

Fifth Community Pharmacy Agreement

Introduction

- 2.1 Chapter 2 focuses on the key issues raised in the Australian National Audit Office (ANAO) Report No. 25 (2014-15). The chapter comprises:
- an overview of the report, including the audit objective, scope and criteria;
 - audit conclusion; and
 - audit recommendations and agencies' responses.

Report overview

- 2.2 The Australian Government provides subsidised medicines to Australians and eligible overseas visitors through the Pharmaceutical Benefits Scheme (PBS). In 2013-14, the PBS subsidised over 210 million prescriptions at a reported cost to government of some \$9.15 billion. The Government also subsidised an additional 12.4 million prescriptions in 2013-14 to the veteran community through the Repatriation Pharmaceutical Benefits Scheme (RPBS), at a cost of \$397.9 million.¹
- 2.3 Since 1990, the Australian Government has entered into and funded successive five year community pharmacy agreements, at a cost of over \$45 billion, to help maintain a national network of approximately 5,460 retail pharmacies as the primary means of dispensing PBS medicines to the public. The Government has also used the agreements to fund

¹ Australian National Audit Office (ANAO), *Report No. 25 2014-15 Administration of the Fifth Community Pharmacy Agreement*, p. 15.

professional programs, and to establish a funding pool to be drawn on by pharmaceutical wholesalers that can meet specified service standards for supplying PBS medicines to retail pharmacies.²

- 2.4 The Fifth Community Pharmacy Agreement (5CPA) was the agreement for the period July 2010 to June 2015 between the Minister for Health, representing the Commonwealth, and the Pharmacy Guild of Australia (Pharmacy Guild), representing the majority of retail pharmacies currently approved to supply PBS medicines.³ The introduction to the 5CPA states that:

Community pharmacy is an integral part of the infrastructure of the health care system in its role in primary health care through the delivery of the Pharmaceutical Benefits Scheme and related services.⁴

The Fifth Community Pharmacy Agreement

- 2.5 To support community access to pharmaceutical services, the 5CPA provided that the Australian Government would deliver \$15.4 billion in funding from 1 July 2010 to 30 June 2015 as follows:
- \$13.8 billion in ‘pharmacy remuneration’ including various fees for approved pharmacists – the owners of retail pharmacies that dispense PBS and RPBS subsidised medicines to the public;
 - \$663 million for several categories of government funded professional programs; and
 - \$950 million to be shared among eligible pharmaceutical wholesalers from a Community Service Obligation (CSO) funding pool, an arrangement which generally requires participating wholesalers to be able to supply the full range of PBS items to any retail pharmacy in Australia within 24 hours at an agreed price.⁵
- 2.6 One of the key objectives of the 5CPA negotiations was to achieve savings to contribute to the structural repair of the Commonwealth Budget as there had been high cost growth under the 4CPA (an average growth of 9.4 per cent per year) that was due, in part, to a \$1.1 billion transitional

2 ANAO, *Report No. 25 2014-15*, p. 15.

3 The Pharmacy Guild is a registered employers’ organisation, which advised the ANAO that it represents the owners of approximately 77 per cent of the 5,457 retail pharmacies currently approved to supply PBS items.

4 ANAO, *Report No. 25 2014-15*, p. 15.

5 ANAO, *Report No. 25 2014-15*, p. 16.

structural adjustment package (financial assistance) to assist pharmacies adjust to the introduction of Price Disclosure in 2007.⁶

2.7 The 5CPA anticipated that the initiatives covered by the agreement would result in \$1 billion in government savings. The major savings initiatives were:

- cessation of the PBS Online incentive payment (\$417.7 million);
- freezing the dispensing fee for two years (\$281.5 million);
- cessation of underperforming professional programs (\$226.4 million);
- reduction in private hospital pharmacy remuneration (\$35.3 million); and
- freezing the CSO Funding Pool for one year (\$19.2 million).⁷

2.8 The 5CPA also referenced the Australian Government's Pharmacy Location Rules (Location Rules), which regulated where new pharmacies that dispense PBS prescriptions may open and where existing pharmacies may relocate.

