Testimony of David A. Balto

on behalf of
Consumers Union, Consumer Federation of America, National Consumers League, U.S. Public Interest Research Group, and the National Legislative Association on Prescription Drug Prices

To the Committee on the Judiciary,
Subcommittee on Antitrust, Competition Policy and Consumer Rights
United States Senate
Regarding "The Express Scripts/Medco Merger: Cost Savings for Consumers or More Profits for the Middlemen?"
Tuesday, December 6, 2011

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Introduction

Mr. Chairman Kohl, Ranking Member Lee, and other distinguished members of the Senate Judiciary Committee, I want to thank you for giving me the opportunity today to speak about the severe competitive problems that may arise from Express Scripts' proposed acquisition of Medco Health Solutions. I am testifying today on behalf of the nation's leading consumer groups including Consumers Union, Consumer Federation of America, National Consumers League, U.S. Public Interest Research Group, and the National Legislative Association on Prescription Drug Prices. As detailed in my testimony, this merger of two of the three largest pharmacy benefit managers ("PBMs") raises serious competitive concerns and could potentially lead to significantly higher prices and diminished service for healthcare consumers.

My testimony today is based on my experience of over a quarter century as an antitrust practitioner, the majority of which was spent as a trial attorney in the Antitrust Division of the Department of Justice, and in several senior management positions, including Policy Director at the Federal Trade Commission's ("FTC") Bureau of Competition and attorney advisor to Chairman Robert Pitofsky. I helped bring some of the first antitrust cases against PBMs and have testified before Congress, regulators, and state legislatures over ten times on PBM competition. [1]

I am here with a simple message for this Committee. The loss of competition caused by this merger will make it more likely for Express Scripts to charge *more* for its services and to pass along *less* of the savings they obtain to their customers, the plan sponsors, ultimately harming the millions of consumers who need these services. Express Scripts and Medco are two of the three largest PBMs and the merger will create a dominant PBM with 155 million covered lives—70 million more covered lives than the next largest competitor—and over five times as

[1] In the present FTC investigation of this merger I represent a number of employers, unions, health plans, consumer advocacy groups, pharmacies, a PBM, and specialty pharmacy groups. (My testimony today solely reflects the views of the consumer groups I represent).

large as the fourth largest firm. Express Scripts-Medco would alone control approximately 50 percent of the large plan sponsor market, 60 percent of all mail order prescriptions, and over 50 percent of the specialty pharmacy market. And although the merging parties assert various efficiencies as justification for this merger, these proffered efficiencies do not outweigh the anticompetitive effects and consumer harm that is likely to result from this transaction.

All consumers will suffer as service and access to their retail pharmacies declines and they are increasingly denied a choice and service. Express Scripts will have greater power to steer plan participants to its own captive mail order and specialty pharmacy operations, reducing choice for all plan participants and quality for many.[2] Additionally, Express Scripts will have a greater ability to drive down reimbursement to pharmacies *below competitive levels* resulting in diminished access to valuable pharmacy services, higher prices, and lost jobs.

The thousands of vulnerable consumers who need specialty drugs will be particularly harmed. These include the millions of patients suffering from diseases such as hemophilia, multiple sclerosis, Crohn's Disease, infertility, HIV/AIDS, and many forms of cancer. The merger will enable Express Scripts to increasingly force these patients to use only their specialty pharmacy and prevent consumers from using their trusted local specialty pharmacy. As these specialty patients are considerably more vulnerable and typically utilize rather complex and expensive treatments, and are more dependent on the services of their community pharmacist, increases in price and diminished service and choice will especially harm this group of consumers.

<u>The Federal Trade Commission ("FTC") is thoroughly investigating this merger and should challenge it because it raises significant threats to competition.</u> The anticompetitive effects and resulting consumer harms which I would like to emphasize include:

- <u>Higher Prices and Reduced Service:</u> This merger will reduce the number of major PBMs from three to two. The diminished competition in the PBM market will allow PBMs to charge plan sponsors more for their services, as well as reduce the quality or variety of their ancillary services. Both results would ultimately be felt by consumers in the form of higher cost health plans and drugs;
- <u>Forcing Consumers into Mail Order/ Denying Patient Choice:</u> With an increased incentive and ability to force consumers into their captive mail-order and specialty pharmacy operations, Express Scripts-Medco will prevent many consumers from using their pharmacy of choice. Some consumers favor the convenience and superb service of their community pharmacy and others prefer the convenience of one stop shopping at a supermarket pharmacy. Mail order fails to provide many consumers with the necessary level of service and counseling.
- <u>Degrading Pharmacy Access and Service:</u> Express Scripts-Medco will have the ability to drive reimbursement to pharmacies down below competitive levels. Cutting reimbursement to pharmacies which already operate on very minimal margins would force many pharmacies to respond by raising prices or cutting

[2] Express Scripts and Medco have already force patients into their captive pharmacy operations leaving many consumers with complaints of reduced choice as well as poor service. Consumers can share these complaints on the "Share Your Story" page of www.PBMWatch.com.

back on hours, services, and employees. In the end, consumers would be harmed by less access, diminished service, and higher prices.

