Pharmaceutical Management Agency
Annual Report

For the year ended 30 June 2011

Presented to the House of Representatives
pursuant to Section 150(3) of the Crown Entities Act 2004

New Zealand Government

PHARMAC
Pharmaceutical Management Agency

CONTENTS

PHARMAC DIRECTORY

(as at 30 June 2011)

Head Office Level 9, Simpl House 40 Mercer Street Wellington	**Postal Address** PO Box 10-254 Wellington Telephone: (04) 460 4990 Facsimile: (04) 460 4995 Website www.pharmac.govt.nz
Board Members Stuart McLauchlan – Chair Kura Denness – Chair, Audit Committee Dr David Kerr Anne Kolbe Jens Meuller	**Chief Executive** Matthew Brougham
Pharmacology & Therapeutics Advisory Committee Prof Carl Burgess – Chair	**Consumer Advisory Committee** Kate Russell – Chair
Auditors Audit New Zealand	**Bankers** ASB Bank Limited
Solicitors Bell Gully	**Insurers** Lumley General Insurance (NZ) Ltd American Home Assurance Company QBE Insurance (International) Ltd

CHAIR'S REPORT

This financial year PHARMAC's decision making on publicly funded medicines in New Zealand resulted in a record number of new subsidised medicines and wider access decisions than in previous years. The value of this decision making has been achieved through an overall increase in the funding available, coupled with effective negotiation and procurement initiatives to maximise positive health outcomes for New Zealanders. An additional 214,603 new patients are estimated to benefit from these decisions over and above those who continue to derive benefits from previous years. This has been achieved within the capped pharmaceutical budget and through working closely with District Health Boards, clinicians, pharmacists, pharmaceutical suppliers and other health sector agencies.

Significant new investments during the year included:

- Levonorgestrel implants – new listing of a long acting form of contraception
- Erlotinib – new listing of treatment for advanced lung cancer
- Atorvastatin – widened access for patients with high cholesterol
- Clopidogrel – widened access to blood thinner for patients at risk of stroke or with heart disease
- Donepezil – new listing of treatment for patients with Alzheimer's disease
- Sunitinib – new listing of treatment for patients with advanced kidney cancer
- Rivaroxaban – new listing of treatment to prevent blood clots after orthopaedic surgery
- Bortezomib – new listing of treatment for patients with multiple myeloma (a type of bone marrow cancer)
- Varenicline – new listing of medicine to aid people trying to give up smoking
- Darunavir – new listing of antiretroviral for multi-drug resistant HIV
- Etravirine – new listing of antiretroviral for multi-drug resistant HIV

PHARMAC's Impacts

PHARMAC has three main areas of impact within New Zealand's health system: access – influence over people's ability to obtain medicines; usage – how people use medicines, and economics and health - helping the health system work more effectively and improving value for money.

Access to medicines

Exceptional Circumstances

Significant progress was made over the year through to completion of the review of Exceptional Circumstances schemes. PHARMAC sought views through a discussion paper circulated widely, before developing a proposal for consultation. This has resulted in the revised 'Named Patient Pharmaceutical Assessment' (NPPA) scheme.

The new scheme has three pathways to funding consideration. It is more permissive, and removes the focus on rarity, instead focusing on unusual clinical circumstances, urgency and seriousness of the patient's clinical condition, and on the overall savings to DHBs for the Hospital Pharmaceuticals in the Community pathway. PHARMAC's expectation is that more patients will have applications made under the new scheme, and that spending will rise as a result. The new scheme is to be introduced from 1 March 2012.

Christchurch earthquakes

New Zealand was stunned when, on the 22 February this year, Christchurch was devastated by a second large earthquake of magnitude 6.3 and continued to be rocked by aftershocks. PHARMAC responded quickly by working alongside the Canterbury Emergency Response Team and the Ministry of Health to design actions to help pharmacists to continue to deliver medicines to patients in the wake of the earthquakes major disruption to infrastructure. These included processes for managing pharmaceutical supplies and distribution, putting in place emergency supply provisions to allow pharmacists to dispense without prescriptions and using the PHARMAC 0800 line as an emergency support line for Christchurch pharmacists.

Consumer Advisory Committee

Membership of the Consumer Advisory Committee (CAC) was refreshed during the year - the Board approved five new members, which meant all the foundation members of the Committee ended their membership. The refreshed membership followed a review of the Committee's Terms of Reference, and brings the committee to nine members. The Board appointed Kate Russell (CEO, Cystic Fibrosis NZ) as Chair of the Consumer Advisory Committee. Anne Fitisemanu (Pacific Cultural Competency Training, Counties Manukau DHB) was appointed the Deputy Chair. CAC continue to work with PHARMAC staff to provide advice on avenues for consumer engagement with medicines issues.

More detailed analysis of our overall impact on access to medicines is provided later in this Annual Report.

Usage

Our Access and Optimal Use work remains a core part of PHARMAC's role. The One Heart Many Lives programme now has a national focus, however its grassroots theme continues with a presence at community days and festivals. Most recently, PHARMAC used One Heart Many Lives as the anchor for a Whānau Hauora Village concept at the 5-day 2011 Te Matatini festival that brought together a range of health agencies to offer health checks. The village concept proved extremely popular, with more than 2500 people visiting during the festival.

PHARMAC has also introduced Space to Breathe, a childhood asthma management programme promoting the best use of asthma inhalers to children and caregivers. This year the programme was run as a pilot in Taranaki using early childhood education centres and kōhanga reo to deliver key campaign messages. Initial evaluation of this strategy led the PHARMAC Board to approve a three year pilot programme using a double-blinded trial format in the west Auckland area.

We continue to investigate new ways of communicating our decision-making processes and their implications. In May this year we collaborated with BPACnz and Mobile Surgical Services on an innovative way to communicate Pharmaceutical Schedule changes to Special Foods. The subsidy changes and wider associated clinical issues were discussed in a very successful live, interactive panel-based session, Prescription Kitchen, screened on Sky TV.

Economics and health

Discretionary Pharmaceutical Fund (DPF)

The Minister agreed to a significant change in pharmaceutical funding budget parameters when deciding that PHARMAC would hold a special fund to help smooth funding decisions across financial years.

The Discretionary Pharmaceutical Fund (DPF) is held by PHARMAC and is used to top up DHB pharmaceutical spending where decisions taken by PHARMAC or unplanned events lead to budget overspend; or to be replenished (up to an agreed maximum) should DHB spending be under budget. This is a shift from the earlier practice where all pharmaceutical funding was held by DHBs. While the DPF represents additional available funding, PHARMAC is still required to manage strictly within the annual pharmaceutical funding budget cap.

Supply issues

We have noticed an increase in the number of times we have had to work with suppliers to ensure ongoing supply of medicines. The most significant issues have been around Special Foods (Ensure and Ensure Plus) and nicotine replacement therapy. The latter was due to an earlier policy change to establish smoke-free prisons. The way stocks are successfully managed is testament to PHARMAC's contracting provisions and close monitoring of supply-chain and contract management issues.

New functions – Hospital medicines and medical devices

After Government reviews of how the health system operates some wider roles for PHARMAC were identified around managing procurement of hospital medicines and medical devices. We have been making steady progress in tackling the development of a national preferred medicines list. Similarly, working with others in the health sector, we are well on the way toward developing a national plan for the management of medical devices and the development of a national catalogue of medical devices; investigating, in the first instance, insulin pumps. Both these projects will continue to be part of our work programme over the next few years.

Our people

David Moore's term on the PHARMAC Board finished in December 2010 – a significant departure given his role in establishing PHARMAC and as inaugural Chief Executive from 1993. David left PHARMAC in 1998, returning as a Director from 2000 to 2010.

The Board was sad to receive Matthew Brougham's resignation in June 2011 with effect from 31 August. Matthew was Chief Executive from 2008 and is moving to a new role with the Canadian Agency for Drugs and Technology in Health. We are truly grateful for his contribution to PHARMAC and the firm foundation and direction with which he guided the organisation.

Stuart McLauchlan
Chair

On behalf of the PHARMAC Board

OVERVIEW OF PHARMAC

PHARMAC is the New Zealand government agency that makes decisions, on behalf of District Health Boards (DHBs), on which medicines are publicly funded in New Zealand and to what level. The core of PHARMAC's role is decision-making which is based on robust processes and analysis, impartiality and integrity. When making its decisions PHARMAC is informed through open consultations, information provided by advisory groups, and rigorous assessment and analysis.

PHARMAC's decisions are far-reaching; they affect the lives of almost every New Zealander in terms of their access to medicines, whether through medicines listed on the Schedule or access to medicines for individuals experiencing exceptional circumstances. As such, these decisions attract high degrees of public and clinical scrutiny. Making robust, evidence-based decisions within a capped budget is central to PHARMAC's processes.

High quality decision-making is essential and PHARMAC's processes have been tested in both the Courts, via judicial review, and by the Ombudsman, via investigations of complaints. PHARMAC has used the outcomes of these reviews and investigations to improve its processes.

PHARMAC's main roles include:

- managing the approx $700m Community Pharmaceutical Budget;
- determining the Pharmaceutical Schedule (the list of Government-funded medicines prescribed and dispensed in the community and the list of pharmaceutical cancer treatments);
- managing Exceptional Circumstance schemes and other special access programmes;
- promoting the best possible (or 'optimal') use of medicines;
- managing national contracts for some medicines and related products used in public hospitals; and
- engaging in research, policy work and support to others in the health sector.

PHARMAC is guided by relevant legislation (including the Public Health and Disability Act and the Crown Entities Act), and current Government expectations, as outlined in relevant Letters of Expectations.

PHARMAC contributes to the Government's goal of a growing, sustainable economy through being part of the New Zealand health and disability system. We contribute to system outcomes of 'supporting New Zealand's economic growth' and 'longer, healthier and more independent lives for New Zealanders' primarily through our contribution to the outcomes defined in Medicines New Zealand – the strategy for the medicines system.

For a more detailed description of PHARMAC's activity, refer to PHARMAC's Information Sheets (www.pharmac.govt.nz/infosheets).

PHARMAC AS A GOOD EMPLOYER

PHARMAC's success depends on high calibre employees and, as a result, recruiting and retaining high performing people is critical. PHARMAC has a range of policies to support this, which encompass good employer principles and obligations. A summary of PHARMAC's good employer obligations, and related activity, is set out below:

Leadership, Accountability and Culture
PHARMAC has the necessary leadership capability, and treat our accountability requirements with high priority. Drawing on internal and external feedback, we continue to build an organisational culture fit for current and future challenges.

Recruitment, Selection and Induction
PHARMAC is an equal opportunities employer and aims to recruit the best person in each case. Vacancies are advertised to attract a range of candidates, according to the type of role. Induction programmes are run for all new staff.

Employee Development, Promotion and Exit
Most PHARMAC roles offer significant levels of autonomy and responsibility. We aim to develop the skills and careers of our employees, including moving within the organisation, acting in more senior roles, external training, support for formal study, and secondments. Our performance management system includes individual and team goals which link to organisational priorities, and includes a focus on individual professional development. All departing employees are offered exit interviews.

Flexibility and Work Design
Provided business needs are met, employees may work flexible hours and at times work remotely. Eleven employees currently work part-time. PHARMAC also offers parental leave entitlements in addition to legal entitlements for both men and women.

