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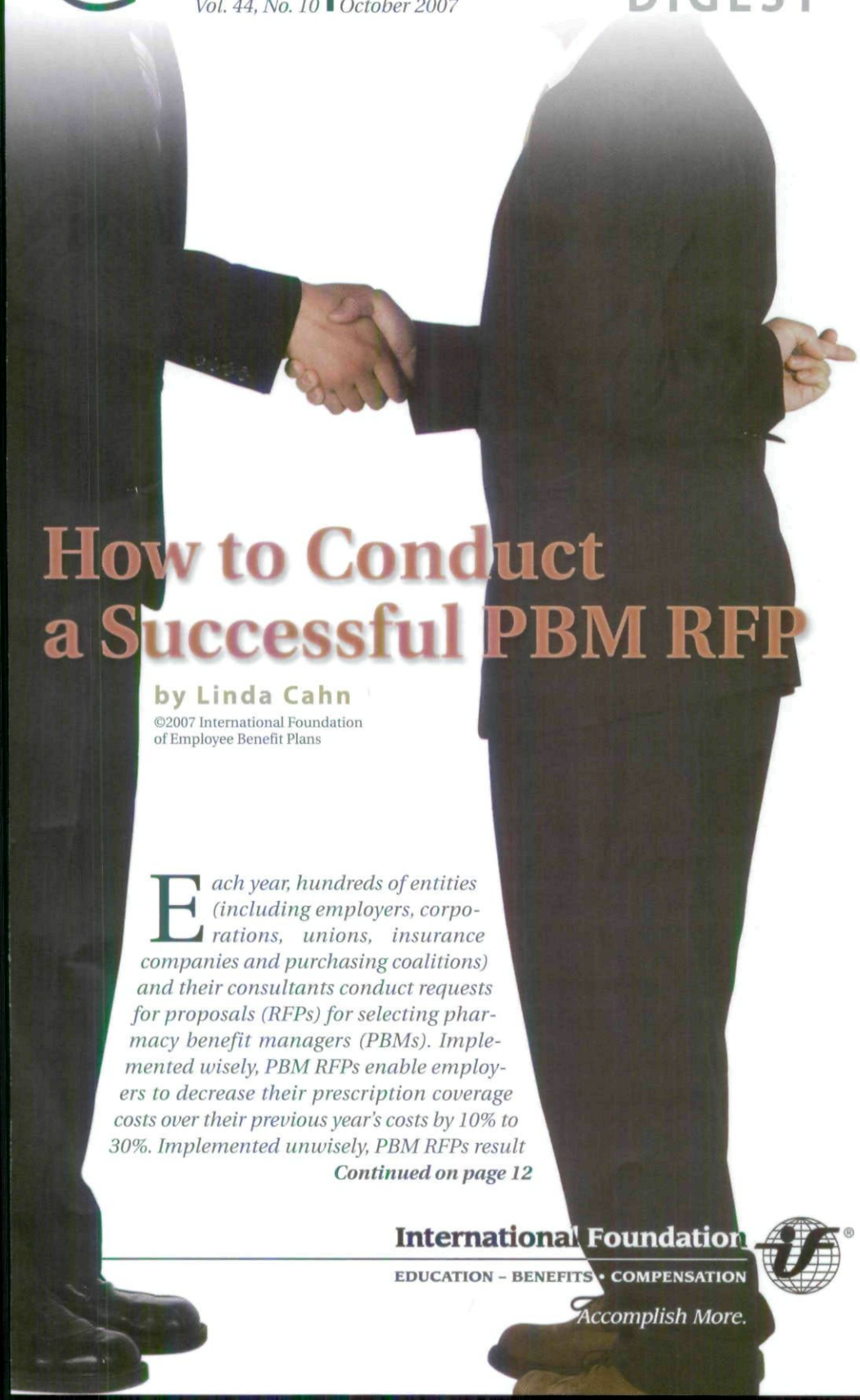

How to Conduct a Successful PBM RFP

by Linda Cahn

Each year, hundreds of entities (including employers, corporations, unions, insurance companies and purchasing coalitions) and their consultants conduct requests for proposals (RFPs) for selecting pharmacy benefit managers (PBMs). Implemented wisely, PBM RFPs enable employers to decrease their prescription coverage costs over their previous year's costs by 10% to 30%. Implemented unwisely, PBM RFPs result

Continued on page 12

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How to Conduct a Successful PBM RFP

Continued from page 1

in no savings whatsoever. To conduct successful PBM RFPs, employers and other entities need to understand why PBM RFPs fail; restructure their PBM RFPs; and incorporate safeguards into their RFPs to guarantee success. This article describes each of these steps.

