ow do you manage to attract government subsidies, obtain government protection from competition and arguably simultaneously use your monopoly power to engage in anticompetitive pricing practices ... all while claiming that you are acting in the public interest? Easy — if you are the Pharmacy Guild.

The Guild represents Australia's 4500 community pharmacies and, as reported in the last edition of *Consuming Interest*, it is currently negotiating a Fourth Pharmacy Agreement with the Government. What has become clearer since then is how the present Agreement gives a kind of tacit approval for anti-competitive pricing practices for some PBS (Pharmaceutical Benefits Scheme) drugs and we suspect the Guild is likely to push for similar protection in this new Agreement.

If you are thinking that this all sounds a bit dry and complicated, bear in mind that these sorts of anti-competitive practices have significant costs for consumers. The practices set an artificially high floor price for some medications and the people who suffer most from this sort of price inflation are people with chronic conditions—people with diabetes, mental illness, hypertension and cholesterol problems for example.

Well, how are they doing it and what can be done to stop it?

# What's going on?

This is complicated — which is, no doubt, how this practice has slipped by unnoticed for so long. To understand it you will, unfortunately, have to become more acquainted with the arcane practices of pharmacy pricing than you might like. But the implications of it are very important for consumers.

Nicola Ballenden is the Consumers' Association's health policy officer.



# Protected species: the community pharmacist

- 1. Every five years the Guild and the Commonwealth Government negotiate a National Community Pharmacy Agreement. The present Agreement finishes on 30 June 2005 and a new Agreement is currently being negotiated. 2. The primary purpose of the Agreement is to determine the level of reimbursement provided to pharmacists by the Government for each medication dispensed under the Pharmaceutical Benefits Scheme (PBS).
- 3. The process by which the reimbursement level is agreed involves the following steps:
- The Guild and the Government agree on the 'Commonwealth price' for each benefit item. The Commonwealth price is an estimate of the total retail cost to pharmacists and includes the wholesale price of the medication to pharmacists plus a dispensing fee which was \$4.70 per dispensed item in late 2004.
- The Government separately determines the maximum PBS copayment amount. This is currently \$28.60 for a general patient and \$4.60 for concession card holders.

The level of reimbursement for each drug is then determined as the Commonwealth price less the copayment amount. If this value is zero or negative then the pharmacist receives no reimbursement from the Government. That is:

- Reimbursement for drug n =Commonwealth price minus copayment.
- The level of co-payment will differ depending on whether the consumer is a concession card holder or not. As a consequence, for drugs where the Commonwealth price is below \$28.60 but above \$4.60 there will be no subsidy if the consumer is a 'general patient' but there will be a subsidy if the consumer is a concession card holder.
- 4. As well as agreeing to the Commonwealth price upon which the Government will base its reimbursement (as per point 3 above), the Agreement also permits an additional patient charge which, when combined with the Commonwealth price, will equal

the list or agreed price as defined in subsection 84C (7) of the National Health Act 1953. This fee is also known as the safety net recording fee which is set at a maximum of \$0.95. This 'fee' does not affect the level of reimbursement paid by the Government because it is not a component of the Commonwealth price. However, this agreed amount does have a role in the implementation of the Government's PBS safety net scheme. Under this policy if a general patient's 'recognised spending' on PBS drugs exceeds \$874.90 p.a. then they receive a subsidy from the Government. The maximum 'recognised spending' on any drug is equal to the Commonwealth price plus the 'additional patient charge'.

Then comes a further additional patient charge of up to \$3.36 (calculated

as 10% of the general patient co-payment plus \$0.50). This further additional co-payment charge plays no role in setting either subsidies paid by the Government to pharmacists or those paid to consumers. In the Agreement it's noted that this charge is "not initiated by the Commonwealth" and the Agreement requires pharmacists to inform customers that the Government does not initiate this charge. In

practice, it is not clear

that this requirement is enforced or even enforceable (see page 11).

- 5. The sum of the above amounts (that is, the Commonwealth price plus the 'additional patient charge' plus the 'further additional patient charge') is then communicated to pharmacists in a number of ways, including:
- Within the Agreement itself which is publicly available from both the Department of Health and Ageing and the Guild.
- In the pricing component of software (WiniFRED) part-owned and distributed by the Guild to pharmacists.

### What does it all mean for consumers?

Basically the Commonwealth is allowing the charging of an unjustified fee through the 'further additional patient charge' that applies to 'below co-payment' PBS drugs sold to general patients. While the language implies that the Government is not very happy with this arrangement, the fee is in the Agreement nevertheless. The inclusion of the fee also undermines other parts of the Pharmacy Agreement — paragraph 60.3, for example, which states that approved pharmacists are free to discount these items below the list

To us it seems likely that negotiations hit an impasse — the Guild wanted more taxpayers' money than the Government

BASICALLY THE COMMONWEALTH IS ALLOWING THE CHARGING OF AN UNJUSTIFIED FEE THROUGH THE 'FURTHER ADDITIONAL PATIENT CHARGE' THAT APPLIES TO 'BELOW CO-PAYMENT' PBS DRUGS SOLD TO GENERAL PATIENTS. WHILE THE LANGUAGE IMPLIES THAT THE **GOVERNMENT IS NOT VERY HAPPY WITH** THIS ARRANGEMENT. THE FEE IS IN THE AGREEMENT NEVERTHELESS.

> wanted to part with. Instead they agreed to pass this on to consumers. And it looks to us as if they did it in such a complicated way that it was unlikely anyone would ever work out what was going on. Well, bad luck — we did.

