United States General Accounting Office

GAO

Testimony

Before the Subcommittee on Civil Service
Committee on Government Reform and Oversight
House of Representatives

For Release on Delivery
Expected at 9:30 a.m.
Thursday, September 5, 1996

BLUE CROSS AND BLUE SHIELD

Change in Pharmacy Benefits Affects Federal Enrollees

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Health, Education, and Human Services Division

Mr. Chairman and Members of the Committee:

We are pleased to be here today to discuss the Blue Cross and Blue Shield Association's recent change in prescription drug benefits covered by its federal employee health plan. Of the approximately 400 health plans available to federal employees, the Blue Cross and Blue Shield Association's plan is the largest, covering almost 42 percent of about 4 million federal enrollees.

In recent years, prescription drug costs have accounted for an increasing share of the total benefits paid by the Association's federal employee health plan. To help control the plan's drug costs, as of January 1, 1996, the Association began requiring enrollees insured under the plan's Standard Option and covered by Medicare part B[1] to pay 20 percent of the price of prescriptions purchased at participating retail pharmacies. Before this change, these federal enrollees, like those in some other federal health plans, did not have to pay anything for retail prescription drugs. The enrollees may continue to receive drugs free of charge, however, if they purchase them through the plan's mail order program.

The benefit change gave enrollees an incentive to use the plan's mail order program. It also raised concerns, however, from Members of Congress and retail pharmacies about the quality of mail order services and the change's effect on the business of retail pharmacies that serve the plan's enrollees. To provide pharmacy services to its federal employee health plan (referred to as the Blue Cross and Blue Shield Service Benefit Plan), the Association contracts with two pharmacy benefit managers (PBM): PCS Health Systems, Inc., provides the plan's retail prescription drug services, and Merck-Medco Managed Care, Inc. (referred to as "Medco"), provides mail order drug services.

As part of an ongoing study of federal employee health plans' use of PBMs, we are looking at several issues concerning this benefit change and the performance of the PBMs that serve the Blue Cross and Blue Shield Service Benefit Plan.[2] Today, I would like to discuss the Association's reasons for the benefit change, how it was implemented, the change's effect on retail pharmacies, and the extent to which PCS and Medco have met their

[1]Medicare part B is a voluntary program financed by enrollee premiums and general federal revenues. It covers physician services and a variety of other health care services, such as laboratory and outpatient hospital services.

[2]Blue Cross FEHBP Pharmacy Benefits (GAO/HEHS-96-182R, July 19, 1996).

contract requirements for all services they provide to the Association's federal health plan.

To obtain information on the benefit change, we met with representatives of the Office of Personnel Management (OPM), Blue Cross and Blue Shield Association, Medco, PCS, National Association of Chain Drug Stores (NACDS), and American Pharmaceutical Association. Regarding the potential effect of the benefit change on retail pharmacies, we reviewed PCS data on recent changes in payments to retail pharmacies for prescriptions dispensed to the Association's federal enrollees. To determine the extent to which Medco and PCS met their contract requirements, we reviewed the Association's contracts with the PBMs and analyzed reports submitted to the Association on their performance in meeting contract requirements.

In summary, the Blue Cross and Blue Shield Association made the benefit change to try to control an average annual 21-percent increase in its federal health plan's drug costs and, as a result, hold down enrollees' premiums. At the inception of the change in early 1996, however, the volume of prescriptions the mail order pharmacy received was much greater and occurred more quickly than Medco or the Association had anticipated. During the last week of January, for example, prescriptions reached 233,000—an amount about 66 percent greater than anticipated. As a result, Medco could not meet its customer-service performance measure for prompt dispensing and delivery of prescriptions to enrollees for several weeks during the benefit change's implementation. Medco, PCS, and the Association collaborated, however, to respond to this increased volume, and, by mid-March 1996, Medco was meeting its customer-service performance measure.

Although the Association and Medco appear to have corrected the problems experienced in implementing the benefit change, NACDS and other critics of the change are concerned about its economic effect on retail pharmacies. Federal enrollees' shift to the Association's mail order program has been substantial. During the first 5 months of 1996, the total amount paid retail pharmacies for prescriptions dispensed to the enrollees affected by the benefit change decreased by about 36 percent, or about $95 million, from the amount paid during the same period in 1995.

