

Dynamics of the Pharmacy Benefit Marketplace—Key Drivers and Emerging Issues

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March 28, 2006

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Questions?

You are welcome to submit questions through the webcast or by emailing Adabelle Cohen at adabelle.cohen@buckconsultants.com

Setting Expectations

- **Discuss the Pharmaceutical Industry today and what can we expect**
 - » Economic landscape
 - » Product mix
 - » Where our money will go
 - » Pricing changes
 - » Distribution channel management
- **How to prepare ourselves for the changes around the corner**
 - » Benefit design
 - » Plan documentation
- **What to expect from vendors**
- **What to expect from advisors**
- **Due diligence and pricing**

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Rx Economic Landscape

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Rx Economic Landscape

- Annual Rx trend over past 5 years—8% to 15% range
- Currently, 8% to 10%
- Result—Rx costs have doubled over past 5 years
- Expected to double again over next 5 years
- Represent about 20% of health plan costs—and growing
- A Budget Buster????
- Newer therapies will be increasingly expensive, while older therapies lose patent protection and become available generically
- As we live longer, we require more medical and pharmaceutical care

Rx Economic Landscape

Key Cost Drivers Outside Employer's Control

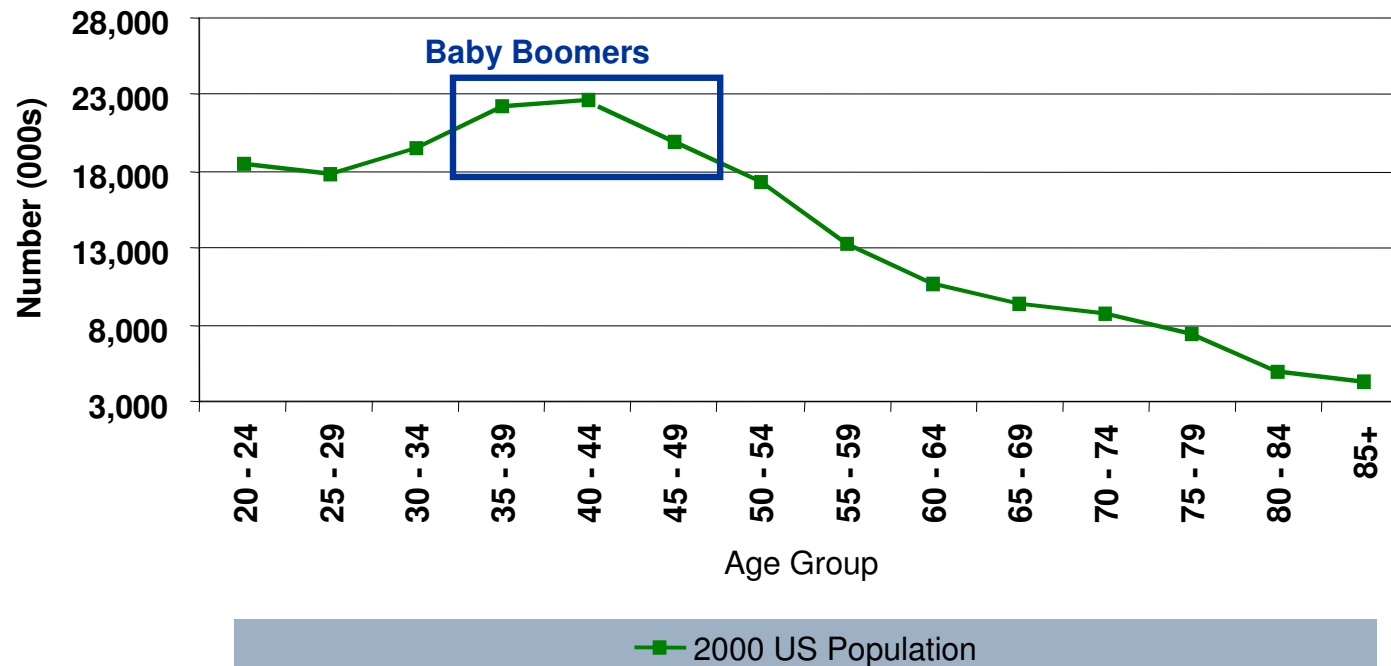
- Drug price inflation (3% to 6%)
- Aging work force correlates with higher Rx utilization
- Obesity, poor health among workers
- Number of new, expensive drugs entering market
- Changes in drug mix (biologicals/biotech drugs vs. oral medications)
- Surge in biotech drugs (emerging “train wreck” for employers) as drug therapy for common chronic diseases
- Changing philosophy of cancer treatment as maintenance therapy
- Feel-better medications vs. asymptomatic therapy
- Direct-to-consumer advertising impact
- Impact of new delivery system technology

Rx Economic Landscape

Aging baby boomers

Will increase the elderly and near-elderly populations...

