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2018-08-14 17:59:58

AET/CVS: Part D Selloffs Manageable; DOJ to Review 'Ripple Effects'

Mon 08/13/2018 12:13 PM

Event Driven Takeaways

- The divestiture by CVS and Aetna of Medicare Part D overlaps should go smoothly, although the DOJ will look closely at regional and national effects of the selloffs.
- Last week, Larry Merlow, chief executive of CVS, said that any Medicare Part D divestitures "would not be material to the deal model." CVS expects the deal to close by early Q4, Merlow said.
- CVS and Aetna will need to find buyers that are neither too large nor too small. This could be difficult in some regions, said Richard Scheffler, a health economics professor at the University of California, Berkeley.

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During an earning call on Aug. 8, Larry Merlow, the chief executive of CVS, said the company had "contemplated a range of possibilities" related to Medicare Part D at the time of deal announcement, and that "any divestitures would not be material to the deal model." CVS expects the transaction to close late Q3 or early Q4, Merlow said.

Mark McCareins, a longtime antitrust practitioner who teaches courses on antitrust and business law at Northwestern's Kellogg School of Management, said the divestiture process should be relatively easy. "There's a predictive nature to it," he said. Even though CVS and Aetna may not receive as much money for the divested assets as they would like, the divestitures themselves should not create serious regulatory issues. "It shouldn't be a problem," said McCareins.

CVS and Aetna have already faced questions related to Part D overlaps during various state reviews. However, the DOJ will ultimately oversee the Medicare selloffs, which will occur based on regional markets. A spokesperson for CVS declined to comment, saying only that the companies "continue to work productively with the DOJ."

Patrick Souter, of counsel at law firm Gray Reed & McGraw, said there are essentially three steps in the Part D divestiture analysis. First, the DOJ and the merging parties will need to identify which regional markets require divestiture, as well as which party divests in those markets. Second, there is a question of whether the higher market share of an acquiring entity will result in a negative impact on regional competition. And third, there will be a review of competition within the entire Part D industry after the divestiture.

"The devil is in the details because divestiture will result in a ripple effect of antitrust issues that will now involve the parties taking on the overlap as well," said Souter.

Jay Levine, co-chair of the antitrust and consumer protection practice group at Porter Wright Morris & Arthur, agreed the DOJ will look closely to ensure that divesting the overlaps would not reduce competition and that any divestiture buyers can compete effectively. "You don't want to go from one problem to creating another," Levine said.

Opponents of the Aetna/CVS deal are encouraging the DOJ to block the transaction even if the agency does not pursue vertical theories of harm. Last week, the American Medical Association, or AMA, sent a letter to the DOJ opposing the acquisition. Richard Scheffler, a health economics professor at the University of California, Berkeley, whose analysis was cited in the letter, told Event Driven that CVS and Aetna may encounter issues when selling off Part D overlaps.

“Selling them to other Part D providers of any significant size would raise its own competitive issues and smaller providers may not have the capital to take this on,” he said. Asked if there is a sufficient subset of potential buyers that are neither too large nor too small, Scheffler said the merging parties could find such suitors in “maybe a few markets but not most.”

Diana Moss, president of the American Antitrust Institute, was also cited by the AMA in its letter. In an interview, Moss said that even if the DOJ’s focus is solely on the horizontal Part D overlaps, divestitures could be “really tricky” due to the complexities, including state regulations, of health insurance markets.

Further, the companies may have a difficult time convincing the DOJ to include Medicare Advantage in the same market as standalone Medicare Part D plans, largely because the agency previously viewed those markets as distinct when it successfully blocked the proposed Humana/Aetna deal in federal court. “The DOJ is going to have to be consistent,” Moss said.

Event Driven’s previous coverage of the transaction, including an analysis of Part D overlaps, can be found **HERE**.

--Ryan Lynch