2.9 Six broad 'principles and objectives' were specified in the 5CPA:

- ensure a fair Commonwealth price was paid to Approved Pharmacists for providing pharmaceutical benefits while maximising the value to taxpayers by encouraging an effective and efficient community pharmacy network.
- ensure that the Programs were patient-focused and target areas of need in the community including continued improvement in community pharmacy services provided to Aboriginal and Torres Strait Islander people.
- ensure transparency and accountability in the expenditure of the Funds.
- promote the PBS's sustainability and efficiency within the broader context of health reform and ensuring that community resources continued to be appropriately directed across the health system, while also supporting the sustainability and viability of an effective community pharmacy sector.
- maintain a co-operative relationship between the Commonwealth and the Guild.
- ensure the Location Rules work for the benefit of the Australian community including increased access to community pharmacies for the population of rural and remote areas.⁸

6 ANAO, *Report No. 25 2014-15*, p. 16.

7 ANAO, *Report No. 25 2014-15*, p. 17.

8 ANAO, *Report No. 25 2014-15*, p. 17.

- 2.10 The 5CPA was a complex multi-part agreement underpinned by a number of further agreements between the Department of Health (Health) and the other entities involved in its administration, including: the Department of Human Services (Human Services); the Pharmacy Guild of Australia; and Australian Healthcare Associates (AHA). The Pharmacy Guild and AHA are non-government entities.⁹

Administrative arrangements

- 2.11 The 5CPA was developed and negotiated by Health and agreed by government. Health had overarching responsibility for its administration. Until 1 March 2014, Human Services administered most 5CPA professional programs on behalf of Health (valued at \$583 million), while the Pharmacy Guild administered some of the smaller programs (valued at \$67 million). On 1 March 2014, Health transferred responsibility for the administration of all 5CPA professional programs to the Pharmacy Guild.¹⁰ This means that, in respect of the 5CPA, the Pharmacy Guild was variously:

- an industry association and advocate acting on behalf of retail pharmacy owners, making representations to government and public inquiries, and conducting public campaigns;
- a publicly funded administrator under the 5CPA, at times acting as the Department of Health's agent;
- a recipient of Commonwealth grants relating to certain 5CPA professional programs;
- an owner of business enterprises that sell products and services to pharmacies on a commercial basis – with some products and services relating to 5CPA programs and activities; and
- an advisor to Health, through its co-membership of the overarching 5CPA governance body under its contracts within the department.¹¹

Audit objective, scope and criteria

Audit objective and scope

- 2.12 The audit objective was to assess the effectiveness of the development and administration of the 5CPA, and the extent to which the 5CPA had met its objectives. The audit examined the development and negotiation of the 5CPA by the then Department of Health and Ageing (now the Department
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9 ANAO, *Report No. 25 2014-15*, p. 17.

10 ANAO, *Report No. 25 2014-15*, p. 18.

11 ANAO, *Report No. 25 2014-15*, p. 18.

of Health), and the administration of the 5CPA by Health. The audit also examined aspects of the 5CPA that were implemented by Human Services and the DVA.¹²

2.13 While the ANAO did not examine the Pharmacy Guild's administration of 5CPA professional programs, the audit referred to aspects of its involvement relating to the development, negotiation and administration of the 5CPA.

2.14 The Pharmacy Location Rules were not examined in this performance audit.¹³ They were considered in 2014 by the report of the National Commission of Audit and the draft report of the National Competition Policy Review.

Criteria

2.15 To form a conclusion against the audit objective, the ANAO adopted the following high level criteria:

- the 5CPA provided transparent and accountable remuneration arrangements for the dispensing of Commonwealth pharmaceutical benefits, which achieved value for money, consistent with Government policy;
- the 5CPA's funding and savings commitments were being met;
- the additional programs and services funded under the 5CPA were managed effectively and provided value for money; and
- the 5CPA performance framework enabled an assessment of the extent to which the 5CPA was meeting its objectives.¹⁴

Methodology

2.16 The audit methodology included:

- interviewing staff from Health, Human Services and DVA;
- extracting pharmacy claims and payment records from Health and Human Services databases;
- reviewing relevant documentation, including departmental files, briefings, legal advice, program guidelines, monitoring and reporting systems, reviews, evaluations and correspondence;
- consulting stakeholders and peak bodies, including the Pharmacy Guild; and

12 ANAO, *Report No. 25 2014-15*, p. 19.

13 The Committee did not consider pharmacy location rules as part of the review of ANAO Report 25 (2014-15).

14 ANAO, *Report No. 25 2014-15*, p. 20.

- reviewing over 100 stakeholder submissions received by the ANAO through its citizens' input facility.¹⁵

Audit findings

2.17 The ANAO report identified various short-comings in the administration and outcomes of the 5CPA. These short-comings were significant, and the ANAO report provided a thorough examination.

