NACDS NATIONAL ASSOCIATION OF CHAIN DRUG STORES

Statement of:

Michael J. Bettiga, R.Ph.

Chief Operating Officer and Executive Vice President

Shopko Stores

Green Bay, Wisconsin

On Behalf of:

The National Association of

Chain Drug Stores

For:

United States Senate

Committee on the Judiciary

Subcommittee on Antitrust,

Competition Policy and Consumer Rights

Hearing on:

"The Express Scripts/Medco Merger:

Cost Savings for Consumers or More Profits for the Middlemen?"

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National Association of Chain Drug Stores (NACDS)
413 North Lee Street
Alexandria, VA 22314
703-549-3001
www.nacds.org

On behalf of the National Association of Chain Drug Stores (NACDS), I am pleased to submit a statement for the hearing on "The Express Scripts/Medco Merger: Cost Savings for Consumers or More Profits for the Middlemen?" My name is Mike Bettiga. I am a pharmacist and have worked in numerous capacities for Shopko Stores for almost 35 years. Presently, I am the Chief Operating Officer and Executive Vice President at Shopko. Shopko is a multi-department retailer that operates in the Midwest, Northern Plains, and Western U.S.

NACDS represents traditional drug stores, supermarkets, and mass merchants with pharmacies – from regional chains with four stores to national companies. Chains operate more than 40,000 pharmacies, and employ more than 3.5 million employees, including 130,000 full-time pharmacists. They fill over 2.6 billion prescriptions annually, which is more than 72 percent of annual prescriptions in the United States. The total economic impact of all retail stores with pharmacies transcends their $900 billion in annual sales. Every $1 spent in these stores creates a ripple effect of $1.81 in other industries, for a total economic impact of $1.76 trillion, equal to 12 percent of GDP.

Express Scripts and Medco are two of the "Big Three PBMs" in the U.S. The proposed merger of these two PBM giants poses significant anti-competitive threats to numerous U.S. industries and markets. If allowed, this merger would have grave consequences for consumers and the nation's community pharmacies that serve them, as well as for health plans and employers that utilize PBM services, specialty pharmacy services, and mail order pharmacy services. NACDS opposes this merger and has urged FTC to block it. In September, the FTC issued a "Second Request" to Express Scripts and Medco to gather more data on the merger. According to media reports, only 4% of similar proposed deals in 2010 were issued a Second Request by the FTC. This merger has received the attention of not only FTC and this Committee, but also numerous other Members of Congress, numerous state Insurance Commissioners, state Attorneys General, and state legislators, who have all asked FTC to give this proposed merger a high level of scrutiny.

Background on PBMs

PBMs manage and administer the prescription drug benefits of more than 210 million Americans. Employers and health plans contract with PBMs to manage and administer prescription drug benefits (as opposed to medical benefits) as part of overall health benefits. PBMs construct and manage drug formularies and use these formularies to negotiate rebates and discounts with pharmaceutical manufacturers. Manufacturers provide rebates and discounts to PBMs as "rewards" for placing their brand drugs on formularies, promoting these products and driving brand usage. In the process, PBMs act as "double agents" working simultaneously for employers/plans (administering patients' pharmacy benefits) and drug manufacturers (maximizing market share via formulary inclusion). PBMs often tout their ability to negotiate these rebates and cost savings and claim that they benefit plans and patients. However, there is no proof that PBMs pass along any savings to plans, employers, or patients, nor do they generally disclose the rebates. In practice, many PBMs retain a large percentage of these rebates even though they are generated by the plans' pharmacy spend. Formularies and rebates drive the usage of selected drugs, thereby maximizing the rebates PBMs can extract from drug manufacturers and incentivizing PBMs to increase the dispensing of certain drugs, even if it increases the plans' costs (i.e., by dispensing brand drugs rather than generic drugs). These rebates and discounts are a significant source of PBM revenue, which often creates a conflict of interest between the PBMs' and the patients' and plans' interests.

The PBM then contracts with community pharmacies to provide prescription drugs and pharmacy services to the plans' beneficiaries. The payment from a PBM to a pharmacy for dispensing a prescription drug differs from the amount a PBM charges a plan for the same prescription drug, to the benefit of the PBM. Plans sponsors are typically unaware of this difference, commonly referred to as the "spread." PBMs profit not only from the spread, but also from additional administrative fees charged to the plan for processing the claim. Many PBMs also own mail order pharmacies that they encourage consumers to

use instead of community pharmacies. In addition, Express Scripts and Medco each separately own two of the largest specialty pharmacy companies in the U.S.