Understanding Why PBM RFPs Fail

Drug coverage benefits and costs are dependent on one matter—and one matter only—the PBM-client contract. In fact, all prescription coverage results flow from the PBM contract. Accordingly, every PBM RFP must focus on one core matter: the terms contained in the PBM contract.

Remarkably, few PBM RFPs ever finalize a PBM contract before the RFP is concluded. Still more startling, most PBM RFPs don't even discuss specific contract terms before finishing the RFP.

The above facts are borne out by a 2007 International Foundation teleweb seminar concerning PBM RFPs. More than 80% of attendees who had conducted RFPs indicated in a survey that they had never negotiated any PBM contract terms until after their RFP was concluded.

Ignoring the task of negotiating actual binding contract terms, most PBM RFPs instead focus on analyzing PBMs' nonbinding representations and price projections. Thus, consulting firms typically conduct PBM RFPs by engaging in the following futile activities.

The consulting firm asks each PBM contestant to provide its "current" or "expected" pricing terms and guarantees. Thereafter, the consulting firm "re-prices" each PBM's submission using the client's "current" claims data to ascertain each PBM's "projected" aggregate costs. Interviews are then conducted, during which each PBM sales team competes in a "beauty contest" by providing still more nonbinding representations. Finally, the client and its consulting firm select the PBM with the lowest projected aggregate costs—and the most skillful sales team—as the PBM finalist, and the RFP is concluded.

Not surprisingly, when the client thereafter begins contract negotiations, the PBM finalist's previously submitted pricing terms and guarantees rarely materialize in the contract. After all, months have elapsed since the PBM submitted its "current" figures, and in any event the PBM never bound itself to the numbers it submitted.

Equally as harmful, the PBM finalist can now propose numerous contract terms that were never discussed during the RFP, all of which may have serious implications for the client. By way of example only:

- The PBM is to be an independent contractor, not an ERISA fiduciary (even though the client is delegating most of its fiduciary duties to the PBM by virtue of the contract).
- The client's selection of an auditor will be limited to those the PBM "approves" (leaving the PBM free to "veto" all auditors who have conducted previous audits and found contract violations).
- The client cannot terminate the contract until three years have passed, unless the client pays substantial penalties of hundreds of thousands of dollars to the PBM.
- The client must pay numerous additional fees—none of which were discussed during the RFP—for matters such as direct member reimbursement, online access to plan information, "nonstandard" reports, "nonstandard" drug utilization review (DUR), annual explanation of benefits (EOB) statements and other never-discussed programs.
- If the client fails to pay an invoice within five days, the PBM is free to terminate all prescription claims processing (leaving the client and its employees without any coverage whatsoever).

Since the RFP has already been concluded, all leverage for the client to resist such terms also has ended. Stuck with the results of a poorly conducted RFP, the client must accept onerous terms into its new PBM contract; commence another RFP where the same mistakes are often repeated; or renew the relationship it had with its previous PBM.

Seeking an alternative, many clients begin a new PBM relationship but postpone the execution of a new contract. Under this scenario, clients purchase hundreds of thousands—or millions—of dollars of prescription drugs without ever executing a new contract. In so doing, they place themselves in a position where their new PBM is free to charge anything it wants for drugs and to alter its charges whenever it wants.

While the above may seem unlikely, it unfortunately is not. In fact, of five plans that most recently sought advice, two were currently obtaining prescription coverage from PBMs without executing a contract with those PBMs. Both entities had concluded RFPs during the previous year and selected PBMs, only to find their newly selected PBMs thereafter insisted on contracts the employers or other entities were unwilling to execute.

To ensure that a PBM RFP results in a contract that the employer or other entity is entirely comfortable executing, the entity must completely restructure the PBM RFP. Here's how to do so.

Restructuring a PBM RFP

Before the RFP begins, draft a model form of the PBM contract. Eliminate or modify all substantive terms that historically appear in contracts and that are against your interests. Include "blanks" for all pricing terms and guarantees to enable PBM contestants to provide their best contract offers when the RFP begins.

