Specialty Healthcare Benefits Council
Defining Specialty Health

Strategies to Improve PBM Management of an Employee Prescription Drug Plan

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ABSTRACT

Background: Prescription drug expenditures are growing at a rate much greater than the expenditures in other healthcare categories. The emergence of specialty pharmaceuticals will continue the upward pressure on these expenses for the foreseeable future.

Objectives: To better manage the prescription drug benefit they offer to employees, employers must gain an understanding of the fundamentals of the pharmaceutical supply chain and the role of various stakeholders, including pharmacy benefit managers (PBMs).

Description: Some key considerations in the pharmaceutical supply chain, particularly the role of PBMs in managing prescription drug expenses are described. For employers who have internal expertise, there may be new opportunities to take more management responsibility for the benefit. In any case, a more engaged and transparent arrangement with the PBM, designed to provide the greatest value to the employer, is critical to maintaining the benefit of highest possible quality for their employees.

Conclusions: Employers should become informed consumers, understanding how revenue is generated by pharmacies as well as by intermediaries such as PBMs. Organizations, particularly those who have internal expertise or internal pharmacies, may be able to take advantage of opportunities to assume more management responsibility for the prescription drug benefit, working in a collaborative and more transparent manner with other stakeholders.

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Employee prescription drug plans are receiving increasing scrutiny due to the projections for significant increases in costs over the next several years.[1] Causes include the decreasing impact of patent expirations, increased utilization, and the introduction of expensive specialty drugs. Over the past decade, prescription drug expenditures have grown faster than any other healthcare category and make up an increasing percentage of per capita health spending.[2] The Segal Health Plan Cost Trend Survey projected prescription drug plan benefit cost increases of more than 7.5% for 2015—more than twice the rate of medical plan costs.[1,3]

The drivers of increased pharmacy benefit costs are generally recognized as: 1) increased utilization, 2) drug price increases, 3) introduction of new drugs and expanded indications, and 4) growth in the specialty drug sector.[1,4,5] The main drivers of the projected cost increases specifically in the next year are the introduction of new and expensive specialty drugs, as well as price increases for both brand name and generic medications. While specialty drugs generally make up 1% to 3% of all prescriptions, they account for over 25% of total prescription drug costs.[5,6] Furthermore, spending for specialty drugs is expected to rise at a rate of 15% to 20% per year for the next several years.[6,7] These forces are causing employers to examine methods and strategies for controlling the rising costs of providing prescription drug benefits to employees.

One key strategy to controlling prescription drug benefit costs is to understand and better manage the relationship with the pharmacy benefit manager (PBM). Given the complexity of prescription drug benefit programs, it is an attractive option to simply turn over management of the employee prescription drug benefit to a PBM using standard clinical and plan designs. However, it is important to realize that while they are serving clients' needs, PBMs are also in business to make a profit. Therefore, the actions that they take may not always be in the best interest of an employer.[8] For that reason and others, employers are increasingly attempting to better understand the prescription drug benefit in order to develop new strategies to control costs and to maintain an affordable, quality drug plan for their employees. Organizations that have internal expertise in medicine and pharmacy, such as health systems and some colleges and universities, may be in an excellent position to assume greater management of their prescription drug benefit.

PRACTICAL IMPLICATIONS

Employers should become informed consumers and when possible, take advantage of internal expertise and capabilities in order to improve the management of their prescription drug benefit.

- Employers will benefit from having well-trained in-house leadership over pharmacy management.
- For employers with internal expertise, assuming greater management of the benefit can be advantageous.
- Given the projected growth of traditional and specialty pharmacy expenses, employers should be educated and work with the PBM to ensure appropriate use according to best practice guidelines and elimination of waste, and should strive for a transparent relationship that provides the best outcomes and lowest net cost for the plan.

