July 10, 2018

The Honorable Commissioner Dave Jones
California Department of Insurance
300 Capitol Mall, Suite 1700
Sacramento, CA 95814

Re: American Antitrust Institute Responses to the Parties' July 3, 2018 Letter in re: the Proposed Acquisition of Aetna Inc. by CVS Health Corporation

Dear Commissioner Jones:

On June 19, 2018, the American Antitrust Institute's (AAI's) President, Dr. Diana Moss, provided telephonic testimony at the California Department of Insurance (CID) hearing regarding the potential anticompetitive and anti-consumer effects of the proposed acquisition of Aetna Inc. by CVS Health Corporation. AAI has reviewed the letter filed by CVS and Aetna dated July 3, 2018. Exhibit A to the letter addresses competition issues raised during the hearing. The AAI respectfully offers the following analysis in response to the parties' letter and requests that our response be placed in the CID record in this proceeding.

As an initial matter, the parties' characterization of AAI's testimony as being "sponsored" by the American Medical Association (AMA) is incorrect. AAI is a non-profit 503(c) research, education, and advocacy organization. AAI does not perform consulting services or take particular positions on behalf of any organization, other than the AAI. Our policies on funding and transparency are fully disclosed on the AAI website (antitrustinstitute.org). We do not receive funding from the AMA. Moreover, as noted by Dr. Moss in her testimony at the CID hearing, AAI's testimony is based on an analysis of the proposed merger contained in a March 26, 2018 letter from AAI to the U.S. Department of Justice Antitrust Division.[1]

I. The Parties Have Failed to Rebut AAI's Statement that Smaller Pharmacy Benefit Managers are Not Good Options

On page 3 of Exhibit A, the parties state (footnotes omitted):

Although an AMA-sponsored witness asserted that "smaller PBMs . . . are not good options," the data plainly contradict that claim. In California alone, PBMs such as Navitus, Argus, and MedImpact currently serve and presumably are good options for even the largest of customers. The commercial reality faced by CVS is as the FTC has described it: "a competitive market for PBM services characterized by numerous, vigorous

[1] https://www.antitrustinstitute.org/sites/default/files/CVS-Aetna_AAI%20Letter_3.26.18.pdf ("AAI DOJ Letter").

competitors who are expanding and winning business from traditional market leaders." To that point, over just the past year, CVS has lost business to more than ten different PBM competitors.

The parties' critique of AAI's testimony fails on a number of counts. First, the data the parties provide to support their assertion that there are good PBM options cuts against their case. Consider, for example, the table labeled "PBMs for Top Health Plans in California" on page 7 of Exhibit A. The table contains data on enrollments, by health plan. It also shows the PBM associated with each health plan.

Based on enrollments by PBM, CVS Caremark and Express Scripts each have about a 25% share. Kaiser has a 25% share, and the remainder is made up by smaller PBMs. While the parties' own data show that smaller PBMs do serve some of the smaller-ranked health plans, they confirm that PBM services in California are dominated by CVS Caremark and Express Scripts, which together control 50%. AAI's testimony, which is based on the AAI DOJ letter, makes this case using PBM data on a national level.

Moreover, in assessing competition in PBM services, it would be a mistake to include enrollment data on Kaiser, which is an integrated Health Maintenance Organization (HMO). Insurers would not look to Kaiser, as an HMO, as an alternative to other PBMs. Without considering Kaiser enrollments, CVS Caremark and Express Scripts each have a share of 33%. Together, they control 66% of PBM services in California.

A scenario in which two firms control more than half of the "market" is hardly competitive. Indeed, as noted by Dr. Moss in her testimony, the next largest PBMs on a national level are a fraction of the size of Caremark and Express Scripts. The parties' own data reinforce this fact. Such market shares highlight the limited options in PBMs available to health insurers in California and the fact that smaller PBMs are a fraction of the size of Caremark and Express Scripts. Optum Rx falls into this category.

Second, the FTC's statement in connection with the acquisition of Medco Health Solutions by Express Scripts, Inc. does not to support the parties' claims that the PBM market is competitive. The Commission's statement is over six years old.[2] Much has changed in the markets for PBM services since 2012 in terms of integration, which has undoubtedly affected the competitive abilities and incentives of market participants. The parties do not provide any information that would assist the CID is ascertaining whether the FTC's conclusion in 2012 still holds today.

Third, the parties' unsupported statement that CVS has lost business to numerous competitors in the last year is of little moment. That CVS does not win every account is not even probative of Caremark's market share, let alone does it undercut the highly concentrated nature of the PBM market.

In short, the parties' response, by focusing on the existence of some competitors, does not undercut (and the data offered tend to support) the proposition that the PBM market is

[2] *See* https://www.ftc.gov/sites/default/files/documents/public_statements/statement-commission-concerning-proposed-acquisition-medco-health-solutions-express-scripts-inc./120402expressmedcostatement.pdf.

dominated by CVS Caremark and Express Scripts and a few much smaller players. As noted in Dr. Moss's testimony, this exacerbates significant concerns that the proposed merger will adversely affect competition.

II. The Parties Claim That CVS Will "Keep Their Doors Open" Essentially Asks the CID to Believe That Their Merger Changes Nothing

On page 5 of Exhibit A, the parties state (footnotes omitted):

CVS/Aetna will not be the first combination of a health plan and a PBM. As the Commissioner noted during the hearing, "We have an example in United and Optum of a vertically integrated health insurer and health plan with a PBM." Per an AMA-sponsored witness, the UnitedHealth/OptumRx combination has been a success: "United Healthcare and Optum have kept the doors open. They will deal with all comers. They have not gone to a[n] ... exclusivity model." CVS will do the same. Although one witness attempted to distinguish OptumRx on the basis that it is a "small" PBM unlike Express Scripts and CVS, the data show OptumRx is in fact nearly the same size as Express Scripts and CVS Caremark.

The parties ask the CID to accept the claim that CVS will keep their doors open and deal with all comers after their merger with Aetna. This reasoning is faulty and should be dismissed. Indeed, it highlights why the CID should be skeptical of the parties' claims since it would require ignoring the significantly changed incentives and abilities of the vertically integrated company in a post-merger world.

As explained in Dr. Moss's testimony and AAI DOJ letter, the merged company will have significant incentives to exclude rival PBMs, retail pharmacies, and health insurers. It will also have stronger incentives to coordinate (versus compete) with other vertically integrated PBM-insurers, particularly if the Express Scripts-Cigna merger also moves forward. Under any of these scenarios, the merged company's, and other integrated PBM-insurers such as United Healthcare/Optum Rx, incentives to deal with rivals could change quickly and significantly. This could lead to a market dominated by a few integrated PBM-insurers with few incentives to deal with rivals, to the detriment of competition and consumers.

Thank you for your attention to AAI's response in this matter.

Sincerely,

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