California Association of Health Plans

MEDICAID MANAGED CARE LOWERS DRUG COSTS

According to a recent study — *A Dose of Managed Care: Controlling Drug Spending in Medicaid* — conducted by a team of professors at Northwestern University's Kellogg School of Management, under the auspices of the non-partisan National Bureau of Economic Research, **allowing managed care organizations (MCOs) to administer the majority of Medicaid drug benefits, as we currently do in California, significantly reduces state spending.**

The California Association of Health Plans shares Governor Gavin Newsom's objective of tackling the high cost of prescription drugs as evidenced by our strong support of efforts to bring down the cost of prescription drugs, including continued support for transparency into the pricing tactics of Pharma.

However, managing pharmacy benefits through Medi-Cal Managed Care plans is an important tool for addressing skyrocketing drug prices. That is why California has been a leader in "carving in" drug benefits to managed care.

> "Policy interventions such as price caps, limits on consumer out-of-pocket costs, and direct price negotiation between government programs and drug manufacturers — may be less effective than allowing MCOs to administer Medicaid drug benefits."
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> ~(Dranove, 2017)

The researchers analyzed differences in spending from 2010 – 2016 and compared 13 states that transitioned the administration of Medicaid drug benefits to Managed Care Organizations (MCOs) to spending in 16 states that did not outsource this administration and found that there are real benefits to having MCOs administer Medicaid drug benefits.

$ Fully transitioning the Medicaid drug benefit to MCOs decreases program drug spending by 22.4%.

"California's Medi-Cal plans can best serve their enrollees by coordinating the full range of services for their members, including administering their prescription drug benefits. This not only produces cost savings for the state, but also improves overall care for enrollees."

~California Association of Health Plans President and CEO, Charles Bacchi

For more information, please go to www.calhealthplans.org

Source: A Dose of Managed Care: Controlling Drug Spending in Medicaid, David Dranove, Christopher Ody, and Amanda Starc; NBER Working Paper No. 23956; October 2017; http://www.nber.org/papers/w23956

KEY FINDINGS

Fully transitioning the Medicaid drug benefit to MCOs decreases program drug spending by 22.4 percent. This significant cost savings for states is attributable to:

- Large reductions in the average price the state pays per prescription when MCOs administer the drug benefit.
- MCOs ability to negotiate with drug manufacturers for greater use of generic substitutes.
- Price differences reflecting the ability of MCOs to negotiate drug prices with pharmacies rather than rely on administratively set prices.
- MCOs are better able to steer demand away from high cost branded drugs and high cost pharmacies.

Carving out the Medicaid Drug Benefit will inadvertently Increase Pharmacy Profits at the State's expense:

- In a carve out model, states directly manage prescription drugs through a fee-for-service model. This model allows states to directly reimburse pharmacies with a fixed fee for filling a prescription, as well as a payment to cover the estimated ingredient cost, typically set as a percentage (85% - 95%, depending on the state, of the average wholesale price).
- The fee-for-service model allows pharmacies to earn profits on the difference between the estimated ingredient cost and the actual acquisition cost, which is often substantially lower.
- This model also gives pharmacies no incentive to utilize lower cost generic drugs.
- States with carved-out pharmacy benefits have experienced increased utilization of drugs with inflated estimated ingredient costs.

Why are MCOs able to negotiate lower drug prices?

- MCOs have more flexibility to shift patients from branded drugs to generics — which produced significant cost savings in carve-in states.
- MCOs can set binding price ceilings known as maximum allowable costs above which they will not reimburse a pharmacy.
- MCO's are not required to use a set formulary like states are, which allows MCO's to shift the mix of drugs and remove a pharmacy's incentive to dispense more profitable drugs.

MCOs are proven to produce significant cost savings for states:

- Roughly 40 percent of the overall decrease in spending per enrollee when MCOs are managing the drug benefit was generated by MCOs paying lower prices to pharmacies for the exact same drugs for which states paid more (for the same pill from the same manufacturer).
- The study also shows that states in which MCOs have control over drug formularies have the largest cost savings. (The effect of carve-ins is stronger when states allow MCOs to design their own formularies).

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