



Rx Collaborative

2010 Annual Report to Employers



2010

Rx Collaborative Annual Report



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About the Rx Collaborative: Quick Facts

As of January 1, 2011, the Rx Collaborative had grown to 144 employers representing diverse geographies, sizes and industries.

- 2010 Members: 2,400,000
- 2010 Prescriptions: 25,000,000
 - Retail: 19,000,000
 - Mail: 6,000,000
- 2010 Drug Spend: \$2,700,000,000
 - Retail: \$1,300,000,000
 - Mail: \$1,400,000,000
- 2010 Generic Dispensing Rate: 70.6%

Letter From

Rx Collaborative Leadership

In 2010, the Rx Collaborative experienced phenomenal growth and change: Our collective size grew to include 144 employers, an increase of 29 organizations, which is more than in any year since our first. The Rx Collaborative is the largest employer-sponsored pharmacy benefit arrangement in the United States — larger than any single employer plan and larger than any other pharmacy purchasing coalition.

We started the year as a new company, Towers Watson, with the combined strength of two pharmacy consulting practices. Early in the year, we appointed a clinical lead to the Rx Collaborative team to help focus our efforts on defining best practices for plan management. Throughout the year we continued to support and further define our joint management approach. Employers benefit from having a Towers Watson–Medco team working with them to set plan performance goals, develop strategies for change and effectively manage their pharmacy benefit.

We also released a request for proposal (RFP) to 25 pharmacy benefit managers (PBMs) and specialty providers. The RFP was our first market check since 2003, when we launched the Rx Collaborative. After reviewing all proposals, we once again determined that Medco is the best PBM partner in the industry and, by leveraging our collective size, were able to negotiate significant improvements to our arrangement with Medco.

In addition to gaining significant financial advantages that will improve over the contract term, we have established that our coalition will be the most actively managed in existence. The result is that we now offer a certified, audited best price based on our aggregate drug spend. We continue to have unparalleled access to Medco's senior leadership, which allows us to address service and operational issues effectively.

Throughout 2010, we worked with employers to redefine the way they manage their pharmacy benefits, identifying ways to take advantage of an ever-growing generic pipeline, and using data-driven analysis to set cost-effective plan management strategies.

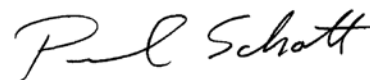
We continue to provide a comprehensive suite of services that includes:

- A robust audit program, including an annual rebate and claim audit, and an operational assessment
- Access to the Towers Watson Reference Formulary® (TWRF), a custom, low-net-cost generics-based formulary developed and maintained by our independent Pharmacy and Therapeutics Committee
- An independent Rx Collaborative Data Warehouse that prepares client-specific reports (for those employers that agree to share data) and benchmarking analysis
- Several communication venues where we share best practices, discuss trends in the pharmaceutical industry and offer operational information

The Rx Collaborative is unique in the marketplace. We look forward to continuing to provide the most innovative pharmacy coalition available to employers. We expect further growth and change as we remain focused on the clinical, financial and plan design levers of pharmacy management.

As always, we strive to better serve your needs, and we welcome your feedback. If you have any questions, comments or suggestions, please connect with your local Towers Watson pharmacy consultant or e-mail the Rx Collaborative mailbox at RxCollaborative@towerswatson.com.

Sincerely,



Paul Schott
Rx Collaborative Team Lead

“The Rx Collaborative is unique in the marketplace.”

Rx Collaborative Value Proposition

On behalf of the Rx Collaborative, Towers Watson developed and released an RFP in December 2009. The purpose of the RFP was to evaluate the marketplace and negotiate the most competitive terms available for pharmacy benefit management (PBM) services. The RFP included marketing of the aggregated \$2.7 billion annual drug spend of our then 121 employers. RFPs were released to 25 providers of PBM services, including major PBMs and specialty pharmacies.

In addition to determining the best price available, our goal was to identify a PBM partner that would closely align with the Rx Collaborative's guiding principles and provide market-leading innovation in pharmacy management and account management best practices.

The RFP was developed to require both qualitative and quantitative responses to a questionnaire, as well as submission of a repriced claim file. Towers Watson evaluated proposals from six bidders. Results showed that Medco is the PBM that most closely aligns with our guiding principles, offers the best financial value and demonstrates a commitment to our account management services model.

Contract Overview

The RFP provided a basis for negotiating improved terms and confirmed that we offer the best contract in the market. The terms of the new contract reflect the aggregate size and spend of the Rx Collaborative and ensure aggressive pricing for all member employers.

Highlights of the arrangement include:

- Contract term from Jan. 1, 2011, through Dec. 31, 2014, with an automatic market-based price improvement effective Jan. 1, 2013
- A two-year term offered in 2015 to all Rx Collaborative employers
- Certified and audited best price based on our aggregate size
- Agreement to jointly manage the Maximum Allowable Cost (MAC) list to ensure aggressive generic pricing for both retail and mail

- Improved financial terms:
 - Generic guarantees that improve annually over the contract term and leverage the increase in generic use due to patent expiration of widely used name brand drugs
 - Component guarantees for retail, mail and rebates that allow employers to maintain tighter control over contract performance
 - Per-employee-per-month administrative fees
 - \$0 mail order dispensing fee for both brand and generic claims
 - Minimum 10% discount on Medco fees for services such as utilization management, consumer-driven health plans, employee group waiver and retiree drug subsidy programs
 - Rebate guarantees on all brand claims, which eliminates the “days’ supply” tactic
- Improved service-level guarantees that include exclusive Rx Collaborative account management and specialty guarantees

Employer Response

The negotiated arrangement was presented to more than 80 Rx Collaborative employers with contracts that offered the option to access improved deal terms in exchange for extending the contract end date by two years — from Dec. 31, 2012, to Dec. 31, 2014. All employers were offered significant savings and, to date, more than 90% have chosen to take advantage of this opportunity and extend their contracts. Our outstanding renewal success reaffirms the attractiveness of the Rx Collaborative value proposition.