Remuneration, Recognition and Conditions
PHARMAC uses independent job evaluation and market remuneration information to set salary ranges for positions. Remuneration is performance-based and pay ranges are reviewed annually with regard to market changes and Government expectations.

Harassment and Bullying Prevention
Conduct and behaviour expectations are clearly communicated through policies and at induction of new employees, and are regularly reinforced. We have policies in place to manage harassment and bullying, and such behaviour is not tolerated.

Safe and Healthy Environment
PHARMAC's health and safety committee includes employee representatives. Information on health and safety responsibilities is included in induction information for new employees. PHARMAC also supports the health of employees through support for fitness-related activities, and the provision of workstation assessments, flu injections and eye tests. The health and safety of our working environment is monitored, including business continuity planning and emergency preparedness.

Staffing
In 2010/11, 6 permanent staff left (10% of total staff). The turnover percentage has increased from the previous year although as our total staff numbers are not high a small increase in actual numbers leaving has a disproportionate effect on the relative turnover. Overall numbers leaving are modest and analysis shows there are no significant organisational "push" factors. Three staff went on parental leave during the year. There has been an increase in recent years in the total number of part-time staff.

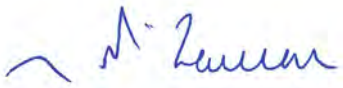
Gender	Part time	Full time	Total
Men	2	27	29
Women	9	27	36
Total	**11**	**54**	**65**

STATEMENT OF RESPONSIBILITY

The Board of PHARMAC accepts responsibility for:

- the preparation of the annual Financial Statements and Statement of Service Performance and for the judgments in them; and
- establishing and maintaining a system of internal control designed to provide reasonable assurance as to the integrity and reliability of financial and non financial reporting.

In the opinion of the Board, the Financial Statements and Statement of Service Performance for the year ended 30 June 2011 fairly reflect the financial position and operations of PHARMAC.



Stuart McLauchlan
Chair

30 September 2011

Kura Denness
Chair, Audit Committee

30 September 2011

PHARMACEUTICAL EXPENDITURE

Key figures

- **$706.1 million** – yearly community pharmaceutical expenditure (on budget)
- **39.7 million** – number of funded prescriptions written (7.0% increase)
- **3.3 million** – number of New Zealanders receiving funded medicines
- **$76.2 million** – amount of savings achieved
- **39** – number of new medicines funded
- **43** – number of medicines with access widened
- **264,452** – estimated number of additional patients benefitting from these decisions in a full year

Community Pharmaceutical Expenditure

PHARMAC's key output is decision-making within the Community Pharmaceutical Budget (Output 1.1); specifically managing expenditure within $710 million for the year to 30 June 2011. The available funding consisted of a DHB allocation of $700 million and up to $10 million from PHARMAC's Discretionary Pharmaceutical Fund (DPF).

Result

The total community pharmaceutical spend by DHBs in 2010/11 was $706.12 million. PHARMAC paid DHBs on 29 June 2011 a total of $6.12 million from the DPF to return the net DHB community pharmaceutical expenditure to $700 million. The residual value of the DPF at year end is reported by PHARMAC as retained earnings of $3.88m, this value remains available for spending on pharmaceuticals in subsequent years. The total community pharmaceutical spend represents an increase of $12.3 million of pharmaceutical spending from the previous year's expenditure. For 2010/11, net spending is made up of gross expenditure of $818.6 million plus $3.4 million of other expenditure, less an estimated $115.8 million expected from suppliers as rebates.

The key drivers of expenditure growth are: $32.2 million net spending increase in the number of prescriptions for subsidised pharmaceuticals filled; and growth associated with new investments and widened access to medicines over the past five years ($46.1 million spending increase). PHARMAC has to work to offset the effect of this continuing volume/mix growth, through savings programmes on currently funded medicines ($56.4 million net savings, plus $11.5 million from the tender). This activity has enabled PHARMAC to continue its track record, since 1993, of effectively managing pharmaceutical expenditure, while increasing access to new and existing medicines.

The following table summarises the factors that have contributed to this increase.

Summary of Community Pharmaceutical Expenditure 2010/11			
	Expenditure ($ million)	**Impact in 2010/11**	**Full year Impact**
Expenditure for year ending 30 June 2010	**$693.8**		
Volume changes			
Volume increases		$43.3	
Volume decreases		-$11.1	
Increased access to medicines already funded		$14.5	
New investments		$11.2	
Growth on new investments 2006/07 to 2009/10		$20.4	
Net volume changes	$78.3		
Subsidy changes			
Subsidy increases		$8.3	$8.4
Subsidy decreases		-$64.7	-$82.5
Savings from annual tenders		-$11.5	-$15.7
Savings from alternative commercial proposals		$0.0	-$0.1
De-listings		$0.2	-$5.4
Residual subsidy increases from 2009/10		$13.3	
Residual subsidy decreases from 2009/10		-$13.6	
Net subsidy changes	-$68.0		
Additional rebates not included above	$2.0		
Total Expenditure for year ending 30 June 2011	$706.1		
Total change from previous year	*$12.3*		

Savings

The breakdown of savings across therapeutic groups is shown below ($ million).

Therapeutic Group	Increase	Saving	Net
Alimentary Tract and Metabolism	$0.06	-$0.19	-$0.13
Blood and Blood Forming Organs	$0.11	-$38.66	-$38.55
Cardiovascular System	$3.85	-$2.55	$1.30
Dermatologicals	$0.25	-$0.02	$0.23
Genito-Urinary System	$0.01	-$0.53	-$0.52
Hormone Preparations - Systemic Excluding Contraceptive Hormones	$0.23	-$0.51	-$0.28
Infections - Agents for Systemic Use	$0.18	-$0.68	-$0.50
Musculo-skeletal System	$1.61	-$6.48	-$4.87
Nervous System	$0.59	-$1.40	-$0.81
Oncology Agents and Immunosuppressants	$0.29	-$4.32	-$4.03
Respiratory System and Allergies	$0.01	-$0.56	-$0.55
Sensory Organs	$0.03	-$0.19	-$0.16
Special Foods	$0.48	-$7.57	-$7.09
Tender	$0.58	-$11.49	-$10.91
Tender ACP	$0.00	-$0.04	-$0.04
EC Expenditure	$0.00	-$1.00	-$1.00
Totals	**$8.28**	**-$76.19**	**-$67.91**

IMPACTS – THE INFLUENCE PHARMAC HAS

PHARMAC's work directly affects the lives of New Zealanders, many of whom rely on medicines to go about their daily lives. PHARMAC is one of many Government agencies that influence the health of New Zealanders. We work alongside others in the health sector to be well informed about evidence-based medicines and we provide assistance to DHBs to achieve wider value for money in other procurement initiatives.

PHARMAC manages the community pharmaceutical budget - a notional budget set aside by DHBs to pay for medicines dispensed in community pharmacies. PHARMAC must manage spending within the budget supplied, however from this year we have the flexibility provided for by PHARMAC's Discretionary Pharmaceutical Fund which enables PHARMAC to take advantage of investment opportunities as well as deal with the sometimes lumpy effects of growth in pharmaceutical usage.

Measuring our impact – the QALY

PHARMAC measures the impact of its decisions using QALYs (quality-adjusted life years). This is an international standard measure that takes into account the impact a pharmaceutical or other medical intervention has on quality and quantity of life.

For example, a person who regularly takes their asthma preventer inhaler as directed not only reduces their small chance of premature death, they also are more able to go about daily tasks such as walking the children to school, doing the housework or paid work. Such factors are all taken into account in the QALY measure.

Impacts

Our work creates impacts, or intermediate outcomes, that contribute to the *Medicines New Zealand* outcomes. We have defined these impacts as:

- Access impacts – our influence over people's ability to obtain medicines
- Usage impacts – how people use medicines, and
- Economic and System impacts – helping the health system work more effectively, and improving value for money.

These impacts are made possible through the day to day work we do – our outputs - which are grouped under the following four classes, which are reported on in full in our Statement of Service Performance (SSP):

Output class	Description	Outputs
1. Decision-making	Work that leads to new medicines being funded and money being saved on older medicines.	1.1. Community Pharmaceutical Schedule 1.2. Pharmaceutical Cancer Treatments 1.3. Hospital Schedule 1.4. Special access panels 1.5. Exceptional Circumstances Schemes 1.6. Schedule Rules 1.7. Medical devices
2. Influencing medicines use	Promoting the optimal use of medicines and ensuring decisions are understood.	2.1. Explaining decisions/ sharing information 2.2. Population Health Programmes

Output class	Description	Outputs
3. Supply management	Ensuring the medicines that are funded are available for patients when they need them.	3.1. Contract management 3.2. Supply vigilance 3.3. Direct distribution
4. Policy, advice and support	Assisting the cohesiveness of the broader health sector.	4.1. Advice and support services to the health sector 4.2. Policy advice

1. Access impacts

This is the influence PHARMAC has over people's ability to have equitable access to medicines.

PHARMAC's decisions to subsidise medicines mean they are affordable for people. Our work in managing contracts and keeping watch on the pharmaceutical supply chain helps ensure medicines are available when people need them. Sometimes when a medicine is funded it is subject to subsidy rules. While these may be seen as an administrative hurdle for clinicians, they do help ensure medicines are targeted to the people who most need them. This helps ensure funded medicines are used cost-effectively.

Information and health education programmes aim to improve people's knowledge of how to obtain funded medicines.

Measuring our impact on access to medicines

	Impact	Aim/target by 2012/13	Progress
1.1	Population health improves as a result of PHARMAC decisions[1]	PHARMAC's decisions lead to: • an overall increase in the number of new patients treated compared with the previous 12 months; and • an increase in the extra life years gained (i.e. QALYs) over their lifetime.	On target. Decisions made in the 2010/11 year are estimated to benefit an additional 214,603 new patients this year. An analysis of the impact of these decisions on QALY gains is reported in a paragraph below.
1.2	The Pharmaceutical Schedule applies consistently throughout New Zealand.	Address all issues of 'Postcode' access, or subsidised medicines not being prescribed in accordance with Schedule rules.	On target. Where we have noted instances of DHBs funding medicines outside of Schedule rules we have highlighted this to DHB planning and funding general managers for audit and compliance purposes.

In 2010/11 PHARMAC listed 39 new medicines in the Schedule and widened access to an additional 43. These are listed in more detail in the section below on economic and system impacts.
We are able to demonstrate that we get better value from pharmaceutical spending, through increasing

[1] Under PHARMAC's mandate to achieve best health outcomes within the funds available, the possible potential numbers of new medicines, new patients, QALY gains, and net savings that can be gained in any year will depend on the mix of funds and investment options (medicines and health needs) available during that year, where increases may be neither necessarily achievable nor desirable in terms of best health outcomes across the population.

effectiveness of medicines and reducing the cost of medicines. PHARMAC assesses additional health gains from these funding decisions. We use cost-utility analysis and measure outcomes in quality adjusted life years (QALYs). This measure enables medicines that perform different functions (such as extending or improving quality of life) to be compared.

Data are available for 28 of the 82 new and widened access medicines to show the impact on people's health. In the first year these medicines were (or will likely be) used by 174,000 patients at a cost of approximately $41.3 million to the Pharmaceutical Schedule (i.e. actual or estimates for 12 months' use following implementation). As these patients keep using the medicines over remaining treatment time spans they may gain consequent improvements in quality of life and/or increased life-expectancy. The new medicines for these patients alone will likely give approximately 4,800 QALYs over remaining treatment time spans more than from standard current treatments, although these extra gains may be as few as 3,800 or as many as 10,700 QALYs (as there is uncertainty with the estimates of individuals' time span gains).

