UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

UNITED STATES OF AMERICA, *et al.*	)	
Plaintiffs,	)	
v.	)	Case No. 1:18-cv-02340-RJL
CVS HEALTH CORPORATION	)	
and	)	
AETNA INC.	)	
Defendants.	)	

BRIEF OF THE AMERICAN MEDICAL ASSOCIATION AS AMICUS CURIAE IN OPPOSITION TO THE PROPOSED FINAL JUDGEMENT

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CORPORATE DISCLOSURE STATEMENT

The American Medical Association (AMA) has no parent company, and no publicly held company has a 10% or greater ownership interest in the AMA.

INTEREST OF AMICUS CURIAE

The AMA is the largest professional association of physicians, residents, and medical students in the United States. Through state and specialty medical societies and other physician groups seated in its House of Delegates, substantially all United States physicians, residents, and medical students are represented in the AMA's policymaking process. AMA members practice and reside in all states and in the District of Columbia. The objectives of the AMA are to promote the science and art of medicine and the betterment of public health.

The AMA and its members have an interest in ensuring that their patients enjoy the benefits of competition in the many markets affected by the merger between CVS and Aetna. The AMA has concluded that this merger would harm competition and patients and that the divestiture remedy contained within the Proposed Final Judgment (Doc. No. 57-1) will not restore competition in the Medicare Part D standalone prescription drug plan (PDP) market to premerger levels. Thus, the AMA respectfully requests that the court deny approval of the Proposed Final Judgment.

The AMA has authority to file this brief by virtue of the Court's order of March 6, 2019. No party has authored this brief in whole or in part, and no party or person other than the AMA has contributed money intended to fund preparing or submitting the brief.

SUMMARY OF ARGUMENT

CVS Health Corporation is the largest retail pharmacy chain, specialty pharmacy, and PDP insurer in the United States. It is also one of the two largest pharmacy benefit managers (PBMs). CVS proposes to acquire Aetna Inc., the third largest health insurer and one of the five largest individual PDP insurers, which account for 83% of PDP enrollment. DOJ Complaint, Doc. No. 1, ¶¶ 15–16; Ex. A, Report of Richard M. Scheffler, Ph.D. (May 29, 2018) at 2.

In studying this merger, the AMA has sought the views of prominent health economists and other experts in health policy and antitrust. Many of these experts testified in a California Department of Insurance hearing on the merger. The experts concluded, and the Department of Insurance agreed, that the merger would likely injure consumers by raising prices, lowering quality, reducing choice, and stifling innovation in five markets: PDP, PBM services, health insurance, retail pharmacy, and specialty pharmacy. Ex. B, California Department of Insurance Letter to Jeff Sessions and Makan Delrahim.[1] The first of these, the PDP market, is the subject of the DOJ's complaint in this case.

Although the DOJ agrees that the proposed merger would harm competition and consumers in the PDP market, it has asked that the merger be approved so long as Aetna divests its individual PDP business. The evidence, however, shows that the proposed divestiture will reduce competition in the PDP market, rather than restore it to premerger levels. Therefore, the Court should reject the Proposed Final Judgment.

[1] The California Department of Insurance is responsible for regulating the largest insurance market in the United States and the fourth largest in the world.

ARGUMENT

I. The Court May Not Enter the Proposed Final Judgment Unless It Will Restore Competition to Premerger Levels.

The Tunney Act (the Act) states that "[b]efore entering any consent judgment proposed by the United States ... , the court shall determine that the entry of such judgment is in the public interest." 15 U.S.C. § 16(e)(1). The government has the burden to "provide a factual basis for concluding that the settlements are reasonably adequate remedies for the alleged harms." *United States v. SBC Commc'ns, Inc*., 489 F. Supp. 2d 1, 16 (D.D.C. 2007) (citing *United States v. Microsoft Corp*., 56 F.3d 1448, 1460–61 (D.C. Cir. 1995)).

Although the Act does not define when a proposed judgment is in the public interest, the DOJ states in its Policy Guide to Merger Remedies, "The Division will insist upon relief sufficient to restore competitive conditions the merger would remove. Restoring competition is the 'key to the whole question of an antitrust remedy.'"[2] This definition is reiterated in a document recently published by the DOJ entitled "*United States v. CVS and Aetna*, Questions and Answers for the General Public," which states, "The standard for an acceptable divestiture is that it restore competition to premerger levels."[3]

The DOJ's complaint alleges that CVS's acquisition of Aetna will substantially lessen competition in the sale of individual PDPs in 16 Part D regions. Doc. No. 1 ¶¶ 30–36. The DOJ has filed a Proposed Final Judgment which would require Aetna to sell its PDP business to WellCare. Doc. No. 57-1 at 4–9. Thus, the Court may not enter the Proposed Final Judgment unless it is satisfied that the proposed divestiture remedy is in the public interest, meaning that

[2] Antitrust Division Policy Guide to Merger Remedies (Oct. 2004) at 4, accessible at https://www.justice.gov/sites/default/files/atr/legacy/2011/06/16/205108.pdf (quoting *United States v. E.I. du Pont de Nemours & Co.*, 366 U.S. 316, 326 (1961)). In September 2018, the DOJ withdrew the 2011 version of the Policy Guide and reinstated the 2004 version.
[3] Accessible at https://www.justice.gov/opa/press-release/file/1099806/download.

the divestiture will restore competition in the PDP market to levels that existed prior to the merger.

II. The Proposed Divestiture Will Not Even Come Close to Restoring Competition to Premerger Levels.

The DOJ has rightly concluded that the PDP market requires competition "to keep annual bids—which form the basis for federal government subsidies and beneficiary premiums—low." Competitive Impact Statement, Doc. No. 3, at 4. The DOJ's conclusion is buttressed by a number of studies showing insurer pricing power in the PDP market. This market power enables an insurer to charge premiums above competitive levels, degrade insurance quality, or both. Ex. C, Report of Amanda Starc, Ph.D., at 7–8. More generally, the weight of the research on insurance markets indicates that more competing firms or less concentrated local markets lead to lower premiums. *Id.* at 7. The proposed divestiture, however, will fall far short of fully restoring competition in the PDP market.