During 2010, prospects were offered access to the negotiated arrangement as well. This market-leading arrangement was well received, and the Rx Collaborative added 29 new employers. We will leverage our ever-increasing size in future contract negotiations to continue to provide aggressive pricing in the future.

“Our goal was to identify a PBM partner that would closely align with the Rx Collaborative’s guiding principles and provide market-leading innovation in pharmacy management and account management best practices.”

Rx Group Purchasing: A New Client Case Study

Background: Company A, in the consumer electronics industry, has roughly 7,000 employees and \$15 million in annual drug spend. In 2010, it was in the final year of a three-year contract with a midsize PBM. The incumbent provided a large national network of retail pharmacies, modestly competitive pricing and a lot of innovative ideas. During the competitive marketing process three years prior, Company A was impressed with this PBM's vision. Despite the abstract value proposition and nonspecific performance guarantees, Company A selected this organization in hopes of discovering a new solution to managing its pharmacy costs.

Issue: Unfortunately, the PBM's account team was not as responsive as Company A had expected, and employees were frustrated with the PBM's inability to resolve issues to their satisfaction. Becoming skeptical about its ability to manage pharmacy trends, Company A decided to seek a different PBM relationship beginning in 2011. It shared this decision with the Towers Watson consulting team.

Action: Company A recalled that Towers Watson had presented a customized Rx Collaborative value proposition in the past at no cost and asked if the offer was still available. Towers Watson responded that it was and requested Company A's current data to prepare an accurate savings analysis. Company A felt that it had very little to lose because the Rx Collaborative savings assessment would only take three weeks from the time data was provided. This would leave enough time to seek a competitive

bid if the analysis was not compelling. Company A knew that the Rx Collaborative could provide an arrangement with a PBM (Medco) the company had reviewed in the past, found its capabilities impressive and was familiar with its senior management. Company A felt that if it could both obtain the consulting services of Towers Watson and receive a transparent arrangement with Medco, it would be able to gain significant time and financial savings by not going out to bid. Company A was also in the process of acquiring a new business and needed to merge the benefits of the new organization with limited resources.

Results: In August 2010, the savings analysis supported Company A's decision to select Medco, through the Rx Collaborative, as its new PBM. When asked why Company A chose Towers Watson, the director of benefits cited the 8% (\$5.3 million) in savings over a new four-year contract term with an automatic price improvement after the second year. Additionally, the company was pleased with the specific deliverables included in the management fees. Company A complimented the Towers Watson consultants for their responsiveness and transparency in answering questions: "[Company A] had terrific experiences with Towers Watson through this process and believe in the value that Towers Watson can continue to bring." Additionally, the company appreciated all the help the team provided in addressing questions related to design and strategy, and was excited about the opportunity to work closely with Towers Watson for help in more effectively managing its pharmacy program.



Clinical Management

The Year in Review

Towers Watson's clinical team works with employers to optimally manage the pharmacy benefit. In 2010, the Rx Collaborative appointed a dedicated clinical lead responsible for working with Towers Watson's pharmacy consultants to define best practices in clinical management for plan sponsors. In addition, the Rx Collaborative has an independent Pharmacy and Therapeutics (P&T) Committee that supports the activities of the Rx Collaborative clinical team. This depth of expertise allows Towers Watson to bring innovative pharmacy management solutions to its clients.

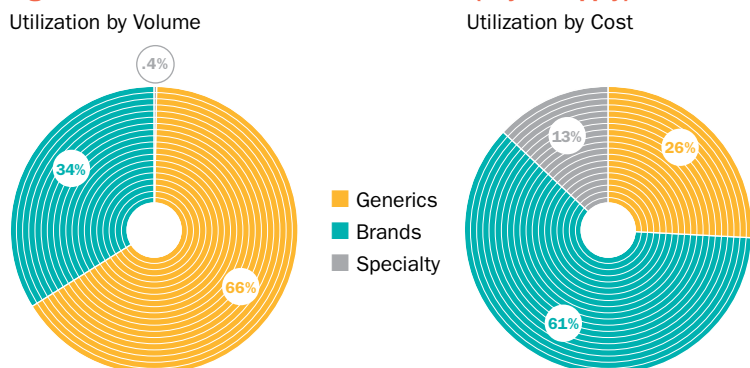
From its inception, the Rx Collaborative has been committed to helping clients manage pharmacy costs and preserve access to needed medications by optimizing the two key factors that drive drug spend:

- Discount terms (the deal)
- Drug mix

The discount terms represent the total discount achieved by applying all parameters of the deal, including rebates, to the average wholesale price (AWP) of the drugs. Drug mix can be simply defined as the average claim volume of generic, brand and specialty drugs. Drug mix drives the total AWP, which is the cost basis of drugs before discounts are applied. Therefore, one major focus of the Rx Collaborative clinical team is to help clients manage cost by optimizing the drug mix.

The Rx Collaborative's 2010 utilization — measured by days of therapy — was unequally divided among generics, brands and specialty medications. Roughly two-thirds of the drug utilization was attributable to generics, one-third to brands and less than one-half of one percent to specialty drugs. In contrast, the group's resulting drug spend, defined as "discounted ingredient cost plus dispensing fees," follows a very different distribution. The Rx Collaborative incurred \$2.7 billion, or \$95 per member per month, in covered charges. While accounting for two-thirds of the utilization, generics made up only one-quarter of the drug spend (\$0.7 billion), while traditional brands drove 60% of the spend (\$1.7 billion) and specialty drugs contributed nearly 15% of the total drug spend (\$0.3 billion).

