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Pharmaceutical Benefits Scheme - Chemists Remuneration

Report

182

Joint Committee of Public Accounts

Parliament of the Commonwealth of Australia 1980

THE PARLIAMENT OF THE COMMONWEALTH OF AUSTRALIA

JOINT COMMITTEE OF PUBLIC ACCOUNTS

182nd REPORT

PHARMACEUTICAL BENEFITS SCHEME - CHEMISTS' REMUNERATION

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CANBERRA 1980

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DUTIES OF THE COMMITTEE

Section 8.(1) of the Public Accounts Committee Act 1951 reads as follows:

8.(1) Subject to sub-section (2), the duties of the Committee are:

(a) to examine the accounts of the receipts and expenditure of the Commonwealth including the financial statements transmitted to the Auditor-General under sub-section (4) of section 50 of the Audit Act 1901;

(aa) to examine the financial affairs of authorities of the Commonwealth to which this Act applies and of intergovernmental bodies to which this Act applies;

(ab) to examine all reports of the Auditor-General (including reports of the results of efficiency audits) copies of which have been laid before the Houses of the Parliament;

(b) to report to both Houses of the Parliament, with such comment as it thinks fit, any items or matters in those accounts, statements and reports, or any circumstances connected with them, to which the Committee is of the opinion that the attention of the Parliament should be directed;

(c) to report to both Houses of the Parliament any alteration which the Committee thinks desirable in the form of the public accounts or in the method of keeping them, or in the mode of receipt, control, issue or payment of public moneys; and

(d) to inquire into any question in connexion with the public accounts which is referred to it by either House of the Parliament, and to report to that House upon that question,

and include such other duties as are assigned to the Committee by Joint Standing Orders approved by both Houses of the Parliament.

PREFACE

The first Pharmaceutical Benefits Act was passed in 1944. The present Pharmaceutical Benefits Scheme had its origins in the changes to previous schemes effected by the Commonwealth Government in 1959.

As a part of these arrangements the Commonwealth Government has paid pharmaceutical chemists a fee to dispense Pharmaceutical Benefits Scheme and Repatriation Pharmaceutical Benefits Scheme prescriptions. When determining the level of the dispensing fee to be paid in the mid-1970s a number of errors occurred which lead to the excess payment of chemists by up to $253 million. This Report examines these errors, the extent of the overpayment, and changes in arrangements which can be introduced to avoid the recurrence of such errors in future.

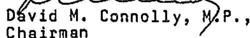
Despite repeated attempts to agree on a basis for determining the dispensing fee paid to chemists, no lasting agreement has at the date of this Report, been attained. The seventh attempt to achieve this was announced by the Minister for Health in November 1976. He said that the aim of the Commonwealth Government was:

- to remove from the political arena the important question of the fees paid to chemists;
- to bring to an end the acrimony that has developed over the years between chemists and successive Commonwealth Governments; and
- to achieve smooth administration of the Pharmaceutical Benefits Scheme.

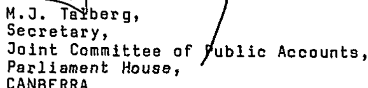
These aims have not been achieved. Besides considering the question of the excess payment of chemists this Report discusses some unsatisfactory features of the administration of the present arrangements, which have prevented the achievement of the Commonwealth Government's three aims, and recommends improvements which will help achieve them.

The Committee wishes to thank the Secretary and staff to the Committee, its advisors and those departments and organisations which made officers available for the inquiry, in the preparation of this Report.

For and on behalf of the Committee,



David M. Connolly, M.P.,
Chairman



M.J. Talberg,
Secretary,
Joint Committee of Public Accounts,
Parliament House,
CANBERRA

16 September 1980

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SUMMARY OF THE

CONCLUSIONS AND RECOMMENDATIONS

1 This Report by the Joint Parliamentary Committee of Public Accounts, examines the question of the excess payment of chemists, up to $253 million. Besides reporting on the direct issues relating to this excess payment, the Committee has made recommendations on a number of broader administrative issues which have contributed to inefficiencies within the pharmacy industry in particular, and the health industry in general.

2 The Committee's investigations and recommendations have been made bearing in mind total expenditure on health services in Australia in 1979-80 of approximately $9000 million. In 1977-78 (the last year of detailed statistics) the cost was about $7000 million, of which pharmacy sector expenditure was $644 million. Of this, Commonwealth Government expenditure on the pharmacy sector was $256 million.

The Error (Chapters 2 to 6)

3 Since the inception of the current Pharmaceutical Benefits Scheme in 1960, negotiations as to the level of remuneration paid to chemists by the Commonwealth Government have been exclusive to the Pharmacy Guild of Australia and officers of the Australian Public Service representing the Commonwealth Government. During this 20 year period there has been a complete failure to establish an agreed method for objectively determining the basic level of remuneration to be paid to chemists. Consequently, most efforts to determine levels of remuneration have ended in protracted and at times bitter negotiations between the Government and the Guild.

4 Over this 20 year period there have been three attempts, using surveys of pharmacy earnings, costs and profits, to determine the cost of dispensing a pharmaceutical benefits scheme prescription. In each case the results of the survey have been unacceptable to one side or the other. The PAC has concluded that fundamental changes are required in the procedures for the determination of chemists' remuneration and has recommended that the Joint Committee on Pharmaceutical Benefits Pricing Arrangements be abolished, a Health Fees Tribunal be established and that a Bureau of Health Economics be established. In addition, the PAC has recommended that the Government initiate a major inquiry into the structure of the pharmacy industry which will, as part of its task, examine alternative methodologies for determining chemists' remuneration.

5 Errors made in the Department of Health's ADP Branch and in the Secretariat Section which supports the Joint Committee on Pharmaceutical Benefits Pricing Arrangements, led to excess payments being made to pharmacists the most serious of which was not detected for four years. This led to the reference of the matter to the Joint Committee of Public Accounts.

6 The extent of the excess payments cannot be quantified definitively. However, the Minister for Health referred to maximum excess payments under the Pharmaceutical Benefits Scheme of $235 million, and the Minister of Veterans' Affairs referred to maximum excess payments under the Repatriation Pharmaceutical Benefits Scheme of $18 million. In total the maximum excess payments could have been $253 million.

7 The maximum excess payments made under the Pharmaceutical Benefits Scheme of $235 million, were derived from an error in the Cost of Goods Sold Analysis of $62 million, an error in the 'allocation of labour costs' of $126 million and errors in updating indices (caused by structural changes in the industry) of $47 million. These errors occurred between the period 1973-74 and April 1980.

8 The question of recoverability of the excess payment was considered by the Committee. It concluded that it would not make any recommendations on the matter as three independent legal opinions indicated recovery was not possible and the Commonwealth Government had already accepted that advice. It did however, reject the suggestion of the confidential "Report of the Public Service Board Team" that certain measures be introduced to ensure that future excess payments be made legally recoverable, as it considered such measures would be administratively cumbersome and potentially unworkable. Instead the Committee has recommended certain administrative measures aimed at reducing the possibility of future errors.

9 From its inquiries, the PAC could find no criminal, malicious or mischievous intent which would have led to the errors that occurred.

10 The PAC concluded that the testing procedures adopted for the processing of the 1972-73 survey were inadequate, that the Department of Health was under excessive pressure to complete the processing of the survey results, that the standards set were not followed, and that there were staff shortages in key areas of the Department of Health associated with ADP processing and ADP audit. If the Public Service Board had agreed to additional ADP audit staff it is likely that the errors would have been located earlier.

11 The PAC has therefore made the following recommendations.

Recommendations (Chapters 2 to 6)

(i) The Department of Health at intervals of not more than two years, review its standards of practice for ADP analysis, design, programming, testing, implementation and documentation to ensure that standards of practice are appropriately detailed, comprehensive and up-to-date.

(ii) The Department of Health ensure that its ADP staff comply with authorized standards and procedures and the Department establish management controls to ensure compliance. Comprehensive internal audit of ADP practices be carried out at intervals of not more than two years.

(iii) The Department of Health's ADP standards and procedures include the requirements for thorough technical review and certification of the requirement specification, analysis, design, programming, documentation and system performance. This should be done by users, peers or supervisors as appropriate. These standards are to include the requirement for the preparation of a detailed system test plan, designed to prove that the system output conforms with the user's requirements specification, not merely with the program design specification.

(iv) When developing standards:

a. it is the responsibility of ADP management to ensure that system development is in accordance with sound professional practice, including compliance with appropriate standards and procedures;

b. Permanent Heads ensure that time-frames for completion of ADP projects are set with due regard to the resources available;

c. If targets are set for the Department of Health without regard for the resources available, and the ADP management considers that it is unlikely that the targets can be met, the increased risk of error and its potential cost be pointed out;

(v) The Public Service Board assist departments to adopt sound practices and achieve high quality systems by:

a. accelerating its preparation and expanding the degree of detail of ADP information guideline manuals;

b. ensuring that these manuals are kept up to date and that they conform with the best of evolving ADP practice;

c. ensuring that Departments understand the importance of maintaining rigorous standards of quality in all aspects of system development; and

d. ensuring that priority is given to establishing positions to carry out system validations, system performance review and audit.

(vi) The Department of Health and the Public Service Board jointly review the staffing requirements of the Department of Health's ADP Branch against its present and prospective workload. The results of this review are to be advised to the PAC in 1981.

(vii) The Department of Health and the Public Service Board jointly review the classification and staffing of the Department of Health's ADP audit capacity against its present and prospective workload. The results of this review are to be advised to the PAC in 1981.

(viii) The Commonwealth Government announce that it will take no steps to introduce the suggested proposal of the Report of the Public Service Board Team (Pharmaceutical Benefits Scheme - Chemist's Remuneration) regarding arrangements with individual chemists binding them to repayment of future possible overpayments.

The Interim Basis for Remuneration of Chemists (Chapter 7)

12 The PAC has noted that the six point package agreed between the Commonwealth Government and the Guild on 9 April 1980 represents an agreement concerning the future basis of remuneration. In this Report the PAC will be recommending alternative ways of achieving the aims of the six point package in an open and constructive manner and with the objective of creating a more stable and orderly environment in which the Government and chemists could confidently proceed to creating an efficient and viable retail pharmacy industry.

13 As an interim measure and until the longer term recommendations of the PAC can be given effect, the PAC is of the view that provision may need to be made for the adjustment of fees.

Recommendation (Chapter 7)

(i) The dispensing fee of $1.31 agreed between the Guild and the Commonwealth Government, and ratified by the Chairman of the Joint Committee on Pharmaceutical Benefits Pricing Arrangements by his determination of 9 April 1980, be used as the only base for any adjustment of the dispensing fee. No adjustment be made to other components of chemists' remuneration.

(ii) Any request for updating the dispensing fee be referred to, and determined by, the recommended Health Fees Tribunal. (see Chapter 8)

(iii) As an interim measure, and until the recommended public inquiry is completed into the structure and remuneration of the retail pharmacy industry (see Chapter 10), findings of the Joint Committee's current methodological review be available to parties appearing before the recommended Health Fees Tribunal.

A Health Fees Tribunal (Chapter 8)

14 The PAC examined the operation and functions of the Joint Committee on Pharmaceutical Benefits Pricing Arrangements, a Committee which has been responsible for setting or for advising on the appropriate level of remuneration for pharmacists dispensing PBS and RPBS prescriptions. As a result of its investigations the PAC has recommended that the Joint Committee be abolished and replaced by a Health Fees Tribunal.

15 The PAC was concerned that the Joint Committee considered only the views of the Pharmacy Guild of Australia and the Commonwealth Government, to the exclusion of all other interested groups. It operated in private and its findings were not open to public scrutiny.

16 As the determination of government paid benefits is not confined to the pharmacy sector but occurs in other areas of medical and para-medical services, and as many of the problems and considerations facing these sectors are common, the PAC concluded that one independent public body should review the level of these payments. Accordingly, the PAC made the following recommendations.

Recommendations (Chapter 8)

(i) Determination of chemists' remuneration be vested in an independent Health Fees Tribunal. This Health Fees Tribunal be operational within 12 months of the tabling of this report.

(ii) The Joint Committee on Pharmacuetical Benefits Pricing Arrangements be abolished concurrent with the establishment of the Health Fees Tribunal.

(iii) The Health Fees Tribunal:

a. consist of one or more members, the Chairman being a Deputy President of the Australian Conciliation and Arbitration Commission;

b. receive public submissions from all interested parties and conduct its hearings in public;

c. as far as possible conduct its hearings in a manner which encourages the making of determinations on questions of fact rather than on questions of law;

d. determine its own criteria for setting remuneration having regard to Commonwealth Government guidelines to the Conciliation and Arbitration Commission for the fixing of salaries and wages;

e. announce its criteria and reasons for its decisions when making determinations; and

f. determinations be legally binding on all parties; and

g. to the extent that it requires a staff this be provided independently of the Department of Health.

A Bureau of Health Economics (Chapter 9)

17 The PAC, throughout its inquiry into the excess payment of pharmacists, was concerned with the general lack of independent objective economic advice on health matters. With total health expenditure throughout Australia of about $9000 million in 1979-80, the Committee considered that the Department of Health should be serviced by a group of specialists advising on health/welfare economic matters.

18 The PAC considers that this group of economists should be technically independent in their operations, and free from day to day administrative matters. Accordingly the Committee has recommended that a Bureau of Health Economics be established and that it operate and function in a similar way to the Bureaus of Agricultural Economics, Transport Economics, Industry Economics and Labour Market Research.

Recommendations (Chapter 9)

(i) A Bureau of Health Economics be established to provide independent, objective and publically available analysis of economic facts and issues relating to the Australian health industry.

(ii) The Bureau of Health Economics to have a charter and powers similar to other Economic Bureaus.

(iii) The Commonwealth Government consider establishing an external independent committee to assist the Bureau of Health Economics.

(iv) The Bureau of Health Economics be formed within one year of the date of tabling of this report, and become operational within two years of the tabling of this report.

Retail Pharmacy in Australia (Chapter 10)

19 There are currently about 5,400 pharmacies in Australia and on average each pharmacy serves about 2,650 people. Average UK pharmacies service about 5,000 people and Swedish pharmacies about 14,000 people. Throughout its inquiry, many witnesses claimed that the smaller pharmacies in Australia were uneconomic.

20 In 1977 attempts were made by the Joint Committee on Pharmaceutical Benefits Pricing Arrangements to examine rationalisation proposals for the pharmacy industry. These negotiations ended in failure.

21 The PAC notes that the structure of the industry has directly affected the level of remuneration paid to pharmacies and that any change to the structure involving the rationalisation of the smaller pharmacies could lower the average cost of dispensing a PBS prescription and lead to savings in government expenditure.

Recommendations (Chapter 10)

(i) The Commonwealth Government initiate a public inquiry into the structure of the retail pharmacy industry. This inquiry examine:

a. the appropriate structure of and numbers in the industry having regard to Australia's geography and its population distribution;

b. the need and justification for rationalising pharmacy numbers;

c. methods of rationalising the industry;

d. forms and levels of compensation that might be used to facilitate the rationalisation process; and

e. methods for determining chemists remuneration.

The Repatriation Pharmaceutical Benefits Scheme (Chapter 11)

22 The level of remuneration paid by the Commonwealth Government to chemists under the Repatriation Pharmaceutical Benefits Scheme has been aligned with that of the Pharmaceutical Benefits Scheme. However, the Department of Veterans' Affairs has not participated in discussions and proceedings of the Joint Committee when changes in procedures or levels of payment have been determined.

23 The Department of Health has also taken over the major processing functions for Repatriation Pharmaceutical Benefits Scheme prescriptions.

24 The Committee concluded that greater economies and efficiencies could be achieved if certain administrative procedures associated with the Repatriation Pharmaceutical Benefits Scheme were handled directly by the Department of Health.

25 Accordingly, the Committee has made the following recommendations.

Recommendations (Chapter 11)

(i) The Department of Veterans' Affairs retain policy control over the Repatriation Pharmaceutical Benefits Scheme.

(ii) The Department of Health be given total responsibility for the administration and claims processing of the Repatriation Pharmaceutical Benefits Scheme.

(iii) The Department of Health integrate the administration and processing of the Repatriation Pharmaceutical Benefits Scheme with the Pharmaceutical Benefits Scheme so as to achieve the utmost economy commensurate with sound management and high standards of service to those submitting claims.

(iv) *A Joint Department Liaison Committee on* Repatriation Pharmaceutical Benefits Scheme matters be established to provide formal communication and consultation between the Departments of Veterans' Affairs and Health.

(v) The Public Service Board, together with the various staff Associations, review policies and procedures for the transfer of staff between departments in order that staff transfers are conducted smoothly and efficiently. The results of this review are to be advised to the PAC in 1981.

CHAPTER 1

INTRODUCTION

1.1 This is the Report of the inquiry into the circumstances of, and reasons for, a significant excess payment by the Department of Health to chemists in respect of their remuneration under the Pharmaceutical Benefits Scheme. Concurrent excess payments were also made by the Department of Veterans' Affairs to chemists under the Repatriation Pharmaceutical Benefits Scheme.

1.2 These excess payments commenced during the financial year 1973-74 and terminated on 9 April 1980 when a fee determination was made by the Chairman of the Joint Committee on Pharmaceutical Benefits Pricing Arrangements. For reasons which are explained in the Report, the excess payments cannot be quantified definitively. According to the Ministers for Health and Veterans' Affairs these excess payments were estimated to have been up to $253 million over this period.

1.3 The excess payments were first officially acknowledged on 2 April 1980, in a statement by the Minister for Health to the House of Representatives. The statement by the Minister for Health is reproduced at Appendix 3 and that of the Minister for Veterans' Affairs is reproduced at Appendix 5.

Terms of Reference

1.4 On April 21 1980, following further consideration of the matter in the House of Representatives, the following motion was carried:

> "That the circumstances surrounding the question of 'excess payments' made under the Pharmaceutical Benefits Scheme as set out in the statement of the Minister for Health to the House of Representatives on April 2 1980 and under the Repatriation Pharmaceutical Benefits Scheme, and the question of whether the relevant administrative process should be altered in the light of the situation described in the statement be referred to the Joint Committee of Public Accounts for inquiry and report."

1.5 As a consequence of this motion this inquiry was forwarded to the Public Accounts Committee (PAC) under Section 8(1)(d) of its Act.

1.6 For the purposes of its inquiry the PAC adopted the following Further Terms of Reference:

1. Summarise procedures (including supporting administrative procedures) leading to determinations of remuneration for chemists prior to December 1976 and present arrangements.

2. Identify those persons associated with the processes and negotiations leading to determinations on the level of remuneration to chemists from 1972.

3. Examine and summarise circumstances leading to the apparent excess of payments to chemists over that indicated by the results of the 1977-78 Inquiry.

4. Compile a set of relevant documents (eg computer systems specifications and correspondence by Department of Health and Committee Secretariat on the 1972 Inquiry, minutes of Joint Committees) in support of the summary provided under (3) above.

5. Formulate questions which might be asked of witnesses appearing before the Committee to determine:

   (a) the circumstances under which an apparent excess in the level of remuneration occurred,
   (b) the amount of the "excess" payments under both NHS and Veterans' Affairs reimbursements, and
   (c) the extent to which responsibility might be attributed for that situation.

6. Identify initiatives taken by the Public Service Board in publishing guidelines to assist in project management functions, and standards and audit aspects for development and control of computer based systems.

7. Make recommendations of any amendment to current procedures for determination of levels of chemists' remuneration considered necessary.

8. Make recommendations for any improvement in public service administration to avoid recurrence of the situation.

9. Seek submissions from interested persons or organisations on any or all of the above matters.

Scope of Report

1.7 The findings of the inquiry go beyond the immediate question of the errors and the excess payments. A number of fundamental problems emerged during the inquiry which could directly affect the possibility of similar problems occurring in the future. Besides affecting the pharmacy sector, a number of matters had broader implications for other sectors of the health industry. These areas of inquiry by the PAC covered the provision of independent economic advice to the Commonwealth Government on health matters, procedures for determining health fees and remuneration and the structure of the retail pharmacy industry.

Public Hearings, Submissions

1.8 Public hearings on this matter were held in Canberra and Sydney during June and July 1980. Details of those hearings are presented in Appendix 1. Witnesses who presented submission included Commonwealth Departments and Organisations, the Joint Committee on Pharmaceutical Benefits Pricing Arrangements, pharmacy and pharmacists organisations, consumers, chemists and health economists.

CHAPTER 2

THE PHARMACEUTICAL BENEFITS SCHEME AND REMUNERATION OF CHEMISTS TO 1976

The Pharmaceutical Benefits Scheme - Historical Outline

2.1 This chapter deals principally with the Pharmaceutical Benefits Scheme (PBS) which allows for the provision of pharmaceutical benefits to the general public. The Repatriation Pharmaceutical Benefits Scheme (RPBS) which provides pharmaceutical benefits to persons granted eligibility under the Repatriation Act 1920 is considered at Chapter 11.

2.2 The Pharmaceutical Benefits Act 1944 authorised the provision of pharmaceutical benefits free of charge to all residents of Australia. The Act restricted benefits to medicines, materials and appliances listed in the Commonwealth Pharmaceutical Formulary. Under this scheme, benefits could only be obtained from approved pharmaceutical chemists on presentation of prescriptions written by registered medical practitioners, on forms supplied by the Commonwealth Government. This scheme was opposed in the High Court of Australia by the Australian Branch of the British Medical Association and the Court found that the Commonwealth Government did not have power to legislate on national health matters except for quarantine. As a result, a referendum was held in 1946 to seek the necessary powers, and was passed.

2.3 The Pharmaceutical Benefits Act 1947 introduced a revised scheme. This also came under attack from the Australian Branch of the British Medical Association which challenged it in the High Court of Australia. The High Court ruled that parts of the legislation were invalid.

2.4 With the change in the Commonwealth Government at the end of 1949 the incoming Minister for Health introduced a new scheme providing 139 'life-saving and disease-preventing drugs' free of charge. This scheme was implemented under the Pharmaceutical Benefits Act 1947-1949 and came into force on 4 September 1950.

2.5 In June 1951 the National Health (Medicines for Pensioners) Regulations were introduced under the National Health Service Act 1948-1949, authorising the provision of medicines for pensioners. The benefits provided, free of charge, all the drugs and medicinal preparations listed in the British Pharmacopoeia or specified in the schedule to the National Health (Medicines for Pensioners) Regulations, together with combinations of these drugs and medicinal preparations. These benefits were made available to all persons in receipt of an Australian age, invalid, widow's or Service pension and to their dependants.

2.6 In December 1953 the National Health Act 1953 was passed, and came into operation on 12 May 1954. Together with National Health (Pharmaceutical Benefits) Regulations this new legislation repealed and, in principle, re-enacted the provisions of the Pharmaceutical Benefits Act 1947-1952 and the provisions of the National Health (Medicines for Pensioners) Regulations under which pharmaceutical benefits had been provided.

2.7 This scheme continued to operate until the Commonwealth Government introduced the current PBS under the National Health Act 1959. The principal features of the new PBS which came into operation on 1 March 1960 were:

- the former pensioner scheme and general scheme were combined. There was no alteration to the entitlement of pensioners and eligible dependants;

- the range of drugs and medicinal preparations available to the public as benefits was greatly expanded; and

- a patient contribution of 50 cents was imposed on each general (non-pensioner) benefit to introduce an element of control and deterrence in the face of rising costs.

2.8 By broadening the range of drugs the Commonwealth Government sought to assist patients facing high drug costs and to give medical practitioners a wider choice of medicines eligible for prescription as benefits. It was also envisaged that doctors would prescribe the less expensive drugs for the less serious illnesses.

Range of Benefits

2.9 Since the current scheme was introduced the range of drugs attracting benefits has increased substantially. At 30 June 1961 there were 436 individual drugs (excluding extemporaneously prepared drugs, i.e. not ready-prepared by manufacturers) listed. Currently this range has grown to about 620 individual drugs available in approximately 1300 ready-prepared forms and strengths. When multiple brands are taken into account there are approximately 2200 items available. In addition there are about 300 extemporaneously-prepared medicines attracting pharmaceutical benefits.

2.10 A feature of the development of the pharmacy industry has been the movement away from the dispensing of extemporaneously prepared drugs to the dispensing of ready-prepared items. For the year ended 30 June 1961 extemporaneous preparations accounted for 27 percent of total dispensing compared with 4 percent for the year ended 30 June 1979.

The Cost of Pharmaceutical Benefits

2.11 A recent analysis of Australian expenditure on health services is contained in the Department of Health's booklet, Australian Health Expenditure 1974-75 to 1977-78: an analysis. The latest figures contained in that booklet refer to Financial Year 1977-78 and it is on the basis of that information that this section is derived.

2.12 Total expenditure on pharmaceuticals in 1977-78 was $644 million. This represented 9.5 percent of all health expenditure in Australia, which totalled $6778 million.

2.13 Total expenditure on pharmaceuticals on which a benefit was paid totalled $410 million or 60 percent of the total. The balance of $234 million was for all other pharmaceutical items outside the PBS and RPBS arrangements.

2.14 The total cost to the Commonwealth Government of providing pharmaceutical benefits in 1977-78 was $256 million. In 1979-80, it was $275 million.

2.15 The Commonwealth Government contributed 46 percent of all expenditure on pharmaceuticals, private individuals 54 percent. While expenditure on pharmaceuticals constituted only 12 percent of total government health expenditure in 1977-78 it was the largest single component of individuals' health expenditure. Pharmaceuticals accounted for 31 percent of health expenditure of individuals - more than twice the expenditure of individuals on any other single form of health care. In part this was because health insurance funds concentrate their activities in the areas of hospital, medical and dental costs.

2.16 Factors influencing the growing level of expenditure on pharmaceuticals include changes in the age distribution of the population, periodic easing of the means test for pensioners and increased prescribing by medical practitioners. Other factors include the increased average cost of a prescription (from $1.90 average in 1960-61 to $4.16 in 1978-79). This is due to increased manufacturing costs, increased payments to chemists by way of adjustments to remuneration rates (markup and dispensing fees), and a tendency on the part of medical practitioners to prescribe newer and generally more expensive drugs, which may be encouraged by promotional pressures of the pharmaceutical manufacturers.

Patient Contribution

2.17 The patient contribution for prescriptions eligible for benefits under the PBS (other than for pensioners holding a Health Benefits Entitlement Card who receive their pharmaceutical benefits free of charge) has increased from 50 cents per benefit in 1960 as follows:

Nov 71	Sept 75	Mar 76	July 78	Sept 79
$1.00	$1.50	$2.00	$2.50	$2.75

2.18 From 1 November 1971 to 30 February 1976 beneficiaries under the Subsidised Health Benefits Plan paid half the patient contribution.

2.19 In the 1980 Commonwealth Government Budget, provisions were envisaged which would allow chemists to charge less than this patient contribution. One group of pharmacies indicated immediately that they would provide a 50 cents rebate; however within two days of this announcement the Government announced that it was setting aside the enabling legislation.

Friendly Societies

2.20 Under the National Health Act 1959 members of Friendly Societies were not required to pay the patient contribution for pharmaceutical benefits supplied at Society dispensaries or pharmacies supplying medicines as contractors to Friendly Societies. In some States where the number of Friendly Society dispensaries was limited, insurance schemes had been introduced by some Societies which paid cash refunds against the cost of prescriptions, including the patient contribution.

2.21 The Pharmacy Guild of Australia (the Guild) took the view that failure to recover the patient contribution reduced the deterrent to oversupply of pharmaceuticals and discriminated unfairly in favour of the Friendly Societies. The Friendly Societies' Pharmacies Association of Australia maintained that their members had already paid part of the patient contribution through their membership fees and that evidence had never been produced to indicate that waiver of the patient contribution had led to oversupply of drugs to its members.

2.22 In 1964, after an intense lobbying campaign, the Guild succeeded in securing an amendment to the National Health Act which required persons joining Friendly Societies on or after 24 April 1964 to pay the full patient contribution. Members who joined Friendly Societies before that date and certain of their dependants retained their entitlement to such rebates and refunds as existed before the passing of the 1964 legislation. The amendments also prohibited any other form of insurance against patient contribution for PBS drugs.

Basis for Remuneration of Chemists

2.23 Prior to the passing of the National Health Act (No. 4) 1976, fees and payments to pharmaceutical chemists for the supply of pharmaceutical benefits were set by the Minister for Health under Section 99 of the Act, after consultation with the Guild.

2.24 The remuneration of chemists consisted of:

- the wholesale cost of ingredients;
- a markup on wholesale cost (33 percent for ready-prepared benefits and 50 percent for extemporaneously-prepared benefits);
- a container allowance where applicable;
- a dispensing fee; and
- miscellaneous allowances in respect of wastage and freight costs.

2.25 In the case of general benefits, the chemist collected the patient contribution from the patient in respect of each prescription and the balance of the price was paid by the Commonwealth Government. For benefits supplied to eligible pensioners or their dependants, the Commonwealth Government paid the full price.

2.26 Amendments to the National Health Act (No. 4) 1976 placed the responsibility for setting fees with the Chairman of the Joint Committee on Pharmaceutical Benefits Pricing Arrangements (Joint Committee).

2.27 The current basis for remuneration of chemists is similar to that outlined above except that the markup on drugs has been reduced to 25 percent for ready prepared items and to 33 percent for extemporaneously prepared items (compensated for by an increase in the dispensing fee), an isolated pharmacy allowance has been introduced and a dangerous drug fee is paid where appropriate.

