February 2, 2012

The Honorable Jon Leibowitz
Chairman
Federal Trade Commission
600 Pennsylvania Avenue, NW
Washington, D.C. 20580

Re: Food Marketing Institute's Concerns Regarding the Proposed Acquisition of Medco Health Solutions by Express Scripts, Inc.

Dear Chairman Leibowitz:

We appreciate the opportunities we have had to bring seven of the largest supermarket chains before the Federal Trade Commission (FTC or Commission) Staff to talk about the significant adverse impact the proposed acquisition of Medco Health Solutions (Medco) by Express Scripts, Inc. (Express Scripts) will have on supermarket pharmacies and their consumers. We write to you on behalf of the Food Marketing Institute (FMI), to fully explain the importance of supermarket pharmacies in the delivery of pharmacy and health care services, detail the harm supermarket pharmacies will incur post-merger and ask the Commission to bring an enforcement action to enjoin the merger.[1]

Food Marketing Institute is the leading voice in the food industry with a significant presence in retail pharmacy around the country. FMI members dispense well over 30% of all prescription drugs in the United States, and the seven chains interviewed by the Commission dispense over 20% of the drugs in the nation. FMI conducts programs in public affairs, food safety, research, education and industry relations on behalf of its nearly 1,250 food retail and wholesale member companies in the United States and around the world. FMI's U.S. members operate more than 25,000 retail food stores and almost 22,000 pharmacies with a combined annual sales volume of nearly $650 billion. FMI's retail membership is composed of large multi-store chains, regional firms and independent operators. Its international membership includes 126 companies from more than 65 countries. FMI's nearly 330 associate members include the supplier partners of its retail and wholesale members.

Specifically this paper explains that:

[1] FMI previously wrote to Chairman Leibowitz urging the Commission to carefully analyze the merger. *See* letter from Erik R. Lieberman, Regulatory Counsel for FMI to Chairman Jon Leibowitz, September 1, 2011.

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- Supermarket pharmacies are a vital competitive force in drug distribution offering the lowest cost drug options to millions of consumers. Additionally, supermarket pharmacies offer convenient one-stop-shopping for consumers and are on the cutting edge of counseling and in-patient health care services.

- The merger will harm supermarket pharmacies by significantly reducing reimbursement rates and forcing supermarket pharmacy patients to Express Scripts' captive mail-order pharmacy. Severe reductions in reimbursement and forced mail-order will result in increased drug prices, reduced generic substitution, decreased consumer choice and access to preferred pharmacy care, and lead to substantial decreases in the hours of operations and number of employees available to service patients, harming the level and quality of health care services for consumers.

- Bringing an enforcement action to enjoin the merger is consistent with past antitrust agency enforcement precedent.

Supermarket Pharmacies Play a Vital Role in the Health Care of American Consumers

Supermarket pharmacies have an increasingly important role in improving the health care of American consumers. First, supermarket pharmacies are among the most efficient and lowest cost competitors in the pharmacy market. Every day hundreds of supermarket pharmacies offer $4 a month or reduced price generic drug programs, discounted 90-day drugs supplies and free antibiotics and vaccinations. Some supermarket chains have free generic drug programs for low income consumers. These programs save consumers significant amounts of money and allow uninsured and underinsured individuals and patients on fixed incomes access to vital generic drugs. The undisputed fact is that supermarket pharmacies are able to provide lower cost drugs to patients than other retailers and PBMs. PBMs simply are not the lowest cost and most efficient form of drug distribution.

Second, as the Commission has learned through the interviews, supermarket pharmacies operate extremely efficiently. Supermarkets traditionally operate at very low margins, obligating pharmacies to operate as efficiently as possible, at very thin margins.[2] The vast majority of supermarket pharmacies warehouse their own prescription inventory, saving significant amounts of money and costs for their patients. Additionally, many supermarket pharmacies have direct buying relationships with pharmaceutical manufacturers substantially reducing costs associated with buying through drug wholesalers. The efficient operations allow supermarkets to provide the best pricing to pharmacy customers.

[2] Supermarket pharmacies also operate as separate profit centers accounting for 10-12% of supermarket revenues.

