
DRUG BENEFIT NEWS

As MLR Enforcement Nears, Report Shows PBM Impact Still Open to Interpretation

With the much-anticipated effective date for the medical loss ratio (MLR) regulation drawing near, an investment analysis by Credit Suisse raises questions about whether insurers can treat outsourced pharmacy services wholly as medical costs. Homing in on possible advantages for WellPoint, Inc. and Express Scripts, Inc. in the area of outsourced mail order pharmacy services, the equity report highlights a considerable gray area around pharmacy services under the MLR requirements. Many consultants concur with the Swiss financial giant that, even as it becomes effective Jan. 1, 2011, the voluminous regulation leaves wide latitude for interpreting what gets chalked up as a medical cost and what comes off a company's bottom line.

"Despite taking 300-plus pages to define a simple ratio of medical expense divided by premium, or 'Medical Loss Ratio,' the regulations still are not clear," the report reads.

Credit Suisse investment analyst Charles Boorady and a team of researchers raise the question of whether outsourcing to a PBM can be logged as a medical cost. They note that the final draft regulations from the National Association of Insurance Commissioners "were fairly silent on the details of how outsourcing of pharmacy...would be handled." But when the interim final reg appeared, the researchers "found language that seems to preclude outsourcing as a work-around of the minimum MLR regulations."

"My interpretation is that outsourcing will allow all PBM costs to be treated as medical unless they are specifically for other [expenditures] than drugs, while the administrative expenses and profit of an in-house PBM or wholly owned subsidiary would be excluded," Roger Collier, a former health care executive and consultant, tells *DBN*. Collier likens the payment mechanism for PBM outsourcing under the MLR reg to the way hospital or provider charges are treated as single payments, without administrative costs broken out.

Other experts predict the miniscule administrative fee attached to the typical drug transaction will provide little or no inducement in itself for a payer to outsource pharmacy services. "The administrative

component of pharmacy is really small," says David Tuomala, director of actuarial services at Ingenix Consulting. "The fees charged by PBMs [per transaction] are measured in cents." But, as Collier points out, for the insurer with an MLR near the minimum of the ratio — 80% for individuals and small groups, and 85% for large groups — every penny counts. "A 1% MLR differential could make the difference between an insurer meeting and not meeting the MLR threshold," Collier says.

Jean LeMasurier, senior vice president for public policy at the Gorman Health Group, is not so sure, though, that administrative fees can be written off as medical costs. She quotes MLR language on deductions for "amounts paid to third-party vendors for network development, administrative fees, claims processing, and utilization management. For example, if an issuer contracts with a behavioral health, chiropractic network, or high technology radiology vendor, or a pharmacy benefit manager, and the vendor reimburses the provider at one amount but bills the issuer a higher amount to cover its network development, utilization management costs and profits, then the amount that exceeds the reimbursement to the provider must not be included in incurred claims."

The idea of outsourcing PBM services versus keeping them in-house or making other arrangements is particularly relevant in the case of the subjects of Credit Suisse's report. In April 2009 WellPoint sold its in-house PBM to Express Scripts for \$4.7 billion and has been outsourcing its pharmacy needs to it ever since.

According to Credit Suisse and others, the additional scenario in which an insurer may be able to allocate its pharmacy business to medical costs is mail order.

"If the entire prescription cost, ingredients plus administrative, is treated as medical costs, this would increase the value of mail-order utilization and incent more direct-to-payer agreements with the retailers to achieve similar treatment," George Van Antwerp, general manager of pharmacy solutions for Silverlink Communications, tells *DBN*. Depending on how the

MLR reg is applied, Van Antwerp says, leveraging mail order could influence decisions around disease management, medication therapy management and outsourced call center work and even further affect the future business models of PBMs.

But as Tuomala sees it, the advantage of mail order is already pretty much overextended. "You probably wouldn't incent insurers to use mail order more

than they already are," he says. "Insurers are already pushing mail order to the degree that they can."

Contact Collier at rcollier@rockisland.com, Tuomala at david.tuomala@ingenixconsulting.com, Van Antwerp via Marit Davies at marit.davies@silverlink.com and LeMasurier at jlemasurier@gorman-healthgroup.com. ✧