A. The Divestiture of Aetna's PDP Business Would Decrease the Number of Firms in Already Concentrated and Rapidly Consolidating PDP Markets.

Aetna, CVS, and WellCare currently participate in all 34 PDP regions/markets. These markets are concentrated and rapidly consolidating. In 2009, the average PDP market Herfindahl-Hirschman Index (HHI) was 1,519—just above the DOJ's threshold of 1,500 for a moderately concentrated market.[4] Ex. A, Scheffler Report (May 2018) at 6. By 2018, the average PDP market HHI had increased to 1,861—an increase of 342, or 23%. *Id.* According to the Merger Guidelines, mergers that would increase HHI by more than 100 points and result in post-merger HHIs between 1,500 and 2,500 "potentially raise significant competitive concerns and

[4] The HHI has been used frequently as a measure of market concentration in merger cases brought by the Antitrust Division of the DOJ and Federal Trade Commission and is used in the Horizontal Merger Guidelines, authored by these agencies.

often warrant scrutiny."[5] And "considerable economic evidence supports the proposition that a merger combining two firms with substantial market shares in a concentrated market is likely to reduce competition and harm customers."[6]

If the CVS/Aetna merger and divestiture is approved, there will be one fewer firm or plan sponsor in the PDP markets, and market concentration levels will rise further. The reduction in number of firms competing in the markets will change plan bids and consequently will increase premiums for the elderly and raise the costs of subsidizing these premiums for the government. Ex. A, Scheffler Report (May 2018) at 9. A Congressional Budget Office working paper and other research show that a reduction in the number of firms or plan sponsors is associated with higher premiums for Medicare beneficiaries and higher costs for the government.[7]

The AMA has asked University of California Berkeley Professor Richard Scheffler, Ph.D., to furnish a report on the effect of Aetna divesting its PDP business to WellCare on PDP market concentration. Ex. D, Report of Richard M. Scheffler, Ph.D. (Dec. 6, 2018).[8] Professor Scheffler concludes, in agreement with the DOJ's complaint, that PDP constitutes a relevant product market and that the relevant geographic markets are the 34 PDP geographic regions created by the Centers for Medicare and Medicaid Services. *See* Doc. No. 1 ¶¶ 23–29. To

[5] U.S. Department of Justice and Federal Trade Commission, Horizontal Merger Guidelines (2010) at 19, accessible at https://www.ftc.gov/sites/default/files/attachments/merger-review/100819hmg.pdf.

[6] Herbert Hovenkamp & Carl Shapiro, *Horizontal Mergers, Market Structure, and Burdens of Proof*, 127 Yale L.J. 1996, 2000 (2018).

[7] Andrew Stocking et al., *Examining the Number of Competitors and the Cost of Medicare Part D*, CBO Working Paper 2014-04 (July 2014), accessible at http://cbo.gov/sites/default/files/cbofiles/attachments/45553-PartD.pdf; *see also* Ex. C, Starc Report, at 7–8.

[8] Professor Scheffler is the Distinguished Professor of Health Economics and Public Policy at the School of Public Health and the Goldman School of Public Policy at the University of California, Berkeley. He holds the chair in Healthcare Markets and Consumer Welfare, endowed by the Office of the Attorney General for the State of California, and is the founding director of the Nicholas C. Petris Center on Healthcare Markets and Consumer Welfare.

address the impact of Aetna divesting its PDPs to WellCare on PDP market concentration, Professor Scheffler calculated 2018 PDP market concentration two ways: (1) assuming Aetna and WellCare have separate PDP businesses (pre-merger HHI); and (2) assuming Aetna and WellCare's PDP businesses are combined (post-divestiture HHI). Professor Scheffler concludes that seven PDP regions, covering nine states, would "potentially raise significant competitive concerns" under the Horizontal Merger Guidelines if Aetna divests its PDPs to WellCare. These seven PDP regions are (ranked from largest to smallest HHI change):

• Mississippi	(Region 20)	+230 HHI
• Arkansas	(Region 19)	+206 HHI
• Maine, New Hampshire	(Region 1)	+148 HHI
• Alabama, Tennessee	(Region 12)	+124 HHI
• Virginia	(Region 7)	+109 HHI
• Texas	(Region 22)	+109 HHI
• Louisiana	(Region 21)	+108 HHI

Ex. D, Scheffler Report (Dec. 2018) at 2. When these increases in already concentrated markets are combined with other market factors discussed below, the merger and divestiture are best understood as injuring competition rather than restoring it to premerger levels, which is the standard of an acceptable divestiture.

B. New Entry Will Not Solve the Problem Because There Are High Barriers to Entry into PDP Markets.

The lost competition from this divestiture is likely to be permanent because barriers to entry prevent new entrants from restoring competitive pricing. The government itself correctly acknowledges that in PDP markets "entry of new insurers or expansion of existing insurers is unlikely." The DOJ explains:

> Recent entrants into individual PDP markets have been largely unsuccessful, with many subsequently exiting the market or shrinking their geographic footprint. Effective entry into the sale of individual PDPs requires years of planning, millions of dollars, access to qualified personnel, and competitive contracts with retail pharmacies and pharmaceutical manufacturers, and companies must establish sufficient scale quickly to keep their plans costs down.

> Because of these barriers to entry, entry or expansion into the sale of individual PDPs is unlikely to be timely or sufficient to remedy the anticompetitive effects from this merger.

Competitive Impact Statement, Doc. No. 3, at 6.