As an industry, PBMs are virtually unregulated. They may have tangential regulatory compliance for insurance related processes through their relationships with health plans and employers. A handful of states directly regulate some PBM functions, such as how they conduct audits of pharmacies, and some state boards of pharmacy regulate them to the extent that their activities can be construed as practicing pharmacy. The vast majority of their remaining functions and activities are unregulated, as there are no state or federal authorities with direct jurisdiction over them.

Overview of Concerns

The proposed merger of Express Scripts and Medco would result in unparalleled market concentration in an already extremely limited marketplace. Because of several mergers and acquisitions over the past decade, the number of large PBMs has declined significantly since 2000 and the concentration among these large PBMs has increased during that time. The market for national prescription drug plans is currently concentrated in just three PBMs. If the merger proceeds, there will be a reduction in competition in already highly-concentrated markets, including those involving PBM services, as well as mail order distribution services and specialty pharmaceutical services.

The proposed merger would be a tipping point in terms of PBM concentration that would have a considerable anti-competitive impact on employers, health plans, federal employee benefit plans, and TRICARE, along with their beneficiaries. The post-merger PBM marketplace would have markedly reduced choice for all patients and consumers, as well as governmental, employer and third-party payors.

Reduced PBM Competition

As two of the "Big Three" PBMs, Express Scripts and Medco control 50-60% of the national overall prescription drug volume.[1] If this merger is approved, more than one-third of all Americans (roughly 135 million people) would rely on the new "mega PBM" to manage their prescription benefits.[2] This "mega PBM" alone would control over 40% of the national prescription drug volume.[3] Certain classes of customers such as large, complex health plans would be left with only two choices for PBM services, the merged entity and the one remaining large PBM. For these large plans that typically choose one of the "Big Three" PBMs, the proposed merger would create a firm with more than 50% market share. Smaller regional PBMs would be unable to constrain anticompetitive conduct because of their smaller size, geographic limitations, and lack of ability to secure rebates.

This substantial reduction in competition will harm purchasers of PBM services and the purchasers' beneficiaries by limiting consumer choice, reducing transparency, reducing access to pharmacy services, and increasing costs to the beneficiaries.

Anti-Competitive Concentration in the PBM Market

The proposed merger will lead to anticompetitive concentration in the PBM market, resulting in market foreclosure practices that harm purchasers of PBM services and consequently, consumers of pharmacy services. Specifically, the merged PBM will have an incentive to use its increased market power as both a seller and a purchaser of pharmacy services to impose unfavorable contract terms on community pharmacies. Consequently, this "mega PBM" would have the ability to raise prices for health plans and patients, limit access to pharmacy patient care and force patients to use the PBM's mail order pharmacies rather than their trusted community pharmacies, driving up costs for employers, health plans and other federal and state programs.

PBMs operate unregulated and in an opaque manner. They claim that they save money by negotiating rebates and discounts from drug manufacturers and negotiating lower reimbursement rates from pharmacies. However, as mentioned above, there is no proof that they pass along any of this purported savings to health plans, employers or consumers. In fact, the PBM industry has been fraught with allegations of extensive deceptive and fraudulent practices. In recent years, cases brought by a coalition of over 30 State Attorneys General have resulted in over $370 million in penalties for deceptive and fraudulent conduct.[4] It was found that PBMs accepted rebates from manufacturers in return for placing higher priced medications on prescription drug plans' formularies, switched customers to the higher priced drugs that were paid for by the health plan/employer, and benefitted from both the rebate received and the higher priced drug payment without passing along the enrichment to the health plan/employer. In essence, PBMs use lack of transparency to negotiate higher rebates from drug manufacturers, higher drug prices for health plans/employers, and lower payments to pharmacies, while keeping the gains for themselves. We can expect a "mega PBM" to have freer reign to engage in similar egregious conduct.

As middlemen, PBMs claim that their ability to negotiate with drug manufacturers and pharmacies reduces overall prescription drug costs. However, despite their claims, overall prescription drug spending continues to steadily increase. Moreover, recent studies show that PBMs' mail order pharmacies have lower generic dispensing rates than retail community pharmacies.[5] A "mega PBM" would be even more likely to increase drug costs by shifting more patients to mail order, which utilizes more expensive, brand name drugs. This increased cost would be borne by health plans, employers, and ultimately consumers.

Our concerns about the anti-competitive nature of this proposed merger were recently echoed by the American Antitrust Institute (AAI) in a letter to FTC, in which AAI urges

FTC to enjoin the merger. In addition, AAI explains why second-tier PBMs are not able to compete with the "Big Three" PBMs, and the proposed merger would make it even more difficult for them to compete. AAI also describes the anticompetitive harm the merger would cause in the specialty pharmacy and mail order pharmacy segments.

