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COOPERATING TO COMPETE:
ANTITRUST ANALYSIS OF HEALTH CARE JOINT VENTURES

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ARTICLE

COOPERATING TO COMPETE: ANTITRUST ANALYSIS OF HEALTH CARE JOINT VENTURES

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I. INTRODUCTION

Antitrust is unlike many other areas of the law. It involves a relatively brief statute, that has existed for over a century with relatively few changes. The statute itself speaks in terms of broad concepts and provides few specifics. Because of its general nature, it has been sufficiently resilient and elastic to meet the challenges of various markets and different eras of the United States economy.

One particularly important success story for antitrust was the health care market. As a regulated profession, physicians had generally been viewed as exempt from the antitrust laws.[1] In its 1975 decision in *Goldfarb v. Virginia State Bar*,[2] the Supreme Court disposed of any notions that health care providers were somehow above the antitrust laws. With antitrust enforcement as nurse-maid, managed care and new forms of competition were able to take shape and the health care marketplace was transformed.

But by the mid-1990s, there were voices calling for reform of the antitrust laws in the health care area. The public policy problem was a simple but important one: health care was increasingly dominated by large powerful buyers,

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1. Goldfarb v. Virginia State Bar, 421 U.S. 773, 779 (1975).
2. *Id.* at 787.

insurance companies, health maintenance organizations and others. Because these organizations represented large numbers of consumers, physicians and other health care providers were compelled to affiliate as providers. Some of these insurers became very large, but antitrust treats single firms benignly unless they possess substantial market power, hence, there was little or no scrutiny as these buyers became large and powerful.[3]

Occasionally groups of health care providers attempted to participate in this intermediary market by forming their own managed care operation.[4] Besides the substantial costs of vertically integrating, they faced an additional barrier—antitrust law was perceived as inhospitable to these endeavors. Under the antitrust laws, most restraints and arrangements are evaluated under a broad rule of reason that balances procompetitive and anticompetitive effects.[5] However, collective activity is scrutinized far more carefully and can be condemned under a rule of presumptive illegality—the so called per se rule.[6] Providers complained that when they attempted to act collectively, the antitrust agencies brought the weight of the antitrust laws to bear, restricted the size of these endeavors and threatened them with prosecution.[7]

During the legislative debate on the Policy Statements, Professor Clark Havighurst of Duke University School of Law, an influential antitrust scholar who generally encouraged the vigorous enforcement of the antitrust laws to the health care profession, criticized the agencies for restricting the ability of doctors to create these new forms of joint ventures. Havighurst summed up the problem as follows:

> Although the health care industry is undergoing a remarkable transformation, the one group of players that might develop the most efficient systems for delivering high-quality personal health care at reasonable cost are somewhat constrained in doing so by the way antitrust law is currently applied to their endeavors. Specifically, physicians organizing joint ventures for the purpose of marketing themselves to major purchasers are being forced by unrealistic antitrust standards into arrangements that may serve consumers less well than arrangements that such standards foreclose.[8]

Politically, in the 1990s there were regular calls for legislation to give

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3. *See generally* Note, *Agency Review of Health Care Industry Mergers: Proper Procedure or Unnecessary Burden?*, 10 ADMIN. L.J. AM. U. 291 (1996).

4. *See generally* U.S. DEP'T OF JUSTICE & FEDERAL TRADE COMM'N, STATEMENTS OF ANTITRUST ENFORCEMENT POLICY IN HEALTH CARE (1996) [hereinafter 1996 POLICY STATEMENTS], *reprinted in* 4 Trade Reg. Rep. (CCH) ¶ 13,153.

5. *Id.*

6. *Id.*

7. *See, e.g.*, Kathleen Day, *Care Providers Urge Easing of Antitrust Laws*, WASH. POST, Mar. 24, 1993, at F1.

8. Clark C. Havighurst, *Are the Antitrust Agencies Overregulating Physician Networks?* 8 LOY. CONSUMER L. REP. 78, 81 (1996).

more liberal treatment to physician sponsored network ventures.[9] This issue came to a head in the 104th Congress, when House Judiciary Committee Chairman Henry Hyde, and over one hundred fifty cosponsors introduced H.R. 2925, which, would have mandated rule of reason treatment for health care provider networks that meet certain statutory criteria.[10] Federal Trade Commission ("FTC") Chairman Pitofsky testified in February 1996, in opposition to the bill, and stated that the Commission, in consultation with the Department of Justice, would issue further guidance on the application of the antitrust laws to health care provider networks in less than six months.[11]

In August 1996, the agencies issued the revised Statements of Antitrust Enforcement Policy in Health Care ("the Policy Statements").[12] This article addresses the impact of the law and the revised Policy Statements on the ability of health care providers to organize their own ventures and enter into the managed care marketplace. As an example, the article discusses the creation of a pharmaceutical benefit manager network by a group of pharmacies.[13]

The article is organized as follows. It begins with a discussion of the formation of an important new intermediary in the delivery of pharmaceuticals—Pharmaceutical Benefit Managers ("PBMs"). PBMs are increasingly serving as a critical mechanism in controlling pharmaceutical costs. The second section discusses the role of networks generally and the antitrust analysis of the networks. The third section discusses the antitrust analysis of joint ventures and how that analysis has been applied to health care ventures. It explains how a pharmacy joint venture would be analyzed and how to avoid antitrust condemnation.

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9. *See, e.g.*, H.R. 2925, 104th Cong. (1996). The House Judiciary Committee approved the Hyde bill on March 12, 1996. *See House Judiciary Approves Bill Easing Antitrust Review of Provider* Networks, 5 Health L. Rep. (BNA), at 378 (Mar. 14, 1996). *See also* Thomas L. Greaney, *Much Ado About* Networks, 29 J. HEALTH & HOSP. L. 307 (Dec. 1996) (describing legislative debate); *Docs Get Their Way: Under AMA Attack, Feds Back Off Antitrust Enforcement*, MOD. HEALTHCARE, Jan. 8, 1996, at 40 (describing AMA efforts to obtain statutory immunities).

10. *Id.*

11. *Health Care Revision Issues: Hearings on H.R. 2925 Before the House Judiciary Committee*, 104th Cong. (1996) (statement of Robert Pitofsky, Chairman of the Federal Trade Commission).

12. 1996 POLICY STATEMENTS, *supra* note 4.

13. *See infra* Section II. The analysis specifically addresses the antitrust issues raised by a joint venture of pharmacies. Joint ventures of other health care providers, such as physicians, may raise different sets of antitrust issues.

