Appendix 4

POSSIBLE CORPORATE STRUCTURE MODEL

8 February 2000

Mr Terry Barnes
Review Secretary
National Competition Policy Review of Pharmacy Regulation
MDP 93
GPO Box 9848
CANBERRA ACT 2601

Dear Mr Barnes,

NATIONAL COMPETITION POLICY REVIEW OF PHARMACY
Our Ref: PMJ 2227304 SEN

In accordance with your instructions we have examined the Review’s reports, various other documents and have matters raised in conference relating to the current restrictions on pharmacy ownership. The advice following addresses the various consideration regarding types of ownership and their importance and relevance to pharmacy practice.

EXECUTIVE SUMMARY

1. Existing ownership structures should be maintained.
2. The concept of pharmacist controlled ownership entities should be maintained.
3. To provide greater commercial flexibility, pharmacist controlled corporate structures may be more broadly utilised.

STATEMENT OF OBJECTIVES

PHARMACIES

Consistent with its terms of reference and need to examine the competitive status of the industry and profession, the Review has assessed a number of alternative ownership models. It has focused on ownership models which it believes would help to produce a competitive, resilient industry whilst maintaining strong
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professional standards and the ability to deliver community protection and public benefit.

The Review’s report comprehensively raises arguments for and against current restrictions embodied in various legislation controlling the pharmacy industry and profession throughout Australia. In particular current restrictions in pharmacy ownership structures have been addressed.

Relevant Assumptions

Our advice makes the following assumptions, in accordance with the Review’s final report at recommendation 1.3 & 4:

(a) that non-pharmacist ownership and minority share holding (except for permitted bodies corporate in accordance with the SA model) is considered an unworkable option outside existing permitted exceptions (eg friendly societies);

(b) pharmacist ownership and control remains a primary feature of the pharmacy industry and profession;

(c) on adoption the proposed models will ensure that pharmacies can operate in flexible, commercial and uniform agreements across the jurisdictions; and

(d) the restriction on the number of pharmacies owned by any acceptable entity will be removed.

Primary Objectives

We understand that it is a primary objective that ownership of pharmacies (with, of course, existing permitted exceptions) should remain in the control of registered pharmacists. This has been a traditional concept of professional pharmacy practice that helps to ensure high professional standards resulting in protection of the community and hence a net public benefit.

We understand that the Review has made certain recommendations which may have some impact on incoming or newly established ownership structures. The proposals set out in this advice would complement existing ownership arrangements.

It is generally consistent with competition policy, that less regulated ownership models may assist in the promotion of competition within the pharmacy industry and profession. Additionally, the alternatives recommended below would assist in providing the ‘young and/or competent pharmacist’ with an achievable alternative to enter management and ownership of pharmacy practice. It is foreseeable that these proposals should also assist in the growth and development, or retention, of the remote or rural based pharmacy.

A common concern expressed in the submissions and comments received from both pharmacy industry participants and professionals was the possibility of, or nature of corporate ownership and the impact which that may have on the pharmacy industry and profession. The approach taken has been to examine various ownership models within the framework which maintains pharmacist control of pharmacies. We
suggest that this is consistent with ensuring that high professional standards and the consequent net public benefit is retained.

Consistent with the preliminary recommendations of the Review, acceptable ownership vehicles for pharmacies may include the following:

1. Pharmacist Owned Corporate Structure
2. Individual Ownership
3. Partnership

In essence, it is intended that acceptable corporate structures would include only such companies that satisfy requirements such as those in the South Australian legislation; that is, where the shareholders and directors are registered pharmacists or family members of the pharmacist. Here, obviously, the concept of pharmacies being owned or controlled by a pharmacist is maintained.

EQUITY IN THE OWNERSHIP ENTITY

Of the submissions received from the various regulatory bodies affecting the pharmacy industry and profession, the fundamental concern has been that the lifting of restrictions on:-

• the type of ownership; and
• the number of pharmacies which can be owned by a particular entity,

may erode the high level of professional control over pharmacy practice.

In response to these concerns, it is suggested that any ‘manager’, of a pharmacy, owned by an acceptable corporate entity, is required to take a level of personal accountability. That is, pharmacists, who either manage a pharmacy or who are employed to supervise and manage a pharmacy owned by a permitted corporation (a Pharmacist Owner-Manager), would, take ‘equity’ in the ownership structure.

