August 19, 2014

Via Electronic Submission

Larry Good
Executive Secretary
ERISA Advisory Council
U.S. Department of Labor, Suite N-5623
200 Constitution Avenue NW
Washington, DC 20210

Dear Mr. Good,

The Directors of the Federal Trade Commission Office of Policy Planning, Bureau of Economics, and Bureau of Competition (collectively, FTC staff) today submitted a letter commenting on the ERISA Advisory Council’s (the Council’s) deliberations regarding PBM Compensation and Fee Disclosure. I write separately to explain why I respectfully disagree with the position staked out in the FTC staff’s letter, and to inform the Council about the FTC’s current information regarding the pertinent issues before the Council.

The primary focus of the Council’s inquiry is a determination “examining the current status of the need for and potential scope of compensation and fee disclosures by PBMs under Section 408(b)(2), whether such information is necessary for plan administrators to determine if reasonable compensation is being paid for PBM services under the statute, and how mandatory compensation and fee disclosures might impact the provision of prescription drug services to participants and beneficiaries of health care benefit plans and the costs of plan administration.”¹ To further its inquiry, James Singer, the Issue Chair of the PBM Team on the ERISA Advisory Council, sent a list of questions to the Federal Trade

Commission seeking specific points of information to aid in the Council’s examination.\(^2\)

In its responsive letter to the Council, dated August 19, 2014, rather than addressing all of the questions that Mr. Singer posed to the FTC, the FTC staff letter includes a description a 2005 study the FTC conducted concerning the PBM market and some more recent work the agency has done in the PBM market generally. The FTC staff letter also highlights two of staff’s prior comments from 2009 and 2007 about PBM fee and compensation transparency legislation pending in the New York and New Jersey, respectively.\(^3\)

The FTC staff letter concludes that mandatory compensation and fee disclosures may harm competition by hindering the ability of plans to negotiate an efficient level of disclosure with PBMs, and by resulting in less aggressive pricing by, or even collusion among, pharmaceutical manufacturers.\(^4\) The FTC staff bases its conclusions not only on the FTC’s 2005 study of the PBM market, but also based on the FTC’s investigation of the merger between ESI and Medco in 2012.\(^5\)

My chief disagreement with FTC Staff’s conclusion that mandatory compensation and fee disclosures may harm competition is that I do not believe this agency possesses sufficient current information to evaluate this issue. I believe the FTC’s 2005 PBM study is quite old at this point, and could not have taken into account the significant changes that have occurred in the market since 2005. Moreover, the FTC’s 2012 review of the proposed acquisition of Medco Health Solutions by Express Scripts, Inc. (ESI/Medco merger) simply did not focus on the issue of mandatory compensation and fee disclosures, and the level of competition that the majority found in the market could well have been because of, rather than in spite of, the significant market changes since 2005. Finally, I believe that the current level of competition in the PBM market as a result of the ESI/Medco merger and a subsequent PBM merger is questionable. Accordingly, I

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\(^3\) I was not a member of the Federal Trade Commission when the FTC published the 2005 PBM report, nor was I a member of the Commission when the 2007 and 2009 staff letters (cited in FTC staff’s letter to the Council) were issued and sent to the New York and New Jersey State Legislature regarding legislative efforts to regulate PBMs.

\(^4\) FTC Staff letter to ERISA Advisory Council, August 19, 2014, at 3-6.

\(^5\) Id.
believe the Council should place the FTC staff’s position in its appropriate context in light of my view that the FTC lacks current and relevant information about the particular issue – the potential benefits and harms from compensation and fee disclosure requirements – before the Council.

The first relevant change in the market since 2005 that should be considered is the effort in recent years of the states to require some level of PBM transparency. The states investigated widespread evidence of deceptive and fraudulent practices within the industry in the months and years following the FTC’s 2005 PBM study. These investigations have led at least 29 states to enact laws that regulate PBMs by, among other things: requiring PBMs to be more transparent with their clients about compensation and rebates; requiring fair audits of pharmacies; licensing PBMs; and requiring Maximum Allowable Cost (MAC) disclosure. The FTC’s 2005 PBM study could not have taken account these state laws – and the competitive effect (if any) they have had on the market or on the FTC’s conclusions about the competitive effects of plan design – since these laws were enacted after the FTC published its study.

