Pension & Health Benefits Committee

Agenda Item 6a

September 15, 2020

Item Name: Conversion of the Pharmaceutical Benefit Manager Contract with OptumRx to an Acquisition-Based Contract with Term Extension

Program: Health Benefits

Item Type: Action

Recommendation

Approve the transition of California Public Employees' Retirement System (CalPERS) existing traditional spread and rebate-driven pharmacy benefit manager contract with OptumRx to a market-leading acquisition-based contract with a one-year contract extension, and an option for a second-year extension at CalPERS' discretion. This new contract would align CalPERS pharmacy spend to actual drug pricing and the extension would enable CalPERS to maintain continuity of our pharmaceutical benefit manager during the COVID-19 pandemic.

Executive Summary

CalPERS maintains an existing five-year contract to administer pharmacy benefits with OptumRx. Under this existing Pharmaceutical Benefit Manager (PBM) contract, OptumRx's compensation is largely driven by acquisition price spread and increasing rebates. This contract does not allow for transparency on actual drug costs and incentivizes increasing rebates over reducing net pharmacy spending. Under this new acquisition-based contract, OptumRx would be compensated for their costs associated with procuring and dispensing drugs, rather than on the margins they profit from through drug manufacturer rebates and acquisition price spread. This model of PBM is critical to CalPERS' ability to lower drug prices for our members. Further, the one-year extension to the current contract will allow us to implement and evaluate the new acquisition-based model without committing to a new five-year agreement.

Of important note, the current PBM contract expires in December 2021. If the current contract is not extended, solicitation for a new PBM contract would need to begin immediately, due to the lengthy transition time and complexity of PBM contracts. Transitioning to a new PBM during a pandemic, given the challenges seen in the pharmaceutical supply chain, as well as the historical member disruption caused by PBM contractor transition, could cause significant issues for our members and possibly delay their access to needed medication.

Strategic Plan

This item supports CalPERS High-Quality Affordable Health Care Strategic Goal.

Background

CalPERS has long sought to reduce its pharmaceutical spend through a variety of innovative programs, including biosimilar first strategies and reference-based pricing. One of the significant challenges CalPERS (and all purchasers) face with traditional PBM contracts is the actual pricing of the drugs is not transparent. Traditional PBM contracts are constructed to increase rebates as a cost-saving measure. The problem with this contract style is that rebates are typically offered on more expensive brand drugs. Often, the most cost-effective drugs are well-proven generic drugs that do not generate rebates, but whose net costs are lower than rebatable drugs.

Transitioning to an acquisition-based contract has many advantages for CalPERS. First, the true cost of each drug is reflected in the pricing, and therefore we will have the ability to tailor our formulary and cost-savings strategies based on actual drug pricing. This transition is guaranteed to save CalPERS at least $2 million, with an additional $10 million in savings projected if extended to the option year.

Analysis

There are two options available:

1. Continue the current spread and rebate-based contract, which will terminate on December 31, 2021; or
2. Transition to a new acquisition-based contract with a one-year extension and an option for a second year at CalPERS' discretion.

Moving to the acquisition-based contract with extension provides cost savings to CalPERS members, increases transparency in drug pricing, and prevents pharmacy benefit disruption during the COVID-19 pandemic. Staying on the existing contract does not produce any cost savings, does not provide transparency in drug pricing and would require negotiating and implementing a new PBM contract during the COVID-19 pandemic, when the potential for member disruption is the highest.

Budget and Fiscal Impacts

The administrative services fees for the one-year contract extension beginning January 1, 2022, through December 31, 2022 will be approximately $10 million. This change to the overall cost of the contract will be reflected in the next Finance and Administrative Committee (FAC) Semi-Annual Prospective report.

Benefits and Risks

The benefits of moving to an acquisition-based contract include cost savings to CalPERS members and increasing transparency in drug pricing. The primary risk of remaining on the existing contract is related to member disruption from contracting for and implementing a new PBM contract during the COVID-19 pandemic.

Attachments

Not applicable.

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