Ideas in Action

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Drug buying pools:

The prescription for what's ailing Washington's health care budget

Summary of findings

As Washington faces difficult state budget issues, Department of Social and Health Services (DSHS) Secretary Dennis Braddock has threatened to cut vital health care programs through the submission of a Medicaid waiver. Meanwhile, the prescription drug industry continues to be one of the most profitable in the world, and a major source of increasing health care costs. By pooling its prescription drug purchases, Washington could save between $8 million and $89 million annually. Additionally, if the uninsured were allowed to purchase prescriptions through the pool, they could save between $79 million and $174 million annually.

Rather than slashing Medicaid and making health care more difficult to access, Washington should pool the prescription drug purchases of its state agencies; open these pools up to the underinsured and uninsured, private entities, and local units of government; and adopt legislation that would enable it to pool prescription purchases with other states. That is why Washington Citizen Action, and a coalition of over 20 organizations representing seniors, labor, health care providers, community and faith based organizations, supports House Bill 2431 and Senate Bill 6368.

HB 2431 and SB 6368 establish a drug purchasing pool to fight the problem of rising prescription drug costs, while providing important consumer protections. The legislation maintains patient access to needed medication, and ensures providers may "dispense as written" the prescriptions their patients need. This means patients who need a specific drug will receive it without any hassle for patients or providers. The legislation also gives seniors and others without prescription drug insurance the opportunity to purchase prescriptions at lower prices based on savings the state negotiates with manufacturers.

Using an extremely conservative calculation of the savings that could be produced by this legislation, the state agencies involved estimate they will collectively save between $4 million and $7 million annually once the program is set up. This number includes exhaustive estimations of the costs involved in setting up the program — from staff to the postage to mail out information to pharmacists and health care providers — and agencies note there may be less expensive and more efficient alternatives to the methods used in the estimate. But their calculation of savings is far more conservative. For example, the estimate does not include savings from pooling drug purchases from managed care health plans, claiming these savings cannot currently be quantified. Additionally, all the agencies used percentages of 5 percent or lower to estimate potential savings from their current spending on prescription drugs.

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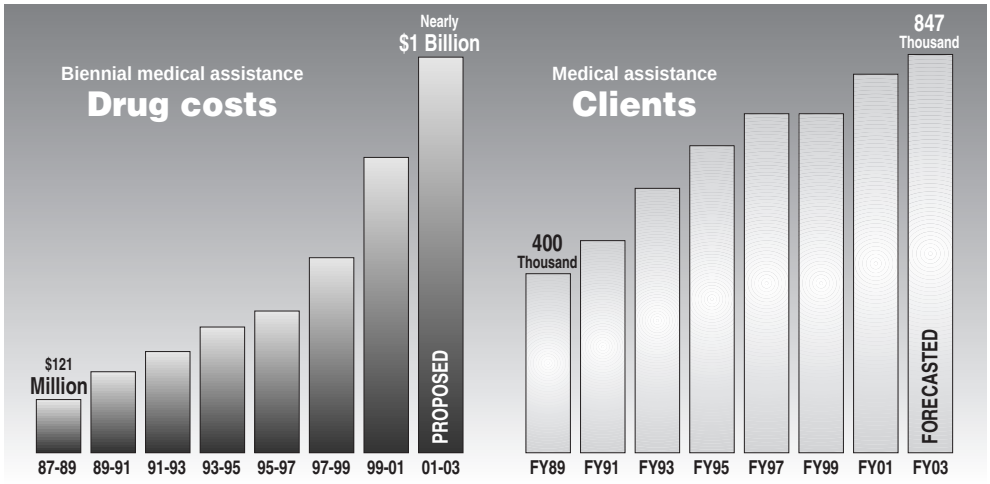
The state of Oregon has passed similar legislation, and with a Medicaid population only 58 percent the size of Washington's, they estimate they will save almost $20 million dollars annually.[1] Our estimate shows Washington will likely save far more with a purchasing pool than the state agencies' estimate of $7 million annually.