Second, the FTC staff letter implies that the FTC’s 2012 review of the ESI/Medco merger confirmed the 2005 study’s conclusion that mandatory compensation and fee disclosures are unnecessary, or might somehow be detrimental to market competition. Yet the FTC’s ESI/Medco merger review did not focus on the issue of the competitive effects of different PBM plan designs, or the competitive effects of state law requirements that mandated either transparent plan designs or the inclusion of proposals with transparent plan designs as a component of PBM bids to plan sponsors. Indeed, to the extent that a majority of the Federal Trade Commission found that the ESI/Medco merger review indicated PBM competition was “intense,” it is possible that the level of competition that the majority found in the market was because of, rather than in spite of, the changes in

8 See FTC Staff Letter to ERISA Advisory Council (Aug. 19, 2014) at 4.
9 It is important to note that the no members of the current FTC Commission other than Chairwoman Ramirez and myself participated in the ESI/Medco merger. Further, none of the senior staff members who signed the FTC staff’s August 19, 2014, letter to the ERISA Advisory Council participated in the ESI/Medco merger review.
the state legislative landscape since 2005. Simply put, from the perspective of the Council’s current inquiries, the FTC’s merger review did not attempt to separate the signal of the effect of different plan designs – including fee and compensation transparency provisions, whether mandated by state law or voluntary – from the noise of the overall level of competition in the PBM market place.\(^{10}\)

Third, the suggestion made by the Commission majority in 2012 that PBM competition “is intense” is debatable and, I believe, not an argument that should sway the Council’s deliberations either way. However, because the Advisory Council expressed interest in my views about the 2012 ESI/Medco merger,\(^{11}\) I’ll note that I continue to believe the PBM industry was then – and remains today - highly consolidated. At the time of the merger, the Big Three PBMs (ESI, CVS Caremark, and Medco) had a combined market share of between 80 and 90 per cent in the large commercial employer market, the antitrust market that the FTC had used in the past to assess the competitive effects of prior PBM mergers.\(^{12}\) Broadening this market out to include all employers, the combined ESI/Medco had a post-merger share of 45 per cent and the Big Three had a combined 73 per cent market share. Even in an all employer market, the Big Three’s nearest competitor, Aetna, had a market share well below 10 percent following the merger of ESI and Medco.\(^{13}\) This market structure, combined with the 90 per cent customer retention rate and significant installed bases enjoyed by the Big Three,\(^{14}\) all pointed – in my careful estimation – toward a market that, once the merger was consummated, would become a “duopoly with few efficiencies in a market with high entry barriers – something no court has ever approved.”\(^{15}\)

As I also explained in my 2012 dissent regarding the ESI/Medco merger, the market as then-structured had already shown signs that coordination between the


\(^{11}\) See Singer July 22\(^{nd}\) email, supra note 2. In Appendix A to this letter, I respond to all of the particular questions posed by Mr. Singer in his July 22\(^{nd}\) email to the FTC.


\(^{13}\) Id. at 3.

\(^{14}\) Id. at 6.

\(^{15}\) Id. at 7, citing *FTC v. H.J. Heinz Co.*, 246 F.3d 708, 717 (D.C. Cir. 2001).
players was feasible and ongoing. I found this to be evidenced in statements made by the ESI CEO to his senior executive team in ordinary course company documents, as well as public statements made by Medco’s senior leadership to analysts, both of which pointed to customer allocation between the large PBMs.16

In sum, I disagreed with the majority of my fellow Commissioners that – in 2012 – competition in the PBM marketplace could be characterized as “intense,” and I remain unconvinced of this today.

As a matter of fact, concentration levels in the PBM industry appear to have increased even more since the ESI/Medco merger in 2012. This apparent increase is a result of the subsequent merger between SXC and Catalyst in April 2012, a merger that was not investigated by the FTC in any meaningful way.17 The FTC staff might argue that – as a matter of economic theory – this structural change in the marketplace since the Commission investigated the ESI/Medco merger is unimportant. However, I would submit that – at a minimum – unexamined changes in the marketplace since 2012, not to mention the unexamined real-world impact of this game-changing merger between ESI and Medco itself, ought to be taken into consideration by the Council in determining the weight to give the FTC staff’s categorical conclusions regarding the intensity of competition in the PBM marketplace today.

Fourth, I also take issue with the FTC Staff’s suggestion that plan design is a significant dimension of competition between PBMs and something that plan sponsors can freely negotiate. In reality, the real-world evidence points to a marketplace in which there are significant bargaining asymmetries between PBMs and smaller plan sponsors. As Consumer Union noted in its June 2014 testimony before the Council, “[i]t is often the case that buyers lack the tools to discipline profiteering because they do not know the extent to which it is practiced. In most cases, plan sponsors do not have access to PBM rebate agreements and other contract terms” needed to negotiate plan design on a level playing field.

16 Id. at 5.
Back in 2012 I called on the Commission to conduct a thorough analysis of the PBM market in order to test whether the then-majority’s prediction – that a merger to duopoly would not have anticompetitive effects – has been borne out in the real world.\textsuperscript{18} At an oversight hearing before the House Commerce Committee on December 3 last year, in response to a question from Rep. Jeanne Schakowsky, I reiterated my call for the FTC to study the PBM market in order to examine whether the ESI/Medco merger and other recent market developments have led to a market that suffered from competition concerns.\textsuperscript{19} Such a study could include a re-evaluation of the competitive impact of different plans designs in light of the significant market changes since the FTC last examined this question a decade ago.

