



The Pharmacy
Guild of Australia

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COMMUNITY PHARMACY
DELIVERING ACCESSIBILITY, QUALITY AND
CHOICE FOR ALL AUSTRALIANS

SUBMISSION IN RESPONSE TO
THE COMPETITION POLICY REVIEW DRAFT REPORT

SUMMARY

Community Pharmacy's critical role

Community pharmacy in Australia is an essential, cost-effective, highly trusted and accessible health care destination. It has the capacity, skills and willingness to deliver a considerably broader set of services and functions for the Australian community, in collaboration with other health professionals, to improve health outcomes.

Regulation for the benefit of patients

The Australian community pharmacy sector operates within a framework of regulations to deliver medicines to the public in a safe, timely, convenient, affordable and equitable manner. This is consistent with the central objective of the National Medicines Policy, intended to achieve the distinct Government aim of delivering the Pharmaceutical Benefits Scheme (PBS) in a way that ensures guaranteed availability, the quality use of medicines and the viability of the sector.

Whilst the Government has a clear interest in controlling the cost of the PBS, it also has a number of broader health and social policy objectives that are intended to support the wellbeing of the Australian community, such as ensuring universal access to high quality pharmaceutical services for the Australian population.

The Review Panel's recommendation

Following the receipt of submissions in response to its Issues Paper released in April 2014, the Review Panel's Draft Report recommended that regulations governing the location and ownership of community pharmacies be removed, asserting that they restrict competition, limit consumer choice, result in poor health outcomes, and are costly for taxpayers.

However, the Review Panel provides no evidence to support its assertions and, in fact, the Panel indicated that existing restrictions have not prevented new pharmacy models from evolving.

Without having considered and evaluated the supporting policies that would be required, the Review Panel is not in a position to conclude that the current arrangements are inferior to undefined alternatives. Given the role of the community pharmacy network in delivering on public policy objectives via the Pharmaceutical Benefits Scheme (PBS) and other programs, the onus of proof should rest with the proponents of change.

Moreover, the Panel has not identified an effective alternative for achieving the underlying policy objectives of ensuring access and quality advice to consumers at an acceptable cost to the budget, instead drawing parallels to general practitioners (GPs) and referring to unspecified 'empirical evidence'. However:

- » The absence of locational regulations for GPs has clearly not enabled equitable access to health care services for all Australians. On the contrary, despite a range of costly interventions, the lack of success of different incentive programs in encouraging medical professionals to move to regional, rural and remote Australia suggests that devising effective mechanisms to achieve this objective through direct subsidies is inherently problematic.
- » Furthermore, the empirical evidence from overseas shows that removing location and ownership restrictions carries significant risks in terms of the accessibility of medicines, particularly to those who most require them, and of horizontal and vertical industry consolidation in the pharmacy sector (raising concerns about market power). In a number of cases, these outcomes have required new policy interventions.



Efficiency rationale for ownership and location rules

Ownership and location restrictions help achieve the Government's overall economic and social policy goals. Specifically, they need to be seen in the wider context of the Government's interest in structuring the commercial framework for the supply of dispensing and advisory services in a manner that is not only efficient, but that also achieves broader social and health policy objectives.

The location rules give rise to a spread of pharmacies that provides a very high level of access and choice without unnecessary duplication of fixed costs.

Ownership rules encourage efficiency in the provision of community pharmacy services while ensuring that these services are provided to an appropriate quality standard. By contracting with independent owner-pharmacists, the Government preserves the strong efficiency incentives that exist in franchise relationships. Owner-pharmacists have an enhanced incentive to conduct themselves and their pharmacies ethically and professionally, and not risk loss of registration and, therefore, loss of value in the pharmacy.

Overall, the restrictions on ownership and location are parts of the package of measures that enable Government to achieve its objectives in an efficient way.

Additionally and importantly, the ownership rules limit concentration in the supply of dispensing services. This provides crucial benefits to Government, as it prevents a situation emerging where the Government, to meet its objectives, would have to purchase distribution services from suppliers with substantial market power. For example, if the Government were to provide for access to the PBS through supermarkets, it would need agreements with the two very large supermarket providers that dominate the market. It is inevitable – and consistent with any economic theory of bargaining – that these two dominant providers would have a high degree of bargaining power in this situation and would hence be able to secure monopoly rents at taxpayers' expense. By avoiding this outcome, the ownership rules result in a substantial public benefit.