> ACA believes that the likely effect of this 'further additional patient charge' is to set an artificially high floor price for all below-co-payment PBS medications. The Pharmacy Guild, on the other hand, says pharmacists set their own prices in a competitive market, and the additional charges set out in the Agreement are purely suggestions/examples. The Government says much the same thing.

We did some research to check the extent to which pharmacists applied the \$3.36 'further additional patient charge'.

In February 2005 we looked at the prices some pharmacies in Sydney and surrounding areas were charging for Logynon EDx4, a common contraceptive pill. We phoned 20 pharmacies: two did not stock the medicine, there was no reply from one and the results from the remaining 17 are listed in the graph below.

The Commonwealth price for Logynon EDx4 is currently \$15.26. This means that the pharmacy will be able to purchase the drug from the manufacturer at a price not exceeding \$9.60 and many pharmacies are able to purchase the medicine at well below this level. The difference between \$9.60 and \$15.26 is explained by the fact that the formula for estimating the Commonwealth price (that is, the price at which the Commonwealth will subsidise sales of that drug to concession card holders) includes a 10% mark-up (\$0.96) plus a \$4.70 dispensing charge as a margin to cover the pharmacist's costs.

If this was a competitive market, you

might expect that pharmacies would price around the Commonwealth price of \$15.26 or even below given that many of them are buying the medicines at below the Government-set 'wholesale price'.

As can be seen from the graph, only two pharmacies priced the medication at close to the Commonwealth price. The remaining 15 pharmacies each priced it at a level close to the maximum price that would result from a mechanistic acceptance of the additional charges described in the Agreement and communicated to pharmacists by the Pharmacy Guild.

As the inclusion of the further additional patient charge appears to be fairly standard practice, none of the pharmacies we visited informed us — as they are supposed to under the Agreement — that "this was not a charge initiated by the Commonwealth government". Two respondents to our calls even told us that the \$19.60 charge (a charge that includes the 'further additional patient charge') was a "standard price" and that we wouldn't find much variation.

While it appears as though pharmacists are ready enough to use

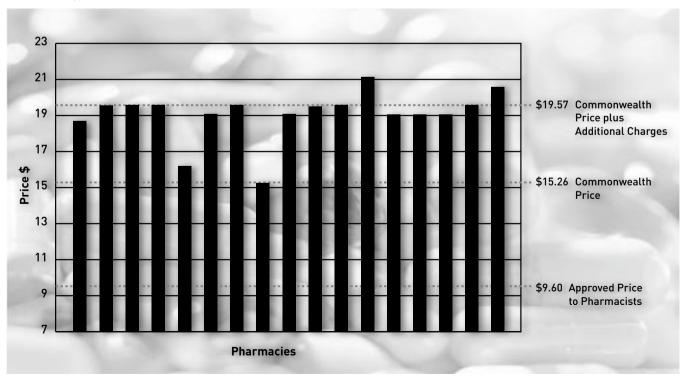
those parts of the Agreement that help them to price anti-competitively, they seem blithely unaware of their obligations to inform consumers of the nature of any extra charges (that is, that they "are not initiated by the Government") or of the fact that the Pharmacy Agreement actually allows discounting of below-copayment PBS drugs.

It would also appear that the practice could be in breach of the Trade Practices Act. Under Section 45A(1) of the Act, an organisation is prohibited from entering into a contract, arrangement or understanding that has the purpose, effect or likely effect of fixing, controlling or maintaining prices. These arrangements are deemed to substantially lessen competition and are therefore prohibited.

It is interesting to note that in its submission to the Dawson review of 2002, the Guild recognised that previous recommendations it had issued, relating to the fees for dispensing PBS items, could represent a breach of the price-fixing provisions of the Act. Given these concerns the Guild sought advice from a trade practices barrister who advised as follows:

"In my view, the practice of the Guild,

## Price of Logynon EDx4 in NSW Pharmacies



if it were to continue would expose the Guild to a high risk of a finding that it had the effect of fixing, and even more clearly, maintaining prices. Given the level of penalties which now prevails, any significant risk would be unacceptable, much less the high risk which in

in WiniFRED, the software distributed to community pharmacists. As mentioned earlier, this software is part-owned by the Guild. Both the Commonwealth price and all additional charges outlined in clause 60.1 of the Agreement are automatically programmed into this

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my view would apply in the present circumstances."

In addition to the above, the Guild was advised that an application for ACCC authorisation of the conduct was unlikely to be successful.

Despite this it appears that the practice is continuing through the inclusion of the 'further additional patient charge' in pricing that comes up

software to calculate the recommended price of each relevant item. If a pharmacist using this software package wished to charge less than this amount, he or she would be required to alter the price components specified in the program. In our view this represents a strong inducement to pharmacists to charge the price recommended in section 60.1 of the Agreement.

### What ACA wants

First, it is clear that this sort of charge has no place in the Pharmacy Agreement. It is anti-competitive and means that consumers are paying much higher prices than they need to for a range of essential medicines. ACA is pushing for these changes:

- 1. Exclusion of such charges in any further Commonwealth/Guild Pharmacy Agreement.
- 2. The Pharmacy Agreement to more prominently state that discounting is permitted for below-co-payment PBS medicines.
- 3. The Guild to desist from sending price guides to its members, either through software or any other published materials.
- 4. The Guild, the ACCC and the Department of Health and Ageing to undertake a communications campaign aimed at informing pharmacists of the Pharmacy Agreement's approval of discounting and encouraging them to discount.
- 5. The publication of 'price only' advertising of below-co-payment PBS medications should be examined to encourage more competition in this field.

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