



Advising the Congress on Medicare issues

Medicare drug spending

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September 11, 2015

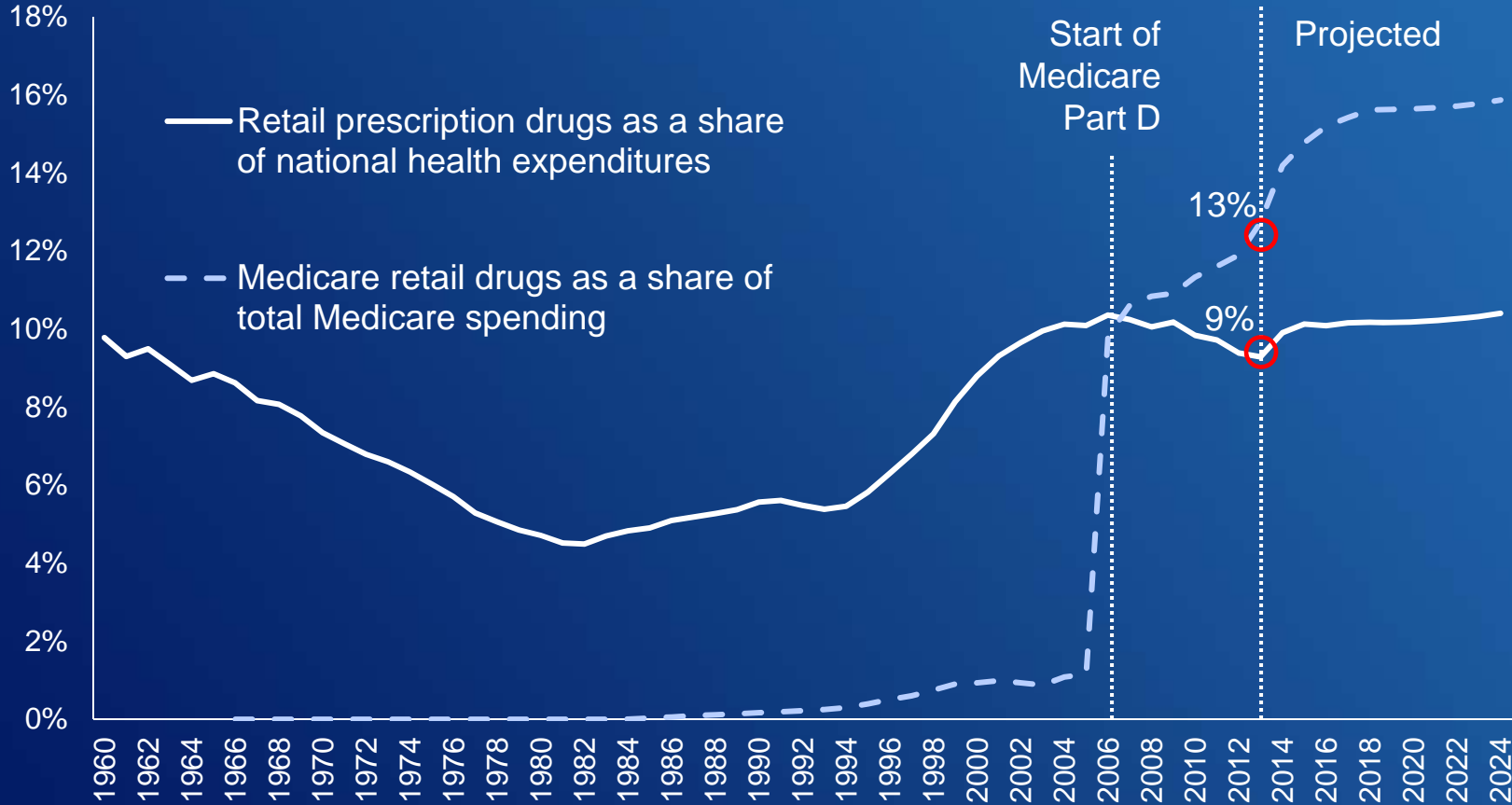
First of two presentations as context for discussing Medicare drug policies

- Today's topics
 - Magnitude of Medicare drug spending
 - How Medicare pays for drugs
- Next month
 - Background on pharmaceutical development
 - Structure of drug-related industries

