

Public Benefit Test
Northern Territory
NCP Review of Pharmacy

Response
of

Australian Friendly Societies Pharmacies
Association Inc.

(AFSPA)

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Executive Summary

- 1. It is the strong submission of the Australian Friendly Society Pharmacies Association (AFSPA) that the provisions of contained in Schedule 8 of the Northern Territory *Health Practitioners Act 2004* fail to meet the National Competition Council requirement that the benefits of the restriction to the community as a whole outweigh the costs.**
- 2. The new pharmacy ownership restrictions now prohibit a friendly society from owning a pharmacy without Ministerial approval which can only be granted in specific circumstances. This new restrictive provision is directly contrary to the recommendations of COAG.**
- 3. Friendly societies are "approved pharmacists" under the provisions of the *National Health Act 1953* and are permitted owners of pharmacy elsewhere in Australia and their exclusion from the jurisdiction of the Northern Territory, except with special Ministerial approval, will deprive the people of the Territory of choice in pharmacy services and the opportunity to access their pharmacy needs at lower prices.**
- 4. Friendly societies are mutual not-for-profit entities that provide their members and the community with quality pharmacy services at the lowest prices permitted under the PBS. All profits from the pharmacy are invested back into the business to provide rebates to their members in the form of lower prices.**
- 5. All friendly society pharmacies have strong policies to provide significant additional free health related and testing services to consumers; many employ community health nurses and other related health professionals. And they are significant financial contributors to community activities and causes.**
- 6. There appears to be no discernable public benefit for their exclusion from the community pharmacy industry in the Northern Territory and this review should find that the provisions of schedule 8 of the Act are not in the public interest and should be amended to include friendly societies in the pharmacy ownership provisions.**

1. Background to the Review

On 1 April the *Health Practitioners Act 2004* (the Act) was passed. That Act now contains provisions which introduce restrictions on who can own and operate a pharmacy in the Northern Territory.

The restrictions referred to are that, only a registered pharmacist may own pharmacy whereas before, ownership was unrestricted. The new restriction now prohibits a friendly society from owning a pharmacy unless it has Ministerial approval which can only be given if specific criteria are satisfied..

These new provisions now require assessment by the National Competition Council (NCC) as to whether the restriction can be justified as being in the public interest or benefit and that the objective/s of the restriction can only be achieved by such legislation.

For this purpose WalterTurnbull consulting firm have been commissioned by the NT Professional Licensing Authority to undertake a review to determine whether the pharmacy ownership restrictions contained in Schedule 8 of the Act meet the public benefit interest test in accordance with Clause 1 (3) of the Competition Principles Agreement

2. Competition Policy Background

National Competition Policy emerged as a direct consequence of commitments entered into by all Governments in Australia when they signed the 1995 Competition Principles Agreement (CPA). The signing of this Agreement was the culmination of work commenced in 1991 when it was agreed to examine a national approach to competition policy.

The first step in this process was the establishment of the National Policy Review Committee chaired by Professor Fred Hilmer. Next, the recommendations of the Hilmer Report resulted in the enactment of the *Competition Policy Reform Act 1995* (CPRA). The main elements of this Act: enabled the provisions of Part IV of *The Trade Practices Act 1974* to be extended to all jurisdictions and to apply to all businesses and persons carrying on a business whether incorporated or not; established the Australian Competition and Consumer Commission (ACCC) by the merger of the Trade Practices Commission and the Prices Surveillance Authority; and created a new advisory body, the National Competition Council.

The CPRA is complemented by a number of inter-governmental Agreements including the Conduct Code Agreement (CCA) and the Competition Principles Agreement. This second Agreement sets out the principles governments will follow in relation to prices oversight, structural reform of public monopolies, review of anti-competitive legislation and regulations, access to services provided by essential facilities and the elimination of net competitive advantage enjoyed by government businesses when they compete with the private sector.

All the heads of Australian Governments at the Council of Australian Governments (COAG) meeting in April 1995 signed these Agreements. Collectively, these Agreements make up a package of reforms referred to as the National Competition Policy (NCP).

