# Premium Development & Drug Pricing Trends

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# Key Points

- The current market for drugs in the U.S. is broken. It's time for a new drug pricing model that rewards needed biomedical innovation at prices patients can afford.
- As a fully integrated health care system we see high drug pricing trends as a threat to affordability and accessibility.
- We work every day to deliver the safest and most effective care possible to our 10 million members – to ensure access to needed treatment – looking at clinical evidence and coordinating patient care.
- Every other part of our health care system is committed to affordability and undergoing changes to pay for results and outcomes – drug companies need to be a part of this transformation as well.

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# Premium Development Process – Some Simplifications

- Kaiser Permanente as an integrated delivery system does not use a traditional fee-for-service (FFS) payment methodology for services offered in our facilities and/or by our healthcare professional practitioners
- Further, we perform services, that we term Integrated Care Management (ICM), that are not “codeable” under FFS methodologies such as emailing your physician, consulting an advice line, etc… that lead to better medical outcomes and lower total costs
- For simplification in our discussion today, we will refer to our internal interactions with our members, including ICM, as “claims”

# Conceptual Premium Development Process

- Premium = Projected Medical and Pharmacy Expenses + Retention (Administration costs and margin)
- Projected medical and pharmacy expenses are developed as a weighted average of group-specific projected claims experience and the projected claims experience of the entire pool (for example, all large groups), adjusted for a group's demographic characteristics such as age and location
- The larger the size of a group, the more weight is given to the group-specific experience relative to the projected experience of the entire pool (also called the Manual Rate)
- The group-specific experience weight is called a credibility weight or a credibility factor

# Conceptual Premium Development Process

- The largest groups, for example, 1000 member groups, have a credibility factor of 100% --i.e., projected claims are based entirely on the group-specific experience
- The smallest groups, for example, under 200 members, have a credibility factor of 0% --i.e., projected claims are based entirely on the experience of the pool adjusted for the demographics of the group

# Conceptual Premium Development Process

- Formulaically: Projected Expenses = (Group Projected Claims) x Credibility% + (Manual Rate) x (1-Credibility%) x Group-Specific Demographic Factors
- Premium = Projected Medical and Pharmacy Expenses + Retention (Administration costs and margin)

# Conceptual Premium Development Process

- Small Group and Individual premium rates are just a special case of the general methodology presented above
  - All projected claims are based on total pool experience
  - Affordable Care Act (ACA) rules limit, and in some instances, specify, the demographic factors you can use
  - ACA requires you price to the market risk, not to the risk underlying your experience

# Three Ways That Pharmacy Can Impact Premiums

1. Group-specific historical claims and/or total pool historical claims will contain the actual Pharmacy expense experienced and hence, be in the base expenses used for projections

2. Anticipated increases in claims due to expected increases in pharmacy expenses (i.e., trend) will be added to the historical base experience to reflect the projected experience for the period in which the coverage is provided

3. As copays and/or coinsurance for members increase, premiums are reduced for all members, but an offsetting increase in out-of-pocket cost for members using benefits subject to the copay/coinsurance is experienced

# Copays and Leveraged Trends

If copays do not increase as rapidly as gross expenses, premiums increase faster than gross expenses.

| | Year 1 | Year 2 | Increase |
|---|---|---|---|
| Before Copay Expense (Gross) | $100 | $120 | 20% |
| Copay | $20 | $20 | 0% |
| After Copay Expense* | $80 | $100 | 25% |

*This is the expense used to develop premiums.

# Overall Trend

- In 2016, the emergence of the blockbuster Hep C drugs (starting with Sovaldi) resulted in a 1%-1.5% additional increase in our premiums.
- Pharmacy expenditure trends continue to outpace regular medical trends by about 2 to 1.
- We anticipate much higher trends for specialty Rx (percentage increases in the mid to high teens) going forward.

# What We've Seen Happen re: Drug Costs Overall (NW)

- The Cost/Rx (per prescription) increased nearly 23% since 2012.
- The Total KP Pharmacy Spend in NW increased nearly 35% and the prescription volume increased nearly 10% since 2012.

# What We've Seen Happen re: Specialty Drugs (NW)

- Specialty drugs are about 56% of the Total Spend but only 1% of the prescription volume in 2015.
- The Cost/Rx for Specialty drugs increased 37% since 2012
- Specialty Drug Total Spend increased about 73% since 2012.
- In comparison, Traditional drug Cost/rx **decreased** 4% since 2012, and Total Spend on traditional drugs increased only about 5% since 2012.

# What We've Seen Happen re: Generic Drugs (NW)

- Generic drugs make up about 28% of the Spend and nearly 92% of the prescription volume in 2015.
- The Generic Cost/Rx increased 50% since 2012, and the Total Spend on Generic drugs increased over 75% since 2012.
- In comparison, the Brand Cost/Rx increased over 92% since 2012, and the Total Spend on Brand drugs increased over 23% since 2012.

# Takeaways

- The high pricing of drugs is contributing to premium increases.
- As a fully integrated health care system we see high drug pricing trends as a threat to affordability and accessibility.
- We work every day to deliver the safest and most effective care possible to our 10 million members – to ensure access to needed treatment – looking at clinical evidence and coordinating patient care.
- Every part of the health care system is committed to affordability; drug companies must take this into consideration when making pricing decisions.

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