Oversight, transparency and value for money

5CPA committed the government to deliver a fixed sum of money disconnected from demand

2.18 Although actual expenditure on the components of pharmacy remuneration was demand driven – depending on the number of PBS and RPBS medicines prescribed by doctors – the 5CPA committed the government to delivering a fixed sum of money. There was no formal mechanism in place to reconcile actual expenditures on pharmacy remuneration against funding specified in the 5CPA.¹⁶

No means for Parliament to be informed of the costs of key 5CPA components

2.19 The 5CPA did not clearly document expected net savings under the agreement, and there was no straightforward means for the Parliament and other stakeholders to be informed of the expected or actual cost of key 5CPA components.

- The agreement did not document that some \$2.2 billion of the \$13.8 billion that the Commonwealth 'will deliver' for pharmacy remuneration was sourced from patient co-payments, which were not a cost to government.
- The department's annual report aggregated the cost of pharmacy remuneration (expenditure on services) with the cost of PBS medicines (expenditure on products), without differentiating between the two types of expenditure.¹⁷

Health could not accurately determine whether the Commonwealth is getting value for money

2.20 Limited departmental information, plus shortcomings in Health's performance reporting and 5CPA evaluation framework, meant that the department was not well positioned to assess whether the Commonwealth was receiving value for money from the agreement overall, or performance against the agreement's principles and objectives.¹⁸

15 ANAO, *Report No. 25 2014-15*, p. 21.

16 ANAO, *Report No. 25 2014-15*, p. 21.

17 ANAO, *Report No. 25 2014-15*, p. 25.

18 ANAO, *Report No. 25 2014-15*, p. 24.

2.21 While some aspects of the agreement were evaluated, the 5CPA evaluation framework did not make provision for reviews of the agreement's two major financial components – pharmacy remuneration (\$13.8 billion) and CSO payments to pharmaceutical wholesalers (\$950 million). Indeed, pharmacy remuneration has not been fully reviewed since 1989.¹⁹

Key negotiation objectives not realised

Health did not achieve key negotiation objectives for the 5CPA

- Objective regarding the restructuring of pharmacy remuneration arrangements 'to diminish their link to the price of PBS medicines' was not realised with the structure of remuneration remaining essentially unchanged from 4CPA to 5CPA.²⁰
- Objective (considered non-negotiable by Ministers) regarding obtaining access from pharmacies to the full range of PBS data, including information relating to prescriptions that cost less than the general patient co-payment (which would help the Commonwealth determine actual PBS pharmacy remuneration from all sources, including patients and the total volume and cost of the PBS to both government and consumers) was only partially realised. The 5CPA only made provision for pharmacies to provide certain prescription information from 1 April 2012; it did not make provision for the receipt of cost information.²¹
- Objective relating to support for IT systems that are fully interoperable with broader e-health systems was not realised. The two Prescription Exchange Services (PESs) that were approved by Health for the purpose of downloading electronic prescriptions by pharmacies did not have systems that were interoperable and government funding was subsequently re-allocated to pay the PESs directly to make their systems interoperable.²²

2.22 Regarding the 'non-negotiable' Commonwealth objectives that were not met, Health advised the ANAO in February 2015 that 'in any negotiation, objectives may or may not be fully realised for a variety of factors. While it is therefore correct that not all the negotiating objectives agreed by Government prior to the commencement of the negotiations were met – it is reasonable to assert that nonetheless, Government was satisfied sufficient objectives were realised through their agreement to the final

19 ANAO, *Report No. 25 2014-15*, pp. 24-25.

20 ANAO, *Report No. 25 2014-15*, p. 86.

21 ANAO, *Report No. 25 2014-15*, p. 86.

22 ANAO, *Report No. 25 2014-15*, p. 91.

package of measures at the conclusion of negotiations, as approved by Cabinet.²³

Significant administrative issues – keeping records, seeking approvals, and meeting legislative requirements

Shortcomings in key aspects of administration, negotiation, and implementation

2.23 There were shortcomings in key aspects of Health's administration at the development, negotiation and implementation phases of the 5CPA. The ANAO identified key issues relating to: the clarity of the 5CPA and related public reporting; record-keeping; the application of financial framework requirements; risk management; and seeking Ministerial approvals.

