Wait, what’s a PBM (and how do they work)?

Dan: Hey there. You may have seen ads recently about access to drugs. Here's one that starts with a woman trying to fill a prescription, but the pharmacist says,

Pharmacist: I'm sorry, this medicine isn't covered by your insurance.

PBM: Yeah,

Dan: This guy in a blue suit comes up from behind. The patient grabs her prescription slip.

PBM: I decide which medicines you can get.

Patient: Wait, you're not my doctor.

PBM: That's right, I'm your insurance company's pharmacy benefit manager, or PBM. And, I don't make as much money off this one.

Dan: You might wonder, wait, what's a PBM exactly? And also, why am I seeing this ad now?

And who's paying for this ad? So PBMs are middleman companies that have a lot to do with which drugs we get access to, how much we pay for them, and yeah, they're sharks. And, these ads are out there because Congress knows we're all mad about drug prices and access to drugs, and they're eager to be seen doing something about it.

And those ads are paid for by pharmaceutical makers. Also sharks in direct competition with PBMs for the gazillions of dollars we spend on drugs as a country. PBMs and their role are a little more complicated, so we are bringing back an episode from this show's very early days. When we get to the end, I'll have some updates, things I've learned since then.

Meanwhile, here's me four years ago, starting to figure out how all this works.

So at the beginning of the year, my family switched to a new health insurance plan and I've got this prescription I take. I get three months worth of it at a time, and in February it was time to renew. The drugstore texted me they had it. I called to check, got the robot voice.

Robot: There's one prescription here for Daniel

Dan: And some news.

Robot: The out-of-pocket cost is $720.69. And that's ready for pickup.

Dan: I was like, what? This is an old-time generic drug. I'm used to paying like 15 bucks.

Robot: Would you like me to repeat that?

Dan: I was like, maybe you better. I want this on tape.

Robot: The out-of-pocket cost is 700.

Dan: I was also like, yeah, I'm just gonna bring my new insurance card over to the drugstore and hope that clears things up.

And it did. The copay was $0. That is some good new insurance right there. And as I walked outta the drug store, I was like, What was that all about? I pulled up a site called GoodRx on my phone. A doctor friend of mine sometimes recommends it to people whose prescriptions cost a lot, and what I found there was weird.

I punched in the name of the medication and my zip code and it showed me prices from a bunch of different places. Drugstore chains like CVS and Walgreens, big box stores like Costco and Walmart, local supermarkets with pharmacy counters. And the spread was crazy. 25 bucks at Costco, 170 at the supermarket, 300-some at CVS, and more than 700 at my drugstore, Walgreens.

And that was just the first set of prices. There were actually two. The first what you'd pay if you just walked in, the second was what you'd pay at each place if you brought in a digital coupon from GoodRx. And with the coupons, another crazy spread, a bunch of $20 options. But 75 bucks at CVS, 195 at Walgreens.

And this was just super, super weird, and it meant I was gonna have to do something I'd been honestly kind of dreading. Figuring out prescription drug prices. I'd done some reading about it before and it always made my eyes glaze over. I was like, ah, no. Too complicated. Let me come back to this, like in some other lifetime.

But this was too weird not to investigate. Because I was used to seeing stories about high drug prices. I figured we all knew that, but I wasn't used to seeing stories about random prices. That was new. Better get on that. This is An Arm and a Leg, a show about the cost of health care. I'm Dan Weissmann.

And I did some reading and eventually I figured out how to maybe explain this to myself without getting totally lost.

And I ended up running this explanation by some experts and they all said, that is not the most idiotic explanation. So here goes. It starts with the old movie. It's a Wonderful Life. Right at the beginning of the movie, the Jimmy Stewart character, George Bailey, is a 12-year-old kid working in the drugstore.

Now, note the sound effect here from this scene. Clip clap. This is olden days, 1919. And in the scene, the kid keeps the pharmacist, Mr. Gower, from sending out literal poison pills.

Film sound: Mr. Gower, you don't know what you're doing. You, you put something bad in those capsules. It wasn't your fault, Mr. Gower, just look and see what you did. The bottle took the powder from… it's poison, I tell you, it's poison.