In addition to taking into account the potential harm to consumers that may result from this particular transaction, I call on the FTC to go beyond this merger and investigate the presence of anticompetitive conduct in the PBM market. The major PBMs' dominance is preserved through a series of exclusionary arrangements that diminish competition and harm consumers with decreased service and higher prices. Further competition and consumer protection enforcement action is necessary to prevent the substantial ongoing harm in this market. This subcommittee should call on the FTC to act.

I. A Broken Market.

PBMs are like other healthcare intermediaries that manage transactions by forming networks and transferring information and money. As a former antitrust enforcer I know that the fundamental elements for a competitive market are transparency, choice and a lack of conflicts of interest. This is especially true when dealing with health care intermediaries such as PBMs and health insurers where information may be difficult to access, there are agency relationships and securing adequate information may be difficult.

Why are choice, transparency, and a lack of conflicts of interest important? It should seem obvious. Consumers need meaningful alternatives to force competitors to vie for their loyalty by offering fair prices and better services. Transparency is necessary for consumers to evaluate products carefully, to make informed choices, and to secure the full range of services they desire.[3] In both of these respects the PBM market is fragile at best. There is certainly a lack of choice especially for those plans that are dependent on the top tier big three PBMs (Medco, Express Scripts and CVS Caremark). And PBM operations are very obscure and a lack of transparency makes it difficult for plans including government buyers to make sure they are getting the benefits they deserve.

When dealing with intermediaries, it is particularly critical that there are no conflicts of interest. A PBM is fundamentally acting as a fiduciary to the plan it serves. The service a PBM provides is that of being an "honest broker" bargaining to secure the lowest price for drugs and drug dispensing services. When a PBM has an ownership interest in a drug company or has its own mail order or specialty pharmacy dispensing operations, it is effectively serving two masters and may no longer be an "honest broker."

Finally, where these factors – choice, transparency and lack of conflicts of interest are absent – often regulation is necessary to fill the gap. And Congress has enacted some regulation that provides a degree of transparency under the Affordable Care Act. But unlike other aspects of the healthcare delivery system, PBMs remain basically unregulated.

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[3] Leading consumer groups have come out in support of legislation requiring greater transparency of PBMs. *See* Consumer Federation of America, U.S. PIRG, and NLARx letter to Congresswoman Nancy Pelosi in support of Representative Weiner's amendment to H.R. 3200, requiring transparency by PBMs who contract with health plans in the national insurance exchange or with public plans (August 20, 2009).

What is the result of this dysfunctional market? PBMs entered the health care market as "honest brokers" or intermediaries between heath care entities. However, the role of the PBM has evolved over time and increasingly PBMs are able to "play the spread" – by not fully sharing the savings they secure. As a result PBM profits have skyrocketed. From 2003 to 2010, the three largest PBMs—Medco, CVS Caremark and Express Scripts— have seen their profits increase by almost 600% from $900 million to almost $6 billion (see Figure-1).