A Pharmacist Owner-Manager may be an employee of the ownership entity, in a management role, and may be nominated by the principal(s) of the company as Pharmacist Owner-Manager. We understand that this concept has been identified and supported by a number of experienced pharmacists.

This suggestion means that every pharmacy (not being one owned by an individual, or partnership) must have at least one Pharmacist Owner-Manager. The outcome of this concept is consistent with ‘one pharmacist-one pharmacy’ principle and also acts as a balance between the need to preserve professional standards and professional conduct on the one hand, and recognition of the entrepreneurial and commercial drive of pharmacists in the industry or profession on the other.

A further benefit is that it would allow the ‘young and/or competent pharmacist’ an opportunity to contribute to the future of the pharmacy industry and profession. The concept of the Pharmacist Owner-Manager would provide many ‘young and/or competent pharmacists’ with an achievable entry point to ownership levels within
any pharmacy. Additionally, with such provisions, a 'young and/or competent pharmacist' may be encouraged to provide fresh and innovative solutions to some of the current challenges in the practice of pharmacy.

We understand that in some submissions received by the Review, concern has been expressed that the pharmacy industry/profession has been prohibitive in providing opportunity to pharmacists who are unable to work in a full-time position. The Pharmacist Owner-Manager concept makes a significant contribution to removing this impediment. It would also benefit the industry and profession as a whole in enabling a wider cross-section of pharmacists to contribute their ideas to the profession, resulting in its growth and development.

It is envisaged that equity in the ownership entity would take the form of acquiring shares in the pharmacist owned proprietary company appropriately constituted.

This proposal stems from the belief that the sharing of professional responsibility would maintain and enhance:

- the current generally high standards of professional conduct the pharmacy industry;
- the pharmacy profession's focus on protecting the public; and
- the value the community places on receiving personal care from pharmacists.

It is also perceived that whilst this suggestion would make a genuine impact on the industry and profession as a whole, it would be particularly effective in ensuring pharmacy industry growth and development including in remote or rural based areas.

The Pharmacist Owner-Manager would have the same potential joint and severable liability for professional misconduct in respect of occurrences in the business in which the pharmacist has equity as though the Pharmacist Owner-Manager was the owner. This must have the effect of promoting awareness, professional responsibility and public protection in delivering pharmacy services.

A pharmacist would of course continue to be subject to the professional requirements under current pharmacy and pharmacist acts, and would continue to be personally accountable for maintaining professional standards.

**Define Pharmacist Owner-Manager**

The Pharmacist Owner-Manager must be a person who has day to day involvement in the particular pharmacy, such that it may equate with the level of interest that an individual owner pharmacist may contribute to his or her own business.

Whilst this is a new concept, which would require detailed definition for effective operation, it is suggested that a pharmacist would be deemed to be a Pharmacist Owner-Manager if he/she was:

- employed to supervise and manage a pharmacy business; and
responsible for staff; and

responsible for the operation of the pharmacy for a minimum period to be determined.

A pharmacist meeting all of these criteria would be required to hold equity in the corporate entity which owns that particular pharmacy.

In meeting the above criteria, any corporate ownership entity conducting a pharmacy must ensure that in respect of that business:

- a Pharmacist Owner-Manager is appointed; and

- at least one Pharmacist Owner-Manager is appointed for each location in which the pharmacy business owned by a corporate entity is operated.

It is proposed that in the suggested pharmacist owned corporate model an appropriate level of equity for a Pharmacist Owner-Manager to hold in the ownership entity should be a minimum of say 10%. Whilst the 10% minimum interest could be generally adopted, the value of the corporate entity may be such that the imposition of a requirement to obtain a minimum 10% equity may be too onerous as a realistic entry point for the ‘young and/or competent pharmacist’. Therefore, it is suggested that a realistic entry point may be that the proposed equity holder should obtain a minimum equity of 10% or $200,000.00 (whichever is the lower).

Whilst these suggestions have been arbitrarily established they provide an appropriate entry level:

(a) to provide a meaningful level of equity and influence in the entity for the Pharmacist Owner-Manager; and

(b) to be at a level which is not prohibitive for young pharmacists who wish to gain access to the ownership of a pharmacy business.

For example, if the value of a pharmacy is approximately $1,000,000.00 a minimum 10% shareholding would be valued at $100,000.00. Such a figure would not be prohibitive for most young pharmacists and would provide a level of entry to business ownership, which is commensurate with the level of entry to ownership of other professional practices.

