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**New York State Office of the State Comptroller**  
Thomas P. DiNapoli

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Division of State Government Accountability

# **Empire Plan Drug Rebate Revenue**

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## **United HealthCare Insurance Company of New York**

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# Executive Summary

## Purpose

To determine if United HealthCare Insurance Company of New York (United) credited the Department of Civil Service (Department) for all rebate revenue due under its contract with the Department. The audit covered the period January 1, 2010 through December 31, 2012 and included a review of revenue from six drug manufacturers.

## Background

The New York State Health Insurance Program (NYSHIP) provides health insurance coverage to active and retired State, participating local government, and school district employees and their dependents. The Department contracted with United to administer the NYSHIP prescription drug program between January 1, 2008 and December 31, 2013. In accordance with the contract, United is required to negotiate agreements with drug manufacturers for rebates, discounts, and other considerations and pass 100 percent of the value of the agreements on to the prescription drug program. United subcontracted key functions of the prescription drug program to Medco Health Solutions, Inc. (Medco), including the negotiation and collection of rebates offered by drug manufacturers. In 2012, Express Scripts Holding Company (Express Scripts) acquired Medco. During our audit period, the Department was credited \$248.4 million in revenue derived from agreements with the six drug manufacturers included in our audit.

## Key Findings

We identified \$694,227 in revenue that was not credited to the Department, including:

- \$493,348 in rebates that Express Scripts failed to allocate to the Department;
- \$159,785 in underpaid rebates that occurred because Express Scripts did not obtain the highest rebate rates to which the Department was entitled;
- \$22,408 in interest due the Department because Express Scripts did not credit rebates to the Department within 150 days as required; and
- \$18,686 in discounts that Express Scripts did not pass on to the Department.

United agreed to credit \$670,470 of the \$694,227 due the Department (\$23,757 was still under review at the time the audit fieldwork concluded).

Throughout the course of our audit, United and Express Scripts delayed access to information we requested, and refused to provide certain amendments to manufacturer agreements. This limited our ability to ensure the Department was credited with all drug rebate and discount revenue due the State. We considered these actions to be an impairment to our audit scope and objective.

## Key Recommendations

- Remit the \$694,227 in rebate and discount revenue identified by the audit to the Department.
- Establish and implement oversight procedures to ensure drug rebate and discount revenues from manufacturers are correct and properly credited to the Department, consistent with the provisions of the contract.

- Fully comply with all provisions pertaining to audits as prescribed by contracts with the Department. This includes (but is not limited to) providing timely access to all documents and other information, in unredacted form, deemed necessary by the State.

### **Other Related Audits/Reports of Interest**

[New York State Health Insurance Program: United HealthCare: Payments for Fraudulent and Improper Claims Submitted by Davis Ethical Pharmacy \(2012-S-10\)](#)

[United HealthCare: New York State Health Insurance Program Payments for Repackaged Drugs Dispensed Under the Empire Plan \(2010-S-38\)](#)

[United HealthCare: New York State Health Insurance Program Payments for Repackaged Drugs Dispensed Under the Empire Plan \(2012-F-13\)](#)

**State of New York**  
**Office of the State Comptroller**

**Division of State Government Accountability**

September 26, 2014

Ms. Paula A. Gazeley-Daily, R.Ph.  
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United HealthCare  
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Dear Ms. Gazeley-Daily:

The Office of the State Comptroller is committed to helping State agencies, public authorities, and local government agencies manage government resources efficiently and effectively and, by so doing, providing accountability for tax dollars spent to support government operations. The Comptroller oversees the fiscal affairs of State agencies, public authorities, and local government agencies as well as their compliance with relevant statutes and their observance of good business practices. This fiscal oversight is accomplished, in part, through our audits, which identify opportunities for improving operations. Audits can also identify strategies for reducing costs and strengthening controls that are intended to safeguard assets.

Following is a report of our audit of United HealthCare entitled *Empire Plan Drug Rebate Revenue*. This audit was performed pursuant to the State Comptroller's authority under Article V, Section 1, of the State Constitution and Article II, Section 8, of the State Finance Law.

This audit's results and recommendations are resources for you to use in effectively managing your operations and in meeting the expectations of taxpayers. If you have any questions about this report, please feel free to contact us.