In addition to assessing Medco's performance related to the benefit change, the Association reviewed both PBMs' overall performance in meeting their contract requirements in 1995. According to the Association,

the PBMs saved the Blue Cross and Blue Shield Service Benefit Plan about $505 million. The Association also indicated that the PBMs met most customer-service performance measures, such as dispensing prescriptions or answering customer calls within specific time frames.

Background

OPM contracts with almost 400 health plans, including fee-for-service plans and health maintenance organizations, to operate the Federal Employees Health Benefits Program (FEHBP). The Blue Cross and Blue Shield Association's plan is the largest, covering almost 42 percent of about 4 million FEHBP enrollees in 1994. The Association's contract with PCS for retail prescription drug services began in 1993; its contract with Medco for mail order drug services began in 1987.

In operating the retail drug program, PCS contracts with a network of pharmacies to provide the Association's federal employee health plan prescriptions at discounted prices. In 1996, this network included 44,751 pharmacies, about 60 percent of which were chain drug stores; the remaining 40 percent were independently owned. In operating the mail order program, Medco provides the plan prescriptions also at discounted prices. Medco receives and dispenses prescriptions from pharmacies in Florida, New Jersey, Ohio, and Texas.

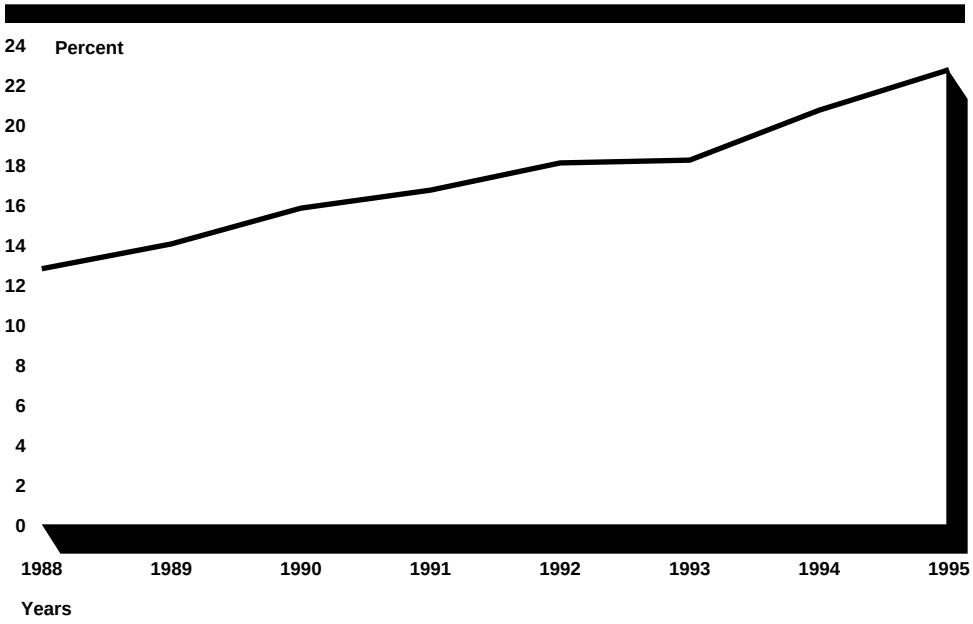
Under its FEHBP contract, the Association must submit to OPM any proposal to change its federal employee health plan benefits. OPM reviews such proposals to assess their cost-effectiveness to the program and potential effect on the delivery of benefits to federal enrollees. In addition, the Association oversees the activities of Medco and PCS and must report to OPM any significant problems that could affect the delivery of benefits to enrollees, such as those Medco initially experienced in implementing the benefit change.