Dan: Now late in the movie, there's a scene with another character, a really grouchy bartender.

Film sound: Hey, look, Mr. We save hard drinks in here for men who wanna get drunk fast, and we don't need any characters around it. Get the joy atmosphere. Is that clear or do I have to slip you my lip for a convincer?

Dan: And here's the thing. At the time of these scenes, the druggist and the bartender were basically in the same kind of business. I'm talking about the structure of the business. You go to the bar, order a martini, the guy grabs the gin, the vermouth, some olives, mixes it up and tells you a price that reflects his negotiations with all his suppliers and his sense of local market conditions, what he thinks you'll be willing to pay for a martini.

And he is balancing all those things and it's like a straight line. You negotiate with the bar keep, he deals with everybody else. In 1919, Mr. Gower is in exactly the same kind of business, except instead of gin and vermouth, he's got big jars, full of powders and okay, I mean, one of those jars is marked poison.

I'm not sure what that's about, but, okay. Mr. Gower measures out doses and sells them to his customers at a price he sets. Same exact deal. Simple. Since then, a couple things have happened. First, scientific breakthroughs made drugs a much bigger deal. I mean, penicillin, insulin, the Polio vaccine, just for starters, it's a miracle and a big business.

The other thing is, health insurance became a thing, including prescription drugs. So now you've got this intermediary standing between you and the provider, hashing out prices, telling you what your share is gonna be. And those two things created an opportunity for a new kind of business: pharmacy benefit managers.

Jeffrey Joyce is an economist at the University of Southern California. He studies the drug supply chain. He says, originally these companies did one narrow, technical thing. They created systems that told the drug store what each customer's specific insurance plan meant that customer was supposed to pay for their specific prescription, and the systems did all that in real time.

Geoffrey Joyce: So that when you show up at the pharmacy, it's a seamless transaction and they know exactly what your insurance is and what your copay should be.

Dan: Because Mr. Gower is not sending you a bill. He needs to ring you up right now. And insurance companies weren't set up to make that happen. So pharmacy benefit managers, PBMs for short, that's what they came along to do.

Geoffrey Joyce: That's what they functioned primarily as for many, many years.

Dan: And then PBMs got this new idea. They said to their customers, the insurance companies, Hey, we could save you some money. How about we start negotiating with manufacturers to get you lower prices? Here's how that works. There's lots of kinds of drugs where different companies make their own version. Like for high cholesterol, there's drugs called statins, and they've got brand names like Lipitor, Mevacor, Crestor.

But they all basically do the same thing. And that is an opportunity for the PBMs.

Geoffrey Joyce: They will go to the different manufacturers and say, who's gonna give us the best price? Who wants to be our preferred statin?

Dan: And that preferred statin? That one's gonna move a lot of units because the PBM and any insurance company they're working for is gonna say to consumers: If you're our patient, our customer covered by our insurance, we want you to take this statin and we'll make it worth your while cuz this one, the preferred statin has a $10 copay and all the others 50 bucks, maybe 75, maybe we don't cover them at all. And suddenly manufacturers are coming to the table

Geoffrey Joyce: And manufacturers offer discounts or rebates. So, hey, I'll give you 40 or 50% off if you make mine the preferred statin with a $10 copay. And all my competitors are either aren't covered on your plan or have a $50 copay.

Dan: And here's an important distinction. The manufacturers are not lowering their sticker prices here for whoever wants to buy. They are giving this rebate to this PBM. In other words, The PBM isn't shopping. They're not comparing the prices on offer in the open market. They're negotiating. They're cutting individual deals behind closed doors, but whatever, okay. At first, to an economist like Jeffrey Joyce, this all set up sounds like great news.

Geoffrey Joyce: I bought into their arguments that they actually lowered prices by negotiating competitively and and with manufacturers.

Dan: Now, sellers can't just charge whatever they want. They've gotta compete to give the best deal to buyers. Everybody wins. It's like economics 101.

Geoffrey Joyce: In, in, in theory, you would want this type of entity. You want them to go around and say, who's gonna gimme the best price?

Dan: But it hasn't worked out that way, which is why Jeffrey Joyce published an essay last year called An Economist's Change of Heart.