Respectfully submitted,

*Office of the State Comptroller*  
*Division of State Government Accountability*

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This report is also available on our website at: [www.osc.state.ny.us](http://www.osc.state.ny.us)

## Background

The New York State Health Insurance Program (NYSHIP) provides health insurance coverage to 1.2 million active and retired State, participating local government, and school district employees and their dependents. The Empire Plan (Plan) is the primary health benefits plan for NYSHIP, serving about 1.1 million of these members. The Plan covers inpatient and outpatient hospital coverage, medical/surgical coverage, Centers of Excellence (for transplants, infertility, and cancer treatments), home care services, equipment and supplies, mental health and substance abuse services, and prescription drugs.

The Department of Civil Service (Department) administers the NYSHIP program. In carrying out its responsibilities, the Department contracted with United HealthCare (United) to administer the Plan's prescription drug program between January 1, 2008 and December 31, 2013. In accordance with the contract, United is required to utilize the Plan's significant enrollment to maximize savings to the prescription drug program by negotiating agreements with drug manufacturers for rebates, discounts, and other considerations and passing 100 percent of the value of the agreements on to the program. During our audit scope period, January 1, 2010 through December 31, 2012, the Department was credited \$635.8 million in revenue derived from agreements with an average of 67 drug manufacturers.

The Department's contract with United contains specific provisions to ensure the program is properly credited with all revenue from drug rebates and discounts to which it is entitled. Specifically, the contract required United to:

- Disclose all direct and indirect revenue arrangements with drug manufacturers. Further, the contract precluded United from entering into any agreement that had the effect of diverting, shortchanging, or trading off any revenue that would otherwise be due the program, including reduced acquisition costs. Also, all manufacturer agreements were required to meet or exceed United's best existing agreements for all individual drugs, ensuring that in no instance would the Department receive less drug manufacturer revenue than United's other clients;
- Credit the Department's cash account with all drug manufacturer revenue received on behalf of the program within 150 days of the end of each quarter. Interest, when applicable, would be calculated using the six-month Treasury bill discount rate as set by the first weekly auction of each month and compounded daily; and
- Calculate and distribute rebate revenue in a fully transparent and verifiable process, and provide all information and documentation the Department deemed necessary to verify proper crediting of all revenue due from drug manufacturers. United's records, methods, and calculations for collecting and allocating this revenue were subject to audit by the Department and other State auditors, including the Office of the State Comptroller (OSC). Further, United was required to maintain and make available those documents necessary to perform such audits, including (but not limited to) source documents, books of account, claim documentation, subcontracts, manufacturer agreements, and correspondence in unredacted form, within 15 business days of the request.

The contract allowed United to subcontract portions of its responsibility to a qualified organization. United, however, retained the ultimate responsibility for all services performed under the contract. Further, all subcontracts must contain provisions that are functionally identical to and consistent with the provisions of the contract with the Department. United subcontracted key functions of the prescription drug program to Medco Health Solutions, Inc. (Medco), including the negotiation, collection, and allocation of rebates offered by drug manufacturers. Express Scripts Holding Company (Express Scripts) acquired Medco in 2012.

## Audit Findings and Recommendations

To determine whether the Department was credited with all rebate revenues due, we selected six manufacturers with rebate terms specific to the State of New York prescription drug program. We refer to the six manufacturers as Drug Company Nos. 1 through 6. The selected manufacturers accounted for \$248.4 million (39 percent) of the \$635.8 million in drug manufacturer revenues credited to the Department during our three-year audit period ending December 31, 2012.

We found United did not properly invoice, collect, and allocate all manufacturer rebates and drug purchase discounts to which the Department was entitled. Rebates and discounts totaling \$694,227 from five of the six manufacturers were not credited to the Department's cash accounts (see Table 1). United agreed to credit \$670,470 of the \$694,227 to the Department (\$23,757 was still under review at the time the audit fieldwork concluded).

