The Outlook for 2017

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WITH THE TUMULTUOUS election behind us, our thoughts turn to a new year and the challenges that lie ahead. The Trump administration has promised to repeal and replace Obamacare, but the specific changes will be negotiated in the new Congress. President Trump promises to lower business and personal taxes, and that should inject additional dollars into the private sector as people and businesses have more money to spend and invest. These changes should be beneficial for the economy while also creating new opportunities and challenges for the pharmacy industry.

INDUSTRY CHALLENGES

We see continued pressure on pharmacy margins as payers continue to negotiate lower reimbursement rates with pharmacies. This situation will be impacted by the transition of fee-for-service Medicaid programs to cost-based reimbursement. Regulations require that state Medicaid programs in their state plan amendments take into account both the cost of the product and the professional dispensing fee in their reimbursement request to the Centers for Medicare & Medicaid Services (CMS). CMS has promised to evaluate the total reimbursement for the pharmacies before approving the plan amendments. Pharmacy will have to be diligent in evaluating the changes and educating its U.S. representatives on the impact these will have on pharmacy access. We do not expect to see this shift to cost-based reimbursement extend beyond Medicaid to commercial plans or Medicare Part D, at least in 2017.

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PREFERRED PHARMACY NETWORKS

Medicare Part D plans have implemented preferred pharmacy networks for approximately 80% of the beneficiaries covered. These networks require a deeper discount for the preferred designation and include direct and indirect remuneration (DIR) that has been problematic for pharmacies. The DIR fees charged to the pharmacy retrospectively have had a negative effect on pharmacy profitability. Prescriptions that were apparently dispensed at a profit turn into a loss months later. In response, NCPA and NACDS support proposed legislation (S. 3308/H.R. 5951) to prohibit Medicare Part D plan sponsors/PBMs (pharmacy benefit managers) from retroactively reducing payment on clean claims submitted by pharmacies under Medicare Part D, therefore eliminating retroactive DIR fees. The proposed legislation would require Part D plans to provide a DIR fee at the time of dispensing to enable the pharmacy to determine its total reimbursement. These bills are expected to be reintroduced in the next Congressional session.

We expect payers to continue to look for ways to leverage pharmacy providers to lower their costs and improve patient outcomes. The next step would be for pharmacies to accept risk-based reimbursement based on their clinical performance, e.g., Medicare Part D star ratings. Pharmacies must evaluate these potential opportunities to determine if they can manage the risk reviewing controllable versus noncontrollable issues. For example, a noncontrollable issue would be single-source brand price inflation. A controllable variable would be the generic efficiency rate expressed as a percentage that represents the times a generic is dispensed when a substitutable alternative is available.

Pharmacy owners will face tough decisions in 2017 on whether or not to participate in preferred networks. Options include participating in the open network, if possible, and then marketing directly to patients the benefits they receive from utilizing your pharmacy services. Since DIR fees have been a detriment to profits in 2016, pharmacy owners may decide to avoid these fees in 2017 and beyond.

DRIVING EFFICIENCY

The three main business drivers of financial results in the pharmacy are reimbursement rates, purchasing (cost of goods sold), and labor costs per prescription. Pharmacy reimbursement is for the most part not controllable, as many third party offers are take-it-or-leave-it propositions. Close focus on purchase effectiveness and ensuring that generics are purchased on contract to

deliver the lowest net cost are essential.

Technology solutions have been employed to lower the labor costs per prescription. These efficiencies, such as IVR systems, robotic dispensing, and med synchronization, enable pharmacies to dispense more prescriptions with the same labor input. We expect new innovations such as the Tech-Check-Tech pilot that will be launched in Wisconsin in 2017. This pilot will evaluate the accuracy of certified pharmacy technicians performing the second verification step in the dispensing process, instead of pharmacists. If successful, this will lower dispensing costs in the retail setting in a few years.

Enhancements to electronic health record systems should continue to move the decision-making on prior authorizations, step edits, and quantity edits to the point of prescribing. These changes will result in fewer prescriptions that require exception processing, leading to lower costs of dispensing. But these changes will be gradual and will also benefit prescribers, with reduced prior authorization forms to fill out and fewer calls from pharmacies.

CLINICAL SERVICES

Clinical service opportunities will be expanded in 2017. Pharmacy has done a great job of incorporating immunizations into its service offerings. Medication therapy management (MTM) has been less successful, mainly due to a paucity of cases per pharmacy and a reimbursement rate per minute that yields fewer gross profit dollars compared to dispensing prescriptions. In 2017, some states will be permitting influenza and strep testing under a collaborative practice agreement. In 2017, pharmacists should be closely monitoring these nondispensing pharmacist-provided services to measure patient uptake, profitability, and the ability to rapidly replicate across retail pharmacy.

INDUSTRY CONSOLIDATION

We expect industry consolidation to accelerate in 2017. Lower reimbursement rates are one reason we have seen an accelerated consolidation of pharmacies. We expect the Walgreens/Rite Aid deal to close in the first quarter of 2017. But 500 to 1,000 pharmacies must be divested before the FTC approves the deal. The financial press has reported that Fred's Pharmacy will purchase 865 stores.

There has also been consolidation in the PSAO (pharmacy services administrative organization) industry, with the formation of Arete Pharmacy Network, which combined H. D. Smith's Third Party Network and American Associated Pharmacies United Drugs. Arete Pharmacy Network announced the acquisition of RxPride, which was formerly owned by the Minnesota-based pharmacy-buying group Smart-Fill Management Group, Inc. These acquisitions enable the organization to reduce administrative costs across a larger membership base.

CHANGE IS THE CONSTANT

The pace of change continues to accelerate, and the ability to adapt and revise strategies and tactics based on limited information is critical. The potential repeal and replacement of Obamacare would likely create new healthcare products that enable patients to pick the one that best meets their family's needs. This may require pharmacy owners to market their services by documenting their value to attract new patients. We see flat-to-negative growth in the number of retail pharmacies. Replacement locations for profitable, aging locations will be the extent of most new pharmacy openings.

Pharmacy has to improve labor costs, which is something that pharmacy has the most control over. We expect to see an emphasis here in 2017. Many pharmacists would like to practice at the "top of their degree," which means providing clinical, nondispensing activities. Pharmacies taking a risk on Medicare D star ratings will need to invest in additional clinical services. It would not surprise us to see a bifurcation develop, where some pharmacists focus only on nondispensing clinical activities that generate a lower return compared to dispensing prescriptions. To maintain a similar net profit margin, a corresponding adjustment to pharmacist compensation may be implemented in the near future. While 2017 will present changes on the political front, we should not be surprised to see changes that reshape the pharmacy landscape. We will share our viewpoints on these changes as they unfold. **CT**

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