3. About National Competition Policy (NCP)

Broadly, this package of reforms is directed towards ensuring that every business or industry in the Australian economy that is currently sheltered from competition is opened to it *except for those businesses or industries for which it can be demonstrated that there is a net community benefit in restricting competition.*

This provision is referred to as the public benefit or interest test. This test requires that governments, when reviewing various NCP reform options, must objectively weigh up all the pros and cons of competition including, but not restricted to, its effects on matters such as employment, equity, social welfare, community service obligations and the interests of consumers generally or a class of consumers.

The rationale for competition reform is that, properly harnessed, competition can boost economic performance and enhance consumer welfare. But the reasons go beyond narrow economic efficiency considerations and touch on matters as, for example, business ethics, environmental sustainability and social equity.

It aims to promote economic goals such as a better allocation of resources between industries and greater flexibility to adapt to rapid changes such as external shocks. The reforms to Government businesses allow them to more transparently address their social obligations as well as providing the opportunity for more informed decisions on whether those obligations are best met by in-house providers or otherwise.

Competition policy also provides a greater element of public scrutiny *and makes it more difficult for governments to provide favours for "friendly" business groups or to strike deals behind closed doors.*¹

The NCP processes do not seek to favour any kind of business over another, nor are they designed to improve the profitability or viability of specific industries themselves. Rather, they are intended to foster conditions in which the businesses that most benefit the community prevail or prosper.

Whilst many sectors of the economy are exposed on a daily basis to the true rigours of a competitive marketplace, some groups are not subject to the same disciplines. As a matter of equity it is right to question the incomes and conditions enjoyed by all special groups *to the extent that those incomes and conditions derive from unwarranted restrictions on competition.*²

Under the NCP Agreements the onus of proof is on those groups who want to retain legislative restrictions to prove that they should be retained.

Once a legislative restriction is identified it must go unless it be robustly demonstrated that the benefits of the restrictions outweigh the costs and that the objective of the restrictions cannot be achieved in other ways.

¹ Graeme Samuel, President NCC, speech to Economics Society Qld 25 November 1998.

² Graeme Samuel, President NCC, speech to Australian Retailers Association 30 May 1998

4. Review of Pharmacy Legislation under NCP

Under the provisions of the second Agreement, the CPA, it was agreed that a joint national review of State/Territory pharmacy legislation and certain provisions of Commonwealth legislation relating to the Pharmaceutical Benefits Scheme (PBS) and the *National Health Act 1953* would be conducted.

That review was conducted by Mr Warwick Wilkinson (the National Review) and his recommendations were released in his Final Report in February 2000.

The fundamental recommendation of the National Review was:

Recommendation 1:

- *legislative restrictions on who may own and operate community pharmacy be retained; and*
- *with existing exceptions, the ownership and control of community pharmacies continues to be confined to registered pharmacists.*

In other words, the National Review recommended that no new entities be permitted to own and operate a pharmacy and that the existing permitted entities, including friendly societies, be retained.

Subsequently the Prime Minister wrote to all Premiers and Chief Ministers proposing that COAG provide a coordinated response to the recommendations of the National Review to promote a nationally consistent approach to pharmacy legislation.

COAG referred the recommendations of the National Review to a Senior Officials Working Group for consideration and to advise whether a coordinated response could be made by COAG and to advise on appropriate responses from each jurisdiction.

The COAG Senior Officials Working Group Report was released on 2 August 2002. It recommended that COAG accept most of the National Review's recommendations and highlighted some significant parts of those recommendations that it recommended to COAG not to accept.

In regard to friendly societies the Senior Officials Working Group Report recommended against introducing new restrictions that would prevent the entry of new friendly societies into the community pharmacy industry noting that the National Review did not demonstrate a net public benefit to justify such restrictions.

Additionally, in recognition of an election commitment made by the Prime Minister to the Pharmacy Guild of Australia (the Guild) in October 2001 it agreed that the ACCC should be requested to inquire into the relative financial and corporate differences between friendly society dispensaries (FSDs) and pharmacist owned community pharmacies and whether these adversely affected competition in the pharmacy industry.

The Treasurer referred this matter to the ACCC as follows:

“(The ACCC) will need to consider whether the tax treatment of FSDs and other competition related factors provide FSDs with significant competitive advantages over pharmacist-owned pharmacies.”