Recent Commission work related to Medicare prescription drug policy

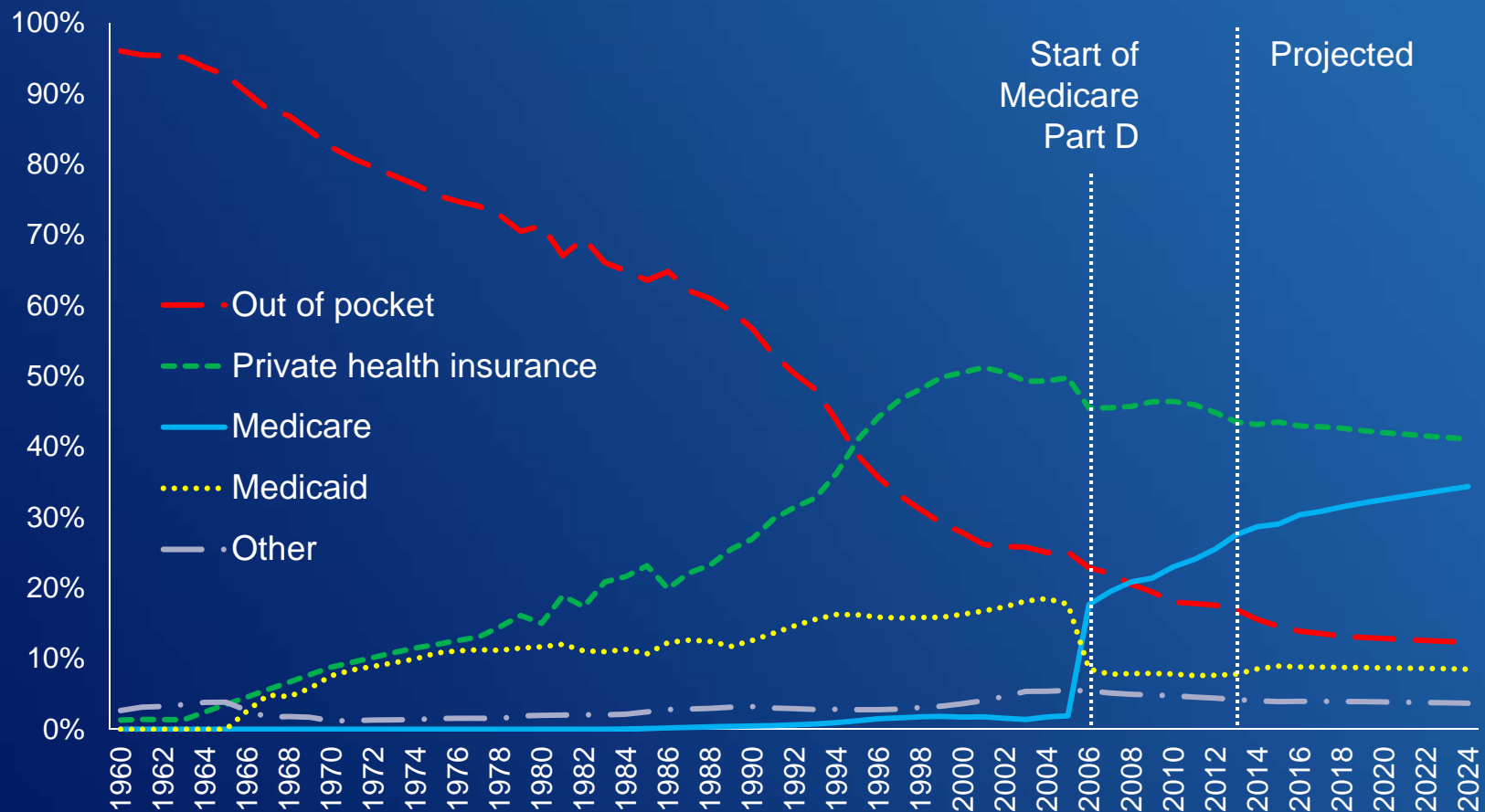
- ASP for Part B drugs
- Value-based approach/bundling for certain Part B drugs
- Part D risk sharing
- Medicare payment and beneficiary cost sharing for 340B drugs

In 2013, retail drugs made up 13% of Medicare spending v. 9% of national health expenditures



Source: MedPAC analysis of historical and projected data from CMS's national health expenditure accounts as of July 2015.