**Table 1**

<b>Manufacturer</b>	<b>Rebates Due the Department</b>
Drug Company No. 1	\$ 371,146
Drug Company No. 2	\$ 209,072
Drug Company No. 3	\$ 72,915
Drug Company No. 4	\$ 22,408
Drug Company No. 5	\$ 18,686
<b>Total</b>	<b>\$ 694,227</b>

In addition, both United and Express Scripts failed to respond adequately and timely to our requests for the documentation necessary for the conduct of our audit. The lack of proper responsiveness delayed our audit and limited our ability to ensure the Department was credited with all drug rebate and discount revenues due the State. We consider these actions to be limitations to the scope of our audit and we are required to report such audit impairments, in accordance with generally accepted government auditing standards.

### Manufacturer Rebates and Alternative Discount Arrangements

#### *Drug Company No. 1*

According to an amendment to the agreement between Drug Company No. 1 and Medco, two drugs met criteria for rebates on both retail pharmacy and mail-order pharmacy claims. However, our review of Express Scripts' Client Audit Rebate Database (CARD) showed the Department did not receive rebates for retail pharmacy claims for these drugs from October 1, 2011 through December 31, 2012. (Express Scripts did allocate rebate funds on mail-order pharmacy claims for



this period.) According to Express Scripts officials, changes to United's formulary (list of preferred drugs) made some United clients ineligible for the rebates on these two drugs. However, the Department's formulary was not affected by these changes, and the Department was, therefore, still eligible for the rebates on those drugs. We determined Express Scripts did not invoice, collect, and allocate rebates totaling \$364,448 to the Department (\$206,156 for Drug A and \$158,292 for Drug B) for the period October 1, 2011 through December 31, 2012.

Furthermore, from January 1, 2008 through September 30, 2011, the Department was entitled to an additional rebate on Drug B. However, according to our CARD analysis, the Department did not receive the rebate for three months (April 1, 2011 – June 30, 2011) during this period. Express Scripts officials agree with the finding and acknowledge the rebates were not invoiced, collected, or allocated to the Department. Based on the Plan's drug utilization according to claims data provided to OSC, we determined United owes the Department \$6,698 in additional rebates for Drug B.

### *Drug Company No. 2*

Based on our review of Medco's agreement with Drug Company No. 2, we determined other United clients were given higher rebate rates for two of Drug Company No. 2's drugs, which violates contract provisions that explicitly require that the Department's revenue from manufacturer agreements meet or exceed United's best existing agreements across their entire book of business. A recalculation of the rebate amount due the Department based on United's best existing agreements found the Department was underpaid \$159,785 (\$136,028 for Drug C for the period January 1, 2010 through September 30, 2010 and \$23,757 for Drug D for the period January 1, 2010 through December 31, 2012).

The Department was also eligible for rebates on an additional drug, Drug E, over the entire 36-month audit period. However, our CARD analysis revealed the Department did not earn rebates for six months during this time period. We determined the Department is due an additional \$49,287 for Drug E for the period from July 1, 2010 to December 31, 2010.

### *Drug Company No. 3*

Our CARD analysis identified \$72,915 that Express Scripts withheld from rebates remitted to United on behalf of the Department from April 1, 2012 to June 30, 2012. Upon further investigation, we found that the \$72,915 was for rebates collected for several Company No. 3 drugs in prior quarters of 2011 that were not credited to the Department: \$24,130 in the first quarter of 2011 and \$48,785 in the second quarter of 2011. The Department's contract with United requires that 100 percent of the revenue derived from agreements with drug manufacturers be passed to the prescription drug program. Therefore, Express Scripts was not entitled to retain these rebates. United agrees with our finding and will credit the Department \$72,915 for the additional rebates collected by Express Scripts.

### Drug Company No. 4

According to our CARD analysis, Express Scripts collected Drug Company No. 4 rebates totaling \$15,435,933 for the period October 1, 2011 through December 31, 2011 (fourth quarter 2011) and \$19,167,484 for the period January 1, 2012 through March 31, 2012 (first quarter 2012). The Department's Cash Flow Statements indicate United credited rebates for these two quarters to the Department's cash account on May 29, 2012 and August 28, 2012, respectively, 150 days after the end of each quarter, in accordance with the contract. However, we found United did not remit the full amounts due the Department, crediting instead only \$10,212,318 and \$1,743,282 for these two quarters, respectively. Although United made subsequent credits to the Department's cash account, a large portion of the rebates collected from Drug Company No. 4 was not credited until a year after they were due, as illustrated in Table 2.