U.S. Population, 2000

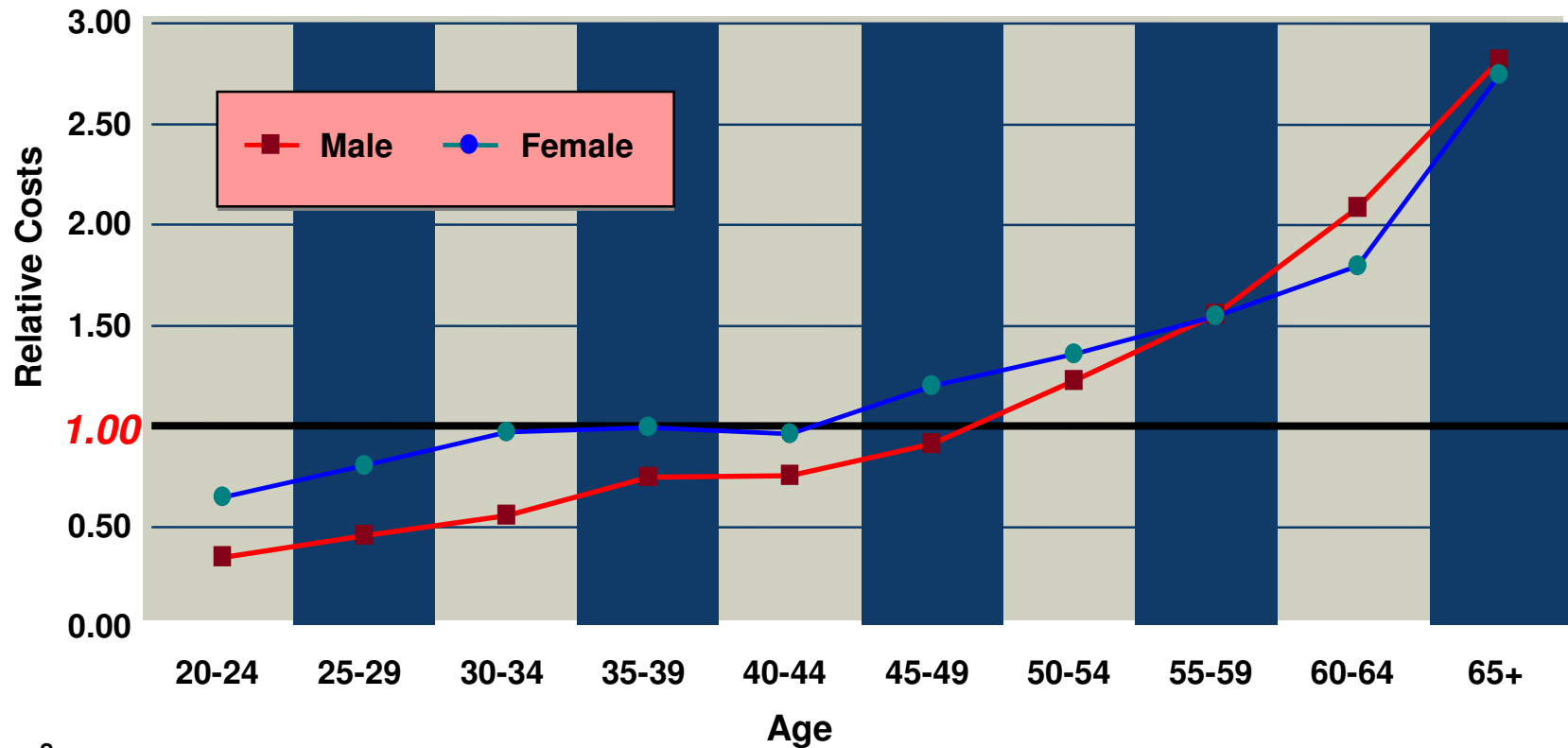


Rx Economic Landscape

Aging Baby Boomers

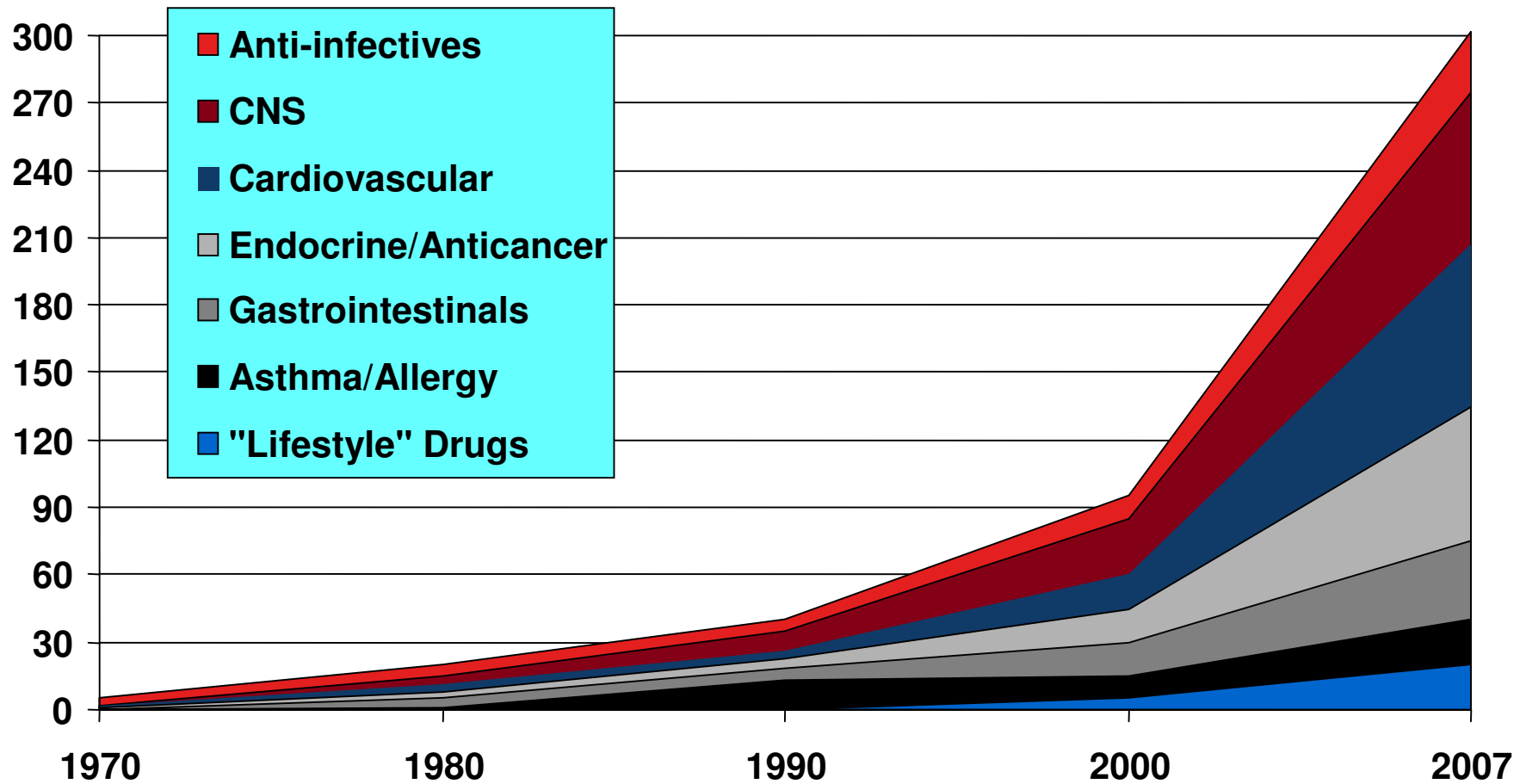
... And drive up drug spending

Cost Increases with Age

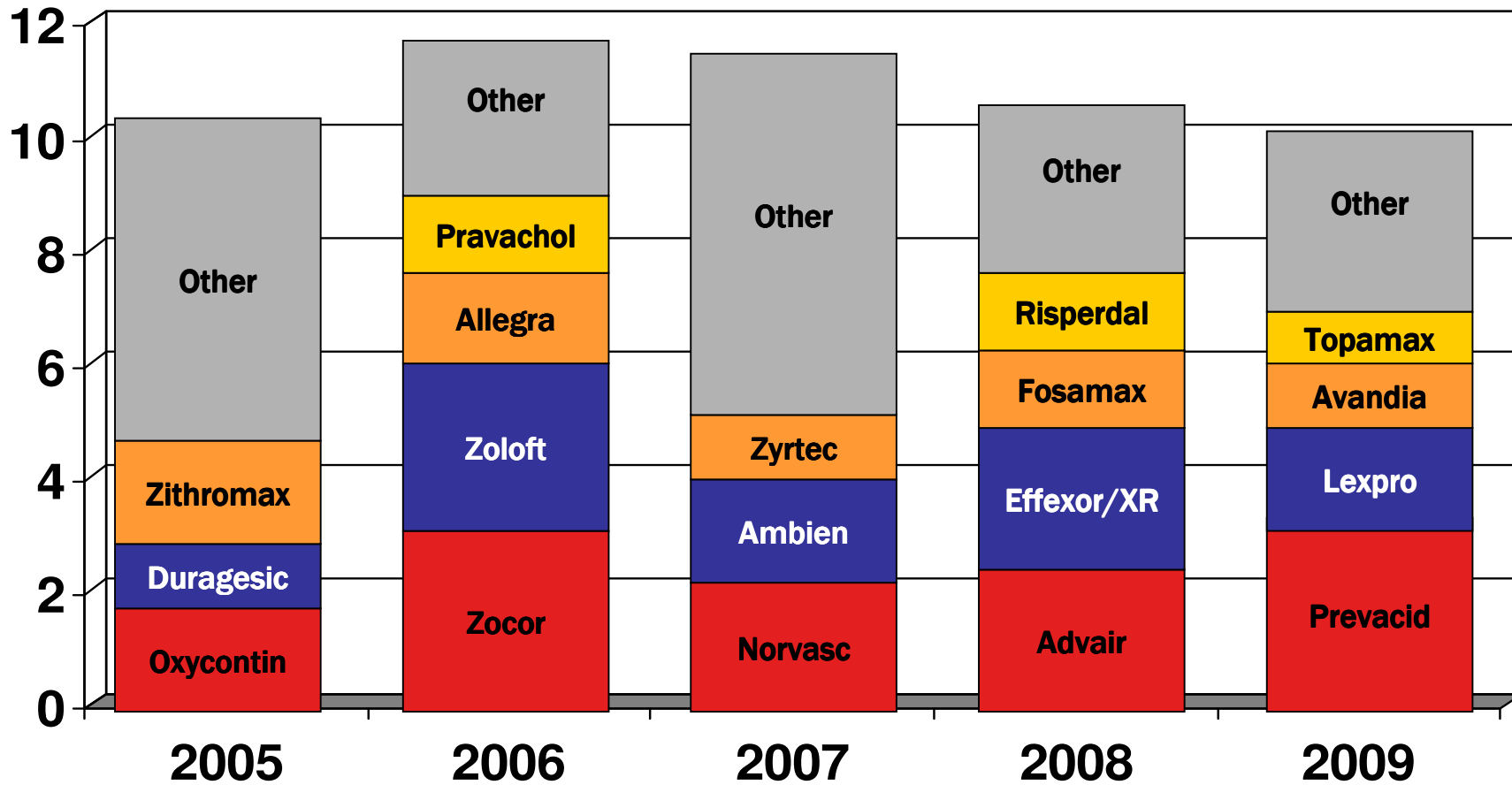


Rx Economic Landscape

Development of New Drugs—Outside Employer's Control



Billion-Dollar Brands Going Generic: 2005-2009



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Rx Economic Landscape—The Generic Opportunity

Medication	Indication	Scheduled generic Introduction	Ave. Rx Cost/30-Day Supply	Comments
Pravachol	High Blood Cholesterol	April 06	\$146.45	Generic may allow step therapy
Zocor	High Blood Cholesterol	June 06	\$135.93	No generic defense. Dramatic decrease in cost expected.
Zoloft	Depression	June 06	\$90.65	Generic may allow step therapy
Wellbutrin XL	Depression	August 06	\$111.74	Generic may allow step therapy
Norvasc	High Blood Pressure/Heart Disease	January 07	\$62.68	Will create generic class at low cost.
Ambien	Sleep	April 07	\$87.21	New CR version to extend patent life
Imitrex	Migraine	June 07	\$251.86	Generic may allow step therapy
Lamisil	Anti-fungal	June 07	\$255.23	OTC topical available
Zyrtec	Allergies	December 07	\$60.44	May move to OTC (Allegra also)

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Specialty/Biotech Drugs: Emerging Challenge

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Specialty/Biotech Drugs

- Today, Specialty/Biotech drugs represent a major challenge for employers.
- Originally, these drugs targeted rare diseases, such as Gaucher's disease, which affects roughly 4,000 people in the U.S.
- Their cost and utilization has spiraled as new drugs have been approved by the FDA and as treatments have broadened to include more common diseases.