<u>Fees and Payments to Chemists Prior to 1977</u>

2.28 Variations in the dispensing fee between 1960 and the present time are shown in Table 1.

Table 1: Movement in P.B.S. Professional Fee for Dispensing 1968-1980

Date of Decision	Effective Date	Ready Prepared Fee	(increase)	Extemporaneously Prepared Fee	(increase)
1960		28c	(-)	50c	(-)
1961		30c	(+2c)	55c	(+5c)
30.10.70	1.7.70	32c	(+2c)	57c	(+2c)
28.4.72	1.1.72	39c	(+7c)	64c	(+7c)
1.8.73	1.5.72	42c	(+3c)	64c	(-)
	1.10.72	44c	(+2c)	64c	(-)
	1.12.72	45c	(+1c)	64c	(-)
1.8.73	1.1.73	50c	(+5c)	72c	(+8c)
31.7.74	1.1.74	57c	(+7c)	79c	(+7c)
13.2.75	1.7.74	62c	(+5c)	84c	(+5c)
25.7.75	1.7.73	61c	(+11c)	83c	(+11c)
	1.1.74	68c	(+11c)	90c	(+11c)
	1.7.74	84c	(+22c)	$1.06	(+22c)
25.10.76	1.7.75	90c	(+6c)	$1.12	(+6c)
3.12.76	1.1.77	95c	(+5c)	$1.17	(+5c)
4.4.77	1.7.76	$1.02	(+12c)	$1.24	(+12c)
4.4.77	1.1.77	$1.07	(+12c)	$1.29	(+12c)
15.5.78	1.7.77	$1.16	(+9c)	$1.38	(+9c)
19.5.78	1.8.78	$1.30	(+14c)	$1.90	(+52c)
18.9.78	1.7.77	$1.21	(+5c)	$1.43	(+5c)
	1.8.78	$1.35	(+5c)	$1.95	(+5c)
9.4.80	1.5.80	$1.31	(-4c)	$1.91	(-4c)

NOTE: The arrows in the Table indicate retrospective adjustments. The figure notated by the upper arrow represents the original determination, whereas the figure notated by the lower arrow represents the final determination including the retrospective adjustment.

SOURCE: *Submissions by the Departments of Health and Veteran's Affairs*

2.29 Early efforts by the Commonwealth Government to establish a scheme for the supply of pharmaceutical benefits were supported by the Guild and throughout the history of the scheme the Guild has been active in representing the views of its members to the Commonwealth Government. The National Health Act 1953 provided for fees to chemists to be set by the Minister for Health after consultation with the Guild and subsequent amendments to the Act have preserved the exclusive position of the Guild as the sole representative of the retail pharmacy industry.

2.30 When pricing arrangements were negotiated for the revised PBS, the Guild sought provision for the automatic adjustment of dispensing fees based on the movements in award wages of registered pharmacists employed by approved chemists. Whilst the Government considered that automatic adjustments of this kind were not in the best interests of the economy generally, it agreed that some provision should be made whereby the level of fees should be reviewed. In negotiations with the Guild, considerable difficulty was experienced in arriving at an acceptable formula.

2.31 The formula eventually adopted was for the dispensing fee to rise or fall in accordance with movements in the weighted average award wages for registered assistants after 31 December 1959. The formula was to be applied on the understanding that if a 'freakish' adjustment occurred in the award wages a halt would be called and the matter reviewed. During its inquiry the PAC established that the agreement between the Guild and the Commonwealth Government covering this provision contained no definition of 'freakish'. Under the formula, an increase in award wages in Victoria in 1960 would have resulted in an increase of 22 percent in dispensing fees. The Commonwealth Government considered this result to be 'freakish' and in 1961 approved an increase of 10 percent in dispensing fees. At the same time the Commonwealth Government indicated to the Guild that it was not prepared to continue with the formula for automatic adjustments and that it wished to negotiate a completely new arrangement for future adjustments.

2.32 Thus the first time an agreement between the Guild and the Commonwealth Government was applied, the Commonwealth Government abrogated the agreement. Indeed, for a decade after this, there was no further adjustment of fees.

2.33 In September 1963 the Guild proposed that fees be increased and repeated its request in August 1964. The formula proposed was unacceptable to the Commonwealth Government and the Guild withdrew its proposals in December 1964 when the first Joint Committee was established, comprising equal Commonwealth Public Service and Guild representation under an independent Chairman.

2.34 In February 1965 the Guild proposed that a survey be conducted by an independent firm of consultants to provide factual information on the cost of dispensing PBS prescriptions. The Commonwealth Government agreed to share the cost of the survey and it was carried out by Associated Industrial Consultants (Aust.) Pty. Ltd.. The results obtained from the survey were rejected by the Guild as being unrealistic. The results indicated that retailing was unprofitable and this did not reflect actual business experience. After examining the outcome of the survey the Commonwealth Government decided in mid-1969 that the dispensing fee would remain unaltered.

2.35 Subsequent to the Commonwealth Government's decision further representations concerning the method of assessing the dispensing fee and the level of the fee were made. These culminated in a new submission by the Guild in March 1970 seeking an immediate increase of 15 cents in the dispensing fees. The Minister for Health referred the submission to the Joint Committee, which reported that apart from the amount of the increase, agreement had been reached on all but one of the issues raised by the Guild. The issue not resolved related to the allocation of labour costs between dispensing and retail activites. The Commonwealth Government considered the Guild's submission and decided that it was not acceptable.

2.36 Data on dispensing costs of PBS prescriptions related to the financial year 1964-65. The Joint Committee updated these figures, using movements in national indices and other relevant factors. In the light of available information and the increase in costs, the Commonwealth Government granted an increase of only two cents in the dispensing fee for PBS prescriptions dispensed on and after 1 July 1970. The small increase was justified on the basis of a lack of up-to-date information. The Commonwealth Government stated that any further increases would only be made if justified by a new survey and that should the Guild be prepared to enter into a new survey and should that survey justify a further increase in dispensing fees, the increase would be made retrospective to an appropriate date.

2.37 Following discussions between the Minister for Health and the Guild on 5 April 1972 the Commonwealth Government, after consideration of all available information, granted an increase of seven cents in dispensing fees for PBS prescriptions dispensed on and after 1 January 1972.

2.38 At that meeting it was agreed that a new Inquiry into Pharmacy Earnings, Costs and Profits under the auspices of the Joint Committee would be planned to cover the financial year 1972/73 in order to provide the factual information needed under both the 'cost accounting approach' proposed by the Commonwealth Government and the 'regression approach' proposed by the Guild.

2.39 Following a recommendation from the Joint Committee the Minister determined on 1 August 1973 that chemists be paid a 'special purpose' payment in respect of ready-prepared PBS prescriptions. The rate determined was three cents per prescription from 1 May 1972 increasing to five cents from 1 October 1972 and six cents from 1 December 1972. The purpose of this payment was to compensate chemists for the loss of rebates and discounts due to manufacturers reducing the discount they normally allowed wholesalers.

2.40 Further recommendations by the Joint Committee led to the Minister for Health approving on 1 August 1973 increases of five cents per prescription with effect from 1 January 1973, seven cents from 1 January 1974, and a further five cents from 1 July 1974. These increases were all based on an agreed updating formula.

2.41 In March 1975 the results of the 1972-73 Inquiry became available and the then Chairman of the Joint Committee made recommendations on four major issues in dispute between the Guild and Commonwealth Government representatives. The Commonwealth Government in July 1975 accepted two of the then Chairman's recommendations, but excluded goodwill, and applied the 'relatively economic pharmacy approach' in determining increases of 11 cents per prescription for 1973-74 and 22 cents for 1974-75. Application of the 'overall average pharmacy approach' which was sought by the Guild, would have yielded larger increases. Later that year the Chairman resigned for personal reasons and the Joint Committee ceased to function until reconstituted in January 1977. The Subcommittee of the Joint Committee continued to meet as a Guild/Commonwealth Government liaison committee during 1975 and 1976.

2.42 The Guild did not accept the Commonwealth Government's decisions of July 1975 about chemists' remuneration and made it clear that it would take out a High Court writ against the Commonwealth Government if it could not achieve a better result for chemists. After the change of Commonwealth Government in November 1975, chemists were offered a further increase of five cents per prescription, retrospective to 1 July 1973, in an endeavour to overcome prior disagreements (described by the then Minister for Health as 'wiping the slate clean for the past') and it was proposed to carry out a new inquiry.

2.43 This offer was not acceptable to the Guild. In April 1976 the Guild and its President issued a writ out of the High Court against the Commonwealth Government seeking certain declarations, orders and damages. Following discussions between the Commonwealth Government and the Guild agreement was reached in October 1976 on the matters in dispute and the Guild agreed to withdraw the writ. The agreement also included:

(a) the National Health Act was to be amended to provide for the establishment of a new Joint Committee in its present form;

(b) the Guild agreed to forego any past payments which it believed were owing to chemists from past unsettled inquiries;

(c) the Commonwealth Government's offer of a five cents increase in chemists' dispensing fees, retrospective to 1 July 1973, was withdrawn;

(d) an increase of six cents per prescription was granted, retrospective to 1 July 1975;

(e) a further increase of five cents per prescription was to operate as from 1 January 1977, which was to be an interim adjustment to be reconciled when the actual figures for 1976-77 became available;

(f) a new Inquiry into Pharmacy Earnings, Costs and Profits was to be carried out in 1977-78 by the Joint Committee for a further review of chemists' remuneration; and

(g) the Guild could present to the Joint Committee a case for adjustment of remuneration back to 1 July 1976.

Summary of Developments to 1976

2.44 Prior to the agreement between the Commonwealth Government and the Guild in October 1976, six attempts were made to determine a base level for dispensing fees which would be satisfactory to both parties. As indicated hereunder, each of these moves proved to be unacceptable to one side or the other.

1. The 1960 agreement for automatic adjustment of fees based on movements in award wages of registered assistants was terminated by the Commonwealth Government because of the "freakish" result in 1961.

2. The results of 1964-65 Survey of Pharmacy Earnings, Costs and Profits carried out by Associated Industrial Consultants (Aust.) Pty Ltd were rejected by the Guild as being unrealistic.

3. A Commonwealth Government proposal in 1970 to conduct a new survey was rejected by the Guild on the grounds that the survey was to be conducted on the same basis as the previous unacceptable survey.

4. The Guild commissioned a firm of consultants, Economic Research Associates to advise on a suitable formula, without significant results.

5. A Guild proposal in 1971 for a survey based on a regression analysis technique to replace random activity sampling was not accepted by the Commonwealth Government as it did not consider the survey would provide the factual information needed.

6. Recommendations by the Chairman of the Joint Committee based on the 1972-73 Survey of Pharmacy Earnings, Costs and Profits, were only partly accepted by the Commonwealth Government.

2.45 Despite this lack of success the 1976 agreement provided for a further survey to be carried out in 1977-78 as a basis for reviewing chemists' remuneration. The nature of that survey and its results are considered in the following chapter.

CHAPTER 3

THE 1977-78 SURVEY & THE EXCESS PAYMENTS TO CHEMISTS

1977-78 Survey

3.1 In accordance with the agreement of October 1976 between the Commonwealth Government and The Pharmacy Guild of Australia (the Guild), the National Health Act was amended in December 1976 to formally establish the new Joint Committee on Pharmaceutical Benefits Pricing Arrangements (Joint Committee). The new Joint Committee came into operation early in 1977, with the Honourable Mr Justice Ludeke as its Chairman. Its main task was to undertake the 1977-78 Survey of Pharmacy Earnings, Costs and Profits in order to obtain up-to-date information for further reviews of chemists' rates of remuneration.

3.2 The 1977-78 Survey was intended to fulfill the following objectives:

a. information collected for the Survey should relate to the Financial Year 1977-78;

b. the Survey should provide detailed information on the earnings, costs and profits in cents per prescription of dispensing Pharmaceutical Benefits Scheme (PBS) prescriptions;

c. the design of the Survey should enable analysis of information by volume of PBS dispensing, both in terms of an overall average and on a stratum basis, with a comparable degree of accuracy for each stratum;

d. the design should endeavour to ensure that, as far as possible, both the Guild and the Commonwealth Government were able to obtain the information they required from the Survey.

Pharmacy Population Sample

3.3 Initially 601 pharmacies were selected to take part in the survey. Of these, 331 indicated willingness to participate. Eventually the number of pharmacies in the sample was reduced to 269 because of closures, transfer of ownership and reluctance or inability of some pharmacies to provide all the necessary information. (Despite the decline in the number participating, the Australian Bureau of Statistics considered the statistical sample to be adequate.) The distribution of the sample pharmacies was as follows:

Table 2: Distribution of Final Numbers in 1977-78 Survey

Stratum*	N.S.W.	Vic.	Qld	S.A.	W.A.	Tas	Total Sample	Total** Population
1	15	13	11	3	3	1	46	1431
2	16	16	10	4	4	3	53	916
3	16	10	8	2	2	1	39	740
4	11	7	4	3	1	0	26	619
5	12	5	4	2	1	1	25	531
6	14	6	5	3	1	2	31	450
7	14	4	3	2	3	1	27	359
8	9	5	3	2	2	1	22	242
Total	107	66	48	21	17	10	269	5288

SOURCE: Joint Committee evidence

Methodology

3.4 The methodology for the 1977/78 Survey comprised four major analyses:

a. A Financial and Wages Questionnaire (FQ) covering details of income and expenditure, salaries and wages, hours worked and capital employed in each of the 269 pharmacies in the sample;

b. A Random Activity Sampling (RAS) of staff and proprietor activities and time spent on each activity, involving 170 pharmacies out of the main sample selected;

c. A Cost of Goods Sold Analysis (COGS) involving the examination of one month's purchases for 80 pharmacies out of the main sample; and

d. An analysis of PBS, Repatriation Pharmaceutical Benefits Scheme (RPBS) and Private prescriptions dispensed during 1977-78 for all 269 pharmacies in the main sample.

3.5 Chemists participating in the survey received a fee of $75. They were required to provide a range of detailed information and some delays were experienced in the receipt of the completed questionnaires.

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* Each stratum dispensed 12.5 percent of all PBS prescriptions

** Based on 1975-76 data.

Arbitration by the Chairman of the Joint Committee

3.6 In the negotiations which defined the parameters of the 1977-78 Survey, and during its processing the Commonwealth Government and the Guild were unable to reach agreement on the interpretation and use of many of the variables used within the survey. The Chairman of the Joint Committee arbitrated and ruled on these disputes. The matters the Chairman was required to decide on were:

- (i) proprietors' notional salary;
- (ii) goodwill;
- (iii) rate of return on funds invested;
- (iv) valuation of fixtures and fittings, plant and equipment;
- (v) settlement discounts;
- (vi) award or actual wages;
- (vii) allocation ratios;
- (viii) motor vehicle expenses; and
- (ix) other expense items:
  - a. advertising;
  - b. pricing books and pricing services;
  - c. business entertainment;
  - d. bad debts;
  - e. travel and conference fees;
  - f. donations; and
  - g. bankcard service charges.

Results of the 1977-78 Survey

3.7 The 'overall average pharmacy' results for the 1977-78 Survey are presented in Table 3 at the end of this chapter. The data in the table has been disaggregated into four sectors; National Health Scheme (PBS) dispensing, Veterans' Affairs (RPBS) dispensing, private dispensing and retail sales.

3.8 A breakdown of the National Health Scheme (PBS) results by stratum is presented in Table 4 at the end of this chapter. The principle applied in determining dispensing fees is that the gross margin per PBS prescription should balance with total costs after allowing for a return on funds employed at the rate of 10.5 percent per annum. Table 4 indicates that the gross margin per PBS prescription exceeded the total costs by 32.7 cents.

The "Six Point Package" Agreement

3.9 Following disclosures, in December 1979, of excess payments of 33 cents per prescription and the ADP errors in the 1972-73 Survey, the Guild by-passed the Joint Committee and negotiated directly with the Commonwealth Government. Out of these negotiations emerged an agreement which was known as the 'six point package'. This was placed before

the Chairman of the Joint Committee and unanimously supported by both sides. Under the terms of the Act, the Chairman had no option other than to make a determination in line with the agreement. The terms of the package were:

a. reduction of the level of dispensing fees by four cents immediately - for administrative purposes the earliest practical date for implementation was 1 May 1980;

b. the Joint Committee to conduct an investigation into alternative methodologies to be suggested by an independent group of accountancy firms and the Industries Assistance Commission, the cost to be borne by the Commonwealth Government;

c. future inquiries to be carried out for the Joint Committee by a mutually agreed independent organisation, at Commonwealth Government expense (as at present);

d. based on such an inquiry, the Chairman of the Joint Committee to make a determination to be effective from a mutually agreed date not later than 1 July 1981;

e. an agreed updating formula to be applied to the figures on which the Chairman bases his determination in (d) above; and

f. should the Chairman's determination in (d) above show that the decrease of four cents was not justified, then a retrospective adjustment would be made by the Government to reinstate the four cents or part thereof - in any event the Chairman's determination would be accepted by the Guild as the basis for future updating.

The Excess Payments to Chemists

3.10 Three separate errors were made between 1972-73 and the end of 1979 which resulted in chemists being paid higher fees under the National Health Scheme (PBS) and the RPBS than was warranted. The errors were

a. a Cost of Goods Sold error made within the Joint Committee Secretariat which gave rise to estimated over-payments of eight cents per prescription for 1973-74 and five cents per prescription for 1974-75. This error was discovered when processing the July 1974 Cost of Goods Sold Analysis. In extracting and processing data for the 1972-73 Survey discounts and rebates were incorrectly applied to minor pack values as well as actual material costs in the earlier calculations;

b. an error in the allocation of labour costs in the 1972-73 Survey. This was a transcription error made by a member of the programming staff provided by a firm of consultants under contract to the Department of Health. The error resulted in wages being incorrectly allocated to lower paid retailing staff on the basis of time/cost ratios applying to higher paid dispensing staff. This error is considered in detail in Chapter 4;

c. errors arising from structural change in pharmacy operations and the use, without adequate adjustment, of indices used in updating fees since 1 July 1976.

3.11 The extent of the excess payments cannot be quantified definitely. It varies depending on the assumptions used. In his statement to the House of Representatives on 2 April 1980 the Minister for Health referred to maximum excess payments of $235 million under the PBS; the Minister for Veterans' Affairs indicated maximum excess payments of $18 million under the RPBS in his statement to the House of Representatives on 21 April 1980. These figures were based on the assumptions that:

> "If a valid determination had been made early in 1980 retrospectively adjusting all fees on the basis of the findings of the 1977-78 Survey of Pharmacy Earnings, Cost and Profits; and if that determination was made on the Relatively Economic Pharmacy Approach basis."

3.12 Using the foregoing assumptions the estimated excess payments for the PBS on an annual basis are as follows:

Year	Estimated Excess per Prescription (cents)	Total ($m)
1973/74	23.3	20.3
1974/75	16.5	16.1
1975/76	25.0	25.2
1976/77	51.0	45.7
1977/78	53.1	49.3
1978/79	55.7	51.7
1979/80 to 31.12.79	assume 55.7	26.3
		$234.6

3.13 The total excess payment under the PBS may be attributed to the three separate errors which occurred as follows:

		($m)
a.	Cost of Goods Sold Analysis error 1973-74 to 1975-76	61.6
b.	Error in allocation of labour costs in the 1972/73 Survey	126.5
c.	Structural change in pharmacy operations and the use, without adequate adjustment of indices used in updating fees since 1 July 1976	46.5
		$234.6

3.14 Excess payments under the RPBS using the previously mentioned assumptions were:

	($m)
1973-74 to 1975-76	4.1
1976-77 to 1978-79	14.1
	18.2

3.15 The PAC has received evidence that recovery of the overpayments, due to the Cost of Goods Sold error between 1973-74 and the end of 1976, was not sought, and that this was done on the authority of the then Minister for Health. As this decision appears to have been a matter of policy, the PAC has not enquired into it further.

3.16 The determination made by the Chairman of the Joint Committee on 9 April 1980 fixed a new dispensing fee for chemists and legally wiped the slate clean - for the second time - of previous errors. This translated PBS overpayments totalling $173 million (i.e. the total of the errors identified above as due to the allocation of labour costs in the 1972-73 Survey and structural change in pharmacy operations) and $18 million RPBS overpayments into "notional excess payments"; notional because, in law, they no longer existed. The circumstances giving rise to these ADP errors and the question of their recoverability are considered further in Chapters 4 to 6.

TABLE 3 : OVERALL AVERAGE PHARMACY REPORT, 1977-78

OVERALL PHARMACY REPORT — ENQUIRY INTO PHARMACY EARNINGS, COSTS AND PROFITS, 1977-78 — PAGE 1 — 7/07/80

STRATA USED - 1,2,3,4,5,6,7,8

SUMMARY OF EARNINGS AND COSTS - PRELIMINARY REPORT

	DOLLARS					CENTS PER NHS PRESCRIPTION
	NHS DISPENSING	V.A. DISPENSING	PRIVATE DISPENSING	RETAIL SALES	TOTAL PHARMACY	NHS DISPENSING
SALES	72385	6780	7604	139255	226025	391.9471
OTHER INCOME	103	9	10	2386	2509	0.5573
TOTAL INCOME	72488	6790	7615	141641	228534	392.5044
COST OF GOODS SOLD	34867	3345	3206	98686	140104	188.7951
GROSS MARGIN	37621	3445	4409	42955	88430	203.7093
STAFF LABOUR COST (AWARD RATES)	9983	805	650	19619	31056	54.0545
DIRECT DISPENSING	642	52	41	0	735	3.4751
ANCILLARY DISPENSING	6566	528	426	0	7520	35.5516
PROF. COUNSELLING DISPENSING	91	7	6	0	104	0.4915
PROF. COUNSELLING OTHER	0	0	0	131	131	0.0000
RETAIL	0	0	0	14816	14816	0.0000
TELEPHONE	191	15	13	126	345	1.0357
COMMON ACTIVITIES	1539	125	101	2589	4355	8.3351
NO ACTIVITY	757	61	49	1729	2596	4.0964
ABSENT	197	16	13	229	455	1.0691
PROPRIETORS NOTIONAL SALARY (NTH)	11866	968	787	6919	20542	64.2537
DIRECT DISPENSING	1085	88	72	0	1245	5.8730
ANCILLARY DISPENSING	7974	650	528	0	9152	43.1785
PROF. COUNSELLING DISPENSING	174	14	12	0	200	0.9421
PROF. COUNSELLING OTHER	0	0	0	224	224	0.0000
RETAIL	0	0	0	3627	3627	0.0000
TELEPHONE	257	21	17	169	464	1.3916
COMMON ACTIVITIES	1254	103	84	2189	3629	6.7901
NO ACTIVITY	1036	85	70	586	1776	5.6093
ABSENT	87	7	6	125	224	0.4691
PROPRIETORS NOTIONAL SALARY (ONTH)	817	68	55	346	1286	4.4263
ANCILLARY DISPENSING	208	17	14	0	239	1.1257
RETAIL	0	0	0	1	1	0.0000
COMMON ACTIVITIES	610	50	41	345	1046	3.3006
PROPRIETORS NOTIONAL SALARY(OHAP)	685	56	45	582	1769	3.7099
TOTAL LABOUR COSTS	23352	1897	1537	27866	54653	126.4444

STRATA USED -
1.2.3.4,5,6,7,8

SUMMARY OF EARNINGS AND COSTS - PRELIMINARY REPORT (DOLLARS) / CENTS PER NHS PRESCRIPTION

	NHS DISPENSING	V.A. DISPENSING	PRIVATE DISPENSING	RETAIL SALES	TOTAL PHARMACY	NHS DISPENSING (CENTS PER NHS PRESCRIPTION)
EXPENSES	6393	697	435	15945	23469	34.6156
PROPERTY	1939	158	137	7613	946	10.4968
SCRIPT PRICING - NHS	44	0	0	0	44	0.2366
SCRIPT PRICING - V.A.	0	187	0	0	187	0.0000
ADMINISTRATIVE	1103	84	78	2090	3355	5.9732
OPERATING	808	65	56	1511	2441	4.3758
ADVERTISING	597	48	41	1270	1956	3.2345
DEPRECIATION	347	28	22	671	1068	1.8778
HIRING & LEASING	559	42	36	1088	1725	3.0283
INTEREST	0	0	0	0	0	0.0000
VEHICLE	389	34	25	668	1117	2.1075
PRICING SERVICES	32	3	2	48	86	0.1759
SUBS & REGISTRATION	112	10	7	185	314	0.6048
BUSINESS ENTERTAINMENT	77	7	5	147	235	0.4164
BAD DEBTS	20	1	2	41	64	0.1067
DONATIONS	12	1	1	23	37	0.0659
TRAVEL & CONFERENCE	105	7	7	187	306	0.5669
BANKCARD SERVICE CHARGES	3	0	0	12	16	0.0173
MISCELLANEOUS	246	22	17	390	674	1.3314
TOTAL LABOUR COSTS & EXPENSES	29745	2594	1972	43811	78121	161.0600
NET PROFIT	7876	851	2437	-855	10308	42.6492
PROPRIETORIAL LEAD						
NO. PRESCRIPTIONS RP	17800	1445	1203	0	20448	
EP	668	51	19	0	739	
TOTAL	18468	1497	1222	0	21187	
I.P.A. (INCLUDED IN INCOME ABOVE)	0					0.0021

SUMMARY OF FUNDS EMPLOYED

	NHS DISPENSING	V.A. DISPENSING	PRIVATE DISPENSING	RETAIL SALES	TOTAL PHARMACY	NHS DISPENSING (CENTS PER NHS PRESCRIPTION)
TOTAL FUNDS EMPLOYED	17407	1355	1176	45205	65143	94.2529
AV.STOCK	5806	469	387	23625	30287	31.4354
AV.FIXTURES & FITTINGS	2429	184	164	4911	7689	13.1547
AV.LEASEHOLD PREMIUM	16	1	1	31	49	0.0879
AV.SUNDRY DEBTORS-TRADE CREDITORS	-915	-38	-69	-2826	-3848	-4.9537
AV.BANK BALANCE	168	15	11	254	447	0.9085
AV.GOODWILL	7295	495	514	14794	23098	39.5020
AV.OTHER ASSETS	73	6	5	152	236	0.3970
AV.OTHER LIABILITIES	-298	-24	-21	-458	-800	-1.6145
AV.MOTOR VEHICLES	609	53	38	894	1593	3.2958
AV.PLANT & EQUIPMENT	1361	107	91	2650	4209	7.3709
AV.MONEY INVESTED IN W'SALERS	862	87	54	1180	2182	4.6690

TABLE 4 - 1977/78 PHARMACY ENQUIRY RESULTS

Summary of Costs & Earnings in Cents per NHS Prescription

	Stratum 1	Stratum 2	Stratum 3	Stratum 4	Stratum 5	Stratum 6	Stratum 7	Stratum 8	Overall Average
Total Income	397.6096	391.8304	394.7914	395.6715	395.6922	384.7732	394.2910	386.4713	392.5044
Cost of Goods Sold	200.7486	189.5560	190.6901	191.7231	190.7069	183.7687	185.9458	179.0405	188.7951
Gross Margin	196.8611	202.2744	204.1013	203.9484	204.9853	201.0045	208.3452	207.4309	203.7093
Staff Labour Costs	43.1861	46.8412	61.2726	51.2899	60.7231	54.6643	53.6714	59.8585	54.0545
Proprietor's Notional Salary	129.3492	96.5996	77.5671	78.1210	69.1389	51.6756	50.2587	33.2724	72.3899
(a) Inside normal trading hours	112.9960	85.9172	70.9037	71.0144	58.8568	44.3615	44.9957	31.0099	64.2537
(b) Outside hours of the pharmacy	9.3671	5.9455	2.7018	5.4522	6.0553	2.6488	2.8290	0.9784	4.4263
(c) Outside hours away from the pharmacy	6.9861	4.7370	3.9616	1.6545	4.2269	4.6653	2.4341	1.2841	3.7099
Total Labour Costs	172.5353	143.4408	138.8397	129.4109	129.8620	106.3399	103.9301	93.1309	126.4444
Expenses	42.3045	36.4106	36.3500	34.9663	31.2987	31.6878	35.0696	29.8802	34.6156
Total Labour Costs and Expenses	214.8398	179.8514	175.1897	164.3772	161.1607	138.0277	138.9997	123.0111	161.0600
Net Profit (before return on funds)	-17.9787	22.4229	28.9116	39.5712	43.8245	62.9768	69.3455	84.4198	42.6492
Funds Employed (Incl. Goodwill)	75.1110	71.0948	77.9654	87.9554	99.8843	104.5672	113.4915	121.4231	94.2529
Net Profit (after return on Funds)	-25.8654	14.9579	20.7252	30.3359	33.3366	51.9972	57.4289	71.6704	32.7526
No. of NHS scripts p.a.	8711	13,211	16,085	18,390	22,774	26,631	32,276	48,023	18,468

CHAPTER 4

THE ADP ERRORS

How the Error was Discovered

4.1 Late in 1978 the early computer printouts of the 1977-78 Inquiry indicated that very large increases in productivity had occurred within pharmacies - to the extent that pharmacies were receiving higher dispensing fees than warranted. The Joint Committee Secretariat carried out extensive testing of the updating formula using the 1972-73 and 1977-78 Inquiry data. It was this testing which pointed up the possibility of an error in labour cost calculations, and further examination revealed, in December 1979, the actual source of the error in the 1972-73 programs.

