjustment for FFT.

The figure below represents the annual percent change for each quarter in the relevant indices over time, since June 2002.

Figure 2: Annual percentage change in contributing indices



Despite some recent easing across all indices other than the CGPI, since mid-late 2007 there has been an upward movement in all indices. Given the method used for the statement of deriving a moving average annual percentage change, it should be highlighted that the process allows for past changes to affect the current fee change amount.

3.3 Changes to each index reported at March 2009

3.3.1 Labour Cost Index (salary and wage rates)

Overview

For all industries combined, the LCI (salary and wage rates) showed a rise of 3.3% in salary and wage rates (including overtime), in the year from the March 2008 quarter to the March 2009 quarter. This is only slightly down from the previous year (the equivalent rate was 3.4 per cent) which represented the largest annual increase since production of the series began in 1992.

Health and Community Services component

In the year to March 2009, the Health and Community Services sector experienced a 4.4 per cent annual increase in salary and wage rates (including over-time); this growth was second only to that experienced within the Education sector, of 5.7 per cent.

In our update report last year, we indicated that strong growth in salary and wage rates at that time reflected the result of settlement of collective employment agreements and suggested that the pressure may potentially exacerbate rather than continue to ease. Continuing labour market shortages for particular groups of health professionals have continued to drive up costs.

3.3.2 Producer's Price Index Input

Overview

The annual percentage change for all industries combined from the March 2008 quarter was 4.7 per cent, in comparison with an equivalent figure of 7.3 per cent for the previous year. The most significant upward contribution to the PPI-I index came from the wholesale and trade index, followed by the air transport index, driven by higher crude oil prices. More recently, reductions in prices for imported crude oil have led to a decline of 2.5 per in the March 2009 quarter. This fall is the largest for a quarter since the series began in December 1997.

Health and Community Services component

For the Health and Community Services component of PPI-I, the annual percentage change from the period March 2008 to March 2009 was 3.8%, in comparison with 4.6% last year, representing some easing of pressure.

The PPI-I shows that the Health and Community Services sector faced a 0.6 per cent increase in prices in the March 2009 quarter, in comparison with a 2.5 per cent decrease in input prices for all industries combined. On an annual basis, the 3.8 per cent increase experienced by the Health and Community Services sector is slightly behind the 4.7 per cent annual change figure for all industries combined.

3.3.3 Capital Goods Price Index (CGPI)

Overview

The CGPI rose 1.2 per cent in the March 2009 quarter, broadly consistent with the increases in the previous two quarters. On an annual basis, the CGPI rose 4.9 per cent from the March 2008 to the March 2009 quarter. This is the largest annual movement since the series began in 1989.

Non-residential buildings component

Specifically, the non-residential component fell 0.4 per cent in the March 2009 quarter, which is the largest downward movement since the June 1998 quarter. The fall was driven by lower labour costs in the construction sector. It is in contrast to increases in three of the six asset groups (namely: plant, machinery and equipment; and construction).

However, overall there was an annual increase of 1.5 per cent in the year to March 2009. This represents the smallest upward movement since December 2007 (with figures of 2.3 per cent and 5.0 per cent in the years to March 2008 and March 2007 quarters respectively).

Plant, machinery and equipment component

The plant, machinery and equipment component made the most significant upward contribution to the CGPI, driven by rises in mining, quarry and construction machinery and in other special purpose equipment. In the year to March 2009, there was a significant increase of 9.0 per cent, the largest annual movement since the series inception in the December 1989 quarter. This rise follows a comparatively small increase in 0.3 per cent in the year to the March 2008 quarter and an increase of 2.8 per cent in the year to the March 2007 quarter.

4 Calculation of the annual statement

4.1 Step one: input-cost related adjustment rate

Using the process outlined in section 2.2, we generate a total fee adjustment rate of **4.8 per cent** for 2009/10. This percentage is determined using the average of the annual percentage change figures (values for the most recent quarter are cited in Table 1: Index movements to March 2009) and developing a weighted average, with the relative weightings for each index remaining the same as the methodology utilised in previous years. It represents the input-cost related change to the total fee for a given year, a crucial intermediate input into the annual statement determination.

Table 2 below provides the equivalent input-cost related adjustment factors for this and previous years.

Table 2: Input-cost related adjustment rate					
	2005/06	2006/07	2007/08	2008/09	2009/10
Input-cost related adjustment factor for total fee	2.6%	3.9%	4.4%	3.7%	4.8%

As shown above, the 2009/10 input-cost related adjustment rate is the highest yet during the history of development of the annual statement. The key drivers relate to a continuation this year of the strong growth in salary and wage rates seen last year, and to a lesser extent (given the lower weighting) the impact of the upward trend across the PPI-I and the two relevant components of the CGPI, particularly the plant, machinery and equipment component). We highlight again that there is a degree of lag built into the way in which the statement is calculated; hence the impact of the recent easing across all but the CGPI is diluted.

4.2 Step two: Adjustment for FFT and calculation of annual statement

Following the calculation of the input-cost related adjustment factor, we apply the known FFT adjustment (which is 3.116 per cent for 2009/10, rounded to 3.1 per cent in the table below) to derive the corresponding level of reasonable increase to co-payments.

Table 3: Future Funding Track adjustments

	2005/06	2006/07	2007/08	2008/09	2009/10
FFT adjustment	2.8%	3.3%	2.6%	2.8%	3.1%

As shown in table 4 below, based on a 50/50 capitation/co-payment revenue split, the annual statement figure for 2009/10 is **6.5 per cent**. As indicated in the table below, this is the highest level that has been determined for the reasonable percentage increase over the five years for which reports have been produced.,

Table 4: Annual levels for reasonable increases to GP patient co-payments

	2005/06	2006/07	2007/08	2008/09	2009/10
Level of reasonable patient co-payment (on basis of 50/50 capitation/co-payment split)	2.4%	4.5%	6.1%	4.7%	6.5%

This calculation is a function of the relativity between the capitation payment from the Government (the FFT adjustment) and the input-related adjustment factor for the total fee, given an assumed split.³ When the FFT adjustment is greater than the input-related adjustment factor, the co-payment increase will be less than the input-related adjustment factor.⁴ This was the case in 2005/06. The opposite is also true, as evidenced in 2006/07.

³ The fee template associated with the annual statement gives the opportunity to use practice, or practice group specific data where this split is not appropriate, as outlined in the next section.

⁴ This is because the weighting attached to the capitation subsidy is greater than that of the co-payment, meaning when the capitation adjustment is greater than the input-related adjustment factor, there is effectively less work to do by the co-payment in order for the total fee adjustment to match the change in costs faced by practices.

4.3 Alternative capitation/co-payment splits

The 6.5 per cent annual statement figure derived above is based on a 50/50 capitation/co-payment split. Various practices and practice groups may have different splits based on their total revenue from both sources.

The table below provides the annual statement change for various capitation/co-payment splits, compared with the equivalent figures for previous annual statements.

Table 5: Annual statement and general adjustments for different capitation/co-payment splits

	2005/06	2006/07	2007/08	2008/09	2009/10
Level of reasonable patient co-payment GP fee increase (assuming 80/20 split)	1.8%	6.3%	11.4%	7.5%	11.5%
Level of reasonable patient co-payment GP fee increase (assuming 70/30 split)	2.1%	5.3%	8.5%	5.9%	8.7%
Level of reasonable patient co-payment GP fee increase (assuming 60/40 split)	2.3%	4.8%	7.0%	5.1%	7.3%
Level of reasonable patient co-payment GP fee increase (assuming 50/50 split)	2.4%	4.5%	6.1%	4.7%	6.5%