- In 2004, Specialty/Biotech drugs had an annual trend of 20%.
- As new drugs come to market for treatment of common diseases, such as diabetes, we expect annual trend to exceed 30%.
- This presents a major challenge for employers and could result in a financial “train wreck” if a sound cost management strategies are not put in place.

Specialty/Biotech Drugs

- **Specialty/Biotech Drugs—Our Definition**
 - » Developed from human cell proteins and DNA, targeted to treat disease at the cellular level
 - Biotech engineering techniques, such as monoclonal antibody and recombinant DNA technologies, are used to develop drugs
- **Traditional Drugs**
 - » Developed from extracting plant chemicals and modifying the structure of chemical compounds in the human body

Specialty/Biotech Drugs

- Offer new treatments and cure for previously untreatable/intractable conditions, including:
 - » Multiple Sclerosis
 - » Parkinson's Disease
 - » Blood Disorders (e.g., Hemophilia)
 - » Rheumatoid Arthritis
 - » Array of Cancers
- Successful treatment can:
 - » Improve quality of life
 - » Lower employer medical/disability plan costs
 - » Enable employee to return to work

Specialty/Biotech Drugs

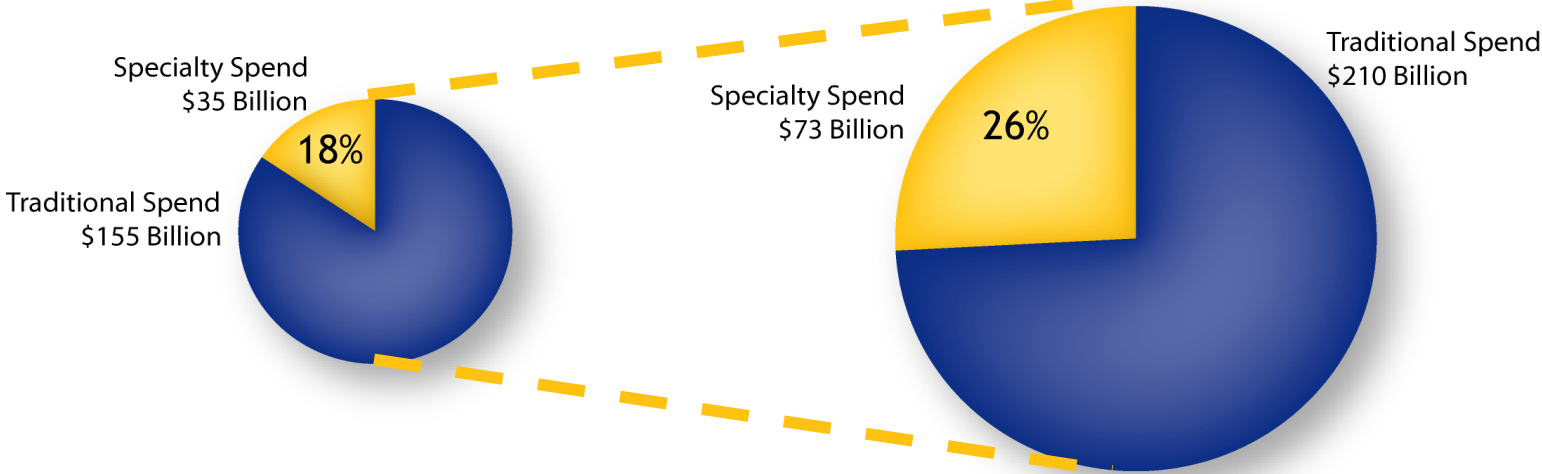
- Requires specialized physicians, pharmacists and nurses
 - » Patient-specific dosing (e.g., weight-based dosing)
 - » Patient compliance
 - » Lab and diagnostic monitoring
 - » Narrow, targeted treatment focus
 - » Special handling during delivery
 - » Patients on multiple medications
 - Average 12 Rx's annually per Specialty patient
 - Compared to 5 Rx's annually per non-Specialty patient