4.2 The Department of Health stated that "there had been no suspicion prior to that date (December 1979) that there was an error in the 1972-73 data processing."

How the Error Occurred

4.3 The error was made by a consultant employed by a firm working under contract to the Department of Health. It occurred in translating a requirements specification - which expressed the task to be done in mathematical notation - into a specification for a computer program to carry out the required processing. The program designer (the consultant) correctly gave directions for calculating a table of ratios to enable the allocation of total pharmacy dispensary staff costs to be made across sectors and activities in the pharmacy. The designer should then have given directions for calculating a corresponding table of ratios for allocating the costs of retail staff labour by sector and activity. Instead, it was specified that both retail and dispensing staff costs were to be allocated according to the one set of ratios calculated for the dispensing staff only. This in turn resulted in an overstatement of the proportion of pharmacy costs attributable to dispensing activities, although the total cost of dispensing activites and retail activities was correct.

The Effect of the Error on the Survey Results

4.4 It is not possible to state precisely the effect of the labour cost allocation error on the final results of the 1972-73 survey. This would have been possible if the 1972-73 data had been procesed through the 1972-73 programs with only the one error (that is, the labour cost allocation error) corrected. This was never done, and would now be a very time consuming task, if it was at all possible to perform.

4.5 After the error was detected in December 1979 the 1972-73 survey data was modified slightly and processed using the 1977-78 programs. However, the latter programs were different in several respects from the 1972-73 programs and would have produced different results even if the labour-cost allocation error had not been remedied.

4.6 The 1972-73 program (the incorrect one), when run with the 1972-73 data, indicated for the overall average pharmacy a loss of 21.8 cents per PBS prescription. This result was consistent with the expectation of The Pharmacy Guild of Australia (the Guild) which believed that PBS dispensing was, on average, unprofitable. When the same data, slightly modified, was run on the 1977-78 programs (in which the allocation error had been corrected) the results showed for the overall average pharmacy, a profit of 14.3 cents per PBS prescription. As indicated above, the difference between the two estimates of 36.1 cents per PBS prescription is not attributable solely to the correction of the ADP error.

4.7 Thus on the evidence available it is not possible to distinguish exactly the effect of correcting the ADP error from the effect of other minor changes and error corrections that were made between the 1972-73 program and the 1977-78 program. The bulk of the difference between the two sets of results is attributable to correction of the labour cost error (an error made by the ADP branch) and the cost of goods sold error (an error made by and discovered by the Joint Committee Secretariat).

Responsibility for the Error The ADP Branch of the Department of Health

4.8 The ADP Branch was required to provide a computing service for the 1972-73 Inquiry.

4.9 A Requirements Specification which expressed the processing task to be done in mathematical terms was prepared by the Central Statistical Unit (CSU) of the Department of Health and by the Joint Committee Secretariat. The function of the ADP Branch was to provide the programming and computing services necessary to effect the processing of the survey. Using the Requirements Specification as a starting point the ADP branch prepared design specifications for the computer programs to carry out the processing.

4.10 The programming of the 1972-73 survey was one of the first applications in the Department of Health (indeed in the Commonwealth Public Service) of modular programming techniques, under which large and complex processing tasks are broken down by a program designer into small modules. By this means the task of writing the program can be divided among a number of programmers, each of whom might write several modules, knowing only the input and output specifications for

those modules and what each one is required to do to the data. To test the program, each module is tested first alone and, when proven correct, linked with other modules and tested in combination. The integration of modules proceeds, with testing at each stage, until the whole program has been tested. This testing strategy was applied by the Department of Health to the modules comprising the total computer program for the 1972-73 survey. The testing verified that the program code performed in accordance with the program design specifications.

4.11 Unfortunately, however - and this was a major departure from sound practice - insufficient testing was done to confirm that the program code performed in all respects in accordance with the CSU's Requirements Specification. In particular, no check was done to ensure that the total pharmacy labour costs were correctly allocated to various sectors and activities in the pharmacy. To perform that check it would have been necessary to print out the actual wage allocation or the time/cost ratios on which they were based. According to the Department of Health:

> "...the...ratios were not recognized to be critical to the checking procedure by either the Central Statistical Unit or the Secretariat and were not requested to be printed out in this way during design or program development.
>
> However at a very late stage of checking by the Secretariat it turned out that these ratios would have been of assistance to check the labour cost allocations. ADP staff involved at the time cannot recall such a request being made. In the extremely tight time-frame available to produce a report for the Joint Committee it was possibly considered desirable but of low priority. It should be borne in mind also that the results of the Enquiry appeared to be valid and no queries were raised by the Sub-committee in relation to the labour costs".

4.12 The PAC does not accept the implication in this statement that checking the conformity of the program code with the client's (i.e. the CSU's) specifications was the responsibility of the client. A programming contractor would normally be expected to provide the necessary quality assurance tests to demonstrate compliance with the client's specification. The client might perform tests of his own but normally this would not absolve the contractor from such responsibility. The PAC considers that this would also be sound practice in the case of work done by the ADP Branch of the Department of Health for those outside that Branch.

4.13 Since the Requirements Specification provided by the CSU correctly stated the procedure for calculating the labour cost allocation ratios, the PAC considers that the responsibility for correctly translating the Requirements Specification into programs rested with the ADP Branch and that testing was part of such responsibility. Nevertheless, where an error could have large financial effects, the prudent course would have been for the client (in this case the CSU) independently to perform its own checks. Indeed, this was done during the 1977-78 Survey when the correctness of labour -cost allocations across pharmacy sectors and activities was checked independently by both the CSU and the ADP Branch by comparing computer print-out with desk calculations.

Responsibility for the Error: The Contractor

4.14 Because of staff shortages in its ADP Branch, the Department of Health engaged seven programmers from a consulting firm to assist in the work of the ADP Branch. The actual transcription error in the labour ratios which led to the ADP error was made by one of these contract programmers.

4.15 In its submission the Department of Health said that during the course of the work there were some minor problems in the management of some of the consultants, including the one who made the error, but that these "were not considered sufficient at the time to exercise clause 10 of the agreement, by which they could be returned to the consultancy firm and be replaced".

4.16 The Department of Health under its agreement was responsible for specifying the qualifications and experience required of the consultants, directing them in the carrying out of their duties, assessing their performance, and replacing them if unsatisfactory.

4.17 The question of legal liability of the contractor for the error has been referred by the Department of Health to the Commonwealth Crown Solicitor.

Was There Any Intention to Defraud?

4.18 The PAC examined the working documents in which the error occurred. Although the error is quite clearly identifiable, these documents are handwritten, untidy, difficult to read, and incomplete. They have every appearance of genuine rather than simulated poor workmanship.

4.19 The Department of Health does not consider that there is any possibility of deliberate error or fraud. In summary, its reasons for this view are:

- no ADP Branch or Joint Committee Secretariat officer would have known in detail the potential effect of the error on the final outcome of the survey;
- there was no link between the perpetrator of the error and the "beneficiary" (5500 pharmacies);
- if the Guild had been involved in a fraudulent conspiracy it would not have agreed to a subsequent survey in 1977-78;
- the nature of the error is more consistent with a genuine mistake than with a malicious or mischievous act; and
- the Public Service Board Team investigated the matter and found no evidence of any criminal action.

The PAC agrees that no criminal, malicious or mischievous intent is evident.

Did the Error Affect the 1977-78 Survey?

4.20 In planning the processing of the 1977-78 questionnaire data, a number of amendments to the earlier programs, particularly the Random Activity Sampling (RAS) program, was made. Discussion and investigation took place on whether it would be easier to rewrite the RAS program based on new specifications drawn up by the CSU or to use the existing program.

4.21 The module in which the error actually resided was originally part of the Financial Questionnaire (FQ) program. One of the changes made for the 1977-78 program was to move this module into the RAS program. Another was the requirement that allocated labour costs be printed out for comparison with manually produced results. It was decided that rather than move the original module for calculating labour cost allocation ratios (which contained the as yet unsuspected error) from the FQ to the RAS program, the module would be rewritten, based on the new "plain English" Requirements Specification which the CSU had produced. The programmer who wrote the new module did so correctly, thereby unknowingly correcting the error which resided in the old version. Thus the error was not carried through to the processing of the 1977-78 Survey. It was not until the 1972-73 data was run with the 1977-78 program late in 1979, and the large discrepancy with the earlier results noted, that the error in the original program was detected.

CHAPTER 5

FACTORS CONTRIBUTING TO THE ERRORS

5.1 The PAC sought to discover why the errors in the 1977-73 program were not detected earlier. It concluded that a number of factors led to the error being made and to the failure to detect it. These included:

- Inadequacy of testing procedures
- Pressures to complete the 1972-73 survey
- Failure to follow standards
- Staffing shortages in the ADP Branch
- Lack of ADP Audit staff

These are discussed in the following sections.

Inadequacy of Testing Procedures

5.2 In large and complex computer programs there may be many alternative processing pathways through the programs. In such cases it could be virtually impossible to test the programs thoroughly without passing a large amount of data through them over a long period of time. However, that situation apparently did not prevail in the case of the programs for the 1972-73 Survey processing, since the equivalent programs for the 1977-78 Survey processing (which are of equal complexity) were tested thoroughly. The structure of the programs, while complex, was such that it would have been feasible to test the 1972-73 programs exhaustively against manual calculations.

5.3 The Department of Health's ADP Standards No. 240-225 and 240-34 (effective date 1/4/73) call for the preparation of a System Test Plan, the purpose of which is :

> "to establish the requirements to be met before the system can be considered as being operational. The System Test Plan will provide a permanent record of the test procedures designed to prove the system".

5.4 The PAC requested the System Test Plans for the 1972-73 and 1977-78 Survey processing. The Department of Health stated that a System Test Plan in the form called for in the Standards Manual had not been prepared. The reasons given were, first that the standards were "in embryo" at the time and second, that the ADP Branch had not been given the responsibility for the systems analysis phase of the project, having received detailed requirements specifications from the Central Statistical Unit (CSU).

5.5 The PAC considers that these are not valid reasons for not formally documenting the testing procedure as called for by the Department of Health's own Standards Manual.

5.6 Such testing of the 1972-73 programs as did occur was carried out only in late 1974, some 18 months after the nominal effective date of the relevant Standards, while testing for the 1977-78 survey was carried out from October 1977 to August 1978. An interval of more than four years seems to the PAC to be an inordinately long gestation period for "embryo" standards.

5.7 With regard to the second point, the view of the ADP Branch is apparently that because it had not been called upon to carry out systems analysis it was not responsible for preparing a System Test Plan. The PAC considers that the ADP Branch's responsibilities as a supplier of programming and processing services to the Joint Committee Secretariat included the requirement to design tests in collaboration with the client, to prove the conformity of the program with the client's specification, to document the tests, and to carry them out.

5.8 The PAC recongizes that simply documenting a Test Plan according to the prevailing Standard would not necessarily result in a thorough or effective test. However, in the 1972-73 Survey processing such a discipline might well have helped to identify gaps in the test procedure. The PAC considers that the Department of Health should have prepared a Test Plan in accordance with its own Standards then current.

5.9 The Department of Health stated that in developing the programs for the 1972-73 survey:

> "...it became necessary to hold a number of three-way meetings between the Central Statistical Unit, the Enquiry Secretariat and ADP to interpret the requirements of the Joint Committee.
>
> In 1977/78 these meetings were formalized into a Review Committee which met 36 times during the course of the Enquiry to discuss matters of detail, including the testing strategies and the results of tests carried out".

5.10 The Department of Health provided the PAC with the minutes of 25 of the meetings of its Review Committee. Among numerous other matters these minutes describe in considerable detail the many changes to the earlier programs which were required for the 1977-78 survey, as well as the tests which were applied, and the results of those tests. Thus the test strategy - if it can be called that - for the 1977-78 survey, is embedded in minutes covering a variety of topics spread over many pages of minutes. The PAC considers that this approach to documenting the test strategy (and to documenting design changes) has the serious disadvantage that it does not allow easy review of the strategy by others. It is as important to apply the principles of technical review to testing strategy as to any other aspect of system development. The PAC therefore considers that the test strategy which evolved during the discussions in the Review Committee should have been extracted from the Minutes and used to update one coherent System Test Plan.

5.11 Although it might be said that the test strategy for the 1977-78 Survey was documented after a fashion, the Department of Health has not provided the PAC with <u>any</u> form of Test Plan - in minutes or otherwise - for the 1972-73 Survey.

5.12 One reason why thorough tests were not applied appears to have been the urgency of completing the 1972-73 Inquiry, which caused a number of short-cuts to be taken. The Department stated:

> "...to duplicate the sort of testing program that was undertaken in the 1977-78 Enquiry would have required an additional three months where we were left alone to finish the 1972-73 Enquiry. In fact as soon as the preliminary printout of the 1972-73 Enquiry was provided to the Sub-committee for their information we received a request from the Guild to come up with a set of regression equations so that they could have a look at the results under their regression approach. Then a further request was received from the Joint Committee to run the program again to implement some decisions the Chairman had made. Then there was a request from the Government to run it to simulate the relative economic pharmacy approach. There was a whole chain of demands on the Secretariat at the time that prevented us from getting back to that...
>
> If the step by step manual calculations had been performed on the CSU specifications ... during those three months I have no doubt that the error would have been discovered".

5.13 The PAC asked why the Joint Committee Secretariat did not go back to checking against manual calculations when the pressure had eased. The reply was, in effect, that there was a considerable amount of turmoil, including the resignation of the Chairman of the Joint Committee, during the 12 months that followed and this prevented retrospective checking. Moreover because the results of the processing were in line with what the Guild expected - showing a loss in the overall average pharmacy in preparing PBS prescriptions and a profit on retail sales - nothing in the results suggested any error in the programs.

Pressure to Complete

5.14 The previous section discussed design and programming short cuts taken due to the pressure from both the Government side and the Guild. This pressure was specifically alluded to by the Director-General of Health in evidence:

> "Secondly, on these points of atmosphere, I would like to emphasise the one of 'pressure', not as an excuse in any sense but as a matter of fact. Many departments and many areas of my Department are used to pressure. In 1972-73 and again in 1977-78 the ADP area, the secretariat of the inquiry and the central statistical unit were all under continuing pressure to complete the inquiries. I can well remember the pressures that were applied in 1973-74 and early 1975 by the Minister, by myself, by the politicians, who were receiving representations by the Guild and the then Chairman of the Joint Committee to finalise the inquiry. I am quite sure that entirely apart from enquiries, there is no area of my Department that has been under such continuing pressure as has the ADP Branch".

5.15 To understand why this pressure was being applied it is necessary to look back to April 1972. At that time, following negotiation between the Minister for Health and the National President of the Guild, it was decided to hold another Inquiry into Pharmacy Earnings, Costs and Profits. As discussed in Chapter 2, there had been a long history of dissatisfaction among chemists regarding the level of remuneration for the supply of pharmaceutical benefits. That dissatisfaction caused the Minister for Health to set an early completion date (March 1974) for the IAnquiry. It appears that this deadline was set in ignorance of the magnitude and difficulty of the task, and the resources which could be applied to it. It was not surprising, therefore, that the deadline proved impossible to meet. The Joint Committee then pressed for the results to be available by May 1975 so that the increase in dispensing fees could be accommodated in the 1975-76 Commonwealth Government Budget. That meant all preliminary results had to be produced by 31 March 1975.

5.16 The Department of Health indicated to the PAC that the ADP Branch had to undertake the design, programming and testing of the program within a period of eight months, despite the fact that initial investigations indicated that it would require at least 12 months with the staff available:

> "As a consequence all available resources not only within ADP but within the the other relevant areas of the Department, e.g. Secretariat, had to be used to undertake the task. This left no time to *undertake those further refinements such as thorough systems testing, etc.* (PAC's emphasis)
>
> The pressure under which the ADP Branch, the Secretary to the Joint Committee and the Enquiry Secretariat worked cannot be over emphasized. There are constant references to the need for expediting finalization in the Minutes of the Joint Committee during 1974 and early 1975. Further pressures resulted from the need to get the matter dealt with within the budget context".

At a result, officers of the ADP Branch felt that they were working under unreasonable deadlines.

5.17 The Department of Health was advised by the CSU in November 1974, of misgivings of the validity of the results of the Survey. The CSU advised that programs should be tested against desk calculations, saying:

> "While it is appreciated that there is a need for the Enquiry to be completed as soon as possible, I *believe that the validity of the results produced* should be insured as far as it is possible".

However, the Department of Health countered:

> "Overriding all that advice ... was the pressure on the Department and the Joint Committee to have the 1972-73 Enquiry wound up and finished ... The pressure and the staff resources did not allow us to go right down the track as experience has shown would have been advisable".

5.18 If unrealistic deadlines are set for ADP staff, the latter should formally communicate to their management any apprehensions they feel about meeting the deadlines and the risk of error that might result from over-hasty work. However, in practice, it is all too common for technical staff, wishing to appear willing and competent, not to protest at deadlines which privately they feel are impossible. The PAC recognizes that calculated risks have to be taken to meet urgent deadlines. However, the danger of setting deadlines in total ignorance of the magnitude of the task or the resources available is grossly irresponsible of management. If the practice persists, sooner or later it will result in programming errors even more disastrous than the one under consideration in this inquiry.

5.19 Both management and professional/technical personnel have responsibilities in this area. Permanent Heads should not make commitments to Ministers without an analysis of the resources needed and available. They should try to create an environment in which technical people are not afraid to argue that deadlines are unrealistic. Formal methods of project planning control should help in establishing realistic schedules in opposition to arbitrarily defined completion dates. The PAC understands that the ADP Branch of the Department of Health has now introduced a project planning and accounting system which may help in this regard.

Failure to Follow Standards

5.20 The formal ADP standards in the Department of Health during the 1972-73 Inquiry were above the average of those applying generally in the Commonwealth Public Service at that time. However, they were not complied with in several important respects for the programming of either the 1972-73 or 1977-78 Surveys.

5.21 For example, a Management Review was mandatory under the ADP Standards in force in 1973. Procedure No. 240-270 of the Department of Health's ADP Standards calls for a management presentation to be made to:

- study documentation created during the design phase;
- decide whether the proposed design is a suitable solution for satisfying the requirements set out in the Statement of Requirements; and
- decide whether the documentation produced is of the expected standard.

The PAC does not consider that management review alone would have detected the ADP error, since this would have required carefully following the design and comparing it at every point with the Requirements Specification. However the PAC considers that in a disciplined environment it is likely that management review of the documentation produced might well have fostered attitudes of more careful and thorough workmanship.

5.22 The Department of Health contends that although these standards bear the words "effective 1-4-73", they were not really in effect at that time. Indeed the Department of Health implied that compliance was optional because the standards at that time were "in embryo". The PAC considers that the orderly implementation of Standards and procedures requires that if standards are in a trial phase and are not obligatory they should be so labelled. The words "effective date ..." should mean the date at which the standards come into force, not the date they are sent to the printer or issued for trial or preliminary use. On the evidence of the words "effective date 1-4-73" the PAC rejects the proposition that it was permissible to ignore the standards because they were not really in force at the time of system design for processing the 1972-73 Survey.

5.23 The Department of Health also argued that responsibility for observing prescribed standards did not apply to the 1972-73 Inquiry processing because different organisational arrangements were made:

> "...the Secretariat in close collaboration with the Central Statistical Unit prepared a detailed statement of requirements for the Pharmacy Earnings Surveys. The survey design and the proposed methodology were referred for consideration and approval by the Joint Committee and a detailed specification of processing requirements was forwarded to ADP. Under this approach the ADP branch was not called upon to carry out systems analysis and design functions in a formalized sense. Consequently the ADP projects standards for systems analysis and design are not directly applicable. (Standards Manual No. 2 - the Project Manual).
>
> The role of ADP for the two surveys was to design and develop suites of programs needed to meet the processing requirements set out in detailed requirements specifications prepared by the Central Statistical Unit and the Secretariat. The programs were designed, developed and tested in accordance with programming standards covering this aspect of ADP work. (Standards Manual No. 2 Vol. 1 - the Programming Manual)".

5.24 The PAC rejects any suggestion that none of the provisions of the Project Manual were relevant to the task undertaken by the ADP Branch. Although it is evident on reading the Project Manual that much of it (e.g. procedures 210-230) was written with a different mode of working with the client in mind, nevertheless much of section 240 (System Design) which occupies the second half of the Project Manual was, in the PAC's opinion relevant to the role of the ADP Branch in providing services to the Inquiry.

5.25 The fact that the client had specified precisely the requirements in mathematical notation did not absolve the ADP Branch from responsibility for system design. In no way could the CSU's requirements statement be regarded as a system design.

5.26 The PAC therefore considers that many of the procedures contained in section 240 of the Project Manual should have been applied. The PAC is extremely concerned that the procedures were not applied and in particular it considers that procedures relating to the following matters should have been observed.

- the conclusion and complete definition and description of data element;
- management review;
- a formal system test plan; and
- formal authorization of system changes.

Staffing Shortages in the ADP Branch

5.27 At its hearings on 16 July 1980 the PAC received evidence which suggested that the Department of Health's ADP Branch staffing requirements had been considered inadequately by the Public Service Board.

5.28 It was the expansion in the volume of prescriptions under the revised National Health Scheme, and hence claims by chemists on the Department of Health, which led to the creation of the ADP Branch. The Department of Health established the initial ADP team in 1962 to develop a system for processing such claims, and by 1965 computer-based payment of claims had commenced. The Department of Health's Assistant Director-General, ADP Branch, stated:

> "Thus Pharmaceutical Benefits Scheme processing was the driving force behind the Department's entry into ADP and still remains one of our major systems".

5.29 The Department of Health made strenuous efforts to overcome resource shortages in the ADP Branch. Because of external constraints which applied at the time it was only partly successful. Its major obstacle was the staff ceiling constraints determined by the Commonwealth Government and imposed by the Public Service Board. Some relief was obtained in late 1972 when seven consultants were engaged to work under departmental control, assisting in the ADP development of the 1972-73 Survey. A major review of the ADP Branch was carried out by the Department and presented to the Public Service Board in August 1973. That submission sought an increase of 72 positions on its prevailing establishment of 135, including three for systems audit and validation, a function which did not at that time exist within the ADP Branch. The balance of 69 positions was, according to the Public Service Board observer at the PAC hearings, "...based on work that was in hand and also projected work programs".

5.30 The extent of the workload within the ADP Branch was known to the Public Service Board. Nevertheless, the Department of Health's bid of 73 positions was countered by an initial offer of 32 positions by the Public Service Board, in February 1974. In its advice to the PAC the Public Service Board acknowledged the increased workload but declined the full increase sought voicing the concern

> "... in a general fashion about the magnitude of the increases being proposed by Health. This concern was against a background of high growth rates in the Public Service at the time and shortages of skilled staff in key work levels. In addition to this general concern there were reservations in the Board's office about some components of the Department's ADP work program. These reservations were related to the extent to which policy questions did not appear to have been adequately resolved at that stage".

5.31 These opposing viewpoints were the subject of intensive negotiations between the Department of Health and the Public Service Board over the next four months. By July 1974 the Department reluctantly agreed to accept an increase of eight positions on the 32 originally granted. This apparent minor gain, however, was offset by the Public Service Board's refusal, in October 1974, to extend the ADP consultancy arrangements beyond that date.

5.32 The PAC considers that control of Commonwealth Public Service numbers is no easy matter. The tensions between the responsibilities of Permanent Heads of departments and the responsibilities of the Public Service Board generally for the overall efficiency and economy of the Public Service have been noted frequently, but never resolved (see for example, the Report of the Royal Commission on Australian Government Administration). Whilst noting that Commonwealth Government policy towards control of Public Service numbers by ceiling restraints has been in force, in its present form, for almost a decade, the PAC is not satisfied that this is always justified on a cost effectiveness basis. There is a considerable element of inefficiency and uncertainty in the process, and in this instance it appears to have been compounded by a mistiming between increasing demands placed on the Department of Health at a time when the general staffing environment was becoming harsher. Noting the pressures to which that critical area of departmental operations has been subjected, the PAC believes that its staffing requirements should be reviewed.

Lack of ADP Audit Staff

5.33 Commencing in 1973, the Department of Health made efforts to set up a systems audit and validation group in its organisation. The Public Service Board opposed its establishment because it did not recognise this as a discrete function at that time. It was not until 1980 that the Department of Health obtained some positions which could be allocated to ADP audit.

5.34 As noted earlier, the Department of Health's August 1973 submission to the Public Service Board seeking an increase of 72 positions for ADP included three positions for a cell with the proposed name of 'systems audit and validation group'. The Public Service Board's agreement to 40 positions out of the 72 sought did not include provision for these three positions. The reasons for this were that:

> "... the work envisaged for this group appeared to be more appropriate to the application section and would normally be performed by project team leaders in that section in accordance with installation standards and procedures as developed by the standards group. I might add here that the Board's ADP officers had considerable respect for the standards that Health was then developing in relation to ADP. On the basis of this discussion, our officers did not agree to the provision of three positions for this group".

In other words, the Public Service Board's view at that time was that the responsibility for ensuring that ADP systems matched users' requirements was more properly a matter for the ADP team leaders themselves than for a group independent of the ADP applications area.

5.35 Progress with the implementation of ADP audit in the Department of Health continued to be negated by the Public Service Board. In 1975 the Department of Health proposed an upgrading and expansion of its internal audit section which then consisted of three positions. The Public Service Board did not agree to the reclassification proposed, nor the provision of another position solely for ADP audit.

5.36 During this period the views of the Auditor-General's office appeared to be at variance in principle with the actual practice of departments and of the Public Service Board. During the PAC hearings the Auditor-General's observer was asked his Office's policy on these matters. The letter of reply drew the PAC's attention to the following extracts from Reports of the Auditor-General since 1970:

1969-70 Report Paragraph 307:

> "... with the rapid expansion of ADP throughout the departments and authorities there appears to be a need for more appropriate training in this area".

1970-71 Report Paragraph 320:

> "Audit reviews during 1970-71 revealed that there has been some improvement in the overall position but that areas remained where internal audit is either not in operation or where the effectiveness leaves scope for further development".

1971-72 Report Paragraph 316:

> "Audit reviews during 1971-72 disclosed that, whilst improvement had occurred in some departments, generally the position remained unchanged from that mentioned in paragraph 320 of my Report date 17 August 1971. Some instances were also revealed where internal audit was in arrear due mainly to internal audit positions not being fully staffed and to the employment of internal audit staff on other duties".

1972-73 Report Paragraph 325:

> "*In its One hundred and thirty-ninth Report the* Public Accounts Committee, among other things, traced the history of the many critical references made in the Reports of successive Auditors-General from 1954-55 which, in general, had emphasised the scope for improvement in the internal audit arrangements in Commonwealth departments and directed attention to the need for establishing uniformity in objectives and practices and for maintaining stability in the staffing of internal audit establishments".

5.37 Reports of the Auditor-General since 1963-64 have referred to the development and growth of Automatic Data Processing in the Commonwealth Government. This growing involvement in computers has brought about a need for auditors, both internal and external, to acquire a knowledge of computer processes sufficient to enable them to audit ADP accounting applications the Auditor-General stated:

1975-76 Report Paragraph 4.7:

> "For a number of years attention has been directed in previous Reports to the need for continued improvement in the general standard of internal audit, particularly in departments.
>
> The main criticisms have centred around;
>
> - insufficient allocation of staff to carry out effectively the internal audit function;
> - arrears of work resulting in inadequate coverage by internal audit;
> - deficient audit programs; and
> - departmental management not taking effective remedial measures on report of internal auditors".

1976-77 Report Paragraph 3.22.13:

> "There is inadequate knowledge of ADP for effectively auditing computerised systems".

5.38 By 1978, the direction of the comments of the Auditor-General's Report on the Department of Health was patently clear.

"3.13.2 Following a review during 1977-78 of the audit in the Department's central and regional offices, my office sought comments and advice of operation of internal remedial action proposed on the following unsatisfactory aspects;

- Internal audit of ADP systems was inadequate. This was a matter for concern, having regard to the high level of expenditure being processed by ADP...

The Department recently advised:

- It was aware of the need to upgrade its internal audit coverage of ADP systems and intends to again seek Public Service Board approval to create a specialist ADP internal audit position. A previous proposal in 1975 was not approved by the Board."

5.39 And again in 1979 the Auditor-General reported:

"2.10.4 Paragraph 3.13.2 of my 1977-78 Report referred to unsatisfactory aspects of the internal audit function in the Department's central and regional offices and the nature of action proposed to remedy the position. Following reviews by my Office during 1978-79, it was found that although some improvements had been made, certain matters were considered to be still unsatisfactory and were represented to the Department. The unsatisfactory features raised and the Department's responses are shown below:

- An ADP specialist internal audit position had not been created as proposed by the Department in August 1978.

  The Departmental reply of 3 August 1979 indicated it had been decided not to submit an organisation proposal to the Public Service Board in view of the then imminent issue of new guidelines by the Public Service Board on the practice of internal audit in the Australian Public Service. Since the issue of the guidelines, the Department has had discussions with officers of the Board and members of the Inter-departmental Advisory Committee on Internal Audit, and a proposal for the reorganisation of the Internal Audit Section is expected to be forwarded to the Board shortly".

