NACDS NATIONAL ASSOCIATION OF CHAIN DRUG STORES

Testimony of the National Association of Chain Drug Stores Before the Colorado House Health and Human Services Committee

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Setting Medicaid Pharmacy Reimbursement Rates to Reflect Colorado Pharmacies' Cost of Dispensing

House Bill 08-1032

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Chairman McGihon and Members of the Health and Human Services Committee:

The National Association of Chain Drug Stores (NACDS) appreciates the opportunity to testify in support of House Bill 08-1032, a bill directs the Department of Health Care Financing to adjust Medicaid dispensing fees for generic drugs to ensure that those fees cover the cost of dispensing a Medicaid medication in Colorado and provide a reasonable profit. We support this legislation because of impending reductions in the federal upper limits (FULs) on reimbursement paid to Medicaid-participating pharmacies for multiple source drugs and because the Colorado Medicaid dispensing fee covers less than one-half of pharmacies' costs to dispense a prescription.

NACDS represents the nation's leading retail chain pharmacies and suppliers, helping them better meet the changing needs of their patients and customers. Chain pharmacies operate more than 38,000 pharmacies, employ 114,000 pharmacists, fill more than 2.4 billion prescriptions yearly, and have annual sales of nearly $700 billion. In Colorado, NACDS' 12 chain pharmacy members operate 587 stores with approximately 51,960 employees, including 2,203 pharmacists, and pay $447.56 million in taxes. In total, there are 731 chain and independent pharmacies in the state, that employ more than 53,090 workers, including 2,436 pharmacists, and pay $454.41 million in taxes.

The Impact of the Deficit Reduction Act

As you will recall from our discussions last year, all of Colorado's pharmacies were scheduled to be hit in January with a federally mandated reduction in the upper limits

(FULs) on state and federal payments for multi-source (or generic) drugs dispensed under the Medicaid program. The reduction is mandated under provisions of the Federal Deficit Reduction Act of 2005 (the DRA). The Government Accountability Office (GAO) predicted in December 2006, before the Centers for Medicare and Medicaid Services (CMS) first published its implementing regulations, now at issue, that those changes would reduce Medicaid payments for generic drugs to 36 percent, on average, below what it costs a pharmacy to purchase those drugs. The federal Department of Health and Human Services' Office of the Inspector General (OIG) separately concurred in predicting a significant impact on pharmacy reimbursement in 2007.

Dr. Stephen Schondelmeyer, Director of the University of Minnesota's PRIME Institute, has projected that reimbursement for generic drugs could drop 65 percent in the first year and more than 80 percent in subsequent years as a result of the changes to federal law. Dr. Schondelmeyer said this could result in the closure of 10,000 to 12,000 pharmacies over the next few years.

We expressed concerns last year that the financial impact from such a severe reduction in pharmacy payments could force Colorado's pharmacies to reduce hours, staff, inventory, and services, or – under a worst-case scenario – force pharmacies in low-income communities to close their doors, denying services to both Medicaid beneficiaries and other low-income residents.

Those concerns have not diminished, despite a federal court's recent temporary injunction against the implementation of the new FULs in a lawsuit that challenges the way CMS has interpreted the DRA. Federal statute still requires that AMP-based

FULs be implemented in some form and this will significantly reduce the Medicaid reimbursement paid to all pharmacies for generic prescription drug product.

Compounding the impending crisis is the fact that Colorado's dispensing fee – the other side of the Medicaid reimbursement equation – has long been inadequate to cover pharmacies' dispensing costs.

Current Dispensing Fees

Colorado's Medicaid pharmacies are currently paid a dispensing fee – the other segment of the Medicaid pharmacy reimbursement equation – that that falls well below the actual cost to dispense Medicaid drugs. In fact, the current $4 fee has remained unchanged since July 2001, when the fee was reduced from $4.08, where it had been since July 1990. The 2007 fee is just 22 cents higher than the $3.78 fee paid by Colorado Medicaid 22 years ago, in 1986, despite constantly escalating pharmacy costs. It is also just 38 percent of the $10.50 that a national survey conducted by an independent accounting firm found in 2007 to be the national cost of dispensing, and about 31 percent of what that same survey found to be the average cost of dispensing a prescription in Colorado ($12.96).[1]

The average profit margin for chain pharmacies is just 2 to 3 percent, a profit margin that has been continuously shrinking due to increasing product and administrative costs. With pharmacies already reimbursed at less than one-half the cost to dispense a prescription, reducing product reimbursement for generics to two-thirds of pharmacies' cost or less poses a real threat to their continued financial viability and, in

[1] Conducted by the accounting firm Grant Thornton, LLP, the study used data from over 23,000 community pharmacies and 832 million prescriptions to determine national cost of dispensing figures as well as state level cost of dispensing

turn, to Colorado Medicaid beneficiaries' access to prescription drugs and pharmacy services.

