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On Behalf of

CONSUMER ACTION

BEFORE THE

NEW YORK DEPARTMENT OF FINANCIAL SERVICES

ON

CVS HEALTH'S ACQUISITION OF AETNA, INC.

October 18, 2018

I would like to thank you for the opportunity to testify today regarding the competition concerns presented by CVS Health's proposed acquisition of Aetna, Inc. and the need for the Department of Financial Services to impose significant behavioral remedies to protect subscribers and market participants.

I am here on behalf of Consumer Action, a national non-profit organization that has worked to protect consumers for 47 years.[1]

The CVS-Aetna Merger Will Harm Consumers and Competition

The CVS/Aetna transaction combines the largest retail pharmacy, one of the two largest pharmacy benefit managers ("PBM"), and the third largest health insurer in the United States, all under one roof. The deal creates a large, vertically integrated firm that operates in markets where only a few meaningful rivals compete.

Last week, the DOJ approved the acquisition with conditions requiring the divestiture of Aetna's Medicare Part D individual prescription drug plans, but did not include any behavioral conditions on the merging parties' future conduct. Despite the proposed divestiture, we are concerned that CVS' acquisition of Aetna will harm consumers because the DOJ failed to address the types of strategic, exclusionary conduct presented by the merger.

The DOJ's approval of CVS/Aetna was done shortly after its approval of Cigna's acquisition of Express Scripts, another vertical integration between a health insurer and PBM. That deal was approved without any conditions at all.

In short, the two vertical transactions will dramatically change the healthcare industry and how it will function going forward. Even prior to the acquisitions, the PBM market was not competitive. Moreover, CVS and Aetna already hold significant market power in the retail pharmacy, PBM, and health insurance markets. Given the structure of these markets, a merged CVS-Aetna will increase its bargaining leverage over its rival retail pharmacies and have an enhanced incentive and ability to disadvantage them. The role of community and independent pharmacies is vitally important to competition and patient choice because pharmacists have daily interactions with patients. Competition and patients will likely suffer through higher prices, lower quality, less innovation, and less choice unless state regulators fill the void and regulate the merging parties and the PBM industry going forward.

[1] Consumer Action has been a pioneer in the consumer rights movement, working to improve and protect consumer rights in areas consumers care about most: credit cards, home ownership, insurance, healthcare, and online and medical privacy. Promoting pro-consumer policy, regulations and legislation and helping consumers be heard by those in power is part of Consumer Action's mission.
David Balto is the former Policy Director of the Bureau of Competition of the Federal Trade Commission and a leading expert on healthcare competition. He has testified before several insurance commissioners including DFS on insurance mergers. Andre Barlow is a former Trial Attorney of the Health Care Task Force of the Department of Justice's Antitrust Division and is an expert on healthcare competition.

The profound concerns over the approval of the merger was set out by the American Antitrust Institute, the nation's leading antitrust advocacy group. "If ever there were a vertical merger that should have been challenged by antitrust enforcers, this would be it," said AAI President, Diana Moss.

PBM Market Is Concentrated and Uncompetitive

The PBM market lacks the essential elements for a competitive market due to the lack of choice, numerous conflicts of interests, and lack of transparency and regulation.[2] Currently, there is a lack of choice because three PBMs (CVS, Express Scripts, and UnitedHealth's OptumRx) control 85% of the PBM market.[3] The three major PBMs clearly face conflicts because they own mail order operations, specialty pharmacies, and, in the case of CVS, the largest retail and specialty pharmacy chain and the dominant long-term care pharmacy.[4] Health plans and employers contract with a PBM to obtain the services of an "honest broker" to secure the lowest prices and best services from both pharmaceutical manufacturers and from pharmacies. The PBMs control the formularies so they determine what drugs we are allowed to purchase, how many times we can fill the prescription, and the amount of our co-pays.