Third, supermarket pharmacies are the vanguard of pharmacy health care service offerings. Supermarkets have innovative and unique approaches to patient counseling, including advice on nutrition to accompany medication regimens. Supermarkets are a convenient one-stop-shop for consumers. Because the average grocery store shopper visits the supermarket at least once a week versus once a month for a traditional drugstore, the supermarket pharmacist has the opportunity to interact with patients much more often than in other retail pharmacy settings.[3] The convenience of accessing supermarket pharmacies is emphasized by the wide array of in-store programs and services designed to improve health care of their patients. Examples of these health care services include:

- Medical therapy management (including diabetes and osteoporosis management),
- medication counseling,
- blood pressure monitoring and other screening programs,
- prescription compounding and delivery,
- medical equipment training,
- patient specific education programs (including smoking cessation and medication adherence programs),
- in-store clinics,
- nutrition counseling (including store tours and health focused recipes),
- 340B drug programs,
- flu shot and other vaccinations and immunizations.[4]

These services and low cost drug alternatives are vital to consumers who rely on their supermarket pharmacies for significant contributions to improving health and wellness.

The Merger will Cause Significant Harm to Supermarket Pharmacies and Their Customers

The merger of Express Scripts and Medco will create a dominant PBM with the ability to drive reimbursement to pharmacies significantly below competitive levels and force consumers away from retail pharmacy to its in-house mail-order pharmacy operations. It will harm proper patient care and adequate pharmacy access, and lead to increased drug prices and decreased consumer choice in pharmacy care. The merger will allow the dominant PBM to control approximately 40 percent of the overall prescription drug volume in the United States,[5] resulting in a dominant purchaser of supermarket pharmacy services and the largest mail-order pharmacy in the nation.

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[3] Barbara Sax, "Supermarkets Offer Patients Accessible Pharmacy Services," Pharmacy Times (Oct. 21, 2010).
[4] Id.
[5] Letter from Senator Harkin to Jon Leibowitz regarding the proposed Express Scripts, Medco merger (October 17, 2011).

First, supermarket pharmacies face the threat of reduced reimbursement levels post-merger. As the FTC has learned in interviews with supermarkets, for any individual chain, Express Scripts and Medco account for at least 30-40% of supermarket pharmacy revenues. For most of these supermarkets if Medco rates alone are reduced to the level of Express Scripts rates, there will be a loss of $10-50 million per year in revenue.[6] Practically every supermarket chain stated that this will lead to profound consequences on consumers, particularly reductions in pharmacy hours and staffing, longer patient wait times, decreases in health care services and counseling, and the end to $4 generic drug programs and free antibiotics. In some cases, supermarkets will have to consider closing pharmacies.

The impact on the vital services provided by the supermarket pharmacies will be just as profound. In the course of the supermarket chain interviews, the Commission has heard numerous examples of the specific harm reduced reimbursement rates may cause and the effects it could have on consumers.

- Some supermarket chains may be forced to cut or eliminate the low-cost $4 generic programs that many consumers rely on, which are often lower than the cost of consumers' co-pays.
- One chain could be forced to cease offering free generic drugs, of which it currently fills 6.5 million per year.
- Another chain most likely would no longer be able to service TRICARE patients in a specific region of the country.
- Another chain may be unable to continue its diabetes counseling and HIV excellence community outreach programs furthering potential risk of non-adherence to vital drug regimens.
- Other chains reported that they would likely have to significantly scale back on patient-pharmacist interaction and therapeutic counseling. The health care services provided could not be possible without a work flow model that ensures pharmacists have enough time to spend counseling their patients.[7]

Reduced reimbursement will significantly impact supermarket pharmacies' staffing abilities and hours of operation, impacting the vital counseling and therapeutic services supermarket pharmacy patients rely on.

Express Scripts may attempt to justify reduced reimbursement suggesting it will lead to lower costs for PBM services and ultimately lower insurance premiums. But this is clearly inconsistent with the facts and the law. Express Scripts has increased its buying power through past acquisitions and there is little evidence that increased buying power led to lower costs for PBM services or lower premiums. And Express Scripts is wrong

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[6] The supermarket interviews documented that Express Scripts has significantly lower reimbursement than Medco.