Difficult times for Washington residents and the state budget

Decreased revenues from tax cuts and the worsening economy together with the September 11th attacks have tightened Washington state's budget. Boeing plans to layoff up to 30,000 workers in response to a downturn in the airline industry. The Office of Financial Management says the Boeing layoffs alone could mean a drop in state revenue of up to $900 million,[2] and tax cuts from 1994 to 2000 reduced 2001-03 state revenue by $2.4 billion.[3] Current projections show a $2 billion shortfall in the 2001-03 budget, and the decrease in revenue is projected to continue into the foreseeable future.[4] The state's unemployment rate has increased as well, creating tough times for Washington residents.



Source: Medical Assistance Budget Drivers, WA DSHS, March 2001.

Vital health care programs targeted for cuts

Since the Department of Social and Health Services (DSHS) is a large part of the state budget, vital public health programs like Medicaid are targeted for these cuts.[5]

DSHS Secretary Dennis Braddock has submitted a waiver that asks the federal government to waive key Medicaid protections for Washington, and would allow the state Medicaid program to cap enrollment, reduce services, increase cost-sharing, and hide future changes from public scrutiny.[6] The waiver requests the ability to radically alter major sections of the Medicaid program, but does not specify what changes will be made or how they will be decided.

The waiver could result in waiting lists, unaffordable costs of coverage and services for Medicaid recipients, and increasing numbers of uninsured Washington residents. These changes would hurt residents already facing rising unemployment, when they most need public safety net programs. A recent analysis of the connection between unemployment and the uninsured found for every 100 people who lose their job, the number of people without health insurance rises by 85. If Medicaid enrollment was capped, the uninsured rate would be even greater.[7]

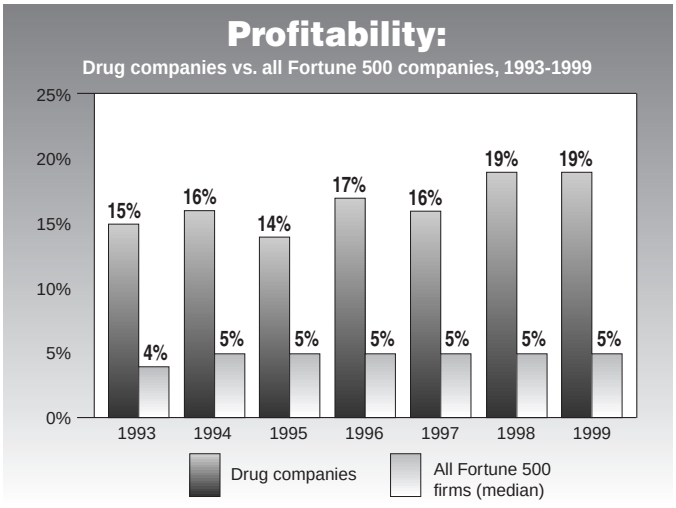
Prescription drugs: The real cost driver

While the state's Medicaid costs are rising — like that of all health care insurance programs — much of this is due to the rising costs of prescription drugs.

From 1987 to 2003 DSHS projected an eight-fold increase in the prescription drug costs paid by Medical Assistance, while the number of enrollees in Medical Assistance programs were only projected to double.

Clearly the increase in prescription drug spending is a much larger factor in the budget than increases in enrollment. Proposed Medicaid cuts like capping enrollment will do nothing to address the major source of cost increases.

Prescription drugs are the fastest growing cost in health care spending.[8] Yet the prescription drug industry is the most profitable in the world: the drug industry's median profit margin exceeded that of all Fortune 500 firms by three to four times in the 1990s.



Source: "Prescription Drug Trends" Henry J. Kaiser Family Foundation, Washington, DC, July 2000.

Several prescription drug companies have recently been the subject of investigations, fines and lawsuits — particularly pertaining to pricing schemes — and the U.S. government has increased its scrutiny of the business practices of pharmaceutical companies.[9]

For example, in the largest penalty to date against a health care company in a fraud prosecution, TAP Pharmaceutical Products has agreed to pay $875 million for charges of illegally manipulating the Medicare and Medicaid programs by inflating the reported price of its prostate cancer drug Lupron.[10] To settle charges under the False Claims Act, TAP will pay over $560 million to the federal government for Medicare and Medicaid violations, and $25.5 million to the states and the District of Columbia for Medicaid liabilities.[11]