The economic literature suggests the location and ownership rules can interact in ways that create net gains to the community. Thus, the location rules can support and reinforce quality performance incentives that arise from the ownership rules. These effects arise because well-defined 'catchment' areas for pharmacies can assure pharmacists that competitors will not 'free-ride' on the advisory and other services they provide. These services are 'free' for consumers, but costly to provide for pharmacists. To the extent to which these effects occur, pharmacists will be incentivised to provide health services without being undercut on price by competitors who do not provide them.

Effectiveness of the regulations – the Evidence

The Guild undertook three streams of new research and analysis:

- » Geospatial analysis of pharmacy location in Australia relative to other vital services such as supermarkets, banking and medical centres (by MacroPlan Dimasi, a leading geo-spatial advisory firm);
- » Qualitative survey of consumer preferences for community pharmacy relative to alternative models of service delivery (by Institute for Choice, a leading academic choice modelling centre); and
- » Willingness to pay valuation of community pharmacy, again relative to alternative models of service delivery (by Institute for Choice).

These three streams form the inputs into a cost benefit analysis (CBA) of the current regulatory arrangements. The economic analysis and the cost benefit analysis were provided by Professor Henry Ergas and Professor Jonathan Pincus.

The empirical analysis undertaken demonstrates that, far from limiting access and choice, the community pharmacy model provides near universal access, high quality service and choice for consumers.

The key messages from the geo-spatial analysis:

- » Using detailed data on locations, the research demonstrates that pharmacy accessibility is high, both in absolute and relative terms, throughout Australia, including for the elderly (less mobile) and low socio-economic communities.
- » For Australia as a whole, pharmacies are in almost every case more accessible than the other three services studied (being supermarkets, banking and medical centres).
- » Crucially, the excellent accessibility to pharmacy services in regional areas provided by the community pharmacy model is not secured at the expense of access in urban areas. Rather, there is a very high degree of choice relative to other essential services, and this does not compromise accessibility in regional areas. As a result, it is simply factually incorrect to claim that consumers have less access to competing outlets than in other service sectors.

- » The data shows that there is high accessibility for those aged 65+ and for low socio-demographics both in absolute and relative terms. This is especially important as there is no reason to believe that a similar outcome would be achieved were locational decisions unrestricted.
- » The data, therefore, strongly supports the hypothesis that the community pharmacy model provides choice and similar levels of competition in urban areas, and that it provides better access compared to supermarkets, banks and medical centres in regional and rural/remote areas.

It is particularly noteworthy that community pharmacy achieves this very high level of accessibility at a significantly lower 'bricks and mortar' cost than the other services as a direct result of the locational rules in place.

Table 1: Accessibility at Grade 1 level (2.5km urban and regional)¹

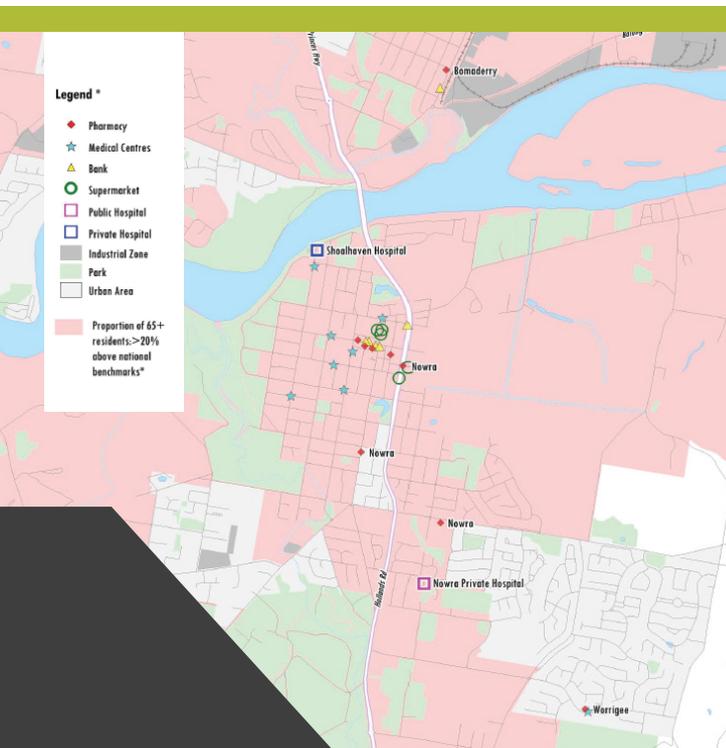
At Grade 2	Pharmacy	Supermarket	Bank	Medical centre
City	95	93	84	91
Rest of State/Territory	72	65	56	58
Total	87	83	75	80

