THE TAYLOR FELDMAN GROUP LLC

Erik Taylor
(916) 601-8542
erik@taylorfeldman.com

David Feldman
(530) 400-5470
david@taylorfeldman.com

Impact of Proposition 79 on Employers and Employees

No Health Premium Relief for Employers through Proposed Purchasing Program,
Drug Discount Card Increases Employee Prescription Drug Costs

Proposition 79 impacts employers and employees by proposing two different features – a state-assisted prescription drug purchasing program for a subset of employers and a drug discount card for employees below specified income thresholds. The intended goals of the purchasing program and discount cards are to provide more affordable prescription drugs to these populations; proponents also that the purchasing program will reduce health premium costs for employers.

This report assesses the impact of these provisions. We conclude that if voters enact Proposition 79:

- The purchasing program will not lower health costs and premiums for employers currently offering prescription drug coverage to employees.
- The discount card program will not be a meaningful alternative to insurance and would substantially increase out of pocket costs to employees who move from an insurance plan to the discount card program.

State Prescription Drug Purchasing Program and Employers

Proposition 79, Chapter 5, provides that the State "*may*" establish a prescription drug purchasing program to assist small businesses, small employer purchasing pools, and labor organizations (Taft-Hartley trust funds) that purchase health coverage for employees and their dependents. The measure also provides that the State shall *seek* to obtain drug rebates from manufactures and discounts from pharmacies that result in a net price "*comparable*" to the those achieved for the Proposition's discount card program. Unlike the discount card program, the purchasing program is voluntary for both pharmacies and manufacturers and is not tied to Medi-Cal participation. The initiative's proponents assert that the purchasing program will result in more affordable prescription drugs and health premium savings for the targeted groups.

Eligible employers' health plan premiums will not change as a result of the state drug purchasing program.

Prop. 79 Impact on Health Premiums

	Best Case	Worst Case
Prop 79 Change in Total Premium	$20 lower	$71 higher
as % of Total Premium	-0.2%	0.8%

Erik Taylor
(916) 601-8542
erik@taylorfeldman.com

David Feldman
(530) 400-5470
david@taylorfeldman.com

Small employers do not self-insure and do not purchase medical services directly. Instead, they purchase health insurance. Health insurance plans typically include benefits for prescription drugs. The prescription drug pricing and claims administration is the province of the pharmacy benefit manager (PBM).

Health insurance companies have significant market leverage and industry expertise to choose between PBMs. Overall drug discounts, rebate amounts and rebate sharing are key components of this decision. As a result, insurance plans already receive significant discounts on prescription drugs and they factor those discounts and rebates into the health plan premium price.

According to an analysis by William Hamm, commercial discounts currently range from 32% to 36%[1]. In any negotiation with manufacturers, the State of California will not have more leverage than the largest insurance companies (who are national in scope). Since the state does not have the ability in this program to manage both the formulary and the benefit plan, it is reasonable to assume the State of California is likely to achieve discounts in the same range, or perhaps a little less than, commercial discounts.

In order to access state purchasing program pricing on behalf of their clients, insurers and administrators would need to implement the state price list. This would require changes to existing insurance policies or creation of new insurance policies, as well as development of new administrative procedures (and the hiring of associated staff) and information technology projects (perhaps costing millions of dollars). These changes would increase the costs for administrators and those costs would be passed on to employers as a higher administration cost component of the premium.

The following table details the marginal impact of the state negotiated pricing and estimated insurer admin costs on a typical family health benefits premium.

	Current Commercial Pricing	Proposed State Program - Alternative Scenarios			
		Low Discounts Low Admin Cost	High Discounts High Admin Cost	High Discounts Low Admin Cost	Low Discounts High Admin Cost
Rx Discount	**34%**	32%	36%	36%	32%
Rx Cost	**$1,084**	$1,117	$1,051	$1,051	$1,117
Medical Cost	**$6,141**	$6,141	$6,141	$6,141	$6,141
Risk and Admin. Cost	**$1,275**	$1,288	$1,313	$1,288	$1,313
% of premium	**15.0%**	15.1%	15.4%	15.2%	15.3%
Premium	**$8,500**	$8,546	$8,505	$8,480	$8,571
$ Change in Premium		$46	$5	-$20	$71
% Change in Premium		0.5%	0.1%	-0.2%	0.8%

The table presents four different scenarios compared to current commercial pricing. Each scenario varies the drug discount and risk / administration cost. The commercial drug discount was set at the midpoint of the range described above. For the high discount scenario, we assumed the state was able to achieve discounts comparable to the best commercial discounts. For the low discount scenario we assumed the

[1] "An Economic Analysis of Two Prescription Drug Discount Programs", William Hamm et.al. Appendix E4

Erik Taylor
(916) 601-8542
erik@taylorfeldman.com

David Feldman
(530) 400-5470
david@taylorfeldman.com

low point of the commercial range. Additional risk/administration costs associated with the state program for the low administration cost scenario were assumed to be 1% higher than current factor, and for the high administration cost scenario they were assumed to be 3% higher than current factors.