The ACCC concluded its review and its report was furnished to the Treasurer. The ACCC prepared its report in consultation with interested parties, relevant Government bodies as well as expert advice.

It concluded that friendly societies do not have significant competitive advantages over pharmacist-owned pharmacies.

5. National Competition Council 2003 Report

The 2003 Progress report on the legislative review progress of all governments found that no governments had satisfied their compliance obligations in regard to pharmacy.

For pharmacy, the NCC indicated that to be assessed as having complied with the National Competition Agreement sufficiently to merit full payment of the competition monies, governments were required to implement the following two core Council of Australian Governments (COAG) recommendations:

- removal of the restriction on the number of pharmacies able to be owned by pharmacist-owners and friendly societies; and
- removal of any discriminatory legislative provisions applying to friendly society owned pharmacies.

In reaching this conclusion the NCC in its report emphasised the extensiveness of the review process that had been undertaken, the detail of the work performed by the COAG Senior Officers Working Group which consisted of senior officials from all jurisdictions and that all governments had signed off on the final recommendations but noting a reservation from NSW.

The NCC went on to report that against this background it expected governments to expedite progress in the pharmacy area and that it would scrutinise reforms to ensure that they did not discriminate against friendly societies in those jurisdictions where they are located currently, or in jurisdictions where they do not currently have a presence.

6. NT Health Practitioners Act 2004 (Schedule 8)

Prior to the enactment of this legislation it had been held by the National Review that there were no ownership restrictions in either the NT or the ACT. All other jurisdictions prohibited pharmacy ownership to only a registered pharmacist or a friendly society.

Additionally, at the time of the National Review other jurisdictions restricted the number of pharmacies permitted to be owned by pharmacist from variously 2 pharmacies to 4 depending on the jurisdiction. Friendly societies were unrestricted in the number of pharmacies permitted to be owned except in SA where one friendly society (National Pharmacies) is restricted to the ownership of 31 pharmacies in that State.

It was found by the National Review that on balance after taking a number of factors into consideration, that the present ownership provisions should be retained. It concluded that there was a public benefit in maintaining the present pharmacy ownership structure of, predominately, pharmacist only and the mutual not-for-profit friendly societies.

It has been argued that the National Review recommended that pharmacy ownership should be restricted to only registered pharmacists. And it appears that the Northern Territory's new restrictive legislation has been based on this premise.

It is most important to emphasise that the National Review did not reach such a conclusion. As stated earlier, its key recommendation was that the present ownership provisions be retained and this included friendly societies.

The National Review's key recommendations consisted of a suite of proposed reforms that, it argued, if they were implemented would justify the retention and the continuation of restrictive ownership provisions that otherwise might be considered anti-competitive.

However, that reasoning by the Review is certainly challengeable if the package of key recommendations are "cherry picked". The exclusion of friendly societies from pharmacy ownership by the provisions of Schedule 8 is an extreme example of "cherry picking" from the package of required reforms. It constitutes a new and real restriction against a previously permitted pharmacy owner and as such its justification must be tested robustly against the public benefit criteria.

7. The Public Benefit Test

Clause 1(3) of the Competition Principles Agreement allows for Governments to assess the net benefits of different ways of achieving particular social objectives and states:

'Without limiting the matters that may be taken into account, where this Agreement calls:

- a) for the benefits of a particular policy or course of action to be balanced against the costs of the policy or course of action; or
- b) for the merits or appropriateness of a particular policy or course of action to be determined; or
- c) for an assessment of the most effective means of achieving a policy objective;

the following matters shall, where relevant, be taken into account:

- i) government legislation and policies relating to ecologically sustainable development;
- ii) social welfare and equity considerations, including community service obligations;
- iii) government legislation and policies relating to matters such as occupational health and safety, industrial relations and access and equity;
- iv) economic and regional development, including employment and investment growth;
- v) the interests of consumers generally or of a class of consumers;
- vi) the competitiveness of Australian businesses; and
- vii) the efficient allocation of resources.

Against these criteria it cannot be ascertained what is the public benefit in friendly societies being prohibited from being permitted owners of pharmacy in the NT.