These are health gains over and above those already available through funded medicines. However, note that not all of the funding decisions had QALY information available; therefore it is likely to be an underestimate of the total QALY gains from the funding decisions in 2010/11.

For this financial year's reporting, the QALY estimates have been discounted (that is, future benefits are valued less than present benefits) at 3.5% – PHARMAC's annual discount rate for its economic analyses.

Health gains will occur for other funding decisions as well. Together these gains will provide opportunities for reprioritising funding for other health services.

2. Usage impacts

We want medicines to be prescribed, dispensed and used by patients was well as possible. If medicines are over-, or under- or mis-used, then people miss out on the health benefits the medicines could provide them.

We work to ensure health professionals are well informed about funded medicines and provide services to help clinicians become better informed about evidence-based medicine. This includes funding a set of services currently provided by the Best Practice Advocacy Centre (BPACnz) and running the PHARMAC Seminar Series for health professionals.

Pharmacists play an important role in helping people understand their medicines, and we provide information to support pharmacists to help people adjust to brand changes.

Our Access and Optimal Use programmes and campaigns often include messages promoting access to, and the optimal use of, medicines

Measuring our impact on usage of medicines

	Impact	Aim/target by 2012/13	Progress
2.1	Medicines are not misused, overused or underused.	Evaluations of our Access and Optimal Use programmes and campaigns provide evidence of their impact on use of medicines.	On target. All programmes are designed using a strong evidence-base and evaluated at key decision-points prior to further resource commitment.

3. Economic and system impacts

Helping the health system work more cohesively, providing certainty for government on the costs of pharmaceuticals and assisting DHBs to obtain better value for money.

PHARMAC manages expenditure of community pharmaceutical funds held by DHBs, and through effective negotiations and procurement initiatives reduce their expenditure on pharmaceutical cancer treatments and some hospital medicines. Through our legislative role to manage spending within budget, PHARMAC gives Government and DHBs certainty that this area of spending will be effectively managed. In addition, PHARMAC's work in achieving efficiencies in DHB hospital spending gives DHBs spending options they wouldn't otherwise have. PHARMAC's economic impact supports the government's overall fiscal management through tight budgetary control. At a time of fiscal restraint and tight budgets, PHARMAC's contribution is increasingly important.

Our work has meant that, since 2000, PHARMAC's activities have saved District Health Boards a cumulative total of more than $4.7 billion. This estimate is based on pharmaceutical prices in 1999 mapped onto actual prescribing activity, and compares actual spending with what would have happened had PHARMAC taken no action. By 2010, the difference in that year alone was $937 million. If not for PHARMAC, this funding would have had to come from other areas of health spending. In short, PHARMAC's work gives District Health Boards funding choices they wouldn't otherwise have.

Measuring our contribution to economic and system impacts

	Impact	Aim/target by 2012/13	Progress
3.1	Pharmaceutical spending is effectively managed.	Community pharmaceutical expenditure is within budget.	On target. Of the $710 million total funds available, DHBs spent $700 million and PHARMAC spent $6.12 million from the Discretionary Pharmaceutical Fund.
		Expenditure on pharmaceutical cancer treatments (PCT) is managed.	On target. Expenditure for the 2010/11 year is estimated to be within available DHB funds. New investments for erlotinib and bortezomib have a gross expenditure in 2010/11 of $2.5 million. Access was widened to capecitabine, rituximab, temozolomide, gemcitabine, and thalidomide.
3.2	Improved value for money across the health sector.*	All major PHARMAC decisions include estimates of: • The cost-effectiveness of new investments**, for those investments where QALYs have been estimated; and/or • The percentage offsets of savings to the health sector by new investments, as a proportion of the gross new expenditure on those pharmaceuticals, for those investments where savings have been estimated.	Achieved. Decisions implemented in 2010/11 are estimated to involve gross pharmaceutical spending of $44.6 million. Other impacts across the health sector, through PHARMAC's decisions implemented in this financial year, have resulted in further savings of $1.8 million. A summary of cost effectiveness data is provided in the graph below.

* these measures do not have specific targets assigned. This is because, under PHARMAC's mandate to achieve best health outcomes within the funds available, the possible cost effectiveness and percentage savings that can be gained in any year will depend on the mix of funds and investment options (medicines and health needs) available during that year.
** the cost-effectiveness of new investments is estimated using the net costs to the health sector (which subtracts [savings from reduced spending on other pharmaceuticals and/or DHB services] from [the gross new expenditure on the pharmaceuticals themselves]) and associated QALY gains

New Listings					
Month started	Funding decision	Condition treated	No. new patients in 2010/11	Estimated no. new patients in first year	Estimated cost in first year
July 2010	potassium iodate	iodine deficiency in pregnancy	33,000	33,000	$230,000
	isotretinoin	acne	7,600	7,600	$200,000
August 2010	hydrocortisone with cinchocaine	haemorrhoids	9,200	10,000	$240,000
	insulin glulisine	diabetes	250	270	$48,000
	levonorgestrel implants	contraception	8,800	9,600	$1,500,000
	tamsulosin	prostate disorders	1,100	1,200	$34,000
September 2010	cephalexin monohydrate	antibacterial	7,000	8,400	$140,000
	lignocaine	anaesthetic	1,000	1,300	$180,000
	meloxicam	haemophilic arthropathy (inflammed joints due to bleeding in haemophilia)	38	46	$2,400
	sodium bicarbonate	kidney failure	4,900	5,900	$60,000
	tenoxicam	pain relief	17,000	21,000	$510,000
	zoledronic acid	osteoporosis and Paget's disease	1,700	2,000	$1,200,000
October 2010	adapalene	acne	11,000	15,000	$470,000
	deferiprone	iron overload	19	25	$95,000
	erlotinib	cancer treatment	170	220	$2,400,000
November 2010	darunavir	HIV/AIDS	43	65	$510,000
	donepezil	Alzheimer's disease	3,600	5,400	$120,000
	etravirine	HIV/AIDS	26	39	$190,000
	sunitinib malate	renal cell carcinoma	95	140	$3,200,000
	varenicline	smoking	23,000	35,000	$9,000,000
December 2010	escitalopram	major depression	3,700	6,300	$74,000
	gemfibrozil	cholesterol	270	460	$13,000
	moxifloxacin	multidrug resistant mycobacterial infections	53	91	$110,000
	Eight oral liquid preparations	for preparing compounded pharmaceuticals	4,200	7,300	$47,000
	rivaroxaban	venous thromboembolism prophylaxis following orthopaedic surgery	230	390	$89,000
	sertraline	major depression	2,400	4,200	$30,000
February 2011	caffeine citrate	preterm apnoea	10	24	$2,500
	potassium citrate	recurrent calcium oxalate kidney/bladder stones	26	62	$10,000
	sodium chloride 7%	cystic fibrosis and bronchiectasis	180	440	$56,000
May 2011	bortezomib	cancer treatment	90	540	$4,400,000
	lacosamide	epilepsy	16	96	$44,000
	modafinil	narcolepsy	9	54	$14,000
Total			**140,725**	**176,162**	**$25,218,900**

widening access					
Month started	Funding decision	Condition treated	No. new patients in 2010/11	Estimated no. new patients in first year	Estimated cost in first year
July 2010	Antiretrovirals: • zidovudine [AZT] with lamivudine • efavirenz • abacavir sulphate with lamivudine • raltegravir potassium	hiv/aids	n. avail	n. avail	n. avail
	domperidone	nausea	1,000	1,000	$30,000
	hormone replacement therapy patch (oestradiol)	oestrogen deficiency	n. avail	n. avail	n. avail
	octreotide	malignant bowl obstruction and acromegaly	22	22	$900,000
August 2010	insulin glargine	type 1 diabetes	1,800	1,900	$1,200,000
September 2010	acarbose	type 2 diabetes	900	1,100	$84,000
	Anxiolytics: • diazepam • oxazepam • lorazepam • alprazolam • buspirone hydrochloride	anxiety	3,400	4,100	$90,000
	atorvastatin	Cardiovascular risks (from dyslipidaemia)	53,000	63,000	$12,000,000
	clopidogrel	cardiovascular risk	3,700	4,500	$200,000
	fentanyl patches	pain	410	490	$130,000
	ibuprofen (long-acting)	pain	n.avail	n.avail	n.avail
	sedatives and hypnotics: • lormetazepam • nitrazepam • temazepam • triazolam • zopiclone • midazolam	anxiety and insomnia	6,700	8,000	$110,000
October 2010	capecitabine	cancer treatment	19	25	$140,000
	ezetimibe	cholesterol absorption inhibitor	1,900	2,600	$860,000
	mianserin	major depression	10	13	$8,700
	mycophenolate	cytotoxic immunosuppressant	100	130	$130,000
	rituximab	cancer treatment	n.avail	n.avail	n.avail
	tenofovir	Hepatitis B	7	9	$25,000
	travoprost	glaucoma	200	260	$44,000
November 2010	adalimumab	autoimmune disease	n.avail	n.avail	n.avail
	etanercept	autoimmune disease	180	270	$2,900,000
	levetiracetam	epilepsy	480	720	$250,000

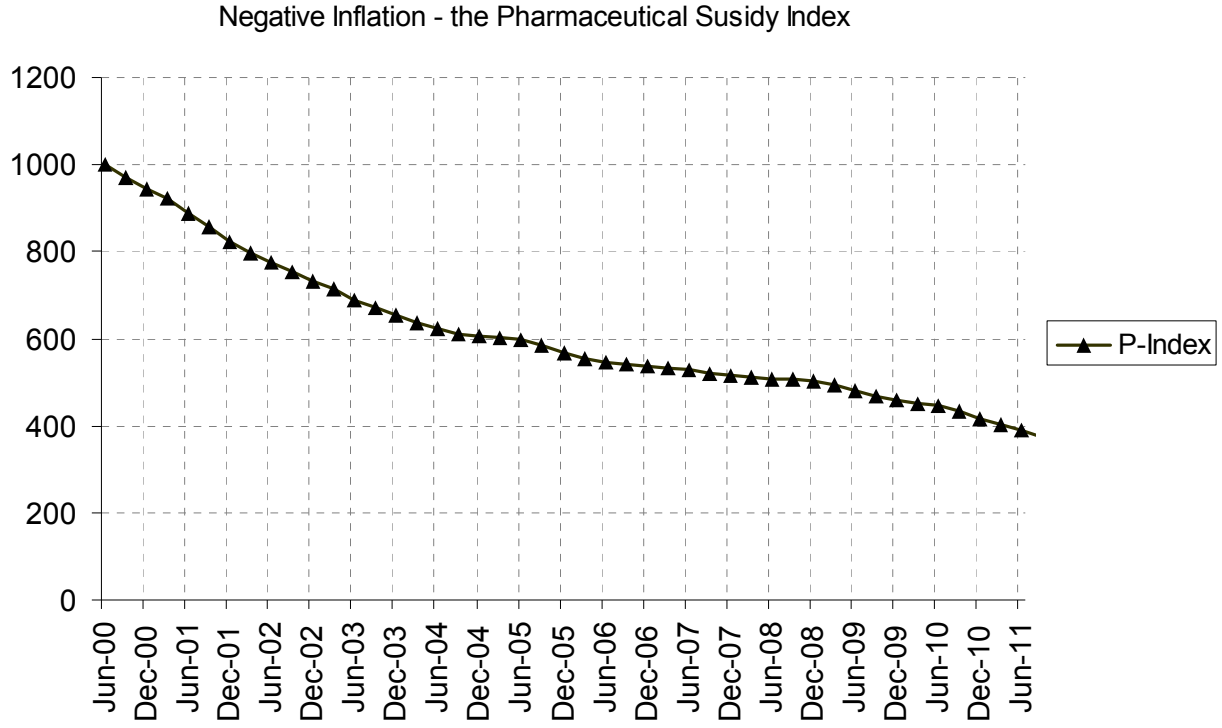
December 2010	multiple sclerosis treatments: • interferon beta-1-alpha • interferon beta-1-beta • glatiramer acetate	multiple sclerosis	n.avail	n.avail	n.avail
	temozolomide	cancer treatment	n.avail	n.avail	$110,000
March 2011	gemcitabine	cancer treatment	43	130	$130,000
	sildenafil	neonates with pulmonary arterial hypertension neonates with Fontan repair. Pulmonary arterial hypertension secondary to chronic lung disease. Pulmonary arterial hypertension secondary to congenital diaphragmatic hernia	7	21	$68,000
May 2011	thalidomide	cancer treatment	n.avail	n.avail	n.avail
June 2011	olanzapine	antipsychotic medication	n.avail	n.avail	n.avail
	sumatriptan injection	severe refractory migraine	n.avail	n.avail	n.avail
Total			**73,878**	**88,290**	**$19,409,700**
Overall Total			**214,603**	**264,452**	**$44,628,600**