5.40 It was not until December 1979 that the Department of Health again proposed a reorganisation of its internal audit unit, and in January 1980 the Public Service Board approved the position sought for ADP audit. The PAC inquired into the reasons for the apparent two year delay between the Auditor-General's strictures and effective action. The Public Service Board informed the PAC that after 1975 it received no proposals until 1979 regarding internal audit positions from the Department of Health. When it received the Department's proposal it acted quickly to approve it. The Department's advice to the PAC was as follows:

> "Having put a proposition to the Board which was not agreed to, we then waited a while. If events had taken a normal course, in 1978 we would have put a further proposal to the Public Service Board for an upgrading of the internal audit area. We were conscious that we needed an upgrading and we wanted an upgrading. At the same time we were also aware of what the Board was doing with regard to the new internal audit guidelines. Therefore we felt that rather than go to the Board with a proposal which subsequent events might prove to be underclassified or some such thing, we would be better off waiting for the guidelines and then approaching the Board as quickly as possible. That is what we did".

5.41 The PAC notes that the sequence of events could indicate that initially the Department of Health was ahead of the Public Service Board in its view of ADP audit and consequently was unable to gain the support of the Public Service Board. Despite the increasing pointedness of the Auditor-General's comments on ADP audit and internal audit the Board's approval of a new approach did not emerge until April 1979. Foreknowledge of this inhibited the Department of Health's approach, and this was the final contributing factor to the delay.

5.42 Both the Public Service Board and the Department of Health indicated that the ADP audit function was approved without knowledge of the ADP error, or the quantum of the excess payment. The PAC has no reason to doubt that. However, noting that, only recently has the Department of Health and the Public Service Board been able to agree on the provision of ADP audit, the PAC considers that a further review should be conducted in the light of the findings of this inquiry.

Conclusions

5.43 Although the following recommendations are mainly directed at the Department of Health, the PAC considers that they are equally applicable to all departments. The Department of Health is reputed to be further advanced in ADP practices than many other departments. However, because they have experienced obvious problems, the PAC is concerned with the risk of ADP errors which must exist in departments whose standards and procedures are less well developed, documented or supervised than in the Department of Health. During 1981, the PAC will require all departments to report on the steps they have taken to ensure that their ADP standards of practice are up-to-date, detailed, comprehensive, and complied with, having regard to the size of the department and the scope of its ADP work.

5.44 Recommendations

(i) The Department of Health at intervals of not more than two years, review its standards of practice for ADP analysis, design, programming, testing, implementation and documentation to ensure that standards of practice are appropriately detailed, comprehensive and up-to-date.

(ii) The Department of Health ensure that its ADP staff comply with authorized standards and procedures and the Department establish management controls to ensure compliance. Comprehensive internal audit of ADP practices be carried out at intervals of not more than two years.

(iii) The Department of Health's ADP standards and procedures include the requirements for thorough technical review and certification of the requirement specification, analysis, design, programming, documentation and system performance. This should be done by users, peers or supervisors as appropriate. These standards are to include the requirement for the preparation of a detailed system test plan, designed to prove that the system output conforms with the user's requirements specification, not merely with the program design specification.

(iv) When developing standards:

a. it is the responsibility of ADP management to ensure that system development is in accordance with sound professional practice, including compliance with appropriate standards and procedures;

b. Permanent Heads ensure that time-frames for completion of ADP projects are set with due regard to the resources available; and

c. If targets are set for the Department of Health without regard for the resources available and of the ADP management considers that it is unlikely that the targets can be met, the increased risk of error and its potential cost be pointed out.

(v) The Public Service Board assist departments to adopt sound practices and to achieve high quality systems by:

a. accelerating its preparation and expanding the degree of detail of ADP information guideline manuals;

b. ensuring that these manuals are kept up to date and that they conform with the best of evolving ADP practice;

c. ensuring that Departments understand the importance of maintaining rigorous standards of quality in all aspects of system development; and

d. ensuring that priority is given to establishing positions to carry out system validations, system performance review and audit.

(vi) The Department of Health and the Public Service Board jointly review the staffing requirements of the Department's ADP Branch against its present and prospective workload. The results of this review are to be advised to the PAC in 1981.

(vii) The Department of Health and the Public Service Board jointly review the classification and staffing of the Department's ADP audit capacity against its present and prospective workload. The results of this review are to be advised to the PAC in 1981.

CHAPTER 6

RECOVERABILITY OF EXCESS PAYMENTS

6.1 Both the Commonwealth Government and the Pharmacy Guild Of Australia (the Guild) contend that the excess payments are not recoverable. The Public Accounts Committee (PAC) examined these claims, and in this chapter reports on how the issues of excess payments were handled by both sides.

6.2 The origins, timing and amounts of the various excess payments were described in the previous chapter. The question of recoverability follows a different time frame which is outlined in this mainly narrative chapter.

Emergence of Overpayment Issues

6.3 The matter of possible overpayments in despensing fees and the question of overpayment was first raised in the Joint Committee on Pharmaceutical Benefits Pricing Arrangements (the Joint Committee) in February 1978. The discussion at that time was in the context of the periodical updating of dispensing fees between surveys, and not in the context of the results of the surveys from which, it later turned out, most of the excess payments arose.

6.4 The revised Joint Committee was formed in early 1977. One of its first tasks was to determine a formula for updating dispensing fees between surveys. Characteristically, it could not agree and, after considering a substantial number of options and discussing these with both parties the Chairman recommended that a particular formula be adopted. The formula which was adopted - D2 as it was known to the Joint Committee - was based on 6 months' actual and 6 months' forecast information. Under such a system of updating using prospective indices there is always the possibility of overpayments if the forecast indices are higher than actual outcomes.

6.5 Between April 1977 and September 1978 there were six adjustments to the dispensing fees, determined by the Chairman using this "fore and aft" formula.

6.6 During this time the Joint Committee and its Subcommittee were settling the detailed specifications for the 1977/78 Survey, which was intended to establish a new dispensing fee base. At the same time the Guild submitted an ambit claim for adjusting the fees, by up to 60-65 cents per prescription. The Government side's first response was to suggest that there be no further adjustments to fees because of the imminent completion of the 1977-78 Survey which, at that time, was expected in March 1979. When that argument appeared to be unlikely to succeed, the Government side, at the November 1977 meeting of the Joint Committee, presented a

paper which reworked the data used by the Guild to show that, in theory at least, chemists could well have been overpaid by 23 cents per prescription.

6.7 There was no suggestion at this time that an overpayment had occurred. Rather, in the context of an ambit claim, the Guild was seeking an increase in fees and the Government side was arguing against it by demonstrating that an alternative interpretation of the figures was possible. That was the clear view held by the Guild:

> "... We saw that as a negotiating ploy. We had no understanding at that time that there might have been an error. In fact, I think it is fair to say ... that we felt that really only related to the updating procedure; their views were related to the updating procedure and not to any error that they may have anticipated".

6.8 At the May 1977 meeting of the Joint Committee the Chairman ruled that, while the two sides could not agree on the issues relating to redetermination of the base, nothing material had been put before him preventing the orderly application of the agreed updating procedure, and he then determined a further adjustment to fees by updating. This suggests that while the validity of the old 1972-73 base may, by the passage of time, have been in doubt, the updating procedure and formula was not considered by the impartial Chairman to be at issue.

6.9 By September 1978 the situation had begun to change. By now the Random Activity Sample (RAS) results were available and, as recorded in the Joint Committee Minutes "Actual results of the RAS analysis showed that dispensing time per prescription was down by 16 percent for qualified staff and 32 percent for unqualified staff ... compared to the 1972-73 Enquiry". From this point the Government side opposed any further increases arising from updating using the argument that the base level could be incorrect and that, should that be confirmed by the total results of the 1977-78 Survey, a substantial overpayment seemed likely to have occurred. At this stage, while an overpayment seemed possible, there was no suggestion of any errors having been made.

6.10 Notwithstanding the indication of a possible overpayment the Guild continued to press for dispensing fee increases based on the updating adjustments to which it considered it was entitled. It was in this context that the question of recovery arose. At the September 1978 meeting of the Joint Committee the Government side urged caution in applying the updating formula to a base that could be excessive. Noting that payments in respect of fee adjustments had

always been made promptly by the Commonwealth Government, the Government side sought "assurances from the Guild that the money would be repaid by chemists within a similar time frame as *would apply to* Commonwealth payments to chemists in a similar situation".

6.11 The Chairman of the Joint Committee asked the Guild what its position was in regard to overpayment if, contrary to their strongly held view, the inquiry results demonstrated an overpayment situation. The Guild responded that it did not have a policy and that this was a matter which would have to be put before the Guild's National Council. The Chairman observed that he had assumed in all of the Joint Committee's deliberations that the Guild's insistence that the updating formula should be applied was accompanied by an understanding that members of the Guild may have to "face up to an accounting if their very confident assumptions about the results of the Inquiry did not materialise". At the conclusion of that meeting the Chairman issued a statement and a press release which were given some prominence in both major pharmacy trade journals. A copy of the Chairman's statement is attached as Appendix 6. It highlights the Chairman's view that *the Guild's National Council should* present to the Joint Committee its views on overpayments and recoverability.

Recoverability : Political and Legal Moves

6.12 Apparently this view was not shared by the Guild. According to the October 1978 issue of Pharmacy Trade the Guild, the day after the Joint Committee meeting, directed its comments instead to the Minister for Health.

6.13 As reported in the Pharmacy Trade article the Guild asked the Minister for Health to state his policy on the method of repayment that the Commonwealth Government would seek if the Inquiry results indicated an overpayment. This related to the request made by the Government side on the Joint Committee that overpayments should be repaid promptly as lump sum payments. The Guild's view was that overpayments should be recovered by retrospective downwards adjustments so that chemists would receive a lower dispensing fee. The Guild told the Minister that:

> "The proposition of the government representatives could have drastic economic and political *implications and consequently I seek your urgent* assurance that your government would not contemplate such an action".

6.14 The Minister's reply of 22 September 1978, as reported in Pharmacy Trade pointed to the original aim of taking the determination of dispensing fees out of the political arena, reminded the Guild that the power of

determination rested with the Chairman of the Joint Committee, and suggested that the Guild should adequately inform chemists as soon as possible about the implications in the event of an overpayment being confirmed so as to minimise individual hardship for chemists.

6.15 This was hardly comforting news to the Guild, and the article went on to outline the further arguments that would be put to the Minister:

"....
- The Judge's responsibility was to determine fees to be paid to chemists.
- The method of payment was not a matter for him to determine as Chairman of the Joint Committee.
- It appeared to the Guild the Minister had been inaccurately advised by his Department.
- The Minister would eventually be faced with the decision on the mechanics of repayment in the 'hypothetical case'.
- If departmental officers were permitted to raise 'hypothetical situations' as a means of attempting to prevent payments for work already done, then the Minister should be prepared to state government policy in respect of those hypothetical situations.
- If he was unable to do so, he should instruct his officers to cease pursuing hypothetical arguments that could disrupt and confuse the operations of the Joint Committee, the Guild, and chemists throughout Australia...".

Despite some apparent internal contradictions in the major points of the Guild's publicly announced strategy of response, subsequent events were to confirm the accuracy of the Guild's viewpoint.

6.16 As well as this exchange of correspondence, there was a further development prior to the next meeting of the Joint Committee. In December 1978 the Guild sought a legal opinion on the issues then before the Joint Committee. When it became aware of this step, the Department of Health also obtained a legal opinion from the Commonwealth Crown Solicitor. At the suggestion of the Chairman of the Joint Committee, discussions on the question of recoverability continued at Subcommittee level. The minutes of that body record that following discussions the two sides exchanged their respective legal opinions.

6.17 Those legal opinions, together with one obtained independently by the Public Accounts Committee, are presented in Appendices 8,9 and 10. On the major points at issue they are all in accord. In brief, both the Government side and the Guild were advised that:

- The Chairman could make a determination to apply retroactively, which would replace a determination he had made previously, and which would lower the amount prescribed in the earlier determination;

- Where payments are made under a valid determination, any excess of payments over those due under a later retrospective determination is not recoverable or repayable;

- The Chairman does not have the power to give directions on such matters as the method of payment of amounts due, and the time within which payments are to be made. Actual processes of payment are not brought within his responsibilities;

- Agreement between the parties on the Joint Committee to acts contrary to the above three points would be of no binding effect; and

- There is no provision in the legislation for the making of a determination upon an interim or provisional basis.

6.18 The key point of the matter was, to quote from the opinion received by the Guild:

> "... *If a payment is properly made at the time of* payment, i.e. if it is made at the rate determined at the time and is in respect of goods and services actually supplied, ... a pharmaceutical chemist will be entitled to retain it against the Commonwealth".

The PAC's legal advice went further and stated:

> "... If a determination is not properly made for the purpose for which it was given but beyond the scope or not justified by the instrument creating the power, then the exercise of the power, as a result of taking some ulterior motive into consideration, renders it invalid .... 98B clearly envisages a determination to be made based on a consideration of cost plus profit. It follows that any determination which took into consideration the fact that chemists had been paid too much in the past would be clearly beyond power and could be successfully attacked".

6.19 That was the situation by March 1979, when the Joint Committee reconvened. The Chairman recapitulated the history of the overpayment issues and clarified the views of both sides. The last updating of dispensing fees had been in September 1978 and the Guild put the view that its application for further updating should be determined because cost increases had occurred. The Government side urged caution in the face of its concern that an overpayment situation was emerging from the results of the 1977-78 Survey, and that "there was no possible legally enforceable recovery of overpayments". The Chairman said that he did not propose to apply the updating formula on this occasion but would reconvene the Joint Committee shortly to consider the question further.

6.20 Shortly after that Joint Committee meeting, the Director-General of Health briefed his Minister on the emerging problems and obtained his consent for the Government side to oppose any further increases based on updating because of the possibility of further overpayments being made which could not be recovered legally. This consent was given after the Minister had consulted with his senior colleagues; and at the next meeting of the Joint Committee - in April 1979 - the Government side withdrew from the updating agreement.

6.21 In the face of the impasse on the updating of dispensing fees all attention was directed to completing the 1977-78 Survey and by December 1979 the definite existence of an overpayment situation had been established. However - and this is the important point - the attitude of both the Government side and the Guild regarding overpayments had been established, in the context of a dispute over updating, at least nine months before any overpayment was proved to exist. Both sides had been advised that overpayments were not recoverable; indeed it was that advice which led the Government side, in March 1979, to withdraw from any further updating arrangements pending the outcome of the 1977-78 Survey.

6.22 Thus, with the avenue of repayments having been closed off, the question of what to do in the face of the excess payments became paramount. After the overpayment situation became known in December 1979 the Joint Committee did not meet until February 1980. At that meeting it considered a letter from the Guild formally requesting that no determination be made altering chemists' remuneration until the Guild placed further information before the Chairman, and this was agreed to. At the next meeting of the Joint Committee, on 10 March 1980, the Guild tabled a long document stating their preliminary views on the outcome of the 1977-78 Inquiry. In summary the Guild stated that the results were defective and did not constitute a reliable basis on which to determine chemists remuneration.

6.23 The final act occurred at the next meeting on 9 April 1980 when the Chairman was presented with a unanimous recommendation by both sides and requested to determine accordingly. By the terms of Section 98B(5) of the National Health Act:

> "Where -
> (a)...
> (b) The members, excluding the Chairman, of the Joint Committee make a unanimous recommendation to the Chairman in respect of that matter, the determination or report by the Chairman of the Joint Committee in respect of that matter shall be in accordance with that recommendation". (emphasis added)

The Chairman, after clarifying the details of this proposal, noted that he was bound under the terms of the Act to make a determination and accordingly did so. The press release which was approved by the Joint Committee to announce the determination and the six point package, is reproduced at Appendix 10.

6.24 The contents and source of the six point package are described at Chapter 3. What is significant for the purposes of this chapter is that the determination was validly made, that it did not effect a recovery of overpayments, that it brought to a conclusion the uncertainties which had existed since September 1978 when the last adjustment to fees was made and when overpayments were at issue, and that it provided an outcome to the 1977-78 Inquiry.

Attitudes Regarding the Overpayment

6.25 In his Ministerial Statement of 2 April 1980 in the House of Representatives the Minister for Health was careful to describe the overpayments as 'excess payments', and he explained why that description was used:

> "I should stress at the outset that these sums of money are not overpayments which are recoverable at law. Amounts determined by the Minister prior to January 1977 and by the Chairman of the Joint Committee since then have been legally made. This has been confirmed by advice from the Attorney-General's Department. The Government and the body representing chemists - the Pharmacy Guild of Australia - have also received separate legal advice that these 'excess payments' cannot be recovered ... These 'excess payments' figures can therefore be seen to be notional only".

6.26 All the major witnesses were asked by the PAC to indicate their views on the excess payments and on the possibility and justice of seeking their recovery.

6.27 The Department of Health was asked whether chemists would have known of the overpayments and in its Submission replied:

> "Pharmacists receiving payment for supplying pharmaceuticals would not have been aware of the 'excess' payment. They received part of their reimbursement via the patient contribution, which they collected, and the balance from the Government on a monthly basis after they had submitted their prescriptions for processing by the Department of Health computer. Most pharmacists do not dissect the cost of operating their dispensary as opposed to the retail side of their business, nor did they have access to the confidential information from the 1972-73 Inquiry which would have enabled them to do so. They would not, therefore, have been in a position to make any objective comparison between their actual costs and the basis on which their fee had been calculated".

6.28 The Director-General of Health in his evidence on 25 June 1980 stated:

> "It is my absolutely honest belief that no pharmacist would have suspected that he was being overpaid".

Earlier that day, in replying to a question, he said:

> "You have used the term 'overpayment'. We used to, but the legal advice is that there has been no overpayment. The payments have all been made legally, under determinations either by the Minister or the statutory authority, which is why we are careful to refer to excess payments rather than overpayment".

6.29 The Guild provided a similar explanation, and then went further than the Department of Health and pointed out:

> "The basic fact is that what has not been established, and cannot be established, is the level of remuneration that would have been determined had the error not occurred. Without establishing this level the existence of "excess payments" can only be speculative".

6.30 In his evidence on 26 June 1980 the National President of the Guild explained that:

> "All of the Guild's thinking and its application to the new inquiry was on the basis that the 1972-73 inquiry was valid and had produced an acceptable result".

6.31 The Department of Veterans' Affairs, the Friendly Societies' Pharmacies Association of Australia and Washington H. Soul Pattinson and Co. Ltd. also testified that their organisations were unaware of overpayments. The last two organisations also stated that if there had been overpayments they had been undetectable to 'lay' recipients.

6.32 The Minister for Health in his statement of 2 April 1980 referred to the investigation of the excess payments which had been carried out by a Public Service Board Team, at the direction of the Commonwealth Government, before the matter was referred to the PAC. The Public Service Board Team also reported that recovery of the past excess payments appeared unlikely and went on to suggest that future excess payments be made recoverable by adopting new arrangements between the Commonwealth Government and individual chemists.

Conclusions

6.33 In view of the legal opinions concerning the possibility of recovering any of the excess payments, and the Commonwealth Government's acceptance of that advice, the PAC does not propose to make any recommendations on the recoverability of past excess payments.

6.34 As to the magnitude of the excess payments, the question arises whether their extent could have been reduced by earlier action by the Department of Health or by the Commonwealth Government. The PAC notes that preliminary evidence of overpayment became available in September 1978, and that after this date there was no further increase in fees. The PAC is not aware of any actions which the Department of Health took which unnecessarily prolonged the duration of excess payments.

6.35 The question arises whether arrangements should be made so that any future overpayments, if these arise, can be recovered. The Minister for Health has indicated that this was one of the suggestions of the Public Service Board Team.

6.36 The PAC doubts that this suggestion can be given effect. First, legal advice indicates that dispensing fees paid under valid determinations cannot be recovered. Any attempt to bypass this advice by seeking, and then enforcing the application of a separate legal agreement with every chemist in Australia may in practice not succeed. Moreover, it is an extremely cumbersome proposal which should, if possible, be avoided. Second, such an arrangement, even if it were capable of achievement, would be contrary to accepted custom, and could lead to severe ill-will between chemists and the Commonwealth Government. Third, if this extreme step were considered necessary it would constitute a prima facie admission that the Department of Health was unable to (ADP) process its various health sector inquiries and payments without error.

Recommendation

The Commonwealth Government announce that it will take no steps to introduce the suggested proposal of the Report of the Public Service Board Team (Pharmaceutical Benefits Scheme - Chemist's Remuneration) regarding arrangements with individual chemists binding them to repayment of future possible overpayments.

CHAPTER 7

THE INTERIM BASIS FOR REMUNERATION OF CHEMISTS

7.1 Chapter 2 of this Report summarised the extended negotiations between the Commonwealth Government and the Pharmacy Guild of Australia (the Guild) which commenced in 1960 and were still proceeding in 1976 regarding the details and the principles on which chemists were to have their base level of remuneration established. During that period six attempts were made - mostly by the Guild - to establish such a base. These included two separate surveys, the first conducted by consultants and the second conducted by the Joint Committee on Pharmaecutical Benefits Pricing Arrangements (the Joint Committee). None of those attempts produced an agreed basis for remuneration, and that period ended inconclusively with a commitment by the Commonwealth Government to yet another survey.

7.2 As discussed in Chapter 2, the remuneration of approved chemists, hospitals and medical practitioners is made on the following basis:

- a refund of the wholesale cost of ingredients;
- allowance of a markup on wholesale cost (25 percent for ready prepared benefits, 33 percent for extemporaneously prepared benefits);
- a dispensing fee;
- a container allowance where applicable;
- a dangerous drug fee where applicable;
- an isolated pharmacy allowance where applicable; and
- a miscellaneous allowance in respect of wastage and freight costs.

7.3 Chapter 3 of this Report described the latest survey in some detail in order to illustrate its complexity and the many points of disagreement which had to be resolved by the independent Chairman of the Joint Committee. One byproduct of this was the very long time it took, more than three years from the time it was agreed that a survey should be conducted for the survey results to be known.

7.4 With the exception of the very first Government /Guild established base in 1960, which was almost immediately abrogated, all subsequent attempts to establish a base for the dispensing fee have been on a cost of production model.

Use of this approach continued despite acknowledged problems of allocating common costs in a mixed business (dispensing and retailing). Allocating such costs is always an exercise of judgements. The National President of the Guild told the Public Accounts Committee (the PAC) that this was an attempt to "know the unknowable". In evidence to the PAC the Director of the Bureau of Agricultural Economics indicated that, where possible, the Bureau had moved away from the use of cost of production models.

7.5 While the cost of production model may have defects, the Commonwealth Government and the Guild have relied on it extensively ever since it was introduced as a methodology for establishing a basis for determining the dispensing fee. Based on the evidence presented to the PAC it would appear that both sides of the Joint Committee were more interested in the outcome of the exercise (that is, whether it resulted in an increase in fees) than establishing a technically factual base.

7.6 In their submissions to the PAC the Department of Health and the Joint Committee provided evidence of very significant changes which were made to the parameters and variables used in the 1977-78 Survey of Pharmacy Earnings, Costs and Profits. Not a single one of these changes was supported by the suggestion that they represented an improvement in the actual methodology, or a refinement of the statistics. Nor did the Guild, in its evidence, seek to provide any equivalent justification for the variations that it had sought or succeeded in having applied.

7.7 The PAC has no evidence which indicates that the 1977-78 Survey methodology has any technical validity in the sense that it unequivocally points to a certain base level of remuneration. All the evidence is to the contrary. The Guild has totally repudiated the Survey's findings on the basis that they do not accord with reality. The PAC is greatly concerned at a situation whereby two successive surveys, each costing the taxpayer about $1 million has led to such inconclusive results. The PAC has come to the conclusion that the Guild and the Government side were more concerned with ensuring a desired end result. This is in no way a criticism of the Guild or the Government side, but it is a strong criticism of the assumption that the 1977-78 Survey was soundly technically based in either theory or reality. It is with that conclusion in mind that the PAC examined the details of the six-point package which the Guild negotiated directly with the Government and which was ratified under the terms of the National Health Act on 9 April 1980.

The Six Point Package

7.8 In its evidence to the PAC the Guild confirmed that *no agreed basis for remuneration presently exists.* It advised that the present rate for dispensing was $1.31 per PBS prescription, and that this rate, in its view, was merely interim. Moreover, the Guild's understanding is that the level of dispensing fee is adjustable only upwards. The PAC regards this understanding of the current agreement as extremely significant. It could place a severe constraint on any suggestion of objectivity in acquiring results in the short term and indicates that other criteria are regarded as more important.

7.9 Second, the PAC examined the preliminary results available *from the four consultants selected by the Joint* Committee to develop alternative methodologies to the present cost of production model. While some of the consultants made specific proposals concerning future methods of establishing facts the PAC has not examined these with a view to testing their technical validity.

7.10 In the light of the long history of unsatisfactory results the PAC noted that none of the consultants appeared to have been fully briefed as to what was expected of them; and this point was specifically referred to by two of the consultants.

7.11 The submission by Ferris Norton Associates Pty Ltd to the Joint Committee states:

> "1.4 Terms of Reference
>
> *We understand that the terms of reference are to produce* ... a detailed proposal for alternative methodologies (or a single preferred alternative) for assessing the future level of pharmacists' remuneration...".
>
> (Emphasis added)

The submission by Price Waterhouse Associates Pty Ltd stated:

> "3. A REVIEW OF THE OBJECTIVES
>
> ...On the basis of all the information made available to us, and on our researches we have formulated the following estimation of the respective requirements of the Department <of Health> and the Pharmacy Guild...".
>
> (Emphasis added)

7.12 In the light of the uncertainty expressed by the two consultants who specifically attempted to state their understanding of what were the terms of reference, the PAC wrote to the Joint Committee requesting details of the terms of reference issued to consultants. The reply to that request confirmed the PAC's original view that no adequate and agreed terms of reference existed. This is particularly worrying as the Guild and the Commonwealth Government have such a long record of disagreement over methods of determining chemists remuneration. The PAC considers that this absence of adequate specifications portends the failure of the effort.

7.13 The third aspect of the Joint Committee agreement relates specifically to the proposed use of consultants. The 1970 *Senate Select* Committee on Medical and Hospital Costs took detailed evidence both from the Guild and the Department of Health on the 1964-65 survey which had proved abortive. As noted in Chapter 2 the 1964-65 Survey was conducted by a consultant who was proposed by the Guild. Yet when the survey results were available they were rejected by the Guild as unrealistic. The Guild's next proposal to use consultants - in 1970 - was not supported by the Commonwealth Government. From this the PAC concludes that the use of external consultants is not in itself any guarantee of greater success in establishing a basis for remuneration.

7.14 The use of consultants can have the disadvantage that, as well as being costly, the actual experience of conducting surveys, determining the parameters and processing the data is lost to the Department of Health. This was one of the explanations given by the Department of Health for its failure to process correctly the 1972-73 Survey, which contained the ADP error. The Department of Health stated that *as well as being inexperienced in ADP at that time it* was inexperienced in processing survey data because the previous survey had been conducted by consultants. The PAC finds it strange that, fifteen years later, the lessons of the 1964-65 Survey appear to have been put aside.

7.15 The fourth aspect of the six point package relates to the timetable of that exercise. Chemists have not received any increases to their dispensing fees since September 1978. After that date fears of an overpayment situation by the Government side of the Joint Committee prevented adjustments being made. In April 1980, following the finalisation of the 1977-78 Survey results, the Chairman of the Joint Committee determined that that the dispensing fee be reduced by four cents per prescription. The terms of the six-point package provided for a determination of fees to be made with a date of effect no later than 1 July 1981.

7.16 In other words, the situation pharmacists are currently facing is that:

- they have recieved no increases since 1978;
- they have accepted a decrease in fees of four cents; and
- while the terms of the agreement guarantee a fee determination with effect from 1 July 1981 it could take the Joint Committee considerably longer than this date to finalise its current inquiries.

7.17 The PAC notes that, historically, Joint Committee supervised surveys of the retail pharmacy sector have taken about three years from conception to completion. This was due to three basic factors. First the physical time to obtain and process the date, second the inability of Joint Committee members to agree on the use of various parameters and third, the cost of production methodology actually used. Other, perhaps more arbitrary methods of establishing fees can be much more rapid. For example, the updating techniques adopted by the Joint Committee for adjusting fees and the recent review of scheduled medical benefit fees, the latter taking only about three months to complete.

Conclusions

7.18 The PAC notes that the six point package represents an agreement between the Commonwealth Government and the Guild concerning the future basis of remuneration. In this and the three succeeding chapters, the PAC will be recommending an alternative way of achieving the philosophy of the six point package. In the PAC's opinion, this alternative way would achieve the aims of the 6 point package in a more open and constructive manner and with a much greater likelihood of success.

7.19 It would have the added effect of creating a more stable and orderly environment in which the Government and chemists could confidently proceed to creating an efficient and viable pharmacy industry.

7.20 As an interim solution, and until the recommendations made in the following chapters can be given effect, the PAC is of the view that provision may need to be made for the adjustment of fees.

Recommendations

(i) The dispensing fee of $1.31 agreed between the Guild and the Commonwealth Government, and ratified by the Chairman of the Joint Committee on Pharmaceutical Benefits Pricing Arrangements by his determination of 9 April 1980, be used as the only base for any adjustment of the dispensing fee. No adjustment be made to other components of chemists' remuneration.

(ii) Any request for updating the dispensing fee be referred to, and determined by, the recommended Health Fees Tribunal. (see Chapter 8)

(iii) As an interim measure, and until the recommended public inquiry is completed into the structure and remuneration of the retail pharmacy industry (see Chapter 10), findings of the Joint Committee's current methodological review be available to parties appearing before the recommended Health Fees Tribunal.

