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Containing Drug Costs – A Prescription for Purchasers

If you purchase health insurance for your company or organization, you are acutely aware that U.S. drug prices are rising more than three times as fast as the Consumer Price Index, and utilization is increasing too. The Kaiser Foundation offers the following evidence: Prescription drug price increases averaged 10.5% per year from 1998-2000, while the annual CPI increased 2.8%; in 2000, the drug hike was estimated to be 17%. Kaiser also notes that utilization (number of prescriptions dispensed) contributes 48% of the rising costs. According to the Segal Company Health Plan Cost Trend Survey, state employee and retiree prescription drug benefit trend rates are estimated to rise 19.7% for active plan members and retirees under age 65 and 20.9% for retirees age 65 and older. These trend rates are similar for mail order and retail pharmacies. What's happening, and what can purchasers do to contain costs?

Background - Pharmaceutical manufacturers develop, test, and seek federal approval for their *brand name* drugs. This process often takes a decade or longer, may cost more than a billion dollars per drug, and final approval is uncertain. Once a drug is approved, the company wants to recoup costs, and make a profit worthy of the risk. While a firm has *patent protection* for many years - meaning another company cannot manufacture the drug without a license agreement - once that patent protection lapses, less expensive *generics* with similar ingredients to the original brand can be sold. Generic drugs may not be appropriate for some medical conditions where small variations in the composition of a drug can significantly affect treatment, for example with respiratory disorders. Often though, generic substitutes are acceptable, saving customers money.

Manufacturers market to wholesalers and/or retailers, typically pharmacies, who then sell to the public with varying margins. Sometimes the manufacturer offers rebates, or discounts off the Average Wholesale Price. Since the mid-1990s, manufacturers have also been allowed to advertise directly to consumers, resulting in greater demand for brand name drugs, contributing to increased utilization and therefore to increased spending on prescription drugs.

The purchaser's role – Today, more than half the U.S. population is covered under plans that include prescription drug coverage through a *Pharmacy Benefits Manager* (PBM). There are more than 100 PBMs serving PA customers.

PBMs apply managed care principles to prescription drug programs with the goal of cost-effective drug prescribing and use. Four defining functions of PBMs are: 1) electronic claims processing and adjudication, 2) pharmacy network management, 3) formulary (see below) development and management for clients, and 4) rebate negotiations with pharmaceutical manufacturers. PBMs provide purchasers with cost savings by taking advantage of economies of scale, as well as pharmacy group practice and health care network concepts.

Many purchasers have established *formularies* - lists of acceptable commonly prescribed drugs, selected by a panel of doctors and pharmacists with expertise in both academic and clinical practice. The list is based on the safety, cost and effectiveness of the drugs, and is designed as a guide to help patients receive the most appropriate prescriptions at a reasonable cost. Many drug plans today offer three tiers of formularies:

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(1) *generics* - offering drugs which employees can purchase for a modest fixed dollar co-payment, (2) *"preferred" brand name* drugs which employees can purchase with a percentage co-payment, and (3) *"Non-preferred"* or newly-approved brand name drugs which cost the employer – and the employee – considerably more. While formularies help contain costs, their implementation can be controversial, and purchasers agree that effective communication to employees is essential.

Many purchasers realize cost benefits by joining a *pharmacy purchasing coalition.* These groups leverage buying power by serving a large number of covered lives, and are able to negotiate discounted rates with pharmacies. You do not need to form your own purchasing coalition – there are several of them in the Commonwealth and some are looking for more members. Your employees' purchasing power adds to their leverage. Business purchasing coalitions and organized labor groups in the Commonwealth sponsor these coalitions. Should you be interested in more details on coalitions, please contact PHC4 for more information.

Purchasers may reduce prescription costs by customizing their plan designs. Raising co-pays or deductibles requires careful communication, and is not the only option. Quantity discounts may be effective. These encourage bulk purchasing (employees buy three months supply instead of 30 days), higher dosing and less dispensing (i.e. a 25mg pill once a day, rather than a 12.5mg pill twice a day), and can yield better patient compliance and save the plan about 50% of the cost. Prior authorization may restrict less than .5% to 1% of the population, and may ensure that patients obtain the most effective drug for their condition. Case management, which targets patients with unusual situations, can improve patients' understanding of the best way to take medication.

The next steps – Some purchasers turn to consulting firms to help find the best PBMs to fit their needs. These consultants include nationally known companies and small "niche" firms. Consultants can help purchasers design their plan, and help find the best deal possible on the financial terms of the plan and the administration of the plan. They might help purchasers audit pharmacies for accuracy when filling prescriptions, find the best possible discounts off Average Wholesale Price, find the lowest dispensing fees and claims processing fees, and most importantly find rebates from drug manufacturers.

Eventually, purchasers might want to "drill down" deeper to find even greater cost containment potential. Here's how. Speak to your legal counsel about privacy issues, then in consultation with your legal counsel, ask your PBM or your consultant to help you review the characteristics of your employees or members: (a) Determine the physicians who treat the majority of your cases, (b) Determine the hospitals that treat the majority of your cases, and (c) Determine the most-prescribed drugs for your cases. Track and identify the prescription writing practices of local physicians with medical directors at local hospitals. Deliver data to the doctors and hospitals about national standards of *best prescription practices.* In effect, you will then ask local doctors to come into compliance with national prescription guidelines for the most-used categories of drugs. By informing doctors of their own prescription patterns that may be outside of professional guidelines, purchasers or coalitions may avoid some costly and perhaps unhealthy practices. "Once the doctor knows that," one large purchaser told us, "it has a positive influence on his prescription patterns," reducing usage and containing costs.

Summary - By using PBMs, coalitions, and/or consultants, establishing formularies, seeking discounts and rebates, managing your plan carefully with audits and dispensing controls, and "drilling down" into your own data, you may be able to offer a valuable pharmaceutical benefit plan while containing costs.

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