C. The DOJ Has Not Meaningfully Responded to These Concerns.

The DOJ does not quarrel with any of these market structure analyses and concedes that after the divestiture, "some regions fall into the category of 'potentially' raising concerns under the Horizontal Merger Guidelines." Response to Public Comments, Doc. No. 56, at 22. In partial response, the DOJ points out that "no regions are above the threshold for 'presumed' concerns." *Id.* But drawing distinctions between "potential" and "presumed" concerns is unenlightening about the efficacy of the divestiture remedy, especially when PDP markets are concentrated with high barriers to entry, the trend is toward increased consolidation, the merger and divestiture raise the existing (premerger) market concentration to levels crossing the DOJ's own threshold of potentially raising "significant competitive concerns," and insurers have pricing power in the PDP context. Simply citing categories within the merger guidelines glosses over all these market conditions, which point to continued harm to competition from the merger. The country needs aggressive antitrust enforcement in health insurance and pharmaceutical markets, as Washington Post economics columnist Stephen Perlstein has urged in the context of this case.[9] Professor Hovenkamp has argued persuasively that "[a]n important purpose of the antitrust merger law is to arrest certain practices in their 'incipiency,' by preventing business firm acquisitions that are likely to facilitate them."[10] This is particularly true when the merger is vertical, which increases

[9] Steven Pearlstein, *CVS bought your local drugstore, mail-order pharmacy and health insurer. What's next, your hospital?*, Wash. Post, Jan. 31, 2019, accessible at https://wapo.st/2Gfk0vh?tid=ss_mail&utm_term=.4a739ca19286. Dr. Perlstein is also the Robinson Professor of Public Affairs at George Mason University.

[10] Herbert Hovenkamp, *Prophylactic Merger Policy*, 70 Hastings L.J. 46, 46 (2018).

the risk of input foreclosure or refusal to deal, or raises the probability of coordination among oligopolists, which is hard to detect.[11] Both situations are present here.

The DOJ also points out that there are "other significant competitors—including CVS's SilverScript product—in every market" and that the combined market share of Aetna and WellCare is below 25%. Response to Public Comments, Doc. No. 56, at 22–23. These facts would be important if the chief concern here were that the merger and divestiture would likely facilitate a unilateral price increase by WellCare. Instead, the primary worry here is that the structural change to the market will trigger a principal concern of merger policy: facilitation of marketwide express or tacit collusion or oligopoly behavior.[12] The PDP marketplace is currently dominated by five plan sponsors (including CVS and Aetna), which account for 83% of PDP enrollment.[13] Upon divestiture, WellCare would assume Aetna's PDP business. However, in contrast with Aetna, WellCare has competitive handicaps and vulnerabilities to rivals' anticompetitive strategies, which are discussed below. Therefore, the market would effectively go from having five principal competitors to four. Antitrust scholar Professor Herbert Hovenkamp observes that when the number of effective players, measured in terms of individual firms' realistic ability to upset collusion or oligopoly by cutting price, is reduced from eight or ten in the case of express collusion or from five or seven in the case of oligopoly, collusive behavior is more likely.[14]

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[11] *Id.* at 51–53, 57–59.

[12] Herbert Hovenkamp, Principles of Antitrust, § 12.1, at 469 (2017) ("Today one principal concern of merger policy is that horizontal mergers may facilitate market wide express or tacit collusion or oligopoly behavior. The 2010 Guidelines use the term 'coordinated interaction' to refer to these things.").

[13] The five sponsors accounting for 83% of PDP enrollment in 2018 are: CVS health (24%, 6 million enrollees), United health (21%, 5.3 million enrollees), Humana (20%, 4.9 million enrollees), Express Scripts (10%, 2.4 million enrollees), and Aetna (9%, 2.1 million enrollees). Ex. A, Scheffler Report (May 2018) at 2.

[14] Herbert Hovenkamp, Principles of Antitrust, § 12.1, at 469 (2017).

D. The Merger and Divestiture Would Eliminate the Unique and Important Role of Competition between Aetna and CVS in the PDP Market.

The DOJ's complaint is a testament to the competition lost when the substantial head-to-head competition between CVS and Aetna disappears. According to the complaint, customers view the merging parties as each other's closest substitutes.[15] Doc. No. 1 ¶¶ 30–36. CVS has found individuals leaving its individual PDPs went to Aetna more often than to any other competitor. *Id.* ¶ 31. CVS's and Aetna's PDPs are "also among the fastest growing individual PDPs, with new-to-Medicare enrollees choosing CVS and Aetna plans at rates higher than their current market shares." *Id.* The DOJ's complaint further alleges that CVS and Aetna have sought to win PDP customers from each other by competing on price and by improving the quality of their services and coverage. "This price competition between CVS and Aetna drives them to lower premiums, copayments, coinsurance, and deductibles." *Id.* ¶ 32. Competition, the DOJ alleges,

> has led the companies to improve drug formularies, offer more attractive pharmacy networks and create enhanced benefits for individuals. For example, in recent years, Aetna has made several changes to improve the coverage of its formulary and pharmacy networks to win business from CVS. This competition gave beneficiaries access to certain drugs at more affordable prices.

Id. ¶ 33. These allegations powerfully establish that competition will be lost in the PDP marketplace when Aetna divests its PDP business to WellCare, which must stand in for Aetna as CVS's principal competitor. The likely post-divestiture result will be that Aetna consumers will turn to CVS and the market will be robbed of the intense competition that has benefited consumers.

[15] For the importance of head-to-head competition in merger analysis, see Section 6.1 of the Merger Guidelines.

E. Divestiture of Aetna's PDP Business to WellCare is Unlikely to Make WellCare as Formidable a Competitor as Aetna.

For the proposed divestiture to restore competition to premerger levels, and keep them there, WellCare must be as formidable a competitor as Aetna was in the PDP market. Otherwise, it will lose some or all of the divested business to other firms, increasing market concentration even further. When it blocked the proposed merger of Aetna and Humana, which involved a proposed divestiture to the insurer Molina, this Court scrutinized Molina's competitive position and capabilities and found them wanting. *United States v. Aetna Inc.*, 240 F. Supp. 3d 1, 72–73 (D.D.C. 2017). A similar analysis here shows that WellCare suffers from significant disadvantages that make it unlikely to retain the divested business.