In sum, I ask the Council to consider that the FTC staff letter does not represent my views. I also ask the Council to consider the FTC’s current level of knowledge regarding the competitive effects of different plan designs in the today’s market, as well as the FTC’s current level of knowledge regarding whether the forces at play in the current market are competitive and adequate to protect consumers of PBM services.

I would be happy to meet with the Council to discuss these matters further.

Sincerely,

Julie Brill
Commissioner
Federal Trade Commission

\textsuperscript{18} Brill Dissent, at 7 and 8.
\textsuperscript{19} December 3, 2013 House Commerce Committee Hearing on FTC at 100, unofficial transcript at 15.
Appendix A


Note: The questions were submitted on behalf of the ERISA Advisory Council and not on behalf of the United States Department of Labor, Employee Benefits Security Administration.

1. Describe existing published guidance by the Federal Trade Commission (FTC) on the impact that disclosures by PBMs of rebates and spreads between contract price for prescription drugs and actual cost of prescription drugs (indirect compensation) have on competition.

Response 1: Commissioner Brill is unaware of any such guidance.

2. Has the FTC conducted further study of the PBM industry since 2005? Have there been changes in the PBM industry that have impacted the competitive nature of the industry since 2005? How does the FTC respond to critics that the 2005 FTC study is not current? Also, Julie Brill, FTC Commissioner at the time of the Medco/Express Scripts merger said in a minority opinion that “this merger is, in fact, a duopoly with few efficiencies in a market with high entry barriers--something no court has ever approved." Have there been any new additional studies on the duopoly issue?

Response 2: the FTC has not conducted a further study of the PBM industry since 2005, other than to review the ESI/Medco merger in 2012. As described in Commissioner Brill’s Aug. 20, 2014, letter, however, this merger review did not examine issues surrounding PBM plan design. The 2005 study is not current, as it is about a decade old (since it is based on information submitted prior to 2005), and could not take into account the significant market changes that have taken place since 2005. The FTC has not studied the competitive effect of the merger, which in Commissioner Brill’s opinion created a duopoly with few efficiencies in a market with high entry barriers.

3. Is the FTC aware that the PBM industry currently discloses indirect compensation by means of “pass through pricing” contracts, and “transparent”
audit rights both of which are commonly offered to plan sponsors? If not, assume that this is true. Would the voluntary disclosure of indirect compensation by the PBM industry in response to market pressures by plan sponsors change the FTC’s conclusion about the anti-competitiveness related to Government required disclosure of indirect compensation? Please explain. Does it make a difference if the PBM industry provides voluntary disclosure of indirect compensation under “pass through pricing” contracts, but does not provide such information under other contractual arrangements with plan sponsors?

Response 3: the FTC has not studied the competitive impact of current trends in the PBM market regarding indirect compensation by means of “pass through pricing” contracts or “transparent” audit rights.

4. Is the FTC aware that in negotiations between the PBM industry and plan sponsors it is a common practice for a consultant to represent the plan sponsor, for the consultant to be paid by indirect compensation from the PBM, and that the disclosure of such indirect compensation is a matter of contract between the PBM and the plan sponsor? If the FTC is not aware of this, assume that it is true. Is the potential of undisclosed indirect compensation to the PBM and undisclosed indirect compensation to the consultant from the PBM relevant to the FTC’s conclusion that the mandatory disclosure of indirect PBM compensation is anti-competitive?

Response 4: the FTC has not studied the competitive impact of current trends in the PBM market regarding indirect compensation by PBMs to consultants who advise plan sponsors.

5. In 2012, the Department issued regulations requiring retirement plan service providers in the financial services industry to disclose indirect compensation. See DOL Reg. Section 2560.408b-2. Has the FTC considered the impact on competition in the financial services industry of the Department’s 2012 regulation? If so, please explain. Has the FTC concluded that if the Department mandated disclosure of PBM indirect compensation in a manner similar to the Department’s Regulation for the financial service industry when providing services to retirement plans, such disclosures would be anti-competitive? If so, please explain.

Response 5: the FTC has not studied the competitive impact of requiring disclosure of PBM indirect compensation in a manner similar to the Department’s
Regulation for the financial services industry when providing services to retirement plans.


Response 6: As described in Commissioner Brill’s Aug 20, 2014, letter, the vast majority of these state laws were enacted after the FTC’s 2005 PBM study. To date, the FTC has not studied the impact on competition of State laws related to disclosure of PBM compensation, or state laws related to similar disclosure requirements for hospitals and other health care providers.