Based on these calculations, we estimate a range of health premium changes – from a reduction of 0.2% to an increase of 0.8%.

State Drug Discount Card vs. Employer-sponsored Insurance

Proposition 79 sets up a pharmacy discount card program for a broad range of eligible individuals. The stated goal of the program is to reduce pharmacy drug costs for uninsured individuals by offering discounted prices at participating pharmacies. However, this program does not provide equivalent coverage compared to most employer-sponsored prescription drug plans.

Employees that lose their employer-based insurance will face significantly higher costs on average for prescription drugs, even if they are eligible for the discount card program.

Employers with employees eligible for the discount card may consider dropping the prescription drug portion of their health plan, assuming that the employee would be adequately covered with the discount card. However, health insurance provides much more coverage than a discount card. With health insurance, an employee pays a portion of the annual insurance premium and then, when filling a prescription, an employee pays a co-payment, deductible or coinsurance for discounted drugs. The insurance plan pays the remainder of the drug price. With the drug card, the employee pays an enrollment fee and then pays the *entire* discounted price for drugs.

The following table illustrates the annual difference between insurance and the drug card for three levels of drug utilization:

Employees with Rx Utilization will face higher costs under Cal Rx Plus

Employee Rx Cost with:	No Rx Use	Avg Utilizer	High Utilizer
Employer-based Insurance	$383	$746	$2,199
Cal Rx Plus Discount Card	$10	$1,580	$6,710
% Rx Card higher than Insurance	-	212%	305%

Discount cards would be lower cost for individuals who do not need prescription drugs, but for the average user, drug costs under the discount card program would more than double, from $746 to $1,580. High utilizers fare even worse as their costs more than triple from $2,199 to $6,710. The calculations are shown in Appendix A.

Erik Taylor
(916) 601-8542
erik@taylorfeldman.com

David Feldman
(530) 400-5470
david@taylorfeldman.com

About The Taylor Feldman Group

Erik Taylor and David Feldman, principals in the Taylor Feldman Group, bring extensive medical insurance analytics to this project with over 40 years combined experience in organizing and analyzing data to support decisions in the managed health care industry. They have delivered analyses to pharmacy benefit managers, insurance carriers, third party administrators, Fortune 100 Corporate clients, government agencies, and providers in both the workers compensation and group health plan arenas.

Taylor and Feldman previously directed the Analytic Consulting and Metrics Departments at First Health, a $900 million national managed care company. They worked directly with the CEO and other top-level executives and business units to increase sales, develop new products, improve operations, and maximize product effectiveness. They designed actuarial benefits modeling software and did extensive consulting with employers and union groups regarding medical and pharmacy benefit plan design and economic incentives to change patient behavior. They provided analyses and reporting on pharmacy program impact and benefit plan performance to the company's clients.

Prior to First Health, Taylor managed a client-reporting department for Blue Cross/Blue Shield of Massachusetts and worked for the California Health Facilities Commission as a health policy analyst. He received his bachelor's degree in Economics from the University of California at Davis. Feldman's prior experience was at the Health Data Institute, where he was responsible for evaluating the performance of various utilization management products for insurance carriers and large self funded health plans. He received his SB in economics from the M.I.T. and his MBA from UC Davis.

THE TAYLOR FELDMAN GROUP LLC

Erik Taylor
(916) 601-8542
erik@taylorfeldman.com

David Feldman
(530) 400-5470
david@taylorfeldman.com

Appendix A – Methodology / Sources

Comparison of Employee prescription drug costs when shifted from employer-based prescription drug insurance to Proposition 79's discount drug card.

With Employer-Based Insurance

Avg Premium (Medical, Rx, Admin)	$8,500
Medical loss ratio	86%
Avg Payments	$7,268
% Rx of Total Payments	15%
Rx Plan Payments	$1,090
Rx Discount %	36%
Employee cost share % (copay,coinsurance,deductible)	25%
Employee cost share ($)	$363
Employee portion of Rx premium (%)	30%
Employee portion of Rx premium ($)	$383
Avg Employee Rx Payments (premium+cost share)	**$746**
Avg Employee Rx Payments (high utilizer)	**$2,199**

With Discount Card

Rx Retail Charges	$2,271	
Discount % under prop 79	41%	
Avg Participant Rx Payments under Prop 79	**$1,350**	181% higher than $746 with insurance
Avg Rx Payments for Participants with utilization	**$1,580**	212% higher than $746
Avg Rx Payments for High Utilizers (5x avg)	**$6,710**	305% higher than $2,199

Sources

	Premium	EE share	Kaiser CA Health Care Chartbook
Single	$ 3,100	14%	July 2004
Family	$ 8,500	30%	
Medical Loss Ratio		86%	TFG Estimate based on Robinson, Health Affairs July/August '97
Drug Cost of total medical cost		15%	Milliman Medical Index 2005
Drug discounts	Third Party	36%	Hamm appendix e4
	Medicaid	41%	
No utilization - individual		38%	EBRI Issue Brief 265 January 2004
No utilization - Family		15%	TFG Estimate based on above
EE Pharmacy Cost share		25%	TFG Estimate based on EBRI Issue Brief 265