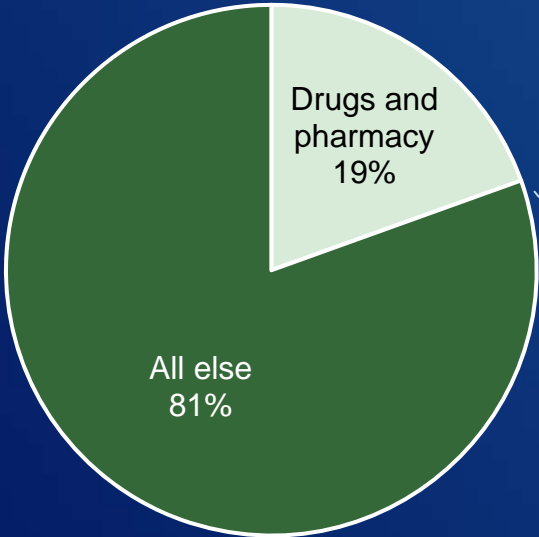
Medicare's importance as a payer for retail prescription drugs has grown



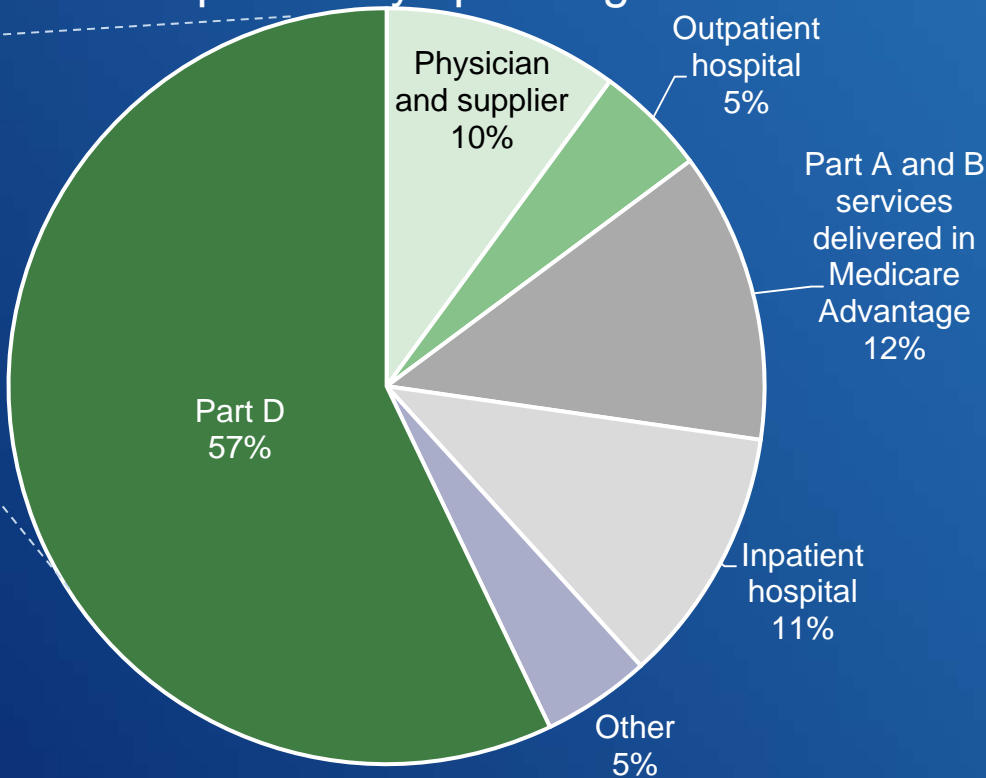
Source: MedPAC analysis of historical and projected data from CMS's national health expenditure accounts as of July 2015.

Broader estimate: drugs and pharmacy made up 19% of program spending in 2013

Medicare program spending = \$574 billion



Components of Medicare drug and pharmacy spending



Note: Estimates are preliminary and subject to change. Amounts exclude beneficiary cost sharing. Part C drug and pharmacy spending is assumed to be the same proportion of Part C program spending as in traditional Medicare program spending. Source: MedPAC analysis of Medicare cost reports, claims, and the 2015 annual reports of the Boards of Trustees of the Medicare trust funds.