Also, the General Accounting Office (GAO) has subpoenaed the drug company Pfizer's CEO Dr. Henry McKinnell after the company did not provide requested pricing information for the GAO's ongoing investigation of whether companies have improperly reported the price used to set Medicaid and Medicare reimbursement rates. Pfizer said the information should remain confidential. The Health and Human Services inspector general estimates that inaccurate reporting of drug prices costs taxpayers more than $1 billion per year just in overpayments for the few drugs Medicare now covers — mostly cancer drugs administered in a doctor's office.[12]

Prescription drug pricing

Drug prices are currently established through a complex web of arrangements between drug manufacturers and different private and public sector purchasers — like retail pharmacies, insurers, health maintenance organizations, hospitals and government agencies.[13] Most of

these agreements and pricing schemes are proprietary. Manufacturers sell the same prescription drug to different purchasers at a wide range of prices, and many of these prices are not available to the public.

Table 1
Washington residents lacking insurance for prescription drugs[16]

Age 65+ lacking Rx coverage	Lack any health insurance	Privately insured w/no drug coverage	Total lacking drug coverage	Percent lacking drug coverage
233,000	717,000	273,000	1,223,000	21%

Under the current pricing system, people without prescription drug coverage pay the most for prescription drugs,[14] as they do not have access to the rebates and discounts larger purchases can negotiate. Approximately one in five Washington residents are without prescription drug coverage.[15]

Table 2
Ten best-selling prescription drugs: Prices in Canada vs. the U.S.[17]

Drug	Drug is used for	Price per pill in Canada	Price per pill in U.S exceeds	% U.S. price exceeds Canadian price
Prisolec	Heartburn/Ulcer	$1.47	$3.31	125 %
Prozac	Depression	$1.07	$2.27	112 %
Lipitor	High cholesterol	$1.34	$2.54	90 %
Prevacid	Ulcer	$1.34	$3.13	134 %
Epogen	Anemia	$ 21.44	$23.40	9%
Zocor	High cholesterol	$1.47	$3.18	116 %
Zoloft	Depression	$1.07	$1.98	85 %
Zyprexa	Mood disorder	$3.39	$5.27	55 %
Claritan	Allergies	$1.11	$1.96	77 %
Paxil	Depression	$1.13	$2.22	88 %

And Americans pay more for prescription drugs than their counterparts just across the border. A comparison of the ten best-selling prescription drugs shows that drug companies set higher prices for the same drug in the U.S. than they do in other countries.

Overall, drugs are more expensive in the U.S.; per-person spending on drugs in the U.S. is almost twice that of other countries like the U.K. and Canada.

Table 3
Per capita spending on pharmaceuticals by country[18]

Country	Per Capita Spending
Canada	$251
U.K.	$251
U.S.	$408

The U.S. government does not currently regulate the price pharmaceutical manufacturers can charge for prescription drugs. But there are federal laws requiring manufacturers to give minimum price discounts to federal agencies, as well as laws requiring manufacturers to pay rebates to state Medicaid programs in order to have their drugs covered by Medicaid.[19]

Federal agencies generally purchase prescription drugs though the federal supply schedule of prices for pharmaceuticals — prices that are set to be better than or equal to the best price a manufacturer charges to a nonfederal customer under similar conditions.[20] On average these prices are estimated to be 42 percent lower than factory prices.[21] The rebates that state Medicaid programs receive was recently estimated to be about 19 percent of their total prescription drug spending.[22]

Washington can save money by changing how it purchases prescription drugs

Six Washington state agencies currently purchase or provide prescription drugs to over 1.5 million Washington residents. These agencies are: the Washington State Health Care Authority (HCA), Department of Health (DOH), Department of Social and Health Services (DSHS), Labor and Industries (L&I), Department of Corrections (DOC), and Washington Department of Veterans Affairs (WDVA). Of the over 1.5 million individuals served in 2000, 60 percent were served through fee-for-service programs, while the remaining 40 percent were enrolled in managed care programs. Many of these programs differ in numerous aspects of how they currently purchase drugs, creating a complex tangle of strategies.[23]

Table 4 only includes spending on brand name drugs in fee-for-service programs. The Washington Department of Corrections and Department of Veteran's Affairs also have fee-for-service programs, but their spending data was not available at print time. The state also purchases generic drugs, which are governed by a very different pricing structure, and so