Source: MacroPlan Dimasi analysis.

Table 2: Accessibility at Grade 2 level (urban (2.5km) and regional (5.0km))²

At Grade 2	Pharmacy	Supermarket	Bank	Medical centre
City	92	89	80	91
Rest of State/Territory	69	65	66	70
Total	84	81	76	84

Source: MacroPlan Dimasi analysis.



Geo-Spatial map Nowra (NSW)

1 'Grade 1 Accessibility' is defined as the proportion of people having access to at least 1 supermarket/pharmacy/medical centre/bank within a 2.5km radius in Metropolitan Areas and either a 2.5km or 5.0km radius in Regional Areas (depending on the simulation being run).
 2 'Grade 2 Accessibility' is defined as the proportion of people having access to at least 2 supermarkets/pharmacies/medical centres/banks within a 2.5km radius in Metropolitan Areas and either a 2.5km or 5.0km radius in Regional Areas (depending on the simulation being run).

The results of the consumer survey:

- » 89 per cent of consumers trust their local pharmacist either very highly or completely;
- » 64 per cent of consumers support the principle that professionals should own the business they work in;
- » Community pharmacies have a clear advantage over supermarkets in terms of trust and quality of service and in relation to the managing of patients' health information; and
- » Consumers trust their local pharmacist to deliver the medicines they need at a level that greatly exceeds their trust in other potential sources of supply.

In absolute terms, the overwhelming majority of survey respondents place a high degree of trust in the ability of their local pharmacy to provide the best service and advice.

These findings are consistent with the results of a similar study conducted by the Guild in 1999³. This indicates consumers have held a positive view of pharmacy and pharmacists over a sustained period of time (15 years). Similarly, the majority of consumers continue to be unsupportive of supermarket chains owning and operating pharmacies.

Cost benefit analysis

The Guild commissioned a cost benefit analysis (CBA) of the Review Panel's draft recommendation to dismantle the community pharmacy model, utilising the new geospatial and consumer survey evidence.

The CBA assessed the value that consumers place on the services pharmacies provide and examined changes in net benefits under alternative scenarios. The methodology is based on the results of a rigorous microeconomic analysis of a detailed consumer survey to derive estimates of consumer valuations of various pharmacy attributes such as convenience, product range, advice and price.

Drawing on the valuations derived from the survey, the likely costs to consumers of altering the structure of supply can be compared to the likely benefits. The results of the CBA are stark in showing a significant reduction in consumer welfare under alternative scenarios where location and ownership rules are removed.

These results are conservative, not only in terms of the assumptions on which they are based, but also because they take no account of other likely effects of removing the rules. For example, were major supermarket chains to secure a high market share in dispensing services, the Government would have less bargaining power in purchasing those services and would therefore incur higher costs.

They demonstrate that consumers – particularly those that are eligible for PBS concessional status (who are the main consumers of medicines and pharmacy services) – would consistently suffer a loss in consumer surplus⁴ and would therefore be worse off as a result of the Review Panel's proposed changes:

- » Given consumer preferences, as revealed in the consumer survey, even a small loss of trust or increase in travel time represents a significant loss in consumer surplus. Individually or in combination, the removal of the location and ownership rules would therefore harm consumers.
- » Consumers value trust and travel time more than they do price reductions, so even a hypothesised fall in prices would not offset the consequent loss in consumer surplus.