As the DOJ has described, Aetna is a formidable competitor for CVS in the PDP market. Its ability to compete with CVS stems from the size and scale of its operations. Ex. E, Report of Neeraj Sood, Ph.D. (Dec. 12, 2018), at 4.[16] First, as the DOJ's complaint notes, Aetna is the nation's third largest health insurance company and fourth largest PDP insurer. Doc. No. 1 ¶ 16. Its national presence and size make it a well-known brand. Second, Aetna's size both in the PDP market and in other health insurance markets likely allows it to obtain more competitive contracts with pharmacies and pharmaceutical manufacturers and thus allows it to compete more aggressively with CVS. Ex. E, Sood Report (Dec. 2018) at 4. Since Aetna will leave the PDP market post-merger, for the divestiture to completely remedy the anticompetitive effects of the merger, the divestiture should make WellCare at least as formidable a competitor as Aetna. This is unlikely to happen because the WellCare brand is not as well known as Aetna's, and the divestiture terms drastically limit WellCare's use of the Aetna brand. *Id.*

[16] Professor Sood is a Professor of Health Policy and Vice Dean for Research at the Sol Price School of Public Policy at the University of Southern California. He is a founding member and past Director of Research of the USC Leonard D. Schaeffer Center for Health Policy and Economics. He is also a research associate at the National Bureau of Economic Research.

According to the terms of the divestiture, WellCare is granted a license to use the Aetna brands for limited purposes such as transitioning to future branded PDPs and for only a limited period ending December 31, 2019. For 2020, the Proposed Final Judgment prohibits CVS from using the Aetna brand for the sale of PDPs. However, after the 2020 plan year, CVS/Aetna can once again offer PDPs under the Aetna brands. Doc. No. 57-1 at 7. Consequently, WellCare will soon be faced with surmounting a well-recognized barrier to entry in health insurance: brand. A DOJ study found that "brokers typically are reluctant to sell new health insurance plans, even if those plans have substantially reduced premiums, unless the plan has strong brand recognition or a good reputation in the geographic area where the broker operates."[17]

Moreover, Aetna is a major player in the non-Part D insurance market, which gives it much greater negotiating power with pharmacies and manufacturers than WellCare. The divestiture does not make WellCare a company of the same size and scale as Aetna. Ex. E, Sood Report (Dec. 2018) at 5. It merely temporarily increases the size of WellCare's Part D operations. Therefore, the divestiture will not give WellCare the same negotiating or bargaining power with pharmacies and manufacturers that Aetna enjoys because of its size in both the Part D and non-Part D markets. *Id.*

Finally, for plan year 2019, all key decisions regarding management of Aetna's divested business to WellCare might be made by Aetna under an administrative services agreement. This will not enhance the ability of WellCare to compete with CVS. *Id.*

F. CVS Provides PBM Services to WellCare, Making It Vulnerable to Input Foreclosure and a Weak Competitor of CVS/Aetna.

Although WellCare has purchased a small PBM—Meridian Rx—it depends on CVS for PBM services. Thus, the DOJ has had to acknowledge a major question confronting the merger

[17] Sharis A. Pozen, *Competition and Healthcare: A Prescription for High-Quality, Affordable Care* (Mar. 19, 2012) at 7, accessible at https://www.justice.gov/atr/file/518931/download.

and DOJ's proposed divestiture remedy: Can WellCare be expected to compete aggressively against the combined CVS/Aetna, given that CVS provides PBM services to WellCare?[18] The DOJ provides a partial response: that Aetna purchases certain PBM services from CVS and has been able to compete aggressively.[19]

The DOJ's partial response does not account for Aetna's strength relative to WellCare, as described above. Also missing from the DOJ discussion is that unlike WellCare, Aetna "performs its [own] core PBM functions."[20] While CVS performs certain PBM functions for Aetna under a 2010 agreement that expires in 2022, Aetna has said, "we retain our PBM and our ability to integrate medical care with clinical and pharmacy programs and actionable data."[21] Thus, two years into the CVS agreement, then-FTC Commissioner Julie Brill found that Aetna was the PBM "Dominant Three's" (CVS/Caremark, Express Scripts, and UnitedHealth Group's OptumRx) "nearest competitor."[22] Indeed, Aetna's 4% share of the highly concentrated PBM market is so substantial that the horizontal merger of Aetna and CVS raises significant competitive concerns in the PBM market under the Guidelines.[23]

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[18] DOJ Questions and Answers for the General Public, *supra* note 3, at 4.
[19] *Id.*
[20] See Aetna Form 10-K (2017) at page 7, accessible at http://investor.aetna.com/phoenix.zhtml?c=110617&p=irol-reportsAnnual.
[21] Aetna Inc., *Aetna Awards Long-Term Contract to CVS Caremark to Provide PBM Services*, accessible at https://news.aetna.com/news-releases/aetna-awards-long-term-contract-to-cvs-caremark-to-provide-pbm-services/.
[22] Dissenting Statement of Commissioner Julie Brill Concerning the Proposed Acquisition of Medco Health Solutions Inc. (Medco) by Express Scripts, Inc. (ESI) (April 2, 2012), https://www.ftc.gov/sites/default/files/documents/public_statements/dissenting-statement-commissioner-julie-brill/120402medcobrillstatement.pdf. According to Adam Fein's Drug Channel Institutes Report, "Aetna controls medical and pharmacy policy, formulary design, pharmacy/medical benefit integration, rebate contracting and many other core PBM functions." https://www.drugchannels.net/2013/06/catamaran-sails-away-with-cignas-pbm.html.
[23] Utilizing the 2017 data on PBM market share by total equivalent prescription claims managed published by the Drugs Channel Institute, AMA has calculated the PBM market HHI as ranging from roughly 1823 (most conservative) to roughly 1830 points. Assuming CVS and Aetna shares are exactly 25% and 4% respectively, the AMA estimates that the merger would cause the HHI

