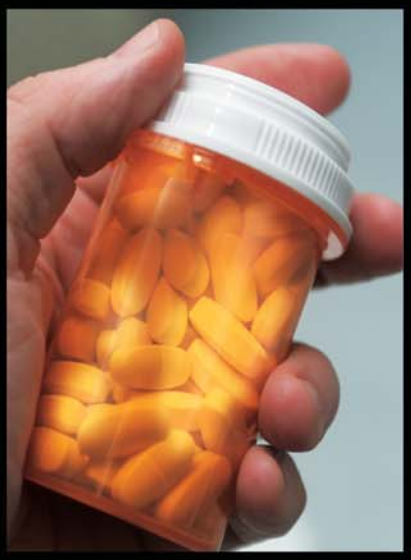

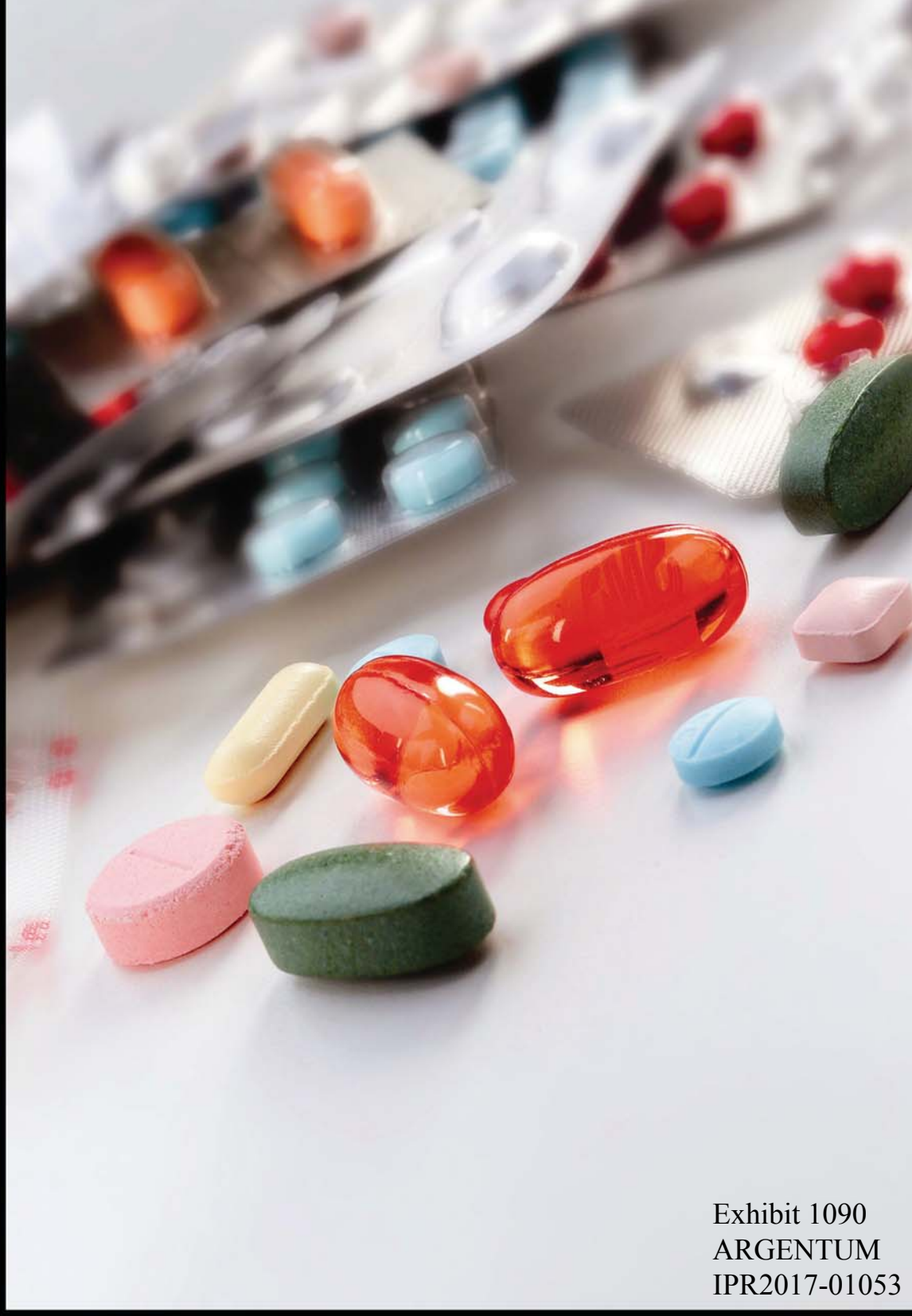

Pharmacy Benefit Managers: Ownership of Mail-Order Pharmacies

Federal Trade Commission

Federal Trade Commission

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Acknowledgments:

The FTC staff appreciates the cooperation of all of the companies subject to the Special Orders and their timeliness in providing requested additional materials.