CHAPTER 8

A HEALTH FEES TRIBUNAL

8.1 In the previous chapter the Public Accounts Committee (the PAC) recommended an interim basis for the remuneration paid to chemists. This chapter examines and recommends on the administrative procedures by which remuneration would be adjusted in future.

The Joint Committee on Pharmaceutical Benefits Pricing Arrangements

8.2 As noted in Chapter 2 there were no variations made to dispensing fees between 1961 and 1970. Variations to dispensing fees granted between 1970 and 1976 were made by the Minister for Health acting on the advice of the Chairman of the Joint Committee on Pharamceutical Benefits Pricing Arrangements (the Joint Committee).

8.3 These arrangments were altered by amendments to the National Health Act in 1976, and the Chairman of the reconstituted Joint Committee was given the authority to determine the level of remuneration, and to update this periodically.

8.4 In his Second Reading Speech of 18 November 1976 the Minister for Health said that:

> "The purpose of this Bill is to give effect to a decision of the Government which will remove from the political arena the important question of the fees to be paid to pharmacists for the supply of pharmaceutical benefits to members of the public. This Bill will bring to an end the acrimony that has developed over the years between the pharmacists and successive Governments. This will be to the lasting advantage of the smooth administration of the pharmaceutical benefits scheme".

As indicated in this Report, events have shown that these aims have not been achieved.

8.5 Under the provisions of Section 98A of the National Health Act the current Joint Committee consists of nine part-time members comprising the Chairman (who must be a Deputy President of the Conciliation and Arbitration Commission) four members nominated by the Pharmacy Guild of Australia (the Guild) and four members of the Australian Public Service. At the present time the Government side representation is two officers of the Department of Health, one from the Department of Finance and one from the Department of Industry and Commerce.

8.6 The Chairman's power to determine chemists' remuneration is qualified by the statutory requirement that the Joint Committee first consider the matter upon which the determination is made; by requiring a determination to conform to a unanimous recommendation of the Joint Committee; and by directing the Chairman to have regard to deliberations of the Joint Committee. The Chairman's determination is binding on both the Guild and the Commonwealth Government.

Operation of the Joint Committee

8.7 The Joint Committee operates for many of its purposes as a forum in which the Government side and the Guild pursue their respective aims of economy on the one hand and greater remuneration for chemists on the other. In many respects it is therefore comparable with an industrial tribunal in which a conciliation process under a Chairman is undertaken and where, if the conciliation process fails, arbitration becomes necessary in order that the issues be resolved.

8.8 The PAC received evidence from the Director-General of Health that changes in approach to the operation of the Joint Committee have been apparent since it was reconstituted in 1976. In his introductory statement to the PAC the Director-General advised:

> "From my view, which is the broad rather than the detailed, I have seen some major changes. There have, of course, also been detailed ones. Prior to the arrangements concluded with the Guild in October 1976, the Chairman was, and had to be a conciliator. Whilst following broad policy, the departmental representatives were freer to take their own stance as in the end the final arbiter was the Minister, or the Minister and the Government. Whilst Sir Walter Scott was a conciliator, he could disagree with the departmental representatives, the Guild or both. But then the Government - the Minister - could reject that advice or advices and the Department was free to brief the Minister as it thought proper. Since the agreement, the statutory authority, the judge, is both conciliator and arbitrator. This has

resulted in my view, as procedures have been worked out, in much more emphasis on the arbitration aspect. It has also entailed much closer Ministerial involvement - certainly in my Department, and, I assume, in the other two departments involved - in the lines to be pursued by the Government representatives. It has resulted in both sides - Government representatives and Guild - taking up the more extreme positions and leaving it to the arbitrator to decide."

8.9 Members of the Joint Committee representing the Department of Health and the Guild also stated that current procedures have tended to polarise views on both sides and that a more adversarial situation has developed. An example of this situation was evident during the 1977-78 Survey of Pharmacy Earnings, Cost and Profits when, because of the complexity of the methodology used it was necessary for nine matters to be submitted to the Chairman for arbitration (see Chapter 3).

Departmental Representation on the Joint Committee

8.10 The PAC is not convinced that any benefit has been gained through the representation of the Department of Finance and the Department of Industry and Commerce on the Joint Committee. Both Departments claimed that their membership ensures that departmental representatives are aware of relevant Government policies when matters before the Joint Committee are being considered. However, neither Department has representation on the Subcommittee which operates on the day to day issues of the Joint Committee and neither Department made a contribution to the design planning for the 1977-78 survey. The Department of Industry and Commerce indicated that it had not made any detailed analysis of alternative methods of setting dispensing fees, despite that Department's acknowledged responsibility for small business, nor had it investigated the problems facing particular sectors of the pharmacy industry experiencing financial difficulties.

Access to the Determination Process

8.11 As previously indicated, membership of the Joint Committee is restricted to a Chairman, four members nominated by the Guild and four officers of the Australian Public Service. Meetings of the Joint Committee and its Subcommittees are held in private and the minutes of meetings are not made available to the public. Information derived from the Joint Committee's surveys of earnings, costs and profits, is treated as confidential.

8.12 While the Guild represents the majority (approximately 90 per cent) of pharmacies in Australia, evidence was received from a number of other interested organisations of the desire to participate in the remuneration setting process and to have access to the information upon which decisions are reached.

8.13 The Friendly Societies' Pharmacy Association of Australia indicated that while it represents only a small number of pharmacies throughout Australia, it does have some significant numbers in Queensland, Western Australia and particularly South Australia where its 32 pharmacies account for about 10 per cent of prescriptions dispensed. The Friendly Societies claimed that dispensaries operated by its members in Ipswich, Ballarat and Adelaide would be among the larger dispensing pharmacies in Australia.

8.14 The Friendly Societies considered that there would be advantages in having access to the fee setting body. It stated that it was promised a position on the Joint Committee by former Ministers for Health but this never transpired because of opposition by the Guild. Instead, a "Friendly Societies Departmental Committee on the National Health Scheme" was established. This meets irregularly to discuss a limited range of national health questions but, because of the secrecy involved in Joint Committee matters, these discussions do not extend to survey results or input, nor is the facility offered for the Friendly Societies to put information to the Joint Committee. The Friendly Societies submitted:

> "It would seem sensible that any future negotiating committee should be comprised of members representing the Pharmacy Guild of Australia together with others from interested pharmacy groups".

8.15 Washington H. Soul Pattinson and Co. Ltd. which operates 42 pharmacies and supplies its manufactured products to another 350 pharmacies throughout New South Wales, Victoria, Queensland and Western Australia, also indicated that it would be prepared to participate in a more open and simpler process of fee determination.

8.16 The Pharmaceutical Society of Australia (PSA) is a national professional society representing more than 8,500 pharmacists from all Australian States and Territories. In its submission to the PAC the Society stated:

> "The PSA does not have strong views as to whether the Joint Committee should continue to act as the regular review body, although we believe that PSA should have the right to present submissions on new methodology and methodology reviews to the body entrusted with responsibility for this activity. If the Joint Committee continues in this role some procedural changes will be necessary to allow PSA to appear in its own right from time to time".

8.17 The PSA also suggested that the Joint Committee was not the appropriate body to consider the development of a new methodology, as it had not demonstrated that it had the capacity to reach agreement on any fundamental changes, despite the obvious need to develop a system more appropriate to community needs. In addition, the PSA was concerned that the survey of methodology currently being undertaken by the Joint Committee would not be satisfactory because it was a closed review and its recommendations would not be subject to independent analysis by all interested parties. Furthermore this review was required to achieve results within a tight deadline as negotiated in the six point package.

8.18 The Australian Federation of Consumer Organizations (AFCO) submitted that the process for determining the level of chemists' remuneration should be open to the public and that minutes and other documents should be publicly available, unless there were overwhelming reasons for privacy. In its submission the AFCO indicated that:

> "It is further considered that the present 'closed shop' committee system should be replaced by an independent tribunal, headed possibly by a judge with experience of arbitration procedures and containing at least one representative of the consumer interest. Such a tribunal should be required to hold its hearings in public and to have the normal powers of being able to require people and organisations to attend and provide information".

8.19 The AFCO suggested that independent data and statistics could be better provided by a research body which would carry out the detailed ongoing research required for the setting of remuneration.

8.20 The Department of Veterans' Affairs stated that while it would not seek representation on the Joint Committee it would like the opportunity to make submissions when it felt that input was required. The Department also saw the desirability of having observer representation during the deliberations of the Joint Committee.

8.21 On the other hand the Guild reaffirmed its broad support for the present restricted membership of the Joint Committee. In the Guild's view this arrangement has the following advantages:

- it enables the use of confidential survey information in a way which would not be possible in an open forum;
- it enables detailed discussion between Guild and Government representatives at both the Subcommittee and Joint Committee level;
- where this discussion does not lead to agreement it enables the implementation of a conciliation function by the Chairman;
- where agreement cannot be reached, a decision can be taken by the Chairman acting as arbitrator; and
- there is scope for the Chairman to avail himself of independent advice if he so chooses.

8.22 The Guild agreed that there could well be advantages in having the Chairman assisted by deputies with expertise in areas such as accountancy and health economics. The conciliation function could be exercised by either the Chairman or a deputy, while collectively they could exercise the arbitral function.

Conclusions

8.23 The PAC does not support the exclusive relationship that has developed within the Joint Committee. There has been carried into the Joint Committee the longstanding adversarial relationship previously existing between the Guild and the Commonwealth Government. The Joint Committee environment descriibed above does not, in the PAC's view, meet the requirements for an impartial fee determination procedure. It has adopted habits of excessive secrecy and it is not accessible to alternative industry or public points of view. The PAC considers that the fee variation function of the Joint Committee would be more appropriately carried out in a new organisation with a suggested title of Health Fees Tribunal. This would require abolition of the Joint Committee and legislative changes to the National Health Act.

8.24 Such a Health Fees Tribunal is recommended for a number of reasons.

8.25 In the PAC's view such an arrangement would be more open and fair, and would be better structured to grant a hearing to all interested parties. Such a Tribunal would resolve the contradictions inherent in the Joint Committee system whereby it acts as both judge and jury in the same case. The "adversarial" method of procedure before a Tribunal has much to recommend it. The parties are recognised, correctly, as having different points of view. The evidence which is adduced by both sides is subject to stringent examination and attack, where necessary. This procedure has the merit that nothing is accepted on trust or faith.

8.26 Secondly, Commonwealth Government, through the Department of Health faces almost identical requirements to adjust remuneration not only for chemists, but also for doctors, optometrists and other providers of health services. Such remuneration is presently determined either in special forums, or by specific tribunals. The PAC considers that it would be more economical, administratively convenient and would enable the development of greater expertise if determination of medical and para medical remuneration all vested in a judicial organisation having a nexus with the Conciliation and Arbitration Commission.

8.27 Thirdly, the PAC notes the current discussions into a more uniform system of Federal/State industrial awards. Noting these discussions the recommendations for a Health Fees Tribunal leave the way open to, and provides a single institution for, the determination of remuneration for all medical and para medical services throughout Australia.

8.28 Fourthly, by legislatively vesting in the Health Fees Tribunal the exclusive power to determine chemists remuneration, the Commonwealth Government's stated objective of removing chemists remuneration from the political arena, can be achieved.

8.29 The PAC proposes that the Chairman of the Health Fees Tribunal be a Deputy President of the Conciliation and Arbitration Commission. Membership of the Tribunal could be representative of wider interests. It is not proposed to make a recommendation as to the number of members but in the view of the PAC, three would be appropriate.

8.30 The PAC considers that the independent Health Fees Tribunal should determine its own criteria for setting remuneration, but should be required to have regard to guidelines given to the Conciliation and Arbitration Commission. The PAC's intention in this respect is to ensure that remuneration determinations are not inconsistent with movements in other professional fees and wages received by other sectors. The PAC is aware of the arrangement that, by vesting control over such remuneration in an independent tribunal, the Parliament and the Government is giving up a power of economic control. The PAC rejects this contention. The Commonwealth Government has available to it other equally strong instruments for affecting the overall costs of the Pharmaceutical Benefits Scheme and Repatriation Pharmaceutical Benefits Scheme. These include its powers to

- control the price of pharmaceuticals;
- vary the patient contribution to the Pharmaceutical Benefits Schemes;
- affect the demand for prescription drugs e.g. by a program of education directed at consumers and prescribers;
- control the number and type of drugs on the NHS list;
- rationalise the availability of RPBS items;
- provide general guidelines to the Conciliation and Arbitration Commission, to which the Health Fees Tribunal is explicitly linked;
- provide specific guidelines to the Health Fees Tribunal; and
- legislate amendments to the enabling legislation establishing the Health Fees Tribunal.

8.31 The PAC considers that the proposed Health Fees Tribunal would be no more expensive than the current Joint Committee in terms of direct costs. If it made its determinations more expeditiously than the three years it has taken the two Joint Committees to reach their respective conclusions on survey inquiries, it should make considerable cost savings. As well, it would determine remuneration in other health related areas therefore facilitating savings as it acquires expertise, rather than continuing with a series of expensive, unrelated inquiries.

Recommendations

(i) Determination of chemists' remuneration be vested in an independent Health Fees Tribunal. This Health Fees Tribunal be operational within 12 months of the tabling of this report.

The Joint Committee on Pharmaceutical Benefits Pricing Arrangements be abolished concurrent with the establishment of the Health Fees Tribunal.

(ii) The Health Fees Tribunal:

a. consist of one or more members, the Chairman being a Deputy President of the Australian Conciliation and Arbitration Commission;

b. receive public submissions from all interested parties and conduct its hearings in public;

c. as far as possible conduct its hearings in a manner which encourages the making of determinations on questions of fact rather than on questions of law;

d. determine its own criteria for setting remuneration having regard to Commonwealth Government guidelines to the Conciliation and Arbitration Commission for the fixing of salaries and wages;

e. announce its criteria and reasons for its decisions when making determinations; and

f. determinations be legally binding on all parties; and

g. to the extent that it requires a staff, this be provided independently of the Department of Health.

CHAPTER 9

A BUREAU OF HEALTH ECONOMICS

9.1 One of the important features of health expenditure in Australia, which in 1979-80 cost about $9000 million has been the apparent lack of objective economic advice to aid the Commonwealth Government, through the Department of Health and other departments, in formulating health and social welfare policies. As a consequence, the Department of Health has undertaken its investigations in a diverse and unrelated manner, and with excessive compartmentalisation. As a result the arrangements adopted have been far from uniform and, to all appearances, have been of questionable standard from a methodological and economic viewpoint.

Expenditure of Health Services

9.2 Expenditure on the Australian health industry is large, and accounts for about 8 percent of the gross domestic product. It is the second largest functional component of Commonwealth Government expenditure. It is against this significant expenditure that the PAC has considered the question of the economic expertise available to the Department of Health.

Table 5 : Analysis of Health Expenditure: Australia : 1974-75 to 1978-79 ($ million)

	1974-75	1975-76	1976-77	1977-78	1978-79
Commonwealth Government	1159	2494	2526	2560	n.a.
Other Government	1196	1151	1318	1500	n.a.
Private	1483	1479	2081	2718	n.a.
Total	3838	5124	5925	6778	7950

n.a. not available

Source: Commonwealth Department of Health, Australian Health Expenditure 1974-75 to 1977-78 : an analysis, AGPS, June 1980; and Minister for Health, Press Release, 18/80, 19 March 1980.

9.3 As discussed in chapter 2, total expenditure on health services throughout Australia, in 1977-78, was about $6800 million, and has been estimated to be about $8000 million in 1978-79. As noted in Chapter 2, total expenditure on pharmaceutical services in 1977-78 was $644 million equivalent to about 10 percent of total health expenditure.

9.4 The PAC has considered the problems facing the pharmacy industry arising from the lack of expert economic advice.

Quality of Surveys

9.5 A major economic and accounting tool adopted by the Joint Committee on Pharmaceutical Benefits Pricing Arrangements (Joint Committee) and the pharmacy industry to determine the level of dispensing fee has been cost of production type surveys.

9.6 The Joint Committee conducted two major surveys into "Pharmacy Earnings, Costs and Profits", covering the 1972-73 and the 1977-78 fiscal years (see Chapters 2 and 3).

9.7 Had these surveys been conducted by a professional and independent group, the results could have been significantly different. This is because the parameters of the survey and the use of particular variables would have been determined solely on technical considerations.

9.8 As it eventuated, in the 1977-78 survey, the Commonwealth Government and the Pharmacy Guild of Australia (the Guild) were unable to reach agreement on the interpretation and use of many of the variables used within the survey. The Chairman of the Joint Committee was obliged to arbitrate and rule on each of these matters. Arbitrating on these technical matters resulted in the use of variables which could have been technically accurate only by accident. It may have led also to variables being excluded or included which, in other circumstances, should not have been considered. As a result, the surveys have been of questionable technical validity.

9.9 On the basis of submissions and evidence before it, the PAC was left in no doubt that the operating rule in the Joint Committee deliberations, which led to the specifications of the 1977-78 Survey, was for the Guild to seek inclusion of items which would yield chemists a higher rate of remuneration, and for the Government side to seek to exclude these, or to introduce variables which would reduce chemists' remuneration. Even while the 1977-78 Survey results were being processed, variations to parameters were proposed, arbitrated and introduced into the processin9.8g. This was one of the reasons why documentation standards were less than adequate and the survey took so long to finalise. An even more blatant example - which led to the issue of a

High Court writ by the Guild - was the Department of Health's successful persuasion of the Minister for Health to adopt the Relatively Economic Pharmacy Approach to the 1972-73 Survey results, well after they had been processed, and against the recommendations of the then Chairman of the Joint Committee.

9.10 The PAC considers that fact gathering needs to be kept distinct from subsequent negotiations about what is meant or implied by those facts. These two steps ought not to be contaminated by each other. Intermixing of these processes suggests either a contempt for the facts themselves, or a misunderstanding of the role of facts in advancing argument and understanding. In any case, such practices undermine the efforts of those whose business it is to provide sound factual analyses, and must be counted as a major cause of the frustration evident in many witnesses.

9.11 During this inquiry into the excess payments made under the Pharmaceutical Benefits Scheme and the Repatriation Pharmaceutical Benefits Scheme, the PAC received evidence that at least two other sectors of the health industry besides the pharmacy sector used surveys to aid in the determination of their fees. These two other sectors covered medical fees and optometrical fees, and were dealt with by different parts of the Department of Health. The PAC was struck by the apparently very different standards of methodological inquiry and quality of data which seemed to apply to determining the remuneration of different providers of health care.

9.12 In the medical sector of the health industry the Australian Medical Association (AMA) has been the principal source of data on costs and incomes of the medical profession. As part of the 1980 Inquiry on Medical Fees For Medical Benefit Purposes, the Minister for Health advised the Medical Fees Tribunal that the AMA:

> "... agreed to assist the inquiry by supplying to you (the Tribunal) and the Government on a confidential basis aggregated data for surveys conducted by the A.M.A. for the years 1976-77 and 1977-78 on which basic costs and income structure for the four groups of medical disciplines adopted by the Association at the 1979 enquiry were derived, and for the following six groups, if possible, for any available later period (pathology, radiology, general practitioners, consultant physicians including psychiatrists, surgeons and other specialists); including information on the ranges of incomes and costs included in the data and the number of practitioners in each class of incomes and costs, without breaching the confidentiality of individual returns...". (Commonwealth Government submission to the "1980 Inquiry on Medical Fees for Medical Benefit Purposes")

9.13 This survey by the AMA of the costs and incomes of certain medical disciplines was not made public nor was the data on which the survey was based subjected to scrutiny by an independent group of accountants and economists. The Australian Bureau of Statistics (ABS) considered, and was critical of, its statistical methodology. The PAC is concerned that the Department of Health was not in a position to objectively assess this survey, or to provide data of its own; especially given expected expenditure of $681 million on medical benefits in 1980-81. The PAC also noted that in respect to both data and methodology the Department of Health imposes harsher disciplines on the pharmacy sector.

9.14 The Australian Optometrical Association (AOA) recently (1980) applied for an increase in schedule fees on which benefits are based for optometrical consultation services. The Commonwealth Government requested that a survey be conducted of incomes and costs of the AOA's members for the Financial Year 1978-79 before any increase could be considered. The PAC notes the differences in approach by the Department of Health to the various surveys. The Pharmacy Surveys involve prolonged discussions and debate over minute detail; the AMA Survey is apparently accepted without question. In a letter to the PAC, the Department of Health stated, regarding the AOA survey:

> "The practice of optometry is usually a mixture of sales and consulting, and for many items of expense there is no clear-cut means of allocating commonly-incurred expenses to the two components. Notional allocations must be made, based on subjective judgements".

The PAC noted that the AOA survey was carried out by independent consultants, outside the Department of Health and that procedures and methodology followed were less tightly constructed than were those applying to the pharmacy Survey.

9.15 The PAC also noted that the remuneration of doctors and optometrists was capable of being adjusted more rapidly than was apparently possible for chemists.

Consultants

9.16 Because of the lack of expertise within the Department of Health for carrying out specific economic tasks it has been necessary to use consultants - whether employed by the Department of Health or by another group - to undertake the work.

9.17 The 1964-65 Survey into earnings, costs and profits, was conducted by Associated Industrial Consultants (Aust) Pty Ltd, under the supervision of the Joint Committee. However, the 1972-73 and the 1977-78 Surveys were conducted by the Joint Committee without the direct use of external consultants.

9.18 Following the rejection of the results of the 1977-78 Survey (see Chapters 2 and 8), the Joint Committee engaged three consultants, namely Deloitte Haskins and Sells, Ferris Norton Associates Pty., and Price Waterhouse Associates Pty. as well as the Industries Assistance Commission, to consider alternate methodologies for determining chemists' remuneration.

9.19 The survey into incomes and costs of Optometrists covering the 1978-79 financial year was conducted by the consultant Arthur Young and Co., on behalf of the AOA.

9.20 With the use of these diversified agencies to undertake these surveys, and with the Department of Health apparently lacking the expertise to critically evaluate and coordinate the undertakings, it is understandable why the standards, the methodology and the quality of the work varies.

9.21 Given a health industry with expenditure in 1979-80 estimated at about $9000 million the question confronting the PAC is, how administratively efficient is a system which allows and, in fact, does nothing to discourage such diverse and hence questionable, economic standards?

Australian Bureau of Statistics

9.22 Although the Department of Health has been unable itself to provide independent economic advice on survey results, the statistical methodology for pharmacy, medical and optometrical surveys has been scrutinised by the Australian Bureau of Statistics (ABS) and the Central Statistical Unit (CSU) of the Department of Health.

9.23 The ABS stated in evidence that it commented, when requested, on the methodology used in the pharmacy Surveys; but did not comment on the results themselves. The CSU, by comparison, had greater day-to-day liaison with the officers conducting the surveys as it was physically located in the Department of Health.

9.24 The ABS had reservations about the statistical methodology employed in the 1964-65 Survey but considered the 1972-73 and 1977-78 Surveys were adequate from a statistical methodological viewpoint.

9.25 When discussing its contributory role to the pharmacy Surveys, the ABS was critical that it was required to comment on questions when it did not know for what purpose the information was required. It stated:

"We ... have not been informed as to all the purposes for which the survey data were to be used or what was done with them. In fact we commented once that it was difficult to give proper advice on a survey design and methodology without having precise definition of the objectives of the survey".

9.26 Besides involvement with pharmacy Surveys, the ABS and/or CSU have scrutinised (in the case of the AMA survey) or contributed to the planning of surveys (optometrists). As a result they have improved the statistical methodology when appropriate, or criticised it if necessary (as they did with the AMA Survey on Medical Fees for Medical Benefit Purposes).

Conclusions

General

9.27 The PAC is concerned that the Department of Health and, as a consequence, the Commonwealth Government has been receiving inadequate objective advice on economic aspects of the health industry.

9.28 The Director-General of Health stated that there was no specific division or unit within the Department of Health which has provided specialised economic advice. However, there were personnel with economics qualifications within existing Divisions of the Department. The Director-General further stated that the Department had been seeking a health economist but to date the position had been unoccupied.

9.29 With total health expenditure throughout Australia of about $9000 million, the PAC considers that the Department of Health should be serviced by a specialised group of economists and other relevant disciplines, advising on economic matters associated with the health industry.

9.30 Much of the specialised work which should have been done by such a group appears to have gone undone, while much of that which has been done has been by consultants acting solely for the various interests.

9.31 A problem associated with the use of consultants, has been that it deprives Departmental officers of the necessary experience and expertise in understanding and conducting the work carried out by the consultant. The Minister for Health told the House of Representatives on 2 April 1980 that the use of consultants for the 1964-65 Survey:

"... meant that the Department did not obtain first-hand experience in the design and conduct of a major inquiry of this nature which could have been used in determining the arrangements made for the 1972-73 inquiry. What all this means is that we were able

to apply checks and balances to the 1977-78 inquiry - particularly in the development stages - which, with the benefit of hindsight, should have been applied to the 1972-73 inquiry".

9.32 The PAC considers that the long term consistency of standards in consultants' submissions is impossible to maintain, especially when they most probably do not see one anothers' surveys, and when the providers of the data impose strict rules of confidentiality.

9.33 The PAC believes that the pharmacy surveys intended to provide objective facts have been open to subjective influence. This has come about because both parties to the Joint Committee have negotiated the extent and usage of variables. When agreement has not been possible, they have sought the intervention of the Chairman of the Joint Committee, requiring him to arbitrate on technical interpretations. As a result, it is highly questionable whether the Surveys have provided a technically objective base for determining chemists' remuneration.

9.34 The PAC is also critical of the confidential status applied to the surveys conducted by the Joint Committee and others. It considers that, to maintain objectivity, surveys should be public documents open to scrutiny and discussion.

Economic Bureaus

9.35 To meet to the current deficiency of economic advice to the Department of Health, the PAC considers that a Bureau of Health Economics comprising a specialised group of economists and persons with complementary skills, should be established. This would obviate much of the need for the current dependence on external consultants to provide a semblance of technically objective advice.

9.36 In its submission to the PAC, the Australian Federation of Consumer Organizations (AFCO) stated, that given the problem of determining the level of chemists remuneration and the time involved in conducting surveys:

> "... points to the need for the establishment of an independent body to provide the necessary information and to carry out the detailed ongoing research into costs in the area which is required for the setting of reasonable remuneration ...".

Further, the AFCO stated:

> "If such a body was to be established it should deal not only with pharmaceuticals but also with the health area generally, as obviously both fields overlap and interact. The recent New South Wales

Prices Commission Inquiry into Medical Fees, for example, was hampered by the lack of detailed survey material, although smaller surveys were conducted by consumer organizations. However, in the sensitive area of fees and costs, little material was available and the surveys conducted by the New South Wales Branch of the Australian Medical Association were not done on a representative basis of doctors practicing in New South Wales".

9.37 The PAC considers that a Division or Branch within the Department of Health would not be the most appropriate organisation for such a Bureau, as it should be independent, and seen to be when providing objective advice. The Director-General of Health outlined to the PAC the problems he has experienced in attempting to recruit to the Department a health economist. The PAC recognises that the difficulty of attracting applicants may be due to their professional independence being at stake in a Departmental environment.

9.38 The PAC considers that the system of Economic Bureaus as they apply in some other Departments, should be applied to the Department of Health.

9.39 Currently there are four Economic Bureaus within the Commonwealth Government:

Bureau of Agricultural Economics (BAE);
Bureau of Transport Economics (BTE);
Bureau of Industry Economics (BIE); and
Bureau of Labour Market Research (BLMR).

9.40 The PAC notes that existing Economic Bureaus generally have the following characteristics:

- on technical matters they are independent of governmental and departmental influences;
- they are not responsible for day-to-day administrative matters, but are basically research oriented institutions;
- they can attract highly qualified staff because professional standards are maintained;
- they can carry out research over a wide range of topics; and
- survey and research results are generally published and freely available to all parties.

9.41 The PAC, in reaching its conclusion to recommend the establishment of a Bureau of Health Economics, was conscious of the cost of this recommendation. It notes, however, that the largest Bureau, the BAE, costs about $5 million per annum while the other Bureaus cost considerably less. If a Bureau of Health Economics was to cost say $2 million, this is equivalent to roughly 2 cents per PBS prescription. Given that it would cover other health and welfare sectors, and the total expenditure on health matters is about $9000 million, were the Bureau to achieve efficiency savings of one percent health care costs, this would equate to a saving of about $100 million.

9.42 In assessing the likely future cost of the Bureau it must be noted:

- that existing staff positions from the Department of Health could be allocated to this Bureau;
- the need for consultants will be reduced;
- the pharmacy Survey conducted in 1977-78 cost about $1 million, and this cost could be reduced by the introduction of a bureau; and
- the advice of such a specialist group could save considerable government and community monies over time.

9.43 The PAC considers that a Bureau of Health Economics would be of major benefit to government and the community. It would be an independent group of economists (along with other specialist staff) providing objective factual advice on all areas of the health industry. It could centralise and coordinate economic matters associated with the health industry and would provide consistent and objective criteria and standards.

9.44 Like other economic bureaus, it would be open in its approach and readily accessible to industry. It could conduct surveys for use in the determination of fees, it could devise techniques for collecting and analysing cost and income information, it could provide advice on fee determination techniques, it could provide assistance with research into social welfare matters, cost/benefit studies into the hospital sector, determine priorities for health expenditure and determine appropriate health insurance arrangements. In undertaking its function a Bureau of Health Economics would be subject to accepted constraints in handling confidential material. However, these constraints do not preclude the release of aggregated industry data such as the results of the various surveys it undertakes. Other economic bureaus successfully operate within accepted conventions when handling confidential material.