- Health did not keep a formal record of its meetings with the Pharmacy Guild during the 5CPA negotiations, and did not document its subsequent discussions with the Guild on the negotiation of related contracts.²⁴
- Health did not assess whether financial framework requirements would apply to the Pharmacy Guild officials when making payments of public money pursuant to the administration of 5CPA professional programs, resulting in a risk of non-compliance with legislative requirements.²⁵
- Health reallocated funds without prior Ministerial approval (as required under the 5CPA) for:
 - ⇒ \$5.8 million communication strategy to be delivered by the Pharmacy Guild. Despite not being a professional program, the communication strategy was nonetheless funded mainly from professional program allocations; and
 - ⇒ \$7.3 million of funding originally approved by Ministers as a component of pharmacy remuneration (the Electronic Prescription Fee (EPF)) to other purposes, including financial assistance paid to Prescription Exchange Services and \$896,110 to the Pharmacy Guild to increase pharmacies' understanding, awareness and uptake of EPF. Health advised that discussions were held with the Minister's office but was unable to provide documented evidence to support this.²⁶

23 ANAO, *Report No. 25 2014-15*, p. 91.

24 ANAO, *Report No. 25 2014-15*, p. 25.

25 ANAO, *Report No. 25 2014-15*, p. 25.

26 ANAO, *Report No. 25 2014-15*, p. 26.

Poor estimation methodology with regards to savings

- 2.24 The 5CPA stated that the initiatives covered by the agreement would result in \$1 billion in gross savings over the term of the agreement (net savings were estimated to be \$600 million). However, ANAO analysis indicated that the net savings estimated before the agreement was signed were closer to \$400 million due to shortcomings in Health's 5CPA estimation methodology. The principle issues related to: unexplained increases in the baseline cost of professional programs; the application of inappropriate indexation factors; and the treatment of patient co-payments.²⁷ In particular:
- The baseline budget for 5CPA professional programs in the Commonwealth forward estimates was \$638.7 million (before adjusting for the negotiated 5CPA savings and spending measures). However, Health's records showed that the approved baseline budget for 5CPA professional programs was only \$511.6 million, and there was no documentary evidence of authority to increase the 5CPA baseline budget in the forward estimates by \$127.1 million.
 - The official indexation factors released by the then Department of Finance and Deregulation (Finance) were not utilised in estimating 5CPA savings, resulting in an overestimate of 5CPA savings of approximately \$43.2 million.
 - Health advised, in the course of this audit, that the estimated savings for the 5CPA incorrectly included \$42.7 million in co-payments made by patients to pharmacies for the receipt of pharmaceutical benefits. Co-payments are a private contribution to the cost of PBS medicines, which are not a cost to government.

Audit conclusion

- 2.25 The 5CPA was the head agreement in a complex scheme of legal, financial and administrative arrangements involving both government entities and third parties in its implementation. The 5CPA arrangements were developed and negotiated by Health, which had overarching responsibility for the 5CPA's administration, and agreed by Government.
- 2.26 Overall, the Health's administration of the 5CPA had been mixed, and there was a limited basis for assessing the extent to which the 5CPA had met its key objectives, including the achievement of \$1 billion in expected savings. The department developed and negotiated a complex agreement and related contracts with the Pharmacy Guild in a timely manner, enabling the 5CPA to be signed by the Health Minister and Pharmacy

27 ANAO, *Report No. 25 2014-15*, p. 22.

Guild on 3 May 2010, prior to the expiry of the 4CPA on 30 June 2010. However, a number of key government negotiating objectives for the 5CPA were only partially realised and there have been shortcomings in key aspects of Health's administration at the development, negotiation and implementation phases.