Benefit Change Intended to Help Control Drug Costs

The Association submitted its benefit change proposal to OPM on May 31, 1995, citing the need to control the Blue Cross and Blue Shield Service Benefit Plan's rising prescription drug costs while maintaining quality service for enrollees. Between 1988 and 1995, the Association's payments for the plan's prescription drugs increased at an average annual rate of about 21 percent, compared with an average annual rate of about 12 percent for total benefit payments. Moreover, prescription drug payments have constituted an increasingly greater share of total benefit payments, rising from about 13 percent in 1988 to about 23 percent in 1995

(see fig. 1). These payment increases appear to result mainly from increases in the number of prescriptions per enrollee and the price of prescriptions.

Figure 1: Prescription Payments as a Percentage of Total Benefit Payments, 1988 to 1995



Source: Blue Cross and Blue Shield Association.

Before the benefit change, the approximately 800,000 people[3] insured under the Association's Standard Option Plan who also had Medicare part B coverage did not pay anything for prescription drugs purchased at network retail pharmacies or through the mail order program. These people must now pay 20 percent of the price of prescriptions purchased at network retail pharmacies.[4] Copayments for retail prescriptions were already required of other enrollees and are similar to those required in several other federal employee health plans. Without the benefit change, the Association contended that it would have had to increase monthly premiums for all of its federal enrollees with Standard Option coverage.

[3]This number includes federal enrollees and their dependents.

[4]In 1995, federal enrollees with Medicare part B coverage paid 20 percent in copayments for prescriptions purchased at retail pharmacies not included in the plan's network of pharmacies. In 1996, this amount increased to 40 percent.

Plan Developed to Meet Increase in Mail Order Prescriptions

To review Medco's strategy for managing the anticipated increase in prescriptions and calls about them, Association staff met with Medco representatives on August 24, 1995. According to Medco officials, they estimated the size and timing of the increase by relying primarily on their own claims experience in managing pharmacy benefits for about 50 million people as well as data from a comparable benefit change made by Massachusetts Blue Cross and Blue Shield.

The resulting Medco forecast estimated a gradual 64-percent growth in 1996 mail order prescriptions. Using this data, Medco planned to gradually increase its capacity to handle prescriptions from about 110,000 a week during the last quarter of 1995 to 180,000 a week during the last quarter of 1996. Medco also planned to handle occasional surges in demand of up to 13 percent more than the forecasted number and increase its telephone capacity to respond to greater demand for customer service. More immediate growth in mail order prescriptions could have been expected from this cost-conscious group of enrollees, however, according to our actuarial consultant's review of this forecast.

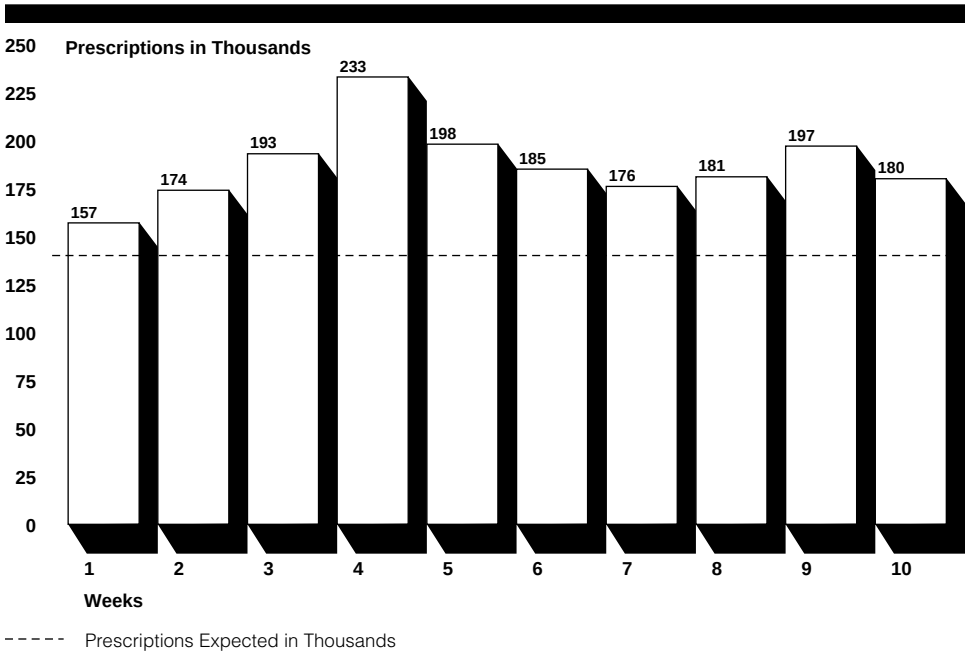
OPM notified the Association that the benefit change had been approved in September 1995. Both OPM and Association officials contended that the change would promote more cost-effective use of the prescription drug benefit by encouraging enrollees to use the less expensive mail order program. According to the Association's actuarial analysis, which included Medco savings estimates related to its contract, the benefit change would save the plan about $193 million in 1996. OPM's actuarial analysis supported this estimated level of savings. Although these analyses did not include an audit of Medco's estimates or related supporting documentation, our actuarial consultant's review of the Association and OPM analyses indicated that the overall savings estimates were reasonable, though possibly understated.