Alternatively, if the value of a pharmacy company is approximately $5,000,000.00 the Pharmacist Owner-Manager would be required to purchase equity for a minimum investment level of $200,000.00. The ability to increase this equity holding would be the subject of the commercial agreement between the parties.

Whilst it is proposed that there be a minimum of either a 10% equity holding or as much equity as can be obtained for $200,000.00, there would be genuine scope for the parties to agree to increase the percentage holding by the Pharmacist Owner-Manager. It is suggested that this may provide both the 'young and/or competent pharmacist' and the rural pharmacist with a genuine opportunity to obtain control of
his/her business. This would be a commercial and contractual matter for the ownership entity and the pharmacists who control that entity.

If adopted, the 10% or possible $200,000.00 equity requirement would be relevant for all newly established pharmacist owned companies.

However, the actual arrangements for how the entity distributes its equity or enables a change of equity level (subject to a minimum shareholding requirements) would be a matter for the decision of the equity holders and of course the Corporations Law.

Ownership Models

The models for the suggested types of pharmacy ownership are set out below and have also been displayed graphically and are attached.

(a) Pharmacist Owned Corporate Structures

As already discussed, it is considered that control of a pharmacy by a non pharmacist ownership is neither workable or practical. However, to avoid the current anti-competitive regulations of the industry and profession, it is important to ensure that the mechanisms for regulating pharmacy services be developed in a more competitive fashion.

One particular benefit of adopting a corporate ownership model is that the level of personal liability in respect of general commercial arrangements would be limited. That is, for example, in a stock, supply or management agreement, it would be the entity who generally enters into these types of agreements, rather than the individual.

However, any corporate entity would be subject to the Corporations Law, and a pharmacist who is also a director of the pharmacist corporate entity would be required to discharge his/her duties as a director in accordance with the requirements of the Corporations Law.

Pharmacist Owned Corporate Entity – see diagram attached

It is proposed that ownership of a pharmacy, by a pharmacist owned corporate entity, be permitted, provided the entity is consistent with the South Australia model for corporate ownership. The primary features of that model are:

- the directors of the company must be natural persons who are registered pharmacists; and
- no share in the company is to be owned other than by a registered pharmacist or a relative of that pharmacist.

In accepting this model, any opportunity for non-pharmacist share holding in pharmacy owned corporate entities is, of course, prohibited.

In this model an individual pharmacist is responsible for the professional conduct of the business of a pharmacist in one pharmacy, that is, 'one pharmacist- one pharmacy'. This therefore retains the fundamental concept of the 'pharmacist in
control of the pharmacy' without limiting potential for competition and growth with the pharmacy industry and profession.

If a corporate entity is established, it may own more than one pharmacy, provided that each pharmacy has attached to it a Pharmacist Owner-Manager as dealt with in the section above dealing with the Pharmacist Owner-Manager. In consequence of the proposed equity requirement the number of pharmacies owned by a corporate entity would effectively be limited by the recommended requirement that each Pharmacist Owner-Manager have a minimum 10% equity in the ownership vehicle. For example, if the pharmacist owner retains a 30% share in the ownership entity, and each Pharmacist Owner-Manager holds the requisite 10% (or $200,000.00) in the entity, the maximum number of pharmacies which could be owned by the entity would be 8: that is the 7 pharmacies 'managed' by the Pharmacist Owner-Manager plus a pharmacy 'managed' by the pharmacist owner.

It is possible that an individual pharmacist may wish to establish a number of corporate entities, each of which could own a number of pharmacies. However, any establishment of such multiple corporate entities would still be subject to the fundamental requirement that the Pharmacist Owner-Manager in each pharmacy have equity in the ownership vehicle.

This concept, given the proposed requirement for Pharmacist Owner-Managers to hold equity in the ownership entity, maintains the current environment in which the pharmacist is personally responsible for the business of a pharmacist.

It also provides scope for a competitive environment to emerge within the pharmacy industry, within the framework of pharmacist control.

If the only acceptable corporate structure is one in which the directors and the shareholders are pharmacists, direct family members or relatives of the pharmacists, then even in a multiple corporate entity model, the level of pharmacist control is maintained.