Figure 1. 2010 Rx Collaborative utilization (day of supply)



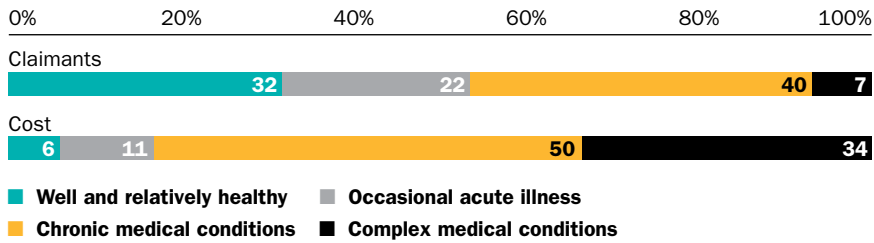
Source: Medco Health Solutions
Totals may not equal 100% due to rounding.

Successful clinical management strategies help control the cost of selected drug categories by moving claim volumes from higher-cost to lower-cost therapies while providing access to equally effective and safe medication classes. In 2010, the Rx Collaborative clinical team focused on strengthening clients' ability to manage costs by optimizing the drug mix.

Trend, Drivers and Mitigators

Overall 2010 costs to Rx Collaborative companies, as a group, increased 2.2% per member per month compared to 2009. Drivers of increased cost included members' health status, manufacturer price increases and drug mix. Mitigators of these costs included increased generic utilization and clinical drug management programs designed to shift utilization toward lower-cost, therapeutically equivalent medications.

Figure 2. Rx Collaborative health status as a group



Source: Medco Health Solutions
Totals may not equal 100% due to rounding.

Population Health Status

Using pharmacy claim data, Medco developed a methodology for stratifying the health status of large populations into four main categories. *Figure 2* above represents the Rx Collaborative stratification for 2010.

Healthy with low drug spend. Roughly one-third (32%) of individuals (claimants) who incurred claims through Medco were well and relatively healthy. While accounting for almost one-third of the population, they accounted for only 6% of the drug spend. These claimants typically use low-cost medications for preventive reasons. Examples of medications among these individuals are oral contraceptives and vitamins.

Slightly less than one-quarter (22%) of claimants had occasional acute illnesses, such as short-lived infections that required a course of antibiotics, or acute events that required brief courses of pain control.

Together, these two groups accounted for more than half of the claimants (54%) who created relatively very little cost (17% or \$0.5 billion). Therefore, relative to other challenges at this time, they do not represent a high-priority cost management target.

Ill with significantly high drug spend. On the other hand, 40% of claimants are affected by chronic medical conditions that drove \$1.3 billion of the drug spend (50%). These individuals have diagnoses such as heart disease, high blood pressure, high cholesterol, diabetes and ulcers. The remaining 7% of claimants are affected by complex medical conditions, which drove nearly \$1 billion (34%) of the drug spend. These individuals have diagnoses such as rheumatoid arthritis, advanced malignancies, organ transplant needed and end-stage kidney disease.

Together, these two groups accounted for less than half of the claimants (47%), yet they incurred nearly all of the cost (84%). These claimants and their conditions present significant cost management challenges and opportunities to Rx Collaborative employers. Therefore, it is the area on which the Rx Collaborative clinical team and the Pharmacy and Therapeutics Committee focus most of their efforts.

Cost Drivers

The Rx Collaborative's top 10 medications, as shown in *Figure 3*, were accounted for by seven chronic or complex conditions. These drugs are all branded products and, while they accounted for only 8% of the utilization, they represented 20% of covered charges in 2010. Compared to 2009, Nexium, Lipitor and Enbrel remained in the first, second and

Figure 3. 2010 Top medications

2009 Rank	2010 Rank	Medication	Therapy Class or Condition	Claimants	Covered Charges (in millions)	% of All Charges for the Class
1	1	Nexium®	Proton pump inhibitor (PPI)	65,000	\$90	60%
2	2	Lipitor®	High cholesterol	85,000	\$85	50%
3	3	Enbrel®	Rheumatoid arthritis	3,000	\$50	50%
6	4	Humira®	Rheumatoid arthritis	2,500	\$40	45%
4	5	Plavix®	Antiplatelet	30,000	\$45	90%
5	6	Advair®	Pulmonary, asthma	40,000	\$40	30%
8	7	Crestor®	High cholesterol	45,000	\$40	25%
7	8	Singulair®	Pulmonary, asthma	55,000	\$40	30%
10	9	Copaxone®	Multiple sclerosis	1,000	\$30	50%
9	10	Actos®	Diabetes, type II	20,000	\$30	30%

Source: Medco Health Solutions

“Successful clinical management strategies help control the cost of selected drug categories by moving claim volumes from higher-cost to lower-cost therapies while providing access to equally effective and safe medication classes.”

third positions. Three other medications rose in rank (Humira, Crestor and Copaxone), and four fell in the ranking (Plavix, Advair, Singulair and Actos).

Furthermore, these individual medications account for significant concentrations of total drug spend for their indications. For example, Nexium accounts for 60% of the expense in the proton pump inhibitor class, with the balance of drug spend spread across the other 11 products, including four generic agents. Another example is in the high-cholesterol class, where Lipitor and Crestor account for nearly 75% of the drug spend. The remaining 25% of cost is spread across 14 other brands and generics that work the same way and can be effective for the vast majority of patients who need moderate decreases in their cholesterol levels.

These examples speak to the imbalance of cost distributions among equivalent therapies and create the basic foundation for Rx Collaborative utilization management strategies.

Managing Utilization

Each employer should have a core strategy in place to manage the primary cost drivers. For example, *Figure 4* lists the Rx Collaborative’s top 10 medications (ranked by cost) as well as the minimum components of a utilization management strategy that should be in place.

Core Utilization Management Components. The cornerstone of every employer’s strategy should include administrative edits to guarantee eligibility for coverage, clinical edits to reduce medication interactions or overdoses, and a formulary with copay differentials. Other rules should be applied based on the medication, treatment guidelines and utilization data.

Prior authorization rules validate diagnosis before a coverage determination is made to avoid claims for investigational use. Almost all specialty medications should have a prior authorization requirement, especially rheumatoid arthritis and multiple sclerosis products. Preferred drug step therapy (PDST) rules maximize utilization for low-cost medications within a therapeutic class. Most of the top 200 medications are candidates for PDST, especially the proton pump inhibitors and cholesterol reducers. Quantity or dose duration rules, designed to avoid stockpiling, are suitable for high-cost claims and inhaled medications such as Advair.