**Table 2**

Quarter	Drug Company No. 4 Rebates Collected by Express Scripts	Drug Company No. 4 Rebates Credited to the Department	Date Drug Company No. 4 Rebates Credited to the Department	Difference	Subsequent Adjustment Credited to the Department (See Note)	Date Adjustment Credited
4 <sup>th</sup> - 2011	\$15,435,933	\$10,212,318	5/29/2012	\$ 5,223,615	\$ 4,388,845	5/30/2013
1 <sup>st</sup> - 2012	\$19,167,484	\$ 1,743,282	8/28/2012	\$17,424,202	\$16,888,844	8/28/2013
<b>Totals</b>	<b>\$34,603,417</b>	<b>\$11,955,600</b>		<b>\$22,647,817</b>	<b>\$21,277,689</b>	

*(Note: Amounts also include adjustments for prior period activity, but do not include additional credits made subsequent to the adjustment dates cited in the table. The Department eventually received the full amounts of credit due for the rebates in question.)*

When questioned about the lengthy delay, Express Scripts officials stated the additional rebates from Drug Company No. 4 were not allocated until completion of the final reconciliation. According to their standard procedures, Express Scripts makes estimated rebate prepayments prior to the final reconciliation. According to a United official, Express Scripts normally has to transfer only a small amount (typically 1 – 2 percent) of additional rebates as a result of the final reconciliation. In this case, the standard process was not followed, and instead a large portion of Drug Company No. 4 rebates were withheld until the final reconciliation. Neither United nor Express Scripts officials were able to provide an explanation as to why the standard process was not followed.

The Department's contract with United requires all drug manufacturer revenue collected on behalf of the program to be remitted 150 days after the end of the quarter. Using the six-month Treasury bill discount rate as set by the contract terms, we calculated the interest due the Department for the two quarters to be \$22,408 (\$5,196 for fourth quarter 2011 and \$17,212 for first quarter 2012). United agreed with our findings and will credit the Department this amount.

### *Drug Company No. 5*

Medco entered into an alternative discount arrangement with Drug Company No. 5 effective March 1, 2010 through December 31, 2012, which allowed Medco to receive discounts for two drugs. According to its contract with the Department, United (and by extension Express Scripts) is required to pass on the full value of manufacturers' discounts to the program. We analyzed CARD data for Drug Company No. 5 and found the Department was not credited for the discounts earned by Express Scripts.

In effect, Express Scripts used the alternative discount arrangement to shortchange the prescription drug program and not pass the savings on to the Department. The Department's contract stipulates that United, and thereby its subcontractor, may not enter into any agreement that has the effect of diverting, shortchanging, or trading off any revenue that would otherwise be due the program. We calculated the amount due the Department for the discounts based on the program's drug utilization, and determined the Department is owed \$18,686 (\$16,638 for Drug F and \$2,048 for Drug G) for the period March 1, 2010 to December 31, 2012.

## **Recommendations**

1. Remit to the Department \$694,227 in additional rebate and discount revenue as identified by our audit.
2. Establish and implement oversight procedures to ensure drug rebate and discount revenues from manufacturers are correct and properly credited to the Department, consistent with the provisions of the contract.

## **Scope Impairment**

Under its contract with the Department, United (and by extension Express Scripts) is required to calculate and distribute rebate revenue in a fully transparent and verifiable process. Further, the contract requires United to provide all information and documentation the Department deems necessary to verify proper crediting of all revenue due from drug manufacturers. United's records, methods, and calculations for allocating and distributing this revenue are subject to audit by the Department and other State auditors, including OSC.

In the conduct of our audit, we faced significant scope impairments and restrictions on our audit activity that delayed our audit and limited the audit team's ability to accomplish its objective. We conduct our audits in accordance with generally accepted government auditing standards, and these standards require that we include in our reports any information limitations or scope impairments, including denials or excessive delays in access to records or individuals.

Prior to our site visit to Express Scripts in Franklin Lakes, NJ, United officials provided "detailed on-site guidelines" for OSC auditors. These guidelines consisted of audit restrictions that under generally accepted government auditing standards would be considered a scope impairment.