Specialty/Biotech Drugs

Economics of Specialty/Biotech Drugs

- **Monthly Cost**
 - » Averages: \$1,400
 - » Range: \$1,000 - \$20,000
- **Annual Trend**
 - » 2004: 20%
 - » 2008: >30% (est.)
- **Cost Drivers**
 - » Aging population
 - » High cost of drugs in marketplace
 - » Robust pipeline—600 drugs in development
 - » Broadening treatment from rare diseases to common diseases
 - » Absence of generic drugs

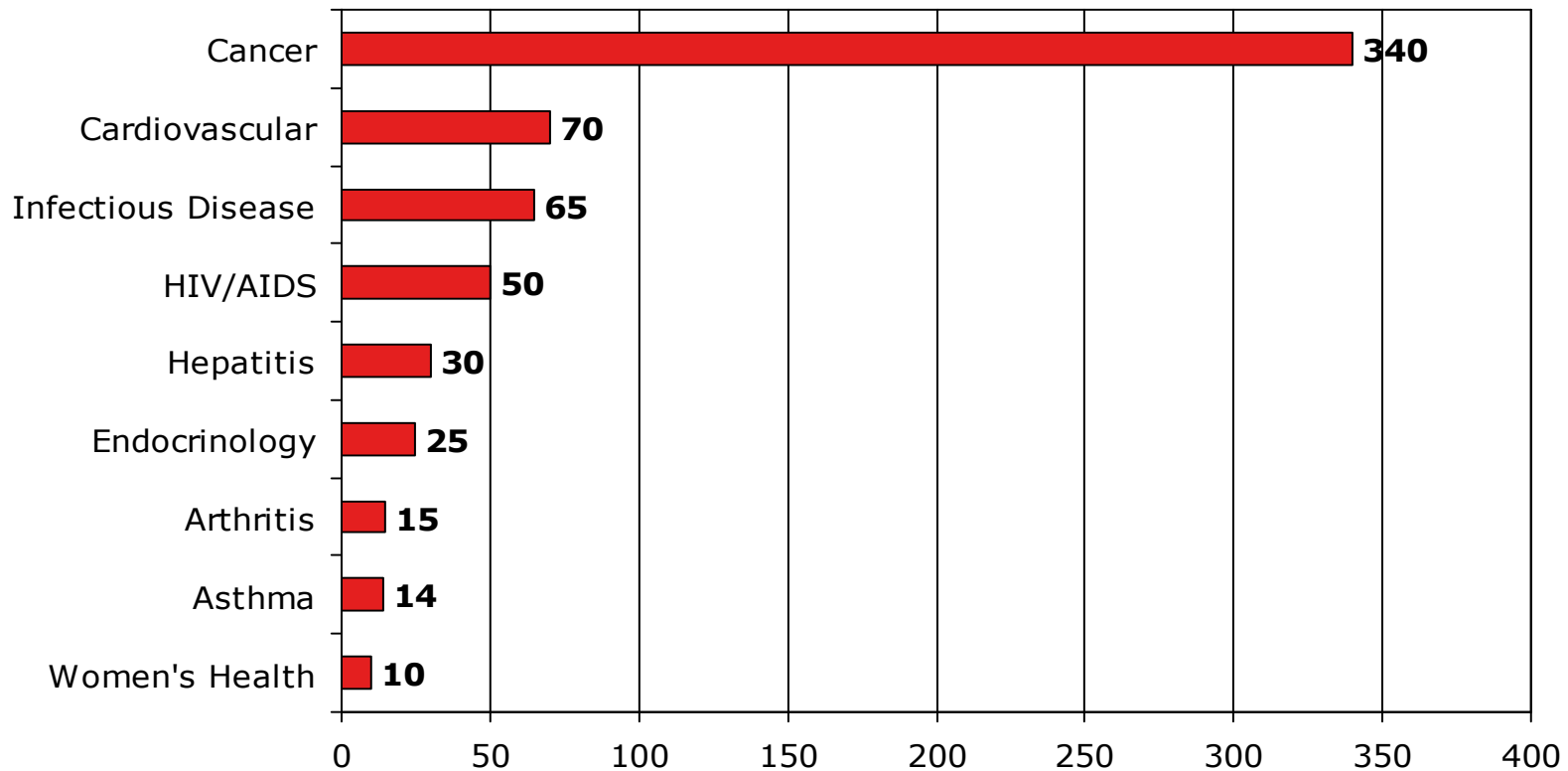
Specialty/Biotech Drugs



Other estimates suggest \$87 Billion in 2008 sales

Sources: IMS Data through November 2004. Wall Street Equity Research, 2004. CMS National Healthcare Expenditure Projection: 2003-2013.