Medco’s Standard Programs Are Customized for Rx Collaborative Utilization. Clients may choose Medco’s standard rule packages, or they may select Rx Collaborative-specific components such as the TW Reference Formulary or the Rx Collaborative utilization management edits. The advantage of a customized Rx Collaborative formulary or utilization

Figure 4. Rx Collaborative core utilization management strategies for the top 10 medications (by cost)

Medication	Therapy Class or Condition	Eligibility and Safety Edits	Formulary With Copay Differentials	Prior Auth. for Diagnosis	Preferred Drug	Quantity or Dose Duration
Nexium	Proton pump inhibitors	✓	✓		✓	
Lipitor	High cholesterol	✓	✓		✓	
Enbrel	Rheumatoid arthritis	✓	✓	✓	✓	✓
Humira	Rheumatoid arthritis	✓	✓	✓	✓	✓
Plavix	Antiplatelet	✓	✓			
Advair	Pulmonary, asthma	✓	✓			✓
Crestor	High cholesterol	✓	✓		✓	
Singulair	Pulmonary, asthma	✓	✓			
Copaxone	Multiple sclerosis	✓	✓	✓	✓	
Actos	Diabetes, type II	✓	✓		✓	

Figure 5. Rx Collaborative benchmark GDR for therapy classes driving cost

Therapy Class	Medication	GDR Benchmark
Proton pump inhibitors	Nexium	60%
High cholesterol	Lipitor	46%
Rheumatoid arthritis	Enbrel	13%
Rheumatoid arthritis	Humira	13%
Antiplatelet	Plavix	5%
Pulmonary, asthma	Advair	3%
High cholesterol	Crestor	46%
Pulmonary, asthma	Singulair	3%
Multiple sclerosis	Copaxone	8%
Diabetes, type II	Actos	71%

management rule is that each was developed based on the Rx Collaborative's own utilization and cost data. The TW Reference Formulary lists preferred products in five of the classes and includes four generics-first PDST rules, which target both proton pump inhibitors and the high-cholesterol therapy class.

Results: Higher Generic Dispensing Rates and Lower Cost. The results of utilization management can be dramatic. The overall generic dispensing rate (GDR) for Rx Collaborative companies in 2010 was 66% (based on days of supply and strictly defined generics), within a range of 81% to 48%, on average. One company achieved a 91% GDR for proton pump

inhibitors, and another achieved an 88% GDR for the high-cholesterol class. Both achievements were the result of formulary and utilization management edits supported by design incentives.

As stated previously, clinical strategies are designed to increase generic dispensing rates, minimize waste and reduce costs without compromising access to essential medications. *Figure 5* illustrates the Rx Collaborative benchmark GDR achieved for some therapeutic classes.

Recommendations for Rx Collaborative Clients

The Towers Watson clinical team has developed a number of proven strategies to help clients better manage their drug costs while preserving access and clinical outcomes. By taking only a few simple steps, Rx Collaborative clients can reduce their pharmacy costs significantly. Working with your Towers Watson pharmacy consultant, we recommend the following five actions for 2011:

1. Identify the Top 25 medications ranked by cost.
2. Itemize the UM programs currently in effect.
3. Determine whether your GDR and cost results are at target.
4. If cost results are not at target, model utilization shifts and savings opportunities.
5. Implement new programs with a strong positively focused communication campaign.

The Rx Collaborative Clinical Lead and the Pharmacy and Therapeutics (P&T) Committee

As the Rx Collaborative clinical lead, Bridget Eber, Pharm.D., is responsible for setting overall clinical strategy and defining best practice pharmacy plan management for Rx Collaborative clients. A pharmacist by background, she acts as liaison to the independent P&T Committee, which consists of physicians and pharmacists who have significant experience in their professional fields and executive-level managed care leadership experience.

On a quarterly basis, the clinical lead and the P&T Committee meet to discuss the best thinking and contemporary ideas in clinical pharmacy management. Members contribute perspectives on current drug therapy practices in their areas of expertise, vote on medications to add or delete from the Towers Watson Reference

Formulary and address practical considerations regarding utilization management strategies for employers.

Our experts come with an understanding of the pharmaceutical industry, government programs, health plans and clinical practice areas, including psychiatry, internal medicine and family practice.

P&T Committee

Dea Belazi, Pharm.D., MPH, Managed Markets Lead, Wolters Kluwer

Mark Fuller, M.D., FACP Psychiatry, kc2 Medical Communications

Allan Goldstein, M.D., MPH, FACP Internal Medicine, Goldstein Health Care Consulting

Gary Owens, M.D. Family Practice, P&T Committee Chair

Chantell Reagan, Pharm.D., Managing Director, InformaCeutica

Rx Collaborative Audit Initiative

The Rx Collaborative offers a comprehensive suite of consulting services that allow plan sponsors to effectively manage long-term pharmacy benefit trends. Towers Watson's approach to effective pharmacy management includes periodic audits of financial terms and PBM operations. These reviews verify contract compliance, ensure continuous quality improvement and allow Towers Watson to identify emerging PBM revenue streams. Insight gained from these audits on financial and operational components of the Rx Collaborative arrangement provide leverage for future contract negotiations and empower us to continue to provide the most effective pharmacy management contract available.

Services provided in 2010 included an audit of 2009 earned rebates and claims and an operational assessment.