Note: Estimated patients and costs in the first year are by 12 months' implementation.

Total full financial year sector impact estimate for 2010/11 is savings of $1,800,000. Sector impact describes the fiscal impact of each decision on health sector costs other than pharmaceuticals. These include such cost increase factors as increases in dispensing fees, diagnostic tests or infusion services. Cost savings can include reductions in home care, infusion services or diagnostic tests.

Graph showing reduced pharmaceutical prices

Pharmaceutical prices are continuing to trend downwards, as illustrated by the graph below (including rebates).



Number of out of stocks

PHARMAC works alongside pharmaceutical suppliers and actively tracks stock levels to ensure continued uninterrupted medicine supply to New Zealand patients. This includes regular information from suppliers on stock supply issues that may require PHARMAC to seek other suppliers or take other remedial action. Stock management is also covered in contracts with suppliers, with minimum stock holding periods required and liquidated damages and indemnities for failure to supply.

In managing delicate stock issues, it is important that any communication is well planned as it can inadvertently lead to stock outages through creating a 'run' on stock.

During 2010/11 the most significant supply management issue was the supply of products from Canadian manufacturer Apotex. This arose as a result of a voluntary import ban by Apotex after problems were found at two of its Canadian factories. These supply issues have now largely been resolved. Supply issues covered a range of products and different strategies were used to manage the stock issues. These included:

- Using Close Control to ration stock;
- Sourcing alternative brands; and
- Providing advice to clinicians on potential alternatives.

Other major stock supply issues during the year included:

- **Special Foods** – (multiple suppliers) changes in the listing criteria of special foods created changes in the demand for certain special foods and resulted in low stock levels.

- **Cefaclor** – Sandoz were unable to supply their brand of Cefaclor from November 2010, alternative supply was obtained from Douglas Pharmaceuticals.

- **Novartis Consumer's Nicotine Replacement Therapy (Habitrol**) - stock levels continue to be closely monitored due to an increase in demand as a result of prisons going smoke-free from 1 July 2011.

- **Ebewe Products** – PHARMAC staff continue to proactively monitor the stock levels of Ebewe products. Sandoz staff send a report to PHARMAC staff each week.

Independent Auditor's Report

To the readers of the Pharmaceutical Management Agency's financial statements and statement of service performance for the year ended 30 June 2011

The Auditor-General is the auditor of the Pharmaceutical Management Agency (Pharmac). The Auditor-General has appointed me, Kelly Rushton, using the staff and resources of Audit New Zealand, to carry out the audit of the financial statements and statement of service performance of Pharmac on her behalf.

We have audited:

- the financial statements of Pharmac on pages 22 to 44, that comprise the statement of financial position as at 30 June 2011, the statement of comprehensive income, statement of movements in public equity and statement of cash flows for the year ended on that date and notes to the financial statements that include accounting policies and other explanatory information; and
- the statement of service performance of Pharmac on pages 17 to 19.

Opinion

In our opinion:

- the financial statements of Pharmac on pages 22 to 44:
  - comply with generally accepted accounting practice in New Zealand; and
  - fairly reflect Pharmac's:
    - financial position as at 30 June 2011; and
    - financial performance and cash flows for the year ended on that date.
- the statement of service performance of Pharmac on pages 17 to 19:
  - complies with generally accepted accounting practice in New Zealand; and
  - fairly reflects, for each class of outputs for the year ended 30 June 2011, Pharmac's
    - service performance compared with the forecasts in the statement of forecast service performance for the financial year; and
    - actual revenue and output expenses compared with the forecasts in the statement of forecast service performance at the start of the financial year.

Our audit was completed on 30 September 2011. This is the date at which our opinion is expressed.

The basis of our opinion is explained below. In addition, we outline the responsibilities of the Board and our responsibilities, and we explain our independence.

Basis of opinion

We carried out our audit in accordance with the Auditor-General's Auditing Standards, which incorporate the International Standards on Auditing (New Zealand). Those standards require that we comply with ethical requirements and plan and carry out our audit to obtain reasonable assurance about whether the financial statements and statement of service performance are free from material misstatement.

Material misstatements are differences or omissions of amounts and disclosures that would affect a reader's overall understanding of the financial statements and statement of service performance. If we had found material misstatements that were not corrected, we would have referred to them in our opinion.

An audit involves carrying out procedures to obtain audit evidence about the amounts and disclosures in the financial statements and statement of service performance. The procedures selected depend on our judgement, including our assessment of risks of material misstatement of the financial statements and statement of service performance, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to Pharmac's preparation of the financial statements and statement of service performance that fairly reflect the matters to which they relate. We consider internal control in order to design audit procedures that are appropriate in the circumstances but not for the purpose of expressing an opinion on the effectiveness of Pharmac's internal control.

An audit also involves evaluating:

- the appropriateness of accounting policies used and whether they have been consistently applied;
- the reasonableness of the significant accounting estimates and judgements made by the Board;
- the adequacy of all disclosures in the financial statements and statement of service performance; and
- the overall presentation of the financial statements and statement of service performance.

We did not examine every transaction, nor do we guarantee complete accuracy of the financial statements and statement of service performance. We have obtained all the information and explanations we have required and we believe we have obtained sufficient and appropriate audit evidence to provide a basis for our audit opinion.

Responsibilities of the Board

The Board is responsible for preparing financial statements and a statement of service performance that:

- comply with generally accepted accounting practice in New Zealand;
- fairly reflect Pharmac's financial position, financial performance and cash flows; and
- fairly reflect its service performance.

The Board is also responsible for such internal control as is determined necessary to enable the preparation of financial statements and a statement of service performance that are free from material misstatement, whether due to fraud or error.

The Board's responsibilities arise from the Crown Entities Act 2004 and the New Zealand Public Health and Disability Act 2000.

Responsibilities of the Auditor

We are responsible for expressing an independent opinion on the financial statements and statement of service performance and reporting that opinion to you based on our audit. Our responsibility arises from section 15 of the Public Audit Act 2001 and the Crown Entities Act 2004.

Independence

When carrying out the audit, we followed the independence requirements of the Auditor-General, which incorporate the independence requirements of the New Zealand Institute of Chartered Accountants.

Other than the audit, we have no relationship with or interests in Pharmac.

K M Rushton
Audit New Zealand
On behalf of the Auditor-General
Wellington, New Zealand

Matters relating to the electronic presentation of the audited financial statements

This audit report relates to the financial statements of the Pharmaceutical Management Agency (Pharmac) for the year ended 30 June 2011 included on PHARMAC's website. PHARMAC's Board is responsible for the maintenance and integrity of PHARMAC's website. We have not been engaged to report on the integrity of PHARMAC's website. We accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website.

The audit report refers only to the financial statements named above. It does not provide an opinion on any other information which may have been hyperlinked to or from the financial statements. If readers of this report are concerned with the inherent risks arising from electronic data communication they should refer to the published hard copy of the audited financial statements as well as the related audit report dated 30 September 2011 to confirm the information included in the audited financial statements presented on this website.

Legislation in New Zealand governing the preparation and dissemination of financial information may differ from legislation in other jurisdictions.

STATEMENT OF SERVICE PERFORMANCE

This Statement of Service Performance (SSP) records how PHARMAC has performed against measures outlined in its 2010/11 Statement of Intent (SOI).

PHARMAC has four output classes:
Output class 1: decision-making
Output class 2: Influencing medicines use
Output class 3: supply management
Output class 4: policy, advice and support

Note that not all outputs are measured and reported on. The Statement of Comprehensive Income provides the actual revenue and expenses incurred compared with budget.

Output class 1: Decision-making

Impact	Output		2010/11 measures	Results
Access Economic and system	1.1	Community pharmaceutical Schedule decisions.	Support the Pharmacology and Therapeutics Advisory Committee through holding a minimum four meetings.	Achieved. PTAC had five meetings in total. PTAC held its regular one and a half day meetings in August and November 2010, February and May 2011. An additional teleconference meeting was held in March 2011
			All funding applications subject to economic analysis, typically cost utility analysis (including an assessment of clinical evidence).	Achieved. During the 2010/11 year 64 new or updated cost utility analyses were completed.
			Decisions on >90% of line items (excluding bids held open while awaiting Medsafe registration) made within 6 months of the tender closing.	Partially achieved. Decisions had been made on 85% of line items (excluding bids held open while awaiting Medsafe registration or patent expiry) within six months of the tender closing. Some decisions were intentionally held until July as they involved price increases and would therefore have a fiscal impact that could be better accommodated within the following financial year.
Access Economic and system	1.5	Exceptional Circumstances Scheme decisions.	Complete a review of Exceptional Circumstances.	Achieved. The review of Exceptional Circumstances was completed in June 2011, with the Board decision to implement its Named Patient Pharmaceutical Assessment process in March 2012.

Output class 2: Influencing medicines use

Impact	Output		2010/11 measure	Results
Access Usage	2.1	Explaining decisions/ sharing information.	Implement Forum workplan within business as usual.	Achieved. Regional PHARMAC Forums planned for September and October 2011. Consumer Advisory Committee advised on plan for obtaining consumer input into the Regional Forums. National PHARMAC Forum is planned for 17 February 2012.
Access Usage	2.2	Population health programmes.	Programme / Campaign evaluations demonstrate effectiveness against specific campaign measures.	Achieved. The consumer focussed generic medicine campaign pilot was presented to the Board in October 2010. This pilot showed that television adverts via Health TV, posters and pharmacy bags demonstrated good recall among consumers and were effective mechanisms for helping to ease concerns with consumers. The Board approved these to be used annually to support supply side changes. An evaluation of the He Rongoā Pai – He Oranga Whānau programme was presented to the Board in February 2011. The evaluation showed the programme meets its target outcomes: • strengthened stakeholder engagement with Māori communities; and • improved Māori health outcomes through access to, and optimal use of, medicines. The Board approved funding for the programme for a further three years.