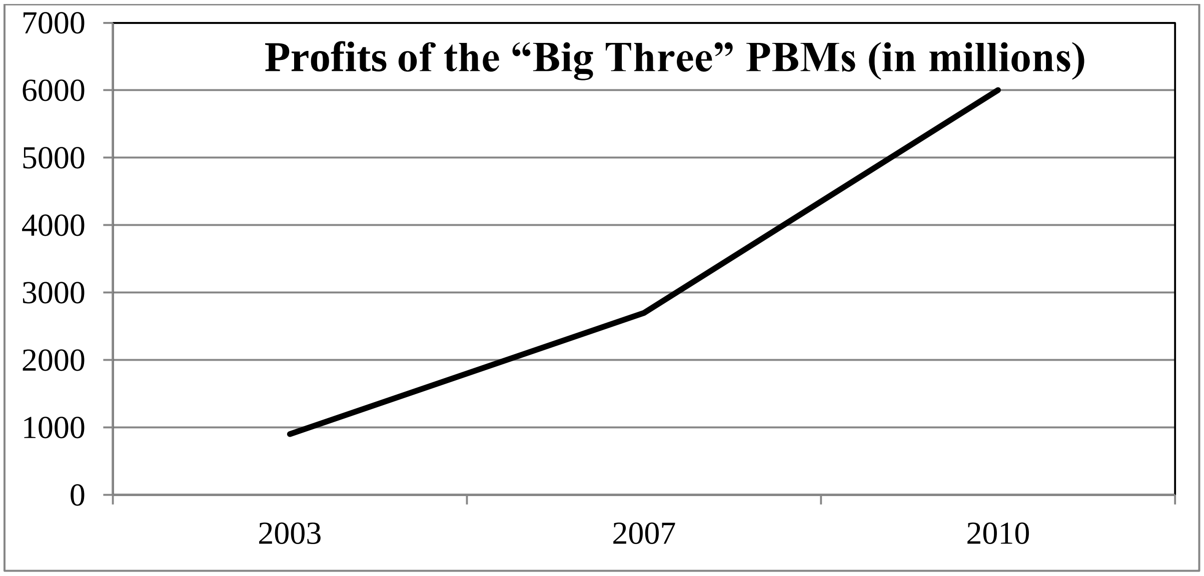

Figure-1

Facing weak transparency standards, the big three PBMs frequently engage in a wide range of deceptive and anticompetitive conduct that ultimately harms and denies benefits to consumers. Some PBMs secure rebates and kickbacks in exchange for exclusivity arrangements that may keep lower priced drugs off the market. PBMs may switch patients from prescribed drugs to an often more expensive drug to take advantage of rebates that the PBM receives from drug manufacturers. In addition, PBMs derive enormous profits from the ability to "play the spread" between pharmaceutical manufacturers, pharmacies, and health care plans. In the past 6 years alone, a coalition of over 30 state attorneys general have brought several cases attacking unfair, fraudulent and deceptive conduct. Between 2004 and 2008, the three major PBMs have been the subject of six major federal or multidistrict cases over allegations of fraud; misrepresentation to plan sponsors, patients, and providers; unjust enrichment through secret kickback schemes; and failure to meet ethical and safety standards. These cases resulted in over $371.9 million in damages to states, plans, and patients so far.

There are three very important lessons here: (1) the fundamental elements of a well functioning market are absent; (2) plans and consumers have already suffered substantial harm from deception, fraud and other egregious practices: and (3) we should be skeptical of claims of cost savings in an environment where profits are skyrocketing.

II. Health Plan Sponsors and Ultimately, Consumers Will Be Harmed by the Merger

Everyone acknowledges there is currently a top tier of PBMs that are the core to competition in the market. The key to PBM operations is exploiting the economies of scale they secure through size. If this merger is not challenged Express Scripts would become phenomenally larger than the remaining PBMs – it will have 155 million covered lives, over 70 million more than the next biggest PBM, CVS/Caremark. The second tier PBMs are far smaller (see Figure-2).