2009 Rebate Audit

For the fifth consecutive year, Towers Watson engaged KPMG to conduct the rebate audit. The audit consists of two components:

- Verifying that 100% of pharmaceutical manufacturer revenue attributable to client utilization was passed on to the plan sponsor
- Verifying that rebate guarantees were paid correctly according to contractual terms and experience for 2009

KPMG works with Towers Watson to select a statistically valid sample of Rx Collaborative plan sponsors and a representative sample of pharmaceutical manufacturers. For the plans selected, data collected from Medco include quarterly rebate reports, utilization data, and formulary and plan designs. KPMG then reviews manufacturer rebate agreements and all agreements that fall under the Total Rebate section of the PBM Administrative Services Agreement. They perform an analysis of the information collected and resolve discrepancies with Medco. Finally, KPMG prepares an audit report. The initial KPMG rebate audit report was released to clients during the Rx Collaborative quarterly call on December 14, 2010, and the final report was released in January 2011.

The audit found that, overall, Medco adhered to the Rx Collaborative contract terms in effect at the time and passed on 100% of the rebates received from pharmaceutical manufacturers — with a few exceptions:

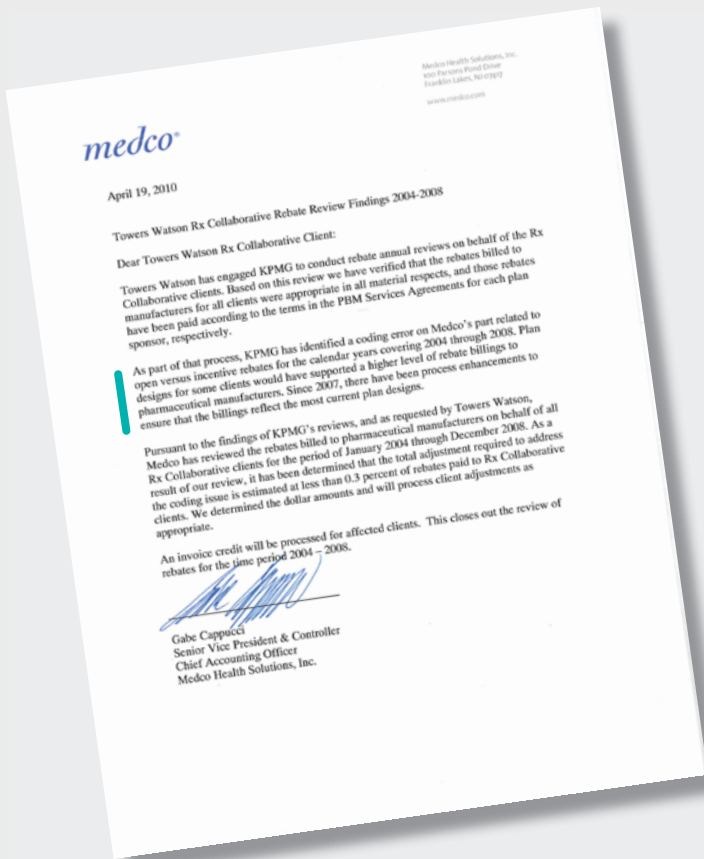
- Medco erroneously paid some rebates at the open formulary level, whereas the plan sponsors' designs qualified for the higher, incentive formulary rebates. Medco determined that the error occurred because the plans were not set up correctly in its system. (While a similar discrepancy was found in the payment of some rebates at the correct formulary level in the 2004–2008 rebate review, the cause of the 2009 error was different.)
 - Medco is in the process of reviewing the accuracy of the setup of all Rx Collaborative plans in its system. The review, and the payment of any financial impact, will be complete by April 30, 2011. Moving forward, quality improvements will be made to ensure that plan designs will be entered correctly.
- Medco misallocated rebates for one product in the first quarter of 2009 for three of the five plans reviewed.
 - Medco confirmed that the misallocation occurred across its book of business. Towers Watson reviewed the financial impact to Rx Collaborative clients, and the financial impact was determined to be minimal in all cases. All affected clients had their December 2010 rebate payments adjusted to reflect the misallocation.

“Insights gained from these audits provide leverage for future contract negotiations and empower us to continue to provide the most effective pharmacy management contract available.”

Audits Lead to Payouts to Plan Sponsors and Quality Improvements

Audits verify that the contract terms are administered properly. An audit finding ensures that clients will receive all funds that are owed and ultimately leads to process and quality improvements at Medco. During the 2004–2008 rebate review, KPMG found that a small subset of clients were paid rebates at the open formulary level when they should have been paid at the higher incentive formulary rebate level.

Medco calculated the financial impact to affected clients, and payments were made in April 2010. Medco prepared a letter, signed by its chief accounting officer, certifying that Medco had reviewed the rebates to all Rx Collaborative clients and that process enhancements implemented at Medco would ensure that future billings reflect the most current plan designs.



2009 Group-Level Claim Audit

During 2010, the Rx Collaborative performed a group-level claim audit of Medco. The audit assessed claims incurred during calendar year 2009 for compliance with each client's transparent contract pricing terms (both pre- and post-AWP settlement) in effect during that time.

Medco provided a file (void of any personal health information) that contained 18,242,922 claims representing \$1,980,697,682 in covered charges for 2009. This audit re-adjudicated each claim that was identified as a traditional prescription. Claims identified as specialty medications, were re-adjudicated based on a representative sample of each pricing option, i.e., "Accredo-exclusive" and "open" distribution channels. The review included claims from mail and retail; the product type was determined (single-source/multisource, brand/generic), and the appropriate discounts were applied using specific adjudication logic.

The audit verified compliance with the transparent Rx Collaborative pricing contract terms in effect (on both pre- and post-AWP settlement) during 2009, except for specialty claims paid for some Rx Collaborative employers. As a result of these employers' enrollment in retail refill allowance (RRA) or retail strategy optimization (RSO), some claims entitled to exclusive pricing for specialty drugs were paid at the nonexclusive level. Medco has identified all Rx Collaborative clients affected, and payments will be made to all affected employers early in 2011.

“Overall, the review found that Medco has well-documented processes and procedures in the areas we evaluated.”