Output class 3: Supply management

Impact	Output		2010/11 measure	Results
Economic and system	3.1	Contract management.	Monitor DHB hospital compliance with restricted brand contracts. Provide a report to DHBs and pharmaceutical suppliers by 31 December 2010.	Achieved. All DHB hospitals received reports on compliance with restricted brand contracts by 31 December 2010. All pharmaceutical suppliers received reports on DHB hospitals' compliance with restricted brand contracts by 31 December 2010.
			All rebates due are collected.	Achieved.
Access Usage Economic and system	3.3	Direct distribution.	Manage stock to reduce wastage and ensure that low volume high cost medicines are available when needed.	Achieved. All stocks were used before additional supplies were sent and patients received supplies when needed.

Output class 4: Policy, advice and support

Impact	Output		2010/11 measure	Result
Economic and system	4.1	Advice and support services to the health sector.	Assist DHBs with pharmacy contracting when requested.	Achieved. PHARMAC worked in partnership with DHBs on issues related to the pharmacy contract, including the role of Close Control in the proposed new community pharmacy services agreement.
Economic and system	4.2	Policy advice.	Provide comment on all relevant policies and papers as requested by sector agencies.	Achieved. PHARMAC provided input into relevant policies and papers as requested by sector agencies. Examples include: • consultation on the Pharmacy Council's Proposed Pharmacist Prescriber Scope of Practice • consultation on the Researched Medicines Industry Association of NZ Code of Conduct. • DHB pharmaceutical budget holding initiatives • Ministry of Health: consultations on Medicines Regulations changes, Nurse Prescribing in Diabetes Services, Medicines Recall Review; Cabinet report-back on devices; Cabinet report-back on vaccines; Government response to Health Select Committee report on the New Zealand Environment for Clinical Trials; development of a Natural Health Products Bill; and changes to the Medicines Act 1981 • Government Review of Expenditure on Policy Advice • Minister of Finance consultation on the rules on capital charge

LEGAL RISK FUND

In performing its functions, PHARMAC also used its legal risk fund. This fund can be used to initiate or defend legal action PHARMAC is a party to. The PHARMAC Board is responsible for approving access to PHARMAC's legal risk fund on the basis of defined rules.

The existence of a legal risk fund recognises high litigation risk associated with the activity of a government agency (evidenced by PHARMAC's litigation history). The size and regularity of litigation can be unpredictable and may extend beyond the level of litigation activity a government agency can manage within normal, year-to-year resourcing. A fund can help better manage litigation risk through being able (and without delay) to commence or continue with major or complex legal proceedings.

The legal risk fund was accessed for two litigation actions during 2010/11, both of which related to patent litigation activity.

In the year to 30 June 2011, spending from the Legal Risk Fund was $94,438.

The balance of the Fund stands at $6,292,868 at year end.

DISCRETIONARY PHARMACEUTICAL FUND

The 2010/11 Output Agreement between the Minister of Health and PHARMAC included the provision for establishment of a multi-year fund called the 'Discretionary Pharmaceutical Fund' (DPF). The purpose of the DPF is to enable PHARMAC to take advantage of investment opportunities that might not otherwise be able to be funded in that year, as well as deal with the sometimes lumpy effects of growth in pharmaceutical usage.

The DPF is shown in PHARMAC's 2010/11 Output Agreement with a starting value of $10 million. The establishment funding was made from within the $710 million overall provision for community pharmaceuticals in 2010/11, resulting in DHBs having a community pharmaceutical expenditure target of $700 million.

The total community pharmaceutical spend by DHBs in 2010/11 was $706.12 million. PHARMAC paid DHBs on 29 June 2011 a total of $6.12 million from the DPF. This payment enabled the net DHB community pharmaceutical expenditure to return to the agreed level of $700 million. The residual value of the DPF at year end is reported by PHARMAC as retained earnings of $3.88m.

HERCEPTIN SOLD TRIAL FUND

The Herceptin SOLD trial is an international research trial examining whether the nine week or twelve month duration of Herceptin offers a better treatment. The trial is headed by Professor Heikke Joennsuu of the University of Helsinki in Finland. In February 2007 PHARMAC contracted to contribute $3.2 million over at least ten years towards the trial costs. The PHARMAC Board established a fund in 2009/10 to ensure PHARMAC could meet its contractual obligations over future years. The fund is noted in the 2010/11 Output Agreement.

In the year to 30 June 2011, spending from the Herceptin SOLD trial fund was $425,000.

The balance of the Fund stands at $1,803,000 at year end.

INTERESTS

Section 68(6) of the Crown Entities Act 2004 requires the Board to disclose any interests to which a permission to act has been granted, despite a member being interested in a matter. Below are the relevant disclosures:

Member	Details of the Interest	Permission granted by	Conditions of permission	Revocation/Changes to Permission
Anne Kolbe	Disclosed a conflict of interest with Space to Breathe, due to her role with the University of Auckland, the owner of the preferred provider.	Board	The Board decided she may participate in discussions but not in decision making.	The permission granted was a one-off dispensation for the Board meeting in question.
David Moore	Disclosed a conflict of interest with Pfizer bundle proposal (venlafaxine, etanercept, varenicline and sunitinib) and changes to adalimumab access criteria due to potential benefit to a family member.	Board	The Board decided he may participate in discussions but not in decision making.	This determination was for the Board meetings in question.
Richard Waddel	Disclosed a conflict of interest regards Special Foods as a family member was involved in submitting on the consultation.	Board	The Board decided he may participate in discussions but not in decision making.	This determination was for the Board meetings in question.
Kura Denness	Disclosed a conflict of interest regarding primary care developments as the Chair of Hauora Taranaki PHO.	Board	The Board noted the conflict of interest and determined she would be absent for PHO discussions.	This determination was for the Board meetings in question.
David Kerr	Disclosed a conflict of interest as the Chairman of Ryman Healthcare, with regard to Special Foods.	Board	The Board noted the conflict of interest and determined that he would not participate in discussions involving Special Foods in rest homes.	This determination was for the Board meetings in question.

STATEMENT OF ACCOUNTING POLICIES

Reporting entity

These are the financial statements of the Pharmaceutical Management Agency (PHARMAC), a Crown entity in terms of the Crown Entities Act 2004. PHARMAC acts as an agent of the Crown for the purpose of meeting its obligations in relation to the operation and development of a national Pharmaceutical Schedule.

PHARMAC has designated itself as a public benefit entity for the purposes of New Zealand Equivalents to International Financial Reporting Standards (NZ IFRS). The financial statements of PHARMAC are for the year ended 30 June 2011. The financial statements were authorised by the Board of PHARMAC on 30 September 2011.

Basis of Preparation

The financial statements of PHARMAC have been prepared in accordance with, and comply with:

- New Zealand generally accepted accounting practices (NZ GAAP)
- requirements of the Crown Entities Act 2004 and the New Zealand Public Health and Disability Act 2000, and
- New Zealand equivalents to International Financial Reporting Standards (NZ IFRS), as appropriate for public benefit entities.

The financial statements have been prepared on an historical cost basis, and are presented in New Zealand dollars (rounded to the nearest thousand dollars ($000)), being the functional currency of PHARMAC.

Changes in Accounting Policies

The accounting policies set out below have been applied consistently to all periods presented in these financial statements.

Early adopted amendments to standards

The following amendments to standards have been early adopted:

NZ IFRS 7 Financial Instruments: Disclosures, the effect of early adoption of these amendments is the following information is no longer disclosed:

- the carrying amount of financial assets that would otherwise be past due or impaired whose terms have been renegotiated; and

- the maximum exposure to credit risk by class of financial instrument if the maximum credit risk exposure is best represented by their carrying amount.

Standards, amendments and interpretations issued that are not yet effective and have not been early adopted

Standards, amendments and interpretations issued but not yet effective that have not been early adopted, and which are relevant to PHARMAC, include:

NZIFRS 9 Financial Instruments will eventually replace NZIAS 39 Financial Instruments: Recognition and Measurement. NZ IAS 39 is being replaced through the following 3 main phases: Phase 1 Classification and Measurement, Phase 2 Impairment Methodology, and Phase 3 Hedge

Accounting. Phase 1 has been completed and has been published in the new financial instrument standard NZ IFRS 9. NZ IFRS 9 uses a single approach to determine whether a financial asset is measured at amortised cost or fair value, replacing the many different rules in NZ IAS 39. The approach in NZ IFRS 9 is based on how an entity manages its financial instruments (its business model) and the contractual cash flow characteristics of the financial assets. The financial liability requirements are the same as those of NZIAS 39, except for when an entity elects to designate a financial liability at fair value through the surplus/deficit. The new standard also requires a single impairment method to be used, replacing the many different impairment methods in NZ IAS 39. The new standard is required to be adopted for the year ended 30 June 2014. PHARMAC has not yet assessed the effect of the new standard and expects it will not be early adopted.

NZIAS 24 Related Party Disclosures (Revised 2009) replaces NZIAS 24 Related Party Disclosures (Issued 2004) and is effective for reporting periods commencing on or after 1 January 2012. The revised related party standards:

i. Removes the previous disclosure concessions applied by PHARMAC for arms-length transactions between PHARMAC and entities controlled or significantly influenced by the Crown. The effect of the revised standard is that more information is required to be disclosed about transactions between PHARMAC and entities controlled or significantly influenced by the Crown.

ii. Provides clarity on the disclosure of related party transactions with Ministers of the Crown. Further, with the exception of the Minister of Health, PHARMAC will be provided with an exemption from certain disclosure requirements relating to transactions with other Ministers of the Crown. The clarification could result in additional disclosures should there be any related party transactions with Ministers of the Crown.

iii. Clarifies that related party transactions include commitments with related parties.

Revenue

Revenue is measured at the fair value of consideration received.

Revenue Crown

Revenue earned from the supply of outputs to the Crown is recognised as revenue when earned.

Interest

Interest income is recognised using the effective interest method.

Leases

Operating leases

An operating lease is a lease that does not transfer substantially all the risks and rewards incidental to ownership of an asset. Lease payments under an operating lease are recognised as an expense on a straight-line basis over the lease term.

Financial Instruments

Financial assets and financial liabilities are initially measured at fair value plus transaction costs unless they are carried at fair value through profit or loss in which case the transaction costs are recognised in the statement of comprehensive income.

Cash and Cash Equivalents

Cash and cash equivalents include cash on hand, deposits held at call with banks both domestic and international, other short term, highly liquid investments, with original maturities of three months or less and bank overdrafts.

Debtors and Other Receivables

Debtors and other receivables are initially measured at fair value and subsequently measured at amortised cost using the effective interest method, less an allowance for impairment.

Impairment of a receivable is established when there is objective evidence that PHARMAC will not be able to collect amounts due according to the original terms of the receivable. Significant financial difficulties of the debtor and default in payments are considered objective evidence of impairment. The amount of the impairment is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted using the original effective interest rate. The carrying amount of the asset is reduced through the use of an impairment provision account and the amount of the loss is recognised in the statement of comprehensive income. Overdue receivables that are renegotiated are reclassified as current.

Investments

At each balance sheet date PHARMAC assesses whether there is any objective evidence that an investment is impaired.

Investments are initially measured at fair value plus transaction costs.

