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Managed Markets
MILITARY HEALTHCARE

LIKE THE PRIVATE HEALTHCARE SECTOR, THE MILITARY HEALTHCARE SYSTEM HAS EXPERIENCED RAPID GROWTH IN DRUG EXPENDITURES OVER THE PAST DECADE. AS A RESULT, THE DEPARTMENT OF VETERANS AFFAIRS AND THE DEPARTMENT OF DEFENSE ARE APPLYING STRICTER COST-MANAGEMENT PRACTICES.

While there has been much focus on the federal government's role with Medicare drug benefits, there are two other significant healthcare segments for which it is also responsible: veterans and military personnel.

In 2005, the Department of Veterans Affairs (VA) spent $4.2 billion on drugs and medicines, and in 2005, the Department of Defense (DoD) spent $5.4 billion on prescription drugs, according to the General Accounting Office.

The military healthcare system's expenditure on pharmaceuticals in the past decade has increased dramatically, and, according to study by Rand Corp., the increase is partly attributable to the double-digit growth in what was spent for prescription drugs.

As a result, both the VA and the DoD are applying healthcare management techniques, such as criteria for use, quantity limits, step therapy, and therapeutic interchange, as well as looking at overall care outcomes to manage costs.

The VA and DoD are applying techniques similar to those used in the private sector to manage pharmacy costs, utilization, and inappropriate use and medication errors. The two agencies have different structures, but they share some of the same processes, especially regarding the purchasing of prescription drugs. The two agencies have also invested heavily in healthcare information technologies.

DR. WILLIAM WINKENWERDER
DELOITTE CONSULTING
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BAYHAM CONSULTING
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GOVERNMENT BENEFICIARIES

The VA, which was established on March 15, 1989, succeeding the Veterans Administration, is responsible for providing federal benefits to veterans and their families.

The VA is the largest integrated healthcare provider in the United States. Almost 8 million patients are enrolled in its healthcare system, and the VA handles more than 57 million outpatient visits annually. During the past 10 years, the VA's patient load has doubled.

In fiscal year 2007, the VA is expected to spend more than $34.9 billion on healthcare, $41.5 billion on benefits, and $160.7 million on the national cemetery system.

In general, medications must be prescribed by a VA provider, filled at a VA pharmacy or through mail order, and be listed on the VA national drug formulary, which comprises 570 categories of drugs. In addition to the VA national drug formulary, facilities can establish local formularies to cover drugs not on the national formulary. In addition, tens of thousands of veterans are now receiving their prescription drug refills from the VA through a new service available over the Internet. More than 70,000 prescriptions have been refilled using MyHealtheVet, the personal online health record system.

The VA's and DoD's prices for particular prescription drugs included on their formularies may be the lowest of a ceiling price, which is the price listed on a federal supply schedule (FSS) or the price negotiated with a manufacturer.

"The federal supply schedule is a multi-award, multi-year federal contract that can be used by any federal government agency," says Alan Bayham, president of Bayham Consulting LLC. "There are a couple of trends that we are witnessing with the VA. One is that the agency — similar to what managed care organizations are doing — is establishing formula-

DEPARTMENT OF VETERANS AFFAIRS

- The Department of Veterans Affairs (VA) is the largest integrated healthcare provider in the United States.
- In 2005, the VA spent $4.2 billion on drugs and medicines.
- Almost 8 million patients are enrolled in the VA healthcare system. The system accommodates more than 57 million outpatient visits annually.
- The VA has an annual budget of almost $3 billion for mental health services alone.
- The VA negotiates directly with pharmaceutical companies through a statutory set lower price. Federal law dictates that the VA pay 24% less than a drug's private-sector wholesale price.

