

Strategic Benefit Solutions, Inc.

Revolutionizing Benefits Procurement

RxQuest™ PBM
Procurement
Process

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Business Problem

The vast majority of self-funded employer groups purchase pharmacy benefit manager (PBM) services without following basic procurement principles.

Principle #1: All variables that materially affect cost must be considered.

Some employer groups do not consider the basic pricing terms: administrative fees, discounts, dispensing fees, rebates, etc. Those that do rarely consider one of the largest drivers of cost: drug mix. There exists a wide variation in the drug mix options, protocols, and performance among PBMs.

For example, in a 2007 RxQuest procurement study on behalf of an 8,000 employee group, two PBM finalists were selected with the following pricing terms:

Pricing Term	PBM A	PBM B
Admin PEPM (\$)	\$0.00	\$0.00
Rebate PEPM (\$)	\$6.19	\$7.93
<i>Discounts</i>		
Retail/Generic (%)	61.50%	62.00%
Retail/Brand (%)	16.50%	16.00%
Mail/Generic (%)	64.50%	65.00%
Mail/Brand (%)	23.00%	23.50%
<i>Dispensing Fees</i>		
Retail/Generic (\$)	\$1.55	\$1.60
Retail/Brand (\$)	\$1.40	\$1.60
Mail/Generic (\$)	\$0.00	\$0.00
Mail/Brand (\$)	\$0.00	\$0.00

PBM B enjoyed a nearly \$2.00 rebate advantage, higher discounts, and nearly identical dispensing fees. If drug mix were not considered, PBM B would have been a natural winner. However, for the client's utilization profile, PBM A was found to have superior drug mix capabilities. Their protocols substituted more generic for brand drugs and more multi-source brands for single-source brands. As a result, a greater percentage of PBM A's pharmacy claims received a generic

discount as opposed to a brand discount – dramatically lowering average script cost.

In fact, the observed 7.5% differential in generic fill rates (GFRs) implied a cost savings for PBM A of \$700,000 over PBM B within the first contract year.

Principle #2: Variables must be combined using financial models that project each vendor's cost over the life of the contract.

Because the vast majority of employer groups do not consider the affect of drug mix, any attempt at the financial modeling of cost is invalid. The modeling that is performed rarely employs the script-level simulations that are ideal for modeling the cost of pharmacy services.

Principle #3: Vendors must be made to back their contracts with performance guarantees that cover all cost variables.

Given the extent to which cost variables are self-reported by bidding PBMs (e.g. aggregate discounts, rebates, drug mix capabilities, etc.), no comparative cost projections can be considered meaningful until all variables are covered by contractual performance guarantees. Remarkably, the vast majority of employer groups have not negotiated such performance guarantees with their PBMs. For example, a group may have only discount-based performance guarantees that do not cover drug mix.

Impact

Not following these principles causes problems both before and after PBM contract execution.

Procurement Impacts

Without credible projections that are based on all cost variables, benefit directors cannot have confidence they are selecting the best PBM or contract. This is a problem for the organization as well as the benefit director whose job it is to identify and partner with the benefit vendors that offer their employer group the most value. Often benefit directors are asked to provide cost projections and justify procurement choices to senior management. When benefit directors do not follow the basic procurement principles when purchasing PBM services, they do so at their peril.

Contract Lifetime Impacts

It is common sense that any process that rigorously follows the basic procurement principles will result in savings over processes that omit any of the three. For example, the same 8,000-employee group mentioned above did not follow the

basic procurement principles in their previous selection of a PBM and contract. During the recent RxQuest procurement study, in which they did rigorously follow the principles, they negotiated dollar-for-dollar performance guarantees covering all cost variables (including drug mix) that will result in a \$2,500,000 savings over the life of their 3-year contract – **without switching PBMs**. By simply putting the business out to bid and following basic procurement principles, they achieved a guaranteed PEPM savings of almost \$9 from their incumbent PBM. A clear impact of not following basic procurement principles is that employer groups are simply spending more than necessary.

The lack of a rigorous procurement process can also result in vague or ambiguous contracts. This can not only complicate contract oversight but additionally draw the ire of external auditors.

Given the yearly cost of PBM contracts, benefit directors can be seen as “caretakers” of significant shareholder assets – defining a fiduciary responsibility. To the extent benefit directors deviate from basic procurement principles in the purchasing of PBM services they can be seen as violating their fiduciary responsibilities. Some of the major law firms that focus on fiduciary litigation on behalf of shareholders are actually studying the procurement of medical and pharmacy benefits as a potential revenue source.

Solution

SBS has partnered with the industry luminaries that revolutionized the procurement of medical benefits among the Fortune 50 to offer RxQuest – a rigorous pharmacy procurement process with **no direct cost** for SBS clients.

A summary of the RxQuest procurement process follows:

1. SBS collects a recent year of client pharmacy data.
2. Our RxQuest service bureau produces client-specific cost variable workbooks for each selected PBM. Bidding PBMs populate these workbooks with both pricing parameters (discounts, fees, rebates) and their drug mix capabilities (generic vs. brand rates, PBM-specific drug interchange protocols).
3. Once the bidder responses are returned, our RxQuest service bureau combines all cost variables within financial models that perform a rigorous, script-level simulation of each PBM’s cost over the life of the contract. This analysis includes an apple-to-apples PBM cost comparison and suggests initial dollar-for-dollar performance guarantee parameters.
4. Once PBM finalists have been selected, our RxQuest service bureau generates detailed financial exhibits justifying our client’s starting point in contract negotiations. To expedite negotiations, SBS’s RxQuest team has pre-negotiated a comprehensive performance guarantee framework with the majority of PBMs.

5. During the negotiation process, PBMs frequently attempt to outbid one another in the richness of their dollar-for-dollar performance guarantees. RxQuest software allows SBS and client negotiators to compute the savings associated with emerging performance guarantee improvements in real-time.
6. Once the winner has been selected, our RxQuest service bureau produces:
 - a. A detailed procurement report, clearly describing the process and demonstrating that the client benefit director chose the PBM that guaranteed the employer group the most value, and
 - b. A PowerPoint presentation summarizing the procurement process, cost variables, financial projections, and competing performance guarantees for senior management audiences.
7. Finally, our RxQuest service bureau reviews the final contract, to help ensure that it is unambiguous, free of common loop holes, and consistent with the terms of the winning bid.

Conclusion

Consider the following questions:

1. Was the selection of your PBM contract based on a rigorous financial projection explicitly considering both pricing terms and drug mix?
2. Does your PBM contract contain dollar-for-dollar performance guarantees that explicitly cover both pricing terms and drug mix?
3. Are you confident your PBM contract is the best possible deal?
4. Could you confidently explain to senior management how your current PBM contract provides your organization more value than other available options?
5. Are you confident your PBM contract is clear enough to withstand oversight by external auditors?
6. Are you confident your PBM contract does not contain common loop holes allowing PBMs to undermine their stated pricing terms?
7. Are you confident you have fulfilled your fiduciary responsibility as a caretaker of shareholder assets?

If you answered no to one or more of these questions, we suggest contacting your SBS representative for more information about this unprecedented RxQuest service.