After recognition investments are measured at amortised cost using the effective interest method.

Impairment is established when there is objective evidence PHARMAC will not be able to collect amounts due according to the original terms of the deposit. Significant financial difficulties of the bank, probability that the bank will enter into bankruptcy, and default in payments are considered indicators that the deposit is impaired.

Property, Plant and Equipment

Property, plant and equipment consist of leasehold improvements, computer hardware, furniture and office equipment, and are shown at cost less accumulated depreciation and impairment losses.

Any write-down of an item to its recoverable amount is recognised in the statement of comprehensive income.

Additions

The cost of an item of property, plant and equipment is recognised as an asset if, and only if, it is probable that future economic benefits or service potential associated with the item will flow to PHARMAC and the cost of the item can be measured reliably.

Disposals

Gains and losses on disposal are determined by comparing the proceeds with the carrying amount of the asset. Gains and losses on disposal are included in the statement of comprehensive income.

Subsequent Costs

Costs incurred subsequent to initial acquisition are capitalised only when it is probable that future economic benefits or service potential associated with the item will flow to PHARMAC and the cost of the item can be measured reliably.

Depreciation

Depreciation is provided on a straight line basis on all property, plant and equipment, at rates that will write off the cost of the assets to their estimated residual values over their useful lives. The useful lives and associated depreciation rates of major classes of assets have been estimated as follows:

Item	Estimated useful life	Depreciation rate
Leasehold Improvements	5 years	20 %
Office Equipment	2.5 - 5 years	20% - 40%
Computer Hardware	2.5 - 5 years	20% - 40%
Furniture and Fittings	5 years	20%

Leasehold improvements are capitalised and depreciated over the unexpired period of the lease or the estimated remaining useful lives of the improvements, whichever is shorter.

Capital work in progress is not depreciated. The total cost of a project is transferred to the asset class on its completion and then depreciated.

The residual value and useful life of an asset is reviewed, and adjusted if applicable, at each financial year end.

Intangible assets

Software acquisition and development

Acquired computer software licenses are capitalised on the basis of the costs incurred to acquire and bring to use the specific software.

Costs that are directly associated with the development of software for internal use by PHARMAC are recognised as an intangible asset. Direct costs include the software development, employee costs and an appropriate portion of relevant overheads.

Staff training costs are recognised as an expense when incurred.

Costs associated with maintaining computer software are recognised as an expense when incurred.

Costs associated with the development and maintenance of PHARMAC's website are recognised as an expense when incurred.

Amortisation

The carrying value of an intangible asset with a finite life is amortised on a straight-line basis over its useful life. Amortisation begins when the asset is available for use and ceases at the date that the asset is derecognised. The amortisation charge for each period is recognised in the statement of comprehensive income. For computer software (the only identified intangible asset), the useful life is assumed as 2-5 years with a corresponding depreciation rate of 20-50%.

Creditors and Other Payables

Creditors and other payables are initially measured at fair value and subsequently measured at amortised cost using the effective interest method.

Employment Entitlements

Employee entitlements that PHARMAC expects to be settled within 12 months of balance date are measured at nominal values based on accrued entitlements at current rates of pay.

These include salaries and wages accrued to balance date, and annual leave earned but not yet taken.

PHARMAC recognises a liability and an expense for bonuses where it is contractually bound to pay them.

Provisions

PHARMAC recognises a provision for future expenditure on uncertain amount or timing where there is a present obligation (either legal or constructive) as a result of a past event, it is probable that an outflow of future economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax discount rate that reflects current market assessments of the time, value of money and the risks specific to the obligation. The increase in the provision due to the passage of time is recognised as a finance cost.

Public Equity

Public equity is the Crown's investment in PHARMAC and is measured as the difference between total assets and total liabilities. Public equity is classified as general funds, Herceptin SOLD trial fund, Discretionary Pharmaceutical Fund and Legal Risk Fund.

Commitments

Expenses yet to be incurred on non-cancellable contracts that have been entered into on or before balance date are disclosed as commitments to the extent that there are equally unperformed obligations.

Cancellable commitments that have penalty or exit costs explicit in the agreement on exercising that option to cancel are included in the statement of commitments at the value of that penalty or exit cost.

Goods and Services Tax (GST)

All items in the financial statements are exclusive of GST, except for receivables and payables, which are stated on a GST inclusive basis. Where GST is not recoverable as an input tax, then it is recognised as part of the related asset or expense.

The net amount of GST recoverable from, or payable to, the Inland Revenue Department (IRD) is included as part of the receivables or payables in the statement of financial position.

The net GST paid to or received from the IRD, including the GST relating to investing and financing activities, is classified as an operating cash flow in the statement of cash flows.

Commitments and contingencies are disclosed exclusive of GST.

Income Tax

PHARMAC is a public authority in terms of the Income Tax Act 2007 and consequently is exempt from income tax. Accordingly no charge for income tax has been provided for.

Budget Figures

The budget figures are those included in PHARMAC's Statement of Intent 2010/11-2012/13 tabled in the House on 2 July 2010 and Output Agreement 2010/11 signed by the Minister and PHARMAC Chair on 22 February 2011. The Output Agreement reflects the actual funding from the Crown.

Cost allocation

PHARMAC has determined the cost of outputs using the cost allocation system outlined below. Direct costs are those costs directly attributed to an output. Indirect costs are those costs that cannot be identified in an economically feasible manner with a specific output.

Direct costs are charged directly to outputs. Indirect costs are charged to outputs based on cost drivers and related activity or usage information.

Critical accounting estimates and assumptions

In preparing these financial statements PHARMAC has made estimates and assumptions concerning the future. These estimates and assumptions may differ from the subsequent actual results. Estimates and assumptions are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below:

- *value of property, plant and equipment* – at each balance date PHARMAC reviews the useful lives and residual values of its property, plant and equipment, including considering factors such as the physical condition of the asset, expected period of use of the asset by PHARMAC, and expected disposal proceeds from the future sale of the asset. PHARMAC has not made significant changes to past assumptions concerning useful lives and residual values. The carrying amounts of property, plant and equipment are disclosed in note 5.

Critical judgements in applying PHARMAC's accounting policies

Management has exercised the following critical judgements in applying PHARMAC's accounting policies for the period ended 30 June 2011:

Lease classification
Determining whether a lease agreement is a finance or an operating lease requires judgement as to whether the agreement transfers substantially all the risks and rewards of ownership to PHARMAC.

Judgement is required on various aspects that include, but are not limited to, the fair value of the leased asset, the economic life of the leased asset, whether or not to include renewal options in the lease term, and determining an appropriate discount rate to calculate the present value of the minimum lease payments. Classification as a finance lease means the asset is recognised in the statement of financial position as property, plant, and equipment, whereas for an operating lease no such asset is recognised.

PHARMAC has exercised its judgement on the appropriate classification of equipment leases.

FINANCIAL STATEMENTS

STATEMENT OF COMPREHENSIVE INCOME

For the year ended 30 June 2011

	Note	Actual 2011 $000	Output Agreement Budget 2011 $000	SOI Budget 2011 $000	Actual 2010 $000
Income					
Crown		24,744	24,724	15,359	13,033
DHB		2,920	2,920	2,920	2,820
Other:					
Interest received		268	120	120	191
Interest received - legal risk fund		275	280	280	212
Interest received - discretionary pharmaceutical fund		0	128	0	0
Other revenue		199	405	405	490
Other revenue - legal risk fund		0	0	0	1,505
Total Income		28,406	28,577	19,084	18,251
Expenditure					
Operating costs		3,663	5,478	6,409	4,299
Personnel costs	1	6,649	7,054	7,054	6,777
Audit Fees		31	35	35	29
Discretionary Pharmaceutical Fund	4	6,116	2,128	0	0
Director Fees		117	129	129	131
Occupancy costs		461	480	480	461
Depreciation & amortisation costs	6 & 7	418	417	417	443
Finance Costs	2	10	9	9	10
Herceptin SOLD trial administration		425	541	541	322
Responsible use of pharmaceuticals		4,151	4,595	4,151	4,548
Total expenditure		22,041	20,866	19,225	17,020
Net surplus/(deficit) for the period		**$6,365**	**$7,711**	**$(141)**	**$1,231**
Other comprehensive income		0	0	0	0
Total comprehensive income		**$6,365**	**$7,711**	**$(141)**	**$1,231**

Explanations of significant variances against budget are detailed in note 21.

The accompanying accounting policies and notes form part of these financial statements.

STATEMENT OF MOVEMENTS IN PUBLIC EQUITY

For the year ended 30 June 2011

	Note	Actual 2011 $000	Output Agreement Budget 2011 $000	SOI Budget 2011 $000	Actual 2010 $000
Balance at 1 July		8,547	8,547	8,399	7,316
Total Comprehensive Income		6,365	7,711	(141)	1,231
Balance at 30 June	3	**$14,912**	**$16,258**	**$8,258**	**$8,547**

Explanations of significant variances against budget are detailed in note 21.

The accompanying accounting policies and notes form part of these financial statements.

STATEMENT OF FINANCIAL POSITION

As at 30 June 2011

	Note	Actual 2011 $000	Output Agreement Budget 2011 $000	SOI Budget 2011 $000	Actual 2010 $000
PUBLIC EQUITY					
Retained earnings and reserves	3	2,932	1,600	1,600	1,600
Herceptin SOLD Trial fund	3	1,803	558	558	971
Legal risk fund	3	6,293	6,100	6,100	5,976
Discretionary Pharmaceutical Fund	3	3,884	8,000	0	0
TOTAL PUBLIC EQUITY		**$14,912**	**$16,258**	**$8,258**	**$8,547**
Represented by:					
Current assets					
Cash and cash equivalents		15,465	17,908	9,908	10,216
Debtors and other receivables	5	6	100	100	53
Prepayments		128	0	0	0
GST Refund		859	0	0	0
Total current assets		16,458	18,008	10,008	10,269
Non-current assets					
Property, plant and equipment	6	685	600	600	540
Intangible Assets	7	270	250	250	195
Total non-current assets		955	850	850	735
Total assets		17,413	18,858	10,858	11,004
Current liabilities					
Creditors and other payables	8	1,790	2,120	2,120	1,694
Employee entitlements	9	536	480	480	519
GST Payable		0	0	0	79
Total current liabilities		2,326	2,600	2,600	2,292
Non-current liabilities					
Provisions	10	175	0	0	165
Total liabilities		2,501	2,600	2,600	2,457
NET ASSETS		**$14,912**	**$16,258**	**$8,258**	**$8,547**

Explanations of significant variances against budget are detailed in note 21.

The accompanying accounting policies and notes form part of these financial statements.