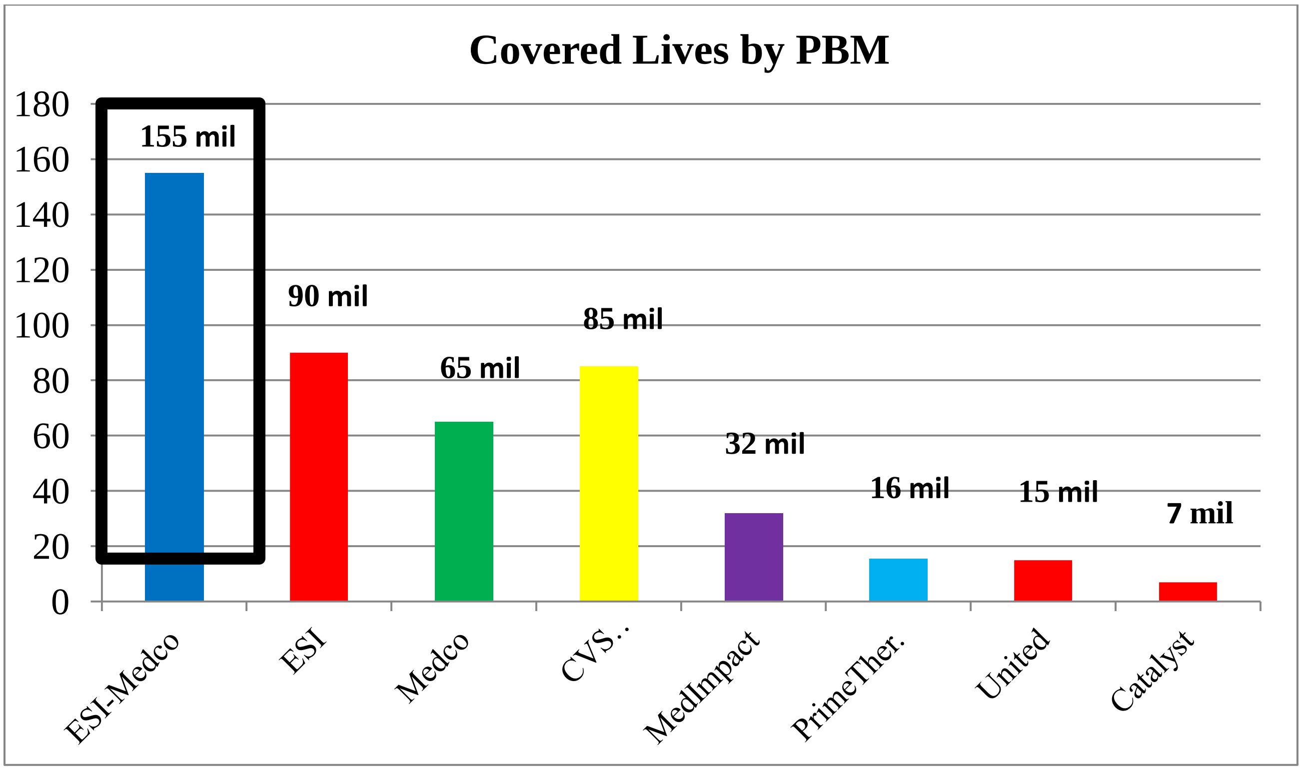

Figure- 2

CVS Caremark, Express Scripts, and Medco make up this top tier and serve a majority of the largest plan sponsors. In fact, over 40 of the "Fortune 50" largest corporations rely on these big three for PBM services. A significant number of employers, unions and health plans view the three major PBMs as their only viable options. Therefore, when one of the major PBMs loses a large contract it is almost always picked up by another of the three. Since the Caremark/Advance PCS merger, there is no evidence that second tier PBMs have taken market share from the big three. Tom Dressler, a board member for the California Public Employees' Retirement System (Calpers), the country's largest pension fund, spoke to this dependence and said, **"'You can count the PBMs that can serve the organizations of this size on a couple of fingers, maybe three,' and they frequently are subject to lawsuits and investigations."**[4]

[4] Brin, Dinah. "CVS, Seeking Calpers Pact, Faces Trial Over Past Work for Fund." *The Wall Street Journal*, (May 18, 2011). *Available at* http://online.wsj.com/article/BT-CO-20110518-711687.html.

For those plan sponsors that depend on the big three PBMs, this merger would reduce the number of viable alternatives from three to two—a significant loss of competition. While some will claim that the second tier will serve as a sufficient price constraint on the remaining two PBMs, this assertion is misguided. As concluded by the American Antitrust Institute on this point,

> The three national full service PBMs already have significant cost advantages from economies of scale and from vertical integration in mail order and specialty pharmacy distribution. When faced with these difficult entry and expansion barriers, the remaining second tier PBMs cannot adequately constrain potential anticompetitive conduct because of their smaller size, geographic limitations, lack of buyer power, and, in some cases, perceived conflicts regarding their corporate affiliation with large plan sponsors.[5]

There are seven main distinctions that prevent the second-tier PBMs from effectively constraining the big three, including:

- Reduced Purchasing Power: Because of their size, smaller PBMs wield less negotiating power with drug manufacturers than the big three. The second tier is therefore unable to secure comparable levels of rebates and to effectively compete on price.
- Less Control of Pharmacy Reimbursement: Second-tier PBMs also have less negotiating power with retail pharmacies and are to secure as low reimbursement rates as the big three.
- Mail Order: Second tier PBMs generally do not have their own mail-order pharmacy operations and if they do, their operations function at a higher cost.
- Specialty Pharmacies: Unlike Express Scripts and Medco who operate the two largest specialty pharmacy businesses, respectively, Curascript and Accredo, second-tier PBMs typically do not have in-house specialty pharmacy operations.
- Claims Processing: Second-tier PBMs generally have much less capacity for claims processing.
- Clinical Management Services: The big three PBMs compete on several services, among them the management of the utilization of covered medications by balancing clinical effectiveness with costs; providing clinical cost containment programs for large plan sponsors; and providing sophisticated service innovations and clinical tools aimed to encourage the best clinical outcomes for patients. These services are most effective when supported by a large number of

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The dependence on the three national PBMs is also highlighted by the California Public Employees' Retirement System's (CalPERS) recent decision to sign a contract with CVS Caremark, despite allegations that the PBM had defrauded the pension fund. Lifsher, Marc. "CalPERS Signs Pharmacy Benefits Deal with CVS Caremark." *Los Angeles Times* (June 21, 2011).

[5] American Antitrust Institute. Letter to Chairman Leibowitz regarding the Proposed Merger of Express Scripts, Inc. and Medco Health Solutions (November 30, 2011).

covered lives. Second-tier PBMs generally lack the resources or scale to offer these services.

- Reputation: Because of the cost and complexity of the relationship, health plans simply cannot afford to risk contracting with a PBM that may lack the capacity or experience to manage an account of their size. Accordingly, health plans often rely extensively on reputation and reference accounts of a certain size when making PBM contracting decision. Thus, second-tier PBMs often find themselves in a catch-22, needing more large contracts in order to prove their capacity to earn more contracts.

Under the antitrust laws, firms are included in a relevant market to the extent they constrain the ability of the merged firm to raise prices. Just because some firms provide similar services does not mean they are all included in the relevant market. As the courts have observed "the mere fact that a firm may be termed a competitor in the overall marketplace does not necessarily require that it be included in the relevant product market for antitrust purposes."[6]

Not only does the second tier fail to serve as an effective constraint on the big three PBMs as of now, but the proposed merger will exacerbate the gap between tiers and make it even more difficult for these smaller PBMS to compete.

