

Guaranteed Net Cost

A Pharmacy Benefit Pricing Model Focused on Net Plan Cost

The Guaranteed Net Cost model, developed by CVS Health, offers plan sponsors cost predictability by simplifying the pharmacy benefit pricing model, and more closely aligning our incentives with clients' objective — net drug cost. The model moves away from a focus on components such as discounts and rebate guarantees, and toward a more holistic approach that enables plan sponsors to clearly see the net cost of drugs, and select their pharmacy benefit manager (PBM) based on who can ultimately deliver the lowest net cost.

A Guaranteed Net Cost Model:

- ✓ Guarantees net spend after rebates for each distribution channel
- ✓ Provides plan sponsors predictability for net plan costs
- ✓ Eliminates the need for plan sponsors to project average wholesale price inflation and changes to drug mix, and the impact on their plan

Table of Contents

| | |
|--|----------|
| General Overview | 2 |
| Pricing | 5 |
| Plan Sponsor/Marketplace Adoption | 7 |
| Plan Design | 8 |

General Overview

1 Why are you proposing a new economic model?

The pharmacy benefit industry is going through one of the most dynamic periods in our nation's history. CVS Health's approach, in order to continue to deliver strong cost control — while also optimizing the quality of care — needs to continue to evolve with market dynamics. As we look to how we can help plan sponsors not only respond to, but stay ahead of, changing trends, we developed a model that is both simpler and provides cost predictability.

The complexity of current models impedes direct comparison because formulary strategies, minimum rebate guarantees, and which claims are excluded from such guarantees, can all vary among PBMs. This can obscure the actual value a PBM delivers in terms of cost control strategies through effective formulary design and utilization management (UM) programs.

Current models don't adapt effectively to changing market dynamics — such as lower list prices. For all these reasons, the time is right for a new approach, one that better aligns PBM incentives with clients' objectives.

2 What motivated this change?

We believe the time is right for change. CVS Health's goal with the Guaranteed Net Cost model is to refocus attention on net plan costs and provide plan sponsors predictability. The Guaranteed Net Cost model simplifies the financial arrangement, better aligns PBM incentives with clients' objectives, and enables us to deliver greater value to plan sponsors through strong cost control strategies that help payors drive savings.

3 What is the Guaranteed Net Cost model?

The Guaranteed Net Cost model, developed by CVS Health, guarantees average net spend per prescription after discounts and rebates for each distribution channel. It provides plan sponsors cost predictability and better aligns PBM incentives with our clients' objectives.

CVS Health's new Guaranteed Net Cost pricing model focuses on a simple concept — net cost per claim. It enables plan sponsors to easily determine which PBM offers them the greatest value as measured by effective cost control through management of the drug mix. It also enables plan sponsors to make plan decisions based on the impact to overall net costs for the pharmacy benefit. Under the new model, the PBM will pass through 100 percent of the rebates, and take accountability for the impact of average wholesale price (AWP) inflation and shifts in drug mix. It eliminates the need for payors and consultants to project drug price inflation, or estimate shifts in drug mix.

4 How is this model different from existing financial models in the market?

CVS Health's goal with the Guaranteed Net Cost model is to refocus attention on net drug costs and provide plan sponsors predictability.

CVS Health's new Guaranteed Net Cost pricing model focuses on a simple concept — net cost per claim. It guarantees average net spend per prescription after discounts and rebates for each distribution channel. Under the new model, the PBM will pass through 100 percent of the rebates to the plan sponsor, and take accountability for the impact of AWP inflation and shifts in drug mix. It provides plan sponsors cost predictability and better aligns PBM incentives with our clients' objectives.

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What is the value add to plan sponsors and/or consultants?

By using a Guaranteed Net Cost model plan sponsors can easily determine which PBM offers them the greatest value as measured by cost control through effective management of the drug mix. The model also enables plan sponsors to make plan design decisions based on the impact to overall net costs for the pharmacy benefit.

Features and benefits of the Guaranteed Net Cost model include:

- ✓ Alignment of incentives with plan sponsor objectives — guarantees average net spend, after rebates, per 30 days supply, across each distribution channel
- ✓ Simplifies financial arrangement — enables plan sponsors to focus on net cost after rebate considerations
- ✓ Provides cost predictability — Provides net cost guarantees, eliminating the need for plan sponsors and consultants to project AWP inflation, shifts in drug mix and the total value of rebates
- ✓ 100 percent of the rebates are passed through to the plan sponsor in the manner they choose (quarterly retrospective distribution or rebates at point of sale (POS) by National Drug Code (NDC) so plan members can see the true net cost of drugs)
- ✓ The PBM takes accountability for the impact of AWP inflation and drug mix

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Will this model apply to only commercial plan sponsors?