[7] Barbara Sax, *Supermarket Offer Patients Accessible Pharmacy Services*, Pharmacy Times (Oct. 21, 2010).

on the law, as observed by a recent Third Circuit decision.[8] In that case, an insurer (Highmark) argued that there was no problem from alleged anticompetitive conduct that reduced reimbursement because lower reimbursement to a hospital (West Penn) would lead to lower premiums. The court rejected the argument holding that 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:

> [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]

Second, with increased dominance in both the PBM and mail-order spheres, Express Scripts will be better positioned to restrict patient choice in pharmacy and force consumers into PBM-owned mail-order. Express Scripts and Medco have the largest mail-order facilities in the United States, accounting for the vast majority of prescriptions filled through mail-order. Post-merger Express Scripts will have incentive and ability to force more consumers into their captive mail-order operations as the combined entity will have more leverage to shift plan sponsors and accrue higher revenue at the expense of supermarket pharmacies and the detriment of consumers.

Mail-order may be more costly than retail ultimately harming the health plans and the patients. Mail-order companies typically dispense expensive brand name drugs at greater rates and dispense generic drugs at much lower rates than retail pharmacies.[10] The average generic drug dispensing rate of supermarket pharmacies is 77 %, significantly higher than that of Express Scripts and Medco, which are over 15% lower. Contrary to a combined Express Scripts, whose goal is to increase its bottom line, supermarket pharmacies are incentivized to provide generic drugs as they save consumers on average $8-10 billion a year.[11]

Additionally, mail-order may result in significant waste. Waste is rampant among mail-order pharmacies with an average of 3 days worth of 90-day drugs going unused.[12] Moreover, mail-order fails to provide the level of convenience and counseling that many consumers require. In the supermarket pharmacy setting where it is convenient for consumers to interact with their pharmacists, the drug adherence level is much greater than that of mail-order patients.[13] The harm to consumers will be compounded by the

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[8] West Penn Allegheny Health System, Inc. v. UPMC, 627 F. 3d 85(3rd Cir. 2010).
[9] Id.
[10] 2010-2011 Prescription Drug Cost and Plan Benefit Design Report at 28; see also James Langenfeld and Robert Maness, "The Cost of PBM "Self-Dealing" Under a Medicare Prescription Drug Benefit", September 2003 (PBM-owned mail-order facilities switch to higher-priced drugs more frequently than nonaffiliated mail-order facilities).
[11] Mathew Hupila, 5 Common Questions About Generic Drugs, Consumer Health Information Corporation (2008).
[12] Valarie DeBenedette, "Is Mail-order Pharmacy Waste Rampant," Drug Topics, November 15, 2011.
[13] *See* Troyen A. Brennan et al., An Integrated Pharmacy-Based Program Improved Medication Prescription and Adherence Rates in Diabetes Patients, Health Affairs, 31, no. 1, (2012) 120-129 (2010 study of diabetes patients

merger as Express Scripts expands its mail-order dominance. The merger undoubtedly leaves consumers worse-off when they are unable to choose the level of pharmacy service they desire.

This Merger is Substantially Different from the Merger of Caremark and Advance PCS

The FTC has addressed PBM mergers previously, but none with the buying power clout that a merged Express Scripts-Medco will have. In the merger of Caremark and Advance PCS, the FTC found in closing the investigation that if the merger created any buying power at all, it would be procompetitive bargaining power. The Commission concluded that monopsony power would be unlikely because the merged firm's buying share would be too low.[14] It stated that the proposed acquisition additionally would not confer monopsony power because it was a shift in purchases to a lower-cost, more efficient source.[15] The FTC opined that the increased buying power gained by the merger was likely to benefit purchasers of PBMs services saying that some of the PBMs savings from lower payments to retail pharmacies would be passed through to PBM clients.[16] Express Scripts' acquisition of Medco is distinguishable from the FTC's findings in Caremark/AdvancePCS.