Demand for Mail Order Service Surpassed Expectations

The number of prescriptions received by Medco quickly surpassed Medco and Association expectations. During the first week of January 1996, the number of prescriptions rose to 157,000, and during the week ending January 27, 1996, they reached 233,000—an amount about 66 percent greater than expected. By the week ending March 9, 1996, and continuing through the week ending April 6, 1996, the number of weekly prescriptions received ranged between 175,000 and 187,000. Enrollees with Medicare part B benefits accounted for most of the increase in prescriptions. About 9 percent of these enrollees' prescriptions were purchased through the

mail order program in 1995, a percentage that increased to about 38 percent by February 1996. Figure 2 shows the increase in mail order prescriptions contrasted with the number of forecasted prescriptions.

Figure 2: Weekly Number of Mail Order Prescriptions Received, Week Ending January 6, 1996, to Week Ending March 9, 1996



Source: Medco.

Medco's processing capacity could not absorb this rapid increase. The number of pharmacists was insufficient to handle prescription orders, and many enrollees did not get their prescriptions filled promptly. For example, although Medco's contract requires that it dispense or return 99 percent of the prescriptions it receives daily within 5 business days, Medco reported that this performance measure was met about 87 percent of the time in January 1996 and about 94 percent of the time in February 1996. In addition, many customer calls were delayed or went unanswered during January and February 1996. Medco's contract specifies that no more than 2 percent of customer calls a week receive a busy signal, known as call blockage. Although the call blockage rate averaged 1.8 percent a week for the 2-month period, about 8 percent, or 11,000 calls, received a busy signal during the week ending January 20, 1996.

During the last week of January 1996, OPM informed Association officials of its disappointment with the customer service being provided to enrollees using the mail order program and indicated that corrective measures should be taken.

Actions Restored Service

Medco responded to the unanticipated demand and associated service problems by moving quickly to increase processing capacity. For example, during the week ending January 20, 1996, Medco officials expanded operations at the company's Florida and New Jersey pharmacies from a 5-1/2-day schedule to 7 days a week, with operating hours expanded from 15 hours to 19 hours daily. Medco also reassigned pharmacists who normally performed other Medco jobs to confirm phone and fax prescription orders. Medco officials also brought pharmacists and support personnel from pharmacies across the country to one Tampa pharmacy to increase processing capacity.

OPM and the Association agreed that Medco would send medications by overnight mail to customers who would not otherwise receive their prescriptions within 5 business days. Between the weeks ending January 6, 1996, and April 27, 1996, Medco sent approximately 160,000 prescription packages by overnight mail at a cost of almost $1 million.[5] In February 1996, OPM also indicated that the Association should arrange for mail order customers who needed delayed medications to get up to a 21-day supply from PCS network retail pharmacies without paying the 20-percent copayment. This ad hoc arrangement required PCS to respond quickly to the needs of the Association and over 5,000 enrollees who used this service.[6] The copayments for over 10,000 retail prescriptions dispensed to these enrollees cost the plan approximately $291,000.

Although Medco continued to use extra means to deliver prescriptions to enrollees through the last week of April 1996, Association data show that the mail order program began to meet performance expectations for turning around prescriptions within 5 days the week ending March 16, 1996. Medco had already begun to consistently meet performance expectations for customer service calls the week ending February 10, 1996.