II. THE PBM INDUSTRY

A. Introduction—The Revolution in the Delivery of Pharmaceuticals

One of the most significant developments in the health care revolution is the creation of Pharmaceutical Benefit Managers ("PBMs").[14] PBMs have been formed in recent years in response to a number of developments, notably the increasing inclusion of pharmacy benefits in health care packages, and the demand for cost-controlling managed care principles—which are now in wide use in other health care markets—in the administration of those benefits. PBMs were virtually unheard of a decade ago, but they now administer pharmacy benefits plans covering more than 150 million people, and that number is expected to increase to more than 200 million by the end of the decade.[15]

PBMs serve a number of functions, including the establishment and administration of a retail pharmacy network, computerized claims processing and drug utilization review, and the establishment of formularies, or lists of FDA-approved drugs that are available through the PBM.[16] These functions combine to enable PBMs to play a significant role in cost containment. For example, a PBM can negotiate rebates and other discounts from drug suppliers on behalf of its customers by offering the suppliers' drugs a place on its formulary in exchange for a discount.[17]

PBMs provide managed prescription drug programs to corporations, labor unions, retirement systems and federal and state employee plans ("plan sponsors"). PBMs select participating pharmacists and drug manufacturers and suppliers, create and administer a point of sale claims processing system, negotiate quantity discounts with pharmaceutical manufacturers, administer the record keeping and payments systems of the plans and maintain quality control. A PBM acts as the agent for the plan sponsor to influence product selection—encouraging generic and therapeutic substitution based on negotiated prices with manufacturers. Additional services offered by a PBM may include drug utilization review, quality control, and mail order service.[18]

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14. Managed care has had a significant economic impact on prescription drug markets. *See, e.g.*, Kenneth R. Cohen, *Managed Competition: Implications for the U.S. Pharmaceutical Industry*, 7 J. RES. IN PHARMACEUTICAL ECON. 29 (1996); Dev S. Pathak and Alan Escovitz, *Managed Competition and Pharmaceutical Care: An Answer to Market Failure?*, 7 J. RES. IN PHARMACEUTICAL ECON. 1 (1996); Hemant K. Shah, *Redefining the Pharmaceutical Industry*, 7 J. RES. IN PHARMACEUTICAL ECON. 19 (1996).

15. Health Industries Research Center, *National Accounts: Marketing Challenges and Opportunities for the 1990s*, at II-7 (1996).

16. *See generally* GENERAL ACCOUNTING OFFICE, PHARMACY BENEFIT MANAGERS—EARLY RESULTS ON VENTURES WITH DRUG MANUFACTURES 5 (GAO/HEHS-96-45 1995) [hereinafter GAO REPORT].

17. *Id.*

18. *Id.*

Formularies are an important way in which PBMs bring managed care to pharmaceutical markets. Like physician and hospital services that are covered by benefits packages, the supply of pharmaceuticals is governed in part by physicians' prescribing patterns that may not fully take into account cost considerations. By providing information and restricting reimbursement for certain drugs, formularies can influence the prescribing patterns of physicians and provide a way for the PBM to control costs to the ultimate benefit of consumers.[19]

A formulary typically designates drugs for which consumers may receive reimbursement. Clinical evaluations are performed by each PBM to determine therapeutic equivalence. After a PBM establishes a formulary that includes, for example, a therapeutic class of cholesterol lowering drugs, the PBM would next seek competitive bids from all the manufacturers of cholesterol lowering drugs and select the best bid. The drug manufacturer providing the best bid would be indicated in a preferred position in the formulary.[20]

PBMs also serve as group buying agents on behalf of their plan sponsors. PBMs are able to aggressively negotiate for discounts with pharmaceutical manufacturers by aggregating the plan sponsors' buying power and by offering preferential positions on the formulary. Costs for the items on the formulary are often based upon negotiated volume discounts from the pharmaceutical manufacturer. The PBM service then includes programs designed to encourage physicians to consider prescribing the formulary preferred drug rather than a competing, therapeutically equivalent drug. This process is generally referred to as "share shifting" because through this mechanism, the PBM company can increase a drug manufacturer's market share.[21]

In addition to using a distribution method for filling prescriptions, PBMs offer several types of cost containment features, such as drug utilization review,[22] generic drug preference programs[23] and discounted drug prescription programs.[24] PBMs also provide on-line claims processing and can often fill prescriptions at a lower cost than patients filing claims after obtaining and paying for the drug directly at their local retail pharmacy.[25]

PBMs were initially formed by a variety of entities, including managed care organizations, claims processors, and mail order pharmacies. One of the most dramatic and controversial aspects of the PBM market was the acquisition of the three most prominent PBMs in the mid-1990s—MEDCO, PCS and DPS—by pharmaceutical manufacturers (respectively, Merck, Lilly and

19. *Id.*
20. *Id.*
21. *See* GAO REPORT, *supra* note 16, at 7.
22. *Id.* at 8.
23. *Id.*
24. *Id.*
25. *Id.*

SmithKline).[26] These three firms currently have about 132 million beneficiaries and over 50% of the PBM market in terms of beneficiaries and almost 70% in terms of prescriptions.[27]

B. *FTC Enforcement Action*

These acquisitions have raised a great deal of controversy in the press and before Congress.[28] Since the purpose of PBMs was, in part, to aggregate buying power on behalf of plan sponsors and their subscribers to secure lower drug prices, it is understandable that the acquisition of the most prominent PBMs by the manufacturers would raise concerns. Two specific concerns are: (1) that the manufacturers will utilize the PBM to foreclose competitor's products from the market; and (2) that the manufacturers will use the PBM, or other PBM directed incentives to encourage or force pharmacists to favor the manufacturer's drugs.[29]

Partially in response to these concerns, the FTC entered into a consent order with Eli Lilly about its acquisition of PCS in 1995.[30] The FTC's complaint charged that the PCS acquisition would harm competition in the national full-service PBM market. The complaint alleged that as a result of the acquisition, products of drug manufacturers other than Lilly could be foreclosed from the

26. *See* Elinor R. Hoffman & C. Allen Garrett, *What's Driving the Vertical Integration*, AM. DRUGGIST, May 1995, at 30; *Doubts Emerge About Drug Industry Merges*, BUS. & HEALTH, Nov. 1, 1994, at 53; GAO REPORT, *supra* note 16. *See also Pharmacy Benefit Managers—Early Results on Ventures With Drug Manufacturers: Hearings Before the Committee on Insurance California State Senate*, (Cal. 1996) (statement of John C. Hansen, Assistant Director Health Financing and Public Health Issues Health, Education, and Human Services Division). The report described both the procompetitive and anticompetitive aspects of these acquisitions. In particular, it noted the opportunity for manufacturer-owned PBMs to exclude drugs that competed with the parent's drugs and ultimately harm competition. The report noted that the Medco formulary was changed around the time of the Merck acquisition to favor several Merck drugs and exclude some competitive drugs. *Id.*

Another study found that after the Medco acquisition, Merck's volume for its own drugs increased by ten percent in the second quarter of 1994 and fifteen percent in the third quarter of 1994. *See* Kevin A. Schulman, et al, *The Effect of Pharmaceutical Benefit Managers: Is it Being Evaluated?* 124 ANNALS OF INTERNAL MED. 906, 911 (1996).

27. HEALTH INDUSTRIES RESOURCE CENTER, NATIONAL ACCOUNTS REPORT (Spring/Summer 1997).

28. *See supra* note 26.

29. For a more detailed discussion of these concerns, see David A. Balto, *A Whole New World?: Pharmaceutical Responses to the Managed Care Revolution*, 52 FOOD & DRUG L.J. 83 (1997). *See generally* Christine Dodd, *The Merck-Medco Merger: An Isolated Incident or a Catalyst for the Transformation of an Industry?*, 63 U. CIN. L. REV. 1767 (1995).

30. *In re* Eli Lilly, No. C-3594 (July 28, 1995) (Azcuenaga, Comm'r, dissenting); 59 Fed. Reg. 60,815 (Nov. 28, 1994) (proposed consent agreement and analysis to aid public comment); 61 Fed. Reg. 31,117 (July 31, 1996) (final consent order and Commission statement) [hereinafter Consent Order].