First, the PBM market now is much more concentrated than it was in 2004. The market is dominated by three large PBMs, Express Scripts, CVS/Caremark and Medco, with close to an 80% share of the large employer market. Due to the increased levels of concentration in the PBM market today, the post-merger share of drugs reimbursed by Express Scripts is much higher than the 2004 Caremark acquisition and approximately 40% of supermarket pharmacies' business. The significant buying power Express Scripts will have over supermarket pharmacies will allow it to depress the amount paid for pharmacy services and decrease the quantity of its purchases from supermarket pharmacies. As a direct competitor in the dispensing of prescription drugs over time Express Scripts will decrease the total volume purchased from supermarket pharmacies forcing consumers into its own mail-order pharmacy.

Second, the merger is not a case in which there is a shift of buying power to a more efficient source, but rather the opposite. As the FTC staff has learned in the interviews, supermarket pharmacies are among the most efficient and lowest-cost downstream competitors. Shifting purchases of pharmacy services away from supermarket pharmacies to mail-order is shifting purchases to a less-efficient source. Supermarkets

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found the adherence to medications and use of concomitant therapies were greater in patients who received counseling in retail setting than in those who received phone calls from pharmacists based in mail-order pharmacies).

[14] Statement of the Federal Trade Commission, In the Matter of Caremark Rx., Inc./Advance PCS, 2004 WL 318280 (F.T.C. Feb. 11, 2004).

[15] Id.

[16] Id.

are frequently the lowest priced competitor of numerous drugs, especially generics. The FTC correctly noted in the Caremark/AdvancePCS closing letter "The exercise of [monopsony] power causes competitive harm because the monopsonist…will shift some purchases to a less efficient source, supply too little output to the downstream market, or both."[17] That harm is clearly a threat in this merger.

Third, it is not necessarily the case that the cost savings achieved by the combined firm will benefit consumers as the FTC assumed in Caremark/Advance PCS. When assessing the merger of intermediaries who purport to benefit consumers by driving down costs through aggregated buying power, the merging firm must show that it is likely to pass these savings on to consumers.[18] As a former Assistant Attorney General has observed If such a merger lowers the price the merged firm pays for its inputs, a decline in input prices to suppliers can represent an "efficiency-reducing exercise of market power that will reduce economic welfare, lower prices for suppliers, and may well result in higher prices charged to final consumers."[19] Given the fact that there will be only two competitors remaining in the market, there can be no expectation that competition will force Express Scripts to pass on any savings to consumers, as the courts have found in similar mergers.[20] Moreover, based on the PBM industry's track record for escalating profits, and exploiting conflicts of interest, there is no reason to suspect the merged firm will pass on any substantial portion of the cost savings it is able to generate.

An Enforcement Action to Enjoin the Merger is Consistent with Past Agency Enforcement Actions

The antitrust enforcement agencies have looked at the issues presented here and have scrutinized similar buyer power conduct in recent past health insurance mergers. As with commercial health insurers purchasing physician services for those enrolled in their networks, PBMs purchase pharmacy services from retail pharmacies in the same fashion. The Antitrust Division has brought several enforcement actions against insurance mergers which threatened to depress the reimbursement rates for physician

[17] Id.
[18] FTC v. Cardinal Health, 12 F. Supp. 34 (1998).
[19] R. Hewitt Pate, Asst. Att'y Gen., Antitrust Div., U.S. Dept. of Justice, Statement Before the Senate Committee on the Judiciary Concerning Antitrust Enforcement in the Agricultural Marketplace, at 4 (Oct. 20, 2003). Former Assistant Director at the Federal Trade Commission John B. Kirkwood, in a recent paper, distinguishes the FTC's statement in 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. He notes that "it is not entirely clear that the Commission's analysis is correct. The most critical factor in distinguishing countervailing power from monopsony power is the structure of the upstream supply market [pharmacies]. If the upstream market is atomistically competitive rather than oligopolistic or monopolistically competitive, a reduction in input prices would represent the exercise of monopsony (or oligopsony) power rather than countervailing power." John B. Kirkwood, Buyer Power and Merger Policy, at 57-60 (2011), *available at* http://ssrn.com/abstract=1809985.
[20] *See* FTC v. Cardinal Health, 12 F. Supp. 34 (1998); FTC v. HJ Heinz Co., 246 F. 3d 708, (D.C. 2001).

services, ultimately leading to consumer harm. We believe an enforcement action to enjoin this merger would be consistent with these past enforcement actions.