Geoffrey Joyce: So instead of sort of serving a, a role of, of constraining drug prices, I think they play a role in increasing drug prices.

Dan: Yeah, wait, how do we go from their holding prices down to their jacking prices up? That's right after this break.

This episode of An Arm and a Leg is produced in partnership with KFF Health News. That's a nonprofit newsroom covering health care in America. Their work is terrific, I'm so pleased to work with them.We'll have a little more information about KFF Health News at the end of this episode.

So, how do pharmacy benefit managers go from holding prices down to jacking prices up? This is where Mr. Gower and Nick the bartender come in. Once upon a time, before penicillin, before insurance, before pharmacy benefit managers, the relationships were simple. Me, Mr. Gower, his suppliers straight line. Now those relationships are a tangled knot. I found this super complicated flowchart made by Jeffrey Joyce's, colleagues from the University of Southern California. It is from a paper called Follow the Money, except the money's impossible to follow.

There's insurance companies, manufacturers, pharmacies, money going back and forth. All over the place. And in this knot, the pharmacy benefit manager is in the middle of everything. Every loop, all the deals and all the money, it all goes through them.

Geoffrey Joyce: You're right. And they're the hub. You're absolutely right. And I think that's at the, the crook of it. They have an inherent conflict of interest.

Dan: That is: Everybody's gotta negotiate with them. The drug makers, the pharmacies, and the insurance company, and nobody knows the deal anybody else is getting. So yeah, in theory, you'd want an entity like the PBMs negotiating on your behalf. But that's not what they're doing. They're negotiating on their own behalf.

Geoffrey Joyce: And they got sued, uh, in several states for saying, hey, you should be acting in the best interest of your clients. And they've won in court and saying, no, we have no obligation to do what's best for our client. We do what's best for us.

Dan: Okay. So how does that work and how does it lead to higher prices? Well, it helps. These companies have gotten huge. There used to be a bunch of PBMs, but they've gone around buying each other up. Now, three PBM companies represent like four fifths of all consumers. The single biggest one covers like 80 million people.

So they make a list of drugs for those 80 million people, which drugs cost $10? Which ones cost $50? And which ones. Aren't covered at all. That list has a

name. It's called the formulary, and controlling a formulary with 80 million customers gives the PBM a whole new kind of leverage.

Geoffrey Joyce: Just let me put it this way. Imagine you are a manufacturer and you produce a good drug and Express Scripts says, we represent 80 million Americans in their drug benefits. If you're off our formulary as a manufacturer, you lose access to 80 million consumers. That's an enormous hit. You'll do anything to stay on that formulary.

Dan: You'll do anything the PBM wants. And what the PBM wants is a big discount and the devious, tricky wild part that Jeffrey Joyce taught me, the easiest way to give a big discount is jack up the sticker price, which sounds like it would never work. Like I know. We'll double the price, then we can charge them the same, but we'll tell them they're getting a 50% discount.

I mean, are PBMs supposed to be stupid? But PBMs aren't stupid. Remember, they're not shopping on the open market. They're negotiating in secret, and they're not just negotiating for discounts. They're getting rebates, not money off, money back. A payout.

Geoffrey Joyce: It's more money that potentially they can retain. Right? So the more, the bigger the rebate, that's money. They have control over them.

Dan: It's, it's literally, it's cash in their pockets.

Geoffrey Joyce: It's cash.

Dan: And Joyce says, those negotiations get totally explicit. Raising prices is part of the deal.

Geoffrey Joyce: And so I've had several CEOs of drug companies tell me, PBMs put a gun to their head.

Raise your prices, i.e. raise your rebate, or you're off our formulary.

Dan: And of course, doing business in a back room someplace is what makes all this possible.

Geoffrey Joyce: Everything is, is proprietary. No one can see what kind of discount or rebates they're getting, and no one really knows how much is being retained and how much is being passed on. And anytime you have that lack of

information and lack of clarity, there's, it's it's a ripe environment for abuse and excess profit.

Dan: There's just one other thing, and I'm kind of reluctant to tell you this cuz I have this rule about the show where it's supposed to be more entertaining and empowering and maybe useful than it is enraging and terrifying and depressing. But I cannot hold back this part. So here it is, that knot, that tangle of deals with money going back and forth and the PBMs in the middle of everything.