For plan sponsors that depend upon the big three PBMs, this merger is a consolidation from three firms to two. The effects of the merger, therefore, would significantly harm large purchasers of PBM services and ultimately, their plan participants—the ultimate consumers—in three ways.

First, the market will immediately lose a major competitor. Medco's presence directly constrains the ability of Express Scripts and CVS/Caremark to raise prices, eliminate services, or mismanage the handling of beneficiaries' pharmaceutical benefit services.

Second, the merged entity will inherit a dominant market position. This may result in an increase in price or degradation of services. The services that PBMs provide plan sponsors are often overlooked in the discussion of this merger, but are very important, and are the direct result of head-to-head competition among the big three. Following the merger, there will be less need for competition, and less incentive for the merged firm to continue offering as many ancillary services.

Third, the big three already impose exclusive networks on plan sponsors, and require them to fulfill mail order and specialty services through their own subsidiaries. The merged entity will have even more incentive, and even more power, to engage in this exclusionary conduct. Plan sponsors may soon see their choices limited by Express Scripts/Medco, and find themselves with little recourse.

[6] Federal Trade Commission v. Cardinal Health, Inc., 12 F.Supp.2d 34, 45 (D.D.C. 1998). (Quoting Federal Trade Commission v. Staples, Inc., 970 F. Supp. 1066, 1075-1076 (D.D.C. 1997)).

III. Pharmacy Access and Service Will Be Harmed

The proposed merger will harm consumers by increasing the ability for Express Scripts to force patients into their captive drug distribution operations, and exercise monopsony market power over retail pharmacies.[7] The three major PBMs have strong incentives to make customers use their wholly-owned mail order pharmacy operations. Accordingly, the major PBMs often restrict network options to drive consumers to their operations.

An Express Scripts-Medco will control over 40 percent of prescription drug volume.[8] With increased dominance in both the PBM and mail-order spheres, the merged firm will be better positioned to restrict patient choice in pharmacy and force consumers into mail-order. Mail-order may be more costly, may result in significant waste, and fails to provide the level of convenience and counseling that many consumers require. Consumers may have existing relationships with a community pharmacy and may not wish to leave the pharmacist they know and trust to be served by a mail order robot. Others simply enjoy the ability to one-stop-shop and prefer the convenience of their supermarket pharmacy. The bottom line is that patients have a whole array of preferences when it comes to pharmacy care and consumers are left worse-off when they are unable to choose the level of service they desire.

This merger will also harm consumers as it would allow the remaining two national PBMs to shrink the number of community pharmacies. By lowering reimbursement to community pharmacies, the big three PBMs already make it difficult for these high-value health

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[7] Courts and enforcement agencies recognize the consumer harm that may result from granting or enlarging monopsony power. *See, e.g.* North Jackson Pharmacy Inc. vs. Caremark Rx, Inc. 385 F. Supp. 2d 740, 749 (N.D. Ill. 2005) (explaining "The exercise of [monopsony] power causes competitive harm because the monopsonist or the group will shift some purchases to a less efficient source, supply too little output to the downstream market, or do both."); United States v. UnitedHealth Group Inc. and PacifiCare Health Systems Inc. Case No. 1:05CV02436 (D.D.C. 2006) (holding that the merger of two health insurance companies would result in anticompetitive in the purchase of physician services. The Department of Justice's Competitive Impact Statement alleged "Since physicians have a limited ability to encourage patient switching, the merger will significantly increase the number of physicians in Tucson and Boulder who are unable to reject United's demands for more adverse contract terms. Thus, the acquisition will give United the ability to unduly depress physician reimbursement rates in Tucson and Boulder, likely leading to a reduction in quantity or degradation in the quality of physician services."). Current scholarship also supports the notion that monopsony power poses potential harm to consumers. For instance, former Assistant Director at the Federal Trade Commission John B. Kirkwood's most recent article concludes that antitrust policymakers should recalibrate their analysis of monopsony in merger review, and argues they should "protect small, competitive sellers from monopsonistic exploitation." Kirkwood also distinguishes the FTC's statements regarding the Caremark and Advance PCS merger, challenging the idea that an increase in buying power is a countervailing benefit, and not a presumptively anticompetitive effect. Kirkwood explains that the idea of increased buying power constituting a procompetitive benefit only applies when the result is a bilateral monopoly, and requires three assumptions: the selling entity has market power, transactions costs prevent parties from reaching efficient outcomes otherwise, and monopsonists can increase supply through demand, which will have a collateral procompetitive impact on price. However, when these assumptions are not met, the benefit of increased buying power is lost. In this case, there is no pharmacy side monopoly power, or reason to believe that the monopsonists will increase supply through demand, since patients and not PBMs provide the supply (and in fact the demand is likely to decrease, since ESI will channel more sales through their own captive mail-order pharmacy. *See* John B. Kirkwood, Buyer Power and Merger Policy, at 57-60, *available at* http://ssrn.com/abstract=1809985.