Table 4
Estimated prescription drug savings for uninsured Washington residents and selected state agency fee-for-service programs under different pricing systems[24]

Payors	Current annual spending on brand name drugs	Rebates received as a percent of current spending	Estimated savings at current Medicaid rebate rate	Estimated savings at Canadian prices	Estimated savings at federal supply schedule prices
Uninsured Washington residents	$413,800,000	0%	$78,600,000	$151,900,000	$173,800,000
Medical Assistance Administration	$298,000,000	19%		$52,700,000	$68,500,000
Health Care Authority Uniform Medical Plan	$34,700,000	4%	$5,200,000	$11,400,000	$13,200,000
Department of Labor & Industries	$13,300,000	0%	$2,500,000	$4,900,000	$5,600,000
Department of Health AIDS Prescription Drug Program	$4,600,000	17%	$90,000	$900,000	$1,200,000
All Selected Agencies	**$350,600,000**		**$7,790,000**	**$69,900,000**	**$88,500,000**
All Selected Agencies & Uninsured Residents	**$764,400,000**		**$86,390,000**	**$221,800,000**	**$262,300,000**

were not included in the calculation.[25] The state purchases prescription drugs through managed care programs through both the Health Care Authority and the Department of Social and Health Services. Information on the current rebate rates received by the managed care programs is proprietary information according the organizations' contracts with the state, so the available data could not be used in the above calculation.[26] HCA's managed care programs alone spent $85.5 million on prescription drugs in 2000.[27] The state's current spending on prescription drugs, and potential savings based on the above pricing scales, is therefore even higher than the figures in Table 4.

Other states are pooling prescription purchases to save money

Rebate amounts from prescription drug manufacturers typically depend on the volume of drugs purchased — the larger the amount purchased, the greater the rebate.[28] A movement is afoot to pool purchases among larger and larger groups of buyers. States are pooling purchases between state agencies, and states are pooling their purchases together to negotiate larger rebates.

Numerous states already have state purchasing pools in the works. Texas, Georgia, and Massachusetts have passed legislation to create multi-agency purchasing programs and are in the process of setting up these programs.[29] Michigan and several other states have set up state preferred drug lists that apply to multiple state prescription purchasing programs.[30]

Two major multi-state coalitions are underway. The New England Tri-State Prescription Drug Purchasing Coalition — composed of Maine, New Hampshire, and Vermont — will start by implementing a purchasing initiative for the states' Medicaid populations, initially including 330,000 individuals. The uninsured and public employees may be added later. They estimate they will save 10-15 percent annually on prescription drug costs by pooling their purchases. The Southern States Coalition Pharmacy Working Group includes five states, and will initially include state employee plan beneficiaries; state Medicaid populations may be added later.[31]

In the Pacific Northwest, Washington and Idaho legislatures both passed resolutions in 2001 urging joint action with Oregon, Montana and other northwestern states.

As savings generally depend on the volume purchased, and Washington state programs currently purchase prescription drugs for over 1.5 million residents — over four times the size of the pool served by the Tri-State Coalition — Washington could attain greater savings than the Tri-State Coalition by simply pooling the purchases of its state agencies. Adding the uninsured and joining a coalition of the uninsured[32] and Medicaid recipients from the states of Oregon, Montana, and Idaho[33] would create a coalition serving over 4.8 million people. By joining such a program, Washington could spend even less on prescription drugs.

Table 5
Washington can save money by pooling prescription purchases: Larger volume purchases save more

Group	Number of people served
Tri-State Coalition[34]	330,000
Washington state agencies[35]	1,500,000
Washington state agencies and uninsured[36]	2,720,000
Washington state agencies and uninsured, and Medicaid enrollees[37] and uninsured[38] from Oregon, Montana, and Idaho	4,840,000

Washington can save money and help the uninsured by pooling the prescription drug purchases of its state agencies and opening these pools up to the underinsured and uninsured, private entities, and local units of government. The state has the potential to save even more money by pooling its purchases with other states.