9.45 Like other economic bureaus, a Bureau of Health Economics could cover matters of concern both to the Commonwealth and State Governments, and possibly even Local Government. Such a broad approach would be to the ultimate benefit of the entire community.

9.46 In view of the likely initial problems which the Bureau of Health Economics might experience, the PAC considers it would be desirable for it to be assisted by an external independent committee. Such a committee could advise on liaison and cooperation with external health groups and organisations, on Commonwealth, State, and Local Government matters, and on research priorities.

9.47 The PAC believes that although positions in the Bureau of Health Economics should not be filled in haste, or with second rate staff, it is quite possible to form the Bureau within 12 months and begin to have a nucleus staff operational within two years.

<u>Recommendations</u>

(i) A Bureau of Health Economics be established to provide independent, objective and publically available analysis of economic facts and issues relating to the Australian health industry.

(ii) The Bureau of Health Economics to have a charter and powers similar to other Economic Bureaus.

(iii) The Commonwealth Government consider establishing an external independent committee to assist the Bureau of Health Economics.

(iv) The Bureau of Health Economics be formed within one year of the date of tabling of this report, and become operational within two years of the tabling of this report.

CHAPTER 10

RETAIL PHARMACY IN AUSTRALIA

10.1 In this chapter the Public Accounts Committee (PAC) considers some of the matters which affect the retail pharmacy industry, and comments on two issues requiring further detailed investigation.

Number of Pharmacies in Australia

10.2 During the 1960s the number of pharmacies increased steadily to reach a peak of 5,912 in 1971. Subsequently the number declined to about 5,400 in 1978, and has since remained at that level.

Table 6: Pharmaceutical Chemist Numbers* : Australia as at 30 June : 1960 to 1980

Year	No of Pharmacies	Population/ Pharmacy Ratio
1960	4696	2213
1964	5243	2151
1966	5501	2128
1968	5728	2120
1970	5876	2155
1971	5912	2211
1972	5891	2255
1974	5719	2397
1976	5504	2542
1978	5392	2643
1980	5417	2650(est)

Source: Department of Health, Annual Reports, various issues and Year Book Australia No. 63, 1979, Australian Bureau of Statistics, Canberra, N.D.

10.3 Despite these overall changes, the PAC could not obtain detailed data to probe the variations. The PAC wishes to record that it sought but was unable to obtain, a considerable amount of data which it expected the Departments of Health and Industry and Commerce might hold in a readily available form, given that over $650 million is spent annually on pharmaceuticals. For example, it could not substantiate claims made that there has been an increase in the number of larger pharmacies (i.e. pharmacies handling a large volume of Pharmaceutical Benefits Scheme (PBS) prescriptions); or that the overall figures mask a significantly

* Pharmaceutical Chemists dispensing pharmaceutical benefit prescriptions

larger number of pharmacy closures, new pharmacy openings, and amalgamations of neighbouring pharmacies. Nor could the PAC establish whether these changes have occurred mostly with respect to pharmacies of a certain size, in certain localities or States.

International Comparisons

10.4 Between 1960 and 1980 the population to pharmacy ratio in Australia has increased from 1:2213 to an estimated 1:2650. The USA, Germany and the United Kingdom, all of which have privately owned pharmacies similar to those in Australia, have equivalent ratios of one to between 4,000 and 5,000. Swedish pharmcies have, since 1970, all been State-owned, and the pharmacy to population ratio is 1:14,000 while in Denmark and Norway, the ratio is 1:12,000. A broader range of international comparisons is available based on the year 1974:

Table 7: World Comparisons of Population to Pharmacy Ratios: 1974

Under 4,000	4,000-7,999	8,000-11,999 (all c)	over 12,000
Australia S	Bulgaria C	Austria	Bahamas C
Belgium C R	Canada	Czechoslavakia	Botswana
France C R	U.K.	Finland	Denmark C
Gibraltar S	Hungary C	Israel	Hong Kong
Greece R	Ireland C	Jordan	Iran C
Ireland S	Italy C	Poland	Ivory Coast C
Malta R	Japan C	S. Africa	Kenya
Northern Ireland S	Lebanon C	Syria	Kuwait C
Spain C R	Luxembourg C		Mauritius
	Philippines		Netherlands C
	Portugal C		Norway
	Switzerland		Rumania C
	USA		Rwanda
	West Germany		Sri Lanka
			Sweden C
			Yugoslavia C

Notes: C - Distribution of pharmacies is controlled
R - Sale of medicines to the public is reserved entirely to pharmacies
S - Sale of some medicines is reserved to pharmacies; other medicines can be sold from other shops, the range of which may or may not be restricted.

Source: Derived from J.C. Bloomfield; The Global Scene in "Pharmacy in the 1980s, Proceedings of the Pharmacy Institute Conference 1928-1978, the Pharmacy Guild, Canberra 1978.

During the hearings the PAC discussed international comparisons with various witnesses. They all concurred that, on the basis of international comparisons, the pharmacy to population ratio in Australia was both high and likely to be unnecessarily so, even allowing for the need to provide reasonable pharmacy services in isolated and remote areas.

Factors Influencing the Number of Pharmacies

10.5 The number of pharmacies in Australia is determined by many factors. These include geographical considerations, the number of doctors prescribing prescriptions, patient expectations of drug usage, the number of prescriptions issued, the cost to the patient of a PBS prescription, pharmacist job opportunities and the salary for such positions, the expected return from operating a pharmacy and Commonwealth and State legislation governing the ownership and control of pharmacies. The returns received by pharmacies will be influenced by the remuneration received for dispensing PBS and Repatriation Pharmaceutical Benefits Scheme (RPBS) prescriptions.

10.6 For the 1977-78 Survey, the pharmacy industry was divided into eight strata, each stratum representing 12.5 percent of the total volume of prescriptions as at 1975-76. The lowest stratum comprised 27 percent of all pharmacies while the top stratum contained 4 percent of pharmacies. Half the prescription volume was dispensed by 70 per cent of the smaller pharmacies and the other half by the 30 per cent of larger pharmacies.

TABLE 8: Number of Pharmacies by Volume of Prescriptions 1975-76

Stratum Grouping	Volume of Prescriptions (percent)	Prescriptions Per Month	Number of Pharmacies
1	12.5	1-896	1431
2	12.5	897-1151	916
3	12.5	1152-1390	740
4	12.5	1391-1641	619
5	12.5	1642-1905	531
6	12.5	1906-2309	450
7	12.5	2310-2971	359
8	12.5	2972+	242
Total	100		5288

Source: Joint Committee on Pharmaceutical Benefits Pricing Arrangements.

10.7 All pharmacies throughout Australia (except for those in remote areas, which receive an additional isolation allowance) have received a common fee for dispensing PBS and RPBS prescriptions. This would have had a significant effect on the structure of the retail pharmacy industry. All pharmacies are remunerated on the basis of the average cost of dispensing a PBS prescription. Because large pharmacies (those handling a large number of prescriptions) have had lower average costs than pharmacies handling a smaller number of prescriptions, financial pressures have existed to encourage the growth of larger pharmacies while penalising smaller pharmacies.

10.8 The changes in the cost structure of pharmacies is exemplified by the data in Table 9 which indicates the average cost of dispensing a PBS prescription in 1977-78, declines as the size (as measured by the number of prescriptions handled) of the pharmacy increases.

Table 9 : Average Cost of Dispensing a PBS Prescription : 1977-78*

Stratum Grouping	Number of Prescriptions handled per month	Average Cost per PBS prescription (cents)
Stratum 1	1 - 896	214.8
Stratum 2	897 - 1151	179.9
Stratum 3	1152 - 1390	175.2
Stratum 4	1391 - 1641	164.4
Stratum 5	1642 - 1905	161.2
Stratum 6	1906 - 2309	138.0
Stratum 7	2310 - 2971	139.0
Stratum 8	2972 +	123.0
Overall Average		161.1

Source : Joint Committee on Pharmaceutical Benefits Pricing Arrangements, Results of 1977-78 Inquiry into Pharmacy Earnings, Costs and Profits.

* In a submission to the Joint Committee, the Guild formally repudiated the Survey findings. Consequently, the absolute levels of cost data in the above and following tables needs to have this constraint noted. However, the relativities expressed in the data are probably reasonably accurate.

10.9 The difference in the cost structure can be attributed mainly to the labour cost component of dispensing a prescription. Most of the pharmacies in Australia, according to the submission of Mr R. Harvey (Health Research Project, Australian National University) are working well under capacity; and analysis in that submission suggested that, for a sole-trader pharmacy, the minimum unit cost operation was being achieved only in Strata 7 and 8.

10.10 If the intention of a remuneration system is to compensate chemists for the costs involved in dispensing PBS prescriptions, then the current system clearly fails to achieve this goal. If the aim is to compensate for actual expenses of dispensing PBS and RPBS drugs then the present diversity of relative size of pharmacies in Australia would require that a system of variable returns based on the throughput of prescriptions be developed.

10.11 However, this aside, the important aspect to be considered is the effect of any remuneration package on the structure of the industry.

10.12 During the inquiry many witnesses commented on the apparent profitability of operating a pharmacy. It was agreed that, while retail margins could be low, retailing was generally profitable. There was no consensus on the financial operations of dispensing. The PAC is in no doubt that the pharmacies with large prescription volumes found dispensing relatively profitable (since remuneration is assessed on an overall average, the top three strata enjoy considerable economies of scale). However, some witnesses were adamant that the lower prescription volume sectors of pharmacy were unprofitable.

TABLE 10 : Apparent Profitability of Dispensing PBS Prescriptions : Australia : 1977-78

Survey Grouping	Total number of pharmacies	profitability cents per prescription (cents)
Stratum 1	1431	-17.98
Stratum 2	916	22.42
Stratum 3	740	28.91
Stratum 4	619	39.57
Stratum 5	531	43.82
Stratum 6	450	62.98
Stratum 7	359	69.34
Stratum 8	242	84.42
	Total 5288	Average 42.65

Source: Joint Committee: Results of 1977-78 Inquiry into Pharmacy Earnings, Costs and Profits.

10.13 At its hearings the PAC ascertained that the Guild's view of unprofitability was quite specific. It was in terms of findings of the 1972-73 Survey (not necessarily in terms of the 1977-78 Survey results), and was to the effect that the lower 70 per cent of pharmacies were not earning sufficient to cover their costs and to make a reasonable return on their capital investment. Data in Table 10 indicates that in 1977-78 the profitability of dispensing PBS prescriptions was directly related to the number of prescriptions handled.

Future Basis for Remuneration

10.14 Past attempts at determining the basis for remuneration have had five broad characteristics:

- they have been between two groups only, the Commonwealth Government and the Guild, with all other parties being excluded;

- they have been conducted in private without public scrutiny;

- attempts at determining an objective method of remuneration have been conducted using no independent objective expertise;

- past surveys have taken a very long time to complete and upon completion the results have generally been rejected; and

- after a breakdown in these attempts to determine an objective basis, political negotiations have resulted.

10.15 Given the disputes between the Commonwealth Government and the Guild using cost of production surveys, the use of movements in award wages, cost accounting approaches, regression approaches, relatively economic pharmacy approaches, overall average pharmacy approaches, updating bases on "fore and aft" wage and price movements, in addition to the multitude of smaller disputes on other matters, it is understandable that the pharmacy industry is in apparent crisis.

10.16 The PAC commented in Chapter 7 that a number of witnesses had identified some deficiencies in the use of cost of production models. For the model used in the 1972-73 and 1977-78 Surveys, the Committee noted (see tables 3 and 4 at chapter 3) three variables as being critical to the definition of the final cost of dispensing a PBS prescription. These are proprietor's notional salary, rate of return on funds employed and the allocation of costs between the four sectors of the pharmacy business.

10.17 In other words, the methods by which these variables are used within the model and the results deriving from that use are significant factors in generating beliefs and expectations as to whether the industry as a while, or certain strata, can be regarded as profitable. While the PAC is not technically analysing the question of methodology, it has previously expressed its reservations about the way in which the cost of production model has been used within the Joint Committee to determined chemists' dispensing fees.

10.18 In its efforts to resolve issues of methodology, the Joint Committee sought the advice of three consultants and the Industries Assistance Commission. The Joint Committee has restricted the giving of advice to these chosen consultants. It has not clearly defined the intentions of the exercise and, as has characterised past situations, will now judge the results not as an independent group but as interest groups with set ideas of the desired result. The PAC has indicated in Chapter 7 that it does not support this arrangement.

10.19 The PAC considers that any method of determining chemists' remuneration requires detailed technical studies by an independent and appropriately qualified organisation.

10.20 The PAC also considers that it is totally inappropriate for the Joint Committee - comprising only two of many parties with direct interests in the outcome to sit in judgement on such a study.

10.21 The PAC will therefore recommend that a major independent inquiry be undertaken into the retail pharmacy industry. This inquiry will consider the general levels of government expenditure on the pharmacy industry and canvass alternate methodologies for determining chemists' remuneration. As discussed next, this inquiry should also consider the industry structure.

<u>Pharmacy Industry Rationalisation</u>

10.22 The discussion at the beginning of this chapter established that :

- On a pharmacy to population ratio Australia has 1: about 2,600, and under present arrangements there is little movement in this ratio.
- Witnesses indicated that on economic grounds there are too many pharmacies in Australia, and this seems to be borne out by the international comparisons available.

- There is general agreement that pharmacies with large volumes of prescriptions are relatively profitable. While there may be room for debate on the way in which profitability of dispensing is presently calculated, the lower strata of pharmacies may not be economic or profitable.

10.23 Examination of the question of possible reconstruction of the retail pharmacy industry indicated that the topic was not new and that previous consideration of rationalisation had raised considerable apprehension.

10.24 In early 1977 the Commonwealth Government requested the Joint Committee to provide possible options for rationalistion. A special sub-committee was established with the Government side and Guild representatives. Both sides presented lists of options for rationalisation of the pharmacy industry in October 1977.

10.25 The Government side's options covered:

1. The amalgamation of pharmacies;
2. the voluntary rationalisation of pharmacies;
3. licensing by State Governments of Pharmacy outlets;
4. placing limitations on PBS approvals;
5. increased dependence on hospital dispensaries;
6. economic pressure on pharmacies; and
7. tendering for PBS remuneration rates.

10.26 The Guild also put forward a discussion paper which reiterated their previously expressed preference for first, encouraging amalgamations and, second, undertaking a detailed research program to investigate all other options in depth. The Guild opposed compulsory rationalisation options but concluded that if government was involved it should:

- provide funds to the Guild to determine the need for rationalisation;
- provide financial assistance in pharmacy amalgamation programs;
- allow the Guild access to data and expertise within Government departments.

10.27 According to evidence the discussions on rationalisation proceeded in secrecy, with no indication to the industry that rationalisation was under discussion. The contents of these negotiations were "doctored" and leaked to the pharmacy press.

10.28 As a consequence, the matter received unfavourable publicity and, in November 1977, the Minister for Health was obliged to send a letter to all chemists "to categorically deny that the Government would in any way consider any moves to rationalise pharmacies unless the chemist specifically requested the Government to consider it".

10.29 This episode illustrates the disadvantages of unnecessary secret discussions. A matter as important as this to the well-being of the retail pharmacy industry should be considered in an open manner before the entire industry, and deserves the fullest consideration by all concerned. Apart from basic considerations of equity and justice the PAC does not see any prospect of pharmacy rationalisation proceeding successfully without a full public inquiry for four reasons.

10.30 More than just present pharmacists are involved. A public inquiry would give all interested parties a chance to be heard. A particularly important sector that needs to be consulted is the universities which produce pharmacy graduates. A recent study in Victoria indicated that there were more pharmacy graduates being produced than could be absorbed across the entire profession. Any reduction in the number of pharmacies could have an impact on the job market for pharmacists, and this would need to be investigated thoroughly.

10.31 Second, an open inquiry into pharmacy rationalisation is necessary to enable the fullest consideration of the numerous options. The Joint Committe's rationalisation subcomittee identified a number of methods whereby rationalisation might be achieved, and the PAC believes that probably more options exist. For example, an inquiry would need to consider the effect on the structure of the industry of variable dispensing fees, and the effect of allowing the patient contribution of $2.75 to be variable. (Recent proposed amendments to the patient contribution, which would have had a major effect on the structure of retail pharmacy, had to be set aside within 48 hours due to apparent lack of adequate consultation.)

10.32 Third, effective rationalisation may require that the Government develop some form of restraint over the opening of new chemists shops; this is not a step to be take lightly and without the fullest possible consultation.

10.33 Fourth, it enables consideration to be given not only to the justification and methods of rationalising the pharmacy industry, but how such measures might be effected with least dislocation and inconvenience, both to chemists and to the public.

10.34 When considering rationalisation proposals an inquiry would need to consider the question of compensation as an inducement to a reduction in the number of pharmacies. The PAC believes that much if not all of this compensation could be self-financing, that is, remaining chemists would achieve higher volumes of dispensing at little or no additional cost. This would increase their profits deferring the need for adjustment of remuneration and that deferred increment could be used to fund a rationalisation scheme without any real increase in expenditure.

10.35 Noting that a one cent increase in fees is worth about $1 million, such a proposal seems worthy of more detailed investigation. Based on the 1977-78 Survey results, the Department of Health carried out for the PAC an analysis to determine the effect on the average cost of dispensing a PBS prescription under the following hypothetical assumptions:

1. Remove Stratum 1 (the shops with the smallest prescription volume)

2. Remove Strata 1 and 2

The results indicated that if these hypothetical examples occurred the average costs of dispensing a PBS prescription fell by about 7 cents in the first instance and by about 12 cents in the second. This hypothetical case disregards the need to maintain adequate access to pharmacy services. The PAC accepts that the assumptions chosen are not realistic, but the calculations made suggest that there could be a 'saving' created of about $5 million to assist in rationalisation. This example highlights how, if some pharmacies closed, the remaining pharmacies would benefit and prescription costs could be contained, to the benefit of the public.

10.36 The PAC fully endorses the attitude of the Guild that before any rationalisation plans can be formulated a full and open study of the industry needs to be undertaken.

10.37 The PAC considers that the Industries Assistance Commission could be the appropriate organisation to carry out such an inquiry into the retail pharmacy industry because the IAC has already the necessary expertise, experience and facilities for conducting such independent public inquiries.

Recommendations

10.38 The Commonwealth Government initiate a public inquiry into the retail pharmacy industry. This inquiry examine:

a. the appropriate structure of and numbers in the industry having regard to Australia's geography and its population distribution;

b. the need and justification for rationalising pharmacy numbers;

c. methods of rationalising the industry;

d. forms and levels of compensation that might be used to facilitate the rationalisation process; and

e. methods of determining chemists' remuneration.

CHAPTER 11

THE REPATRIATION PHARMACEUTICAL BENEFITS SCHEME

11.1 Additional to the 92.9 million pharmaceutical items prescribed under the Pharmaceutical Benefits Scheme (PBS) in 1978/79 were about 7.5 million items prescribed under the Repatriation Pharmaceutical Benefits Scheme (RPBS). Total expenditure on the PBS in 1978-79 was $391 million (including patient contribution) while the cost of the RPBS was $36 million, excluding administration and salary costs.

11.2 As indicated in Chapter 3 excess payments to chemists of up to $18.2 million were made under the RPBS.

11.3 This chapter examines the administration of the RPBS by the Department of Veterans' Affairs in the context of these excess payments.

Evolution of RPBS

11.4 The RPBS was established in 1919 and, until the 1960s, arrangements with chemists were negotiated outside the framework of the PBS. In 1948 a rudimentary pharmaceutical benefits scheme was established for the community at large. Although the PBS was eventually to have a profound impact upon pharmaceutical services throughout the community, initially the number of drugs available was so restrictive in comparison to the RPBS that its impact upon the latter was minimal.

11.5 In its Fifteenth Report submitted in 1954, the Public Accounts Committee (PAC) reported upon its investigation of a number of selected activities of the then Department of Repatriation, including its administration of the RPBS. That Report questioned whether it would not be more appropriate for the price checking functions to be performed by the Commonwealth Government rather than by the Pharmacy Guild of Australia (the Guild). A subsequent review confirmed that price checking could be performed at a lower cost by the Department. In late 1954 the Guild agreed to reduce its commission for price checking services from 1.5 percent to 1.0 percent. In July 1961 the Department of Health took over the price checking functions on behalf of the Repatriation Commission, and the Guild's participation reverted to providing manual pricing services on behalf of individual chemists submitting claims under the RPBS.

11.6 According to the Department of Veterans' Affairs' submission, the decade after 1954 was a time of considerable contention and lengthy debate between the Guild and the Commonwealth Government, not only as to the merits of the price checking functions continuing to be undertaken by the Guild, but also as to whether dispensing fees and mark-ups under the RPBS should be aligned with the NHS. At this time the RPBS payments to chemists were based upon the private dispensing fees as determined by the various State Branches of the Guild from time to time. These were virtually entirely divorced from the basis of pricing and fees developed under the PBS.

11.7 In 1963 the fees paid by the Commonwealth Government to chemists under the RPBS were aligned with those paid under the PBS, and since that time the two schemes have been drawn closer together. However the two schemes retain basic differences, which are summarised below.

MAJOR DIFFERENCES BETWEEN THE RPBS AND THE PBS

ITEM	RPBS	PBS
. Range of drugs	unlimited	confined to drugs listed in the Schedule of Benefits
. Quantities and repeats	one month's supply, two repeats	specified for each item
. Restrictions on prescribing	prior departmental approval required for specified items of limited therapeutic value	prior departmental approval required for specified items which are for limited use or are expensive; also some items are restricted to specified purposes which must be acknowledged by the prescriber notating prescriptions 'S.P.'
. Patient contribution	nil	pensioners: nil; others: statutory amount (currently $2.75)

As the Department of Veterans' Affairs noted in its submission, none of the above differences have been inconsistent with the principle of maintaining parity in the pricing arrangement between the two schemes.

11.8 Over the years there has been an increasing trend for RPBS prescribing to conform to the PBS. Whereas in 1960 PBS items constituted some 60 percent of all RPBS prescription items, by 1980 this proportion had increased to 80 percent.

Rationalisation of Resources between Departments of Veterans' Affairs and Health

11.9 In 1977 some moves were made to rationalise ADP resources in the health/welfare area. A joint Departments of Health/Veterans' Affairs Working Party was established to formulate a detailed plan for the processing of chemists' RPBS accounts. Its report identified certain economies that could be realised and, inter alia, led to an agreement between the two Departments whereby the Department of Health would take over the pricing and checking functions of the RPBS on behalf of the Department of Veterans' Affairs, on the Department of Health's ADP system. This occurred on 1 May 1979 in Victoria, and on 1 July 1979 in the other States. Desirable as this action appears to have been, the PAC notes that it led to some serious staffing problems.

11.10 The workload of the RPBS pricing and checking function involved 48 positions in the Department of Veterans' Affairs, and the Public Service Board agreed to transfer these to the Department of Health. The New South Wales Region of the Department of Health was allocated 19 of these positions. Following the re-categorisation of these positions (because the Department of Veterans' Affairs was on a manual system and the Department of Health was on an ADP system) only four trained staff were actually transferred to the Department of Health. The Public Service Board played a major part in these staffing re-arrangements, and it provided the PAC with details of the circumstances whereby the Department of Health suffered a major and unforseen staffing deficit as a result of the change of administrative arrangements. The result of the re-categorisation led to only nine of the 19 positions remaining as Clerical Assistant; and only four of these nine positions were actually staffed by trained staff from the Department of Veterans' Affairs because of an unforseen refusal by most staff to accept the offer of transfer.

11.11 As the direct result of the unsatisfactory transfer of staff, considerable delays in the processing of RPBS claims occurred. This resulted in numerous complaints and representations; the Department of Health experienced severe operational and personnel problems.

11.12 The PAC considers that this was due to lack of application, foresight and planning. In addition, when the problem was first emerging the Public Service Board appeared to have failed to assist the Department of Health in making

up the numbers. Accordingly the PAC will be recommending that the Public Service Board and relevant departments conduct thorough investigations and planning when transferring staff between departments.

Policy on the RPBS

11.13 Since 1963, in accordance with the directive of the Commonwealth Government, changes in the dispensing fee of the PBS have been, by convention, automatically applied to the RPBS. These arrangements have been covered in formal agreements between the Guild and the Repatriation Commission. The first agreement was made in March 1963 and the current agreement dates from the end of 1971. The Department of Veterans' Affairs advised that the 1971 agreement is to be amended. The agreement is backed by a booklet called 'Notes for Pharmacists' which establishes the basis upon which individual chemists dispense drugs under the RPBS.

11.14 While the Department of Veterans' Affairs has an identical dispensing fee structure to that of the Department of Health under the PBS, the former does not participate in any meaningful way in determining those fees. It stated that it has "never been called upon to make submission to, give evidence before, or take part in the deliberations of the Joint Committee". By the terms of Clause 120 of its 1971 agreement with the Guild:

> "... the Pharmacist shall ... be paid by the Commission at the rates which would be applicable if the particular items were priced in accordance with the principles of pricing determined by the Minister of State for Health from time to time under the National Health Act ...".

11.15 This distancing of the Department of Veterans' Affairs from essential administrative aspects of its own scheme was explored by the PAC during its hearings, and particularly in regard to the excess payments. At the PAC's request the Department subsequently prepared a calendar of relevant events relating to the excess payments issue, and this is reproduced at Appendix 12. From that document and the evidence orally given to the PAC it appears that:

- Certain officers in the Department of Veterans' Affairs became aware via "grapevine rumours" early in 1980 of the possible existence of excess payments.

- When the story broke in the press on 14 February 1980, a briefing note for the Minister for Veterans' Affairs was prepared but held back due to lack of specific confirmation of details.

- Two months elapsed before the Department of Veterans' Affairs was given access to the data on which to base its estimates of the excess payments in respect of the RPBS.

- The Department of Veterans' Affairs was not at any stage made privy to the deliberations of Cabinet concerning the excess payment.

- Nor was a copy of the 'Report of the Public Service Board Team' made available to it.

- The Department of Veterans' Affairs was not made aware of the Minister for Health's first statement on the excess payments - of 2 April 1980 - until it read about it in the newspapers.

- When the press started questioning the Department of Veterans' Affairs - two weeks after the Minister for Health's first statement - as to its share of the total excess payments, the Department of Veterans' Affairs had insufficient data to prepare a reasonable estimate.

- Data on which to calculate the excess payments was made available to the Department of Veterans' Affairs only on the Friday before its Minister's Monday statement to the House of Representatives.

11.16 These events highlight that, over the years, the Department of Health has become predominant with respect to the PBS and RPBS generally, and the Department of Veterans' Affairs had taken, or been forced, into a back seat role. As well as the instances noted above, the PAC received evidence that when the Department of Veterans' Affairs was trying to brief its Minister and was seeking information it was told that it ought not to make inquiries. The haphazardness of this episode is illustrated by two examples. First, during the entire two months between the emergence of the possibility of excess payments and the Minister's speech (February to April 1980) there was, according to the Department, no correspondence at all on the subject. Second, the Department, to its credit, sought its own legal opinion from the office of the Crown Solicitor on what its situation might be regarding the excess payments. It received some oral advice but is, almost five months later, still awaiting written confirmation of that advice.

11.17 A similar sense of distance from events was perceived by the PAC during its investigation of whether the Department of Veterans' Affairs participated, or wished to participate in, the actual fee determination process. The Department of Veterans' Affairs advised that it did not have a need nor did it wish to participate in the Joint Committee deliberations:

> "... we do not feel that as a Department ... we would be able to bring a level of expertise to that Committee over and above that already available within the Department of Health. We are still of the view that we do not see a need to pursue representation on that Committee".

11.18 Considerable evidence was produced to support the view that the close alignment of the RPBS with the PBS, the taking over of some administrative and processing tasks of the RPBS by the Department of Health, and that Department's predominance in the various negotiations over prices of pharmaceuticals and dispensing fees had resulted in more efficient and effective management and considerable savings in ADP costs and by unifying processing staff.

11.19 The PAC endorses these conclusions, and in its following recommendations proposes that the responsibilities of the two Departments should be made clearer, with the aim of benefiting them both, and avoiding some areas of potential and actual deficiencies of management and ADP processing. The PAC considers that its recommendations would enable greater economies and efficiency to be achieved, and that some further staff savings might be possible if the Department of Veterans' Affairs ceased to handle those administrative functions already carried out by the Department of Health, and on which the Department of Health could deal directly with 'customers'.

11.20 The above changes can be achieved by means of administrative arrangements, and require no alterations to legislation. The PAC notes that, based on a supplementary paper on staffing provided by the Department of Veterans' Affairs, there are currently almost 70 staff available in its Central Office and State Branches to continue the policy and liaison work proposed above, should that number prove necessary.

Recommendations

(i) The Department of Veterans Affairs retain policy control over the Repatriation Pharmaceutical Benefits Scheme.

(ii) The Department of Health be given total responsibility for the administration and claims processing of the Repatriation Pharmaceutical Benefits Scheme.

(iii) The Department of Health integrate the administration and processing of the Repatriation Pharmaceutical Benefits Scheme with the Pharmaceutical Benefits Scheme so as to achieve the utmost economy commensurate with sound management and high standards of service to those submitting claims.