[8] Letter from Senator Harkin to Jon Leibowitz regarding the proposed Express Scripts, Medco merger (October 17, 2011).

care providers to survive. The transaction would exacerbate this trend, and result in community pharmacies lessening their services or, worse – closing their doors.

Express Scripts and Medco portray this as a benefit of the merger. They claim they are lowering consumer prices by allowing them to pay less for drugs. But does this argument hold water? First, the PBMs skyrocketing profits suggests that the benefits from restricted networks may not benefit consumers, but rather, the PBMs themselves. Second, reduced reimbursement is not necessarily good for consumers, especially in healthcare markets. When monopsony power forces healthcare providers to accept less money for services, it is likely that the consumer will suffer through a lessening of quality of service. As the Third Circuit explained in a case alleging that an insurer (Highmark) reduced reimbursement to a hospital (West Penn). The insurer argued that there was no problem because lower reimbursement would lead to lower premiums, but the Court rejected the argument:

> [E]ven if it were true that paying West Penn depressed rates enabled Highmark to offer lower premiums, it is far from clear that this would have benefitted consumers, because the premium reductions would have been achieved only by taking action that tends to diminish the quality and availability of hospital services.[9]

The market power resulting from the proposed merger will harm consumers as it will allow the remaining two PBMs to decrease compensation to retail pharmacies below competitive levels. Why should consumers care? Because their community pharmacist is the most trusted professional they deal with. Because retail pharmacies provide consumers with valuable clinical services and counseling, often free of charge. Because some pharmacies, especially supermarket pharmacies, offer drugs at lower prices than the PBMs, such as through $4/month generic programs. Anticompetitive cuts to reimbursement jeopardize these types of programs that consumers highly value. As retail pharmacies are already economically efficient and operate on very minimal margins, these cuts to pharmacy reimbursement would, in the end, likely result in harm to consumers.

IV. Specialty Pharmacy Patients Will Face Reduced Service and Higher Costs

The anticompetitive impact of this merger on prices, service, and consumer choice are particularly profound for the thousands of patients suffering from hemophilia, HIV/AIDS, Crohn's Disease, multiple sclerosis, hepatitis, infertility, and many form of cancer, who require specialty pharmaceuticals. This merger would combine the two largest specialty pharmacy businesses, Express Scripts' Curascript and Medco's Accredo, giving the joint company a 52 percent share of this market (see Figure-3). This incredible consolidation of the specialty market is of particular concern given the fact that specialty drugs are expected to be the single greatest cost-driver in pharmaceutical spending over the next decade. The cost of specialty drugs is rising rapidly—increasing by 19.6 percent in 2010 and expected to reach as high as 27.5 percent by 2013.[10] Meanwhile, by 2016, 8 of the top 10 prescription drugs are expected to be specialty.[11]

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[9] West Penn Allegheny Health System, Inc. v. UPMC, 627 F. 3d 85(3rd Cir. 2010).
[10] Express Scripts. *2010 Drug Trend Report: A Market and Behavioral Analysis* (April 2011).

Specialty pharmacies manage the highly-expensive and very complex treatments for the most intricate and serious illnesses. The service they provide is both distinct and significant from other retail pharmacies. Beyond merely dispensing drugs, specialty pharmacies help administer complex treatments, assist physicians in monitoring patient therapy, and play an important role in medication compliance and improved health outcomes. Specialty pharmacies educate patients on effective utilization, monitor side effects, and partner with physicians to identify ineffective medications and recommend treatment changes. Specialty pharmacies play an active role in providing continuity of patient care to ensure that costs are minimized and health outcomes improve.