Specialty/Biotech Drugs



Over 600 Biological and Specialty medications in the pipeline

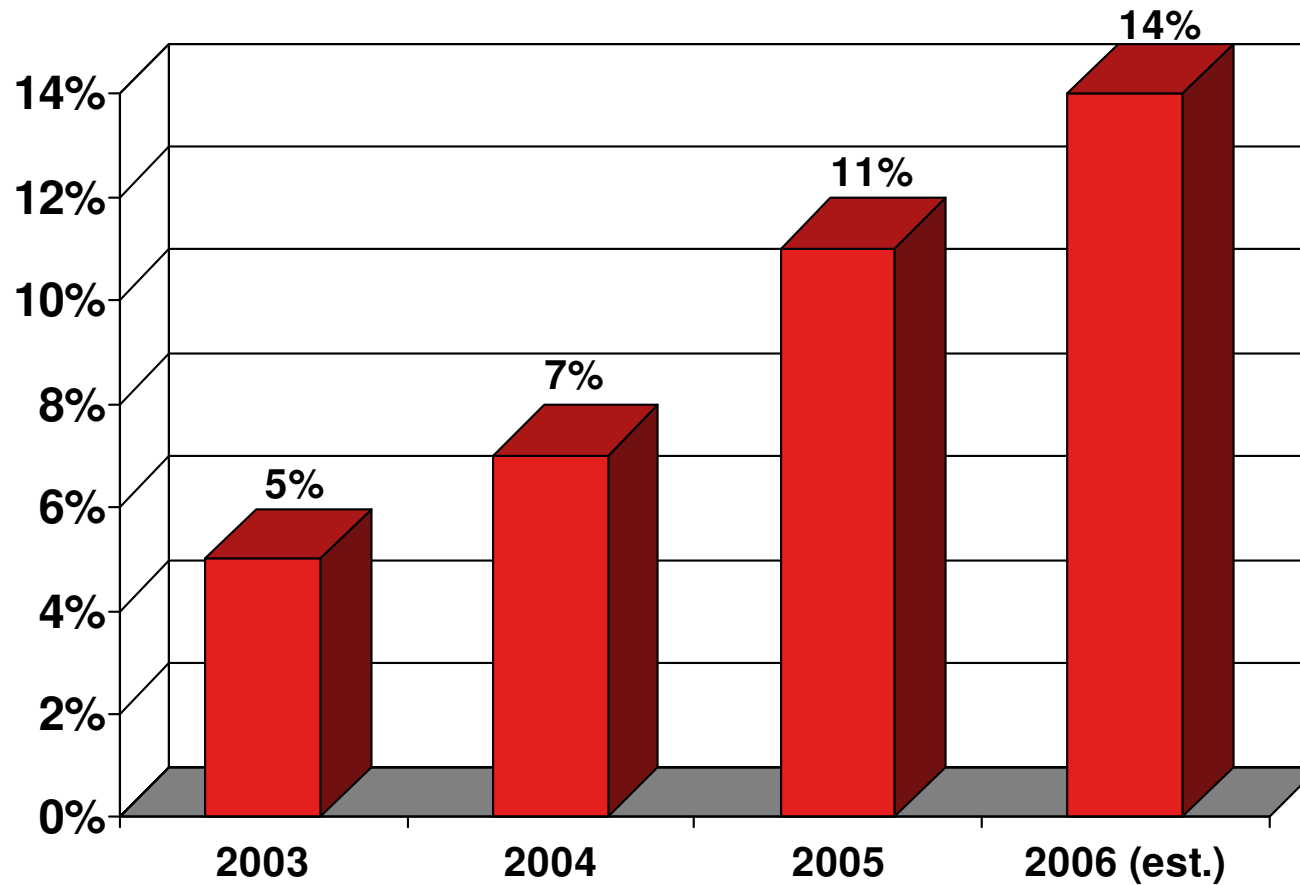
Source: Raymond James & Associates, Industry Report. PhRMA, International Federation of Pharmaceutical Wholesalers & Biotech Industry Organization.

Specialty/Biotech Drugs

- **Dilemma for Employers**
 - » **Dual coverage of Specialty/Biotech drugs**
 - ~50% of Specialty/Biotech drug cost covered by medical plan
 - ~50% through Rx plan
 - » **Result**
 - Fragmented patient management
 - Drug waste
 - Sub-optimal pricing
 - Poor tracking of outcomes

Specialty/Biotech Drugs

Specialty/Biotech Drugs: % of Total Rx Plan Costs



Source: Buck Consultants' National Pharmacy Practice Database

Specialty/Biotech Drugs

Key Employer Issues

- Employee cost sharing
- Separate copay/coinsurance for Specialty/Biotech drugs?
- Maximum annual or lifetime benefit?
- Formulary for Specialty/Biotech drugs in selected disease states?
- Coverage limits/exclusions?
- Evaluation criteria for selecting Specialty Pharmacy vendors
- Overall cost/utilization management strategy

Specialty/Biotech Drugs

Strategic Approaches

- **Option 1: Status Quo–Do nothing**
 - » Continue with dual coverage through medical and Rx plans
- **Option 2: Full Carve-Out**
 - » Pull out coverage from both medical and Rx plans
 - » Have all Specialty/Biotech drugs dispensed and managed by Specialty Pharmacy
- **Option 3: Partial Carve-Out**
 - » Pull out self-injectable and oral drugs from medical and Rx plan
 - » Have these drugs dispensed and managed by Specialty Pharmacy
- **Option 4: Consumer-Choice Plan Design**
 - » Do not carve out Specialty/Biotech drugs
 - » Restructure employee cost share–most favorable cost share (lowest) if these drugs dispensed through Specialty Pharmacy

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New Delivery Systems

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Pharmacogenomics: Today



- Genetic tests screen patients for enzymes responsible for drug disposition¹
- For example: Cytochrome P450 (CYP)²
 - » Responsible for metabolizing many drugs
 - » DNA variations in genes coding for the enzyme influence drug metabolism
 - » Researchers conducting clinical trials use genetic tests for variations in P450 genes to screen and monitor patients
 - » Pharmaceutical companies screen compounds for susceptibility to CYP enzymes

¹ Scientific American.com Web site. Available at: <http://www.sciam.com/article.cfm?articleID=000A68D9-BD17-1CDA-B4A8809EC588EEDF>. Accessed April 20, 2005.

² Human Genome Project Information Web site. Available at: http://www.ornl.gov/sci/techresources/Human_Genome/medicine/pharma.shtml. Accessed April 20, 2005.

Home Telemedicine

- **Monitoring and two-way communication¹**
- **Ensure early intervention²**
- **Cost control²**
- **Convenience³**
- **Quality of life³**
 - » **Is Home ultra-sound that far away?**
- **Improved compliance³ and patient feedback from health care professional**



¹ Long Term Care Link Web site. Available at: http://www.ltclink.net/find_remote.html. Accessed April 19, 2005.

² U.S. Food and Drug Administration Web site. Available at: http://www.fda.gov/fdac/features/2001/301_home.html. Accessed April 19, 2005.

³ News-Medical. Net Web site. Available at: <http://www.news-medical.net/?id=4127>. Accessed April 19, 2005.

⁴ ERCIM News Online Edition Web site. Available at: http://www.ercim.org/publication/Ercim_News/enw60/husemann.html. Accessed April 19, 2005.

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PBM Marketplace

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PBM Marketplace

Current PBM Players	Est. Covered Lives
Caremark	80 million
Medco	62 million
Express Scripts	48 million
Pharmacare	30 million
Wellpoint Pharmacy Mgt.	22 million*
Aetna Pharmacy Mgt.	8 million*
Walgreen's Health Initiatives	5 million
Catalyst Rx	3 million
Total	258 million

* Includes carve-in and carve-out Rx plans.

PBM Marketplace: Benefit Concerns

Employers

- Trends
- Overall perspective
- Contribution vs. cost share
- Active vs. Retired
- Recent trend-setting news
- Issues on the horizon
- Distribution channel management
- Plan documentation
- Data and reporting needs
- Plan design—influencing factors

PBM Marketplace

- Tiers
- Consolidation
- How they make their money
- Recent history & changes
- Future expectations
- New players
- Carriers
- Distribution channel management
- Growth areas

PBM Marketplace: Vendor Pricing Strategies

Today's Model:

- Ingredient costs
 - » Brand/Generic
 - » 30 day/90 day max. supply
- Pharmacy dispensing fees
- Administrative & clinical expenses
- Rebates & other manufacturer revenue
- Credits
- AWP basis
 - » Purchase size vs. 100-unit count at Mail vs. actual ingredient cost
- MAC Basis

Emerging Model:

- Alternative Benchmark Pricing (ABP)
Is your organization prepared?
- AAWP
- WAC, SWAC, AWAC, other
- Rebate games & terms
- Transparency

What rights do clients have?