PCS formulary and that PCS would be eliminated as an independent negotiator of pharmaceutical prices with manufacturers. The complaint also alleged that the acquisition could facilitate collusion through reciprocal dealing, coordinated interaction, and interdependent conduct among Lilly and other vertically integrated pharmaceutical companies. In addition, the complaint alleged that entry into PBM and certain pharmaceutical markets may be more difficult because it could require entry at more than one level. The complaint further alleged that the impact of the acquisition in the affected pharmaceutical markets likely would be to increase prices, diminish quality and reduce the incentives of other manufacturers to develop innovative pharmaceuticals.[31]

The consent order has two principal provisions which address potential foreclosure and collusion. The first provision requires Lilly to maintain an open formulary, which would not give unwarranted preference to Lilly products, but also allows Lilly to offer a closed formulary. The second provision, a "firewall," precludes communications between Lilly and PCS concerning bids, proposals, prices or other information related to other drug manufacturers' products.[32]

The Order's open formulary would help prevent anticompetitive foreclosure of competing drug manufacturers. As used in the Order, an "open formulary" is not one on which every FDA-approved drug must be listed. Rather, under the Order, an independent Pharmacy and Therapeutics Committee, utilizing only objective criteria, decides which drug products to include on the formulary. To ensure Lilly can not thwart the intent of the Order by refusing to accept discounts or rebates on other products (thereby giving Lilly products preference on the formulary or making the formulary so expensive that no one will use it), the Order prevents Lilly from refusing to accept discounts and from inaccurately reflecting such discounts on the formulary.[33]

Since the Order requires an open formulary, new entrants to pharmaceutical markets would face lower entry barriers because they would not need to enter at both levels of the industry. The open formulary would provide access for new products that offer an objective advantage over existing products.

C. *Past Antitrust Scrutiny of Joint Venture Pharmacy Benefit Managers*

One important function of PBMs is that they serve as distribution networks. PBMs recruit pharmacies to participate in their network. The PBM-pharmacy agreement typically requires the pharmacy to accept any contract negotiated with a plan sponsor. This requirement is imposed so that consumers know that their PBM membership will be accepted whenever they see a PBM network's logo at a pharmacy. In the typical situation small independent

31. *See* Balto, *supra* note 29.
32. *Id. See also* Consent Order, *supra* note 30.
33. *Id.*

pharmacies may have at best a minor role in negotiating with the PBM—offers are often made on a take it or leave it basis.[34]

Independent pharmacies are in a particularly weak bargaining position with respect to PBMs. In order to attract plan sponsors in a given area, PBMs must offer a network of pharmacies geographically dispersed throughout that area. This kind of extensive coverage can only be provided cost effectively by chain pharmacies with multiple locations in various geographic areas.[35]

In FTC investigations of mergers between chain pharmacies, the analysis has focused on the market for providing retail pharmacy services for PBMs.[36] The investigations determined that most PBMs initially secure contracts with the large chains, which serve as an "anchor" for the network.[37] These chains can bid more aggressively than independent pharmacies because of their economies of scale.[38] Moreover, there are significant transactions costs savings. Given the choice of signing up a single chain with three hundred stores with one contract, or three hundred independent stores with separate contracts, a PBM will invariably select the chain.[39] Because of the transactions costs involved and the chain's economies of scale, from the perspective of the PBM's, independent pharmacies can not serve as an anchor.

Only after the chain is signed up, does the PBM fill out the remainder of the network by signing up independent pharmacies.[40] Independent pharmacies still present higher transactions costs in terms of contracting, communicating, billing, quality control and monitoring.[41] Because of the higher transactions costs, independent pharmacies are often excluded or are only included at a lower reimbursement rate.[42]

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34. *See generally* Balto, *supra* note 29.

35. George S. Cary, Deputy Director for Mergers, Bureau of Competition, *Staying Ahead of the Merger Wave* (visited Oct. 8, 1997) <http://www.ftl.gov/speeches/ftc/other/corp/htm> (Remarks before the 15th Annual Corporate Counsel Institute on Dec. 12, 1996). "[P]rices to third party payors and their PBMs are effectively established by competition between the lowest cost suppliers, which are inevitably the larger chain drug stores who benefit from economies of scale. Only after a price level is set through this competition do smaller, higher cost retail operations join the third party payor's network. However, these higher cost independents would not themselves compete prices down to that same level in the absence of chain store competition." *Id.*

36. Balto, *supra* note 26, at 84.

37. Cary, *supra* note 35.

38. *Id. See also* Donald I. Baker, *Compulsory Access to Network Joint Ventures Water the Sherman Act: Rules or Roulette?*, 1993 UTAH L. REV. 999, 1010 (1993).

39. *See* Dodd, *supra* note 29, at 1781.

40. Cary, *supra* note 35.

41. *Id.*

42. *Id.* In several states, independent pharmacies have responded to this problem seeking legislation to require PBMs to be open to "any willing provider." *See generally Recent Legislation, Health Care Law—HMO Regulation—Arkansas Requires HMOs to Accept Any Provider Willing to Join Their Networks—Patient Protection Act*, 1995 Ark. Acts 505, Amended by 1995

In order to overcome these transactions costs, some groups of independent pharmacies have entered into joint venture PBM's. For example, in the early 1990's over 400 independent pharmacies in Maryland and the metropolitan D.C. area formed a joint venture PBM known as EPIC.[43] The venture, now about five years old, has successfully competed against some of the larger PBM's.[44]

In 1986, the Antitrust Division of the Department of Justice approved the formation of two pharmacy-sponsored PBM's: Service For You ("SFY") and Pharmaceutical Care Network ("PCN").[45] The Division initially noted that the formation of PBM's

> can benefit the public by increasing competition among providers. By offering consumers another type of prescription drug delivery system to compete with chain drugstores, prescription card services, and other methods of providing prescription drug services, [these entities] may spur greater cost-containment efforts and contribute to lower health care costs.[46]

The Division stated that they would be concerned if the effect of the operation of PCN were to facilitate anticompetitive price-fixing agreements among providers or to inhibit significantly the formation and entry of other joint ventures that would provide competing services to third-party payers.[47] The Division listed several factors relevant to their analysis such as: the proportion of the total number of providers in the market who are members; the availability of actual or potential competitive alternatives to the PBM; the activities of the PBM that could limit competition among members, such as engaging directly in the setting of prices or fees on behalf of its members; whether the PBM's members are free to participate in competing organizations; whether the parties have an anticompetitive purpose, such as the exclusion of competing health care delivery systems; and any procompetitive bene-

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Ark. Acts. 1193, 109 HARV. L. REV. 2122 (1996). This type of legislation has been considered in over 30 states. *Id.* at 2124.

43. Margie Freany, *Ailing Drugstores Seek Life-Saving Prescription*, BALT. BUS. J., Aug. 20, 1993, Sec. 1. A similar venture of independent pharmacies, American Family Pharmacy, was formed by the National Wholesale Druggists Association and the American Pharmaceutical Association. Ken Rankin, *AFP is Latest Effort to Rescue Independents*, DRUG STORE NEWS, Dec. 9, 1996, at 33.

