

**EMPLOYEE BENEFIT  
Adviser**<http://eba.benefitnews.com>[« Back to Article](#)

## A prescription for better comp

By Molly Bernhart

May 1, 2008

No strangers to the inside of a courtroom, it looks like benefit brokers and their PBM cohorts may be heading back before the judge unless they make some changes to the way they move employer and employee money around. The DOL's ready to act and the regulator can't be too quick or severe for people like Linda Cahn.

Linda Cahn may be a consultant, but she's not your typical intermediary between PBMs and employers.

The attorney and president of Morristown, N.J.-based Pharmacy Benefit Consultants made it her mission to clarify the complicated fee and service structure of PBMs and pharmacy benefit brokers. She has done this through litigation and by example with her consulting firm, where her clients - employers - pay her directly.

"The consulting firm should not be in a position where its own financial interests are not squarely aligned with the plan's interests, particularly because the plan trustees have a fiduciary obligation to act solely and exclusively in the interests of the plan," says Cahn.

Benefit broker compensation breeds questions of objectivity. For many critics of the industry, the typical benefits broker has too many bosses - too many people writing it checks.

Employers often ignore confusing and questionable compensation structures because they are either too busy to care or the convoluted payment plan is actually the cheaper plan. Both lines of thinking can lead to a fiduciary breach.

David Kikumoto, president and CEO of Denver Management Advisors says fiduciaries typically do not understand PBM contracts, which means they don't know how the money flows.

"The fiduciary should know what they're paying in pharmacy costs, administrative fees and whether or not the [broker] is receiving or obtaining consulting fees that aren't disclosed ... unless that's totally transparent it creates an environment where there could be biased decision making," says Kikumoto.

## **Other People's Money**

A best practice is finally emerging. Any money an adviser receives for servicing an employer should be disclosed. Disclosure may not be required, but it is increasingly justified given heightened interest on the part of DOL, Cahn and others out to expose the industry's misdeeds.

It is standard industry practice for advisers to accept undisclosed commissions - both flat and per-prescription - as an incentive to reward PBMs with employer business.

"Conflicts [of interest] remain rampant in the consulting industry," says Cahn. "In fact, only a few weeks ago, my firm received a call from a PBM offering to pay my firm as much as three dollars a prescription if my firm would only bring business to the PBM that had contacted us."

For many, such practices are abusive and will continue to drive regulatory and legal interest. Disclosure remains the lone source of salvation for advisers looking to stay above the fray.

"If a brokerage relationship is not disclosed to an employee benefit plan retaining a consulting firm to conduct a PBM RFP, clearly there is a conflict of interest. The plan thinks the consulting firm is conducting an independent evaluation of all PBM contestants, when in fact, the consulting firm has a financial interest in ensuring that a particular PBM wins the RFP," says Cahn.

But not all disclosure statements are equal.

"The first distinction that should be made is between a firm that is acting as a consulting firm and a firm that is acting as a broker. There's a big difference," says Cahn.

"Any employee benefit plan that is retaining an entity to serve as an adviser ought to know right out of the box whether the adviser has ever served as a broker for any PBM. If it has, it's already aligned its interests with a PBM and cannot represent the health plan's interests properly."

And if advisers think they are in the clear because they work as a broker for multiple PBMs, guess again. If one PBM is offering \$3 per-prescription for the business, a second is offering \$2 per-prescription for the business and a third is offering \$1 per-prescription for the business, the bias still exists.

The goal for employers, according to experts, is to get a PBM contract that squeezes as much of the cost out as possible and offers the most transparency.

Do brokers have the same goal? Not every adviser is so eager to watch his commission revenue shrink due to disclosure.

More legal and regulatory action is unsurprising, especially given that some say an adviser's failure to properly

disclose his compensation ultimately jeopardizes the employer's fiduciary status under ERISA.

"It seems to me that there's a fiduciary responsibility to understand how parties in interest to a plan are compensated," says Marcia Wagner, president of Boston's Wagner Law Group. Wagner adds that there has been some litigation in this area, but for the most part the cases have been settled in the early stages.

A recently proposed Department of Labor regulation is looking closely at how advisers are handling fees and commissions, and would apply to PBM contracts.

"Regardless of whether the Department of Labor adopts its proposed regs, health plans should use the DOL regs as guideposts. The regs clearly explain the importance of eliminating all conflicts of interest, and the regs set forth all of the disclosures that should be obtained to do so," says Cahn.