(iv) A Joint Department Liaison Committee on Repatriation Pharmaceutical Benefits Scheme matters be established to provide formal communication and consultation between the Departments of Veterans' Affairs and Health.

(v) The Public Service Board together with the various staff Associations, review policies and procedures for the transfer of staff between departments in order that staff transfers are conducted smoothly and efficiently. The results of this review are to be advised to the PAC in 1981.

APPENDIX 1

DATES OF HEARINGS, DETAILS OF WITNESSES AND ASSISTANCE TO THE COMMITTEE

During the course of the Inquiry hearings were held as follows:

In public	25 June 1980	Canberra
	26 June 1980	Canberra
	15 July 1980	Canberra
	16 July 1980	Canberra
	23 July 1980	Sydney
In camera	23 July 1980	Sydney

The following witnesses were called and examined by the Committee.

Dr Geoffrey Earle Brooks, Director, (Treatment Policy Development), Department of Veterans' Affairs, Canberra

Mr John George Burt, Assistant Director-General, Automatic Data Processing Branch, Department of Health, Canberra, Australian Capital Territory

John Kelvin Cornish, Acting Assistant Statistician, Australian Bureau of Statistics, Cameron Offices, Belconnen, Australian Capital Territory

Mr Robert Paul Davies, Director, Health Research Division, Pharmacy Guild of Australia, 30 Strickland Crescent, Deakin, Australian Capital Territory

Miss June Drury, Computer Systems Operator (Grade 2), Department of Health, Canberra, Australian Capital Territory

Mr Donald Mervyn Gibbons, Executive Director and Public Officer, Pharmacy Guild of Australia, 30 Strickland Crescent, Deakin, Australian Capital Territory

Mr Edward Keith Graver, National Vice-President and Chairman, National Health Committee, Pharmacy Guild of Australia, 30 Strickland Crescent, Deakin, Australian Capital Territory

Dr Gwyn Howells, Director-General, Department of Health, Canberra, Australian Capital Territory

Mr Graham Alexander Ingerson, National Vice-President, Pharmacy Guild of Australia, and member of the National Health Committee, 30 Strickland Crescent, Deakin, Australian Capital Territory

Mr Leslie Ion, Acting Assistant Director-General ADP Branch, Department of Health, Canberra, Australian Capital Territory

Mr Louis William Lane, First Assistant Director-General, Management Services Division, Department of Health, Canberra, Australian Capital Territory

Mr David Colin Leaver, Acting First Assistant Statistician, Australian Bureau of Statistics, Cameron Officer, Belconnen, Australian Capital Territory

Mr Richard Thuell Lord, Director, Pharmacy Inquiry Secretariat, Finance, Pharmacy Earnings and Projects Branch, Department of Health, Canberra, Australian Capital Territory

The Hon. Mr Justice J.T. Ludeke, Chairman, Joint Committee of Pharmaceutical Benefits Pricing Arrangements, Department of Health, Canberra, Australian Capital Territory

Mr Brian John Meredyth, Assistant Secretary, Department of Industry and Commerce, Canberra, Australian Capital Territory

Mr George Thomas Miller, First Assistant Commissioner, (Management Services), Department of Veterans' Affairs, Canberra

Mr James Sinclair Millner, Chairman and Managing Director, W.H. Soul Pattinson and Co, Ltd, 160 Pitt Street, Sydney, New South Wales

Mr John William Muir, First Assistant Commissioner (Treatment Services), Department of Veterans' Affairs, Canberra

Mr Alan Alexander Russell, National President, Pharmacy Guild of Australia, 30 Strickland Crescent, Deakin, Australian Capital Territory

Mr John Franklin Scown, National Counsellor, Pharmacy Guild of Australia, and member of the National Health Committee, 30 Strickland Crescent, Deakin, Australian Capital Territory

Mr John William Shaw, Assistant Director-General, Finance Pharmacy Earnings and Projects Branch, Department of Health, Canberra, Australian Capital Territory, and member of the Joint Committee on Pharmaceutical Benefitis Pricing Arrangments

Mr Arthur Edward Shields, Assistant Director-General, Pharmaceutical Benefits Branch, Department of Health, Canberra, Australian Capital Territory, and member of the Joint Committee on Pharmaceutical Benefits Pricing Arrangements

Mr Francis Robert Somes, First Assistant Secretary, Department of Industry and Commerce, Canberra, Australian Capital Territory, and member of the Joint Committee on Pharmaceutical Benefits Pricing Arrangements

Mr Kenneth Edward Walker, Consultant to Pharmacy Guild of Australia and a member of the Joint Committee on Pharmaceutical Benefits Pricing Arrangements, Pharmacy Guild of Australia, 30 Strickland Crescent, Deakin, Australian Capital Territory

Mr John Mervyn Wark, First Assistant Secretary, Social Security Division, Department of Finance, Canberra, Australian Capital Territory, and member of the Joint Committee on Pharmaceutical Benefits Pricing Arrangements

Mr Gregory Allan Woodward, Assistant Commissioner (Finance), Department of Veterans' Affairs, Canberra

APPENDIX 2

SUBMISSIONS AND EXHIBITS RECEIVED BY THE COMMITTEE

1. Department of Health, submission of 12 June 1980

2. Department of Veterans' Affairs, submission of 10 June 1980

3. Agreement between the Repatriation Commission and the Pharmacy Guild of Australia, submission of 17 June 1980

4. Pharmacy Guild of Australia, submission of 17 June 1980

5. Joint Committee on Pharmaceutical Benefits Pricing Arrangements, submission of 13 June 1980

6. Bureau of Agricultural Economics, submission of 15 July 1980

7. Director ADP Application, Department of Health, memorandum to Director, Standards and Control Section, 4 July 1973

8. Secretary, Joint Committee on Pharmaceutical Benefits Pricing Arrangements, presentation on 1977-78 Pharmacy Inquiry Methodology and Results, 16 July 1980

9. Department of Health, Statement on the Estimate of Excess Payments to Chemists 1973-74 to 1978-79, 16 July 1980

10. Pharmacy Inquiry Secretariat, response to request to estimate possible excess payments to chemists from 1973-74 to 1978-79, 16 July 1980

11. Joint Committee on Pharmaceutical Benefits Pricing Arrangements, tables and printout relating to the 1972-73 and 1977-78 Inquiries into Pharmacy Earnings, Costs and Profits

12. Department of Industry and Commerce, submission of 20 June 1980

13. Friendly Societies' Pharmacies Association of Australia, submission of June 1980

14. Pharmaceutical Society of Australia, submission of 30 July 1980

15. Australian Federation of Consumer Organisations, submission of 8 August 1980

16. Roy Harvey, B Sc, MEc, Research Fellow, Health Research Project, Australian National University, submission of August 1980

17. *Pharmacy Guild of Australia, final submission of 15* August 1980

18. Joint Committee on Pharmaceutical Benefits Pricing Arrangements, memorandum of 15 August 1980

19. W. Bookallil, 14 Starkey Street, Forestville, 2087, letter of 8 August 1980

20. P.G. Cains, 83 Grandview St, Pymble, 2073, letter of 13 August 1980

21. G.B. Croker, 308 Pacific Highway, Lindfield, 2070, letter of 10 August 1980

22. A.J. Dumas, shop 24 Arndale Centre, Frenchs Forest, 2086, letter of 8 August 1980

23. J. Jackson, 778 Pacific Highway, Gordon, 2072, letter of 8 August 1980

24. G. Lee, 5 St Johns Avenue, Gordon, 2072, letter of 4 August 1980

25. R. *Miller, 29 Babbage Road, Roseville Chase, letter of* 12 August 1980

26. D. Moyes, 23 Lindfield Avenue, Lindfield, 2070, letter of 9 August 1980

27. H.S. Price, 2 Philip Mall, West Pymble, 2073, letter of 6 August 1980

28. D.O. Steenbhom, 21 Lindfield Avenue, Lindfield, 2070, letter of 11 August 1980

Statement by the Minister for Health
to the House of Representatives,
2 April 1980.

PHARMACEUTICAL BENEFITS

Ministerial Statement

Mr MacKELLAR (*Warringah—Minister for* Health and Minister assisting the Prime *Minister*)—*by leave*—Honourable members will recall that I have been asked in recent weeks to confirm or deny that an 'overpayment' has been made to chemists in Australia for the supply of pharmaceutical benefits. I indicated that the inquiry being undertaken by *Mr Justice Ludeke* and the Joint Committee on Pharmaceutical *Benefits Pricing Arrangements* had not been finalised and until it was finalised it would not be appropriate for me to comment on the media reports. Though Mr Justice Ludeke has not yet made his determination, the Government now has additional information which it believes should be made available to the Parliament.

Late last year the emerging results of an inquiry into pharmacy earnings, costs and profits for the financial year 1977-78 suggested that an 'excess payment' situation might exist in relation to fees paid by the Commonwealth for the dispensing of prescriptions under the national health scheme. The Government was originally concerned to ensure that payment to chemists for dispensing prescriptions should be at a level which is appropriate to cost structures and reasonable returns. But on learning of this possible excess payment situation, it also became concerned to arrive at an independent assessment of how this possible 'excess payment' situation could have arisen. Accordingly, the Government asked for a report from the Public Service Board covering the circumstances which led to the potential for 'excess payments' to be made to chemists; the extent to which responsibility might be attributed; and any appropriate action.

The Public Service Board set up a team comprising one of its senior officers, and senior officers from the Department of Finance and the Auditor-General's office. The team was responsible to the Board for the duration of the exercise and its report was made available through the Board to the Government. The report of the Public Service Board team indicates that if the Chairman of the Joint Committee had made a determination solely on the basis of information

flowing from the 1977-78 inquiry which became available late last year, 'excess payments' of $93m or $173m, depending on the method of assessment, would have accrued between 1 July 1976 and the end of December 1979. It also indicates that 'excess payments' of $12m or $62m, once again depending on the method of assessment, would have occurred between 1973-74 and 1975-76 on this same basis.

The 'excess payments' of $12m in 1973-74 and 1975-76 and $93m from 1 July 1976 to 31 December 1979 were assessed on the basis of what would be an appropriate level of remuneration for an 'average' pharmacy. The 'excess payments' of $62m in 1973-74 and 1975-76 and $173m from 1 July 1976 to 31 December 1979 were assessed on the basis of what would be an appropriate level of remuneration for an 'economic' pharmacy under which the influence of small, less economic pharmacies on the cost evaluation is lower than in relation to the 'average' pharmacy approach. I should stress at the outset that these sums of money are not overpayments which are recoverable at law. Amounts determined by the Minister prior to January 1977 and by the Chairman of the Joint Committee since then have been legally made. This has been confirmed by advice from the Attorney-General's Department. The Government and the body representing chemists—the Pharmacy Guild of Australia—have also received separate legal advice that these 'excess payments' cannot be recovered.

I would further emphasise that in arriving at a decision on the level of chemists' remuneration based on the 1977-78 inquiry data, the Chairman of the Joint Committee will obviously consider other factors put before him in Joint Committee which are relevant to the outcome of the inquiry. These 'excess payments' figures can therefore be seen to be notional only. They are attributable to the following factors: An error which occurred in 1974 in the translation of the statistical specifications into computer systems specifications to be used for allocating labour costs; and the method of updating determinations.

My inquiries suggest that by far the greater share of the notional excess payment is due to the error which occurred in 1974. For this reason I intend to focus first, and in particular, on the circumstances surrounding that error. The error itself, which I shall describe later, occurred in an area of considerable technical complexity. The working environment, including relationships between the relevant Minister, advisory—and later statutory—bodies, supporting units and departments, is equally complex. For this reason I trust that honourable members will bear with me as I provide some of the more important background which emerged from examinations by officials, the Public Service Board team and myself of the pertinent papers.

There have been three major inquiries carried out to date to assist in making determinations of amounts payable to chemists for pharmaceutical benefits supplied under the national health scheme. The inquiries were carried out in respect of the financial years 1964-65, 1972-73 and 1977-78. They all basically involved an inquiry by a committee made up of representatives of the Pharmacy Guild and the Government, the committee being chaired by an independent chairman.

The comprehensive manner in which the inquiries were designed and carried out meant that it took some considerable time after the inquiry year before figures became available for use in the making of a determination. Between inquiries updating arrangements have been applied to take account of chemists' changed cost and price structures. The inquiry results provide base figures on earnings, costs and profits of pharmacies and are used as a basis for reviewing the level of remuneration paid to chemists for the supply of pharmaceutical benefits. The level of remuneration comprises a dispensing fee and a mark-up on goods—mark-up is a percentage of the list price of goods to chemists, currently 25 pee cent in relation to ready-prepared pharmaceuticals.

The 1964-65 inquiry was conducted by the Joint Committee on Pharmaceutical Benefits Pricing Arrangements, under the chairmanship of Sir Walter Scott. This inquiry followed many years of negotiating remuneration increases between the members of the Pharmacy Guild and Government representatives. During the years prior to 1964, considerable difficulty had been experienced in arriving at an acceptable formula for determining increases for the remuneration for chemists. It was against this background that the Guild in February 1965 proposed that an inquiry be conducted by an independent firm of consultants to provide factual information on the costs of dispensing National Health Service prescriptions.

The 1964-65 inquiry failed to substantiate an increase for chemists and to provide the expected factual information on which to base future increases in remuneration. By early 1972 the Guild and the Government had reached an impasse

which could only be overcome by another inquiry based on more modern concepts of statistical analysis and better design based on the limited experience gained from the 1964-65 inquiry. At the same time a small increase was approved in the level of remuneration as an interim measure.

Agreement was subsequently reached that a new inquiry should be undertaken with respect to the financial year 1972-73. It was originally expected that this inquiry would be finalised by March 1974. When the March 1974 'deadline' was not met, the Government came under strong pressure to finalise this matter quickly. The resultant problems were exacerbated by the difficulties involved in getting sufficient skilled staff for undertaking the very complex work involved in the inquiry. But the report did not become available until May 1975—some three years after the inquiry was initiated.

The time constraint, pressures and 'pathfinding' involved in this inquiry are obvious. But they should be seen in perspective. In order to do so, I need to explain the arrangements which then existed for the conduct of the inquiry—as these are different in certain material respects from arrangements which now apply.

In this period—indeed, until 1976—there existed a non-statutory committee know as the Joint Committee on Pharmaceutical Benefits Pricing Arrangements. This Committee was charged with responsibility for advising the Minister for Health on matters relating to the pricing and supply of pharmaceutical goods. The Committee comprised four representatives of the Pharmacy Guild, and four government representatives—three from the Department of Health and one from the then Treasury—and an independent Chairman. The Chairman's role was very much akin to that of a conciliator. The Chairman attempted to reach agreement where differences of view existed. Where these differences could not be resolved, the Minister for Health was the final arbiter. The role of the Minister is important to remember as this point assumes particular relevance later when the government of the day took decisions which were not in accord with the advice of the Chairman.

As I have said previously, processing of the 1972-73 inquiry was lengthy and troublesome and the Government was under strong pressure to finalise the matter. Indeed, towards the end of 1974-75 the President of the Pharmacy Guild felt sufficiently concerned about the matter to press for a decision. As I understand it, the then Prime Minister was informed in mid-July 1975, of the situation by his Health Minister. In doing so the then Minister was concerned that one likely decision of the inquiry could be an increase in chemists' remuneration backdated to 1 July 1973 which would have involved a substantial charge to revenue.

The then government decided in July 1975 to wind up the 1972-73 inquiry and agreed to an increase in chemists' remuneration. However, the Guild was not satisfied with the outcome of the inquiry. It particularly objected to the fact that the government of the day did not accept the Chairman's recommendation in that it decided firstly to exclude goodwill from calculations in relation to this issue and, secondly, to analyse the results of the inquiry on the 'economic pharmacy approach' I referred to earlier. The Guild considered that its objections warranted consideration of whether action should be taken in the High Court of Australia on this matter.

The records indicate that when the caretaker Government assumed office in 1975 the then Health Minister was briefed on the inquiry. There was no suggestion during that briefing of any doubts about the reliability of the inquiry data. Later briefings of the Minister in January 1976 and of the Prime Minister (Mr Malcolm Fraser) in February 1976 once again did not raise any doubts about the reliability of the inquiry data. There was, however, some uneasiness among officials at the time about figures relating to the question of the treatment of costs of goods sold in the inquiry which led them to initiate another survey on this particular aspect. Results which became available in July 1976 revealed an error of 8c per item for 1973-74 and 5c per item for 1974-75. On establishing this, the base data for future updating was corrected for subsequent years.

During 1976 there were further discussions between the Government and the Guild. These discussions were conducted in the context of a High Court writ issued by the Pharmacy Guild in April 1976. At the end of 1976 agreement was reached between the Government and the Guild on a new arrangement. In summary this involved:

> The amendment of the National Health Act to empower the Chairman of the Joint Committee on Pharmaceutical Benefits Pricing Arrangements to determine chemists' rates of remuneration for the supply of pharmaceutical benefits.
>
> The Chairman would be a Deputy President of the Conciliation and Arbitration Commission.

The determinations made by the Chairman would be binding on the Government as well as on the Pharmacy Guild and its members.

The Pharmacy Guild would withdraw its *High Court writ.*

The Pharmacy Guild would agree to forego past payments which it believed were owing to chemists from past unsettled inquiries.

The Guild accepted that an offer made in April 1976 by the Government to increase chemists' professional fees by 5c from 1 July 1973 had been withdrawn.

A new inquiry into pharmacy earnings, costs and profits would be carried out in 1977-78 to obtain up-to-date data for further reviews of chemists' rates of remuneration.

A 6c increase in fees was to be paid from 1 July 1975 and a further 5c from 1 January 1977.

In December 1976 the National Health Act was amended to provide for the establishment of a Joint Committee on Pharmaceutical Benefits Pricing Arrangements comprising four government officials, four nominees of the Pharmacy Guild of Australia and an independent Chairman. The Chairman of the Joint Committee in consultation with the Committee members was charged with the *responsibility for determining,* at the specific request of either the Minister or the Pharmacy Guild of Australia, the level of remuneration to be paid to chemists for the supply of pharmaceutical benefits to the public. The Chairman's determination was to be binding on *both the Government and the Guild. In addition,* where members made a unanimous recommendation to the Chairman his determination was to accord with that recommendation.

Mr Justice Ludeke was appointed Chairman on 13 January 1977 and planning for the 1977-78 inquiry commenced under the aegis of the new statutory Joint Committee at that time. In April 1977 the Chairman of the joint committee determined that the level of chemists' remuneration should be increased by 12c per prescription on and from 1 July 1976. The decision was also taken to introduce a new method of updating fee levels.

In 1977 the Pharmacy Guild had advanced several proposals for varying amounts each of which, if agreed to, would have signficantly increased the then current fee levels. These cases were the result of the Guild's dissatisfaction from the failure to reach agreement on the outcome of the 1972-73 inquiry. The Guild's aim was to establish an acceptable level of remuneration which could be updated during the course of the 1977-78 *inquiry and which it confidently* expected would be validated by the 1977-78 inquiry.

With the Joint Committee operating on the basis of *conciliation and facing several ambit* claims presented by the Pharmacy Guild to increase remuneration by up to 60c per prescription, the Government officials felt obliged to present a tough counter proposition which adopted the position that the figures available *purported to show a posible excess payment. The* Chairman in the absence of firm cost information from either party decided that the matter could not be resolved until the 1977-78 inquiry had been completed.

The excess payment figure presented by the government officials—which was claimed to be 23c per item—was based on a number of assumptions, some of which were subsequently rejected by the Chairman for inclusion in the processing of the 1977-78 inquiry. I should stress that this *figure cannot be, nor should it be, related to the* outcome of the 1977-78 inquiry. As I said earlier, it simply represented an initial bargaining position for discussion in the Joint Committee at that time.

In February 1978 the Chairman, after considering the cases presented by Guild and Government representatives, declined to approve an increase in the fee level. But in May 1978, on the basis of updating procedures, the Chairman made a determination granting an increase of 9c in *fee level with effect from 1 July* 1977. On 19 May 1978 he made a further determination reducing the mark-up on cost of goods sold, and increasing the fee level to compensate.

In September 1978 consideration was again given to representations from the Guild that an increase be granted. Government officials stated that they were unable to agree to a further increase and that there was a need for the Committee to approach the question of future increases with considerable caution because of the possibility of an excess payment, as might have been expected. The Chairman sought an indication from Guild representatives on what the Guild's position would be if the 1977-78 inquiry results demonstrated that an excess payment situation existed. He had earlier indicated that *there were still considerable uncertainties to be* resolved in the 1977-78 inquiry and that if there was ultimately an under or over-payment he considered it could be adjusted retrospectively to 1 July 1976. The Chairman requested the Guild to make its views known at the next Joint Committee *meeting. He then determined an increase*

of 5c per prescription, with effect from 1 July 1977, on the basis of the updating procedures.

On 17 March 1979, after further processing of the inquiry data, my predecessor was informed by his Department of the real prospect of an excess payment situation existing. Mr Hunt sought urgent discussions with senior colleagues and agreement was reached that every endeavour should be made to expedite the results of the 1977-78 inquiry because of the absolute necessity for informaton to put beyond all doubt the question of whether or not an excess payment situation existed. It was also agreed that any further increases in remuneration should be strongly opposed in Joint Committee, pending the resolution of the excess payment question, and that appropriate action should be taken in the light of the Chairman's determination on the 1977-78 inquiry.

The Joint Committee reached decisions on the numerous matters necessary to finalise the processing of the data gathered during the inquiry. This was completed during the November 1979. Later, following analysis by the secretariat to the Joint Committee and by departmental officers, the problem which I now describe became evident. A comparison of the 1977-78 inquiry results with the updated 1972-73 figures disclosed a disproportionate increase in labour costs as they applied to the retail side of chemists' operations as against labour costs involved in dispensing. I must reiterate that this comparison could only be made after the 1977-78 results became available.

An investigation into this error showed that it had occurred in the translation of certain statistical specifications into computer-based systems specifications to be used for allocating labour costs for the 1972-73 inquiry. The computer programme written from these specifications failed specifically to allocate retail labour costs, which were then automatically allocated in the same proportion as dispensing labour costs. The result of this misallocation was that the costs attributed to National Health prescriptions were inflated and the costs attributed to the retail sector of pharmacy were proportionately lowered. In the final analysis the inquiry showed an increase in the level of remuneration much greater than that which would have applied if the error had not occurred. The error was made by one of a number of programming staff provided by a firm which had contracted to supply the Department of Health with the services of seven consultants for a number of automatic data processing projects. The consultant worked under the immediate supervision of departmental ADP staff. A spot checking system operated in relation to all work but these checks did not reveal the error in the specification. It appears that testing was carried out in respect of individual components of the system but certain test data relating to the particular area could not be checked because the system design was such that certain necessary ratios could not be made available. A check against sample manual calculations, which was a feature of the 1977-78 inquiry, was not carried out in respect of the 1972-73 inquiry.

As I said earlier, there were severe staffing shortages during the latter part of 1974 and early 1975 when testing was being carried out. I should add that unavoidable movement of certain key staff also took place at that time. The complex relationships which existed between the Chairman, the Joint Committee, its subcommittee, its secretariat and departmental units, and the tight timetable which applied, should also be borne in mind when considering how this error arose. I think honourable members should be aware that a great deal was learnt from the problems that the 1972-73 inquiry revealed particularly in relation to any timetable that might be involved in collecting and interpreting the necessary data.

Flowing from this experience certain important changes were made in the design of the 1977-78 inquiry, particularly in relation to the computer programme. The main changes were: The 1972-73 inquiry was used as a bench mark against which the development of the 1977-78 inquiry could be tested; the specifications which set out the methodology for the 1977-78 inquiry were expressed in plain English—not mathematical terms—which reduced the complexity of the inquiry and therefore minimised the possibility of misinterpretation; and revised procedures allowed the adoption of a better timetable for development, testing and checking of the various components of the inquiry. In addition, a higher level of co-ordination was possible between the areas involved because of the experience gained in the earlier inquiry.

Members may ask why some of this experience was not obtained from the 1964-65 inquiry. The simple answer is that the first inquiry, as I mentioned earlier, was carried out by an independent firm of consultants and the Joint Committee exercised only a supervisory role. This meant that the Department did not obtain first-hand experience in the design and conduct of a major inquiry of this nature which could have been used in determining the arrangements made for the 1972-73 inquiry. What all this means is that we were able to apply checks and

balances to the 1977-78 inquiry—particularly in the development stages—which, with the benefit of hindsight, should have been applied to the 1972-73 inquiry.

In addition to the problems of setting a new level of remuneration on the basis of the inquiry, problems also occurred in the updating of remuneration between inquiries. Successive governments have been aware of these problems. There has also been general recognition of the need to strike a reasonable balance between claims of chemists for regular updating of fee levels to compensate for inflationary pressures and structural change in relation to the operation of pharmacies and the need for payments by the Commonwealth to be kept at levels which, naturally, are clearly justified. To help meet these problems action is at present being taken by officers of relevant departments to devise a set of appropriate labour indices which can be used for updating purposes. At this stage the most fruitful area of inquiry would seem to involve the use of award wage rates with necessary weightings for particular occupations. This has only become possible with the recent availability of the 1977-78 inquiry results. With this information we are now able to compare actual pharmacy costs with a forecast labour cost using an average weekly earnings based index, or other indices now judged to be more appropriate such as an award rate index related specifically to the pharmacy area.

I now return to the investigation made by the Public Service Board team. That investigation indicates that there does not appear to be evidence of criminal action by any person in connection with the matters reviewed. Having regard also, among other things, to the difficulties which were then encountered by Government officials at critical times during the period under review, the team did not consider that there was evidence of negligence or misconduct which would warrant action against any individual. My own examination—so far is it has gone—has given me no reason to disagree with these conclusions.

The Public Service Board team also made a number of suggestions. In summary these are: that firstly, all departments and authorities be reminded of their responsibility for the adequacy of standards, including controls and checking procedures, covering the development and operation of computer-based systems—the team noted that action had already been instituted in the case of the Department of Health: that secondly, similarly departments and authorities should be reminded of the need for adequate systems and procedures for checking and validating data used in the making of determinations; thirdly, that changes be made in arrangements for updating fees payable to chemists: fourthly, that alternative arrangements be made for the conduct of major reviews, that is, the possible use of more frequent but smaller surveys: fifthly, that ways be found to legally bind individual chemists in relation to determinations; sixthly, that consideration be given to the possibility of treating NHS and repatriation pharmaceutical benefits in total in assessing fees and mark-up, with potential for reduction in Commonwealth outlays; and seventhly, that the roles and lines of responsibility between the Chairman, the Joint Committee, the sub-committee, the secretariat and the Department of Health be clearly defined. The Government concurs with these recommendations and has instructed the Board to take appropriate action so that in future every effort will be made to ensure that there is no recurrence of the type of error made in the 1972-73 inquiry analysis arrangements, either in the Department of Health or elsewhere in the Government sector. This action is now being undertaken.

Mr Deputy Speaker, I realise that tonight I have taken honourable members through a complex and necessarily detailed series of events extending over many years. I can well understand that members might wish to have the opportunity to explore the matter further. However, to facilitate informed discussion the Government believes that there would be particular advantage if the matter was to be referred to the Joint Committee on Public Accounts for examination and report. In doing so, the Government invites the Committee to make recommendations on how administrative processes could be tightened up beyond those changes suggested in the report of the Public Service Board team. The report of the Public Service Board team will be made available on a confidential basis to the Committee. The Government also believes that the report should be forwarded to the Auditor-General. I have written to the Committee and the Auditor-General advising them of this. I seek leave to table copies of these letters.

Leave granted.

Mr MacKELLAR—I wish to conclude my statement on this issue by emphasising that it is an extremely difficult area. It has caused successive governments for some 15 years significant difficulties which have had to be borne because of the importance of the pharmaceutical benefits scheme to all Australians. The technical problems involved led to the error I have described tonight in this statement. On confirmation of the existence of this error, the Government acted swiftly to discover the reasons for it and instigate appropriate action to ensure that every action will be taken in future to prevent the recurrence of this or similar errors.

Speech by the Minister for Health
to the House of Representatives,
21 April 1980.

PHARMACEUTICAL BENEFITS: REFERENCE TO JOINT COMMITTEE OF PUBLIC ACCOUNTS

Mr MacKELLAR (Warringah—Minister for Health) (5.34)—I move:

> That the circumstances surrounding the question of 'excess payments' made under the Pharmaceutical Benefits Scheme as set out in the statement of the Minister for Health to the House of Representatives on 2 April 1980 and under the Repatriation Pharmaceutical Benefits Scheme, and the question of whether the relevant administrative processes should be altered in the light of the situation described in the statement be referred to the Joint Committee of Public Accounts for inquiry and report.

As honourable members will recall, in my statement of 2 April last I set out the details of the circumstances surrounding this matter. As I stated at that time, this matter arose because of the following factors: An error which occurred in 1974 in the translation of certain statistical specifications to be used for allocating pharmacy labour costs when determining the formula for calculating the size of the fee for dispensing items under the pharmaceutical benefits scheme and the method of updating the fee.

Honourable members will recall that in my statement I noted that my inquiries suggested that by far the greater share of the blame for why this situation has occurred can be attributed to the error which occurred in 1974. As I noted at that time, the whole question of the appropriate fee to pay to chemists for dispensing items under the pharmaceutical benefits scheme is an extremely technical and complex one and the problems involved were exacerbated by severe staffing shortages during the latter part of 1974 and early 1975.