The state of Washington has introduced legislation, House Bill 2431 and Senate Bill 6368, that would pool prescription drug purchasing. Using an extremely conservative calculation of the savings that could be produced by this legislation, the state agencies involved estimate they will save collectively between $4 million and $7 million annually once the program is set up. This number includes extensive estimations of the costs involved in setting up the program — from staff to the postage to mail out information to pharmacists and health care providers — and notes there may be less expensive and more efficient alternative methods to those estimated in this figure. But the figure is distinctly conservative in the calculation of the savings. For example, this figure does not include estimated savings from the inclusion of managed care health plans, claiming these savings cannot currently be quantified. Many agencies used percentage ranges of 5 percent or lower to estimate potential savings from their current spending on prescription drugs. Our estimates show the state of Washington is likely to save more than their estimate of $7 million annually on this program.

Conclusion

Washington should pool the prescription drug purchases of its state agencies; open these pools up to the underinsured and uninsured, private entities, and local units of government; and adopt legislation that would enable it to pool prescription purchases with other states. By doing so, the state can save money, help the underinsured and uninsured, and retain the strength of important public health care programs.

Endnotes

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8 Kaiser Daily Health Policy Report, January 8, 2002.

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15 Sager, Alan and Deborah Socolar. *A Prescription Drug Peace Treaty*. October 5, 2000.

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18 *Prescription Drug Trends: A Chartbook*, The Henry J. Kaiser Family Foundation, Washington, D.C., July 2000, p. 27.

19 Hansen, John. *United States Prescription Drug Pricing and Reimbursement Policies*. US General Accounting Office.

20 Ibid.

21 Sager, Alan and Deborah Socolar. *A Prescription Drug Peace Treaty.* October 5, 2000.

22 *Prescription Drugs: Expanding Access to Federal Prices Could Cause Other Price Changes*, US General Accounting Office, August, 2000.

23 *Washington State Prescription Drug Project Phase I Final Report*, June 29, 2001.

24 Sources: Current spending and rebate data on the agencies was provided by the agencies. Current spending is the 2000 total spending on brand name prescription drugs after rebates. Current spending on the uninsured is estimated from an October 2000 study by Sager and Socolar, Boston U. School of Public Health, "A Prescription Drug Peace Treaty: Cutting Prices to Make Prescription Drugs Affordable for All and To Protect Research — State by State Savings." This study is based on drug manufacturers' own reports of their revenues. The authors' Washington worksheet refers to these payments as "self-pay" and they are assumed to enjoy no discounts or rebates. This ignores discounts or rebates that might be paid to insurers for some patients — probably very few counted as self-pay but were in fact insured. See Appendix on Methods of the report cited above. The percentage savings for Canadian (36.7 percent) and federal supply schedule pricing (42 percent) is also from this report. These percentages were based on the "factory price," a figure that is not publicly available. Although the state currently purchases prescription drugs under a number of different pricing systems, applying these percentages to current spending provides an estimate of the difference.

Sample Calculations for Table 4:

1. Uninsured Data: Estimated uninsured WA residents spending on non-generics for 2000: $413, 852,839. Estimated rebate percentage: 0%.
   a. Savings at Medicaid rates (19%)
      413,852,839 * .19 = 78,632,039 = 78.6M
   b. Savings at Canadian rates: (36.7%)
      413,852,839 * .367 = 151,883,992 = 151.9M
   c. Savings at FSS rates (42%)
      413,852,839 * .42 = $173,818,192 = 173.8M
2. MAA Data: spending on brand-name prescription drugs (2000): $298,000,000. Medicaid's rebate percentage: 19%.
   a. Savings at Canadian rates: 36.7% - 19% = 17.7%
      298,000,000 * .177 = 52,746,000 = 52.7M
   b. Savings at FSS rates (42%) : 42% - 19% = 23%.
      298,000,000 * .23 = 68,540,000 = 68.5M
3. Health Care Authority (UMP) Data: non-generic spending for 2000 = $34,700,000, rebate percentage: 4%
   a. Savings at Medicaid rate 19% - 4% = 15%
      $34,700,000* .15 = 5.2 M
   b. Savings at Canadian rate: 36.7% - 4% = 32.7%
      $34,700,000* .327 = 11.4 M
   c. Savings at FSS rate 42%-4% = 38%
      $34,700,000* .38 = 13.2M

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31Ventimiglia, Samantha. *Pharmaceutical Purchasing Pools*, National Governor's Association Issue Brief, October 24, 2001.

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