Operational Review

During 2010, the Towers Watson Rx Collaborative performed an operational review of Medco. The primary objectives of the review were to document Medco's effectiveness in providing a high level of service and to identify opportunities for process improvement and/or to streamline administration. The evaluation was an exercise in due diligence and consisted of the following activities:

- A review of Medco's official SAS 70 report on operational controls
- Interviews with key Medco operational and clinical leaders
- Completion of a questionnaire documenting operational procedures in key areas:
 - Retail network and network management
 - Mail service operations
 - Specialty prescriptions
 - Consumer-driven health plan capabilities
 - Member/customer service
 - Billing, invoicing and payment procedures
 - Clinical program administration
 - Claim administration
 - Implementation activities
 - Internet, data transfer and data security
 - Medicare Part D retiree drug subsidy support

Overall, the review found that Medco has well-documented processes and procedures in the areas we evaluated. However, members and clients encounter service issues periodically. We found that the root cause is often a result of failure to adhere to procedures or a miscommunication between senior leaders and customer service representatives.

Towers Watson interviewed Dawn Pagano, Medco VP and Chief Operating Officer for Employer Accounts, and Matt Gibbs, Chief Clinical Officer for Employer Accounts. Highlights of the standard administration processes include:

- A goal of Six Sigma accuracy and consistency, which includes processes that are easily repeatable and measurable
- The following attributes among employees: business with integrity, passion for customers, speed without compromise, ownership of actions, strength through teamwork and inspiring others to excel
- Reliance on subject matter experts for implementing processes using the following focus: define and confirm the intent, design operational parameters, test, communicate and validate in production

The Six Sigma approach applies to Medco's clinical area as well as to the goal of following consistent processes and using measurable outcomes. Medco maps the clinical team's areas of responsibility, assigns objective performance measures and assesses results. If rework is required, Medco provides coaching and measures performance based on the findings. Finally, Medco reviews performance metrics and sets goals to identify areas that require improvement.



Data Warehouse and Reporting Initiative

It is important for employers to be able to make pharmacy plan management decisions based on data-driven analysis. Towers Watson's approach to pharmacy management includes the maintenance of an independent data warehouse that can be used to verify PBM reporting and perform analysis that is aligned with the employer's best interest, not the PBM's.

One of the original strategic initiatives of the Rx Collaborative was the Data Warehouse, launched in 2005. By 2010, the RxC Data Warehouse had grown to include 89 companies resulting in combined claim experience for 1.66 million participants totaling \$1.8 billion in annual drug spend.

Employers participating in the RxC Data Warehouse receive custom reports on a quarterly basis that they can review with their Towers Watson pharmacy consultant to monitor cost and utilization in their pharmacy benefit plan. Executive summary reports are sent semiannually, and these include specific clinical recommendations.

In 2010, employers participating in the RxC Data Warehouse continued to receive custom benchmarks for the key metrics in quarterly reports. In *Figure 6*, key metrics and year-over-year trend values for the Rx Collaborative population are shown in aggregate.

Towers Watson uses the extensive data in the RxC Data Warehouse to perform analysis that Medco does not — and in some instances cannot — produce. Here is just one example:

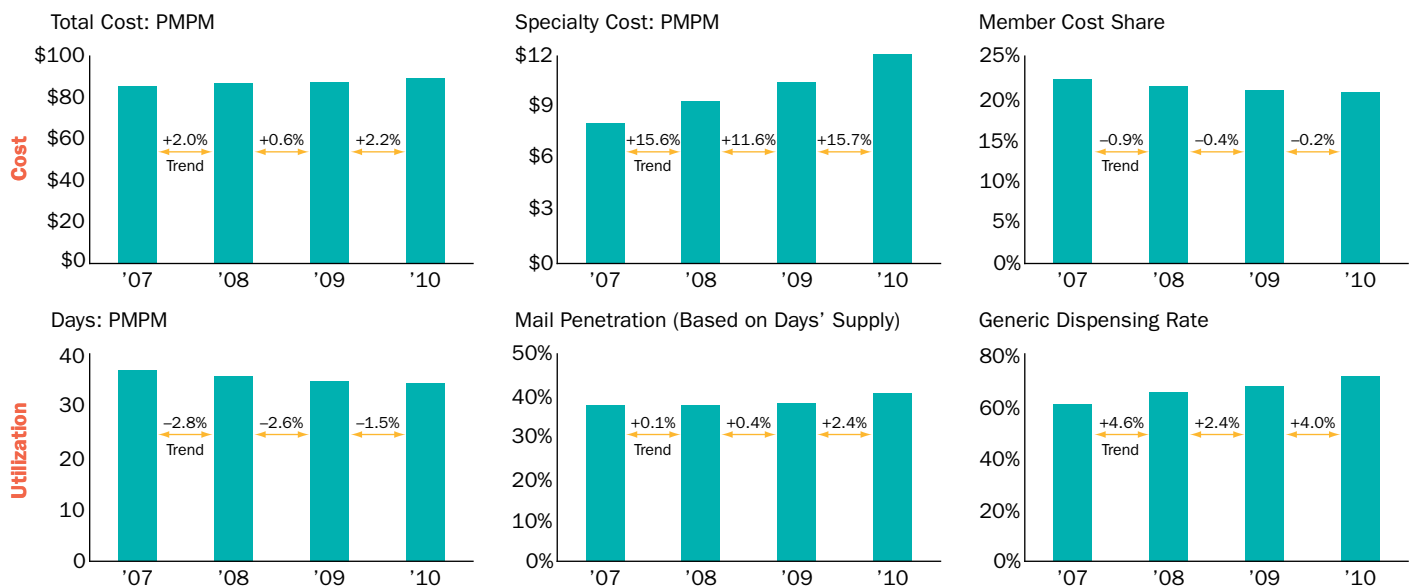
All employers are concerned about pharmacy drug trend, which may fluctuate for many reasons, including:

- Shifts in utilization, financial terms and membership
- New drug therapies introduced
- Changes in the drug mix — by channel, brand/generic
- Drug inflation (e.g., per-pill cost)

Based on companies for which we had complete data in 2009 and 2010, we calculated that, while 2010 overall cost trend (compared to 2009) was 3.8%, drug price inflation was 6.4%, and the combined contribution to trend from other factors was -2.6%. In other words, while trend increased, most of the increase was attributable to inflation, not other factors.