Employers are going to get better disclosure statements one way or the other, experts say. Either the DOL is going to force the issue, or progressive advisers are going to begin offering detailed and comprehensive materials for the benefit of their firms and their employer clients. For example, Cahn's Website offers employers and advisers a free download of her conflict of interest disclosure form for their own use.

### **Making Something Out Of Nothing**

Not everyone is convinced that the industry is in crisis over PBM compensation practices. Some experts argue that the issue is overblown and that many advisers make their revenue streams crystal clear.

John Jones, senior VP of professional practice and pharmacy policy at Prescriptions Solutions, says there are more people acting as consultants (being paid by their client) than as brokers (being paid by commission) with his company at this time.

"Nevertheless, we have the relationship with [both brokers and consultants]. Many of the consultants are pharmacists who have worked in managed care - who have worked for PBMs or health plans and have gone on to their own consulting businesses," says Jones.

#### **DOL says: Show Me The Money**

The Department of Labor's proposed rule on reasonable contracts or arrangements under Section 408(b)(2) has many industry players nervous. After two days of testimony on the proposed regulations, the Employee Benefits Security Administration concluded hearings on April 1.

At the time this issue went to print there had been no further action

announced by the DOL. There is much advisers can learn from the content of the rule and the industry's reaction to help them prepare for future legislation.

### **What is 408(b)(2)?**

The proposed regulation seeks to clarify a Section 404(a)(1) of ERISA, which requires plan sponsors not only to act solely in the interest of plan members when choosing a service provider, but to make sure it involves a "reasonable contract or arrangement."

In the past, a plan only needed to have the option to be terminated without penalty on reasonably short notice in order to be considered "reasonable." This reg would clarify the meaning of "reasonable" contracts and arrangements in two other distinct areas: disclosure concerning compensation and services, and disclosure concerning conflicts of interest.

### **Why did the DOL want the clarification?**

The DOL says that fee structures for benefit service providers - brokers, consultants, health insurance companies, PBMs, TPAs, retirement plan providers, to name a few - have become increasingly difficult for employers to decipher. This makes it more difficult for plan sponsors to discern who exactly is being paid for what, potential conflicts of interest and the quality of the services rendered. Because fiduciaries are unable to understand fee structures, they are choosing service providers in a way that breaches their fiduciary duty.

### **What would it require?**

If approved, the regulation would require service providers to disclose all compensation it will receive, directly or indirectly, and any conflicts of interest that may arise in connection with its services to the plan. Indirect compensation includes fees that service providers receive from parties other than the plan, the plan sponsor or the service provider.

Compensation is broadly defined as money and any other thing of

monetary value received by the service provider or its affiliate in connection with the services provided to the plan; for example: gifts, awards, trips, research, finder's fees, placement fees, commissions, soft dollar payments, float income and fees based upon a percentage of the plan's assets.

If a service provider cannot provide the employer with the specific monetary amount, he may use a formula; for example, explaining a fee per prescription arrangement.

The service provider would be required to describe any material financial, referral or other relationship it has with various parties that causes or may cause a conflict of interest. It is possible that service providers have policies to manage these real or potential conflicts and the DOL encourages providers to disclose details of those procedures to plan sponsors as well.

#### **Testimony is telling**

The Pharmaceutical Care Management Association testified at the 408(b)(2) hearing. Speaking on behalf of the group was William J. Kilberg of Express Scripts who argued that the proposed regulations should not be applied to employee health and welfare benefit plans, specifically PBM contracts.

Wellpoint has also commented on the regulation in a letter to the DOL's Kristen Zarenko that strongly urges the department to withdraw the proposed rule as to health and welfare benefit plans. The company argued that the rule would have an anticompetitive effect on the industry, especially due to the fee disclosure requirement for PBMs.

"By requiring disclosure of rebates and other manufacturer payments to PBMs, the proposed rule will require PBMs to disclose their cost structure to benefit plans, and in all likelihood, to their benefit consultants also. The more broadly internal and proprietary information on PBM cost structures is disseminated, the more likely that information will become known to competitors in the PBM

industry. Knowledge of competitors' cost structures diminishes incentives for PBMs to bid aggressively and fosters tacit collusion. This will likely lead to higher drug costs for benefit plans and for the consumers who participate in them," Stephen Northrup, VP of federal affairs for Wellpoint, wrote in his letter.

---

[About Us](#) | [Contact Us](#) | [Privacy Policy](#) | [Site Map](#)

© 2008 Employee Benefit News and SourceMedia, Inc. All rights reserved.

SourceMedia is an [Investcorp](#) company.

Use, duplication, or sale of this service, or data contained herein, is strictly prohibited.