44. *See* Calvin H. Knowlton, President, Amer. Pharmaceutical Ass'n, Testimony before FTC Hearings on the *Changing Nature of Competition in a Global and Innovation-Driven Age* (Nov. 8, 1995) (describing the efficiencies from pharmacy-sponsored PBMs) (transcript available at FTC Headquarters and at FTC website, http://www.ftc.gov).

45. The Department's position was stated in separate business review letters from Charles F. Rule, Acting Assistant Attorney General, *Antitrust Division*, to Robert Taylor, Antitrust Counsel for PCN and to Frank Sanchez, Coordinator for SFY, (October 3, 1986) (available in WESTLAW in FAIR-BRI database).

46. *Id.* (Letter from Rule to Sanchez).

47. *Id.*

fits likely to result from the integration.[48]

As to PCN, there was no concern over the exercise of market power because the venture was non-exclusive and PCN limited the size of its venture to a thirty percent market share of the retail pharmaceutical market in each county, except in rural areas.[49] Price fixing was not of concern because the venture did not set the prices of the PBM. Rather it served as a messenger of bid information between the plan sponsor and participating pharmacies.[50]

The analysis of the SFY venture was similar. However, unlike PCN, SFY actually set prices for the PBM. The Division observed that "the negotiation of price can have anticompetitive effects, but also can be an integral part of a demonstrably procompetitive" venture.[51] The Division observed that SFY would not exceed a thirty percent market share (in terms of prescription drug sales in the county).[52] Thus, there were significant providers who were not members of SFY and who remained free to compete against SFY either alone or through participation in competing PPOs.

III. THE ROLE OF NETWORKS GENERALLY

The following provides a brief discussion of the role of networks to put the issues presented by this article in a larger context. Networks, such as PBM's, play a vital role in the economy and antitrust has generally not interfered with their creation.[53]

A network is a mixture of facilities and rules that allow a firm or group of firms to exchange or share transactions, data, electronic impulses, information, energy or physical traffic.[54] Networks play an increasingly vital role in today's economy. The dramatically declining costs of communication, permit networks firms to provide services of a scale and scope heretofore unknown. Moreover, networks permit the creation of new products or markets, where previously there was no market at all.[55] "The new networks provide magnificent opportunities for innovation. . . . The sheer diversity of the new networks now being developed makes it hard to see what the finished product will look

48. *Id.*

49. *Id.* (Letter from Rule to Taylor).

50. *Id.*

51. *Id.*

52. *Id.* (Letter from Rule to Sanchez).

53. For a thoughtful survey of various types of networks and the antitrust issues they face, see STEVEN S. WILDMAN & MARGARET E. GUERIN-CALVERT, ELECTRONIC SERVICES NETWORKS: A BUSINESS AND PUBLIC POLICY CHALLENGE (1991).

54. Thomas A. Piraino, Jr., *The Antitrust Analysis of Network Joint Ventures*, 47 HASTINGS L.J. 5, 6 (1995). *See also* Courtney G. McKenzie, *Lawyers and the Internet: Are You Connected?*, SOUTH CAROLINA LAWYER, Sept./Oct., 1996, at 21.

55. *See* Piraino, *supra* note 54, at 21-22.

like."[56]

Networks are owned both by single firms and joint ventures.[57] A joint venture is a particularly attractive device for creating a network because any single firm may lack the level of demand, the number of distribution outlets or potential output to justify the creation of a single network. A joint venture network may overcome the significant transactions costs involved in entering into vertical contracts with its members. A joint venture also enables firms to share the risks of new entry into the network market. In many cases, joint ventures have permitted groups of relatively small competitors to join together and offer a network facility similar to that offered by larger firms.[58] Some of the most important and prominent networks in the United States, including credit card and ATM networks, are joint ventures.[59]

Networks provide a wide variety of competitive benefits. By combining the traffic of numerous users in communications, networks tend to decrease per-unit transmission costs, and hence provide significant economies of scale. Some networks, such as PBM's, are driven by the need to provide a service over a wide geographic area or with a certain level of coverage. A network such as a stock exchange floor or a multiple listing service may be efficient because it creates a market. Risk sharing and the creation of new products are other efficiencies brought about by networks.[60]

The history of networks provides several examples of where groups of competitors have joined together to compete in a network market dominated by single firms. Among the most outstanding examples are financial services. The initial credit card networks, National BankAmericard (now VISA), American Express and Diners Club were all owned by single firms (in the case of BankAmericard, a single bank).[61] Individual banks offered credit card programs, but these could not effectively compete with the national networks because these programs operated in relatively small geographic areas. In order to effectively compete with the national networks, groups of banks formed regional joint ventures to provide a wider scale of access.[62] In the 1970s, these networks merged into a single network—InterBank—which eventually became Mastercard.[63]

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56. *The Fruitful, Tangled Trees of Knowledge*, ECONOMIST, June 20, 1992, at 85.

57. *See* MCI Communications Corp. v. A.T.&T. Co., 708 F.2d 1081, 1131 (7th Cir. 1983), *cert. denied*, 464 U.S. 891 (1983).

58. *See* Baker, *supra* note 38, at 1003.

59. *See* Piraino, *supra* note 54, at 5.

60. *Id.* at 21.

61. *See* Jeffrey Kutler, *Smart Card Forum Eyes Past for Light on Present Series*, AM. BANKER, Sept. 20, 1996, at 11.

62. For a general history of the development of bank cards see Baker, *supra* note 38, at 1057-61.

63. *Id.* at 1057. These ventures have survived challenge under the per se rule. *See, e.g.*,

Not all banks issue their own credit cards. Historically, smaller banks relied on correspondent relationships with larger banks which issued the cards on behalf of their smaller counterparts. Because of the size of the banks, they paid comparably high fees for this service. In the 1970s, the Independent Bankers Association of America formed a joint venture, owned by its members, to perform card-issuance and related activities on behalf of its members.[64] The venture currently provides these services for thousands of small banks. It is one of the largest card-issuers in the United States, and recently secured a seat on the VISA Board of Directors.[65]

Similarly, in many metropolitan areas, shared Automated Teller Machine ("ATM") networks arose in response to relatively dominant networks owned by a single bank. For example, in New England, the YANKEE 24 ATM network was formed by a group of smaller banks, none of which individually justify a large ATM network, in order to enable these banks to compete against the ATM networks of larger banks.[66] The creation of shared regional networks in other metropolitan areas has followed a similar course.[67]

Examples abound in other industries. For example, during the 1960's and 1970's many investor-owned utilities, including both large and small firms, along with municipal and cooperative utilities formed "electric power pools."[68] The purpose of these pools was to facilitate power transactions between firms.[69] Such purchases could help the firms reduce reliability costs (economies of massed reserves), as well as take advantage of differences in the timing of demand peaks (reduce investments in costly peaking plants). Small utilities also pooled efforts to realize economies in transactions costs and to improve their bargaining position with suppliers of surplus power.

One of the most recent examples involves the WORLDSPAN computer

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Worthen v. National Bank/Americard, Inc., 485 F.2d 119, 127 (8th Cir. 1973) (rejecting application of *per se* rule to joint venture exclusivity rule), *cert. denied*, 415 U.S. 918 (1974); National Bancard Corp. ("NaBanco") v. VISA U.S.A., Inc., 596 F. Supp. 1231 (S.D. Fla. 1984) (upholding interchange fee established by credit card joint venture), *aff'd*, 779 F.2d 592 (11th Cir.), *cert. denied*, 479 U.S. 923 (1986).