A PBM such as CVS can design the benefit in such a way that patients will pay higher co-pays at rival retail pharmacies. When the PBM is commonly owned with the entity it is supposed to bargain with, or has its own mail order operations, there is an inherent conflict of interest, which can lead to deception, anticompetitive conduct, higher prices, and less choice for the patient. Because of a lack of transparency, the prescription drug rebates negotiated by PBMs from pharmaceutical manufacturers are not fully passed on to employers or consumers and the dispensing fees reimbursed to retail pharmacies are far less than what the insurance plan is actually paying for the drug. The PBMs can make money off the spread between what they pay retail pharmacies and what they charge the insurance plan. Indeed, the PBMs are in many cases making more money per prescription than the retail pharmacy that is buying and dispensing the drug. PBMs take advantage of a lack of transparency, misaligned incentives, and conflicts of interest to make larger profits than any other players involved in the drug supply chain (distributors, insurers, or pharmacies).[5] The current structure and characteristics of the PBM market has led to higher drug costs.[6]

Past Vertical Healthcare Mergers Have Harmed Consumers

There is little evidence that past vertical acquisitions by CVS have resulted in significant benefits to consumers. Indeed, past vertical mergers have resulted in anticompetitive conduct that has

[2] Testimony of David Balto, Before House Judiciary Committee, October 8, 2009.
[3] Reforming Biopharmaceutical Pricing at Home and Abroad, The Council of Economic Advisors, White Paper, February 2018. The White House Council of Economic Advisers found that the three large PBMs control more than 85% of the market, "which allows them to exercise undue market power against manufacturers and against health plans and beneficiaries they are supposed to be representing, thus generating outsized profits for themselves."
[4] Testimony of David Balto, Before the California Senate Committee on Business Practices and Economic Development, March 20, 2017.
[5] Charlie Grant, *Hidden Profits in the Prescription Drug Supply Chain*, Wall Street Journal, February 24, 2018.
[6] *Id.*

harmed independent pharmacies and consumer choice. If CVS and Aetna are allowed to join forces, the results will be predictably harmful to competition as well as consumers.

In 2007, CVS, acquired Caremark, a PBM giant and used that power to exclude competition, reduce patient access to vital healthcare services from their pharmacists of choice, and drive up prices. After closing on the acquisition, the vertically integrated firm formed exclusive pharmacy networks that prevented consumers from accessing pharmacists of their choice and increased their costs for prescription drugs. CVS will undoubtedly enter into similarly exclusive arrangements if it is permitted to acquire Aetna.

In addition to the exclusive arrangements, CVS has allegedly engaged in a strategy of squeezing its rival retail pharmacies with "take-it-or-leave-it" non-negotiable contracts.[7] Rival retail pharmacies are required to sign contracts with CVS Caremark in order to process prescriptions through the PBM for payment. Because they have no bargaining power, CVS was able to depress the dispensing fees to rival retail pharmacists to uncompetitive levels in the fall of 2017 by drastically decreasing generic prescription and Medicaid reimbursement rates while at the same time reimbursing its own CVS pharmacies at higher rates.[8] Sometimes these rival pharmacies were not reimbursed enough to cover the cost of filling the prescription, and, in many cases, CVS was reimbursing the rival retail pharmacies less than half of what was being charged to the health insurance plans.[9] The declining reimbursement rates caused a number of rival retail pharmacies to shut their doors, reducing patients' treatment options and access. To the ones still in business, CVS sent letters offering to purchase them.[10] Because many of the rival retail pharmacists are small and lack bargaining power, they are susceptible to exclusionary conduct and take-it-or-leave-it contracts.

Moreover, CVS has successfully steered many of its PBM customers to its pharmacies and mail order. While CVS claims that its mail order saves money for customers and/or employers, there is considerable dispute on whether those claims are valid. Customers want choice and even after being steered to CVS' mail order, many of these patients reportedly come back to their independent and community pharmacies to ask questions about their prescriptions and medications even though they are receiving prescription drugs from CVS' mail order. This happens because patients want access to a pharmacist who sees them regularly. These patient access concerns are particularly great in underserved inner city and urban areas. In essence, CVS is free riding on independent and community pharmacists, and if this continues, this could eventually run these rival retail pharmacists out of business.

While CVS proclaims that its acquisition of Aetna will result in substantial efficiencies, it is often the case that efficiencies even if realized are rarely passed on to consumers in the form of lower prices and better services.