In mid-2010, plan sponsors using the RxC Data Warehouse received executive summary reports that included a custom exhibit showing the impact of drug price inflation on their cost trend.

Figure 6. RxC Data Warehouse trends



Source: RxC Data Warehouse
Trend for member cost share, mail penetration and generic dispensing rate are the difference between year two and year one rates. Trend for other metrics are based on the ratio of year two to year one.

2010 Rx Collaborative Annual Meeting

Redefining Pharmacy Management

The sixth annual Rx Collaborative employer meeting was held May 17–19, 2010, in Orlando, Florida. The meeting attendees included a record 59 clients, several Towers Watson consultants, representatives from Medco's executive sponsorship team and members of the Rx Collaborative core team. As always, it provided a unique forum for members to provide feedback and discuss pharmacy benefit management with their peers.

The theme of the meeting was “Redefining Pharmacy Management,” and sessions highlighted topics of interest to employers, for example:

- **For Members Only** showcased Towers Watson's efforts on behalf of the Rx Collaborative to redefine successful pharmacy management. Towers Watson negotiates and monitors the market-leading financial terms, provides a unique account management approach, performs group-level audit services and provides a comprehensive suite of services. The structure of the Rx Collaborative is unique in that it provides joint management of the pharmacy benefit by Medco and Towers Watson.
- **Health Care Reform** reviewed the changing legal landscape of medical and pharmacy benefit sponsorship and provided a list of issues for employers to consider over the next year and beyond.
- **Retiree Options in a New World** spotlighted recent changes in the retiree health care space.
- **Pharmacy in Focus** presented an overview of topics of interest to our employers:
 - Specialty drug spend and how to manage it
 - Low-cost generics
 - Towers Watson's new Custom Care Management Units
 - Personalized medicine
 - Value-based plan designs
 - Consumerism
 - Canadian Rx Collaborative
- **OTC Considerations** discussed how to educate employees on drug alternatives and consumer choice.
- **Towers Watson Reference Formulary** presented a case study of how South Shore Hospital implemented the formulary and experienced impressive first-year results.
- **Overview of Medco's Therapeutic Resource Centers** included Towers Watson's point of view.
- **Meet the Medco Executives** offered attendees the chance to ask questions and gain insights from Kenny Klepper, Medco's President and Chief Operating Officer; Dawn Pagano, Vice President and Chief Operating Officer of Employer Accounts; Mike Romanzo, President of Medco's Systemed Group; and Tim Wentworth, Group President of Employer Accounts.

The meeting included several feedback sessions where employers could discuss the presentation topics with each other and Towers Watson consultants. The annual meeting continues to be one of our most important communication vehicles and the best way to convey pharmacy intellectual capital to Rx Collaborative members.

At the close of the conference, we surveyed attendees on overall content and experience. This year's meeting was rated highly by attendees: 4.2 on a scale of one (poor) to five (excellent).

“The meeting included several feedback sessions where employers could discuss the presentation topics with each other and Towers Watson consultants.”



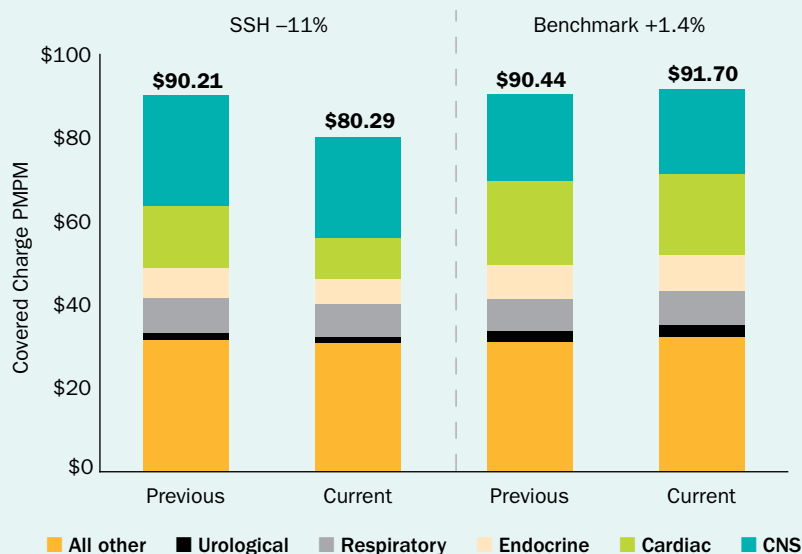
South Shore Hospital: A Year of Impressive Results

South Shore Hospital has been an Rx Collaborative employer since 2004. It is the largest independently operated hospital in southeastern Massachusetts and employs 3,800 people. Over the last several years, cost trend became a concern and, due to the economic downturn, there was pressure to control overall health costs. Working with their Towers Watson pharmacy consultant, South Shore developed an approach designed to meet several objectives:

- Address pharmacy trend.
- Develop a contemporary yet uncomplicated pharmacy benefit design.
- Enhance the value of generics.
- Align retail and mail-order member share while maintaining mail incentives.
- Employ selected utilization management programs to increase efficiency, reduce waste and lower trend.
- Educate employees about opportunities, challenges and solutions.

This approach would be accomplished in three stages: 1) update the plan design, 2) adopt a generic-focused formulary, and 3) develop and execute an employee communication campaign.

Figure 7. Drug spend February 2009 through January 2010 compared to the previous year



Source: RxC Data Warehouse

Completing the second phase included implementation of the Towers Watson Reference Formulary in February 2009, along with targeted utilization management programs. Targeted therapeutic chapters included CNS, endocrine, urological agents, cardiovascular and respiratory. Results for South Shore Hospital were impressive, including an increase in Generic Dispensing Rate over time. As a result of all changes, drug spend for South Shore Hospital decreased by 11% in the year starting Feb. 1, 2009, compared to the year starting Feb. 1, 2008. The RxC Data Warehouse benchmark increased 1.4% over the same period.

