Iowa Department of Human Services

Terry E. Branstad
Governor

Kim Reynolds
Lt. Governor

Charles M. Palmer
Director

December 14, 2012

Michael Marshall
Secretary of Senate
State Capitol
LOCAL

Carmine Boal
Chief Clerk of the House
State Capitol
LOCAL

Dear Mr. Marshall and Ms. Boal:

Enclosed please find a copy of the report to the General Assembly relative to the Iowa Medicaid pharmacy dispensing fee adjustment recommendation between completion of the cost of dispensing survey.

This report was prepared pursuant to direction from the 84th Iowa General Assembly enacted during the 2012 Iowa Legislative session and contained in Senate File 2336, Section 33:

> No later than December 15, 2012, the department shall report to individuals specified in this Act for submission of reports, providing recommendations for adjusting pharmacy dispensing fees between completion of surveys to ensure fair and adequate reimbursement for pharmacies.

Please feel free to contact me if you need additional information.

Sincerely,

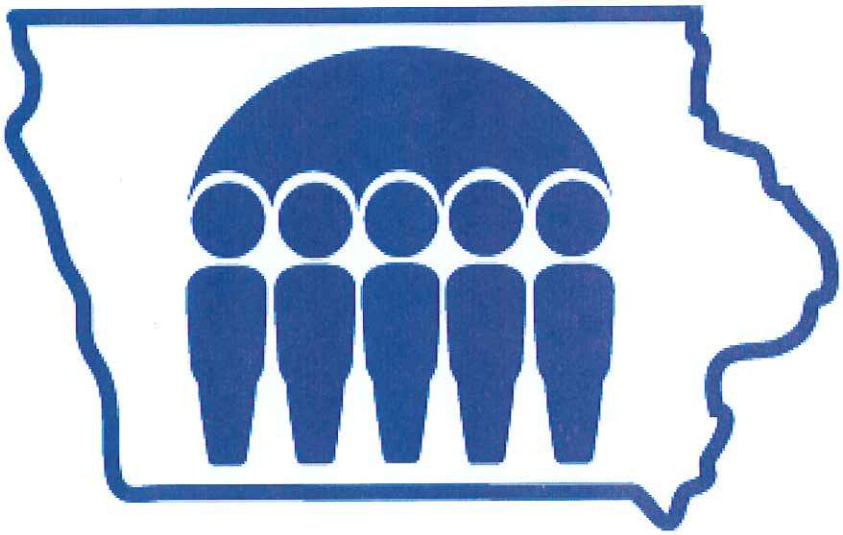
Jennifer Davis Harbison (dlj)

Jennifer Davis Harbison
Policy Advisor

JDH/slp
Enclosure

cc: Terry E. Branstad, Governor
Senator Jack Hatch
Senator David Johnson
Representative David Heaton
Representative Lisa Heddens
Legislative Service Agency
Kris Bell, Senate Majority Caucus
Josh Bronsink, Senate Minority Caucus
Carrie Kobrinetz, House Majority Caucus
Zeke Furlong, House Minority Caucus

Iowa Department of Human Services



Recommendation for Pharmacy Dispensing Fee Adjustment in Response to Senate File 2336

December 2012

Executive Summary

Section 33 of Senate File 2336 directs the Department to provide recommendations for adjusting the pharmacy dispensing fee between completion of surveys no later than December 15, 2012.

Other state Medicaid programs that utilize average actual acquisition cost (AAC) reimbursement methodology for drugs do not conduct annual cost of dispensing (COD) surveys or adjust their dispensing fee between COD surveys.

The Centers for Medicare and Medicaid Services (CMS) has a Proposed Rule that requires States to evaluate the appropriateness of the professional dispensing fee when changing the reimbursement methodology for drug ingredient cost. However, the CMS proposed regulations do not provide guidance regarding the frequency for updating the professional dispensing fee.

There are factors that make performing COD surveys on an annual basis impractical. These factors include provider fatigue and administrative burden, necessity for frequent COD surveys and dispensing fee updates, state plan amendment preparation, and inflation indexing.

Recommendation

The Department recommends *maintaining the dispensing fee at the level established by a COD survey in between COD surveys, and performing COD surveys every two years.*

Based upon experience from other Medicaid programs that implement an average AAC reimbursement, the recommendation will not decrease access for Medicaid members to pharmacy services.

The IME will continue to monitor for guidance issued by the CMS with regards to the frequency of dispensing fee updates as well as approvable methodologies for performing updates.

Iowa Medicaid Enterprise

Senate File 2336 Required Report
Recommendation for Pharmacy Dispensing Fee Adjustment

I. Introduction

Section 33 of Senate File 2336 directs the Department to provide recommendations for adjusting the pharmacy dispensing fee between completion of surveys to ensure fair and adequate reimbursement for pharmacies, no later than December 15, 2012. This document constitutes the Department's report issued in compliance with the legislative direction.

