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Strategies for Controlling Drug Costs

by Forrest G. Hester, R.Ph., M.A.

As health care cost containment initiatives intensify, the need to control drug costs becomes more critical than ever before. Yet few oncology practices have sufficient time to develop a formal strategy to address the issue.

Many physicians and program administrators believe there is little they can do. After all, drugs used in oncology practice are inherently expensive, and there is a limited market over which to spread the cost of research and development. Moreover, there is a strong probability that today's drugs may be obsolete tomorrow.

Fortunately, a few fundamental strategies can help control drug costs and significantly contribute to the bottom line.

DEFINING DRUG COST

Traditionally, "drug cost" is viewed as product price alone. In other words, drug cost is the cost to purchase the particular agent in question. To understand the entire picture, however, it is necessary to consider drug cost as a continuum that includes:

- the selection of the specific drug regimen
- product acquisition
- inventory carrying costs
- delivery of the agent to the administration site
- administration of the drug(s)
- monitoring of the effectiveness of the drug(s), and finally
- the resulting clinical outcome.

Looking at the entire drug process in this manner allows for numerous opportunities in which to achieve savings.

Although a discussion of the entire continuum is beyond the scope of this article, reasonable attention to product acquisition and inventory carrying costs can produce substantial savings.

PRODUCT ACQUISITION

Average wholesale price (AWP) has become the benchmark by which to measure the cost of a particular pharmaceutical agent. AWP is the price that is listed in the *Red Book*, which is published annually and updated monthly by Medical Economics Data (5 Paragon Dr., Montvale, N.J. 07645). The publication is widely distributed and, over the years, has become a common resource for drug pricing.

Just as you would never pay sticker price for an automobile, neither should you pay AWP for a pharmaceutical. Better pricing can always be negotiated. The degree to which you can improve an AWP is usually determined by the size of your institution or practice (volume purchasing power), your business structure (e.g., for profit or not for profit), and/or your ability and willingness to join buying groups and develop prime vendor relationships with wholesalers. Also contributing to the bottom line is the particular pharmaceutical in question and whether it is available from just one or from more than one manufacturer.

Spread over the entire inventory, you should be able to improve on AWP by 15 to 17 percent.

INVENTORY CARRYING COSTS

Drugs on hand (current inventory) represent cost. Simply stated, dollars tied up in inventory are not available for other use, such as purchasing something else with the money or reducing debt. Where no debt exists, and where there is no immediate need for cash, dollars tied up in inventory reduce the cash assets of the organization.

Some inventory is always required to meet current needs. However, a balance must be achieved between providing adequate amounts of needed agents and limiting dollars tied up in inventory to an amount that meets only the immediate need.

Inventory represents risk. If you worked in a bank, you and your associates would be subjected to numerous security procedures and controls designed to safeguard the banks assets (cash), which you handled in the performance of your duties. You would not consider such controls excessive and would accommodate the rigid requirements such a system imposed. In contrast, in the clinical setting it is common for there to be no security proce-

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dures or controls, even for pharmaceuticals costing several hundred dollars a vial. As a result, cost is incurred through carelessness, inattention to detail, and, in some cases, theft.

The amount of risk is determined by the degree to which controls are established. For example, in a group practice, each physician may delegate the responsibility of ordering drugs to a nurse or other staff member. In other practices, one or two individuals may perform this task for the entire group.

Agents may be kept in one area, or they may be located in several locations throughout the practice facility. Pharmaceuticals may be purchased from one, two, or several sources. Physicians in practices may try to standardize agents, or each physician may order and use his or her own preferred agents.

While each method offers its own advantages, convenience is always a trade off against cost. Success is achieved by thoughtfully discovering the balance between control and convenience that best serves each organization.

TEN STEPS TO CONTROLLING DRUG COSTS

Simple strategies can help achieve savings.

1) Develop a procedure that centralizes control of the purchasing and inventory process. Assign responsibility for that function to one individual and designate a back-up individual.

2) Evaluate agents used by individual group members and facilitate a process designed to achieve as much standardization as possible. Doing so will enhance volume purchasing power and will also reduce the number of sources from which agents must be obtained.

3) Determine which agents should be maintained in inventory. Base your determination on historical information along with evaluations resulting from strategy number two. In addition, define the quantity needed of each item based on the frequency of expected orders and expected use. Establish reorder points and quantities required to maintain the needed inventory, but at the same time avoid excess. Allowing a reasonable margin for error, you should never have more of these agents on hand than is normally used during the time interval between deliveries.

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4) Concentrate efforts on those relatively few agents that represent most of your drug cost. It is not uncommon for 20 percent of all items purchased to account for 80 percent of total cost.

5) Identify drug wholesalers who service your area. Your local hospital pharmacy director(s) will know who they are.

6) After you have identified drug wholesalers, interview each to determine their level of interest in serving you and the level of services provided, such as the frequency of delivery. Frequent deliveries allow for smaller inventories, thus reducing the needed investment. Also important is the wholesaler's availability in emergencies, the frequency with which they are unable to fill an order, and their policy on returns. Obtain from each wholesaler a list of buying groups with whom they conduct business and who may be willing to extend pricing to your market segment.

7) Prepare a request for bid. This is simply a list of the agents you wish to purchase and the expected quantities to be purchased over a six-month or one-year period. Submit your request to those buying groups that do business with your prospective wholesalers.

8) As responses to bid requests are received, compare pricing as well as buying-group membership fees and services. For those items not available through the buying group, ask wholesalers to provide their best price. Award the contract to the buying-group/wholesaler combination that offers the best value to your organization.

9) Establish reasonable security and control procedures. The simplest accounting procedure applied consistently and accompanied by staff education on avoiding waste and loss goes a long way toward reducing drug costs.

10) Work closely with your selected wholesaler and buying group representatives. Ask them to evaluate your purchasing history over time and advise you about opportunities to reduce cost. A strong relationship with a good wholesaler and buying group can be your most effective strategy for controlling drug cost.

Although the high cost of drugs requires a significant capital outlay for inventory, these guidelines can lead oncology practices to a more favorable bottom line. ■