64. *See* Independent Bankers Assoc. of America v. Smith, 534 F.2d 921, 962 (D.C. Cir. 1976).

65. *See FCRA Legislation Expected to Emerge in New Session of Congress*, FIN. SERV. REP., Nov. 21, 1990, at 6 (noting that Bancard Chairman Charles T. Doyle won a seat on Visa's board of directors as a "Special Director at Large").

66. *See* David A. Balto, *Access Demands to Payment Systems Joint Ventures*, 18 HARV. J. L. & PUB. POL'Y 623, 629 (1995).

67. *Id. See In re Arbitration Between First Texas Savings Ass'n and Financial Interchange, Inc.*, 55 Antitrust & Trade Reg. Rep. (BNA) NO. 1380, at 340 (Aug. 25, 1988) (collective price setting not per se illegal; striking down price restraints under rule of reason analysis).

68. *See* Baker, *supra* note 38 at 1006-07.

69. *Id.* at 1010. *See* Central Iowa Power Cooperative v. FERC, 606 F.2d 1156 (D.C. Cir. 1979).

reservation service ("CRS") network. CRS networks enable travel agents to access flight information by computer, make reservations and purchase tickets. The CRS market has been dominated by the APPOLLO and SABRE networks, owned respectively by United and American Airlines. A group of large carriers including Northwest, Delta, and TWA formed WORLDSPAN to enable them to effectively compete in the CRS market.[70]

These ventures are only a small sample of the hundreds of network joint ventures which perform valuable functions in our economy. Many of these networks engage in joint price setting.[71] Although each of the ventures described above has been subject to scrutiny by the Antitrust Division, none have ever been challenged. As explained below, under a narrow application of precedent each of these ventures could have been condemned as per se illegal. Whatever rule of law that is applied should take into account the established, procompetitive role of these network ventures.

IV. JOINT VENTURE ANALYSIS

Courts and enforcement agencies have applied a two-part analysis to the activities of joint ventures: (1) does the joint venture reflect legitimate integration or a thinly-guised cartel?; and (2) if a legitimate joint venture imposes restraints upon its members, are those restraints reasonably necessary to the efficiencies sought to be achieved by the venture?[72] As will be described below, careful and extensive analysis is necessary to avoid per se condemnation. Nevertheless, an independent pharmacy joint venture PBM should pass muster.

A. Legitimate or Sham

Under modern antitrust analysis, joint ventures and their attendant restraints are typically analyzed under the rule of reason. Recent Supreme Court cases such as *Broadcast Music, Inc. v. Columbia Broadcasting Systems*

70. Robert A. Skitol, *Analysis New DOJ-FTC-State Cooperation Initiatives: More and Less Than Meets the Eye*, FTC WATCH (Washington Regulatory Reporting Associates, Washington, D.C.), Mar. 9, 1992.

71. For example, members of electric power pools jointly decide on the price that the pool's power will be sold to third parties. *See* Central Iowa Power Cooperative v. FERC, 606 F.2d 1156 (D.C. Cir. 1979). Similarly, ATM networks bid, on behalf of their bank members, to provide electronic benefits programs for welfare recipients. *See also* Milton Mueller, *Telecommunications Access in the Age of Electronic Commerce: Toward A Third-Generation Universal Service Policy*, 49 FED. COMM. L.J. 655, 666-67 (1997). In each case, the venture acts as a joint sales agent for its members. This "price fixing" has never raised antitrust concerns, because these ventures do not prevent their members from competing with the venture. *See also* Business Review Letters, *supra* note 45.

72. *See* 1 ANTITRUST LAW DEVELOPMENTS (FOURTH) 395-96 (A.B.A. Section of Antitrust Law ed., 1997); 1996 POLICY STATEMENTS, *supra* note 4.

(*"BMI"*),[73] *National Collegiate Athletic Association v. Board of Regents* (*"NCAA"*),[74] and *Northwest Wholesale Stationers, Inc. v. Pacific Stationary & Painting Company*[75] emphasize the primacy of the rule of reason. In each case, the Court rejected the opportunity to condemn joint venture restraints under the per se rule, choosing rather to analyze the restraints under the rule of reason.[76] This approach finds support in the legislative history of the National Cooperative Production Act which compels rule of reason analysis for certain joint ventures.[77]

However, there is a threshold inquiry as to whether the venture is legitimate or simply a sham endeavor for masking cartel-like behavior. The label "joint venture" is not dispositive. As the Supreme Court recognized over fifty years ago, simply labeling an agreement as a "joint venture" will not immunize it from antitrust scrutiny.[78] Where a so-called "joint venture" does not involve any integration of resources and is really no more than an attempt by horizontal competitors to restrict competition, the courts and enforcement agencies have condemned the joint activity as a "naked restraint of trade," and invalidated it as unlawful per se.[79]

Thus, the initial inquiry is whether the venture is legitimate or sham, that is, whether it possesses the potential for such efficiencies that it can avoid condemnation under the per se rule. This is a crucial inquiry. If an arrangement is evaluated under the per se rule, the plaintiff invariably will prevail since there is no consideration of defenses such as the purpose or size of the venture. Thus, under the per se rule, a venture of two physicians that sets prices in a large metropolitan area will be illegal and may even subject the competitors to criminal penalties.[80] Finally, since this inquiry is about the legitimacy of the venture, per se condemnation carries a stiff penalty—the dissolution of the venture.[81] As such, unless a proposed venture is legitimate in the antitrust

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73. 441 U.S. 1 (1979).

74. 468 U.S. 85 (1984).

75. 472 U.S. 284 (1985).

76. *See BMI*, 441 U.S. at 16; *NCAA*, 468 U.S. at 100; *Northwest Wholesale Stationers, Inc.*, 472 U.S. at 297.

77. *See* National Cooperative Production Act Pub. L. No. 103-42, 107 Stat. 117, § 3(c)(5) (1993) (codified 15 U.S.C. § 4301).

78. Timken Roller Bearing Co. v. United States, 341 U.S. 593, 598 (1951) (holding arrangement to divide markets was illegal per se). *See Brunswick Corp.*, 94 F.T.C. 1174, 1266 (1976) ("A price-fixing scheme or other cartel-like behavior cannot be insulated from review simply by fixing the 'joint venture' label to a device used to engage in behavior inherently pernicious to competition."), *modified*, 96 F.T.C. 151 (1980), *aff'd sub nom.*, Yamaha Motor Co. v. FTC, 657 F.2d 971 (8th Cir. 1981), *cert. denied*, 456 U.S. 915 (1982).

79. *In re* Brunswick Corp., 94 F.T.C. 1174, 1979 F.T.C. LEXIS 107, 233 (1979).

80. *See* United States v. Alston, 974 F.2d 1206, 1210 (9th Cir. 1992) (holding that price fixing among health care professionals was per se illegal and subject to criminal prosecution).

81. *See id.* at 1209.

sense, it cannot be created.