II. Background

The 84th Iowa General Assembly enacted during the 2012 Iowa Legislative session the requirement that the Department of Human Services (DHS) perform a cost of dispensing (COD) survey and implement an average acquisition cost reimbursement methodology for all drugs reimbursed through the Iowa Medicaid pharmacy program (Senate File 2336, Section 33). The Department was directed to determine its dispensing fee based upon a COD survey performed by the Department. In response to this legislation, the Iowa Medicaid Enterprise ("IME") conducted a pharmacy COD survey and is in the process of implementing an average actual acquisition cost (AAC) reimbursement methodology.

In addition, the Department was directed to produce a report providing recommendations for adjusting pharmacy dispensing fees between completion of COD surveys to ensure fair and adequate reimbursement for pharmacies. This document constitutes the Department's report on compliance with this legislative directive.

Given the increased level of importance of the pharmacy dispensing fee in a reimbursement methodology based on actual acquisition cost, there will be a greater need to establish a dispensing fee that reflects the average costs incurred by pharmacies to dispense prescriptions to Iowa Medicaid members.

A. Iowa Cost of Dispensing Survey

The IME hosted several stakeholder meetings from June 2012 to October 2012 with the purpose of discussing the various changes due to the legislation. In these meetings, the cost of dispensing survey was introduced to stakeholders and feedback was solicited. The stakeholders invited to the meeting included the Iowa Pharmacy Association (IPA), national chain drug store associations, and all enrolled pharmacy providers.

A cost of dispensing study was initiated in June 2012 following the methodology and using a survey instrument similar to those used by Myers and Stauffer in Medicaid pharmacy engagements in several other states. The methodology was consistent with guidelines from the Centers for Medicare and Medicaid Services (CMS) regarding the components of pharmacy cost that are appropriately reimbursed by the pharmacy dispensing fee of a state Medicaid program.

All 986 Iowa Medicaid-enrolled pharmacies were requested to submit survey information for the study. Myers and Stauffer performed basic desk review procedures to test completeness and accuracy of all dispensing cost surveys submitted.

B. Experience in other State Medicaid Programs

There are four other state Medicaid programs (Alabama, Oregon, Idaho, and Louisiana) that currently employ an average actual acquisition cost (AAC) reimbursement methodology for drugs. In these programs, drugs are reimbursed at the average AAC with a dispensing fee determined through a COD survey. This approach is identical to the methodology to be used in Iowa.

With regards to updates to the dispensing fee, none of these Medicaid programs conduct a COD survey annually or at any other predetermined frequency. They do not adjust their dispensing fee between COD surveys. In the programs that utilize volume-based tiered dispensing fees, the Medicaid volume of pharmacies is assessed on an annual basis for the purpose of assignment of pharmacies into dispensing fee tiers. However, dispensing fee values are not changed on an annual basis.

C. CMS Direction Regarding Professional Dispensing Fees

In its Proposed Rule published in February 2012, CMS made several major revisions affecting pharmacy reimbursement. Among the changes was the revision of the reimbursement for drug ingredient cost from "Estimated Acquisition Cost" to "Actual Acquisition Cost." Per legislation, Iowa Medicaid is shifting its reimbursement to average actual acquisition cost, which is in compliance with the Proposed Rule.

In addition, the CMS has proposed replacing the term "dispensing fee" with "professional dispensing fee" and requiring States to reconsider their dispensing fee methodologies when changing their payment for drug ingredient cost. Performance of pharmacy "cost to dispense" studies and adjustment of state reimbursement of dispensing fees to a level supported by the study to provide pharmacies a dispensing fee that acknowledges their observed cost to dispense would satisfy this requirement. However, the CMS does not provide guidance within its Proposed Rule regarding either the frequency or an acceptable process for updating the professional dispensing fee, aside from the COD study.

D. Considerations for Pharmacy Dispensing Fee Update

While the performance of an annual COD survey would provide information upon which to base updates to the dispensing fee, there are factors that make performing a COD survey on an annual basis impractical as a long-term process.

1. Provider fatigue/administrative burden: Provider fatigue from frequent sampling is one issue that would surface with annual COD surveys. Unlike acquisition cost surveys which require minimal administrative effort to respond, COD surveys are more involved endeavors. Requests for pharmacies to complete COD surveys on an annual basis can lead to decreasing participation rates in subsequent years due to the repeated level of work involved. Sufficient response rates are important for surveys to capture results that are most representative of the population.

2. Frequency of COD surveys and dispensing fee updates: While it is important to perform surveys of Iowa pharmacies to assess the costs for Iowa pharmacies to dispense drugs, it is unnecessary to conduct these surveys on an annual basis. The Medicaid programs that have implemented average AAC programs (as early as 2010) have not performed annual COD surveys or updated dispensing fees every year. These programs have not had any concerns from providers that the dispensing fees are insufficient to allow continued Medicaid participation. We are not aware of any Medicaid pharmacy program that performs an annual cost of dispensing survey.

3. State Plan Amendment preparation: Another factor for consideration is the process of submitting a State Plan Amendment (SPA) on an annual basis if adjusting the dispensing fee on an annual basis. CMS will require a SPA for changes to the dispensing fee. The SPA process is a lengthy process to complete with heavy involvement from the IME staff.

