COLORADO DEPARTMENT OF HEALTH CARE POLICY & FINANCING

1570 Grant Street, Denver, CO 80203-1818 • (303) 866-2993 • (303) 866-4411 Fax

John W. Hickenlooper, Governor • Susan E. Birch MBA, BSN, RN, Executive Director

November 1, 2012

The Honorable Cheri Gerou, Chairman
Joint Budget Committee
200 East 14th Avenue, Third Floor
Denver, CO 80203

Dear Representative Gerou:

Please find the Department's response to the Joint Budget Committee on the Department of Health Care Policy and Financing's Medical Services Premiums; Legislative Request for Information #5.

Legislative Request for Information #5 states:

The Department is requested to submit a report by November 1, 2012, to the Joint Budget Committee regarding the Department's efforts to ensure that pharmaceuticals are purchased at the lowest possible price.

The attached report describes in detail the Department's efforts to ensure that pharmaceuticals are purchased at the lowest possible price.

Questions regarding this response can be addressed to Cathy Traugott, Pharmacy Section Manager, at 303-866-6338.

Sincerely,

Susan E. Birch, MBA, BSN, RN
Executive Director

cc: Senator Mary Hodge, Vice-Chair, Joint Budget Committee
Senator Pat Steadman, Joint Budget Committee
Senator Kent Lambert, Joint Budget Committee
Representative Jon Becker, Joint Budget Committee
Representative Claire Levy, Joint Budget Committee
Senator Brandon Shaffer, President of the Senate
Senator John Morse, Senate Majority Leader
Senator Bill Cadman, Senate Minority Leader
Representative Frank McNulty, Speaker of the House
Representative Amy Stephens, House Majority Leader
Representative Mark Ferrandino, House Minority Leader
John Ziegler, Staff Director, JBC
Eric Kurtz, JBC Analyst
Henry Sobanet, Director, Office of State Planning and Budgeting
Erick Scheminske, Deputy Director, Office of State Planning and Budgeting
Bettina Schneider, Budget Analyst, Office of State Planning and Budgeting
Legislative Council Library (6 copies)
State Library (4 copies)
Susan E. Birch, Executive Director
Suzanne Brennan, Health Programs Office Director
John Bartholomew, Finance Office Director
Lorez Meinhold, Community Partnerships Office Director
Dr. Judy Zerzan, Clinical Services Office Director
Tom Massey, Policy and Communications Office Director
Antoinette Taranto, Client Services Eligibility & Enrollment Office Director
Phil Kalin, Center for Improving Value in Health Care (CIVHC) Director
Mary Kathryn Hurd, Legislative Liaison
Joanne Zahora, Public Information Officer
HCPF Budget Library, HCPF Budget Division

COLORADO DEPARTMENT OF HEALTH CARE POLICY AND FINANCING

REPORT TO THE JOINT BUDGET COMMITTEE

COST EFFECTIVE ACQUISITION OF PHARMACEUTICALS

NOVEMBER 1, 2012

Legislative Request for Information #5 states:

The Department is requested to submit a report by November 1, 2012, to the Joint Budget Committee regarding the Department's efforts to ensure that pharmaceuticals are purchased at the lowest possible price.

The Department engages in multiple activities to ensure pharmaceuticals are purchased at the lowest possible price. From the Department's perspective, the lowest possible price is considered to be the lowest price that can be paid without creating a barrier to access for Medicaid clients. This is consistent with federal statute which states that a state plan must assure that payments are consistent with efficiency, economy, and quality of care and are sufficient to enlist enough providers so that care and services are available under the plan at least to the extent that such care are services are available to the general population in the geographic area[1]. The current efforts to identify the lowest possible purchase price and subsequently lowest possible pharmacy benefit expenditure focus primarily on 1) an updated payment methodology (which shifts focus from published list price to actual pharmacy acquisition prices and costs for professional pharmacy services) and 2) the Preferred Drug List process. Through the past years, several other methods for lowering purchase price have been examined by the Department and many have been discussed in prior Legislative Requests and annual reports. Therefore, the focus of this response will be on current efforts, which following exhaustive research, have been deemed the most likely to result in the lowest purchase prices without creating barriers to access for clients.

Current Methods for Payment

The Department's methodology for pharmacy reimbursement is undergoing significant changes. The redesign of the pharmaceutical reimbursement methodology began in the spring of 2011 when it became necessary for the Medicaid Program to replace the Average Wholesale Price (AWP) as the primary component of pharmacy reimbursement. This came as the result of a legal settlement in which First Data Bank (a national provider of pharmaceutical market information and information technology) was accused of artificially inflating drug pricing. One key term of the settlement required First Data Bank to cease publishing Blue Book AWP within two years of the final court ruling. Ultimately, this led the Colorado Medicaid Program, and countless other pharmacy payers that depend on First Data Bank for drug pricing data, to find a suitable replacement before the end of September 2011. Although AWP had been established nationwide as a standard for pharmacy claims processing, the need for more transparent and dependable pharmaceutical pricing is clear. The Department is working closely with the impacted stakeholder community to develop a permanent methodology that adheres to these principles. The primary objective of the reimbursement methodology is to realign pharmacy reimbursement with the actual ingredient costs and dispensing costs incurred by pharmacies.