CVS will have the incentive and ability to disadvantage WellCare in the PDP market, thus making WellCare a weak competitor for CVS. Professor Sood and Northwestern University Professor Amanda Starc have opined that a merged CVS/Aetna would have weaker incentives to control prescription drug costs and overall healthcare costs for health plans competing with Aetna. Ex. C, Starc Report, at 10–11; Ex. G Sood Report (June 14, 2018) at 9–10; Ex. H, Sood Response to Aetna, at 4–5. Accordingly, CVS/Aetna would be unlikely to compete aggressively for PBM contracts serving CVS/Aetna competitors such as WellCare. The DOJ recognizes this incentive for the CVS/Aetna to interfere with WellCare's ability to compete, including in the Proposed Final Judgment a provision that "[divestiture] must be accomplished so as to satisfy the United States, in its sole discretion, after consultation with the Plaintiff States, that none of the terms of any agreement between an Acquirer and Defendants give Defendants the ability unreasonably to raise the Acquirer's costs, to lower the Acquirer's efficiency, or otherwise to interfere in the ability of the Acquirer to compete effectively." Doc. No. 57-1 at 6. This concern is heightened because CVS is the PBM for WellCare and a major player in the pharmacy market. As WellCare's PBM, CVS provides critical services to WellCare such as negotiating with

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to increase by 200 points. Professor Sood has done his own calculation and has concluded that the PBM HHI is roughly 1900 and that the merger of Aetna/CVS would increase HHI by roughly 200 points. Ex. F, Sood Presentation to DOJ, Slide 6. The further lessening of competition created by the horizontal merger between CVS and Aetna in the PBM market has not been challenged by DOJ. It is notable, however, that a report by The Council of Economic Advisors concludes that the existing market structure allows PBMs "to exercise undue market power." Council of Economic Advisers, *Reforming Biopharmaceutical Pricing at Home and Abroad*, Feb. 2018, at 10, accessible at https://www.whitehouse.gov/wp-content/uploads/2017/11/CEA-Rx-White-Paper-Final2.pdf. The report recommends "policies to decrease concentration in the PBM market that can increase competition and further reduce the price of drugs paid by consumers." *Id.* Similar remarks have been expressed by FDA Commissioner Scott Gottlieb. *See, e.g.*, Scott Gottlieb, *Capturing the Benefits of Competition for Patients* (Mar. 7, 2018) ("Too often, we see situations where consolidated firms -- the PBMs, the distributors, and the drugstores -- team up with payors. They use their individual market power to effectively split some of the monopoly rents…."), accessible at https://www.fda.gov/NewsEvents/Speeches/ucm599833.htm.

manufacturers and pharmacies. CVS, therefore, has the ability to increase costs and reduce efficiency for WellCare. Despite the DOJ's reservation of the right to approve the terms of the divestiture transaction, there is no plausible way for the United States to assure that CVS/Aetna will preserve WellCare's competitive strength on a long-term basis. A major reason for this is that drug pricing suffers from lack of transparency and is characterized by price obfuscation, as discussed below.

Moreover, the national market for PBM services is highly concentrated. CVS/Caremark, Express Scripts and UnitedHealth Group's OptumRx (the Big Three), account for at least 70 percent of the market.[24] In the event of a CVS/Aetna merger, Aetna would be eliminated as a potentially disruptive competitor in the PBM market, and all suppliers of PBM services with the scale to drive deep discounts with pharmaceutical companies would be vertically integrated into the PDP market. There would simply be no standalone PBM alternatives that would possess the buying power necessary to drive deep drug discounts. Thus, there is an appreciable danger that the Big Three would engage in market-wide express or tacit collusion or oligopoly behavior of not competing aggressively for PBM customers competing with the Big Three's PDP business. University of California, Hastings College of Law Professor Thomas Greaney, a widely published scholar on antitrust in health care, explains this likely anticompetitive behavior in the analogous context of the Big Three's dealings with health insurers competing with the Big Three's health insurance business:

> Vertical mergers may also impair competition when they enhance the ability and incentives to engage in horizontal coordination. As an example, the mergers currently under review — Express Scripts' announced plans to merge with Cigna and CVS's acquisition of Aetna — along with UnitedHealthcare's operation of a PBM would establish an oligopolistic market in health and pharmacy management with three of the nation's largest health insurers owning the three

[24] Drug Channels, *The CVS-Aetna Deal: Five Industry and Drug Channel Implications,* accessible at https://www.drugchannels.net/2017/12/the-cvs-aetna-deal-five-industry-and.html.

> largest pharmacy benefit management entities. Controlling by some estimates over 70% of the PBM market, and with only a very small portion of the market served by entities not integrated with a health insurer, the "Big Three" vertically integrated firms would have common incentives to weaken the competitive conditions of rival health insurers. For example, as one analysis put it, they could "act on shared incentives to withhold or weaken PBM bids to health plan rivals" that would "raise rivals' costs or lead to a diversion to sub-scale PBMs with higher costs and lower quality." Given cost advantages arising [from] their leverage in negotiating with pharmaceutical companies, the Big Three would face little threat from rival PBMs and have strong incentives and capacity to coordinate their strategies to disadvantage rival health insurers.[25]

Such coordinated conduct would also be difficult to detect because PBM "customers may not always be well placed to provide evidence regarding what is essentially opaque activity."[26] The Council of Economic Advisers recently observed that drug pricing suffers from a lack of transparency characterized by price obfuscation.[27] The size of manufacturer rebates and the percentage of those rebates passed onto health plans are secret.[28] One expert has concluded that most of the increase in drug pricing can be attributed to rebates pocketed by PBMs.[29] In short, the strategy of raising rivals' costs is likely to work.

G. Further Dampening WellCare's Prospects Is a Significant Danger That CVS/Aetna Would Raise the Costs of Retail Pharmacy Inputs Available to Its Competitors.