In performing the above tasks, consider the following to avoid simply rewriting the typical PBM contract. For example:

- Virtually all PBM contracts contain definitions that are ambiguous or contrary to PBM clients' interests: A *claim* is defined to allow a PBM to invoice its client for "reversed" or "rejected" claims, which may constitute as much as 20% of all claims. *Average wholesale price (AWP)* is defined to enable a PBM to retain all "bulk purchase" savings and to cherry-pick the highest prices among national reporting services' different prices. *Brand drugs* and *generic drugs* are defined loosely to enable the PBM to relabel each, in the PBM's own best interests. In short, most contract definitions must be rewritten to ensure they are airtight and in client's interests.
- Almost all PBM contracts contain financial "guarantees" that are essentially useless. For example, "generic savings guarantees" are written stating the PBM warrants a specific aver-

age "AWP discount" on all generic drugs for which the PBM is creating a MAC (maximum allowable cost). However, the contract does not also require that the PBM create a MAC for a large percentage (say, 90%) of all generic drugs. Therefore, the guarantee's value can easily be eviscerated if the PBM only creates MACs for a small percentage of generic drugs.

- Almost all PBM contracts also contain numerous "performance guarantees" that purportedly ensure that PBMs dispense retail, mail and specialty drugs in a timely and accurate manner. However, these performance guarantees are missing core terms that will ensure their success, because the guarantees do not identify a specific methodology for auditing each guarantee and do not include sufficient penalties to incentivize PBMs to comply with each guarantee. Accordingly, each performance guarantee must be rewritten to include those critical components.
- Almost all PBM contracts incorporate three-year terms, with limited or no rights for clients to terminate the contract. As a result, clients are locked into three-year contracts that become ever more noncompetitive and out of date with each passing year. Draft the proposed contract so it provides for a one-year term, or a three-year term coupled with a "90-day, with or without cause, termination right." If the contract contains a three-year term, include a "right to renegotiate," at least annually, every pricing term and every guarantee. Termination and renegotiation rights will enable an entity to "hold the PBM's feet to the fire" to obtain ever better terms annually, thereby ensuring that the contract remains a state-of-the-art, competitive contract throughout its three-year duration.

After finalizing a carefully drafted PBM contract, begin the RFP. Transmit the RFP to all PBM contestants, and make sure it contains two parts: the typical questions that are included in all PBM RFPs by all consultants, and a copy of your proposed PBM contract. Require each PBM to provide its response, which must also include two parts: answers for all questions, and a "contract markup" identifying each change the PBM will request in the proposed contract if that PBM is selected. Ensure that each PBM also includes in its contract markup a number for each blank, representing the PBM's best offer for each pricing term and guarantee. Also, require each PBM to identify any and all additional fees the PBM will charge the plan.

Make clear in the RFP documents that each PBM's contract markup and financial terms offer represents a binding representation that cannot be further negotiated or modified by the selected PBM. Attach a certification in the RFP documents that states the above, and require each PBM to execute it. Refuse to review any contestant's RFP response until receiving a signed, sworn certification from the PBM. You cannot—and should not—waste your time reviewing PBM representations unless they constitute binding representations, on which services will be provided without further negotiations or modifications.

Having obtained binding contract markups and binding financial terms from each PBM contestant, compare each PBM's offer, and attempt to obtain even better offers by requiring each PBM to compete against other contestants' proposed terms. Assuming the consulting firm is experienced in negotiating contracts, require it to negotiate with each PBM to modify its proposed contract changes and to improve its financial offer.

For example, if some PBM contestants accepted proposed contract language stating the PBM is an ERISA fiduciary, and other PBM contestants rejected or altered proposed contract language, the consultant should negotiate with each of the latter PBMs to change their positions and accept ERISA fiduciary language. While almost no PBM-client contracts currently in the marketplace require a PBM to act as an ERISA fiduciary, entities have recently obtained such contract language from PBMs by requiring the language during RFPs. Moreover, the language is extremely important—particularly if the PBM's fiduciary duties are specifically listed in the contract. After all, an ERISA fiduciary is required to act "solely and exclusively" in a plan's interests.