PBM Marketplace: Vendor Changes

- **Key Issue**
 - » Ongoing M&A activity has consolidated the PBM industry to 3 large vendors
 - » Caremark's recent acquisition of AdvancePCS
 - » Consolidation of smaller PBMs (sale of EHS to PharmaCare)
 - » Acquisition of specialty vendors by mainstream PBMs
 - (ESI–CuraScript/Priority Health; Medco–Accredo)
 - » Health plan refocus on pharmacy (e.g., Aetna, WellPoint/Anthem)
- **Why Important?**
 - » Concern about lack of choice Specialty/Biotech Drugs
 - » Concern about impact on pricing
 - » Carve-in vs. carve-out
 - » Formulary choices made for us?

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Benefit Design

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To manage the industry change

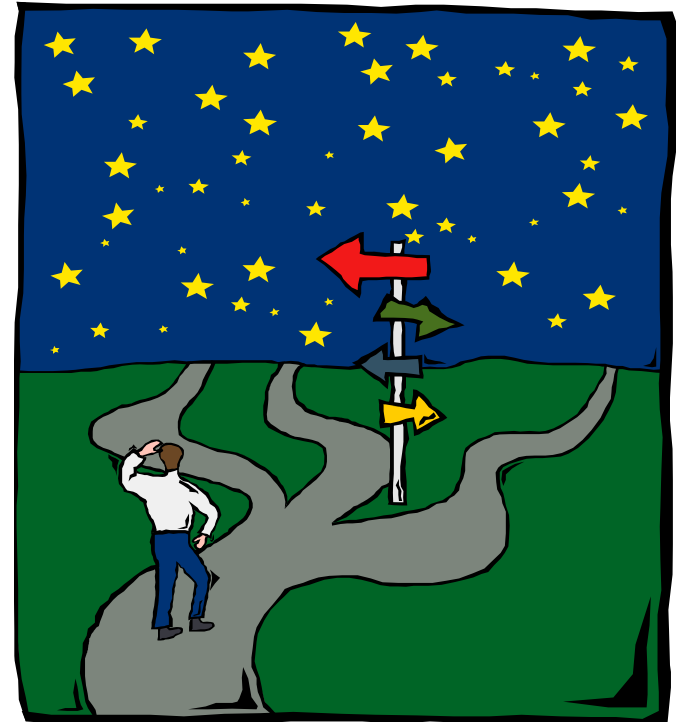
Key Cost Drivers Within Employer's Control

- **Employee/retiree cost sharing**
 - » Contribution strategy moves membership
 - » Legal implications of change
- **Copay/Coinsurance structure**
 - » Range of 3% to 50% **not** including contribution
 - » Preferred (formulary) drug therapy and generic drug incentives through tiered cost-sharing
 - Tiers save payer money, not patient
- **Rx drug coverage rules**
 - » Lifestyle/cosmetic use medications
 - » Utilization management programs
 - » Quantity vs. time limitations
- **COB enforcement**
- **Utilization and clinical management programs**
- **Employee/retiree contribution strategy**
- **PBM/vendor contractual pricing**
- **Employee/retiree communications and education**
- **Drug distribution channel management**

Benefit Design Management

Other Benefit Design Considerations

- Formulary size
- Quantity and duration of therapy limits
- Step-therapy approaches
- Therapeutic MAC programs
- Coinsurance
- Mandatory vs. voluntary programs
- Distribution channel management
- Unique populations
- Implementation of vendor's clinical and utilization management programs
- Linkage with disease management programs