On the other hand, if the venture is legitimate, it must be analyzed under the rule of reason. Under that mode of analysis, there is a more complete consideration of the purpose and effects of an arrangement or given restraint.[82] Typically the plaintiff must demonstrate that the activity at issue is anticompetitive in a defined relevant market.[83] The defendant has the opportunity to demonstrate that the anticompetitive effect was small or that there were countervailing efficiencies.[84] The burden of showing that the practice is on balance anticompetitive remains with the party challenging the venture.[85]

Thus, the determination of whether the per se rule or the rule of reason will be applied is often outcome determinative. The courts have identified two principal factors, either of which may support the existence of integrative efficiencies. First, whether the joint venture leads to the creation of a new product or is a prerequisite to marketing that product. Second, whether the joint venture involves integration between the parties, such as a pooling of resources and risk sharing.[86] Although the courts have not identified any clear bright lines in determining whether either of these tests are met, they often have implemented the first test and analyzed the joint venture under the rule of reason.[87] In contrast, the agencies appear to have focused exclusively on the second test, and until recently, looked at risk-sharing as the critical form of integration.[88]

1. New Product—Supreme Court Precedent

Modern analysis of the efficiencies of joint ventures begins with *Broadcast Music, Inc. v. Columbia Broadcasting System*.[89] In that case, Broadcast Music, Inc. ("BMI") and the American Society of Composers, Authors and Publishers ("ASCAP") issued blanket licenses to copyrighted music compositions.[90] ASCAP and BMI set the fees for these licenses and, as such, clearly qualified as price fixing in a strict sense. The Court, however, noted that

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82. *See* National Society of Professional Engineers v. United States, 435 U.S. 679, 692 (1978) (noting that the purpose of the rule of reason analysis is to evaluate the competitive significance of the restraint); Chicago Bd. of Trade v. United States, 246 U.S. 231, 238 (1918) ("The true test of legality is whether the restraint . . . merely regulates and perhaps thereby promotes competition or whether it . . . may suppress or even destroy competition.").

83. Alan J. Meese, *Antitrust Balancing in a (Near) Coasean World: The Case of Franchise Tying Contracts*, 95 MICH. L. REV. 111, 123-24 (1996)

84. *Id.*

85. *Id.*

86. ANTITRUST LAW DEVELOPMENTS (THIRD) 373 (A.B.A. Section of Antitrust Law ed., 1992).

87. *Id.* at 375.

88. *See generally In re* Brunswick Corp. 94 F.T.C. 1174 (1979).

89. Broadcast Music, Inc. v. Columbia Broad. System, Inc., 441 U.S. 1 (1979).

90. *Id.* at 4.

> this is not a question simply of determining whether two or more potential competitors have literally "fixed" a "price." As generally used in the antitrust field, "price fixing" is a shorthand way of describing certain categories of business behavior to which the per se rule has been held applicable. The Court of Appeals' literal approach does not alone establish that this particular practice is one of those types or that it is "plainly anticompetitive" and very likely without "redeeming virtue. . . ." Thus, it is necessary to characterize the challenged conduct as falling within or without that category of behavior to which we apply the label "per se price fixing."[91]

In an effort to delineate which factors distinguish per se from rule of reason treatment, the Court went on to set out the analytic framework for consideration. The "inquiry must focus on whether . . . *the practice facially appears to be one that would always or almost always tend to restrict competition and decrease output . . . or instead one designed to 'increase economic efficiency and render markets more, rather than less, competitive.'*"[92]

Because the blanket license was not a "'naked restraint of trade with no purpose except stifling of competition,' but rather accompanie[d] the integration of sales, monitoring, and enforcement against unauthorized copyright use," it was not illegal per se.[93] The Court focused on the new product aspect of the integrative efficiencies issue, holding that the blanket license was not a naked restraint of trade, "but rather accompanie[d] the integration of sales, monitoring, and enforcement against unauthorized copyright use."[94] The blanket license was a practical necessity because of the transactions costs involved. It was prohibitively expensive for thousands of composers to negotiate individually over the use of each song, for each user to report the amount of use and for each composer to police the use of his works by authorized and unauthorized users. Hence, the blanket license "created a forum for buyers and sellers . . . and yielded improvements in the market for performing rights of copyrighted compositions which were unrelated to price."[95] Without the blanket license, individual sales would be "quite expensive" and "costs [would be] prohibitive,"[96] thus the license becomes "to some extent, a different product."[97] As to the collective price setting:

> the blanket license cannot be wholly equated with a simple horizontal arrangement among competitors. ASCAP does set the price for its blanket license, *but that license is quite different from anything any individual owner*

91. *Id.* at 8-9.

92. *Id.* at 19-20 (emphasis added) (quoting United States v. U.S. Gypsum Co., 438 U.S. 422, 441 n.16 (1978)).

93. *Id.* at 20, (quoting Witte Motor Co. v. United States, 372 U.S. 253, 263 (1963))

94. *BMI*, 441 U.S. at 20.

95. *Id.* at 22.

96. *Id.* at 20.

97. *Id.* at 22.

could issue.[98]

The underlying teaching of *BMI* appears to be that courts should look to whether the restraint at issue potentially could create an efficiency enhancing integration to which the restraint is ancillary. "In other words, the issue is whether the price fixing 'achieve[s] purposes unrelated to price formation.'"[99]

The Court also used the new product test in *National Collegiate Athletic Association v. Board of Regents.*[100] In that case, a number of academic institutions formed a joint venture for the purpose of regulating athletic contests between the members.[101] The venture limited competition among its members in a number of areas. Besides setting the rules of competition, including "the size of the field, the number of players on a team, and the extent to which physical violence is to be encouraged or proscribed," the NCAA imposed competitive limitations on its football-playing members designed to produce and market a "particular brand of football—college football."[102] To this end, the NCAA proscribed other competitive actions of its members, including setting the price of a principal input (football players) at tuition plus room and board.

The Court rejected application of the per se rule because "it would be inappropriate to apply a per se rule . . . [where] horizontal restraints on competition are essential if the product is to be available at all."[103] The joint venture actions, therefore, "widen[ed] consumer choice—not only the choices available to sports fans but also those available to athletes—and hence can be viewed as procompetitive."[104] The fact that restraints on competition between NCAA members were necessary to produce the product was sufficient to remove the analysis of venture and its restraints from the per se category.[105]

In a decision prior to *NCAA*, the Court considered and rejected the new product approach in condemning a "sham" joint venture in *Arizona v. Maricopa County Medical Society.*[106] The case involved two medical societies which operated foundations for medical care. The Maricopa Foundation for Medical Care ("Maricopa Foundation") represented approximately seventy

98. *Id.* at 23 (emphasis added).

99. National Bancard Corporation (NaBanco) v. Visa U.S.A., Inc. 779 F.2d 582, 599(11th Cir., 1986) (citing United States v. Southern Motor Carriers Rate Conference, 672 F.2d 469, 479 (5th Cir. Unit B 1982), *aff'd*, 702 F.2d 532 (5th Cir. 1983) (*en banc*), *rev'd on other grounds*, 105 S. Ct. 1721 (1985)).

100. National Collegiate Athletic Association v. Board of Regents, 468 U.S. 85 (1984).

101. *Id.* at 99.

102. *Id.* at 101.

103. *Id.* at 100-01.

104. *Id.* at 102.

105. *NCAA*, 468 U.S. at 100-01.