That knot is getting tighter. Cuz the players are merging with each other. Those three big PBMs, one of them is CVS, the drug store chain, which is also merging with an insurance company, Aetna, and the other two? One belongs to an insurance company, and the other is getting bought by one.

Geoffrey Joyce: They always argue there are economies of scale and synergies, et cetera. Historically, we've seen the consumers lose when you see greater and greater concentration within an industry.

Dan: Great.

You know what's funny? None of this quite answers the question I started with. Why were there so many prices for that one generic prescription I tried to fill? And it turns out, Jeffrey Joyce has actually done research on this narrow little question, random prices at the drugstore. He sent hundreds of USC students to drugstores in LA with fake prescriptions to fill. His findings: My experience was not a one-off. Not an accident.

Geoffrey Joyce: And it's basically the drug store or whatever saying, Hey, here's a consumer that may or may not know the price, and we can charge them what we think we can get away with.

Dan: So Mr. Gower is still with us, and he's also trying to make a buck however he can.

Geoffrey Joyce: You or your child is sick and you need an antibiotic.

You've maybe not used that antibiotic in the past, or it's been a long time. You don't know what the price of that is. You don't know what a reasonable price is.

Dan: Your doctor's like, you need a Z-Pak.

Geoffrey Joyce: Exactly.

Dan: And you're like, alright.

Geoffrey Joyce: And when you walk in, would you know if a Z-Pak is, you know, a hundred dollars? That that may be the price you have no idea.

Dan: So basically we gotta watch our backs with everyone, which is turning into kind of a theme on this show. And sometimes I guess an outfit like GoodRx can help us know if Mr. Gower is trying to put one over on us. And it offers discounts with those coupons it has. So I asked Jeffrey, Joyce, and the other experts I talked with, how do I need to watch my back with GoodRx?

I mean, there's a catch right? And they said, no, not exactly, except that it's, you know, just a bandaid. It's not changing anything about the big picture with the PBMs and all the other players. In fact, when GoodRx shows us a coupon for a discount, it's because they've made a deal with a pharmacy benefit manager behind the scenes to get it.

So GoodRx wrangles its prices outta that same crazy float chart, that same crazy knot that produce the jacked up prices we see. And presumably it's finding a way to make a profit, but if a bandaid is useful to you, I guess it's useful.

That's where we left things four years ago.

I wanna recap my big takeaway from that Adventure: PBMs push drug makers to set higher list prices because the higher the list price goes, the bigger the rebate, the cash payout the PBMs can grab.

And here's a couple things that we didn't hit. By setting preferred drugs based on which company gives 'em the biggest rebates, and by making us pay super high prices for anything else. PBMs work with insurance companies to limit access to drugs.

And if you have a high deductible, or a copay, or percentage of list price you're supposed to pay at the pharmacy counter, the PBM still gets their full rebate.

In other words, some of the money coming outta your pocket may go directly to them.

Some things have changed since we first put this story out. The biggest PBMs have gotten bigger. For instance, the biggest, Express Scripts, now covers 100 million people, up from 80 million.

It seems worth mentioning that their parent company is United HealthGroup, the ever-growing behemoth we talked about a couple episodes ago.

And the biggest PBMs have been experimenting with new shenanigans -- enough for at least a whole new episode.

But not all the news is bad. In the last few years, state legislatures have passed 150 laws attempting to regulate PBMs. Every state has passed at least one.

A few states have passed laws saying that PBMs have to pass rebates along the consumers at the pharmacy counter.

In other words, trying to stop the PBMs from that situation where they're getting money directly outta your pocket.

Couple other states have passed laws saying PBMs cannot force you to use their mail order pharmacies, which great, but geez, I guess that means it's legal in 48 states and Congress has held five hearings so far this year specifically on PBMs with members from both parties eager to get their licks in.

I am not saying that the cavalry or Congress is about to ride in and fix everything. I wish. But I am saying, by understanding better what's going on, we can get a better sense of what we want our elected folks to do. I'll catch you in a few weeks till then, take care of yourself.

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