December 3, 2004

Honorable Lane Evans
Ranking Democratic Member
Committee on Veterans' Affairs
U.S. House of Representatives
Washington, DC 20515

Dear Congressman:

This letter responds to your request that we provide a formal cost estimate for H.R. 1309, the Veterans Prescription Drug Benefits Act of 2003, as introduced on March 18, 2003. That bill would direct the Department of Veterans Affairs (VA) to implement a prescription drug program for certain veterans. Because many of the specifics that would underpin a detailed cost estimate are left to VA's discretion and thus are difficult to predict, CBO cannot provide a precise cost estimate at this time. In this letter, we provide a description of the proposed program, an estimate of the number of veterans this bill would affect, and an estimate of total spending on prescription drugs that could potentially be affected by this bill.

Description of Proposed Prescription Drug Program

H.R. 1309 would direct VA to establish a new prescription drug program for all Medicare-eligible veterans and for those veterans who have service-connected disabilities rated at 50 percent or higher. Veterans with a service-connected disability rated at 50 percent or higher are considered priority 1 veterans and have the highest priority for the purpose of receiving health care from VA. Priority 1 veterans would be eligible to use this program in addition to receiving regular medical care from VA. Medicare-eligible veterans in priority categories 2 through 8 who enrolled in this program would not be eligible to use VA for any medical care other than the prescription drugs covered under this new program. The bill would provide for an annual enrollment period of two months beginning on August 1 of each year.

The bill would allow VA to dispense drugs and medicines prescribed by physicians or other authorized health care professionals who are not employed by VA to veterans enrolled in the new program. Under current practice, VA does not usually dispense drugs for prescriptions written by doctors or health care professionals who are not employed by the department. (Veterans who receive health care outside the VA medical system but want VA to fill their prescriptions are usually first examined by a VA doctor.)

Under H.R. 1309, VA would have to charge an annual premium to those veterans who enroll in this program and set copayments for each 30-day supply of a prescription drug. All costs to VA for administering this program for Medicare-eligible veterans, including the expense of new personnel, equipment, or new facilities, would be reimbursed by the Department of Health and Human Services (HHS) out of Medicare's Supplementary Medical Insurance (SMI) Trust Fund. Those payments from the trust fund would be considered direct spending. The annual premiums and copayments received from the Medicare-eligible veterans who participate in this program would be deposited into the SMI Trust Fund and would partially offset the cost of providing the prescription drugs to Medicare-eligible veterans.

VA would be responsible for the cost of providing prescription drugs to those priority 1 veterans who are not eligible for Medicare. However, CBO does not expect that many priority 1 veterans would enroll in this plan, as they are already eligible to receive free health care from VA, including prescription drugs.

Because the SMI Trust Fund would only reimburse VA for incurred costs, VA might initially need to use discretionary appropriations to fund the program. HHS would reimburse VA's initial outlay for the new program, and VA would be able to spend that reimbursement to further provide prescription drugs to the enrolled veterans. Upon spending the reimbursement from HHS, VA would receive yet another reimbursement from HHS that it also could spend to fund the new program. This process would repeat indefinitely. Thus, after spending an initial amount, VA would have a permanent stream of reimbursements from Medicare that could be used to fund the program.

How much discretionary spending VA would need to spend to fully fund the program would depend on how quickly VA would implement this new program and on how much time HHS would require to process VA's requests for reimbursement. (Under the bill, VA could take up to five years to fully

implement this new program.) For example, assuming it takes three months from the time VA submits its claim until it is reimbursed by HHS, and assuming that the SMI Trust Fund reimburses VA on a weekly basis, as specified in the bill, VA would have to incur additional net outlays of $1 billion in 2006 in order to provide a prescription drug benefit of $4 billion a year for every year thereafter. Alternatively, if reimbursements from the SMI Trust Fund were received by VA before the agency would need to pay the pharmaceutical companies, VA could operate this new program without using discretionary appropriations.

Estimate of Eligible Population

Using data from VA, CBO estimates that in 2005 more than 10 million veterans will be eligible for Medicare, about 25 percent of the total Medicare-eligible population. CBO also estimates that more than 3 million of those Medicare-eligible veterans are enrolled to receive health care from VA and about 2.5 million of those veterans actually receive care from the department. Most of the 2.5 million veterans currently receiving care at VA would probably not enroll in the new prescription drug program. Thus, the proposed program could affect up to 7.5 million Medicare-eligible veterans, although actual participation would depend on the amount of the annual premium and copayments, which are left to VA's discretion.

Estimate of Prescription Drug Spending by Medicare-Eligible Veterans

The premiums and copayments that VA would need to set would affect participation by Medicare-eligible veterans both in this new program and in Medicare Part D, Medicare's prescription drug benefit. Thus, VA's spending for this new program would be offset partially by reductions in spending for Medicare Part D. Costs also would depend on how quickly VA would implement the new program and how much of its discretionary appropriation it would spend to start the program.

CBO estimates that, under current law, total spending on prescription drugs for all Medicare beneficiaries will be more than $1.9 trillion over the 2006-2014 period. Using data from VA, CBO estimates that veterans will constitute about 25 percent of the total Medicare-eligible population in 2006; that percentage will fall to about 20 percent by 2014. Thus, CBO estimates that

total spending on prescription drugs for all Medicare-eligible veterans will be a little more than $400 billion over the 2006-2014 period.

However, many Medicare-eligible veterans already receive health care services and prescription drugs from VA and would be unlikely to use this new program. In addition, many low-income veterans will be eligible for free prescription drugs under the low-come subsidy program for Medicare Part D. Accounting for those veterans, CBO estimates that total spending on prescription drugs by the remaining Medicare-eligible veterans will be about $240 billion over the 2006-2014 period. Under current law, Medicare Part D, TRICARE-for-Life, and other federal programs will cover about $90 billion; the remaining $150 billion will be covered by private insurance companies or paid by the individual veterans.

Some portion—perhaps a substantial portion—of that $150 billion would be paid by Medicare under the new program that would be established by H.R. 1309. How much would depend on how VA structures the program. Low premiums and copayments might attract a substantial enrollment; high premiums and copayments would offset more of the costs and attract fewer participants. The veterans most likely to enroll would be those who have the highest costs that are not reimbursed under Medicare Part D. If VA provides a generous benefit with low premiums and copayments, veterans in the new program might use more prescription drugs than they currently do, adding further to Medicare's costs.

If you have any questions, the CBO staff contact is Sam Papenfuss.

Sincerely,

Douglas Holtz-Eakin
Director

cc: Honorable Christopher H. Smith
Chairman