STATEMENT OF CASH FLOWS

For the year ended 30 June 2011

	Note	Actual 2011 $000	Output Agreement Budget 2011 $000	SOI Budget 2011 $000	Actual 2010 $000
CASH FLOWS – OPERATING ACTIVITIES					
Cash was provided from:					
- Crown		24,744	24,724	15,359	13,033
- DHBs		2,920	2,920	2,920	2,820
- Interest		546	528	400	420
- Other		243	405	405	1,995
		28,453	28,577	19,084	18,268
Cash was disbursed to:					
- Legal Risk Fund expenses		(94)	0	0	0
- Discretionary Pharmaceutical Fund expenses		(6,116)	(2,128)	0	0
- Payments to suppliers and employees		(15,408)	(17,671)	(18,158)	(15,560)
- Goods and services tax (net)		(938)	(650)	(650)	(1,043)
		(22,556)	(20,449)	(18,808)	(16,603)
Net cash flow from operating activities	11	5,897	8,128	276	1,665
CASH FLOWS – INVESTING ACTIVITIES					
- Purchase of property, plant and equipment		(389)	(300)	(300)	(21)
- Purchase of intangible assets		(259)	(117)	(117)	(23)
- Purchase of investments		0	0	0	0
Net cash flow from investing activities		(648)	(417)	(417)	(44)
Net increase/(decrease) in cash		5,249	7,711	(141)	1,621
Cash at the beginning of the year		10,216	10,197	10,049	8,595
Cash at the end of the year		15,465	17,908	9,908	10,216

The GST (net) component of operating activities reflects the net GST paid and received.
The GST (net) component has been presented on a net basis, as the gross amounts do not provide meaningful information for financial statement purposes and to be consistent with the presentation basis of the other primary financial statements.

Explanations of significant variances against budget are detailed in note 21.

The accompanying accounting policies and notes form part of these financial statements.

OUTPUT EXPENDITURE REPORT

For the year ended 30 June 2011

Actual 2010/11	Funding MOH	Funding DHB	Funding Other	Output expenditure	Net surplus/(deficit)
Decision Making	16,684	300	599	-12,109	5,474
Influencing Medicine Use	6,698	2,100	72	-8,036	834
Supply Management	602	120	71	-790	3
Policy Advice and support	760	400	0	-1,106	54
Total	**24,744**	**2,920**	**742**	**-22,041**	**6,365**

Output Agreement 2010/11	Funding MOH	Funding DHB	Funding Other	Output expenditure	Net surplus/(deficit)
Decision Making	16,664	300	833	-9,622	8,175
Influencing Medicine Use	6,698	2,100	50	-9,169	-321
Supply Management	602	120	50	-859	-87
Policy Advice and support	760	400	0	-1,216	-56
Total	**24,724**	**2,920**	**933**	**-20,866**	**7,711**

SOI 2010/11	Funding MOH	Funding DHB	Funding Other	Output expenditure	Net surplus/(deficit)
Decision Making	6,963	300	705	-7,981	-13
Influencing Medicine Use	6,977	2,100	50	-9,169	-42
Supply Management	627	120	50	-859	-62
Policy Advice and support	792	400	0	-1,216	-24
Total	**15,359**	**2,920**	**805**	**-19,225**	**-141**

Actual 2009/10	Funding MOH	Funding DHB	Funding Other	Output expenditure	Net surplus/(deficit)
Decision Making	5,909	200	2298	-6,240	2,167
Influencing Medicine Use	5,920	2,100	50	-8,890	-820
Supply Management	532	120	50	-913	-211
Policy Advice and support	672	400	0	-977	95
Total	**13,033**	**2,820**	**2,398**	**-17,020**	**1,231**

STATEMENT OF COMMITMENTS

As at 30 June 2011

Operating leases as lessee.

The future aggregate minimum lease payments to be paid under non-cancellable operating leases are as follows:

	Actual 2011 $000	Actual 2010 $000
Capital commitments approved and contracted	-	-
Operating commitments approved and contracted		
Not later than one year	461	461
Later than one year and not later than five years	1,844	1,844
Later than five years and not later than ten years	922	1,383
Total commitments	**$3,227**	**$3,688**

The rental lease expires 24 July 2013 with an additional right of renewal for a further term of five years. It is expected that this right of renewal will be exercised; therefore the commitment is recognised for the full term of 10 years.

PHARMAC leases three floors of an office building. Half a floor is sublet due to it being surplus to requirements. The sub-lease expires on 31 October 2011.

PHARMAC has recognised a make good provision of $175,000 (2010 $165,000).

STATEMENT OF CONTINGENT ASSETS AND LIABILITIES

As at 30 June 2011

PHARMAC had no contingent assets at 30 June 2011 (2010: $nil).

PHARMAC had no contingent liabilities at 30 June 2011 (2010: $nil).

Explanations of significant variances against budget are detailed in note 21.

The accompanying accounting policies and notes form part of these financial statements.

NOTES TO THE FINANCIAL STATEMENTS

Note 1: Personnel Costs

	Actual 2011 $000	Actual 2010 $000
Salaries and related costs	6,558	6,553
Employer contributions to defined contribution plans	88	117
Increase/(decrease) in employee entitlements	3	107
Total personnel costs	**$6,649**	**$6,777**

Employer contributions to defined contribution plans include contributions to the State Sector Retirement Savings Scheme and Kiwisaver.

Note 2: Finance Costs

	Actual 2011 $000	Actual 2010 $000
Discount unwind on provisions (note 9)	**$10**	**$10**

Note 3: Public Equity

RETAINED EARNINGS	Actual 2011 $000	Actual 2010 $000
Balance at 1 July	1,600	2,705
Net surplus/(deficit)	6,365	1,231
Net transfer from/(to) Herceptin SOLD trial fund	(832)	(971)
Net transfer from/(to) discretionary pharmaceutical fund	(3,884)	0
Net transfer from/(to) legal risk fund	(317)	(1,365)
Balance at 30 June	**$2,932**	**$1,600**

HERCEPTIN SOLD TRIAL FUND	Actual 2011 $000	Actual 2010 $000
Balance at 1 July	971	0
Add:Net transfer from/(to) retained earnings	832	971
Balance at 30 June	**$1,803**	**$971**

LEGAL RISK FUND	Actual 2011 $000	Actual 2010 $000
Balance at 1 July	5,976	4,611
Add: Interest received transferred from/(to) retained earnings	274	212
Add: Other Income received transferred from/(to) retained earnings	137	1,505
Less: Litigation expenses transferred from/(to) retained earnings	(94)	(352)
Balance at 30 June	**$6,293**	**$5,976**

DISCRETIONARY PHARMACEUTICAL FUND	Actual 2011 $000	Actual 2010 $000
Balance at 1 July	0	0
Add: Income received transferred from/(to) retained earnings	10,000	0
Less: Pharmaceutical expenses transferred from/(to) retained earnings	(6,116)	0
Balance at 30 June	**$3,884**	**$0**
TOTAL PUBLIC EQUITY	**$14,912**	**$8,547**

Note 4: Discretionary Pharmaceutical Fund

The Discretionary Pharmaceutical Fund is a new fund. The expenditure of $6,116,000 relates to the purpose of the DPF to enable PHARMAC to take advantage of investment opportunities that might not otherwise be able to be funded in that year.

Note 5: Debtors and Other Receivables

The carrying value of debtors and other receivables approximates their fair value. Debtors are non-interest bearing and generally on 30 days terms.

	2011			2010		
	Gross $000	Impairment $000	Net $000	Gross $000	Impairment $000	Net $000
Not past due	6	0	6	48	0	48
Past due 30-60 days	0	0	0	5	0	5
Past due 61-90 days	0	0	0	0	0	0
Past due > 91 days	0	0	0	0	0	0
Total	**$6**	**$0**	**$6**	**$53**	**$0**	**$53**

Note 6: Property, Plant and Equipment

	Cost at beginning of year	Additions during the year	Disposals during the year	Accumulated Depreciation beginning of the year	Depreciation for the year	Elimination on disposals	Net Carrying Amount as at 30 June
	$000	$000	$000	$000	$000	$000	$000
2010							
Furniture and fittings	471	5	0	380	31	0	65
Computer hardware	1080	10	0	955	89	0	46
Office equipment	419	1	0	330	34	0	56
Leasehold improvements	771	5	0	287	116	0	373
Fixed asset work in progress	0	0	0	0	0	0	0
Total PPE Assets	**$2,741**	**$21**	**$0**	**$1,952**	**$270**	**$0**	**$540**
2011							
Furniture and fittings	476	0	1	411	28	0	36
Computer hardware	1090	347	1	1044	65	0	327
Office equipment	420	35	5	364	33	0	53
Leasehold improvements	776	4	0	403	108	0	269
Fixed asset work in progress	0	0	0	0	0	0	0
Total PPE Assets	**$2,762**	**$386**	**$7**	**$2,222**	**$234**	**$0**	**$685**

Note 7: Intangible Assets

	Cost at beginning of year	Additions during the year	Disposals during the year	Accumulated Amortisation beginning of the year	Amortisation for the year	Elimination on disposals	Net Carrying Amount as at 30 June
	$000	$000	$000	$000	$000	$000	$000
2010 Total Intangible Assets	$775	$23	0	$430	$173	0	$195
2011 Total Intangible Assets	$798	$259	0	$603	$184	0	$270

Note 8: Creditors and Other Payables

	Actual 2011 $000	Actual 2010 $000
Creditors	1,107	933
Accrued expenses	683	761
Total trade and other payables	**$1,790**	**$1,694**

Creditors and other payables are non-interest bearing and are normally settled on 30 day terms. The carrying value of creditors and other payables approximates their fair value.

Note 9: Employee Entitlements

	Actual 2011 $000	Actual 2010 $000
Annual leave entitlement	404	401
Accrued salaries and wages	132	118
Total employee entitlements	**$536**	**$519**

Note 10: Provisions

	Actual 2011 $000	Actual 2010 $000
Non-current provisions are represented by:		
Lease make-good	175	165
Total provisions	**$175**	**$165**

Movement for “make good” provision

	2011 $000	2010 $000
Balance at 1 July	165	155
Additional provisions made	0	0
Amount used	0	0
Unused amounts reversed	0	0
Discount unwind	10	10
Balance at 30 June	**$175**	**$165**

The make good provision relates to a rental lease that expires 24 July 2013 with an additional right of renewal for a further term of five years. PHARMAC leases three floors of an office building. Half a floor is sublet due to it being surplus to requirements. The sub-lease expires on 31 October 2011.

Note 11: Reconciliation of the Net Surplus from Operations with the Net Cash Flows from Operating Activities

	Actual 2011 $000	Actual 2010 $000
Net (deficit)/surplus from operations	$6,365	$1,231
Add non-cash items:		
Discount on unwind provision	10	10
Depreciation & Amortisation	418	443
Total non-cash items	$428	$453
Add (less) movements in working capital items:		
Decrease/(increase) in debtors and other receivables	47	59
Decrease/(increase) in prepayments	(128)	62
(Decrease)/increase in payables	96	(271)
(Decrease)/increase in make good provision	10	10
(Decrease)/increase in employee entitlements	17	34
(Decrease)/increase in net GST	(938)	87
Net movements in working capital items	(896)	$(19)
Net cash flow from operating activities	**$5,897**	**$1,665**

Note 12: Related Party Transactions

PHARMAC is a wholly owned entity of the Crown. The Crown, through the Ministry of Health, significantly influences the role of PHARMAC as well as being its major source of revenue.

PHARMAC enters into transactions with other government entities on an arm's length basis. Those transactions that occur within a normal supplier relationship on terms and conditions no more or less favourable than those which it is reasonable to expect PHARMAC would have adopted if dealing with that entity at arm's length in the same circumstance, are not disclosed.

All related party transactions have been entered into on an arms length basis. Other than described above, the value of transactions relating to key management personnel and entities over which they have control or significant influence were as follows:

Transaction	Reference	Transaction value year ended 30 June		Balance outstanding year ended 30 June	
		2011	2010	2011	2010
		$000	$000	$000	$000
Sapere Research Group	(i)	0	15	0	0
Tui Ora limited	(ii)	0	238	0	0
NZMA	(iii)	1	0	0	0
Taranaki PHO Limited	(iv)	0	5	0	0

Specific notes on each transaction follow noting that all transactions were carried out, and service providers appointed, in accordance with PHARMAC's procurement processes.