- 2.27 Actual pharmacy remuneration (paid by government and patients) in the first four years of the 5CPA aligned closely with the commitment made originally in the 5CPA. However, during the life of the agreement there had been two estimates variations (in 2011 and 2013) relating to the cost of one component of pharmacy remuneration – the Premium Free Dispensing Incentive – which increased the expected cost to government of pharmacy remuneration by \$292 million and also impacted the level of savings from the 5CPA.
- 2.28 In addition to the shortfall in anticipated savings, a number of the Government's other strategic negotiating objectives were only partially realised, as previously indicated. In this context, the then Government and department considered that the 5CPA offered an opportunity to improve health outcomes and value for money by restructuring pharmacy remuneration arrangements 'to diminish their link to the price of PBS medicines'. The Commonwealth anticipated doing so by shifting financial incentives from the volume driven sale of medicines to the delivery of value-adding professional services. However, the structure of pharmacy remuneration remained essentially unchanged and key wholesaler and pharmacy mark ups continued at previous rates.
- 2.29 Six broad principles and objectives were included in the 5CPA. Limited departmental information, plus shortcomings in Health's performance reporting and 5CPA evaluation framework, mean that the department was not well positioned to assess whether the Commonwealth was receiving value for money from the agreement overall, or performance against the six principles and objectives.
- 2.30 In addition to shortcomings in 5CPA costings, performance reporting and the evaluation framework, this audit identified scope for improvement in key aspects of the department's general administration which covered the 5CPA's development, negotiation and implementation phases.
- 2.31 The 5CPA was a substantial agreement that was integral to the parties achieving shared objectives – the maintenance of a national network of retail pharmacies as the primary means of dispensing PBS medicines to the public, and providing professional services to patients. Features of the 5CPA included complexity in policy design and administrative arrangements, and a key lesson of the audit was the importance of identifying and treating risks at the earliest opportunity. The successful

implementation of complex programs requires active management and a disciplined and co-ordinated approach to managing risks and challenges through the program life cycle – including the development, costing, negotiation and implementation phases. Further, there is a need to ensure that there is appropriate authority for revised positions and outcomes when events do not unfold according to expectations.

Audit recommendations and agency response

2.32 Table 2.2 sets out the recommendations for ANAO Report No. 25 (2014-15) and the agencies' responses.

Table 2.2 ANAO recommendations, Report No. 25 (2014-15)

1	<p>To clarify the nature of financial commitments entered into by the Australian Government, the ANAO recommends that the Department of Health presents, in key documents, estimated government payments and patient payments for both subsidised and unsubsidised Pharmaceutical Benefits Scheme and Repatriation Pharmaceutical Benefits Scheme medicines.</p>
	<p>Health response: <i>Agreed.</i></p>
2	<p>To provide assurance regarding the basis of costings for the next community pharmacy agreement, the ANAO recommends that the Department of Health applies the relevant forecast indexation factors released by the Department of Finance.</p>
	<p>Health response: <i>Agreed.</i></p>
3	<p>To improve its ability to satisfy accountability requirements and capacity to protect the interests of the Commonwealth in the event of disputes or legal action, the ANAO recommends that the Department of Health:</p> <ul style="list-style-type: none"> • maintains an adequate record of the negotiation of the next community pharmacy agreement and related contracts; and • reviews its internal guidance on record keeping for the negotiation of significant contracts and agreements.
	<p>Health response: <i>Agreed.</i></p>
4	<p>To improve the accuracy and transparency of reporting on Australian Government expenditure under the Pharmaceutical Benefits Scheme and the Repatriation Pharmaceutical Benefits Scheme, the ANAO recommends that the Departments of Health, Veterans' Affairs and Human Services liaise on the collection, recording and sharing of information regarding payments to suppliers, so as to clearly identify the actual cost of medicines and the components of pharmacy remuneration.</p>
	<p>Health response: <i>Agreed.</i></p>
	<p>Veterans' Affairs response: <i>Agreed.</i></p>
	<p>Human Services response: <i>Agreed.</i></p>
5	<p>In order to effectively discharge its advisory, accountability and contract management obligations in a timely manner, the ANAO recommends that the Department of Health reviews its record keeping arrangements for the Fifth Community Pharmacy Agreement and the next community pharmacy agreement.</p>

Health response: *Agreed.*

- 6 To improve transparency in agreement-making, the ANAO recommends that the Department of Health documents anticipated levels of Australian Government funding for third party administration for the next community pharmacy agreement.

Health response: *Agreed.*

- 7 To improve transparency and the quality of program performance reporting, the ANAO recommends that the Department of Health reports annually on the actual cost of each major component of the Fifth Community Pharmacy Agreement and the next community pharmacy agreement, including pharmacy remuneration, CSO wholesaler payments and professional programs.

Health response: *Agreed.*

- 8 To inform decision-making and the assessment of outcomes by stakeholders, the ANAO recommends that the Department of Health reviews performance reporting to improve alignment between the next community pharmacy agreement and public reporting against the program objectives, deliverables and KPIs relating to the department's Program 2.1 and Program 2.2.

Health response: *Agreed.*