EXECUTIVE SUMMARY

For millions of Americans, breakthroughs in medical research have allowed prescription drugs to save lives, reduce suffering, and enhance life. But these breakthroughs come with a price: increased usage and rising prices have pushed prescription drug expenditures to $179.2 billion in 2003, or 10.7% of national health expenditures. Prescription drugs are the most rapidly increasing component of U.S. health care costs.

Against this backdrop, Congress in 2003 added a new benefit to Medicare that provides senior citizens and other Medicare beneficiaries with a voluntary prescription drug benefit beginning in 2006. The new benefit relies heavily on private sector entities and competition to ensure that Medicare enrollees have a choice of prescription drug plans.

Private sector entities that offer medical insurance ("plan sponsors"), such as employers, labor unions, and managed care companies, also offer prescription drug insurance coverage. Plan sponsors often hire pharmacy benefit managers (PBMs) to manage these insurance benefits. This Study examines one facet of private sector competition – how PBMs' use of mail-order pharmacies that they own affects their clients' prescription drug costs.

PBMs engage in many activities to manage their clients' prescription drug insurance coverage. PBMs assemble networks of retail pharmacies so that a plan sponsor's members can fill prescriptions easily and in multiple locations by just paying a copayment amount. PBMs consult with plan sponsors to decide for which drugs a plan sponsor will provide insurance coverage to treat each medical condition (*e.g.*, hypertension, high cholesterol, etc.). The PBM manages this list of preferred drug products (the "formulary") for each of its plan sponsor clients. Consumers with insurance coverage are then provided incentives, such as low copayments, to use formulary drugs. Because formulary listing will affect a drug's sales, pharmaceutical manufacturers compete to ensure that their products are included on these formularies. They do so by paying PBMs "formulary payments" to obtain formulary status, and/or "market-share payments" to encourage PBMs to dispense their drugs. These payments are based on the quantity of drugs dispensed under the plans administered by the PBM.

PBMs use mail-order pharmacies to manage prescription drug costs. Many plan sponsors have encouraged patients with chronic conditions who require repeated refills to seek the discounts that 90-day prescriptions and high-volume mail-order pharmacies can offer. Many PBMs own their own mail-order pharmacies. These PBMs have suggested that they have greater control over the drugs dispensed through mail-order pharmacies and, therefore, can provide greater formulary compliance.

And this is where the controversy lies. If a plan sponsor's agreement with a PBM does not properly align the plan's interests with the PBM's incentives, there could be a conflict of interest. Although PBMs are tasked to manage and lower the costs of pharmacy benefits, in theory they could have incentives to increase costs and generate additional profits through their mail-order pharmacies. Congress requested that the Federal Trade Commission (FTC or Commission) determine whether a PBM that owns a mail-order pharmacy acts in a manner that

maximizes competition and results in lower prescription drug prices for its plan sponsor members.

At the request of Congress, the Commission collected aggregate data on prices, generic substitution and dispensing rates, savings due to therapeutic drug switches ("therapeutic interchange"), and repackaging practices. These data provide strong evidence that in 2002 and 2003, PBMs' ownership of mail-order pharmacies generally did not disadvantage plan sponsors. Because these data are aggregated, they do not answer whether each plan sponsor has negotiated the best deal possible or whether each PBM has fulfilled its contractual obligations due to each of its plan sponsor clients. The data also do not indicate whether, in individual instances, a PBM might have favored its mail-order pharmacy in ways contrary to a plan sponsor's interests. Nonetheless, these data suggest that competition in this industry can afford plan sponsors with sufficient tools to safeguard their interests.

Congressional Request

Congress requested in the Medicare Prescription Drug, Improvement, and Modernization Act of 2003 (MMA) that the Federal Trade Commission undertake a "Conflict of Interest Study" to examine "differences in payment amounts for pharmacy services provided to enrollees in group health plans that utilize pharmacy benefit managers," including:

> (1) An assessment of the differences in costs incurred by such enrollees and plans for prescription drugs dispensed by mail-order pharmacies owned by pharmaceutical benefit managers compared to mail-order pharmacies not owned by pharmaceutical benefit managers and community pharmacies (Question 1).
>
> (2) Whether such plans are acting in a manner that maximizes competition and results in lower prescription drug prices for enrollees (Question 2).[1]

As explained in the Conference Report for the MMA, Congress requested that the Commission determine whether the use of mail-order pharmacies owned by PBMs that administer the Medicare prescription drug benefit would adversely affect Medicare spending, as compared to the use of mail-order pharmacies not owned by a PBM. Accordingly, Congress asked the FTC to consider the following business practices:

> (1) whether mail-order pharmacies that are owned by PBMs (or entities that own PBMs) dispense fewer generic drugs compared to single source drugs within the same therapeutic class than mail order pharmacies that are not owned by PBMs (Question 3);
>
> (2) whether mail-order pharmacies that are owned by PBMs (or entities that own PBMs) switch patients from lower-priced drugs to higher-priced drugs (in the

[1] *See* Medicare Prescription Drug, Improvement, and Modernization Act of 2003, Pub. L. No. 108-173, tit. I, § 110, 117 Stat. 2066, 2174 (2003) (codified at 42 U.S.C. § 1395w-101 (Historical and Statutory Note)).

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