DEPARTMENT OF DEFENSE

- In 2005, the DoD spent $5.4 billion on prescription drugs.
- More than 9 million active and retired U.S. military personnel and their families receive drug benefit coverage through the DoD Tricare system.
- The military health system of the DoD provides medical care through a $42 billion dollar healthcare system consisting of a worldwide network of 70 military hospitals, more than 500 military health clinics, and an extensive network of private sector healthcare partners.
- The DoD Physician Data Transaction System connects the DoD database with 55,000 retail pharmacy outlets; about $3 billion in prescriptions are dispensed a year.

ry criteria, which are not necessarily based on cost. For example, a generic that has shown a high incidence of side effects may not be included. Case in point: in June of this year the VA was looking at monoamine oxidase inhibitors, MAOIs. These are mostly generic drugs that have been out for a while but the VA is evaluating them for side effects to make sure they are being used appropriately."

He says pharmaceutical companies need to be well-prepared to deal with the government, not only in terms of what is happening at the agencies regarding formulary policies but with various drugs, side effects, and so on.

"If a drug can help reduce the length of hospital stays, or prevent complications, or reduce hospital admissions, companies need to know what that means for total healthcare cost and be able to communicate that information," Mr. Bayham says. "Companies need to look beyond drug costs. They need to look at total healthcare costs and what role and value their drug has in that healthcare delivery system."

On Jan. 1, 2006, the VA instituted a $1 increase for a 30-day supply of prescription drugs; this was the first change in VA prescription drug copayments in four years. The increase to $8 from $7 was required by federal law, which bases the VA's copayments for outpatient prescriptions on increases in the Medical Consumer Price Index.

THE VA IS THE LARGEST INTEGRATED HEALTHCARE PROVIDER IN THE UNITED STATES.

One of the largest areas of therapeutic focus for the VA is mental health. With an annual budget of almost $3 billion for mental health services alone, the VA is the largest provider of mental healthcare in the nation. The VA employs more than 9,000 front-line mental health professionals, an increase of more than 15% from just four years ago. Today, mental health services are provided at each of the VA's 153 medical centers and 882 outpatient clinics.

More than 9 million active and retired U.S. military personnel and their families receive drug benefit coverage through the DoD three-tier copay Tricare system. DoD provides options for obtaining both formulary and non-formulary drugs. Beneficiaries can get prescription drugs through network retail pharmacies, non-network retail pharmacies, DoD military treatment facilities, and mail order.

Tricare's policy requires that prescriptions be filled with a generic product, if one is available. Beneficiaries currently pay the pharmacy copayment based on a three-tier formulary. Active duty service members do not pay copayments for prescriptions.

The Uniform Formulary (UF) process established a new cost share of $22 per prescription for both mail order and retail pharmacy services for medications that are being designated as nonformulary. Under the UF process, the DoD pharmacy and therapeutics (P&T) committee makes recommendations regarding which medications should be designated as nonformulary.

In the first full year since the DoD began implementing the UF process to review and classify prescription drugs, $500 million has been saved through improved formulary and contract management.

ELECTRONIC HEALTH INFORMATION

The VA and DoD have made tremendous investments in technology to be able to share health information.

In fact, the two agencies are working to

integrate their information systems. In August, the DoD and the VA successfully tested and deployed an interface that was developed to extend the reach and capabilities of the Bi-directional Health Information Exchange (BHIE), which is the mechanism that allows the two departments to share electronic health information on patients treated by both departments.

This new interface also allows VA providers to access information from all DoD healthcare facilities. Currently, medication and allergy profiles; laboratory results, including surgical pathology reports; and radiology reports are shared and viewed.

The types of data that will be shared through BHIE and this interface will be expanded in future releases to include patient problem lists, encounter notes, procedures, vital signs, family history, images, questionnaires, and other documents.

"Based on my experiences in the private sector and the Department of Defense, the government is ahead of the game in many areas, especially areas that relate to electronic transfer of data and doing business in a digital fashion," says William Winkenwerder, M.D., senior advisor, federal, state and commercial healthcare practices, at Deloitte Consulting. Dr. Winkenwerder also is the former assistant secretary for health affairs at the U.S. Department of Defense.