If the proposed contract included language requiring the PBM to pass through to the plan all rebates and all other financial benefits the PBM receives from every

Continued on next page

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drug manufacturer, and certain PBMs rejected and altered the proposed contract language, leverage the power of the RFP to require each PBM to agree to such terms. Tell all recalcitrant PBMs that certain PBMs have accepted the proposed language (which some PBMs will do, if you make sure to include smaller PBMs as contestants). Further inform recalcitrant PBMs that those PBMs that refuse to accept the terms will be eliminated as contestants. If more and more clients require such language in contracts during RFPs, PBMs' widespread practice of retaining most manufacturer payments will change, dramatically increasing client savings.

If the proposed contract contained a list of all specialty drugs (numbering approximately 1,000 drugs) and the RFP asked each PBM to submit a guaranteed minimum discount for each specialty drug, compare each PBM's proposed discounts and negotiate with each PBM on a drug-by-drug basis to improve all noncompetitive discounts. In so doing, entities or their consultants will be creating a "reverse auction" and thereby inducing each PBM to better its financial terms. The same procedure should be used during the RFP to negotiate every noncompetitive pricing term and every noncompetitive financial guarantee offered by a PBM contestant.

After concluding negotiations with each PBM, memorialize each PBM's changes into a final, proposed contract for that PBM. Before semifinalists are selected, require each PBM to execute its revised contract, as well as another binding certification.

Interview each semifinalist based on the semifinalist's revised binding contract. Use the interview process not to conduct "beauty contests" among sales teams, but rather to extract further binding contract concessions from each PBM contestant. Before a finalist is selected and announced, make sure all contract changes have been memorialized into a binding contract, and require each contestant to execute its contract and a final binding certification.

On the day the finalist is chosen and announced, the entity will be in a position entirely different from virtually all entities that conduct PBM RFPs: It will be able to execute the final contract, without any further negotiation or modification, knowing that it has used the leverage of the RFP to obtain as good a contract as possible.

Incorporating Safeguards to Ensure the RFP's Success

Before retaining a consulting firm or law firm, require the firm to provide an initial free consultation to gauge its expertise. Supply the firm with basic information about plan design—and a copy of the existing PBM contract—and ask the firm to identify in a conference call the key plan design and contract changes it would recommend. Compare the recommendations and select the firm that has demonstrated the greatest expertise.

Before a finalist is selected and announced, make sure all contract changes have been memorialized into a binding contract, and require each contestant to execute its contract and a final binding certification.

Thereafter, understand the recommendations and incorporate them into the RFP. Draft a proposed contract that improves plan design, for example, by altering the copay structure, identifying different formulary requirements or incorporating a mandatory generic program. Rewrite the other terms in the contract as well, by reformulating all contract definitions and all guarantees and by eliminating all terms that historically drive up entities' costs.

Employers that suspect their PBM is retaining—and not passing through—most generic drug savings due to poorly drafted generic guarantees should focus on drafting better generic drug terms: Define *generic drug* and *maximum allowable cost (MAC)* carefully. Draft enforceable annual aggregate generic discount guarantees. Also include a list of the 200 most commonly used generic drugs, and require each PBM contestant to provide pass-through pricing, coupled with a drug-by-drug maximum per pill cost guarantee at retail, and at mail, for each drug.

Employers that suspect their specialty drug costs are particularly excessive should consider conducting a two-track RFP: one track for retail and mail drugs (with only PBMs as contestants), and one track for specialty drugs (with PBMs and independent specialty drug vendors as contestants). In so doing, PBM contestants may be induced to provide more advantageous discount guarantees for specialty drugs.

Finally, make sure that the contract attached to the RFP—and subsequently executed—is an airtight contract. After all, everything related to prescription drug coverage will flow from the contract proposed and finalized during the RFP. The goal must be to eliminate all contract loopholes, not most contract loopholes.

Far too many employers assume that if they obtain most of the contract changes they seek, they will have accomplished their goal. However, if the new PBM-client contract contains one unlimited loophole that gives the new PBM the discretion to dramatically overcharge the plan, whatever savings that may have been obtained by eliminating all other loopholes may disappear through the one remaining loophole. **B&C**

Linda Cahn is the founder and president of Pharmacy Benefit Consultants (PBC), a consulting firm in Morristown, New Jersey. PBC's focus is on analyzing PBM client contracts, drafting and negotiating contracts, and conducting PBM RFPs. PBC's clients have included corporations, unions, insurance companies and purchasing coalitions. In 1997, Cahn initiated the first class action litigation in the country against PBMs. She received a bachelor's degree from Princeton University and a law degree from Hofstra Law School.