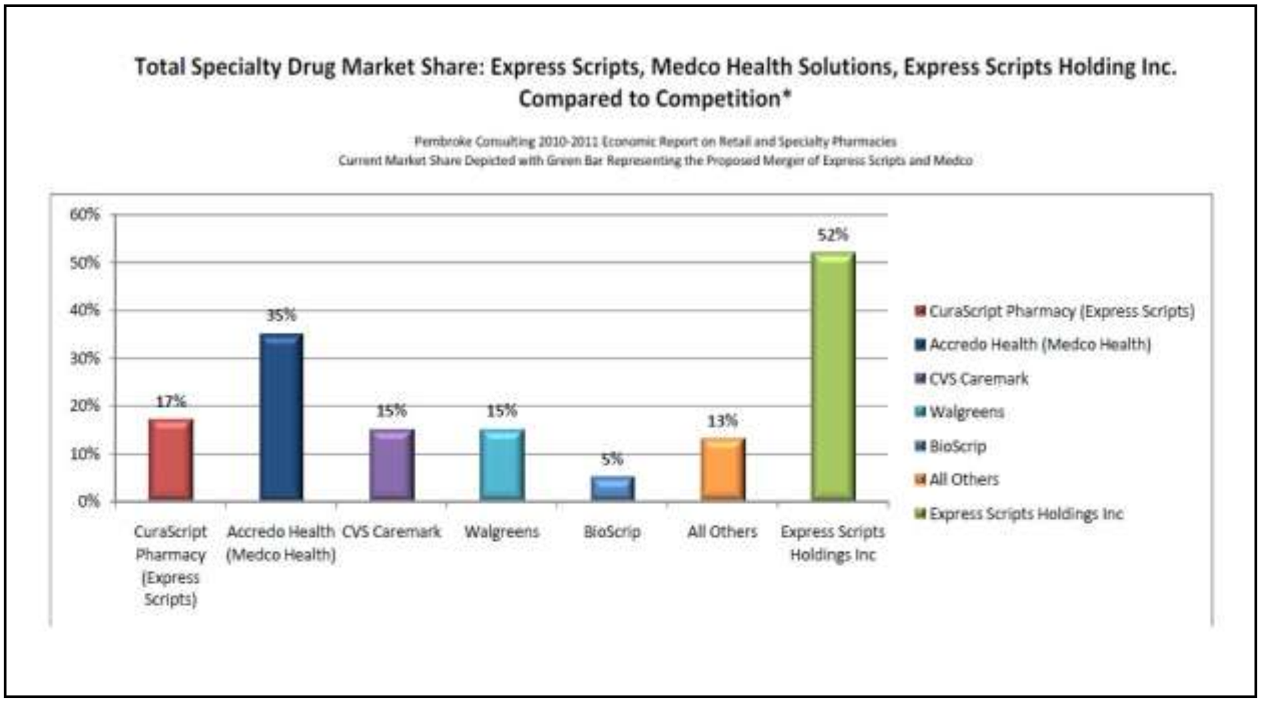

Figure- 3

The ownership of specialty pharmacies creates the conflict of interest problem described earlier. At times, these PBMs have used their market clout to extract exclusivity arrangements from manufacturers significantly increasing the price of drugs. Take the case of H.P. Acthar Gel, a drug for severe epilepsy whose price jumped from $1,600 a vial to $23,000 after Express Scripts was named the sole distributor.[12] These PBMs have also created exclusive specialty networks to prevent retail pharmacies in their network from dispensing specialty drugs. Express Scripts and Medco in particular steer plan participants towards their captive specialty pharmacy (which in turn forces the plan participants to use the PBM's captive mail order facility).

[11] Medco Health Solutions. *2011 Drug Trend Report.* (2011).
[12] Freudenheim, Milt. "The Middleman's Markup." *The New York Times* (April 19, 2008).

Restrictive networks and steering practices rob consumers of the choice to use their preferred pharmacy and method of distribution; and—with this important rivalry gone– consumers also miss out on the benefits of vigorous competition including lower prices and improved service. These restrictive networks deny patients a choice in provider and, given the high-touch nature of services in this area, this choice is highly valued by many consumers. As both Express Scripts and Medco control sizable specialty pharmacy operations, their combination necessarily presents potential harm to consumers that depend on the high-cost products and services that are of great, and even life-altering, significance to patients in the specialty drug market.

Restricting networks can also lead to disruptions in the continuum of care which degrade health outcomes and increase healthcare costs. Patients on specialty drugs often require regular contact and counseling from their pharmacist (who is often assisted by a nurse). For many disease states, the pharmacist and nurse regularly contact the patient to make sure the drug is properly administered, taken on time, and the drug is working effectively. Disrupting this patient-provider relationship in complex and expensive treatment of very sensitive health conditions imposes significant harm to both the consumer and the health plan. Many patients have been harmed by inadequate care from these restrictive pharmacy networks[13] and that has led patient advocacy groups, such as the Hemophilia Federation of America, to publicly oppose such network designs.[14]

With even greater dominance in the upstream PBM market, a merged Express Scripts-Medco will have an increased incentive and ability to engage in this anticompetitive practice of restricting networks and forcing patients to their own specialty businesses. These restrictive networks, likely to increase post-merger, threaten to restrict patient choice, lead to disruptions in care, increase specialty drug prices, and limit patient's access to critical medications.

V. Efficiencies Do Not Outweigh the Potential Harm to Consumers

Express Scripts' and Medco's proffered efficiencies do not pass antitrust scrutiny, and certainly do not satisfy the burden of outweighing the above-described anticompetitive effects of the transaction. Antitrust law only recognizes efficiencies that are cognizable, verifiable, and merger-specific. The Merger Guidelines provide that "efficiency claims will not be considered if they are vague, speculative, or otherwise cannot be verified by a reasonable means" and "cognizable efficiencies are merger-specific efficiencies that have been verified and do not arise from anticompetitive reductions in output or service."[15] The Supreme Court has never condoned the notion that an otherwise anticompetitive merger can be legally procompetitive based solely on the efficiencies created. Although lower courts have embraced this theory, they have also noted that in cases of extreme market consolidation, such as would occur from Express Scripts' acquisition of Medco, defendants must demonstrate "proof of extraordinary efficiencies."[16] The

[13] Kimes, Mina. "The decline of the specialty pharmacy." *Fortune* (October 25, 2010).
[14] Hemophilia Federation of America. "HFA Statement of Position." http://hemophiliafed.org/old-list/single-source-provider.
[15] MERGER GUIDELINES § 10.
[16] Federal Trade Commission v. HJ Heinz Co., 246 F. 3d 708, 720 (D.C. 2001).

