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## PSNC Briefing 017/14: Purchase Margin and Margin Reforms

This PSNC Briefing explains the changes to assured levels of margin and the work to reform the systems for managing margin that have been agreed as part of the 2014/15 settlement.

### Introduction and the 2014/15 settlement

When the Community Pharmacy Contractual Framework (CPCF) was introduced in 2005 it was agreed that as part of the overall funding to be delivered to community pharmacies in England they would collectively be allowed to retain a guaranteed £500m in purchase margin each year, measured by a margin survey of independent pharmacies. [Purchase margin is the margin made when pharmacies are able to purchase medicines for NHS patients at prices below those at which the NHS reimburses them for those medicines. This is also known as 'retained margin' and it is measured after discount deduction.]

To date pharmacies have been able to retain purchase margin earned above the agreed £500m each year, and this provided, almost every year, substantial additional income. Since the National Audit Office investigation reported in 2010, there has been a drive to account fully for all margin income and to deliver a known and set amount of funding to pharmacy.

For 2014/15 NHS England have agreed that the assured annual purchase margins for community pharmacy should be £800m. This £800m will form part of the overall funding to be delivered to pharmacy under the settlement.

This is an important change in funding mechanisms, and the end to the system that allowed pharmacies to earn and retain additional purchase margins each year. That extra purchase margin reflected the massive success pharmacies have had in driving down medicines prices for the NHS, and provided funding, drawn not from NHS funds but from reduced prices, of varying amounts, but in the region of £250m.

As part of the agreement PSNC has committed to future changes to the funding mechanisms that will account for all margin within the annual sum. The settlement figure of £2.8bn therefore recognises the additional margin that contractors have earned and retained in previous years, accounting for the apparent increase.

To implement this agreement we expect to make more frequent changes to medicines prices, as well as addressing some other problems with how purchase margin is delivered, aiming to equalise opportunity to earn margin income and make the system as fair as possible to all contractors. These changes are being worked on and will take some months to finalise and implement, but PSNC has committed to collaborate to make them happen.

### FAQ: Will assured purchase margin change in future years?

Negotiations for future years have not yet begun so it is not possible to say at this stage what changes may or may not be made. PSNC's objective will be to protect contractors' income levels and to ensure stability of funding delivery as far as is possible.

### FAQ: Not all contractors make the same levels of margin, so how is this increase fair to those making less?

It is impossible to measure and assure margin levels at an individual contractor level. Instead the margins survey process calculates margins earned by independent contractors. The sample of pharmacies from which the data for the survey is obtained is chosen carefully to include a range of volumes and locations. PSNC will continue to

work to assure fair delivery of income to contractors as we make progress with DH on reforms to the reimbursement system.

### **The October 2014 reimbursement changes**

The emerging margins data suggests that keeping prices at the current level would result in an under-delivery of the £800m guaranteed for 2014/15 so an upwards adjustment has been made from October of £10m per month to seek to ensure provision in year of the £800m. This will be kept under review as more data becomes available.

### **Changes to reimbursement and margins reform**

As part of the 2014/15 agreement, PSNC has committed to a programme of work to reform the systems for managing margin delivery and make changes to reimbursement. The work will be carried out with DH, who retain responsibility for medicines reimbursement and the Drug Tariff, working closely with NHS England, the commissioner of community pharmacy services.

The following work has been agreed:

- Reforming the current system for managing margins, with more frequent adjustments to reimbursement prices.
- Developing a methodology for assessing multiples' margin. (This has not historically been assessed because the margins survey has used invoices from independent contractors).
- Changes to the Drug Tariff to equalise access to margin, including review of price concessions and arrangements for reimbursement of, Category A medicines, non-Part VIII products and specials.

### **FAQ: How will the new systems work?**

Although DH and PSNC have made progress in discussions, details have not yet been agreed, so it is not yet possible to comment on how they will work. The changes will take some months to finalise and implement, and it is likely that they will not come into effect before next April.

PSNC's objective throughout this work is to ensure fairness in income and margin delivery for contractors and ensure income stability. We are also concerned that any reforms to the systems for managing margins should maintain incentives for effective procurement and protect against any risk of under-delivery of the agreed margin levels.

## **Further information on retained margins**

### **Monitoring retained margins**

Monitoring the value of purchase margin being delivered to pharmacies is very difficult; in each financial year an estimate of the amount that has been delivered is made by PSNC and DH based on the results of the margins survey. This survey examines prices paid for a representative sample of medicines by a number of independent community pharmacies, analysing prices and wholesaler discounts from invoices from the pharmacies to estimate how much margin has been made in the year.

The survey is carried out retrospectively and so the results for any given financial year are only available in the summer of the following year (e.g. results of the 2013/14 survey were available in the summer of 2014).

### **Assuring delivery of margins – the future**

As outlined above, the NHS is now looking to deliver the agreed margins in future and we are working with them to reform the systems for managing margin. We expect to see more regular adjustments being made to Category M prices as this new system is introduced, and we will be seeking to ensure that delivery of margin to contractors is smooth and fair, and that the agreed margin levels are hit accurately each year, minimising the need for any subsequent adjustments.

For more information on the community pharmacy funding settlement for 2014/15 please visit the [PSNC Briefings page on our website](#) and see Briefings 015/14 to 019/14. If you require further information on margins please contact [Mike Dent, Head of Finance](#).