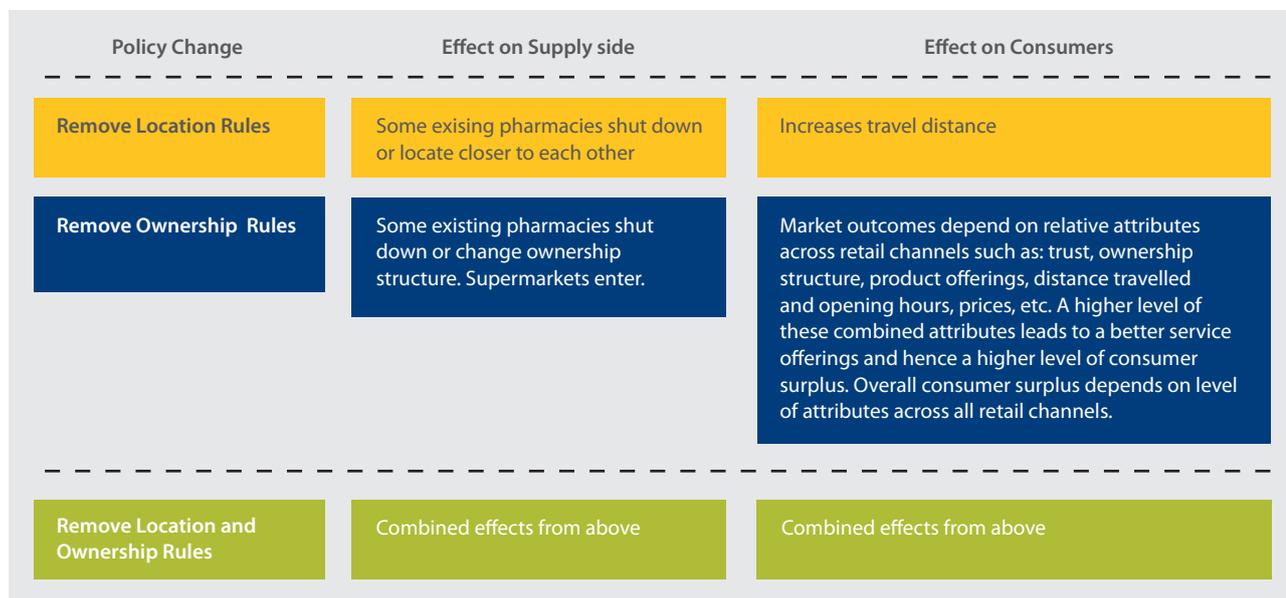
Scenarios

- » Baseline: Status Quo
- » Scenario A: Location rules **removed**, Ownership rules **retained**
- » Scenario B: Ownership rules **removed**, Location rules **retained**
- » Scenario C (Main policy change scenario): Ownership and Location rules **both removed**
- » Scenario D: Same as C (**both removed**), but takes a more optimistic view of the impact of the changes in terms of price reductions, travelling time, maintenance of trust, and access to the full array of medicines
- » Sensitivity Analysis: Individual attributes in scenario C varied one at a time, to test effect of assumptions

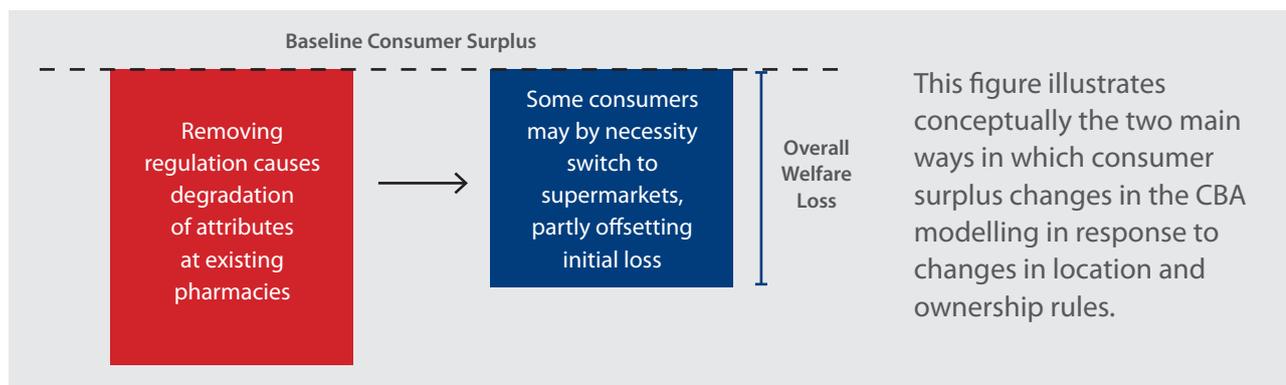
³ Consumer Survey – value of pharmacist ownership of pharmacies, KPMG Consulting July 1999