Because the Department did not yet have a replacement methodology that would be viable in the long term, the Department implemented an interim reimbursement methodology in October 2011, when the AWP statistics became unavailable. This methodology is currently being used. The interim methodology, developed with significant stakeholder input, reimburses pharmacies

[1] 42 U.S.C. 1396(a)(30)(A)

at a level approximately equivalent to what reimbursement would be under the AWP based reimbursement methodology. The methodology utilizes Wholesale Acquisition Cost (WAC) (Adjusted WAC for brand name pharmaceuticals where prices have been shown to follow pharmacy purchase prices) and State Maximum Allowable Cost (SMAC) rates for most generically available options (generic pricing showed no linear correlation between WAC values and acquisition prices). This methodology relies heavily on SMAC rate pricing based on average acquisition cost values supplied from an external vendor which is then inflated to bring reimbursement up to the approximate level it would have been at had AWP been used; the disconnect between actual acquisition cost and the current level of pharmacy reimbursement still exists in the current (interim) reimbursement methodology.

While this methodology allowed for post-AWP payment to proceed, it can only be a temporary solution. CMS approved the methodology under the condition that the Department was ultimately pursuing an Actual Acquisition Cost (AAC) based methodology which would be implemented in the near future. Additionally, looking at SMAC adjustments of up to 233% in some cases, it is obvious that the current methodology does not accurately reflect the cost of pharmaceuticals or the cost to the pharmacy to provide the service. To that end, the Department has been meeting regularly with the pharmacy stakeholder groups to establish a new methodology which will more appropriately determine costs for pharmaceutical products and professional services as experienced by pharmacies in Colorado.

Why Average Acquisition Cost?

With First Data Bank no longer publishing AWP, many states have had to pursue alternative reimbursement methodologies. The fundamental problem with many of the alternative options is that most rely on proprietary pricing lists that could share the same flaws as AWP. The true relationship between reimbursement to pharmacies and what pharmacies actually pay to acquire drugs would not be known to the Department. Consequently, the lack of transparency results in the state potentially underpaying or overpaying pharmacies. The solution is to identify what pharmacies actually pay to acquire pharmaceuticals and align reimbursement accordingly.

Alabama was the first state to explore this option by working with stakeholders and CMS. A consulting firm conducted surveys of Medicaid program registered pharmacies to statistically determine the AAC for most available drugs based upon Alabama pharmacy invoices. The consulting firm also identified a Cost of Dispensing which more accurately accounts for the costs of professional services involved in filling a prescription. In addition, successful implementation of AAC has since occurred in Oregon and Idaho.

Aligning pharmacy reimbursement with actual costs instead of relying on proprietary pricing statistics that are not transparent or dependable enables a state program to purchase pharmacy products and services at the lowest possible cost while still adhering to the requirements of the Social Security Act. CMS has publicly supported this methodology and has used similar concepts in the development of their National Average Drug Acquisition Cost program.

Implementing AAC in Colorado

Efforts began upon implementation of the interim methodology to develop an AAC based solution for the Colorado Medicaid program. Following a competitive bidding process, Mercer Government Human Services Consulting (Mercer) began working with the Department in 2011. The contractor is assisting the Department with identifying Colorado specific AAC prices by surveying pharmacies and analyzing survey results, incorporating stakeholder feedback in the survey process, and maintaining a pricelist on an ongoing basis.

With Mercer, the Department defined and drafted the survey process for Colorado Medicaid pharmacies and then shared with the pharmacy stakeholder community for feedback. After careful consideration of the stakeholder feedback, the Department and Mercer contacted all pharmacy providers by mail alerting them to the survey process, survey completion instructions and important submission dates. Mercer then collected and compiled the survey data for independent analysis of pharmacy costs amongst Colorado Medicaid participating pharmacies. Mercer reported the results of the analysis to the Department and shared with the stakeholders in a presentation on May 15, 2012.

The Cost of Dispensing Report concluded that $11.67 best represents the average cost of dispensing a prescription across pharmacies within Colorado. The report also concluded that total prescription volume is a strong predictor of the cost of dispensing for any given pharmacy.

The Department has since met regularly with the pharmacy stakeholder community to discuss the proposed use of $11.67 as an average cost of dispensing along with discussions of how future surveys should be updated and collected. Given all of the information derived from Mercer's analysis, the Department has proposed a new reimbursement which meets the $11.67 average across three distinct tiers of reimbursement based upon pharmacy total prescription volume. This approach gives consideration to the relationship between pharmacy volume and lower cost of dispensing. It is hoped that it will further protect client access to services by minimizing the impact on any one individual pharmacy.

While the dispensing fee is increasing significantly, in combination with bringing reimbursement for prescriptions in line with the costs of acquiring them, the change in methodology is anticipated to generate savings on the order of 5.5% of overall pharmacy expenditure. This amount of savings indicates how large of a disconnect AWP generated between reimbursement and the actual cost of acquiring pharmaceuticals.