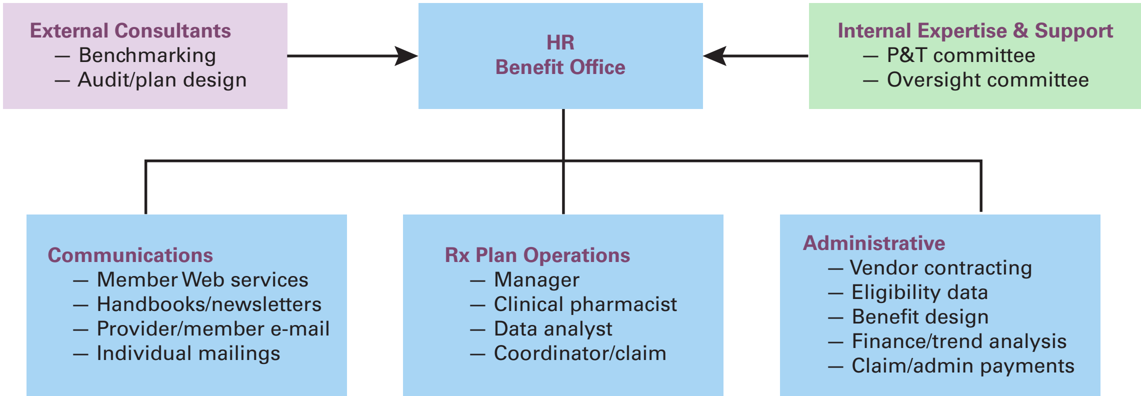
Understanding the PBM Financial Model

An initial step in achieving better prescription drug benefit performance is more thoroughly understanding how PBMs generate profits.[9] With such understanding of this model, employers are better positioned to negotiate a more favorable relationship with their PBM and to address how to best align strategies between the employer (as payer) and the PBM.

Generally, PBMs generate revenue through the following strategies[10-12]:

- **Administrative fees.** PBMs often charge a transaction fee to the payer and pharmacy for every claim they process. However, they are able to generate revenue for themselves in many ways other than administering the claims.
- **Differential discounts on branded products.** PBMs create a contract with the employer to pay for a brand name drug at a discount from the Average Wholesale Price (AWP) of the drug. They also create a contract with the retail pharmacies in their network to pay for brand name products, but at a different discount rate. For example, the contract with the employer may be for AWP minus 14%, but with the retail pharmacy it may be AWP minus 16%. This differential pricing, or "pharmacy withhold," is retained by the PBM as profit.
- **Differential discounts on generic products.** PBMs will generally contract for generic prices with either an AWP discount or a set rate called a Maximum Allowable Cost (MAC). It is not uncommon to see PBMs contract with employers at an AWP discount while contracting with the pharmacies for a MAC price. Similarly, PBMs may use a different MAC price list for employer invoicing than is used for paying pharmacies. Again, the differential between these 2 methods is retained by the PBM as profit.
- **Differential pharmacy dispensing fees.** Similar to the strategies for ingredient costs for brand and generic medications, PBMs will often negotiate different pharmacy dispensing fees over the term of a contract for the employer and the retail pharmacy network. The difference in these dispensing fees may be retained by the PBM as profit.
- **Rebates.** PBMs typically negotiate rebates with drug manufacturers based on access, volume, or market share within a particular therapeutic class. The PBM may hold rebate contracts—which are often confidential and viewed only by auditors—or aggregate volume claims with a subcontractor. This is a challenging area to manage and validate in that it is difficult to ascertain whether the PBM is sharing the rebates with the employer in a fair manner. Often, when a PBM claims that they are sharing a percentage of the rebates with the employer group, it may be for the volume/market share components alone—not the rebates received for preferred formulary access. Rebates may also create misaligned incentives for the utilization of drugs within a particular class. For example, it may be advantageous for the PBM to position a particular branded product on a preferred formulary or to see utilization of specific branded products in a therapeutic category due to significant rebates, whereas the lowest net cost to the employer may be through greater utilization of generic products.
- **Manufacturer-sponsored programs.** These include a variety of activities through which PBMs may be deriving revenue. While less common than in the past, included in this category are therapeutic switching programs in which manufacturers pay PBMs to attempt to influence employers to switch

Figure. The Functional Areas of an HR Benefit Office Prescription Drug Plan



HR indicates human resources; P&T, pharmacy and therapeutics.

favored prescriptions to different brand name drugs in a particular therapeutic category. Another strategy is for the PBM to sell prescription data to manufacturers or to third parties—data that support market research and strategy so that these businesses can better target their sales efforts to prescribers.

- **Other services.** The PBM may also provide a variety of other services for the employer benefit plan, including prior authorization and appeals administration, drug utilization review, disease management programs, and formulary management.

Improving the Nature of the Relationship With the PBM

When the employer understands the sources of revenue for a PBM, the employer is in a better position to manage the PBM relationship and to negotiate contracts that maximize the value in the prescription drug benefit. This is particularly true for employers who have internal expertise in medicine and pharmacy, such as health system employers or academic institutions that have schools of medicine, pharmacy, and/or public health. Mobilizing internal expertise, along with having human resources personnel develop a more sophisticated understanding of the complexities of the prescription drug benefit, can lead to more effective management of the overall benefit. This will help to ensure appropriate dispensing and payments, and by extension, control plan cost.