The merged CVS/Aetna may also foreclose smaller insurers, such as WellCare, from competing successfully with Aetna by denying access to CVS "must-have" retail pharmacies, either entirely or by offering terms that are not competitive with those offered to Aetna. Ex. I, AMA Letter to Makan Delrahim, at 19–20. Professor Sood reasons that CVS/Aetna could

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[25] Thomas L. Greaney, *The New Health Care Merger Wave: Does the "Vertical, Good" Maxim Apply?*, 46 J.L. Med. & Ethics 918, 921 (2018) (footnotes omitted).
[26] Brill Statement, *supra* note 22, at 5.
[27] Council of Economic Advisers, *Reforming Biopharmaceutical Pricing at Home and Abroad*, *supra* note 23, at 10.
[28] *Id.*
[29] Robert Goldberg, Center for Medicine in the Public Interest, *Drug Costs Driven by Rebates*, http://bionj.org/wp-content/uploads/2015/11/drug-costs-driven-by-rebates.pdf.

leverage its must-have pharmacy network to disadvantage competing plans. Ex. G, Sood Report (June 2018) at 11. PDP plans that do not have CVS in their pharmacy network will be less attractive to consumers, especially in markets where CVS has a dominant pharmacy market share. CVS/Aetna could exploit this fact by charging higher prices to PDPs competing with CVS/Aetna. This effect, says Professor Starc, may be especially important in the market for generic drugs, which are generally competitive at the wholesale, but not the retail, level and represent a large fraction of total bills. Ex. C., Starc Report, at 11. In recent years, prices for some generic molecules (even old ones whose branded equivalents' patents expired decades ago) have increased substantially. According to Professor Sood, if health plans refuse to accept the high prices and do not include CVS/Aetna pharmacies in their network, they risk losing customers. If they accept the higher prices, then they face higher health care costs, which might result in higher premiums and lower market share for these health plans. This will result in less competition in the insurance market. Ex. G, Sood Report (June 2018) at 10; *see also* Ex. C, Starc Report, at 11.

The government contends that it "investigated the potential for vertical harms from the merger by obtaining and reviewing documents as well as interviewing industry participants." Doc. No. 56 at 25. Based on this review, it says that "the evidence showed that CVS is unlikely to be able to profitably raise its PBM or retail pharmacy costs post-merger" because "it would lose customers to competing PBMs or retail pharmacies, and the merged entity likely would not be able to offset these losses by capturing additional health insurance customers." *Id.* at 26–27.

The DOJ's simplistic analysis ignores that the profitability of input foreclosure depends on various industry and market factors, and all of these factors suggest that input foreclosure is likely a profitable strategy for CVS/Aetna. First, the profitability of input foreclosure decreases with the probability of detection of input foreclosure because an increase in probability of

detection means a higher risk of losing PBM or retail pharmacy customers. Here, the probability that input foreclosure will be detected is fairly low, given the opacity of the PBM industry. As noted earlier, a CEA report observes that drug pricing suffers from a lack of transparency characterized by price obfuscation, and PBM customers have scant information about the rebates supposedly negotiated on their behalf because contracts between PBMs and drug manufacturers are claimed as trade secrets.[30] In addition, non-price input foreclosure in the form of poor customer service to enrollees of rival plans or higher administrative burdens for rival health plans may also be difficult to detect.

Second, the profitability of input foreclosure falls with the level of competition in the input market, as rival firms that detect input foreclosure will find it easier to obtain those inputs at a fair price from other firms. Here again, the facts support profitability of input foreclosure by CVS/Aetna. The markets for the two key inputs supplied by CVS/Aetna—PBM and retail pharmacy—are not competitive. For example, CVS has publicly stated that "[w]e currently operate in 98 of the top 100 United States drugstore markets and hold the number one or number two market share in 93 of these markets."[31] Similarly, and as discussed above, the PBM market is also very highly concentrated. In addition, the dominant PBMs—CVS, Cigna's Express Scripts, and UnitedHealth's OptumRx—are all PDP insurers. Thus, rival PDP insurers that detect input foreclosure do not have many outside options to seek these inputs at a competitive price from other firms.

Third, the profitability of input foreclosure depends on the relative profitability of input and output markets. For example, if CVS/Aetna were to pursue a strategy of input foreclosure, it could gain additional health insurance customers (including PDP customers), but if input

[30] *See supra* page 15 & notes 27–28.
[31] CVS Health Corporation Form 10-K (2015) at 6, accessible at https://www.sec.gov/Archives/edgar/data/64803/000006480316000074/cvs-20151231x10k.htm.

foreclosure is detected, it risks losing PBM and pharmacy customers. Therefore, the profitability of input foreclosure for CVS/Aetna depends on the profitability of health insurance customers relative to the profitability of PBM or pharmacy customers. Here again, the facts support the profitability of input foreclosure. Professor Sood discusses this issue in his expert report for the California Department of Insurance:

> Consider a consumer who spends $10,000 a year on average (this is roughly equal to US per capita health spending) on health care and $1,000 or roughly 10% of her total spending (this is roughly equal to the fraction of health spending on prescription drugs) is on prescription drugs. Data from SEC on the profitability of PBM and health insurance sectors suggests a net profit margin of PBM services of 2.3% and a net profit margin of health insurers of 3.0%. Therefore, if CVS-Aetna were to lose this consumer as a PBM customer then CVS-Aetna would lose about $23 (2.3% x 1,000) in profits. However, if CVS-Aetna were to gain the same consumer as a health insurance customer then CVS-Aetna would gain about $323 in profits stemming from $300 (3% x 10,000) in profits from providing insurance and $23 in profits from providing PBM services. Therefore, 1 insurance customer is as valuable as 14 PBM customers; providing strong incentives for CVS-Aetna to disadvantage competing health plans to gain insurance customers even if it risks losing some PBM customers.
>
> The numbers are similar when we look at incentives on the pharmacy market. Net profit margins in the pharmacy sector are 4%. Therefore, if CVS-Aetna were to lose an average pharmacy customer they would lose roughly $40 in profits per year. However, if CVS-Aetna were to gain this customer as a health insurance subscriber who also bought his or her prescriptions from CVS-Aetna they would stand to gain $363 in profits. Therefore, 1 insurance customer is as valuable as roughly 9 pharmacy customers; providing strong incentives for CVS-Aetna to disadvantage competing health plans to gain insurance customers even if it risks losing some pharmacy customers.