⁴ An economic measure of consumer satisfaction, which is calculated by analysing the difference between what consumers are willing to pay for a good or service relative to its market price.

Changing Existing Regulation



Overall Welfare Effect: Scenarios C and D



Results of the CBA – Annual net benefits (\$ per year)

	CBA scenarios				
	Baseline	A (Location)	B (Ownership)	C (Both)	D (Both)
Concession (\$ per patient)	0	-\$15.59	-\$77.75	-\$86.83	-\$78.53
General (\$ per patient)	0	-\$2.03	-\$38.51	-\$39.55	-\$12.91
Total (\$ million)	0	-\$115.25 million	-\$659.83 million	-\$726.50 million	-\$588.48 million

The results are ongoing, annual absolute dollar changes in consumer surplus, relative to the baseline scenario. To place these numbers in perspective, aggregate value added by Australian pharmacies in 2012 (measured as the sum of industry wages and salaries plus profits), was approximately \$3.2 billion, with a total value of sales of \$15.8 billion.

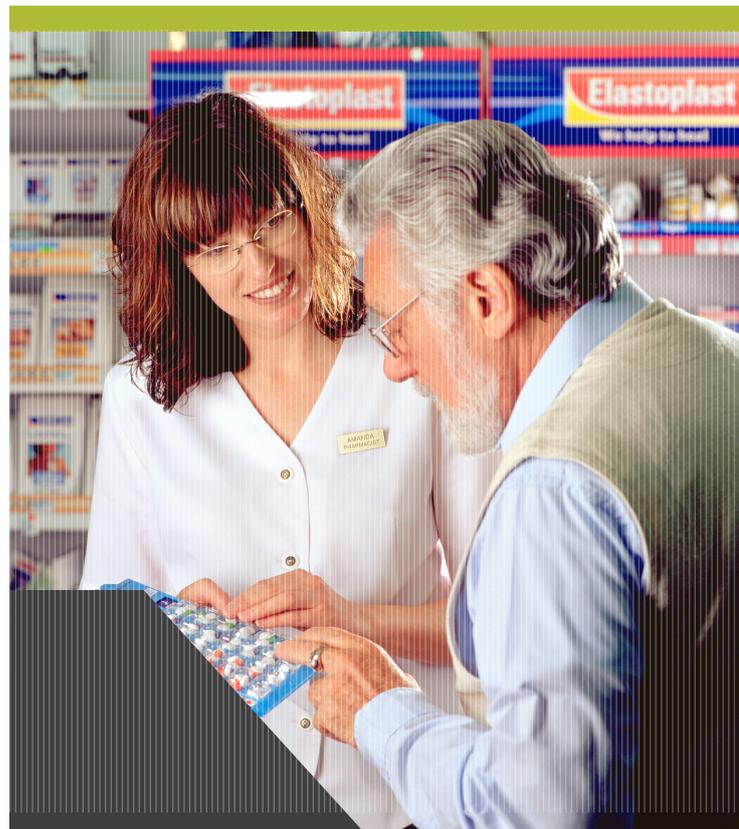
Hence, the annual losses computed in scenario C are equivalent to an annual, ongoing loss of approximately 6.6 per cent of current pharmacy prescription sales, or an annual ongoing loss equivalent to 23 per cent of total industry value added.