CVS Health's initial focus is employer plan sponsors, but we plan to discuss this approach with any plan sponsors who express an interest.

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What is the structure of the Guaranteed Net Cost proposal? Will you still have minimum rebate guarantees? Who receives the rebates in this new model? What happens to rebate guarantees to plan sponsors?

Under the new model, the PBM will pass through 100 percent of the rebates to plan sponsors in the manner they choose (quarterly retrospective distribution, or rebates at point of sale (POS) so members can see the true net cost of drugs). The PBM also takes accountability for the impact of AWP inflation and drug mix. There are no minimum rebate guarantees, but the overall rebate value is accounted for in the net cost guarantees which will be aggregated by channel.

8

ESI just came out with a new PBM payment model. How is what you are proposing better/different?

The Guaranteed Net Cost model guarantees average net spend, after rebates, per 30 days supply across the distribution channel, enabling plan sponsors to see the net cost of their pharmacy benefit, and offering cost predictability. Under the new model, 100 percent of the rebates will be passed on to plan sponsors. This provides cost predictability and eliminates the need for plan sponsors and consultants to project AWP inflation and drug mix. It applies to all therapy classes and no electronically processed point-of-sale claims are excluded from the guarantee.

9 **Pharmaceutical manufacturers are claiming that the clamor by you and ESI to come up with a new pricing model is evidence that PBMs have been the problem with high-cost drugs all along because of your convoluted contracting practices. How do you reply to that?**

Pharmaceutical manufacturers — and no one else — set drug prices. In recent years, this has led to ever-increasing launch prices, and double-digit price increases from one year to the next. As a PBM, our job has always been to help our clients manage costs in the face of these escalating prices, without compromising clinical care, so they can continue to provide an affordable benefit to their members. The Guaranteed Net Cost model refocuses on net plan costs, better aligns PBM incentives with plan sponsor objectives, reduces complexity, and offers plan sponsors cost predictability.

10 **How would the Guaranteed Net Cost model need to be adjusted if the Administration passes legislation completely removing rebates?**

The Guaranteed Net Cost model is focused on net plan costs. Given that, it positions CVS Health well to help plan sponsors control net plan costs even if state or federal legislation or regulation was to be passed eliminating manufacturer rebates. Whether rebates are eliminated, replaced by a different discount mechanism, or lawmakers simply require manufacturers to lower list prices, the model will still be able to provide plan sponsors with a predictable net cost. Under the new model, 100 percent of rebates would be passed on to plan sponsors, as long as the rebate mechanism exists. This pricing model is durable and can adapt to market trends — whether there are high list prices and high rebates or low list prices and no rebates.

11 **Will the net cost guarantees be auditable?**

Yes. Plan sponsors will be able to continue to perform standard annual rebate audits, as they do today. In addition, they will also receive standard annual financial audits that allow them to verify net costs instead of calculating individual drug AWP discounts.

12 **How will CVS Caremark define “rebates” under the Guaranteed Net Cost model?**

Under the Guaranteed Net Cost model, 100 percent of the rebates will be passed on to the plan sponsor. We define rebates as being inclusive of price protection and manufacturer administrative fees. Our contracts define “rebates” as formulary rebates — which may include base, market share, and price protection rebates we collect in our capacity as a group purchasing organization (GPO) on behalf of the plan — that are attributable to the utilization of covered drugs by members.

13 **How will CVS Health make money under the new model?**

In the Guaranteed Net Cost model with a traditional network, PBM margin comes from the difference between the drug cost to the client/member and the pharmacy, and includes mail and specialty margin.

14 Is CVS Health looking at a model without rebates? With an alternate NDC or other?

The Guaranteed Net Cost model is focused on net plan costs. Given that, it positions us well to help plan sponsors control net plan costs even if state or federal legislation or regulation was to be passed eliminating manufacturer rebates. Whether rebates are eliminated, replaced by a different discount mechanism, or lawmakers/the Administration simply require manufacturers to lower list prices, the model will still be able to provide plan sponsors a predictable net cost. Under the new model, 100 percent of rebates would be passed on to plan sponsors, as long as the rebate mechanism exists. This pricing model is durable and can adapt to market trends — whether there are high list prices and high rebates or low list prices and no rebates.

15 What kind of reporting will be available?

Clients will continue to receive actual claims data, which show drug cost, and quarterly rebate reports. New reports will be available to show how the two together are combined to calculate the net cost, which can be tracked on a monthly or quarterly basis.