Ex. G, Sood Report (June 2018) at 11–12. Neither CVS/Aetna nor the government has disputed this analysis.

Similar concerns about input foreclosure were raised when CVS, the pharmacy chain, acquired Caremark, one of the biggest PBMs. The concern was that the PBM arm of CVS would steer pharmacy business towards its own pharmacies and would pay its own pharmacies more than rival pharmacies. Several reports in the media suggest that CVS is engaging in such input

foreclosure. For example, a recent news story suggests that CVS paid its own pharmacies much more than it paid rival pharmacies.[32] Another news story alleges that that the PBM arm of CVS set up a website for consumers to compare drug prices. But the site disadvantaged pharmacies competing with CVS pharmacies by automatically putting CVS pharmacies at the top of the comparison list. In addition, the PBM arm of CVS lowered Medicaid payment to independent pharmacies, putting them under financial duress. Then the pharmacy arm of CVS sent letters to many of the same pharmacies, asking whether they would be interested in selling their pharmacies to CVS.[33] The claims in these media reports that the PBM arm of CVS is steering business towards its own pharmacies is also borne out by analysis of data from CVS's financial statements by industry expert Adam Fein: the data show that in 2014 the PBM arm of CVS accounted for 35% of CVS retail pharmacies' revenue even though the PBM arm of CVS's national market share was only 24%.[34]

H. The Purchase Price of the Divested Assets Suggests That They Are Unlikely to Stay Viable and Therefore Are Unlikely to Remedy the Harm Alleged in the Complaint.

Professor Sood has observed that the purchase price of Aetna's divested assets suggests that they are unlikely to stay viable. Ex. E, Sood Report (Dec. 2018) at 5–6. As noted in the DOJ's complaint, Aetna has about 2.2 million customers in the PDP market. The average yearly

[32] Marty Schladen & Cathy Candisky, *CVS paid itself far more than some major competitors, report says*, Columbus Dispatch, Jan. 20, 2019, accessible at http://gatehousenews.com/sideeffects/cvs-paid-far-major-competitors-report-says/site/dispatch.com/.

[33] Catherine Candisky et al., *Three CVS actions raise concerns for some pharmacies, consumers*, Columbus Dispatch, Apr. 15, 2018, accessible at http://www.dispatch.com/news/20180415/three-cvs-actions-raise-concerns-for-some-pharmacies-consumers.

[34] Drug Channels, *CVS Health: Newest Data on Retail–PBM Revenue Synergies*, accessible at https://www.drugchannels.net/2015/03/cvs-health-newest-data-on-retail-pbm.html.

premium paid by a Medicare beneficiary for a PDP is estimated to be about $500.[35] The federal government subsidizes premiums for Medicare beneficiaries, paying on average about 75% of the total premium paid to a plan sponsor. Therefore, Professor Sood estimates that Aetna receives approximately $2,000 ($500 paid by beneficiaries and $1,500 paid by the government) in premiums per year from its 2.2 million customers. This translates to annual revenues of about $4.4 billion for its PDP business. *Id.*

According to Aetna's Q3 2018 financial statement, its profits or earnings were about 8.6% of premiums.[36] Therefore, Aetna's PDP business should generate about $378 million in profits per year. If this business were to remain viable for multiple years, the fair price of this asset would be multiple times the yearly profits, or well over a billion dollars. However, the purchase price of Aetna's PDP business in the proposed divestiture is well below this fair price estimate. In its Q3 2018 financial statements, Aetna notes "[t]he purchase price is not material to us." In response to a question posed by the Court during the November 29, 2018 hearing in this matter, the DOJ stated that the purchase price of Aetna's divested PDP business was in the $50 to $100 million range. 11/29/18 Tr. at 11:11–22. Why is an asset that generates approximately $4.4 billion in revenues and $378 million in profits per year being sold for $50 to $100 million? One logical conclusion is that the parties do not expect the asset to be viable in the medium to long term. In contrast, for the nine months ending Q3 2018, Aetna's earnings were $3.4 billion and CVS is buying Aetna for $69 billion, or more than 15 times annualized earnings.

The DOJ, in its response to these concerns about the low purchase price, suggests that a low purchase price may simply mean that WellCare "is getting a bargain." Response to Public

[35] Henry J. Kaiser Family Foundation, *Medicare Part D: A First Look at Prescription Drug Plans in 2019*, accessible at https://www.kff.org/medicare/issue-brief/medicare-part-d-a-first-look-at-prescription-drug-plans-in-2019/.
[36] Aetna Form 10-Q (Q3 2018), accessible at http://investor.aetna.com/phoenix.zhtml?c=110617&p=irol-reportsother.

Comments, Doc. No. 56, at 24. In other words, CVS and Aetna are being naive in selling their assets at such a low price to WellCare. The AMA believes that the lack of viability of the assets, rather than naiveté of CVS/Aetna, is a more plausible explanation for the low purchase price. In fact, the DOJ took the opposite position in seeking to block the merger of Aetna and Humana, which included a proposed divestiture to another insurer, Molina, at a bargain price. *United States v. Aetna Inc.*, 240 F. Supp. 3d at 72 ("The government counters that it reflects the riskiness of the transaction, and makes Molina more able to abandon many plans, counties, and members (i.e., not adequately replace lost competition) while still making a profit given the modest outlay."). Judge Bates agreed with the DOJ:

> The low purchase price thus further supports the conclusion that Molina has serious doubts about its own ability to manage all the divestiture plans but is willing to try given the low risk to the company reflected in the bargain price. That does not give the Court confidence in Molina's ability to effectively replace the competition lost by the merger.

Id.

The DOJ also states that it believes that WellCare will continue to compete in the PDP market. Response to Public Comments, Doc. No. 56, at 24. The relevant question, however, is not whether WellCare will continue to compete in the PDP market, but whether it will be able to *successfully* compete in the market and retain the customers from Aetna's PDP business that it acquires as a result of the divestiture. The purchase price of the divested business, which is *de minimis* in the context of this merger, strongly suggests that WellCare will not do so.