Concerns about Specialty Pharmacy and Mail Order Services

Specialty pharmaceuticals are high cost drugs required by patients undergoing intensive therapies for chronic, complex, relatively rare and/or potentially life-threatening illnesses. Industry experts anticipate that sales of specialty pharmaceuticals will account for an increasing dollar share of all drugs consumed, estimated to be 27% of all drug sales by 2015.[6]

The merger would combine two of the three largest suppliers of specialty pharmacy services, creating an entity with more than 50% share of all specialty pharmacy sales. CuraScript (owned by Express Scripts) and Accredo (owned by Medco) are the two largest specialty pharmacies in the U.S. Combined, these two entities account for an estimated 52% of all specialty pharmaceuticals in the U.S.; this would be enough power to stifle competition in the specialty pharmacy market and command even higher prices. Both PBMs have attempted to significantly increase prices of specialty pharmaceuticals in recent years. We can expect an even greater effort to do this should the merger be approved.

The merger will also create the largest mail-order pharmacy accounting for close to 60% of all mail-order prescriptions processed in the U.S.[7] The merged company will have even more market power to reduce patient access to community pharmacies and force consumers and employers to use its own captive mail order operation. Although the merging firms may claim that shifting prescriptions to mail order prescriptions from retail community pharmacies will drive down drug costs to consumers, their increased market

power is likely to result in an artificially high reduction in prescriptions filled through community pharmacies, and increased costs for payors and beneficiaries.

The ability of PBMs to drive prescriptions to their own mail order facilities is inherently anticompetitive. Congress has recognized the potential for this type of abuse, and in Medicare, this type of "self dealing" in the case of physicians is illegal. Moreover, PBMs determine the income received by pharmacies (by setting pharmacies' reimbursement rates) and then directly compete with pharmacies by driving prescriptions to their own mail order facilities. Further consolidation of PBMs and mail order pharmacies, in addition to the lack of transparency in PBM operations, will further exacerbate these conflicts. The result will be increased costs for public programs such as Medicare, beneficiaries, private health plans and employers, and the American taxpayer.

In addition, the merged entity's ability to shift patients to its mail-order operations will have a direct and harmful impact on patient care. It will allow the mega PBM to limit consumers' access to their local pharmacies and the vital healthcare services and one-on-one counseling they provide. As mentioned recently by Medco CEO David Snow, PBM mail order pharmacies utilize robots as opposed to pharmacists.[8] In addition to dispensing prescriptions, pharmacists counsel patients on a daily basis to ensure that they take their medications as directed by their doctors. They also provide a broad range of critical, cost-effective services such as immunizations, counseling for diseases such as diabetes, and other health education and screening programs. These high quality services increase the therapeutic benefits of prescription drugs, which improve health outcomes and lowers costs. Robots in remote facilities cannot provide these personal, customized services. There is simply no substitute for the in-store, face-to-face services provided by pharmacists.

Conclusion

NACDS thanks the Committee for consideration of our comments on the proposed merger of Express Scripts and Medco. We are deeply concerned about the anti-competitive impact the merger would have and are extremely skeptical that the American public can trust a "mega PBM" to look out for the best interests of patients and payors, or to pass any purported "savings" along to beneficiaries and other consumers. These concerns are compounded by the fact that the PBM industry as a whole is virtually unregulated.

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[1] Atlantic Information Services ("AIS"), 2010 data; J.P. Morgan, Healthcare Technology & Distribution, Gill's Guide to Rx Channel – An Investor Handbook, May 10, 2011.
[2] Bloomberg, Express Scripts-Medco Deal May Spur Purchases by Rivals, July 22, 2011.
[3] Atlantic Information Services ("AIS"), 2010 data; J.P. Morgan, Healthcare Technology & Distribution, Gill's Guide to Rx Channel – An Investor Handbook, May 10, 2011.
[4] The American Antitrust Institute; "Commentary: The FTC Should Issue a Second Request on Express Scripts' Proposed Acquisition of Wellpoint's PBM Business," May 11, 2009.
[5] See 2010-2011 Prescription Drug Cost and Plan Benefit Design Report at 28, available at http://www.benefitdesignreport.com/Portals/0/2010-2011_BDR_R1.pdf.
[6] See CVS Caremark Corp., 2010 Annual Report at http://www.annualreports.com/HostedData/AnnualReports/PDFArchive/cvs2010.pdf (citing ModernHealthcare.com).
[7] AIS 2011 data.
[8] See, for example, http://blog.pharmexec.com/2011/10/11/medco-ceo-champions-robots-over-pharmacists/; accessed November 26, 2011.