Pricing

16 How does this new economic model address concerns regarding drug price transparency?

The Guaranteed Net Cost model guarantees average net spend, after rebates, per script across the distribution channel. Under the new model, the PBM will pass through 100 percent of the rebates to plan sponsors, and take accountability for the impact of AWP inflation and shifts in drug mix. Net cost guarantees are calculated using plan utilization, expected rebate value, and applying projected AWP inflation and expected drug mix shift. It is a move away from the current focus on components such as discounts and rebate guarantees in order to impact the cost of pharmacy benefit and toward a more holistic approach that enables plan sponsors and consultants to clearly see the net cost of their pharmacy benefit.

17 Will this model be in addition to/on top of your current pricing guarantees?

The Guaranteed Net Cost replaces any discount, dispense fee, and rebate guarantees.

18 How is the guaranteed net cost calculated? How will it be impacted by drug price inflation during the year and the introduction of new brand and/or generic drugs?

Net cost guarantees are calculated using plan utilization, expected total rebate value, and applying projected AWP inflation and expected shifts in drug mix, including anticipated new drug launches. The net cost guarantee is normalized for a 30-day supply and no point-of-sale claims are excluded. The PBM takes on accountability for total AWP inflation, and shifts in drug mix. The PBM also passes on 100 percent of rebates to plan sponsors. This simplifies the financial arrangement and enables plan sponsors to focus on net cost.

19 Will the Guaranteed Net Cost model include three-year guarantees?

Net cost guarantees will be offered for each distribution channel for all three years of a standard contract with individual guarantees for each year. The net cost guarantee will be evaluated annually for potential adjustment in case of unexpected market trends. The net cost guarantee can also be adjusted if plan sponsors implement additional cost-control strategies that may help lower overall net plan costs.

20 Will you quote on a reverse cost basis, where we give you a target guarantee \$\$\$ amount by channel and you tell us what the plan design, formulary, and programs will be?

We work closely with plan sponsors to understand their goals for their pharmacy benefit plan and plan members. The Guaranteed Net Cost model can help deliver higher savings and lower plan costs depending on plan sponsors' willingness to adopt key cost management tools, and we can make recommendations on what plan design and programs can help them meet their plan cost targets.

21 Does the Guaranteed Net Cost model assume a pass through of retail network discounts or traditional (spread) network discounts?

Plan sponsors can select from two versions of the Guaranteed Net Cost model — traditional or pass through (transparent). For transparent, or pass-through, contracts there will be an administrative fee and performance sharing in the guarantee results. There will not be an administrative fee for traditional contracts nor a share in the guarantee results.

22 What information is necessary for your pricing underwriters to achieve a high degree of confidence?

The data requirements provided during the request for proposal (RFP) process will be used to calculate the net cost guarantees.

23 If the actual cost comes in below the guaranteed cost, will plan sponsors still pay the guaranteed cost, allowing CVS Health to retain the difference as incremental revenue?

It depends on what network arrangement plan sponsors choose for their pharmacy benefit plan. For plans with a traditional network, plan sponsors would retain any difference between the guarantee and actual performance below the guarantee. Plans that are based on a transparent network would include a component of sharing in the performance.

24 Will you share an estimate with plan sponsors of what the rebate component of the net cost guarantee is?

Upon request, CVS Health can provide a total rebate estimate.

25 Is there an administrative fee with this structure?

There are no base administrative fees if the Guaranteed Net Cost model is implemented using a traditional retail network. Additional fees may apply for the implementation of optional programs.

26 Under this new model, would there be any sort of annual reconciliation?

Net cost guarantees are reconciled annually including the full value of 100 percent pass through of rebates to plan sponsors.

Plan Sponsor/Marketplace Adoption

27 Are you planning to incorporate this new model into your responses to all new RFPs moving forward?

CVS Health will include the Guaranteed Net Cost model in our RFP responses when requested by plan sponsors or consultants.

28 How many plan sponsors do you expect to adopt this approach?

CVS Health believes in alignment with our clients' objectives. We are confident this is the right thing to do, the right approach for the future, and are confident that plan sponsors will agree with us and want to adopt this model. Clients, prospects and consultants have already expressed a strong interest in the Guaranteed Net Cost model and we are currently working on several Guaranteed Net Cost pricing proposals. We have two clients implementing the new model in early 2019 and expect more to move into this model in 2020.