Specifically, Express Scripts sought to impose the following restrictions on our audit efforts:

- An Express Scripts representative will be present and observing the auditors at all times;
- Auditors would not be allowed to take notes using laptops or other electronic devices;
- Auditors could take and retain written notes only to the extent necessary to document any identified errors;
- Express Scripts would be entitled to review auditors' notes to affirm compliance;
- Express Scripts could review manufacturer agreements to determine if there was anything in the agreements that would preclude Express Scripts from allowing OSC to take copies; and
- Such copies of manufacturer agreements could be redacted.

Because these restrictions constituted audit impairments, we advised United that we would not proceed with the audit unless United, as required by the contract, assured us unfettered access to all information OSC deemed relevant to the audit objectives.

Although United and Express Scripts provided assurances of information access to OSC, throughout the course of the audit both failed to honor them. Both parties delayed our access to certain documentation, did not disclose pertinent information, refused to provide other documentation, and redacted pertinent information from documentation that was provided. This delayed our audit and limited our ability to ensure the Department was credited with all rebate revenue due. We consider these actions to be limitations to the scope of our audit that restricted our ability to render objective opinions and conclusions about the full range of rebates credited to the Department. Therefore, in accordance with professional standards, we are required to report these restrictions as scope impairments.

In its response to our preliminary report, United maintained that delays in providing requested documentation were due to a complex retrieval process. Nevertheless, the contract requires United to respond to all audit requests within 15 business days. United failed to comply with this requirement, taking more than five months to provide many of the requested items, including numerous invoices. Further, United maintained that certain portions of the manufacturer agreements we requested did not apply to the State, and therefore, they did not deliver them to us. Therefore, we could not determine if United credited the Department with all rebate revenues due under the terms of those manufacturer agreements. As previously noted, the Department's contract requires United to provide all information and documentation deemed necessary by the State (not United) to verify the program was credited with all rebate revenue due under the contract's terms.

Readers of this report should consider the effect of these scope limitations on the findings and conclusions presented in our report. Moreover, based on the audit work we were able to perform, we believe there is considerable risk that material amounts of rebates for other drugs (and from other manufacturers) are due the State for the period of our audit.

## Recommendation

3. Fully comply with all provisions pertaining to audits as prescribed by contracts with the Department. This includes (but is not limited to) providing timely access to all documents and other information, in unredacted form, deemed necessary by the State.

## Audit Scope and Methodology

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The objective of our audit was to determine if United credited the Department with all rebate revenue due under their contract with the Department for selected drug manufacturers. The audit covers the period January 1, 2010 through December 31, 2012.

To perform our audit, we obtained and reviewed the contract between the Department and United. We selected six manufacturers with at least one drug with State of New York-specific rebate terms. The six manufacturers were among the largest manufacturers in terms of rebate revenues United credited to the State. We reviewed manufacturer agreements, amendments, purchase discount agreements, and invoices for the selected manufacturers. We analyzed CARD data, Quarterly Rebate Reports, and Cash Flow Statements. We also interviewed officials at the Department, United, and Express Scripts and assessed United's internal controls relative to our audit objective.

We conducted our performance audit in accordance with generally accepted government auditing standards, with the exception of the scope impairment detailed in our report. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

In addition to being the State Auditor, the Comptroller performs certain other constitutionally and statutorily mandated duties as the chief fiscal officer of New York State. These include operating the State's accounting system; preparing the State's financial statements; and approving State contracts, refunds, and other payments. In addition, the Comptroller appoints members (some of whom have minority voting rights) to certain boards, commissions, and public authorities. These duties may be considered management functions for purposes of evaluating organizational independence under generally accepted government auditing standards. In our opinion, these functions do not affect our ability to conduct independent audits of program performance.

## Authority

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The audit was performed pursuant to the State Comptroller's authority as set forth in Article V, Section 1, of the State Constitution and Article II, Section 8, of the State Finance Law.

## Reporting Requirements

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We provided preliminary copies of the matters contained in this report to United officials for their review and comments. Their comments have been taken into consideration in preparing this report.

Within 90 days of the final release of this report, we request United officials report to the State Comptroller advising what steps were taken to implement the recommendations included in the report.

## Contributors to This Report

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### Vision

A team of accountability experts respected for providing information that decision makers value.

### Mission

To improve government operations by conducting independent audits, reviews and evaluations of New York State and New York City taxpayer financed programs.