The administration of the pharmaceutical benefits scheme has caused successive governments for some 15 years significant difficulties which have had to be borne because of the importance of the scheme to all Australians, particularly pensioners. These difficulties led to the situation that I described in my earlier statement which existed under successive governments from 1973-74.

On learning of this situation, the Government acted swiftly to discover the reasons why it occurred and to instigate appropriate action to ensure that every step will be taken in future to prevent the recurrence of this or similar errors. As part of this action, the Government called for a report from the Public Service Board on the matter. The Board in turn set up a team of senior officers to investigate the matter, which reported promptly to the Government. The Public Service Board team has made a number of suggestions as to what action should be instigated to ensure that everything possible is done in future to prevent the recurrence of this or similar errors in other areas of government. A summary of those suggestions was contained in my statement of 2 April last.

As I also stated at that time the Government believes that there would be particular advantage if this matter was referred to the Joint Committee of Public Accounts for examination and report. The Government considers that the Committee's examination of the Public Service Board's mandata computer scheme has afforded its members with a particularly high expertise in computer matters. As I also stated on 2 April last, in referring the matter to the Committee, the Government invites it to make recommendations on how administrative processes can be tightened up beyond those changes suggested in the report of the Public Service Board team.

Honourable members should be aware that when making my statement on this matter on 2 April I did so because of the Government's firm belief that the full facts surrounding this matter should be laid before Parliament and the people of Australia. The Government has, in the same spirit, decided to refer this matter to the Public Accounts Committee—a committee on which members from both sides of Parliament are represented—for examination and report. The wide terms of reference decided upon similarly reflect this view of the Government. I am sure the Committee's report on this matter will fully meet the Government's expectations.

Speech by the Minister for Veterans' Affairs to the House of Representatives, 21 April 1980.

Mr ADERMANN (Fisher—Minister for Veterans' Affairs) (5.38)—I support the initiative of my colleague the Minister for Health (Mr MacKellar) in proposing that the Joint Committee of Public Accounts be asked to inquire into and report on all the circumstances surrounding the question of payments made under both the pharmaceutical benefits scheme and under the repatriation pharmaceutical benefits scheme.

A complex problem has emerged; it is capable of varying interpretations. This is an important matter not only involving a great deal of money, but also with implications for the means of delivery of a vital component of the Australian health care system. Because the Government would want the Parliament to be informed, both in relation to the fact of the payment and how it was arrived at, and because there are difficulties in specifying a simple quantum, it will be of considerable benefit to the Parliament, to the Ministers involved and to the departments to have the Joint Committee of Public Accounts search out the detailed, relevant facts in an objective manner.

The Joint Committee of Public Accounts has proved itself over very many years to be a very responsible and searching body, and is ideally placed to examine this complex problem in detail and to establish not only how the present dilemma occurred but also whether the current administrative processes are at fault and whether or not they ought to be altered. In fact I have previously had the privilege of serving on the Joint Committee of Public Accounts and I would be confident of the Committee's ability to present this Parliament with a full and even-handed report. This is not to withdraw in any way from the advice already provided to this Parliament by my colleague the Minister for Health or me. When a problem of this magnitude arises, it must be dealt with urgently and brought to notice with all honesty. That is exactly what the Minister for Health and I have done.

I take this opportunity to update the information available to the House in regard to the application of the chemist's remuneration formula to the Department of Veterans' Affairs. In answer to a question by the honourable member for Scullin (Dr Jenkins) on 17 April, I acknowledged that the situation described by the Minister for Health in his statement to this House on 2 April had an application to payments to chemists under the repatriation pharmaceutical benefits scheme, and indicated that I hoped to be in a position very soon to make a quantification of such application.

My Department has now provided me with its best possible estimate of the 'excess payment' which can be considered to have been incurred in payments to pharmacists under the repatriation pharmaceutical benefits scheme. Before announcing these figures to the House, there are some general comments I should like to make. In the first place, I make it clear that, as Minister for Veterans' Affairs, I became aware that a situation of some concern relating to payments to chemists under the NHS formula had arisen in relation to the national health scheme when this was reported to Ministers by the Minister for Health during February, and that I was advised by my Department at I think about the same time that there was a flow-on effect in relation to the repatriation prescribing. At that stage, the amount of any excess payment under the national health arrangements had not been finally quantified, and there was no basis upon which the impact on repatriation prescribing could be accurately determined. As I mentioned in the House last week, I was not prepared to provide speculative estimates until I was more confident that these figures were as accurate as possible. Such figures have become available to me only within about the last 48 hours or, more specifically, over the weekend.

I should reiterate the point that I made in my answer last week to the question by the honourable member for Scullin. The same dispensing fees as are fixed from time to time under the National Health Act are also applied to similar services provided under repatriation prescribing arrangements. It has been a matter of Government policy for many years that determinations made under the National Health Act in relation to dispensing fees should be applied automatically to pharmaceutical benefits dispensed under my Department's scheme.

My colleague the Minister for Health, in his statement to this House, emphasised the complexity of this matter of payment of pharmaceutical dispensing fees. The application of these complexities to the repatriation prescribing arrangements, which differ significantly in some respects from the national health scheme, has not been straight forward and some time has necessarily been taken departmentally in making the necessary adjustments to reflect the differences between the two schemes.

Repatriation local medical officers are encouraged, when prescribing for eligible repatriation beneficiaries, to confine such prescribing to the drugs listed in the national health scheme schedule of benefits. They also have a discretion to prescribe drugs outside this range

where, in their clinical opinion, there is no therapeutic alternative available within the national health list. The fact that quite a high proportion of such items are prescribed, and that some attract a dispensing fee while others do not, is the first factor complicating somewhat the extraction of the figures in relation to veterans' affairs. A further factor has been the availability of detailed data and the speed with which it can be drawn. Payments to chemists for benefits dispensed under the repatriation prescribing arrangements have been made by computer only since 1 May 1979, in the case of Victoria, and 1 July 1979, in all other States. Some of the data required for the compilation of the estimates provided to me by the Department of Veterans' Affairs I have been advised had to be drawn and adjusted manually.

I turn now to the quantum of the figures provided to me by the Department of Veterans' Affairs. I understand that these have been assessed on exactly the same basis as were quoted by my colleague, subject only to necessary adjustments because of differences between the two schemes. I shall therefore draw the same distinction as did my colleague in presenting figures on the one hand on the basis of what would be an appropriate level of remuneration for an 'average' pharmacy and on the other of an 'economic' pharmacy.

If the Chairman of the Joint Committee on Pharmaceutical Benefits Pricing Arrangements had made a determination solely on the basis of information flowing from the 1977-78 inquiry, the excess payments which would have accrued between 1 July 1976 and 31 December 1979 under repatriation arrangements would be either \$7.54m or \$14.13m, depending on the method of assessment, and that which would have occurred between 1973-74 and 1975-76 on this same basis, again depending on the method of assessment, would be \$790,000, or \$4.12m. Thus the advice provided to me, summing those figures, is that based on an average pharmacy the amount is estimated at \$8.33m. Based on an economic pharmacy the estimate is \$18.25m.

I should like to reiterate several points made in the statement by my colleague the Minister for Health on April 2. Firstly, in arriving at a decision on the level of chemists' remuneration based on the 1977-78 inquiry data, the Chairman of the Joint Committee obviously considered other factors put before him in joint committee which were relevant to the outcome of the inquiry. These excess payments figures can, therefore, be seen to be notional only. Secondly, these sums of money, according to advice tendered to Ministers, are not overpayments which are recoverable at law. Just as amounts determined by the Minister for Health prior to January 1977 and by the Chairman of the Joint Committee since then in relation to dispensing under national health arrangement have been legally made, so the application of such amounts to repatriation prescribing arrangements have similarly been legally made. I have no doubt that this aspect of this whole question will be considered in depth by the Joint Committee of Public Accounts.

In conclusion, I commend to the House the proposal to refer to the Joint Committee of Public Accounts for inquiry and report the circumstances surrounding the question of the payments made under the pharmaceutical benefits scheme and under the repatriation pharmaceutical benefits scheme and the question of whether the relevant administrative processes should be altered in the light of the situation described in the statement of the Minister for Health to this House on 2 April. As Minister for Veterans' Affairs, I welcome the inquiry and can assure the Committee of both my own and my Department's full co-operation.

APPENDIX 6

Statement by Mr. Justice J.T. Ludeke
Chairman of the Joint Committee on
Pharmaceutical Benefits Pricing Arrangments
11 September 1978

When the Joint Committee adopted the up-dating procedure in April 1977 it thereby introduced a means of ensuring that chemists' remuneration would be established within orderly and equitable guidelines.

On this occasion, although it is acknowledged by all members of the Joint Committee that the actual calculations which lead to an increase in that remuneration are correct, the Government representatives have stated serious doubts which they have concerning the effects of payment in accordance with the agreed procedure. Those doubts do not relate to the procedure but to the results of applying the agreed formula to facts which in the Government representatives view are themselves uncertain.

The Government representatives suggested that when the results of the current Enquiry are known it may become clear that the up-dating procedure had resulted in overpayments to pharmacists and they have called upon the Pharmacy Guild to give an undertaking that in the event of overpayment being established there would be a prompt repayment to the Government of monies overpaid. The Chairman said that this was a serious question and one which in his view should be resolved by the Guild. He considered that the matter should be dealt with by the governing body of the Guild and an answer presented to the Joint Committee no later than the next occasion on which the up-dating was due to be considered which would be in February 1979.

However, so far as the application of the up-dating formula was concerned at the present time, he said that he had no doubt that the procedure which was the subject of a consensus by the Joint Committee should be applied in accordance with the calculations tendered at today's meeting. In regard to these calculations there was no disagreement. He determined an increase of 5 cents per NHS prescription to apply from 1 July 1977 in accordance with the opinion expressed above.

APPENDIX 7

THE PHARMACY GUILD OF AUSTRALIA

MEMORANDUM OF ADVICE

This memorandum confirms advice given in conference with officers of the Pharmacy Guild and my instructing solicitors on the 18th December 1978.

I am asked to advise whether the Commonwealth can recover from the Pharmacy Guild and/or its members any amounts "overpaid" to them for the supply of pharmaceutical benefits after the 1st July 1976 if the 1978 inquiry establishes a lower base from which to calculate increases in costs.

In my opinion amounts paid after the determinations made on the 4th April 1977, the 18th May 1978 and th 11th September 1978 which were paid at prices calculated under those determinations were properly paid and neither the Pharmacy Guild nor its members will be liable to repay any amount on the ground that a lower base than the one used by the Chairman of the Joint Committee is established for the 1st July 1976 by the inquiry.

Section 98B of the National Health Act 1953 (as amended by the National Health Amendment Act (No. 4) 1976) authorizes the Chairman of the Joint Committee to determine the manner in which the Commonwealth price of pharmaceutical benefits is to be ascertained for the purpose of payments to approved pharmaceutical chemists for the supply of pharmaceutical benefits as defined by the Act. The "manner determined" is required to take account of the matters set out in paragraphs (a), (b) and (c) of sub-sec. (1). Sub-sections (4), (5) and (6) qualify the Chairman's power by requiring the Joint Committee first to have considered the matter upon which the determination is made; by requiring a determination to conform to an unanimous recommendation of the Joint Committee; and by directing the Chairman to have regard to deliberations of the Joint Committee. If those requirements are observed, the Chairman's determination is binding. The Minister has no power to reject it. Section 98D requires a determination to be in writing and makes it effective from the date specified in it, being a date not earlier than the 1st July 1976. It is clear from sec. 98D that a determination can have a degree of retroactivity: paragraph (b) speaks of its coming into operation or being "deemed to have come into operation" from the specified date.

The Act does not provide for the making of a determination upon an interim or provisional basis. Further, in my opinion, it does not authorize the alteration of a determination so as to affect the lawfulness of a price at which

payments have already been made. If a payment is properly made at the time of payment, i.e. if it is made at the rate determined at the time and is in respect of goods and services actually supplied, in my opinion a pharmaceutical chemists will be entitled to retain it against the Commonwealth. *See sec. 99(2). Cf.* The Commonwealth v. Burns <1971> V.R. 825. If sec. 98B were to be interpreted as authorizing the Chairman to make a determination purporting to alter the manner in which the Commonwealth price was to be ascertained for a past period which had the effect of reducing the price, in my opinion it would be beyond constitutional power if it were to apply to impose a liabiliity to repay amounts previously paid.

I do not consider that either the Agreement of the 9th March 1978 or the statement in the Pharmacy Guild's position paper "Procedures for Establishing a Correct 1 July 1976 Base" that a retrospective adjustment could be made to the 1st July 1976 if the inquiry figures were to show any under or overpayment affects the legal rights of pharmaceutical chemists to whom payments were made at prices established by the three determinations in 1977 and 1978.

J.D. Merralls.

1104 Owen Dixon Chambers,
Melbourne

22nd December 1978.

APPENDIX 8

Commonwealth Crown Solicitor

21 February 1979

The Director-General of Health,
Department of Health,
P.O. Box 100,
WODEN A.C.T. 2606

National Health Act 1953 - Joint Committee on Pharmaceutical Benefits Pricing Arrangements

I refer to your memorandum 72/5283 of 30 October 1978 concerning the results that could flow from a determination made under sub-section 98B(1) of the National Health Act 1953 ("the Act") that in effect reduces the Commonwealth price of pharmaceutical benefits with retrospective effect.

2. Sub-section 98B(1) of the Act provides for the Chairman of the Joint Committee established under section 98A, when requested as described, to determine the manner in which the Commonwealth price of pharmaceutical benefits is to be ascertained. Payments to approved chemists in respect of supply by them of those benefits is then to be made on that basis. The sub-section provides for the bases of different benefits, and for the addition of fees and other amounts specified in or ascertained in accordance with the determination.

3. It appears from your memorandum that the previous determinations made under that sub-section 98B(1) provided from some retrospectivity of operation, but with increases in the amounts payable as the Commonwealth price of the benefits. In each of those cases an adjustment was made by making lump sum payments to chemists of the difference between the amount payable under the new determination and the amount paid under the previous determination, in respect of the period back to the date on which the new determination came into operation.

4. Your questions and my answers thereto are as follows.

Q.1 Could the Chairman make a determination to apply retrospectively, which would replace a determination he had made previously, and which would lower the amount prescribed in the earlier determination?

5. The effective date of a determination by the Chairman of the Joint Committee is governed by section 98D of the Act. That section provides that a determination shall be in writing and shall come into operation, or be deemed to have come into operation, on such a date, being a date not earlier than 1 July 1976, as is specified in the determination.

6. The reference to a determination being deemed to have come into operation on a date specified in the determination clearly contemplates the possibility of the determination indicating a date of operation that is prior to the date on which it is made. Alternatively, a determination could specify a date that is or is later than the date on which it is made. Section 98D is not limited in its terms to the first or any other determination made after enactment of section 98B and the other relevant sections. Nor does section 98D differentiate between a determination that, in fixing the manner in which the Commonwealth price for benefits is to be ascertained, leads to an increase in that price, and one that leads to a reduction. There would be no doubt that the section must therefore be taken to apply to any determination made under section 98B (or, although not now relevant, section 98C).

7. In my view, the answer to your question is 'Yes".

<u>Q.2</u> If the answer to question 1 is 'yes', what means are open to the Commonwealth to seek recovery of the excess payments made to chemists?

8. I take this question to be directed to the situation described in question 1, in which a determination has the ultimate effect of reducing the Commonwealth price of pharmaceutical benefits with effect from a date prior to that on which it is made. The reference to 'excess payments' would apply to the difference between amounts already paid under the previous determination in the period from the date on which the new determination is deemed to have come into operation, and the amount due in repect of that period under the new determination.

9. There appears to me to be considerable doubt whether the amount of that difference could be recovered by proceedings in a Court. A determination, when duly made and applied as the Act requires, provides a valid and subsisting authority for payment of amounts due under the scheme envisaged in the Act. If that determination is subsequently varied so as to increase the amount due with retrospective effect, then the new authority is properly applied by an adjustment that takes into account payments made at the former rate in the period since the date of operation of the new authority.

10. If the effect of a new determination is to reduce the rate of payment retrospectively, the difficulty arises where payments have already been made under the previous determination in respect of the period since the date on which the new determination is deemed to have come into operation. In the present instance there was clearly no mistake of law that could be regarded as applicable at the time at which the payments were made under the previously existing determination. Indeed, at the time of making payment the determination then in force was a proper statutory authority for those payments and for the entitlement of the payees to recieve the amounts due.

11. I have been unable to find any case in which a Court has had to consider a claim for the recovery of money paid under a statutory determination that was valid and subsisting at that time but which was subsequently affected by a further statutory determination made to apply retrospectively, and without any statutory direction as to the effect on moneys already paid out under the earlier authority.

12. Where no payment has been made under a previous determination in the period since the date on which a new determination is deemed to have come into operation, it is of course proper and necessary to apply the new determination to payments due in respect of that period. In those circumstances, a determination can be applied with retrospective effect as section 98D of the Act allows, whether the effect of the new determination is an increase or decrease in the rate of payments to be made.

13. Where however payments have been made in the period referred to in paragraph 12 under a contemporaneous and valid determination, it appears that any excess of those payments over those due under a later retrospective determination is not recoverable or repayable in the absence of express statutory provisions authorising that action. Where a right of recovery or obligation to repay is not provided in those circumstances by the statute, it would appear to be a necessary inference that the Parliament did not intend to authorise a right or obligation of that nature.

14. It follows, from the comments made in paragraphs 12 and 13, that the time at which a payment of the Commonwealth price of pharmaceutical benefits is made affects the rate at which payment is made or the amount paid. That situation is a necessary consequence of the statutory provisions as they stand.

<u>Q.3</u> Whatever the advice may be on question 1, could the Chairman include in a determination directions as to the method for payments by the Commonwealth of the amount determined, or for the repayment by chemists to the Commonwealth of amounts overpaid, and

particularly, the time in which such payments or repayments are to be made?

15. Section 98B of the Act requires the Chairman, when requested as described, to "determine the manner in which the Commonwealth price of all or any pharmaceutical benefits is to be ascertained for the purpose of payments to approved pharmaceutical chemists...". Clearly the Chairman's function does not extend giving directions on such matters as the method of payment of amounts due to chemists and the time within which those payments may be made. His function is the determination of the manner in which the Commonwealth price of the benefits is to be ascertained. Actual processes of payment are not brought by the Act within his responsibilities.

Q.4 How would the response to questions 1 and 3 differ, if at all, depending on whether or not there was agreement between the members of the Joint Committee on the matters involved?

16. The answer to question 1 would not be affected by any agreement between the members of the Joint Committee as to the powers of the Chairman to make a determination with retrospective effect, which would replace a prior determination and which would in effect reduce the amount payable by the Commonwealth. The powers of the Chairman are as set out in the Act and, particularly as to retrospectivity, section 98D makes specific provision in regard to the indication of the date on which a determination shall come into operation.

17. In regard to the answer to question 3, it would seem that the situation would be as I have commented in paragraph 16. The Chairman's function is to determine a manner in which payments due by the Commonwealth would be ascertained. Further provision, even with the agreement of all members of the Joint Committee, that deal with the matters described in question 3 would be of no binding effect.

18. I will be available to discuss any matters that arise from your consideration of this memorandum, if you so desire.

(J.B. Fisher)
for Crown Solicitor

APPENDIX 9

PHARMACEUTICAL BENEFITS SCHEME - CHEMISTS' REMUNERATION

OPINION

Following upon the 1977-78 Enquiry into fees to be paid by the Commonwealth for the dispensing of prescriptions under the National Health Scheme, it was discovered that an error had occurred in the 1972/73 Enquiry in the translation of approved statistical specifications to be used for allocating labour costs.

This error (made by one of seven members of a programming staff), and the method of updating determinations thereafter has, according to a Ministerial statement, resulted in overpayments to chemists totalling $105 million or $235 million, depending upon whether their remuneration was determined on an "average" or an "economic" pharmacy approach. Although the greater part of the overpayments were made after 1st July, 1976, overpayments prior to that date amounted to $12 million, based on a determination on an "average" pharmacy basis, or $62 million based on a determination on an "economic" pharmacy basis.

I am asked to advise, first, as to whether any of these overpayments are recoverable and, secondly, whether the Chairman of the Joint Committee on Pharmaceutical Benefits Pricing Arrangements could, by determinations made in the future, fix prices of pharmaceuticals at figures which, from a practical point of view, would result in the overpayments eventually being recovered.

Subject to certain exceptions set out by Robert Goff, J., in Barclay Bank Limited v. W.J. Simms, Son & Cooke (Southern) Limited (1980) 2 W.L.R. 218, at p.232, which are not relevant, if money is paid under a mistake of fact, that money can be recovered.

If, moreover, public funds are disbursed other than under parliamentary authority, amounts so disbursed can be recovered back. Auckland Harbour Board v. R. (1924) A.C. 318, The Commonwealth v. Thomson (1962) 1 C.C.R. (Vic) 37; The Commonwealth v. Burns (1971) V.R. 825.

Prior to 1st January, 1977, determinations concerning the rates of payments to chemists were required to be made by the Minister, after consultation with the Pharmacy Guild of Australia, under the then s.99(1) of the National Health Act. In practice, the determinations were normally made by a Department of Health officer under delegation from the Minister, after considering the advice of a non-statutory committee established by the Minister under the authority of s.136 of the Act.

But after 1st January, 1977, the "Joint Committee on Pharmaceutical Benefits Pricing Arrangements" was established by s.98A of the National Health Amendment Act (No. 4) 1976. Section 98B authorises the Chairman of the Joint Committee to determine the manner in which the Commonwealth price of pharmaceutical benefits is to be ascertained for the purpose of payments to approved pharmaceutical chemists for the supply of pharmaceutical benefits as defined by the Act. The manner which is described in subs. (1)(a), (b) and (c) of the section is, in substance, a cost plus profit basis. Subss. (4), (5) and (6) of the section require the Chairman to conform to a unanimous recommendation of the Joint Committee and to have regard to its deliberations but, subject to this, the Chairman's decision is binding on the Commonwealth and the chemists.

By s.98D, any determination is effective from the date specified in it, being a date not earlier than 1st July, 1976 and it is clear from this section that a determination can operate either retrospectively or prospectively; it is to be noted, also, that no provision is contained in the amending Act for any determination, once made, to be altered.

I am of the opinion that overpayments made either before or after 1st July, 1976 cannot be recovered. All such payments were duly made under parliamentary authority; all of them were made deliberately although as a result of a mathematical miscalculation. If Government or anyone in the private sector, in determining how much to pay for property or services makes a miscalculation in reaching such determination, that is not a mistake of fact which enables the recovery of any or portion of the moneys. As to payments made after 1st July, 1976 there is the additional ground that these were payments determined by a statutory authority and their validity cannot be questioned.

I have considerable doubt as to whether the view of the Crown Solicitor expressed in paragraph 4 of his letter of 21st February, 1979, that the Chairman could make a determination to apply retrospectively which would replace a determination he had made previously and which lowered the amount prescribed in the earlier determination, is correct.

But even if a determination could be so made, if one of its purposes were to recover moneys already paid to chemists as a result of an error, such a determination would, in my opinion, be invalid for reasons expressed hereafter.

As to this question, the Committee functions, I think, as a domestic, executive or administrative body entrusted with statutory powers rather than as a legislative body but no matter whether it functions as a legislative authority on the one hand, or a domestic, executive of administrative authority on the other, there is a clear authority in Australia

(although the matter has never been considered in England) that the purposes or motives of a public authority may be investigated in relation to its exercise of legislative authority as well as in relation to its exercise of discretionary powers.

If a determination is not properly made for the purpose for which it was given but beyond the scope or not justified by the instrument creating the power, then the exercise of the power, as a result of taking some ulterior motive into consideration, renders it invalid. Arthur Yates and Company Pty. Limited v. The Vegetable Seeds Committee 72 C.L.R. 37; Brownell's Limited v. The Ironmongers Wages Board 81 C.L.R. 108 and Professor Whitmore, Principles of Australian Administrative Law, 5th edn. As I have indicated, s.98B clearly envisages a determination to be made based on a consideration of costs plus profit. It follows that any determination which took into consideration the fact that chemists had been paid too much in the past would be clearly beyond power and could be successfully attacked.

C.L.D. MEARES

24th June, 1980

MEDIA STATEMENT BY MR JUSTICE LUDEKE, CHAIRMAN, JOINT COMMITTEE ON PHARMACEUTICAL BENEFITS PRICING ARRANGEMENTS

Chemists' Professional Fees Reduced
4 Cents

The Chairman of the Joint Committee on Pharmaceutical Benefits Pricing Arrangements, Mr Justice Ludeke, announced today that chemists' professional fees for dispensing pharmaceutical benefits prescriptions will be reduced by 4 cents from 1 May 1980.

The Joint Committee on Pharmaceutical Benefits Pricing Arrangements comprises four representatives of the Pharmacy Guild of Australia and four Government representatives, under an independent Chairman, Mr Justice Ludeke.

Mr Justice Ludeke said that at the meeting of the Joint Committee held today the members of the Joint Committee had reached a consensus and had made a unanimous recommendation incorporating the following features:

(a) reduction of the level of professional fees by 4 cents from 1 May 1980;

(b) the Joint Committee to conduct an investigation into alternative methodologies to arrive at appropriate rates of remuneration to chemists for the supply of pharmaceutical benefits. An independent group of cost accountancy firms and the Industries Assistance Commission will be asked by the Joint Committee to suggest possible methodologies for this purpose, the cost to be borne by the Government;

(c) future Inquiries to be carried out for the Joint Committee by a mutually agreed independent organisation, at Government cost (as at present);

(d) based on such an Inquiry, the Chairman of the Joint Committee to make a determination to be effective from a mutually agreed date not later than 1 July 1981;

(e) an agreed updating formula to be applied to the figures on which the Chairman bases his determination in (d) above; and

(f) should the Chairman's determination in (d) above show the decrease of 4 cents was not justified, then a retrospective adjustment would be made by the Government to reinstate the 4 cents or part thereof - in any event the Chairman's determination would be accepted by the Guild as the basis for future updating.

Accordingly, as required by the National Health Act, Mr Justice Ludeke determined that professional fees be reduced from $1.35 to $1.31 for ready prepared prescriptions and from $1.95 to $1.91 for extemporaneously prepared prescriptions. The current rates of mark-up (25% for ready prepared and 33-1/3% for extemporaneously prepared prescriptions) are not affected by this determination.

The Joint Committee has already started work on the other matters contained in the recommendation.

9 April 1980

APPENDIX 11

LIST OF RELEVANT DATES RELATING TO ACTION INITIATED BY DEPARTMENT OF VETERANS' AFFAIRS IN RELATION TO THE EXCESS PAYMENTS ISSUE

DATE	EVENT
14-2-80	. Press reference to possible inaccuracy in pricing formula.
	. Briefing note to Minister drafted - held back due to lack of specific confirmation of details.
15-2-80	Contact made with Department of Health Officers informally. Response was excess payments could not be quantified.
18-2-80	. Ministerial brief reviewed.
	. Contact again made with Department of Health - response that excess payments could not be quantified and that estimates were heavily dependent on methodology used.
25-2-80	Minister for Health's submission of 21-2-80 received in Department.
26-2-80	. Best possible estimate of D.V.A. component of excess payment sought - briefing note to Minister updated.
	. Replacement submission of 26-2-80 by Minister for Health - received in Department.
29-2-80	. Replacement submission of 26-2-80 by Minister for Health - received in Division.
	. Briefing note sent to Minister.
	. Health officials contacted. Normal channels of liaison found not to be involved in carriage of this issue.
3-3-80	D.V.A. Ministerial liaison section informed of our interest in decision of Cabinet relating to Minister for Health's replacement submission of 26-2-80. Cabinet expected to meet 4-3-80 and decision expected at D.V.A. 6-3-80.

DATE	EVENT
5-3-80	Inquiries initiated as to legality and means of recovery of any over-payment.
about 10-3-80	Cabinet decision requested through Minister's Office and also Cabinet Office. Informal advice that decision not available but that P.S.B. was conducting a confidential inquiry into 'Excess Payment Issue'.
13-3-80	Discussions as to legality and means of recovery.
18-3-80	Verbal advice of Senior Legal Officer that payments made were not recoverable.
18-3-80	Minister for Health's further submission of 13-3-80 received in Department.
3-4-80	Press reports of Minister for Health's statement in the House on 2-4-80.
?	Hansard for Representatives, 2-4-80, received.
16-4-80	Press inquiries as to fact of an quantum of 'excess payments' in respect of R.P.B.S. Data available insufficient to provide reasonable estimate.
16-4-80) 17-4-80)	Verbal briefings of Minister.
16-4-80) 17-4-80)	Arrangements between Ministers that Health data would be provided.
17-4-80	*Question without Notice by Dr Jenkins.*
17-4-80	Meeting between representatives of Health and Veterans' Affairs. Corrective factors provided and means of further liaison established.
18-4-80	Approach to P.S.B. for copy of report. Advised that copies not available except by personal clearance of Minister for Health.
18-4-80	Basis of calculation of 'excess payments' established. Further data sought from and provided by Health.
19-4-80 (late afternoon)	Draft Ministerial Statement forwarded to Nambour. 'Indicative' costs provided.
18-4-80 (evening)	Calculation of 'excess payments' finalised.
21-4-80	Minister's Statement in House.

APPENDIX 12

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