(i) David Moore, a PHARMAC Director (2000-2010), works with Sapere (formerly LECG). Specific consultants at Sapere (not David Moore) were contracted to provide some specified policy-related consultancy services to PHARMAC. Sapere was the most appropriate provider of services. Payments were negotiated and commensurate with general market rates for the provision of the relevant services. Contracting for the relevant services was a matter for the Chief Executive, not the Board. Accordingly, David Moore (nor any other Director) was not involved in discussions or negotiations related to the services. As specific consultants were contracted, David Moore was also not involved in provision of the services for Sapere.

(ii) Kura Denness, a PHARMAC Director, is a Director of Tui Ora Limited, a provider of Māori health services. PHARMAC contracted with Tui Ora for the provision of services related to PHARMAC's Space to Breathe initiative. Having conducted a contestable process, it was decided that Tui Ora was the most appropriate provider of services. Tui Ora disclosed the Directorship of Kura Denness in their proposal for the work. Kura Denness also has a standing disclosure on the Board's interest register related to her involvement with Tui Ora. Contracting of the relevant services was a matter for the Chief Executive, not the Board. Accordingly, Kura Denness (nor any other Director) was not involved in discussions or negotiations related to the services. Kura Denness was also not involved in provision of the services for Tui Ora.

(iii) David Kerr, a PHARMAC Director, was the President of the NZMA at the time of some payments by PHARMAC to the NZMA for recruitment advertising and access to an online version of the NZ Medical Journal. Payments of this kind are a matter for the Chief Executive, not the Board. Accordingly, David Kerr (nor any other Director) was not involved in discussions or negotiations related to the services. David Kerr was also not involved in provision of the services for NZMA.

(iv) Kura Denness, a PHARMAC Director, is a Director of Taranaki PHO Limited. PHARMAC made payments to Taranaki PHO Limited relating to PHARMAC’s One Heart Many Lives initiative. The payments covered fees and refreshments for 14 clinical staff from Taranaki PHO Limited who provided health checks as part of One Heart Many Lives. Kura Denness has a standing disclosure on the Board's interest register related to her involvement with Taranaki PHO Limited. These payments were a matter for the Chief Executive, not the Board. Accordingly, Kura Denness was not involved in discussions or negotiations related to the payments.

No provision has been required, nor expense recognised for impairment of receivables from related parties (2010 $nil).

Key management personnel compensation

	Actual 2011 $000	Actual 2010 $000
Salaries and other short term employee benefits and directors' fees	1,477	1,487
Post Employee Benefits	19	22

Key management personnel includes the Chief Executive, Directors and six managers. There have been no changes in the definition of key management personnel from 2010.

Note 13: Events after the Balance Sheet Date

There have been no significant events after the balance sheet date.

Note 14: Financial Instrument Risks

Currency risk

Currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates.

There are no financial instruments that expose PHARMAC to foreign exchange risk.

Interest rate risk

Interest rate risk is the risk that the fair value of a financial instrument will fluctuate or the cash flows from a financial instrument will fluctuate, due to changes in market interest rates.

PHARMAC has no interest bearing financial instruments and, accordingly, has no exposure to interest rate risk.

Credit risk

Credit risk is the risk that a third party will default on its obligation to PHARMAC, causing PHARMAC to incur a loss.

In the normal course of its business, credit risk arises from debtors and deposits with banks.

PHARMAC's maximum credit exposure for each class of financial instrument is represented by the total carrying amount of cash and cash equivalents and debtors. There is no collateral held as security against these financial instruments. PHARMAC is only permitted to deposit funds with New Zealand registered banks. PHARMAC does not have a bank overdraft facility.

PHARMAC is guided by the following counterparty limits:

Total amount invested	Number of Banks to be used	Maximum amount with 1 Bank
$0-$1m	1 or more	No restriction
$1m-$3m	2 or more	No more than 66%
>$3m	3 or more	No more than 40%

PHARMAC does not have significant concentration of credit risk.

Liquidity risk

Liquidity risk is the risk that PHARMAC will encounter difficulty raising liquid funds to meet commitments as they fall due.

In meeting its liquidity requirements, PHARMAC closely monitors its forecast cash requirements. The table below analyses PHARMAC's financial liabilities that will be settled based on the remaining period at the balance sheet date to the contractual maturity date. The amounts disclosed are the contractual undiscounted cash flows.

	2011 Less than 6 months $000	2010 Less than 6 months $000
Creditors and other payables	**$1,790**	**$1,694**

Fair value

The carrying amounts of financial instruments as disclosed in the financial statements at 30 June 2011 approximate their fair values.

Note 15: Categories of Financial Instruments

The carrying amounts of financial assets and liabilities are as follows:

Financial assets

LOANS AND RECEIVABLES	Actual 2011 $000	Actual 2010 $000
Cash and cash equivalents	15,465	10,216
Debtors and other receivables	6	53
Total loans and receivables	**$15,471**	**$10,269**

Financial liabilities

FINANCIAL LIABILITIES AT AMORTISED COST	Actual 2011 $000	Actual 2010 $000
Trade and other payables	1,790	1,694
Total financial liabilities at amortised cost	**$1, 790**	**$1,694**

Note 16: Capital Management

PHARMAC's capital is its equity, which comprises accumulated funds and other reserves. Equity is represented by net assets.

PHARMAC is subject to the financial management and accountability provisions of the Crown Entities Act 2004, which imposes restrictions in relation to borrowings, acquisition of securities, issuing guarantees and indemnities, and the use of derivatives.

PHARMAC manages its equity as a by-product of prudently managing revenues, expenses, assets, liabilities, investments and general financial dealings to ensure PHARMAC effectively achieves its objectives and purpose, whilst remaining a going concern.

PHARMAC is currently exempt from the imposition of the Crown's capital charge.

Note 17: Employee Remuneration

Total Remuneration and Benefits	Number of Employees	
$000	**2011**	**2010**
100 – 110	6	6
110 – 120	5	6
120 – 130	3	4
130 – 140	1	0
150 – 160	0	2
160 – 170	1	1
170 – 180	1	1
190 – 200	2	0
200 – 210	0	1
210 – 220	1	1
280 – 290	0	1
290 – 300	1	0

Note 18: Indemnities and Insurance Cover for Board Members and Employees

This information is presented in accordance with sections 152(1) (e) and (f) of the Crown Entities Act 2004. Under individual employment contracts, PHARMAC indemnifies employees should they be found liable in any proceedings for damages arising out of the employee's reasonable performance of their duties and responsibilities. Insurance cover is provided to board members and employees under Directors and Officers Liability, Personal Accident and Overseas Travel policies.

Note 19: Board and Committee Fees

Board members received the following fees during the year:

Member	Fees	
	2011	**2010**
	$000	$000
Mr Stuart McLauchlan (Chair)	36	21
Prof Gregor Coster	0	2
Ms Kura Denness	18	18
Dr David Kerr	18	18
Mrs Anne Kolbe	18	0
Mr David Moore	9	18
Prof Jens Mueller	18	0
Mr Richard Waddel	0	36
Ms Adrienne von Tunzelmann	0	18
Total Board fees	**$117**	**$131**

Board, Committee and PTAC Sub-Committee members paid more than $500 are listed below. Some members do not claim fees. In 2010/11 the following fees were paid:

Committees

	Payment ($000)		Payment ($000)
Consumer Advisory Committee		**PTAC**	
Barbara Greer	1	Carl Burgess	21
Sandra Coney	2	Melissa Copland	8
Matiu Dickson	2	Stuart Dalziel	15
Maurice Gianotti	1	Ian Hosford	17
Anne Fitisemanu	2	Sisira Jayathissa	14
Anna Mitchell	1	George Laking	9
Katerina Pihera	1	Jim Lello	12
Kate Russell	6	Dee Mangin	8
Jennie Michel	1	Graham Mills	16
		Peter Pillans	6
		Mark Weatherall	16
		Howard Wilson	19

PTAC Sub-Committees

	Payment ($000)		Payment ($000)
Cardiology		**CaTSOP**	
Malcolm Abernethy	2	Scott Babington	6
Sisira Jayathissa	1	Carl Burgess	5
Lannes Johnson	1	Bernie Fitzharris	1
Stewart Mann	1	Tim Hawkins	2
Richard Medlicott	1	Vernon Harvey	7
Peter Pillans	1	Lochie Teague	4
Mark Weatherall	2		
Diabetes		**Hospital**	
Carl Burgess	1	Billy Alan	3
Nic Crook	1	Carl Burgess	4
Craig Jefferies	1	Marilyn Crawley	3
Bruce Small	1	Matthew Dawes	3
		Sarah Fitt	3
		Jan Goddard	3
		Andrew Herbert	2
		Christopher Jay	3
		Paul Tomlinson	3
		Mark Weatherall	2
Growth Hormone		**Neurological**	
Carl Burgess	1	Peter Bergin	2
Ian Holdaway	2	Alistair Dunn	1
Penelope Hunt	2	Lindsay Haas	3
Patrick Manning	1	Richard Hornabrook	2
		Sisira Jayathissa	1
		William Wallis	3
Special Foods		**Tender**	
Simon Chin	1	Sarah Fitt	1
Kim Herbison	3	Jim Lello	2
Jim Lello	3	John McDougall	2
		Clare Randall	1
		Geoff Savell	2
		John Savory	2
		David Simpson	2
		Paul Tomlinson	2

Note 20: Cessation Payments

This information is presented in accordance with section 152(1)(d) of the Crown Entities Act 2004. Cessation payments include payments that the person is entitled to under contract on cessation such as retirement payment, redundancy and gratuities. During the year PHARMAC made no payments to former employees or members in relation to cessation. (2010: $nil).

Note 21: Explanation of Major Variances Against Budget

The Output Agreement reflects a subsequent agreed increase in funding from the original Statement of Intent (SOI) of $9,365,000 Crown funding. This is due to the establishment of the Discretionary Pharmaceutical Fund (DPF) with $10,000,000 and a reduction in the requested level of the Crown's baseline contribution of $635,000 from the SOI.

Explanations of major variances from PHARMAC's estimated figures in the SOI are as follows:

Statement of comprehensive income

The net profit for the year ended 30 June 2011 of $6,365,000 is $6,506,000 more than the SOI budgeted deficit of $141,000.

The main differences in revenue include the Crown funding $10,000,000 for the DPF.

A significant increase in expenditure was due to payment from the DPF to DHBs of $6,116.000.

The main difference in operating expenditure reduction results from a delay in implementing $1,332,000 in one-off and some of the first year costs associated with investing in PHARMAC's expanded role in respect to hospital pharmaceuticals and medical devices.

Statement of financial position

Cash and cash equivalents are $5,557,000 more than the SOI budget reflecting the movements above.

ISSN 1179-3759 (Print)
ISSN 1179-3767 (Online)

Pharmaceutical Management Agency

Level 9, 40 Mercer Street, PO Box 10-254, Wellington 6143, New Zealand
Phone: 64 4 460 4990 - Fax: 64 4 460 4995 - **www.pharmac.govt.nz** - Freephone Information line (9am-5pm weekdays) 0800 66 00 50