[5]As of August 28, 1996, Blue Cross and Medco had not resolved which company would pay these overnight mail costs under their contract. A Medco official estimated the actual cost to be about $542,000, considering the cost Medco would have incurred by using the regular mail service.

[6]PCS officials said that although PCS was not contractually required to implement this policy change, the company developed procedures for it and implemented it within 1 week of learning of the problem.

Customer Service Surveys Reflect Difficulties

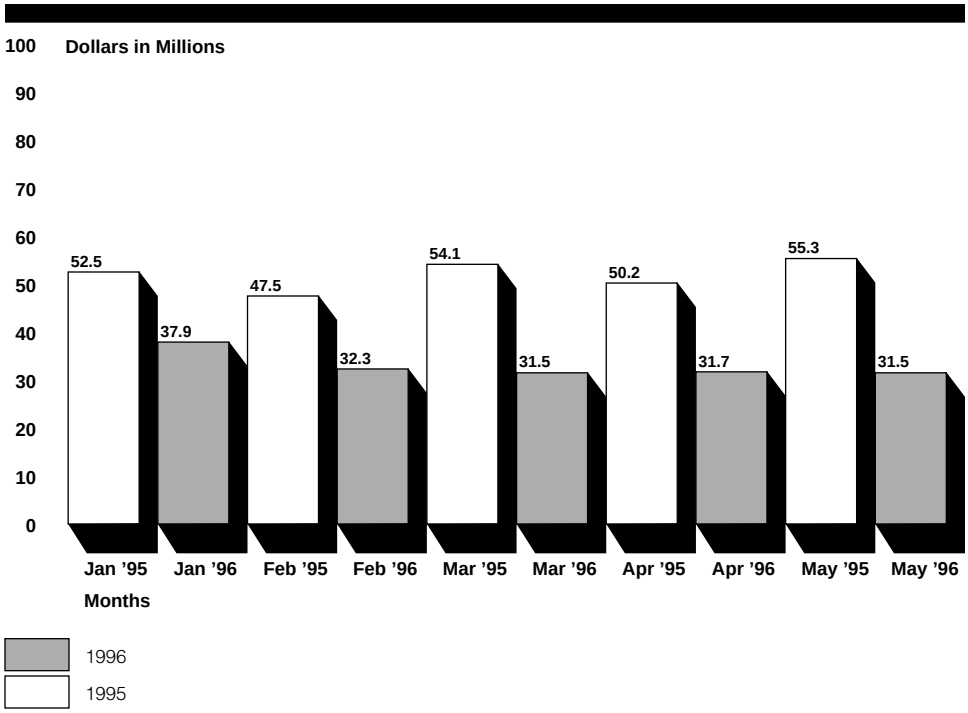
The difficulties enrollees had with the mail order program during early 1996 were reflected in an Association's customer satisfaction survey of mail order customers. During the first quarter of 1996, about 81 percent of those surveyed indicated that they were satisfied with services. Enrollee responses indicated that they were most concerned about the time it took to fill prescriptions. About 75 percent responded that their prescriptions were filled promptly, down from quarterly averages of 94 percent in 1994 and 92 percent in 1995.

Concern About the Effect of the Benefit Change on Retail Pharmacies

NACDS and many chain and independent pharmacies foresee the benefit change shifting millions of dollars in prescription drug sales to the mail order program. Because the benefit change is recent, we could not determine how many federal enrollees affected by the change will continue to shift prescriptions to the mail order program. Therefore, determining the benefit change's effect on retail pharmacies' sales is difficult. Nevertheless, payments to retail pharmacies for prescriptions dispensed to enrollees affected by the benefit change decreased substantially from 1995 to 1996, according to our analysis of PCS payments to retail pharmacies.[7] (See fig. 3.)

[7]All analyses of payments to retail pharmacies included copayments and deductibles paid by enrollees.

Figure 3: Payments to Retail Pharmacies for Prescriptions Dispensed to Enrollees With Standard Option and Medicare Part B Coverage, January to May, 1995 and 1996



Source: PCS.