Anti-competitive legislation must have a discernable and identifiable public benefit which is able to be measured against the above criteria in order to be justifiable under the CPA. Protecting the public interest by mandating that identifiable services must only be delivered by a qualified and registered person must not be confused with the concept that the ownership of the business that delivers that service must also only be owned by a registered person.

It has been argued that safe and ethical pharmacy services can only be guaranteed if the business is owned by a pharmacist. There is no evidence for such a claim. In fact there is considerable evidence to the contrary.

Friendly society pharmacies have been providing pharmacy services at the highest standards elsewhere in Australia since the 1840's.

All pharmacy legislation in Australia has stringent provisions requiring that a pharmacy must be in the control of and under the supervision of a pharmacist at all times it is open. It is this provision that ensures the proper and safe delivery of all scheduled medicines.

8 Friendly Society Pharmacies and their Association

The Australian Friendly Societies Pharmacies Association Inc. is the national body representing the interests of its members who are not-for-profit friendly society pharmacies recognised by relevant legislation within the Commonwealth of Australia.

Australia wide there are 34 friendly societies which own and operate a total of 131 not-for-profit pharmacies which represents around 2.3% of the total number of approved pharmacies. Collectively these friendly societies have memberships of approximately 400,000 representing some 800,000 individuals and in 2002/03 dispensed over 7.3 million prescriptions.

All friendly society owned pharmacies are accredited under the Guild's Quality Care Pharmacy Program. In fact friendly society owned pharmacies were the first "banner" group of pharmacies to achieve 100% accreditation.

A History

Friendly society dispensaries were first established in Australia by friendly societies in the 1840's. Their establishment then was in direct response to two significant problems of the day:

- The high cost of medicines for their, mainly poor, members; and
- The fact that many chemists commonly adulterated their drugs³.

The purpose of friendly societies in establishing their own Dispensaries was to ensure the supply to their members of quality medicines as prescribed and at an affordable price. They were able to do this because the Dispensaries were established and operated by the friendly societies on a true not-for-profit, co-operative principle.

³ *Mutual Aid or Welfare State* Australia's Friendly Societies David Green & Lawrence Cromwell ISBN 086861 6567

Throughout their history in Australia from those very early days up to and including the present time the not-for-profit pharmacies have had to struggle for their continued survival against the powerful vested interests of the members of the Pharmacy Guild.

The present restrictions on friendly society pharmacies are as a direct consequence of the successful campaign of the Guild to persuade Governments at that time to restrict friendly societies so that they could not compete with the pharmacist owned pharmacies.

It was argued then that the development of the Pharmaceutical Benefits Scheme by the Commonwealth meant that as all members of the community would have access to subsidised medicines there was no longer a role for the not-for-profit pharmacies.

The friendly society pharmacies vehemently disagreed with that premise then, as it continues to do so today.

And this is despite the fact that under the Third Community Pharmacy Agreement between itself and the Federal Government, the Guild is committed to the continued development of an effective, efficient and well distributed community pharmacy service in Australia which takes account of the recommendations of the Competition Policy Review of Pharmacy and the Objectives of National Competition Policy.⁴

The Guild continues to use the language of yesteryear to justify its members' absolute monopoly of the provision of an essential public health function: the safe and professional custody and dispensing of prescribed medicines to the community. As recently as 1 June 2004 in a letter to the Victorian Premier the Guild described friendly society pharmacies as an "anachronistic sector which at least one economist has described as a dinosaur".

The reality is that friendly society pharmacies continue to flourish and where they operate they have brought more affordable pharmaceuticals to their members and increased competition and professional service to the community⁵. They continually provide the best range and quality of pharmaceutical products at the most affordable prices. For the payment of an annual membership contribution to a friendly society pharmacy a member obtains rebates/discounts on their pharmacy purchases. The pharmacy prices are competitive and available to members of the public.

Friendly society pharmacies are the longest, continuous operators of the business of pharmacy in Australia. They have achieved this with no prosecutions for breaches of professional regulations and they hold a legitimate place in the future of the community pharmacy industry.

Their Role Today

It has been argued that the rise of the welfare state and the provision of Government services in industries where once only charitable and not-for-profit organisations operated means that there is now no longer a role for such entities. Such arguments might have had more validity some decades ago when the costs of such services provided by Government were more balanced against the community's needs for such services. That is certainly not so today.