Conclusions – Key Points

- » The ability of community pharmacies to provide consumers with a **high level of access and choice**, while ensuring equity and lowering the costs of distribution, is underpinned by the location and ownership rules. They also help to protect quality and maintain an extremely high level of public trust in pharmacies and pharmacists. The cost-benefit analysis shows that repealing these rules would reduce community welfare by an amount equivalent to almost one-quarter of the sector's value added. The rules are therefore clearly in the public interest and should be maintained.
- » A detailed geo-spatial analysis of pharmacies, supermarkets, medical centres and banks demonstrates that community pharmacy provides a **high level of access** not only to metropolitan consumers but particularly to consumers in regional areas, to older consumers and to consumers in areas of socio-economic disadvantage.
- » The geo-spatial data also shows that universality of access is achieved without compromising competition and choice, with a high proportion of consumers close to two or more pharmacies. Furthermore, access to community pharmacy has increased over recent years, potentially bringing benefits closer to an ever greater number of consumers.
- » Importantly, the data shows the goal of universal access is secured at relatively low cost. Community pharmacy provides approximately the same level of access as medical centres (broadly defined) but does so with 16% fewer outlets. Were the density of pharmacy equal to that of medical centres, access would scarcely rise but costs to consumers and taxpayers would be higher, in present value terms, by \$1 billion.
- » The analysis also shows that the ownership rules bring substantial benefits. By ensuring that the ownership of pharmacies remain widely spread, the major supermarket chains are prevented from securing the high degree of market power they have obtained in grocery retailing, including through the use of buying power. Conversely, were the ownership rules repealed, experience in Australia and overseas suggests they would acquire that market power. As a result, the Commonwealth would find its bargaining position in purchasing dispensing services on behalf of the public severely weakened, raising costs for taxpayers and consumers.

- » At the same time, the ownership rules ensure that pharmacies are owned by pharmacists with a financial, personal and professional interest in providing high quality service. The consumer survey shows that consumers understand that fact, have great trust in the current system and do not regard supermarket pharmacies as an acceptable alternative. While this view is broadly held, older consumers place even more value on community pharmacy than consumers generally. These consumers would likely suffer more, and gain less from changes to the current arrangements.
- » In short, the evidence demonstrates that the current framework provides substantial net benefits. The benefits that these kinds of restrictions can bring have long been recognised as legitimate in competition law and practice.

The evidence shows that the current framework yields significant public benefits in terms of efficiency and equity. Unless and until a better alternative has been specified, properly tested and proven to be demonstrably superior, it would be irresponsible to jettison a system which has clearly demonstrated its merit.



The Australian Federation

The Prime Minister has said that 'The White Paper on the Reform of the Federation' process is designed to ensure that each level of Government is 'sovereign in its own sphere'.⁵

The Australian Constitution makes clear that the safe provision of health services to Australians is primarily the responsibility of the States and Territories.

These governments are therefore responsible for ensuring that pharmacy services are delivered to the public safely and to a quality standard.

It is noteworthy that when implementing the national registration and accreditation scheme for health professionals every Australian jurisdiction reconfirmed the community pharmacy model as the best model to ensure the safe and ethical provision of pharmacy services to Australians.

It is also why the *Intergovernmental Agreement for a National Registration and Accreditation Scheme for the Health Professions* makes pharmacy licensing and ownership matters the responsibility of the States and Territories.⁶

States and Territories should be allowed to continue to develop and maintain a system that best suits the circumstances of their communities, with intergovernmental agreements developed in areas where a co-ordinated outcome is in the best interests of citizens (e.g. mutual recognition of qualifications). This structure is a far better structure than a proposal to use 'competition payments' to 'persuade' jurisdictions to change laws to satisfy the theoretical policy desires of one area of central government that could lead to unintended and undesirable consequences for the Australian community if applied unthinkingly in a mechanical fashion.



The two complete submissions (June 2014 and November 2014) in response to the Competition Policy Review are available on the Guild website at:

www.guild.org.au/competitionpolicyreview

⁵ Hon Tony Abbott *Sir Henry Parkes Commemorative Dinner*, Tenterfield 25 October 2014: www.pm.gov.au/media/2014-10-25/sir-henry-parkes-commemorative-dinner-tenterfield

⁶ Paragraph 1.33 of the Agreement

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