

From Dr. Borzilleri's (Relator's) SDNY Opposition to Defendants' Motion to Dismiss, filed on November 19, 2018

Prior to Medicare Part D, the PBM Defendants made virtually all their profits from the portion of rebates/discounts they “retained” from their negotiations with drug manufacturers on behalf of payer clients. SAC ¶ ¶ 12, 201. Until very recently, independent PBM and pharmaceutical industry experts still universally held that manufacturer rebates were the PBM Defendants’ primary source of profits. In reality, since the 2006 arrival of Medicare Part D, the PBM Defendants have secretly and knowingly (with virtually no public disclosure) made the large majority of their PBM profits from U.S. brand drugs via manufacturer “service fees”. SAC ¶ ¶ 13, 102, 460-1, 736, 779-805. For many U.S. brand drugs, especially the drugs targeted in this case, the meteoric increase in fraudulent “service fee” payments have been driven solely by similarly massive and fraudulent “list” price increases.

Very recently, for the first time, the PBM Defendants CVS Health and Express Scripts finally publicly admitted what the Relator has long known; namely that brand drug “manufacturer rebates” now account for little PBM Defendant profits, leaving secretive “manufacturer services fees” as their primary income source.

On its August 8, 2018 earnings conference call with Wall Street analysts, CVS CEO Larry Merlo stated: *“And while some have speculated that our retained rebates represent as much as \$2 billion, the simple fact is that over the last number of years, we have positioned the Caremark model and its broader value proposition to the point where in 2018, we expect retained rebates to be about \$300 million, or about 3% of our annual adjusted earnings per share.”* (emphasis added).

In its own quarterly earnings report just two days prior, on August 1, 2018, Express Scripts disclosed: *“Rebates are applicable to less than 10% of Express Scripts’ claims; Express*

Scripts retains approximately \$400 million of rebates.” With Express Scripts reported net income of \$4.5 billion in 2017, retained “manufacturer rebates” accounted for a maximum of 9% of their overall profits, and potentially far less. See CVS Health and Express Scripts 2Q 2018 SEC filings and earnings conference call transcripts.

Despite the prior widely held view that “manufacturer rebates” account for a large proportion of PBM profits, no Wall Street analyst asked the senior managements of either CVS or Express Scripts on the earnings conference calls about the major source of company profits. Of course, as set forth in the Second Amended Complaint, the long-standing “dark secret” is “manufacturer service fees”, commonly linked to massive US drug prices and price increase. *See SAC generally. See CVS Health and Express Scripts 2Q earnings conference call transcripts.*

Astoundingly, even following these PBM Defendant disclosures, the press still refers to manufacturer “rebates” and “discounts” as the primary profit source for the PBM Defendants. Just the other day, on November 15, 2018, Express Scripts announced plans for a “new formulary” that “upends the status quo by creating a path to preferred status for drugs that have lower list prices.” The Bloomberg article begins: “Express Scripts Holding Co. and other pharmacy-benefit managers make money by negotiating drug prices on behalf of health-plan providers. The list prices that pharmaceutical companies set for their drugs diverge wildly from their real cost, and PBMs widen and feast on the gap, which helps make them some of the principal beneficiaries of America’s byzantine pricing system.” Ironically, putting lower price drugs on their formularies is exactly what the PBM Defendants have been deceitfully claiming to be doing for the past decade-plus, while they are actually fraudulently making most of their profits via secretive “manufacturer service fees” linked to massive “list” prices. *Lower Drug Prices Get an Assist from a Big Player, Bloomberg, November 15, 2018.*