4. Inflation indexing: Some stakeholder groups have suggested the use of an inflation index, such as the Consumer Price Index, to automatically update the dispensing fee in between cost of dispensing surveys. The concept behind this idea is that the IME would not need to conduct a COD survey to update the dispensing fee every year, while the dispensing fee can be updated for increases in dispensing costs through an inflation index. However, there are several issues that make this approach impractical. There are no State Medicaid programs that currently utilize this approach to updating dispensing fees. We are unaware of analysis available that compares adjusted dispensing fees indexed to inflation factors to actual cost of dispensing to determine the accuracy of such an approach. Without this information, there is risk that the dispensing fees will be adjusted to a value that is not reflective of the cost that Iowa pharmacies incur to dispense prescriptions, potentially providing reimbursement greater than the cost for pharmacies to dispense prescription drugs.

Other factors besides inflation can also influence pharmacy cost of dispensing in both positive and negative directions. Dispensing costs can change over time based on changes in pharmacy efficiency and volume. For example, overall higher levels of prescription volume in a group of stores can lead to efficiency gains that may partially offset inflationary pressures. Similarly, the opening of new stores (typically with low prescription volume initially) or other declines in prescription volume at individual stores can lead to increases in average dispensing cost that are not specifically driven by inflationary pressures.

For time periods greater than two to three years, the use of estimates based solely on inflation factors may become unreliable. Accordingly, a schedule to update cost of dispensing survey information to recalculate the average cost of dispensing every two to three years is reasonable.

For years in which a cost of dispensing survey is not performed, there are several options available to the DHS relating to the use of inflation-based adjustments:

1. No inflation updates to the dispensing fee. This approach would recognize that inflationary pressures on the cost of dispensing over the relatively short time period of two to three years are relatively small and therefore does not require an adjustment to the dispensing fee. After two or three years, a subsequent COD survey is performed and the dispensing fee is updated to reflect current provider cost.

2. Inflation updates to the dispensing fee are performed on an annual basis. The most significant disadvantage to this approach is that each update of the dispensing fee will require that a SPA be filed with CMS with a corresponding lengthy approval process and the administrative burdens and notification requirements that accompany the SPA approval process. It is unknown whether CMS would approve a SPA with a methodology that proposed automatic adjustments to the dispensing fee reflective of changes in an inflation index.

3. A one-time inflation update could be applied to the cost of dispensing calculated from the current survey that will inflate dispensing cost to the midpoint of the anticipated rate-setting period. For example, if the IME were to opt for a three year survey interval, a dispensing fee that was implemented on January 1, 2013, would be expected to be in place until December 31, 2015, (after which a new fee, determined from a cost of dispensing survey performed in 2015, would be implemented). Accordingly, the dispensing fee to be implemented on January 1, 2013, would be inflation-adjusted to July 1, 2014, the midpoint of the three-year period for which the dispensing fee would be in place. The inflation update would effectively pay slightly more than the estimated average cost of dispensing for the first 18 months and pay slightly less than the estimated average cost of dispensing (adjusted for inflation) for the remaining 18 months of the rate period. Over the course of the three-year

period, the dispensing fee in place would represent the estimated average dispensing cost over the entire period. This approach is relatively simple and would have the advantage of only requiring one SPA approval process for each rate-setting period. It should be noted that the accuracy of estimates based on extrapolation over extended periods of time would potentially become unreliable. In addition, it is unknown whether CMS would approve a SPA with this proposed approach.

III. Recommendation

Upon consideration of the factors listed above, the following recommendation is presented for updating the dispensing fee in between COD surveys.

Recommendation: In between COD surveys, maintain the dispensing fee at the level established by a cost of dispensing survey. Perform a COD survey every two years to update the dispensing fee.

The recommendation to maintain the dispensing fee in between COD surveys is consistent with the dispensing fee update approach used by other Medicaid programs that implemented an average AAC program. While CMS has not provided guidance in its Proposed Rule regarding the update frequency of dispensing fees, CMS has approved SPAs for average AAC programs where the dispensing fee is not updated between COD surveys.

The frequency of surveys is recommended to be performed every two years, with the potential to increase the time between surveys to every three years after cost of dispensing results appear to be stable. By limiting the frequency of COD surveys to once every two years, the IME would decrease the potential for provider fatigue in responding to such survey requests. Maintaining sufficient survey response rates is important for the establishment of adequate dispensing fee reimbursement. This approach achieves the goal of maintaining future provider survey participation.

Based upon experience from other state Medicaid programs that implement an average AAC reimbursement, the recommendation will not decrease access for Medicaid members to pharmacy services. Within states where average AAC reimbursement is accompanied by a dispensing fee that is not updated between COD surveys, pharmacies continue to provide services to Medicaid members when the dispensing fee is not updated annually.

The recommendation of not applying inflation updates to the dispensing fee is coupled with the recommendation to perform a COD survey every two years. As previously discussed, the inflationary pressures on the cost of dispensing are relatively small over a two-year time span and therefore do not require an adjustment to the dispensing fee. After two or three years, a subsequent cost of dispensing survey is performed and the dispensing fee is updated to reflect current provider cost. The IME will continue to

monitor for guidance issued by the CMS with regards to the frequency of dispensing fee updates as well as approvable methodologies for performing updates.