In recognition of the level of entrepreneurship which some pharmacists may wish to pursue it may be appropriate to consider an extension of this simple corporate model. This may allow a pharmacist controlled company established in accordance with the South Australian legislation to itself hold shares in a company otherwise owned by pharmacists. That company could then be a shareholder in a second or subsequent company which itself owned a pharmacy, provided that the company was the only shareholder in the subsequent corporate entities not being a registered pharmacist or a family member of a pharmacist. That is, generally the corporate entity must be structured in accordance with the South Australian model except in the situation where company, which meets the requirements of the South Australian model, may itself hold shares in other pharmacy owning companies.

This suggestion simply provides greater commercial flexibility to pharmacists while maintaining the concept of pharmacist control of pharmacy ownership. It is a limited extension to the simple corporate model outlined above. It is also consistent with the Review's recommendations for there to be no restrictions on the number of pharmacies in which a registered pharmacist may hold a proprietary interest.

The control of the company, and consequently the extent to which the Pharmacist-Owner Manager has an effective ownership interest, would depend on the company
structure and the classification of shares and voting rights. There may need to be some requirement, which addresses the structural issues to ensure that the philosophy of ‘equity’ is being delivered.

It must be noted that other than to the extent that the shareholding is to comply with requirements of relevant pharmacy legislation, all other corporate governance issues and matters of record are governed by the Corporation Law which is administered by the Australian Securities & Investment Commission.

(b) Individual Ownership

Ownership of a pharmacy by an individual is not proposed to be effected or changed by any of the suggestions or recommendations in the Report. Where an individual pharmacist personally wishes to acquire an additional pharmacy business he/she may wish to utilise the opportunity to use a simple company structure but if they did not wish to do so the pharmacist could continue to own the business in his/her own right or through a partnership.

(c) Partnerships

We understand that it is not envisaged that any proposed change would affect existing or future partnership arrangements.

Partnerships have been a traditional entity for ownership of pharmacies, and in the past have been an effective structure for the provision of professional pharmacy services to the community. This is consistent with the concept of proprietors being involved in maintaining their own practice.

It is proposed that current requirements relating to partnership would not change including the requirement that a partnership be a partnership of pharmacists only. This is consistent with the philosophy of pharmacies being owned and controlled by pharmacists and consistent with the concept of those individuals being responsible for maintenance of appropriate professional standards in the practice of pharmacy.

Partners in a partnership delivering professional services are personally responsible for the operation of the pharmacy. We assume that these requirements would remain in place.

(d) Ownership – Transition Provisions

It is highly desirable that any recommendations in relation to pharmacy ownership structures should be consistent across all States and Territories of Australia to promote uniformity and consistency across the industry. Such consistency could be promoted by ensuring professional consultation and involvement in developing a final model.

On adoption, we suggest that appropriate transitional and savings provisions would be required to be incorporated in any legislative adjustment. These provisions should include appropriate time frames to accommodate pharmacists complying with the new requirements.
We assume that the new provisions would become effective and enforceable at the time the entity wishes to acquire or establish a new pharmacist owned corporate entity.

Yours sincerely

[Signature]

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<table>
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<th>Proposed Ownership Models</th>
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**Legend**

- M.D.
- P.O.
- Managing Pharmacist
- Pharmacist Owner
- Pharmacy
PHILLIPS FOX

CONTRASTS:

Limit on number of pharmacies in
company
MP must own 10% of shares in
company to be PC controlled (SA mode)

FEATURES:

MP has equity in ownership entity
Company may own one or more pharmacies
Family company, pharmacist controlled

SINGLE COMPANY MODEL
**PHILLIPS FOX**

**FEATURES**
- Limited liability of company.
- MP has equity (shares) in ownership vehicle.
- Co-B.
- Holding company may be used subject to Co V.
- Owners have one number of corporate entities.
- Unlimited number of corporate entities.
- Shareholder other than authorized shareholders in meaning S/V model and Co A being the only.

**CONSTRAINTS**
- Each MP to have minimum of 10% in the adopted (proposed) P.O. to have control of Co V (S/V model to be.

**MULTIPLE CORPORATE ENTITIES**

**CORPORATE OWNERSHIP**
LIMITS INDIVIDUALS TO SINGLE PARTNER
NO ABILITY TO GIVE EQUITY IN OWNERSHIP ENTITY

CONTRAINTS:

NO ENTITY INVOLVED IN OWNERSHIP
PHARMACEUTICAL OWNERSHIP OF PHARMACY

FEATURES:

SINGLE PHARMACIST OWNERSHIP