Magnitude of Medicare drug spending in 2013

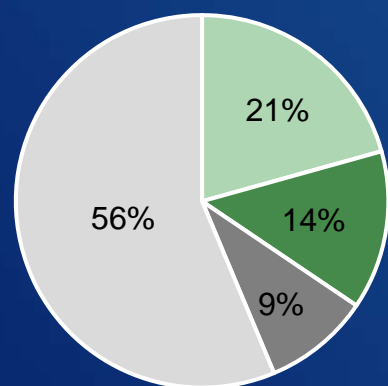
- Retail spending on prescription drugs
 - 9% of national health expenditures
 - 13% of Medicare spending
- Broader measure
 - Retail spending as above
 - Also drugs and pharmacy used as service inputs (e.g., for hospital, SNF, hospice care)
 - 19% of Medicare program spending

How does Medicare pay for drugs and pharmacy services?

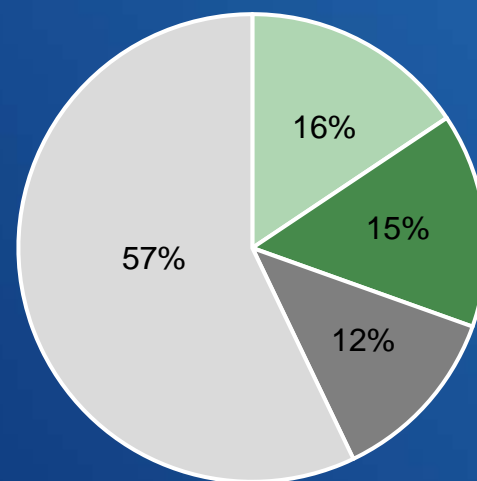
- Varies across health care sectors
 - Included within prospective payment bundles
 - Average sales price + 6% for certain Part B-covered drugs
 - Medicare Advantage plans receive capitated payments based on benchmarks and bids
 - Private drug plans receive capitated payments and reinsurance based on bids
- In each case, Medicare's influence over drug pricing is limited

Change in the distribution of Medicare's payments for drugs and pharmacy

2007 Medicare drug program spending of approximately \$82 billion



2013 Medicare drug program spending of approximately \$112 billion



- Fee-for-service prospective payments
- Fee-for-service average sales price-based payments
- Payments for Part A and Part B services delivered in private medical plans (Part C)
- Payments to Part D plans (both stand-alone and Medicare Advantage drug plans)

Note: Estimates are preliminary and subject to change. Amounts exclude beneficiary cost sharing. Part C drug and pharmacy spending is assumed to be the same proportion of Part C program spending as in traditional Medicare program spending. Source: MedPAC analysis of Medicare cost reports, claims, and the 2015 annual reports of the Boards of Trustees of the Medicare trust funds.

Prospective payment bundles

- Group together services expected to use similar levels of resources
 - Used for hospital inpatient, most hospital outpatient services, skilled nursing, hospice, and dialysis services
 - Drugs are an intermediate input
- Providers (and their group purchasers, wholesalers, and pharmacies) negotiate drug prices

Average Sales Price + 6%

- Infusible and injectable drugs administered in physician's offices and in hospital outpatient departments
- Reflects prices obtained by manufacturers based on sales to (nearly) all purchasers
- Payments are set administratively, but Medicare's influence on price is indirect because rates are set based on market prices

Medicare payments to Part D plans

- Based on bids that reflect prices negotiated among plan sponsors, pharmacies, and drug manufacturers
- Medicare pays 74.5% of basic benefits
 - Capitated direct subsidy
 - Open-ended individual reinsurance
- Low-income subsidy
- Law prohibits the Secretary from
 - Interfering with negotiations between drug manufacturers and pharmacies and plan sponsors
 - Requiring a particular formulary or instituting a price structure for reimbursement

How do other federal programs pay for outpatient drugs?

- Medicaid
 - Purchase drugs via retail pharmacies (as in Part D)
 - Statutory rebates as condition of coverage
 - Most states negotiate additional rebates by using preferred drug lists
- VA and DoD
 - Directly purchase drugs
 - Access to prices with statutory discounts
 - Obtain further price reductions using drug formularies

How do private payers obtain rebates and discounts?

- By the ability to “move market share”— encourage use of certain drugs over competing therapies
- Formulary management
 - Tiered cost sharing
 - Utilization management tools
 - Exclusion of some drugs from the formulary
- Evidence of comparative effectiveness

But obtaining price concessions may not be possible if there are no competing therapies

Next steps

- Presentation on drug-related industries in October
- Discussions about specific Medicare drug policy issues during this meeting cycle