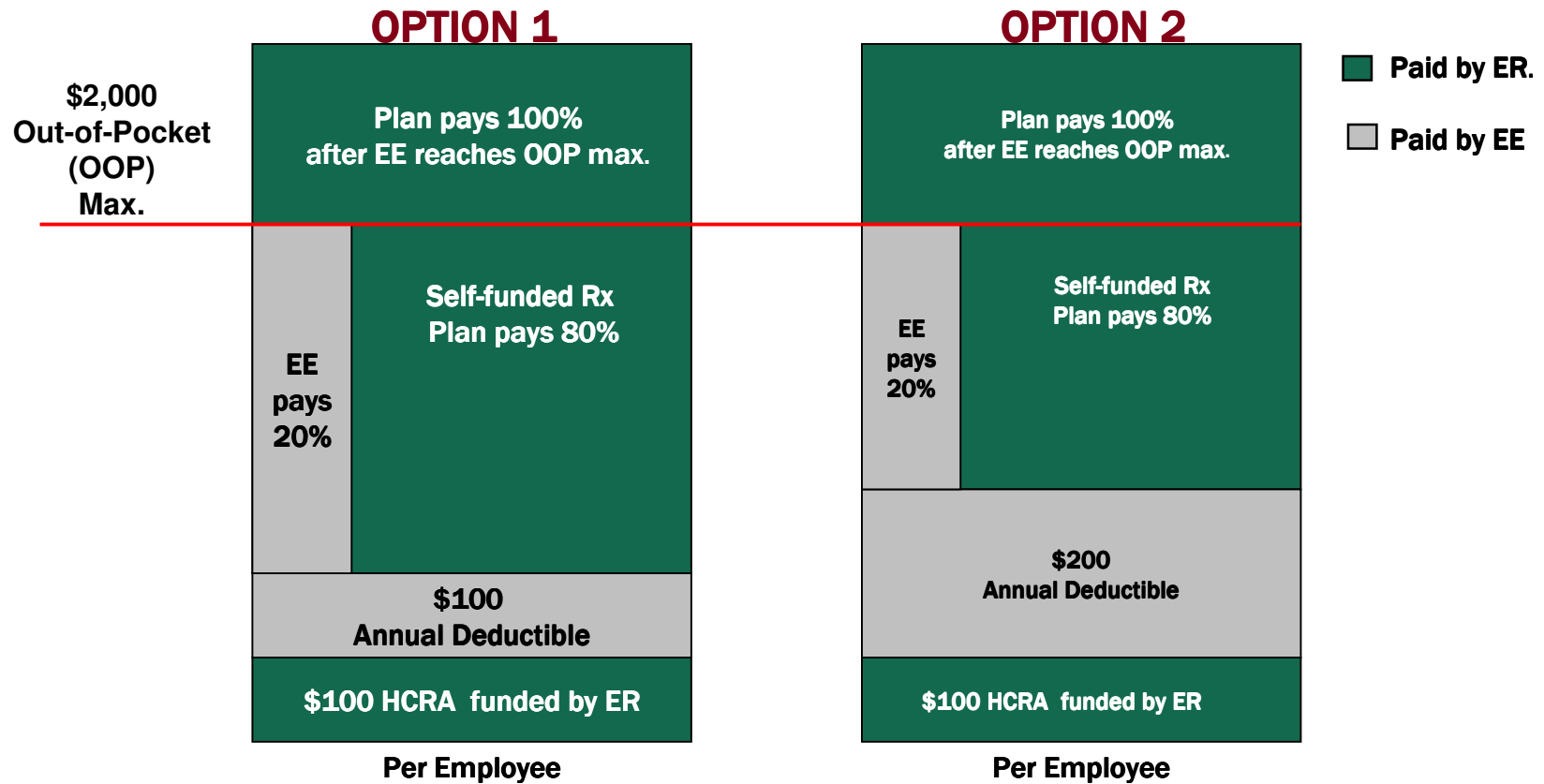


Common Plan Design for Multi-Tier Copayments

Tier	Two-Tier Design	Three-Tier Design	Three-Tier Design	Four-Tier Design
First Tier	Generic	Generic	Generic	Generic
Second Tier	Brand	Single-Source Brand	Preferred (Formulary) Brand	Preferred Brand
Third Tier	NA	Multiple-Source Brand	Non-Preferred (Non-Formulary) Brand	Non-Preferred Brand
Fourth Tier	NA	NA	NA	Biotech drugs, lifestyle, non-formulary, or other high-cost drugs

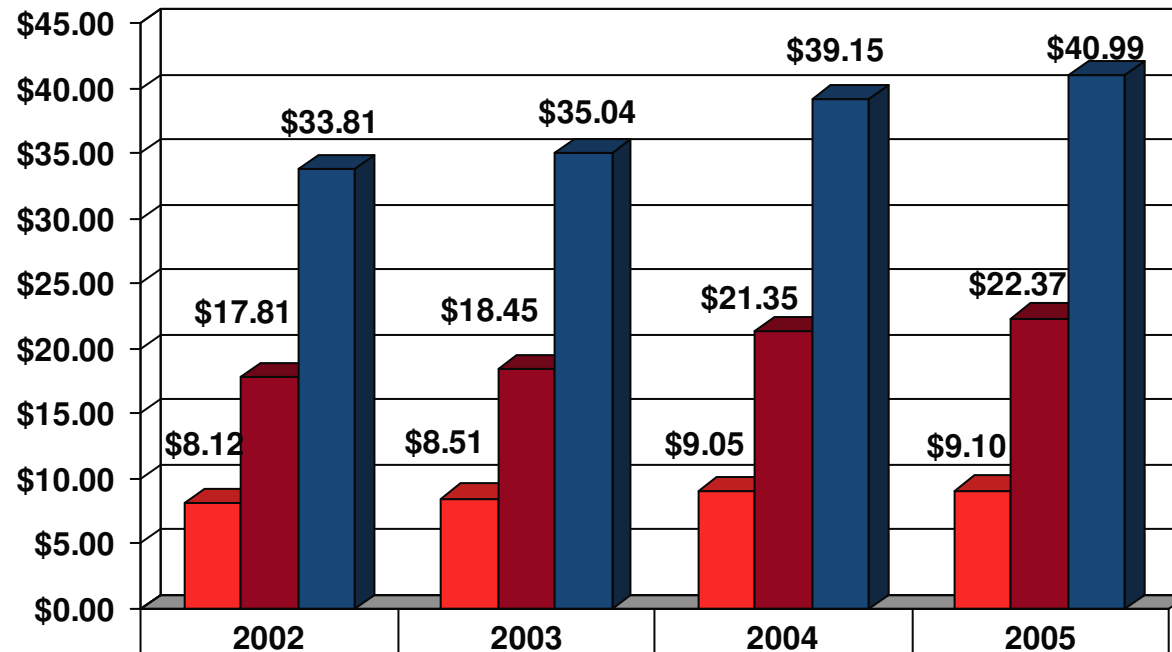
CDHC Prescription Drug Plan

Plan Design Alternatives



To manage industry change

Average Retail Copays: 2002 - 2005

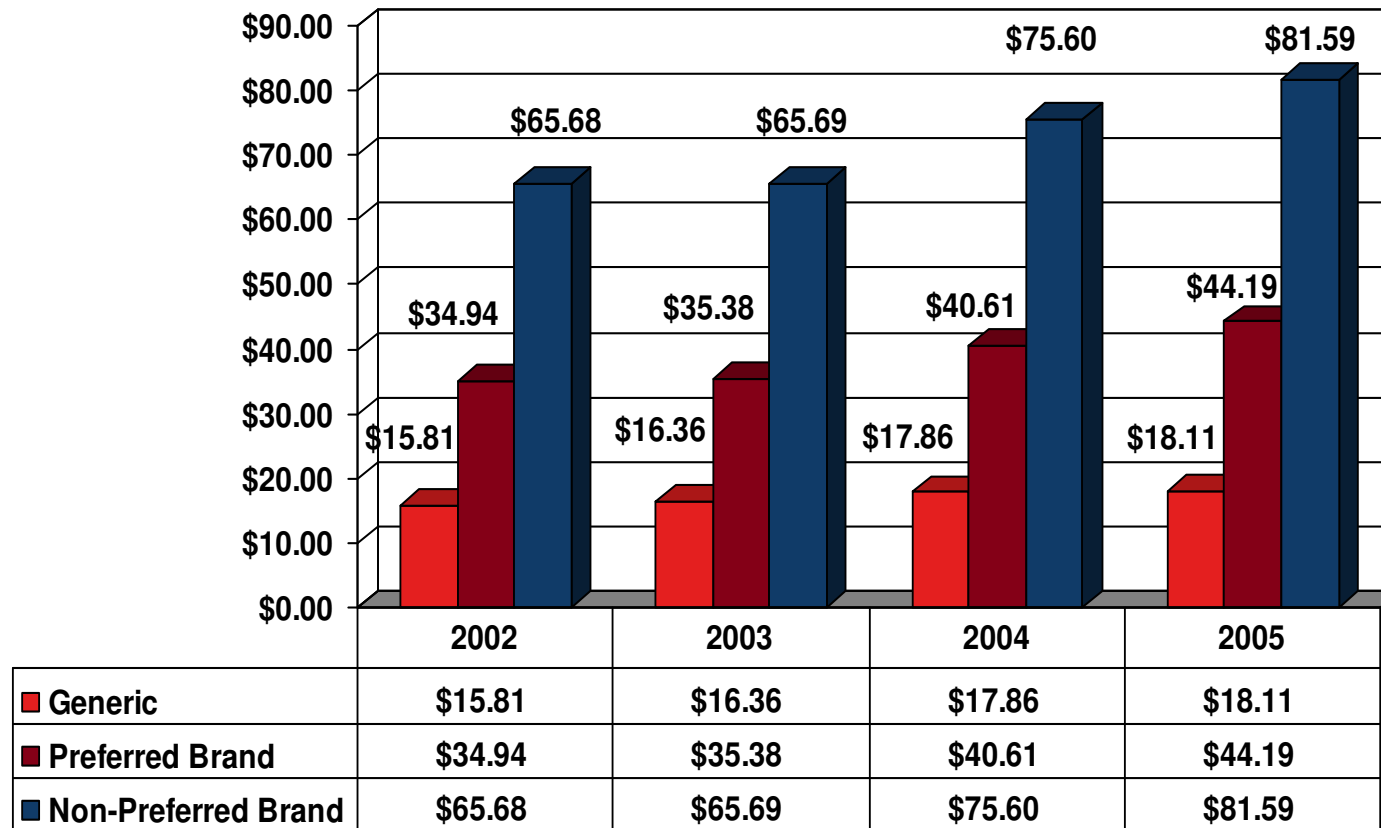


■ Generic	\$8.12	\$8.51	\$9.05	\$9.10
■ Preferred Brand	\$17.81	\$18.45	\$21.35	\$22.37
■ Non-Preferred Brand	\$33.81	\$35.04	\$39.15	\$40.99

Source: Kaiser/HRET Survey of Employer-Sponsored Health Benefits; Goldman Sachs Estimates; PBM data.