The Clinical and Health Data Repository initiative provides real-time exchange of computable health data between the Defense Department's electronic health record system, AHLTA, and the Veterans Health Information Systems and Technology Architecture, or VistA.

Every physician and healthcare provider on board is part of VistA. It is one of the most comprehensive and sophisticated electronic systems in use anywhere. VistA integrates all elements of a patient's health history — medications, lab work, X-rays, scans, EKGs, medical diagnoses, as well as other pertinent data in one place.

In addition, the DoD developed an integrated software application about four years ago called PDTS, Physician Data Transaction System. It is an Internet system that connects the DoD database with 55,000 retail pharmacy outlets.

"Four years ago, we consolidated all of the pharmacy contracts in the retail sector into one big contract and through that retail network, more than $3 billion in prescriptions are dispensed," Dr. Winkenwerder says. "The system connects with a retail pharmacy office so that a member's unique information can be accessed, and pharmacists are able to view a person's entire medical prescription history, not just those prescriptions from a particular chain. This system has been a real advance in terms of addressing adverse drug interactions."

Savings have also come from the DoD/VA pursuit of joint contracts for pharmacy programs. In fiscal 2007, it is estimated that the agencies will save almost $200 million alone by using joint national contracts.

With this electronic process, Tricare beneficiaries who also have other health insurance no longer have to file paper claims for prescriptions they fill at Tricare retail network pharmacies. Retail pharmacists submit the electronic claims.

The DoD's electronic program was launched in April 2006. In the following eight months, more than 350,000 Tricare beneficiaries used the service, and more than 1 million prescriptions were processed electronically.

The number of Tricare claims processed through the electronic program has increased an average of 15% each week.

Since the program's inception, Express Scripts Inc., Tricare's pharmacy contractor, electronically processed more than 850,000 prescriptions with Tricare as a second payer. ✦

NEGOTIATING DRUG PRICES WITH THE VA AND DOD

The VA and DoD have several options available to obtain favorable prices for drugs covered on their formularies. Both agencies pay the lowest of several prices available for a given drug, and both can negotiate with suppliers to receive additional discounts. In addition, both have adopted certain practices that affect negotiations, such as the use of formularies, or that otherwise contribute to lower costs, such as the use of mail-order pharmacies.

The VA and DoD have access to a number of prices to consider when purchasing drugs:

- FSS prices. The VA's National Acquisition Center negotiates FSS prices with drug manufacturers. These prices are available to all federal purchasers. FSS prices are intended to be no more than the price manufacturers charge their most-favored nonfederal customers under comparable terms and conditions. Under federal law, drug manufacturers must list their brand drugs on the FSS to receive reimbursement for drugs covered by Medicaid. All FSS prices include a fee of 0.5% of the price to fund VA's National Acquisition Center.
- Federal ceiling prices. Federal ceiling prices, also called Big Four prices, are available to the VA, DoD, the Public Health Service, and the U.S. Coast Guard. These prices are mandated by law to be 24% lower than nonfederal average manufacturer prices.
- Blanket purchase agreements. Blanket purchase agreements are national contracts with drug manufacturers that allow the VA and DoD — either separately or jointly — to negotiate prices below FSS prices. The lower prices may depend on the volume of specific drugs being purchased by particular facilities, such as VA or military hospitals, or on being assigned preferred status on the VA's and DoD's respective national formularies.

In a few cases, individual VA and DoD medical centers have obtained lower prices through local agreements with suppliers than they could have through the national contracts, FSS prices, or federal ceiling prices.

In addition, the VA's and DoD's use of formularies, pharmacies, and prime vendors can further affect drug prices. VA and DoD formularies encourage the substitution of lower-cost drugs determined to be as effective or more effective than higher-cost drugs. Both the VA and DoD use prime vendors, which are preferred drug distributors, to purchase drugs from manufacturers and deliver the drugs to VA or DoD facilities.

Source: United States Government Accountability Office, Washington, D.C. For more information, visit gao.gov.

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