29 Do you expect this new model to be competitive in the marketplace?

Yes, CVS Health expects the Guaranteed Net Cost model to be very competitive. The model shows plan sponsors the true value of a PBM in managing drug cost and drug mix, which we expect plan sponsors will welcome. The Guaranteed Net Cost model simplifies the financial arrangement and refocuses attention on the net plan cost. This is the right approach for a rapidly evolving pharmacy benefit landscape. Even though some manufacturers have recently lowered the list prices for some drugs, this practice has only been true for a select few drugs and the pharmaceutical market still includes a large number of very expensive drugs, with high list prices. The Guaranteed Net Cost model focuses on a simple concept — the net cost of a drug. It provides cost predictability and eliminates the need for plan sponsors and consultants to project AWP inflation and drug mix.

30 What if no other PBM adopts this model? Will you continue to offer it? Why do you think other PBMs would adopt it?

CVS Health believes guaranteeing net cost is in the best interest of plan sponsors and we are confident plan sponsors and consultants will also see it that way. We think this model is the right choice for any PBM that wants to demonstrate the value of its cost-control strategies and alignment with plan sponsors' objectives.

31 Will CVS Health propose both traditional proposals and Guaranteed Net Cost proposals if requested?

Yes. CVS Health believes in alignment with our clients. We are confident this is the right approach for the future and that plan sponsors will agree with us and want to adopt this model. We encourage you to have a conversation with your clients and explain the features and benefits of the Guaranteed Net Cost model, prior to their releasing a request for proposals.

32 What is the floor limit for the number of members or annual drug spend that you will quote for this arrangement?

There is no minimum lives or minimum annual pharmacy benefit spend threshold for CVS Health to discuss.

Plan Design

33 How do claims adjudicate at the point of sale?

Claims will still be adjudicated at industry-competitive discounts, with separate discounts for brands and generics, to approximate relative differences in drug cost. This minimizes member disruption from plan sponsors choosing to move to a new pricing model. In addition, plan sponsors' existing plan design copay structure would apply.

34 Will there be a formulary specifically aligned to the Guaranteed Net Cost model? What about plan sponsors that choose to opt out of the formulary or align with a custom formulary?

CVS Health is developing a new formulary that will continue to promote lower-cost generic alternatives, while allowing coverage for single-source brand drugs. Plan sponsors that align with the new formulary will be able to derive the greatest benefit from the Guaranteed Net Cost model. We firmly believe that the formulary we are developing to align with the Guaranteed Net Cost model will strike the right balance between cost control and minimizing member disruption.

35 Will you no longer have drug exclusions in your formulary?

We will continue to utilize our industry-leading formulary strategies — including drug exclusions — to help plan sponsors control cost.

36 Does the Guaranteed Net Cost model incorporate exclusions from pricing guarantees? Please list out all exclusions and caveats.

The Guaranteed Net Cost model does not propose to exclude any drug classes or electronically processed covered point-of-sale claims from the guarantees and we hope the industry will follow our lead. We are currently working on a contract template for the Guaranteed Net Cost model and expect to be able to share that with plan sponsors in January 2019.

37 How will you adjust the net cost guarantee if clients implement a UM edit or remove a drug?

Any program plan sponsors choose to implement to help control utilization or encourage use of lower-cost therapeutic alternatives will potentially impact their plan cost. The net cost guarantee can also be adjusted if the client implements additional cost-control strategies that may help lower overall net costs, so that the impact of such an implementation is captured in the net cost calculation.

38 **Is the net cost guarantee offer contingent upon clients adopting or implementing any plan design changes, clinical programs and UM edits (prior authorization, step therapy, or quantity limits)?**

The Guaranteed Net Cost model is the right choice for plan sponsors who want to control costs and choose to align with one of our standard formularies and UM strategies to drive low net cost. In addition, adoption of our recommended formulary and UM programs that drive to a low net cost will help ensure the most competitive net cost guarantee.

39 **Why do you have a requirement that plan designs must stay consistent year over year? What happens if the plan needs to make a plan design change mid-year?**

As always, plan sponsors have the ability to make plan design changes at any time. However, plan design influences the utilization of drugs based on preferential placement for lower-cost alternatives. Some plan designs steer toward lower-cost alternatives more efficiently. Changes in plan design from year to year that may affect members' drug choices need to be equitably accounted for in the evaluation of the Guaranteed Net Cost model offering because it can affect a plan's overall cost. Therefore, we will review how any changes impact the net cost guarantee.

40 **Will shifts in mix impact the guarantee within a plan year?**

CVS Health assumes the risk for mix changes in the net cost guarantee. A reservation of rights will be included in the contract that will cover major changes in the marketplace that are not in CVS Health's control.