

Summary

**Price Controls v. Negotiated Prices:** Debate about whether or not the system used by the Department of Veterans Affairs (VA) for purchasing pharmaceuticals is negotiations or price controls has been spurred by the “noninterference” provision of the Medicare Prescription Drug, Improvement and Modernization Act of 2003.<sup>1</sup> Critics of the provision say that Medicare should copy the VA’s “negotiated pricing” system rather than be precluded from “interfering” in the negotiations between pharmaceutical companies and the private plans that will offer the new prescription drug benefit. This contention ignores both the legal structure created by the Veterans Health Care Act of 1992 described below, and the logistic differences between the two programs. Specifically, the VA actually purchases individual drugs, while Medicare will not be paying for individual prescriptions, but rather contracting with private entities for enrollees’ drug benefits – like the Federal Employees’ Health Benefits Program contracts with health plans for government workers’ health insurance benefits.

**Veterans Health Care Act of 1992:** Public Law 102-585 established two major price controls for pharmaceuticals paid for by certain federally funded programs, and required companies to provide these discounted prices if they are to participate in Medicaid. The narrower price control provision applies to pharmaceuticals purchased by the VA (and DoD, Public Health Service and Coast Guard<sup>2</sup>), and it requires pharmaceutical companies to sell medicines to these so-called “Big-4” agencies at a minimum 24% discount off of their “non-Federal Average Manufacturer Price.” This price is also known as the “Federal Ceiling Price” (FCP). The broader price control provision of P.L. 102-585 requires pharmaceutical companies to sell medicines to the VA through the Federal Supply Schedule (FSS) at the “best price” offered to their most-favored private sector customers. The FSS best prices must also be made available to a large number of healthcare programs that receive Federal funding known as 340B entities. This “best price” provision thus grants Federal agencies and grantees an entitlement to piggy-back on top of private sector negotiations without actually conducting any negotiations themselves. Under the provisions of P.L. 102-585, the VA is entitled to receive the lower of these two controlled prices, i.e. either the FCP or the FSS’s best prices.

**Veterans National Formulary Restricts Access and Rations Care:** With the mid-1990s reorganization of the Veterans Healthcare System, the VA also instituted a national formulary that included closed and preferred classes. The pharmaceuticals included in these classes are obtained through contracts and similar arrangements that commit the VA to use these medicines and prevent the use of other medicines in the same class. Because the VA is guaranteeing market exclusivity under these contracts, they can also extract discounts below those required under Federal law. Only about 2% of classes have been classified as preferred or closed, and the vast majority of the VA’s pharmaceutical spending went for medicines purchased at the FSS prices.<sup>3</sup> In fact, for over 83% of the FSS items listed by the VA’s Pharmacy Benefits Management group, no Blanket Purchase Agreements, National Contracts, or other restrictive mechanisms have been implemented, and thus the VA buys these items at the FSS prices.<sup>4</sup>

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<sup>1</sup> 1860D-11(i) of the Social Security Act as added by P. L. 108-173.

<sup>2</sup> While the term “VA” means the Department of Veterans Affairs, the price control provisions of P.L. 102-585 that apply to the VA also apply to the Department of Defense, the Public Health Service, and the Coast Guard.”

<sup>3</sup> “In 1999, about 81 percent of VA and DOD’s combined \$2.4 billion in drug expenditures were for drugs bought through the FSS for pharmaceuticals.” VA and DOD Health Care: Factors Contributing to Reduced Pharmacy Costs and Continuing Challenges,” GAO-02-969T

<sup>4</sup> Analysis of the VA’s Pharmacy Benefits Management Strategic Healthcare Group FSS price list as of 8/8/04