For example, the Department of Justice (DOJ) saw similar problems that exist with this merger in the proposed health insurance merger between UnitedHealth Group (United) and PacifiCare Health Systems (PacifiCare).[21] The DOJ's complaint alleged that the merger of the two health insurance companies would harm competition in the purchase of physician services. In the alleged markets, United and PacifiCare were the dominant insurance companies and the merger, without condition, would have led to a significant control of a large share of revenue of a substantial amount of physicians and a large share of their patients. Due to this control, terminating the relationship with the merged United or encouraging patients to switch to other health insurers were not feasible solutions for the physicians. As the Competitive Impact Statement observed:

> 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.[22]

It is notable that the Justice Department brought an enforcement action in the Boulder market, even though they did not necessary find a downstream effect on consumers.

As in the United/PacifiCare scenario supermarket pharmacies have a limited ability to maintain the business of patients enrolled in a PBM plan. If a pharmacy were to terminate that plan, the pharmacy could attempt to retain patients by encouraging them to switch to another plan the pharmacy services. However, it is nearly impossible for a patient to switch PBMs because their employers choose the PBM with whom they contract, and the patient would need to persuade the employer to sponsor an additional plan with the pharmacy's preferred network. Moreover, Express Scripts and Medco prevent pharmacies from trying to inform consumers about PBMs that may provide better access and coverage. Alternatively, a patient could remain in the plan and visit the pharmacy on an out-of-network basis, but this would require the patient to pay significantly higher out-of-pocket costs. Consequently, a supermarket pharmacy's ability to terminate a relationship with the new Express Scripts depends on the pharmacy's ability to make up lost business by switching to an alternative PBM provider. But those alternatives are clearly lacking, especially with a combined Express Scripts

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[21] United States v. UnitedHealth Group Inc. and PacifiCare Health Systems Inc., Case No. 1:05CV02436 (D.D.C. 2006).

[22] Competitive Impact Statement, UnitedHealth Group Inc., Case No. 1:05CV02436 (D.D.C. 2006). *See also* Marius Schwartz, Speech, 5th Annual Health Care Antitrust Forum, Northwestern University School of Law, Chicago, Illinois, October 20, 1999 (elaborating on the theory of buyer power reducing reimbursement leading to the degradation in the quality of physician medical care in the Aetna/Prudential merger).

Medco amounting to 40% of the business of some supermarket pharmacies.[23] As a result, reduced reimbursement will force the pharmacy to reduce the level of its services to consumers in response to a decrease in compensation.

Conclusion

Post-merger Express Scripts will undoubtedly have the capability to unilaterally reduce reimbursement rates and drive consumers to their own mail-order operations. This will have a real-world effect on competition for pharmacy services and profound negative impact on consumers. Supermarket pharmacies are among the lowest cost competitors of pharmacy dispensing services, offering $4 generic drug programs and discounts for 90-day drug supplies, as well as free antibiotics and other health care services. The merger will threaten to diminish or eliminate the critical competition offered by supermarket pharmacies and jeopardize the ability of supermarket pharmacies to provide patients with the current levels and quality of vital health care programs, and at the same time deny consumer choice and access to adequate pharmacy care. The FTC should bring an enforcement action to enjoin the merger.

Thank you for your attention to this matter.

Sincerely,

Cathy Polley, RPh
Vice President, Health & Wellness
Executive Director, FMI Foundation

Erik R. Lieberman
Regulatory Counsel

cc: Commissioner J. Thomas Rosch
Commissioner Edith Ramirez
Commissioner Julie Brill
Director of Bureau of Competition Rich Feinstein

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[23]Some supermarket pharmacies have told the Commission that the next highest percentage of business that any one PBM comprises after Express Scripts, Medco or CVS Caremark is 5% or less. This concern is consistent with the Horizontal Merger Guidelines which state "Market power on the buying side of the market is not a significant concern if suppliers have numerous attractive outlets for their goods or services. *However, when that is not the case*, the Agencies may conclude that the merger of competing buyers is likely to lessen competition in a manner harmful to sellers." FTC/DOJ Horizontal Merger Guidelines, ¶ 12 (2010)(emphasis added).