Strategies to accomplish this include:

- **Formulary management.** When an employer learns that the PBM may have incentives to provide preferred access to certain products based on access rebates, the employer may find it beneficial to have a greater degree of management of the formulary and preferred drugs. Utilizing internal experts in medicine and pharmacy to evaluate products within therapeutic categories, to apply best principles of evidence-based medicine, and to consider the lowest net cost of therapy for the employer can prevent misaligned incentives in the utilization of particular drugs. Another benefit is that there will likely be greater "buy-in" with formulary decisions and approved-use criteria if they are made internally by local experts than if they come externally from a PBM. This buy-in is important for both prescribers and patients to gain credibility; additionally, increased cooperation with the goals of the program will help to achieve more optimal drug utilization.
- **Utilization of internal pharmacies.** Health system or university employers often have internal pharmacies that could be used to retain a greater degree of savings within the organization. In some cases, either 340B drug purchasing programs or "own use" purchasing, utilizing more favorable classes of trade in drug ingredient costs, could be used for a significant portion of the employee drug benefit. Where eligible, these savings can be substantial and can help extend the benefit available to employees as well as retain more of the benefits within the organization. For example, the University of Michigan Prescription Drug Plan utilizes a collaborative relationship with the pharmacies within the University of Michigan Health System for specialty pharmaceuticals. This arrangement has produced significant savings for the benefit plan. Savings help to offset annual

employer healthcare premium increases, limit increases to member co-payment cost sharing, and retain plan quality by reducing restrictions that are commonly made in plan design, pharmacy networks, and the formulary.

- **Use of internal experts to enhance negotiations with PBMs.** By taking advantage of internal expertise and knowledge, a more transparent and flexible arrangement with PBMs may be pursued. Anticipating the degree of control and flexibility needed in vendor agreements is essential to adopting best practices and to strengthen cost-containment strategies.
- **Use of internal experts to manage plan changes.** Collaboration with key stakeholders can identify potential benefits of and barriers to new incentives. This partnership can address those behavioral changes that are required for implementing new strategies. Employers want to balance appropriate use, meet employee needs, meet their fiduciary responsibility, and pilot new designs and initiatives with a high likelihood of success. Incenting members and prescribers, addressing PBM operational requirements, and using multiple media to communicate to prescribers, members, and pharmacies will increase positive outcomes.

While there are significant benefits to taking more internal responsibility for the prescription benefit plan, several challenges need to be considered as well. To start, there will be more administrative complexity, and additional resources will be needed in order to manage the program. Generally, however, the substantial savings that can be achieved will more than compensate for the added complexity and incremental resource costs. Use of a national pharmacy consultant is instrumental in the support of plan sponsors. Typically, such a consultant benchmarks data and best practices, validates employer patterns of use and cost, and models financial and utilization programs when plan design changes are being considered and a strong business case is needed. If an agreement with a PBM is structured such that transparency increases around differential discount pricing strategies, the result might be an increase in administrative fees charged to the plan. Examples of the functional responsibilities that should be considered when taking ownership of the employee prescription drug plan are illustrated in the Figure.

Secondly, effective communication with employees is necessary to gain their support and cooperation, and for them to take "ownership" of the plan's goals. Given that this effort is being made to preserve a high-value benefit for the employees, this communication effort should be positively received.

A further challenge is the difficulty in coordinating data from medical plans with those of the prescription drug plan to aid in decision making—and that can be significant whether the employer decides to let the PBM run the program or chooses to play a more active role.

Finally, employees may also have privacy concerns, chief among them the fear that other employees in the organization will have access to their protected health information in the course of operating the benefit plan. Such concerns can be addressed through the establishment of policies that protect the employees' privacy.

Finally, regardless of the degree of self-management of the prescription drug benefit that an organization decides to assume, there are still opportunities to develop more favorable agreements with PBMs that enhance transparency, improve alignment of objectives, and help to achieve the plan's goals.

SUMMARY

The growth in prescription drug spending, especially with the emergence and importance of specialty pharmaceuticals, will bring increasing emphasis on managing the prescription drug benefit. Employers should become informed consumers, understanding how revenue is generated by pharmacies as well as by intermediaries such as PBMs. Organizations like health systems and academic institutions who have internal expertise or internal pharmacies may be able to take advantage of opportunities to assume more management responsibility for the prescription drug benefit, working in a collaborative and more transparent manner with other stakeholders. Those employers without internal expertise may still benefit through a greater understanding of the pharmaceutical supply chain and consulting assistance in negotiating mutually beneficial arrangements with PBMs and other stakeholders.

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