Figure 3 shows that between January and May 1995, total prescription payments to retail pharmacies for prescriptions dispensed to enrollees affected by the benefit change were about $259.6 million, compared with about $164.9 million between January and May 1996—a decrease of about 36 percent.

Retail pharmacies serving the largest percentages of the federal enrollees affected by the benefit change experienced similar percentage decreases in prescription payments, according to PCS data. Between 1995 and 1996, Walgreens, Rite Aid, CVS, Revco, and Wal-Mart had, on average, a 41-percent decrease in total retail payments for prescriptions dispensed to the enrollees with Medicare part B coverage and a 14-percent decrease in total payments for prescriptions dispensed to all plan enrollees.

Total payments to all retail pharmacies for prescriptions dispensed to enrollees in the Association's federal employee health plan also decreased

between 1995 and 1996. This total includes payments to enrollees affected by the benefit change. PCS data indicate that between January and May 1995, total payments were about $473.3 million, compared with about $439.8 million between January and May 1996—a decrease of about 7 percent.

PBMs Met Most Blue Cross 1995 Performance Measures

The Blue Cross and Blue Shield Association contracts with Medco and PCS include annual performance measures that focus on savings and customer service. The contracts provide financial incentives for exceeding certain performance measures and penalties for not meeting them. According to information from Association officials, in 1995, Medco and PCS met most of their savings and customer service measures for the Blue Cross and Blue Shield Service Benefit Plan.

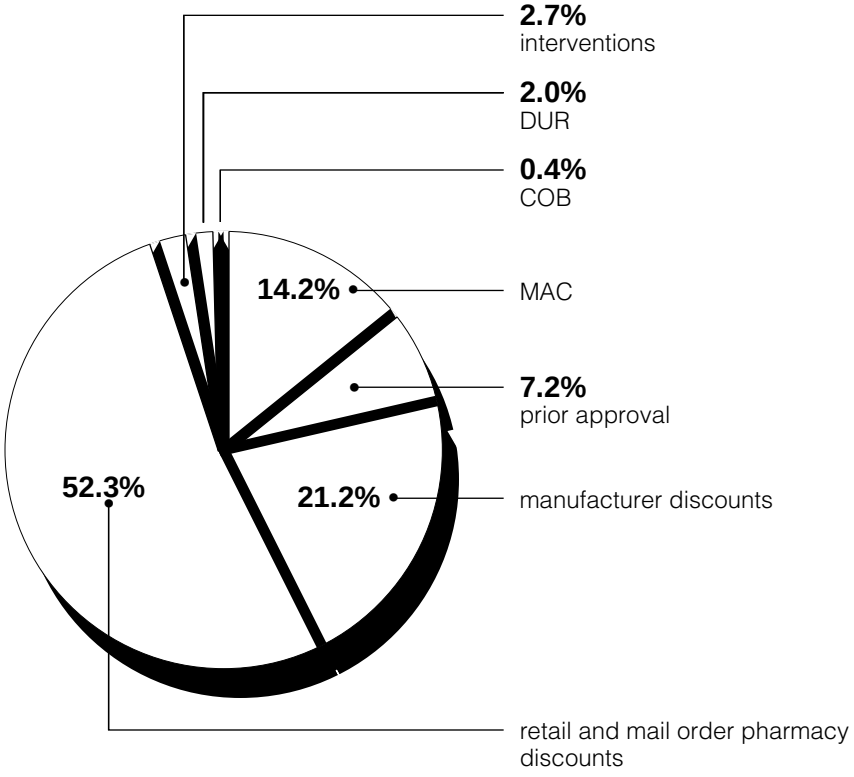
PBM Performance Produced Savings in 1995

The Blue Cross and Blue Shield Association estimated that its two PBMs saved the plan about $505 million in 1995. Association officials indicated that these savings are used to support the pharmacy benefit program, as well as to contain enrollee premiums, deductibles, and copayments.