Guidelines support this proposition, stating "when the potential adverse competitive effect of a merger is likely to be particularly substantial, extraordinarily great cognizable efficiencies would be necessary to prevent the merger from being anticompetitive."[17] Merging parties with large market shares in a constrained market have a stiff burden to overcome to survive scrutiny under the Clayton Act. The parties at hand fail to overcome this burden.

Federal Courts have already addressed the question of whether, and to what extent, the burden of demonstrating an "extraordinary" efficiency is satisfied in a merger to duopoly in which the combined firm proffers to benefit consumers through additional cost savings. In *Federal Trade Commission v. Cardinal Health, Inc*.[18] the Federal District Court for the District of Columbia considered whether increased buying power through the merger of national drug wholesalers constituted a cognizable efficiency sufficient to offset competitive concerns. The court concluded that the benefits did not outweigh the concerns, concluding that the savings were not likely to be passed on to consumers, and that the efficiencies were not specific to the merger. The court, in finding for the FTC, explained "much of the savings anticipated from the mergers could also be achieved through continued competition in the wholesale industry. While it must be conceded that the mergers would likely yield the cost savings more immediately, the history of the industry over the past ten years demonstrates the power of competition to lower cost structures and garner efficiencies as well."[19]

The efficiencies offered by the combining firms can be boiled down to two basic arguments: the merger will increase Express Scripts' buying power, and therefore enable it to better control healthcare costs; and the combined firm will be able to implement a series of clinical management programs to oversee the quality of care. Neither of these proposed efficiencies is cognizable or merger-specific.

Express Scripts' contention that it will pass on saving to consumers does not satisfy antitrust concern. The law readily recognizes that cost savings must be passed on to consumers to count as a countervailing efficiency. With only two competitors left in the market, there is no guarantee that the savings will be passed on to consumers. As noted earlier the big three PBMs are among the most profitable companies in America. Annual profits for these companies skyrocket annually, suggesting they are not passing on the savings to consumers as they say they will. Federal Courts have acknowledged the likelihood of merging parties to reap higher profits rather than sharing the savings with consumers, stating "while reducing the costs of doing business provides several advantages for the merged firm, these advantages could show up in higher profits instead of benefiting customers or competition."[20]

The argument that Express Scripts will harness its augmented buying power to the benefit of the consumer is not a cognizable efficiency sufficient to overcome the presumption of anticompetitive effects from the merger. Both Express Scripts and Medco already have massive buying power. Either of these firms controls enough of the market that they could unilaterally

[17] MERGER GUIDELINES § 10.
[18] 12 F.Supp.2d 34 (D.D.C. 1998).
[19] *Id.* at 63.
[20] F.T.C. v. CCC Holdings, 605 F. Supp. 2d 26, 74 (D.D.C. 2009).

seek this improved price, or could seek to improve their negotiating position through internal growth rather than merger.

The policies and programs that Express Scripts aims to implement are neither cognizable nor merger-specific. To date, Express Scripts never explained how the merger would actually facilitate the creation of these programs where they do not already exist, or why they have been unable to do so before now. With the current three-firm top tier PBM structure, competition compels these firms to invest in such programs. It is more likely that we would lose these beneficial programs, rather than gain them, after the consummation of the merger. The Merger Guidelines provide for analysis in situations in which the consumer gains a nominal benefit in price reduction, but suffers an overall loss in quality of service, providing "purported efficiency claims based on lower prices can be undermined if they rest on reductions in product quality or variety that customers value."[21]

VI. Conclusion

By severely diminishing competition in the PBM market, the proposed merger of Express Scripts and Medco stands to impart significant harm on healthcare consumers. In the form of higher priced health plans and drugs, plan participants will bear the cost of the competition lost for large plan sponsors. As reimbursement is driven below competitive levels for pharmacies, the pharmacy access and service many consumers value will degrade. And with increased dominance, the joint-firm will continually deny patient choice by forcing consumers, including specialty patients with complex therapy needs, away from the service they trust into inferior mail order programs. The Federal Trade Commission should challenge the proposed transaction because it raises significant threats to competition and accordingly, the interests of American consumers.

[21] MERGER GUIDELINES § 10.

Appendix
Related Testimony on Pharmacy Benefit Managers

David Balto, Testimony before Department of Labor on Fee Disclosures to Welfare Benefit Plans (Dec 7, 2010). *Available at* http://www.dol.gov/ebsa/pdf/1210-AB08-CAPAF.pdf.

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