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[7] Linette Lopez, *What CVS is Doing to Mom and Pop Pharmacies in the U.S. Will Make You Boil,* Business Week (March 30, 2018).
[8] *Id.*
[9] *Id.*
[10] *Id.*

In fact, past health insurer-PBM alliances have not led to lower health care prices or improved quality of care. In 2007, UnitedHealthcare acquired CatamaranRx, then the fourth-largest PBM, into its OptumRx PBM, and in 2011, Express Scripts and Medco, two of the three largest PBMs at the time, merged. Both deals promised efficiencies that would result in lower prices for consumers, however, there has been no evidence of improved care, lower premiums and overall costs, increased savings, or any resulting benefits passed on to consumers. Rather, consumers have suffered through higher drug prices, fewer choices, poorer service, and increased fraud and abuse.

CVS/Aetna Merger Is Likely to Harm Competition and Rival Retail Pharmacies

CVS' history suggests that it will continue to engage in exclusionary conduct to steer patients away from rivals and to depress pharmacist reimbursement rates to uncompetitive levels through take-it-or-leave-it contracts.[11] The acquisition of Aetna enhances the ability and incentive of the merged firm to impede competition in retail pharmacy. Before the merger, Aetna has the incentive to deal with all retail pharmacy rivals for its commercial insureds. Post-merger, these incentives change because CVS/Aetna will have the increased incentive and ability to steer Aetna's patients to CVS' mail order or its retail pharmacy stores. CVS will be able to cut off rival retail pharmacies' access to Aetna insureds by implementing some changes either explicitly requiring the Aetna insureds to use CVS mail order and/or retail pharmacies or implementing financial disincentives to Aetna insureds from using rival retail pharmacies.

Behavioral Remedies Are Necessary To Protect Pharmacy Competition

The role of the U.S. Department of Justice is to bring law enforcement actions against anticompetitive mergers. The DOJ has made clear in a number of recent speeches over the past year that its focus is on demanding structural remedies to resolve competition concerns, and it will not engage in the regulation of merging parties post-merger.[12] Therefore, it is up to the state regulators to regulate the PBM industry and CVS/Aetna's post-merger conduct to prevent competitive harm and to protect patients' access to the pharmacy of their choice.

The vertical integration of the three largest PBMs with health insurers threatens the incentives of companies with innovative business models to enter and effectively compete at either level. Thus, there is a concern that they could act strategically to harm consumers and patients through higher prices, lower quality, less choice, and less innovation in markets for prescription drugs and retail pharmacies. Undoubtedly, CVS's acquisition of Aetna threatens to reduce the number of quality choices of rival retail pharmacies available to patients by increasing the merging parties' incentive and ability to engage in conduct that would foreclose competition. For these reasons, NYDFS should seek comprehensive relief to ensure that PBMs are regulated and that CVS will not have the ability to foreclose rival retail pharmacy competition, deny patients access to their pharmacy of choice, and deny the medicines patients need. Without stringent regulations

[11] Karen E. Klein, *End of Days for Independent Pharmacists?*, Bloomberg Business Week, (March 8, 2012).
[12] Assistant Attorney General Makan Delrahim Delivers Remarks at the Antitrust Division's Second Roundtable on Competition and Deregulation**,** April 26, 2018; *see also*, Assistant Attorney General Makan Delrahim Delivers Keynote Address at American Bar Association's Antitrust Fall Forum, November 16, 2017.

on the PBM industry and the merging parties, patients can anticipate an increase in prescription drug prices and out of pocket costs. We recommend that the NYDFS take the following steps to regulate PBMs' and CVS' future conduct:

- Prohibit CVS from creating pharmacy networks that exclude rival retail pharmacies and drug formularies that deprive patients of the medicines they need and require CVS to report compliance;
- Require PBMs and CVS to report information related to their pharmacy networks and drug formularies that would allow NYDFS to make sure that patients have access to all pharmacies and their prescription drugs;
- Prohibit CVS from entering into or enforcing contracts with rival retail pharmacies that make it financially unattractive for them to fill prescriptions for patients;
- Require PBMs and CVS to create provider networks that enable fair access to community and independent providers including all retail pharmacies;
- Prohibit CVS from creating benefit designs that discriminate against rival retail pharmacies and require CVS to report compliance to ensure that its benefit designs do not manipulate co-pays in a way that disadvantage rival retail pharmacies;
- Create license requirements and a requirement that all PBMs register with the state as separate entities so that the PBMs can be regulated; and
- Develop a process for patients, retail pharmacies and other providers to file complaints related to PBM and CVS misconduct.

We appreciate the opportunity to testify on this important merger.