Savings in 1995 resulted from seven categories of PBM services, according to Association estimates. These estimated savings were based on what the Association projected it would have paid for prescription drugs and related services had it not contracted with the PBMs. The Association developed this methodology, which represents one way to determine potential savings from PBM services. We plan to evaluate the soundness of this methodology and compare it with those developed by other federal health plans for our final report.

Figure 4 shows the percentage of total savings each of seven service categories represents.

Figure 4: 1995 Blue Cross FEHBP Pharmacy Savings



Source: Blue Cross and Blue Shield Association.

- Retail and mail order pharmacy discounts accounted for about $264 million in savings. For retail, the savings represent the discounts PCS achieved from negotiating with individual pharmacies the amount PCS would reimburse them for prescriptions.[8] Mail order savings were derived from discounts that the Association negotiated with Medco.
- Maximum allowable cost (MAC) savings accounted for approximately $72 million in savings. MAC refers to the maximum price that retail pharmacies in PCS' network may be paid for certain generic drugs. Savings resulted from the difference between drugs' MAC prices and their usual and customary prices.

[8]Total retail savings resulted from the difference between the reimbursement amount PCS paid pharmacies for all individual prescriptions and the drugs' usual and customary prices. The usual and customary price is what each pharmacy charges its cash-paying customers whose prescriptions are not covered by health plans.

- Manufacturer rebates accounted for about $107 million in savings and represent the guaranteed discounts that PCS and Medco negotiated with drug manufacturers. The plan received 90 percent of the total rebates, and the PBMs retained 10 percent as an administrative fee and incentive to increase the amount of discounts. PCS did not meet its rebate guarantee in 1995 and as a result incurred a penalty.
- Concurrent and retrospective drug utilization review (DUR) accounted for about $10 million in savings that resulted from clinical activities the PBMs performed. Concurrent DUR is performed before dispensing a drug to prevent problems such as drug interactions and therapeutic duplications. Retrospective DUR is a program PCS conducts to encourage physicians and enrollees to use the most cost-effective drugs and regimens to optimize drug therapies.
- Medco's intervention program accounted for about $13.5 million in savings. The program encourages patients to use, and physicians to prescribe, less expensive brand-name drugs considered as safe and effective[9] as other, more expensive brand-name drugs.
- The prior approval program accounted for about $36.5 million in savings. This program covers 13 drugs that require Association approval before dispensing and derived savings from prescriptions denied reimbursement or never filled.[10]
- The coordination of benefits (COB) program accounted for about $2 million in savings. COB is an industrywide method used to avoid paying duplicate benefits to an individual covered by another insurer.

Performance Measures Focus on Providing Quality Customer Service

The Association's contracts with its PBMs also specify performance measures for the quality of customer service provided to the federal plan and its enrollees. For example, as previously discussed, Medco's contract requires dispensing prescriptions and answering customer calls within specific time frames. Medco's contract also requires that its pharmacy dispense all of its prescriptions annually with less than a .005-percent error rate. In addition, PCS' contract has several guarantees for the accuracy and timeliness of prescription claims submitted by enrollees for

[9]Medco uses an independent group of health care professionals, known as a Pharmacy and Therapeutics Committee, to evaluate drugs in all therapeutic categories on the basis of safety, efficacy, and substitutability.

[10]Prior approval is required for medications that may be used to treat conditions or illnesses that are not covered by the Association, are outside the Food and Drug Administration or manufacturer guidelines, and have a high potential for abuse.

reimbursement. In two instances, PCS did not meet claims timeliness guarantees and therefore paid the Association minor penalties.[11]

PCS' contract also guarantees that it provide plan enrollees convenient access to its network pharmacies. The guarantee states that a network pharmacy be located within 5 miles of 98 percent of the enrollees. PCS data indicate that this guarantee was met in 1995 and as of April 1996.

Mr. Chairman, this concludes my prepared statement. I will be pleased to answer any questions.

For more information on this testimony, please call John Hansen, Assistant Director, at (202) 512-7105. Other major contributors included Joel Hamilton, Jennifer Arns, and Mary Freeman.

[11]According to PCS officials, neither instance disrupted service to enrollees, and the company was within 4 days of meeting the performance measure.

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