Explanation of 2012/13 interim funding agreement

The practice under the new contractual framework has been to settle funding for the financial year in time to make changes to fees, allowances and reimbursement prices in the October Drug Tariff, calculated to deliver the agreed funding sum by the end of the financial year. This timing is driven by the need to measure independents retained purchase margin accurately.

DH informed PSNC that, as we will not be able to determine CoSI based funding in time, it would need to make interim adjustments to the October DT. These were to reflect the results of the margins survey for 2011/12, which showed significant excess margins, to avoid accruing a significant overspend by March 2013, if funding remained at the core sum agreed for 2011-12 of £2.486bn. This work could have a significant financial impact for contractors and is too important to rush. In the meantime DH determined to apply adjustments as if funding continued at the annual level of £2.486bn.

Purchase margins are measured by the Margins Survey, using data from independent pharmacies. Margins earned in 2011-12 are calculated, and the calculations for 2012-13 assume that the same levels of margin continued. Projected full year payments to pharmacy, based on 2011/12 Margins Survey and projected item growth for 2012/13, were as follows:

Fees / Remuneration	£2008m
H1 Retained purchase margin	£347m
H2 Retained purchase margin	£347m
Total	£2704m

As such, projected over delivery of funding for 2012/13 was £216m.

By reducing Category M prices in October 2012 so that £250m in margin is delivered in H2, projected over delivery for 2012/13 is reduced to £119m. To ensure funding is not over delivered by £119m, Practice Payment levels are adjusted.

The calculations show that overall, a total of 45p must be removed per item so that funding is not over delivered in 2012/13. On this occasion the formula showed that the Practice Payment should be reduced by 25ppi and average reimbursement values by 20ppi. PSNC's Negotiating Team debated moderating the formula-driven result and felt that it was better to protect the level of Practice Payment. It proposed to the Committee tempering the reduction in the Practice Payment to 15ppi with the impact on average medicines reimbursement values being increased by 10ppi to 30ppi. The net result for the average contractor is the same, but the higher level of practice payment gave greater certainty in income to contractors. It was felt unlikely that any more radical rebalancing would be acceptable, given the need to avoid massive price shocks. The Committee accepted this proposal.

This adjustment total of 45ppi is an average figure per item. Whilst the specific impact of the reduction in the practice payment is predictable, the impact on margins of the reduction in reimbursement prices is less so. The impact on any individual contractor depends on their dispensing mix (brand vs generic and within generics) and also the response of the generics market in setting prices.

When the settlement for 2012/13 has been finalised further adjustments to the DT will be made to reflect the agreed sum to be provided for the year.