⁴ Third Community Pharmacy Agreement, Objectives c) page 8

⁵ Report to the Pharmacy Board Victoria: The Regulation of Pharmacists and Pharmacy Business August 1998

The ability of Government to continue to meet the rising needs of the community in a range of social welfare areas and particularly in the health care industry is limited. The role of the not-for-profit sector is as important today as it ever was. This was emphasised by the Prime Minister in his Federation speech when he outlined the view that traditional state-centered welfare has failed to prevent social problems. The role of community organisations needed to be enhanced and that his Government was committed to promoting a re-engagement with the community and the work performed by the not-for-profit sector.⁶

The Prime Minister's recent personal intervention into the community pharmacy industry against the not-for-profit pharmacy sector seems to represent a retreat from this position. This is unfortunate and bodes ill for the not-for-profit sector because what starts in one sector as a result of Government policy or intervention generally is often carried through to other sectors.

The value to the community of the work performed by the not-for-profit sector has long been recognised by the taxation system as providing a measure of vertical equity that could not be compensated by government provided services at the same costs. Not-for-profit entities such as friendly society pharmacies do not provide their services for a commercial intent; they provide their services as true co-operatives investing in services for the benefit of the community for the purpose of improving members' better health outcomes at the lowest possible cost.

Friendly society pharmacies are taxed as mutuals or co-operatives under the "principle of mutuality" in accordance with the provisions of Division 9 of the *Income Tax Assessment Act 1936*. Simply, this provides that income derived from trading with its members is not taxed and furthermore, the expenses incurred in earning that member income is excluded as a taxable deduction. But when applied to friendly society pharmacies all income received under the PBS is excluded from the mutuality principle and is fully taxable in the same manner as other pharmacies.

During 1998 the Ralph committee undertook a full review of Australia's tax laws. That committee, in taxation terms, described in a Discussion Paper horizontal equity as being, broadly, taxpayers (including business entities) in similar circumstances should be taxed similarly. Vertical equity was described also broadly, as being that tax burdens should depend on ability to pay and that those more able to pay (should pay) more tax.⁷

That Discussion Paper focused on business taxation policy and to what extent business tax should be based on horizontal equity allowing the personal tax system and social security and related payments systems to reflect vertical equity concerns. It particularly looked at the operation of the mutuality principle as part of the business tax system.

The Ralph Review concluded that the mutuality principle should continue to be applied to certain business entities *including friendly societies and their dispensaries* and that this should be given explicit effect to in the tax law⁸.

Despite these findings the Guild and the Pharmaceutical Society of Australia continue to proclaim that this provision gives friendly society pharmacies an unfair trading

⁶ Federation Address "The Australian Way" delivered by Prime Minister, 28 January 1999

⁷ Review of Business Taxation (RBT) Discussion Paper *A Strong Foundation*. November 1998

⁸ RBT *A Tax System Redesigned* Report, July 1999 (the Ralph Report).

advantage⁹. This issue has now, as reported above, been finally concluded by the inquiry most recently conducted by the ACCC which reported that friendly societies do not have a significant competitive advantage in relation to pharmacist-owned pharmacies.

For-profit entities provide services for which the profit margins are within commercial benchmarks in order to provide a return on capital invested. In contrast the emphasis of not-for-profit entities is to return surpluses to the business to fund services, reinvest in and replace assets and in improving services to their members and the public that would be unlikely to be undertaken by the for-profit entity.

The election of office holders and members of the Board and attendance at annual and general meetings vest ownership of these pharmacies in their members who participate in the policy development of their pharmacy by the normal manner of such societies whilst the management of the pharmacy is in the control of the pharmacist superintendent. Ownership is transparent, accountable and not a tradable commodity.

Friendly society pharmacies as mutual co-operatives have been stringently controlled under State legislation for financial and other probity matters and as of 1 July 1999, as a result of Financial Sector Reform legislative changes, are fully corporatised under the Commonwealth Corporations legislation and under regulation of the Australian Securities and Investments Commission.