Employer

Communications

Quarterly Calls

The Rx Collaborative Quarterly Calls continue to be well attended by employers. (We averaged 30 members per call in 2010.) The calls provide a forum through which to share operational updates, benchmarking and analysis from the RxC Data Warehouse, and intellectual capital from Towers Watson's pharmacy consulting practice. During these calls, employers are given the opportunity to ask questions and provide feedback.

During 2010, plan sponsors joined the calls to hear updates on the results of the RFP, the negotiations with Medco and the improvement of contract terms. Operational updates focused on highlights from the Annual Employer Meeting and the results of our three group audits — rebates, claims and operations. In addition, employers heard Towers Watson experts speak about health care reform and what it means to employers. Towers Watson pharmacy consultants joined the call to give clinical updates and generic pipeline management.

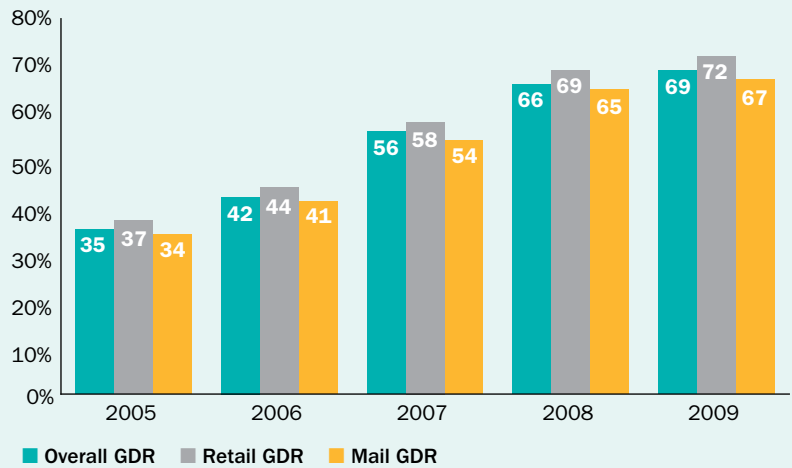
“Towers [Watson] is the backbone of the arrangement. Medco has a great product, and Towers [Watson] ensures consistent delivery of that product.”

— Carol Taylor, Bristow Group

Using Data to Improve Perspective

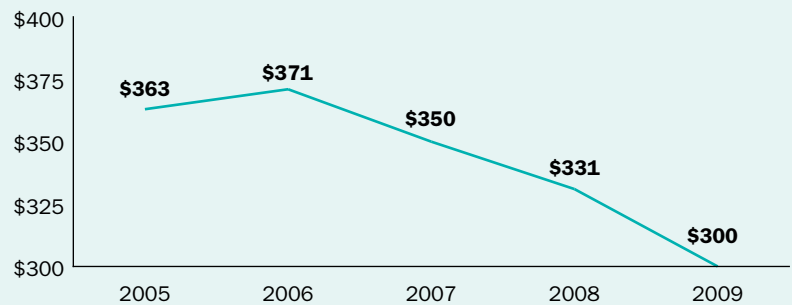
Towers Watson pharmacy consultants access the Rx Collaborative Data Warehouse to perform analyses that put current trends and drug pipeline changes in perspective. During the March 9, 2010 quarterly call, we focused on a select group of therapeutic classes: cholesterol reducers, antihypertensives, ulcer medications, antidepressants, men's health and allergy medications. We reviewed historical generic dispensing rates and trends, comparing 2005 to 2009. While the generic dispensing rate is only one of many components that affect drug spend, this analysis does highlight the relationship between generic utilization and drug spend.

Figure 8. Generic dispensing rates



Source: RxC Data Warehouse

Figure 9. Covered charges per member/year



Source: RxC Data Warehouse

Findings on the select therapeutic classes include: While utilization overall did not change significantly over the time period, GDR virtually doubled — from 35% to 69% — and cost PMPY decreased 17%.

Employer Survey

Each year, the Rx Collaborative core team solicits feedback on the services and value the Rx Collaborative provides. We use this critical feedback to enhance our service and direct our future focus. In 2010, we had a record 23% response rate from our employers.

Results of the 2010 employer survey include:

- Clients most value the transparent pricing of the Rx Collaborative arrangement, the robust audit services, and our clinical management and plan design review.
- Clients are most interested in the integration of pharmacy and medical data as a focus for 2010, an interest that has continued to increase each year since 2008.
- Rx Collaborative members are also focusing on legal issues relating to health care, clinical management and generic optimization in 2011.
- 94% of the Rx Collaborative members that responded and participate in the RxC Data Warehouse rated the information in the reports either extremely or somewhat useful.
- 79% of respondents said Medco provided either a very high or high level of service.
- 93% of respondents said their joint Towers Watson–Medco client team provided either a very high or a high level of service.

E-Newsletters

Each month, Rx Collaborative members receive our e-newsletter featuring specially selected articles that bring employers the latest news related to prescription drug trend as well as implications for employer health benefit programs.

Additionally, the Towers Watson Pharmacy Practice contributes commentary on hot topics and pharmacy-related issues. This past year, we published articles related to:

- Warfarin reference formulary status and utilization management
- Utilization management opportunity: Respiratory syncytial virus (RSV) agents
- Insomnia: Are sleeping pills always the answer?
- The generic pipeline: A focus on the high blood pressure therapeutic category Angiotensin II receptor blockers
- Prolia, a new osteoporosis treatment and a cost management opportunity for the class
- Mental health parity legislation 2010 update and pharmacy management considerations
- Managing utilization of diabetes medications

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About Towers Watson

Towers Watson is a leading global professional services company that helps organizations improve performance through effective people, risk and financial management. With 14,000 associates around the world, we offer solutions in the areas of employee benefits, talent management, rewards, and risk and capital management.

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