106. Arizona v. Maricopa County Medical Society, 457 U.S. 332 (1982).

percent of the physicians in the Phoenix, Arizona area.[107] The Pima Foundation for Medical Care ("Pima Foundation") represented somewhere between thirty and eighty percent of the physicians in its area.[108] The Foundations were formed for the express purpose of "promoting fee for service medicine" and as an alternative to existing health insurance plans.[109] The foundations had three primary activities: (1) establishing a schedule of maximum fees for patients insured under plans approved by the foundations; (2) conducting utilization review; and (3) performing claims administration.[110]

The joint venture set the maximum fees that member physicians could charge for services under insurance plans that were approved by the venture.[111] The Court, by a four to three vote, characterized the setting of the maximum fee schedule as per se illegal price fixing, and rejected the procompetitive justifications offered by the defendants.[112] It observed that the "anticompetitive potential inherent in all price-fixing agreements justifies their facial invalidation even if procompetitive justifications are offered for some."[113]

The Court suggested that consideration of efficiencies was not relevant because the per se rule does not countenance their consideration.[114] Nevertheless, in dicta, the Court disposed of the defendants' efficiency claims. In terms of a new product justification, the defendants claimed that "their fee schedules are procompetitive because they make it possible to provide consumers of health care with a uniquely desirable form of insurance coverage that could not otherwise exist."[115] The unique features claimed by the venture were choice of doctors, complete insurance coverage, and lower premiums. But the first two of these attributes were available in numerous insurance plans. Further, although the Court noted that complete coverage required an agreement on prices to be charged between insurance companies and physicians, the insurance companies could have set these prices with participating physicians. Thus, the Court held that "nothing in the record even arguably supports the conclusion that this type of insurance program could not function if the fee schedules were set in a different way."[116]

The Court distinguished *BMI*, noting that in this case: (1) the members of the venture competed with each other; (2) the venture did not enable them to

107. *Id.* at 339.
108. *Id.* at 340 n.8.
109. *Id.* at 339.
110. *Id.* at 339-40.
111. *Maricopa*, 457 U.S. at 335-36.
112. *Id.* at 348.
113. *Id.* at 351.
114. *Id.* at 345. That observation was clearly inconsistent with *BMI* where evaluation of efficiencies took the case out of the per se rule.
115. *Id.* at 351.
116. *Maricopa*, 457 U.S. at 358.

offer any different product; and (3) the venture merely permitted the members to engage in price formation.[117]

2. New Product Analysis of PBM Joint Ventures

The lower courts and the antitrust agencies appear to have divergent attitudes toward the new product defense. On the one hand, many lower courts have resolved the question of legitimacy through a "new product" inquiry as in *BMI*.[118] On the other hand, the enforcement agencies have never used the "new product" label in any business review letters under the earlier or revised set of Policy Statements.[119] There is only a brief reference in a footnote to the new product defense in the 1996 Policy Statements.[120] Perhaps part of the reason the new product concept is underutilized by the agencies is that it is fairly elastic, and there is relatively little guidance in its application.

In any case, in order to meet this defense, a joint venture must demonstrate that it offers a product that its members could not offer individually. The reason why the courts focus on the capabilities of the members is, in part, to determine if there is an incentive for the members to enter into a cartel. If the members are capable of offering the joint venture's product individually, then cartel-formation concerns exist, because there may be an incentive to enter the market together in order to foreclose competition. If, however, the members are incapable of producing the joint venture's product, these cartel-formation concerns are not present.

The strongest new product argument could be presented where a joint venture consists of numerous independent pharmacies, none of which could independently create a PBM network. Thus, their joining into a joint venture would not eliminate any potential or existing competition. The purpose of this type of venture could be to enable some of the small pharmacies to acquire the economies of scale and scope of large chain pharmacies. This in turn enables small pharmacies to compete more effectively with pharmacy chains in both the pharmacy and PBM markets. Some commentators, such as Professor Pitofsky, suggest that a joint venture should be per se legal where it permits participants to enter a market they could not have individually entered.[121]

117. *Id.* at 356. For a criticism of the Court's decision see *infra* notes 158-64 and accompanying text.

118. *See, e.g.*, Northrop Corp. v. McDonnell Douglas Corp., 705 F.2d 1030, 1052-53 (9th Cir. 1983) (new Navy aircraft); Worthen Bank & Trust Co. v. National BankAmericard, Inc., 485 F.2d 119 (national credit card system); National Bancard Corp. ("NaBanco") v. VISA U.S.A., 596 F. Supp. 1231 (S.D. Fla. 1984) (transaction interchange system for member banks), *aff'd*, 779 F.2d 592 (11th Cir. 1986).

119. Roscoe Starek, III, Commissioner of FTC, Remarks Before the Antitrust Common Ground Conference (May 17, 1996).

120. 1996 POLICY STATEMENTS, *supra* note 4, ¶ 20,817 n.36.

121. Robert Pitofsky, *Joint Ventures Under the Antitrust Laws: Some Reflections on the Sig-*

Even assuming some members could independently enter, there would seem to be strong arguments that a joint venture PBM offers a new product. A PBM joint venture may create a network which includes a computer system, point-of-sale claims processing and information gathering, a formulary, a group buying arrangement and a joint sales agent. The joint venture helps assist the functioning of the market by providing a claims transaction system and facilitating negotiations between a large number of market participants. It provides benefits for pharmacy members, plan sponsors and consumers, by providing an efficient means of claim processing and utilization review.[122] In addition, by amassing purchasing power, it can aggressively negotiate for discounts from pharmaceutical manufacturers on behalf of its members.[123]

One might argue that a joint venture among two or three large pharmacy chains that currently have their own PBM networks should be condemned as a sham. Although the fact that this type of venture might pose a threat of exercising market power because of its size, per se condemnation would be premature. Market power is appropriately analyzed under the rule of reason.[124] If the venture possesses market power it would appropriately be analyzed under the rule of reason.

Even where none of the pharmacies could independently enter the PBM market, one could argue that a new product argument is unavailing because this type of joint venture will not offer anything to the market that is not already offered by independent PBMs such as PCS and MEDCO.[125] That argument would go too far. If the courts required a showing of "uniqueness," none of the network ventures described earlier would have survived antitrust scrutiny. For example, the WORLDSPAN joint venture offers no unique efficiencies vis-a-vis the other CRS networks.[126] Similarly, if uniqueness is the standard, once one joint venture is in the market, no other joint venture may be able to enter, because the new product will no longer be unique.

The one case that specifically dealt with the issue of whether a new product had to be "unique," *National Bancard Corporation (NaBanco) v. Visa*

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nificance of Penn-Olin, 82 HARV. L. REV. 1007, 1053 (1969). Thomas A. Piraino, Jr., *A Proposed Antitrust Analysis of Telecommunications Joint Ventures*, 1997 WIS. L. REV. 639, 665 (1997) (where the "joint venture partners are not currently competing in the joint venture market or, absent the joint venture, could not have competed in the market, the joint venture will not eliminate any competition that otherwise would have occurred" and should be treated as per se legal).

122. *See supra* Section II.A.

123. *Id.*

124. FTC Enforcement Policy on Physician Agreements to Control Medicare Prepayment Plans, 46 Fed. Reg. 48,982 (1981).

125. Such an argument might receive support from the language in *Maricopa* that the foundations were not offering a new product, because there were already insurance companies offering similar fee schedules. *See supra* note 116 and accompanying text.