The Department anticipates taking the rule to update the pharmaceutical reimbursement methodology to the Medical Services Board in November. If approved, the new methodology could be implemented in February 2013. In addition, the Department has submitted a State Plan Amendment to CMS for approval of this reimbursement methodology.

See the appendix for a detailed timeline of key events in the implementation of the AAC reimbursement methodology.

Additional Mechanisms to Ensure the Lowest Purchase Price

The Department continues to utilize the Preferred Drug List (PDL) as a savings tool to ensure the lowest available prices are paid for pharmaceutical products. The Department implemented the PDL program in 2008 as a mechanism to promote clinically appropriate utilization of pharmaceuticals in a cost effective manner. The process considers safety, effectiveness, clinical outcomes, and costs in an attempt to drive utilization to the most proven cost-effective agents in drug classes where multiple therapeutic options are available. The PDL drug classes are reviewed on an annual basis, with the various drug classes divided among four quarterly reviews. Following each Pharmacy and Therapeutics (P&T) Committee review of the medications, the Department's costs are modeled to compare net costs of the drug based on utilization from claims data, current product reimbursement, the current federally mandated unit rebate and available supplemental rebates offered. Within the clinical context recommended by the P&T Committee, preferred products are selected that will maximize benefit and value to Medicaid enrollees, while minimizing expenditure. For FY 2011-12, the Department collected over $5,000,000 in supplemental rebates for preferred products on the PDL.

In summary, the Department is planning to implement pharmacy acquisition cost based reimbursement in early 2013. The Department took many steps to ensure that the opinions of stakeholders have been included in the consideration of this significant change and that true costs of providing professional services have been accounted for. Reimbursement will take into account the costs to Colorado pharmacies that participate in the Colorado Medicaid program. It will create a fair reimbursement, and will not impact client access to pharmacy services. It will also not be affected by price inflation or manipulation that is possible with less transparent pricing lists. In conjunction with the ongoing PDL efforts, this methodology change helps to ensure that the Colorado Medicaid program is purchasing all of its pharmaceuticals at the lowest fair price.

Appendix – Timeline of Key Events

Date	AAC/Dispensing Fee Implementation Timeline
Summer 2011	The Department met with the provider community regularly to outline the interim reimbursement methodology currently used by the Department. This process involved Mercer providing the pharmacy community a comprehensive analysis on the budget neutrality of the interim reimbursement methodology and the Department providing the rates to the pharmacy community for increased transparency. This process also included outlining the Department's overall goal of an AAC reimbursement methodology with an updated dispensing fee to be implemented the following year.
October 1, 2011	The Department transitioned to the interim reimbursement methodology.
December 20, 2011	The Department & Mercer presented the proposed reimbursement methodology and AAC/cost of dispensing fee survey process to the provider community.
February & March 2012	Mercer, with the assistance of the Department, surveyed Medicaid-enrolled Colorado pharmacies to determine 1) AAC of all Medicaid billable drugs, and 2) average per prescription cost of dispensing a drug to a Medicaid client.
May 15, 2012	The Department & Mercer presented a preliminary draft of Mercer's AAC and dispensing fee survey analysis to the provider community.
May 16, 2012 to September 2012	The Department has been meeting with the provider community on a monthly basis to discuss any misunderstandings, concerns, or recommendations with the proposed AAC reimbursement methodology or revised dispensing fee. The Department also kept the provider community apprised of its tentative timetable for presenting the rule change to the MSB and the tentative effective date of the reimbursement methodology/dispensing fee change.
September 17, 2012	The Department met with RX-Plus and Colorado Pharmacist Society to discuss different several proposed tiered dispensing fee options, a phased-out percent increase to AAC rates for rural pharmacies, and the projected change to pharmacy reimbursement with the proposed reimbursement methodology.
September 18, 2012	The Department met with National Association of Chain Drug Stores, Colorado Retail Council, and King Soopers to discuss different several proposed tiered dispensing fee options, the impact of the proposed dispensing fee options on King Soopers, and the projected change to pharmacy reimbursement with the proposed reimbursement methodology.
September 20, 2012	The Department posted the proposed rule and provided notice that the rule will be heard at the October 2012 MSB meeting. The Department provided written notice to the stakeholders that the rule was posted and that the Department intended to present the rule in October.
September 24, 2012	The Department presented the proposed rule at the Department's Public Rule Review Meeting.
Late September 2012 and Early October 2012	Because several members of the provider community could not attend the meeting on September 24, 2012 and because the Department wanted to give the provider community time to respond to the information presented at the

Date	AAC/Dispensing Fee Implementation Timeline
	meetings on September 17, 2012 and September 18, 2012 the Department held a separate meeting after the Department's Public Rule Review Meeting on October 2, 2012 and then again on October 9, 2012. Given the concerns raised at those meetings, the Department decided to pull the rule from the October MSB meeting and will instead present the rule at the November 2012 MSB meeting.
Late October 2012	The Department asked the pharmacy community for a final list of their concerns. The Department provided responses to those concerns. The Department also continues to meet with the pharmacy community to discuss issues raised by the pharmacy community.
January 2013 Forward	The Department will meet with the pharmacy community on a regular basis to address any ongoing issues.