

## **Prescription for Transparency: A Partnership Focused on Drug Savings**

By Samuel H. Fleet

Miracle drugs have done much to contribute to increased longevity – but the costs of these new pharmaceuticals are also driving health care spending to new highs. The corporate world is painfully aware of the growing costs. Companies know they must have an attractive health care benefits package to retain talented employees – but they also have had to watch their profitability sag under the weight of increasing health care expenses. With baby boomers getting ready to swell the ranks of retirees, many with job-provided retirement health coverage, the pressure has never been greater to find ways to deliver clinically effective health care, including prescription drugs, at an economical cost.

For decades, Pharmacy Benefit Management (PBM) businesses have been part of the cost-containment strategies embraced by employers. Companies contracted out management of their drug benefits, expecting PBMs to negotiate the best pricing with pharmaceutical makers and distributors, as well as take the headaches out of claims administration. In more recent years, however, PBMs have come under scrutiny and employers have begun to question where their loyalties lie. Were they really interested in obtaining the best deal for the employer – or more focused on generating income streams that they could dip into for their own profit?

One response to the rising suspicion about their motivation has been the emergence of a new type of PBM – one that offered “transparency” so that companies would know everything that was going on behind the scenes. But transparency has not always been the as-advertised panacea. Simply because the employer now knew about the discounts, rebates and access fees did not ensure that the PBM was going to cast aside its own interests and operate wholly on behalf of the employer. There had to be a better way to ensure alignment of incentives so that both the PBM and the employer were pursuing the same goals.

The answer: transparency accompanied by a true partnership that directs the benefits to the employer and is funded by a fair administrative fee.

### **A History of Perverse Incentives**

PBMs got their start by promising deep drug price discounts and low administrative costs to employers that were made possible by negotiated price rebates from drug companies and bulk dispensing discounts from pharmacies. The PBMs made their profit margin by charging a small administrative fee, often on a per-transaction basis, and then skimming off a share of the rebates, discounts and other special fees they were able to arrange with the drug industry.

Eventually, employers began to question who was actually benefiting from the negotiations undertaken by PBMs. Not only were the employers upset that they were not receiving the full value of rebates and discounts, but they also were beginning to suspect that PBM decisions about formularies and utilization authorization might be influenced by something other than the best interests of the employers.

It was difficult for PBMs to argue that the incentives kept them aligned with employers’ goals. Because PBMs took a share of rebates and dispensing-fee discounts, their revenue grew if more people used more drugs – which could occur more easily if there was a lax utilization review process. Because negotiations resulted in different levels of rebates and discounts, it would only

be natural for a PBM to lean toward more generous drug makers and dispensers in making decisions, regardless of what the eventual cost to the employer was. And because rebates are available for newer drugs rather than generics, a PBM would be working against its own earnings if it counseled members to stick with older or generic drugs with the same efficacy of new drugs – even though such a choice would be cheaper for the employer.

More frequent use of drugs, higher costs for the drugs dispensed – these outcomes were the exact opposite of what employers hoped to achieve when they began contracting with PBMs. In short, there were simply too many reasons for a PBM to operate on behalf of its own interest for employers to be sure they were getting the best deal possible and maximizing cost savings.

### **The Promise of Transparency**

The PBM industry's answer to employers at first was to stonewall. They argued – somewhat reasonably – that they needed to make a profit somewhere, and that giving up their slice of fees and discounts would mean having to charge higher administrative costs upfront.

But soon PBMs seeking to differentiate themselves from competitors offered a better accounting of how they were making money. This new transparency was sometimes half-hearted: perhaps rebates were fully documented, but not access fees. Or deals with pharmacies were detailed, but discounts weren't shared. But soon transparent PBMs competed against each other to deliver the kind of performance employers were looking for.

Today, employers can compare PBMs to look not just for transparency but also for the key criteria that indicate the PBM will work as a full partner in the effort to contain drug purchasing costs while at the same time providing clinically appropriate care for employees. Those criteria include:

- **Per-member pricing.** When a PBM bases its administrative charge on transactions, it has an incentive to increase the number it performs. There is no such incentive when the pricing is based on the number of members in the plan. In addition, per-member pricing provides the employer with a total annual cost for administration at the beginning of the fiscal year, instead of a variable cost that can't be determined until the end of the year.
- **Rebate pass-through.** To eliminate a motive to base decisions about drug utilization and authorization on something other than clinical evidence, rebates and volume discounts should pass through to the employer rather than becoming a source of profit for the PBM.
- **Independence.** When a PBM is a subsidiary of a drug company, it's difficult to remain dispassionate about formulary choices and hard to be tough in negotiations that will produce the best discounts. Employers should look for a PBM that has no relationship to other industry companies but instead offers a solid track record of performance as an independent entity.
- **Rich formulary.** Good drug utilization review does not impose unnecessary barriers but instead is based on appropriate and effective clinical practices. PBMs that have a minimal number of drugs in each category of a formulary put members through extra hoops to gain approval without improving care or cutting costs. A well-developed formulary should provide multiple drugs per category to provide a broad span of choices while still maintaining effective control.

- **Consumer education support.** The best way to cut health care costs is to ensure that consumers have all the information they need to make wise choices. A PBM that supports the member education efforts of the employer is providing added value that will pay off in lower health care costs.

Between the rising costs of health care and the changing demographics of their workforce, employers already face a tough job when it comes to making health plan decisions. They don't need health benefit partners who are more interested in generating revenue than the cost savings they have promised. What they do need is a fully transparent partner who shares their goal of providing employees access to appropriate, effective drugs at the lowest possible cost. That's what real transparency and partnership is all about.

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