How The Deficit Reduction Act Works

As you will recall, the reductions in generic drug reimbursement will occur because the DRA mandated a change in how the maximum of what states can pay pharmacies for generic prescription drugs dispensed under Medicaid is calculated. The Federal Upper Limits (FULs) are now to be based on the lowest so-called "average manufacturer price (AMP)" – the price that manufacturers use in selling to wholesalers for resale to the retail pharmacy class of trade. The AMP data on which generic drug FULs, and pharmacy reimbursement, are to be based will not include the markup that retail pharmacies normally pay to wholesalers. This is a significant change from current practice, under which FULs have been based on the lowest list price (expressed as either average wholesale price (AWP) or wholesale acquisition cost (WAC)). In addition, FULs are to be established as soon as there is one generic on the market, rather than after there are two, as has been the case.

However, under the DRA, Congress also directed the Centers for Medicare and Medicaid Services (CMS) to clarify its guidance on the calculation of "average manufacturer price" by regulation. Unfortunately, in defining AMP, CMS unlawfully exceeded statutory language and congressional intent by including prices paid by, and discounts provided to, entities that obtain discounts and rebates not normally available to retail pharmacies. CMS redefined AMP to include discounts available to mail order pharmacies but not retail pharmacies. The definition also requires calculating AMP based on sales made by manufacturers to entities that are not wholesalers for drugs

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information for 46 states. This landmark national study was prepared for the Coalition for Community Pharmacy Action

that are not distributed to retail pharmacies, such as sales to individual patients and physicians, hospitals, surgical centers, dialysis centers, clinics, PBMs, and mail order pharmacies.

NACDS and the National Community Pharmacists Association (NCPA) – the independent pharmacies – objected to this overly-broad and unlawful definition. So did 46 United States Senators – including Colorado Senator Ken Salazar – who were so taken aback by CMS' plans to include these discounts and sales in calculating AMPs that they wrote CMS on March 13, 2007, asking that the agency revise its AMP regulations. CMS did not make the requested changes.

CMS also refused a request to extend the comment period on the final rule defining AMP beyond January 2, 2008, so that community pharmacy could provide feedback on the rule's impact based on the real AMP data scheduled to be made public in December 2007. At the same time, the agency refused a request by drug manufacturers to delay implementation of the rule by 90 days so that the manufacturers could ensure that the AMPs they were calculating to report to CMS were accurate.

Attempts by community pharmacy to achieve passage of federal legislation that creates an appropriate benchmark for Medicaid pharmacy reimbursement continue, but to date have been stymied by Congressional pay-as-you-go rules. While NACDS has offered several viable approaches to offsetting the cost of the legislation,

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(CCPA), with financial support from the Community Pharmacy Foundation.

Congressional staffers were unable to get CBO sign-off on those savings proposals before the 2007 end-of-year adjournment.

Litigation

As a result, NACDS and the National Community Pharmacists Association (NCPA) brought suit against CMS on November 7, 2007, in the U.S. District Court in Washington, D.C., alleging that the AMP rule established an illegal method of calculating AMP and FULs. The pharmacy plaintiffs stated that CMS' regulatory definitions of AMP and "retail sales" did not comply with the underlying statutory language, previous agency interpretations, or common usage.

The plaintiffs filed a motion for a preliminary injunction, asking that District Court Judge Royce Lambert prohibit CMS from using AMP data generated under the new rule to calculate FULs or publishing AMP data on the CMS website, pending resolution of the lawsuit. After a December 14 hearing, Judge Lambert granted the motion for a preliminary injunction.

In his written order granting the injunction, the judge said the plaintiffs were likely to prevail on the merits of the lawsuit and had demonstrated a clear threat of irreparable harm. Judge Lambert prohibited CMS from utilizing its new definition of AMP to calculate pharmacy reimbursement, and barred the agency from posting AMP data or AMP-based FULs on the CMS website or transmitting AMPs to the states, pending resolution of the litigation. The agency is allowed to utilize the new AMPs to calculate manufacturer rebates under the Medicaid program.

CMS has until mid-February to file a notice of appeal of the preliminary junction. If CMS files an appeal, it could be several months before it could be heard in the appellate court. In the mean time, CMS did file a pro forma answer to the complaint on January 14 denying all allegations.

Dispensing Fee Increases Still Needed

Despite the federal court's temporary injunction against the implementation of the new federal ceiling on Medicaid pharmacy reimbursement for generic drugs, the Colorado legislature should still act in increasing pharmacy dispensing fees to a reasonable level. It is important to note that the lawsuit does not address the inadequacy of state dispensing fees, and does nothing to ensure that Medicaid dispensing fees cover the cost for pharmacies of dispensing Medicaid prescriptions. Even if the federal court eventually permanently bars CMS from implementing the current AMP rule, the significantly lower AMP-based FULs mandated by Congress will still be implemented. Pharmacies serving low-income communities will still face a continued threat to their financial viability.

Conclusion

For these reasons, we urge the Health and Human Services Committee to pass out House Bill 08-1032, to help ensure that Colorado Medicaid dispensing fees are adequate to cover the costs of dispensing a Medicaid prescription and provide a reasonable profit. Passage of this legislation will help the Medicaid program continue to maintain beneficiary access to prescription drugs and pharmacy services at a level that is, as required under federal law, commensurate to the level of access available to the general population of the state.

Thank you for your continued interest in this important issue, crucial to those pharmacies, chain and independent, providing prescription drugs and pharmacy services to Colorado's approximately 401,700 Medicaid beneficiaries.