9. Issues For Comment

(1) Whether any restrictions on competition arise from schedule 8 of the Act

The key restriction that arises from schedule 8 of the Act is the clear exclusion of friendly societies as permitted owners of pharmacy. This restriction is in clear contradiction of the recommendations of the National Review and of COAG.

Friendly societies are mutual not-for-profit entities whose objectives are to provide to their members and the communities where they are located the best pharmacy services at the lowest possible price.

Where ever they operate they bring a new dynamic to the community pharmacy industry and importantly provide consumers with a choice of pharmacy provider. Prohibiting them from the industry deprives consumers of choice and the opportunity for lower prices in those categories where discounting is permitted.

The *National Health Act 1953* prohibits discounting of the co-contribution fee required to be paid by consumers.

(2) The operation of the Third Australian Community Pharmacy Agreement as a factor

The above Agreement is made under provisions of the *National Health Act 1953* The parties to the Agreement are the Guild and the Minister for Health and Ageing. Its provisions are applicable to all "approved pharmacists" under that Act. Friendly societies are "approved pharmacists" for the purposes of that Act. An approved pharmacist is a

⁹ Pharmacy Guild letter to Premier Victoria 1 June 2004

person or entity approved to dispense PBS medicines from a pharmacy owned by them. (An approved pharmacist is not an employee pharmacist).

The various provisions of the Agreement are applied by different instruments enacted pursuant to relevant provisions of the Act and again, are applicable to all "approved pharmacists".

The key provision of the Agreement is to set out the mechanism for the calculation of the remuneration to be paid by the Commonwealth to each "approved pharmacist". The remuneration arrangements are based on a risk sharing arrangement for the purpose of keeping the costs of the PBS sustainable.

Savings in costs are achieved in a number of ways but principally through the approval mechanism which limits the total number of pharmacies throughout Australia and only allows new pharmacies to be opened by the application of strict location rules. Further the viability of existing pharmacies is secured by restricting the relocation of pharmacies.

Consequently competition in the industry between pharmacies is constrained.

If friendly societies were permitted to own pharmacy in the NT a society would either have to buy an existing pharmacy or qualify under the strict location rules applying to a new pharmacy. Approvals for a new pharmacy are considered by the Community Pharmacy Authority strictly in order of application.

(3) Factors unique to the regulation of pharmacy in the NT

The Territory's vast areas and numerous remote Aboriginal communities make the delivery of community pharmacy services particularly challenging. The new ownership restrictions deprive the NT of the opportunity to explore new and innovative models of pharmacy delivery services such as a local council owned pharmacy employing pharmacists or other possible arrangements such as Private Public Partnerships (PPPs).

The traditional pharmacist only ownership model is not necessarily the best way to ensure pharmacy services to remote and or uneconomic regions. The financial risks and the professional isolation are significant deterrents including the concern of not being able to sell the business in the future.

The Ministerial approval provision included in schedule 8 does not address these issues and in fact adds to them. If a non-pharmacist entity did get approval and undertook the financial risks that entity in turn would also face the concern of the ability to sell the business at some time in the future.

10. Conclusion

Under the NCP process the review of pharmacy legislation has been one of the most comprehensive, detailed and protracted reviews undertaken.

The recommendations for changes to the community pharmacy finally arrived at namely:

- that the restrictions on the number of pharmacies permitted to be owned, be removed; and
- that the restrictions on friendly societies be removed.

are modest and balanced. The implementation of them was judged as being capable of opening the community pharmacy industry only to a degree carefully calculated to give the industry the potential to become more competitive and more responsive to the needs of both urban and rural communities.¹⁰

The new restrictive pharmacy ownership provisions in the NT are regressive and anti-competitive. If implemented they will have the effect of depriving the people of the Territory of choice in pharmacy services and the opportunity of accessing medicines at lower prices where these are permitted.

The Government will have lost the opportunity to encourage and explore new and innovative models for the delivery of pharmacy services to particularly its remote Aboriginal communities.

The delivery of scheduled medicines into the community is one of the most regulated industries and the pharmacist only ownership provision is not the key provision to the wellbeing and safety of the community. The pharmacist in charge provision is the most important rule.

¹⁰ Chairman, National Review of Pharmacy Mr W Wilkinson. Letter to Prime Minister 8 January 2000.