III. Divestitures Are Ineffectual in Restoring Competition in Health Insurer Mergers.

Research has shown that divestitures often fail to restore competition in the marketplace.[37] In the area of health insurance mergers, there have been only a few consent

[37] John Kwoka, *Mergers, Merger Control, and the Remedies: A Retrospective Analysis of U.S. Policy* 120, (MIT Press 2015).

decrees.[38] The inadequacy of the divestiture remedy in health insurance merger cases is well illustrated by the retrospective studies of two of them: the UnitedHealth/Sierra and the Aetna/Prudential mergers. Those studies showed that the consolidations resulted in significant premium increases notwithstanding that both cases were resolved by consent decrees requiring divestiture.[39]

A past divestiture closely linked to the current case is DOJ's divestiture remedy in Humana's acquisition of Arcadian. The remedy required Humana and Arcadian to divest Medicare Advantage plans in 51 counties. These divested assets were bought by three companies: Cigna, Vantage, and WellCare. An analysis by the Capital Forum shows that this divestiture was not successful in restoring competition.[40] Many of the plans that acquired the divested assets exited the market, Humana was able to regain its market share, and premiums for the elderly increased.

In its response to the comments it received, the DOJ states that "as a general matter, however, the factual circumstances in every divestiture are different." Doc. No. 56 at 19. The AMA agrees that the failure of past divestitures does not, standing alone, mean that the current divestiture will fail. However, the AMA also believes that we can learn from history. There are several factual similarities between the DOJ's divestiture remedy in the Humana/Arcadian case and the divestiture remedy in the current CVS/Aetna case. First, both divestitures are in

[38] Humana's acquisition of Arcadian Management Services in 2012; United Health Group's acquisition of Sierra Health in 2008; United Health Group's Acquisition of PacificCare in 2006; and Aetna's acquisition of Prudential in 1999.

[39] See Leemore Dafny et al., *Paying a Premium on Your Premium? Consolidation in the US Health Insurance Industry*, 102 Am. Econ. R. 1161 (2012); José Guardado et al., *The Price Effects of a Large Merger of Health Insurers: A Case Study of UnitedHealth-Sierra*, 1 Health Mgmt., Policy & Innovation 16 (2013).

[40] Center for American Progress, *Divestitures Will Not Maintain Competition in Medicare Advantage*, accessible at https://www.americanprogress.org/issues/healthcare/reports/2016/03/08/132420/divestitures-will-not-maintain-competition-in-medicare-advantage/.

insurance markets for the elderly. Second, under both remedies WellCare is a buyer of the divested assets. Third, both cases required divestitures of insurance subscribers rather than a separate business entity. Fourth, with both divestitures, the company selling the subscribers can compete in the same market with its own branded product. The DOJ points out that the CVS/Aetna divestiture is larger, Doc. No. 56 at 19–20, but it provides no evidence that the success of a divestiture is correlated with its size.

IV. Claimed Efficiencies Do Not Justify This Merger and Divestiture.

DOJ's press release accompanying its settlement with CVS/Aetna touts the possibility of merger-related efficiencies. However, apart from one oblique mention of this press release, Doc. No. 56 at 34, the DOJ has not presented and efficiency-related arguments in its Tunney Act pleadings. Thus, AMA will not discuss here the CVS/Aetna efficiency claims it raised before the California Department of Insurance. (AMA has also raised this issue to the DOJ. Ex. I, AMA Letter, at 23–29.) The AMA notes, however, that according to the California Department of Insurance, the merger parties provided "no reliable evidence" concerning claimed efficiencies. The New York Department of Financial Services was even more blunt, stating,

> Neither [CVS] nor [Aetna], in their written and oral testimony, provided any concrete analysis that the CVS/Aetna merger would result in specific reduced costs for New York consumers, or any business plan or study of asserted improved health outcomes to benefit New Yorkers. Likewise, the applicants did not set forth specific actions to be taken by CVS Health or Aetna Inc. post-transaction to accomplish the asserted benefits of this transaction in reducing costs to the New York consumer and improving New Yorkers' health outcomes.[41]

Even the DOJ has expressly rejected the notion that the merger would generate verifiable, merger-specific efficiencies sufficient to outweigh the anticompetitive effects that are likely to

[41] Ex. J, Decision and Order in The Matter of The Application by CVS Health Corporation and CVS Pharmacy, Inc. For Approval to Acquire Control of Aetna Health Insurance Company of New York (Nov. 26, 2018), at 3.

occur in the PDP markets. Complaint, Doc. No. 1, ¶ 38. Thus, there should be no dispute that the anticompetitive effects of the merger in the PDP market are not redeemed by efficiencies.

CONCLUSION

The nation has learned the hard way that overlooking consolidation in health insurance markets is costly. Studies of mergers with consent decrees that required divestiture have shown that these mergers result in higher insurance premiums. The divestiture here is especially flawed. It would raise the existing pre-merger market concentration to levels crossing the DOJ's own threshold of concern, and the loss of competition caused by the divestiture would likely be permanent because of high barriers to entry. It would eliminate the unique and important role of competition between Aetna and CVS in the individual PDP markets. WellCare is not the competitor that Aetna is in the PDP market; it lacks Aetna's size, negotiating power with pharmacies and pharmaceutical manufacturers, and after the 2020 plan year, Aetna's brand.

Further, substantially dimming the divestiture's prospects of restoring competition post-merger is the merger's vertical structure and its likely anticompetitive effects in input markets where WellCare and other smaller sellers of PDPs must turn for PBM and retail pharmacy services.

All of these competitive factors explain why the purchase price of the divested assets reflects that they are unlikely to stay viable, and therefore unlikely to remedy the harm alleged in the DOJ's complaint. The economic evidence strongly points to competitive harm, even with the proposed divestiture, and the DOJ has done little in its response to public comments to address this evidence. Therefore, the AMA respectfully requests that the court conclude that the proposed divestiture will not restore competition to pre-merger levels, and that the court reject the Proposed Final Judgment.

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Respectfully submitted,

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