To manage industry change

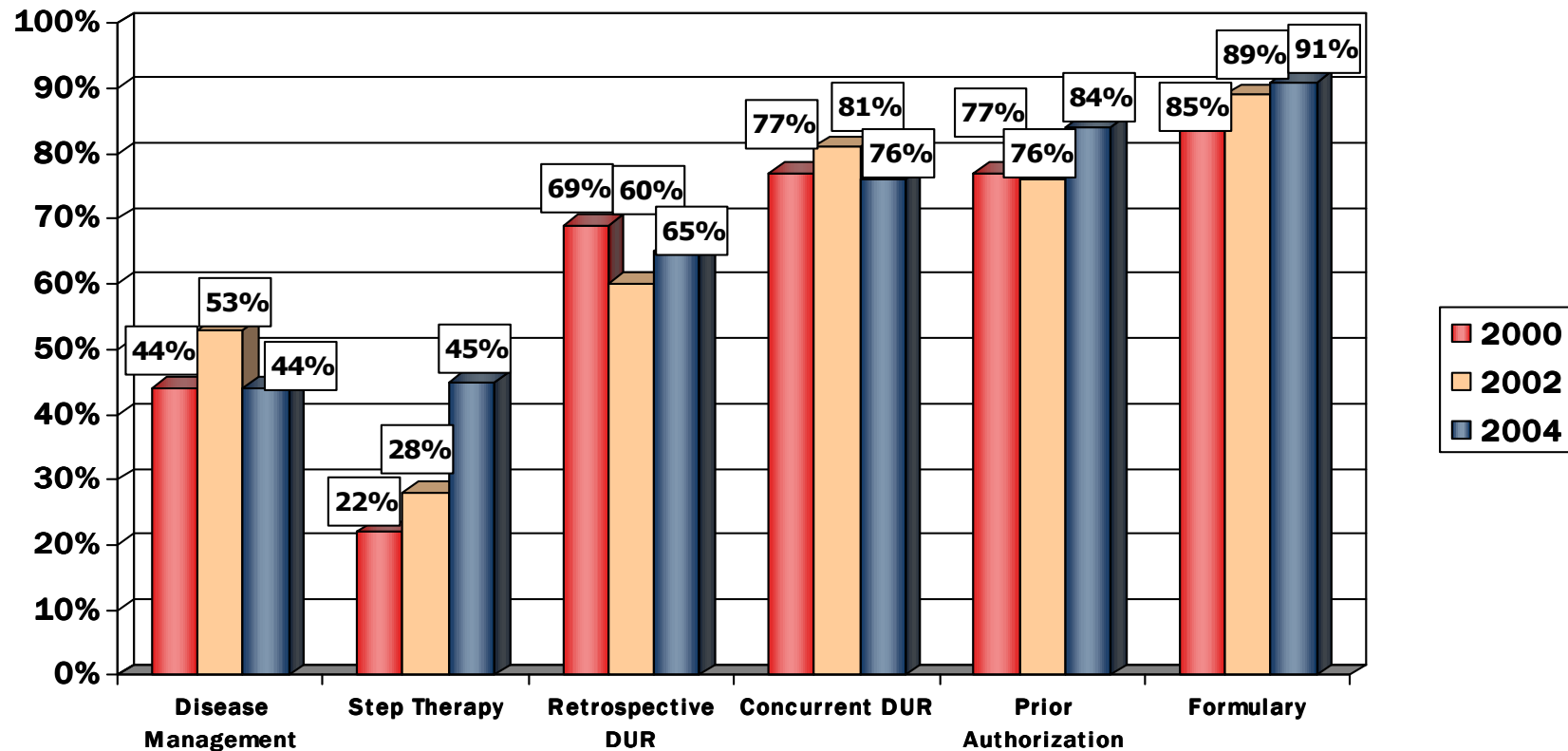
Average Mail Order Copays: 2002 - 2005



Source: Kaiser/HRET Survey of Employer-Sponsored Health Benefits; Goldman Sachs Estimates; PBM data.

To Manage Industry Change, Payers Need To:

Utilize Management Programs



Source: Takeda Pharmaceutical Company Survey, 2005

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Due Diligence & Pricing

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Due Diligence & Pricing

What Thoughts will lead to Action?

- Look at Rx plan as an investment
- Fiduciary responsibility protocols
- Increased Rx plan costs comparable to 2006 salary increase for average employee
- Verify everything the vendor tells us, and then double check it!
- Savings estimates are based on vendor data and calculated by vendor
 - » **Do you always believe your kids when they say why they broke the rules?**
- If your recommendations to customers cost your company money, how often would you make them?

Due Diligence & Pricing: Activities to Consider

- Audits
 - » Operational
 - » Financial & Service
 - » Benefit administration
 - » Implementation and service
- Benchmarking
 - » Employee payments
 - » Financial terms
 - » Offered benefits
- Verification of ROI for programs
 - » Clinical and Formulary rebates
 - » Prior Authorization
- Manage utilization

Timing of audits can influence vendor renegotiations, service levels, cooperation in account management and implementing benefit changes

Knowing where we stand in the world can open our eyes to our position

Our fiduciary and SOX responsibility

Performing Due Diligence for Subsidy Collection

Why?

- Minimize financial consequences of errors in Retiree Drug Subsidy (RDS) data submission
- Streamline RDS administrative oversight
 - » Minimize risk of errors in subsidy submissions
 - » Maximize subsidy reimbursements to Plan Sponsors
- Potentially simplify new RDS roles and responsibilities
- Integrate medical and pharmacy claims data for Part B versus Part D drugs for reporting purposes
- Audit vendors on an ongoing basis

Today's Pharmacy Benefit Marketplace

Summary

- Economic landscape does not show short-term relief for employers
- Effective management of the Pharmacy benefit can help
- Cost sharing needs to be monitored
- Vendor impact is growing
- Specialty/Biotech drugs present unique challenges
- Technology opens new worlds of opportunity and cost
- More proactive employer involvement is required moving forward
- Due diligence is critical element to managing Pharmacy costs
- We have options to help manage Pharmacy costs more effectively as employers address challenges on the horizon