126. *See supra* note 70 and accompanying text.

U.S.A., Incorporated,[127] rejected that limited interpretation the defense. The case involved NaBanco's challenge to VISA's issuer reimbursement fee, which facilitated credit card transactions between card-issuing and merchant banks. NaBanco argued that the case should be analyzed under the per se rule because the "new product" defense of *BMI* was limited to those circumstances where the joint venture created a unique product. Since there were independent credit card networks, such as American Express and Diners Club, and individual banks issued their own credit cards, VISA's new product argument would have been doomed to failure if "uniqueness" was necessary to meet the new product standard.[128]

The court rejected NaBanco's interpretation of *BMI*:

> *Broadcast Music* and *Maricopa* do not require the court, as NaBanco contends, to make a subjective judgment as to whether a joint venture's product is "unique." Rather, they call for the court to compare the product of the venture to the individual offerings of the venture's members and determine whether the venture offers procompetitive abilities which its members acting alone could not offer.... Thus the agreement to market compositions in *Broadcast Music* survived the per se test even though the individual composers could market their compositions on their own.... The consolidation of thousands of what would otherwise be balkanized local cards into one internationally accepted card makes the VISA system a viable and competitive whole which is "truly greater than the sum of its parts."[129]

Thus, the court concluded that the rule of reason was appropriate because VISA's members, acting alone, could not offer a product comparable to the national credit card access offered by VISA.[130]

Thus, the focus of the new product inquiry is on the *capabilities of the venture members*, not on whether there are other similar arrangements in the market. A uniqueness standard would be an excessive threshold, forbidding most joint conduct unless it was in the unusual position of creating a market. This standard would in turn, limit the ability of joint ventures to enter markets where competitors currently exist.

Where a PBM joint venture creates a new entrant in the market and its members are not capable of independently competing in the PBM market, it would have a compelling argument that it meets the new product test. In the words of *BMI*, the creation of the joint venture "'increases economic efficiency and renders markets more, rather than less, competitive.'"[131]

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127. 596 F. Supp. 1231, 1254 (S.D. Fla. 1984).

128. *Id.* at 1250.

129. *Id.* at 1254 (citing Broadcast Music, Inc. v. CBS, 441 U.S. 1).

130. *Id.* at 1254.

131. *Broadcast Music*, 441 U.S. at 19 (quoting United States v. United States Gypsum Co., 438 U.S. 422, 441 n.16 (1978)).

3. Integration

A second and related approach to determining the legitimacy of a venture is to look whether there are integrative efficiencies. Unfortunately, integration, like new product, seems like a vague and elastic term.[132] Both the courts and the antitrust agencies have struggled with the concept.[133] The agencies particular application of the integration standards in the 1994 Policy Statements was the source of much criticism in the debate on the Policy Statements. Unlike the new product concept, there is extensive discussion of integration both in the Policy Statements and business review letters.

Neither the courts nor commentators have established clear standards for the degree of integration necessary to avoid per se treatment. As one prominent commentator has observed: "[o]ne looks in vain for a test of integration in the decided cases."[134] Most courts have ignored the issue of integration. The few that address the subject have applied a relatively simple standard in finding sufficient integration, looking more to the new product concept—the venture was legitimate simply because some form of productive capacity was created.[135]

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132. As FTC Commissioner Azcuenaga has observed:

> [The emphasis on integration] may be misdirected. What is appropriate and necessary for one venture may not be appropriate and necessary in another context. Instead of emphasizing the form of the business association, it may be more useful to ask the fundamental questions whether a venture achieves efficiencies and whether any restraints are reasonably necessary to accomplish that result. Despite the frequent repetition of the term "integration" in connection with legitimate joint ventures, remarkably little attention has been devoted to giving content to the term.

Mary Azcuenaga, Remarks Before the ABA Antitrust Section, (Aug. 7, 1995) (transcript available on WestLaw).

133. *Id.*

134. M. Laurence Popofsky, *Integration, Market Power, and Necessity: Guideposts for the Practitioner*, 54 ANTITRUST L.J. 1141, 1142 (1985). *See also* Thomas L. Greaney & Jody L. Sindelar, *Physician Sponsored Joint Venture Antitrust Analysis of Joint Ventures: An Antitrust Analysis of Preferred Provider Organization*, 18 RUTGERS L.J. 513, 573 (1987). "Unfortunately, the case law is quite deficient in describing the nature of integration required or the magnitude of the integration benefits needed for lawful joint ventures." *Id.*

135. *See, e.g.*, Hassan v. Independent Practice Assocs., 698 F. Supp. 679 (E.D. Mich. 1988). Professor Brodley has presented a useful test for the integration inquiry. Under a "presumptive, incentive-modifying" approach, to avoid the per se rule the activity must, as a threshold matter, be a true joint venture, defined as "an integration of operations likely to lead to the expansion of output." Joseph F. Brodley, *Joint Ventures and Antitrust Policy*, 95 HARV. L. REV. 1521, 1525 (1982). Richard D. Raskin, *Antitrust Issues for Independent Health Care Providers: "Integration" and the Per Se Rule, in* ANTITRUST AND EVOLVING HEALTH CARE MARKETS: A SYMPOSIUM FOR HEALTH CARE INDUSTRY PARTICIPANTS, COUNSEL, AND POLICY MAKERS 73, 74 (1995) (integration is a benchmark "designed to help differentiate between mere agreements among competitors and cooperative business arrangements that amount to, or at least approximate, the operation of a single entity."); Thomas A. Piraino, Jr., *Beyond Per Se, Rule of Reason or Merger Analysis: A New Antitrust Standard for Joint Ventures*, 76 MINN. L. REV. 1, 7 (1991)

In the health care area, there is a wide variety of integrative factors one could look to including financial investment, purchase of facilities, contractual arrangements with plan sponsors, practice profiling, utilization review, credentialing and others. In fact, in an early, pre-*Maricopa*, statement, the FTC listed a broad range of functional and financial characteristics that would be indicia of sufficient integration.[136] However, in the 1993 and 1994 Policy Statements, enforcement actions, and several staff advisory letters, the agencies focused almost exclusively on financial risk-sharing, and, in particular, on capitation and withholds as the primary indicia of integration.[137]

a. *Maricopa* and Integration.

The focus on financial risk-sharing is based on Justice Steven's opinion in *Maricopa*.[138] In dicta the Court responded to the argument that the foundations brought efficiencies to the market. But the Court rejected the argument, because of the structure of the foundations:

> The foundations [in this case] are not analogous to partnerships or other joint arrangements in which persons who would otherwise be competitors pool their capital and share the risks of loss as well as the opportunities for profit. . . . If a clinic [had] offered complete medical coverage for a flat fee, the cooperating doctors would have the type of partnership arrangement in which a price-fixing agreement among the doctors would be perfectly proper. But the fee arrangements disclosed by the record in this case are among independent competing entrepreneurs. The members of the venture do not risk their capital in search of profit opportunities. They merely agree to fix the prices at which they sell medical services to insurance companies.[139]

Notably, the Court in *Maricopa* focused solely on indicia of financial integration and did not find significance in the performance of utilization review, joint claims administration, or other operational aspects of the foundation ventures.[140]

Should *Maricopa* be the rosetta stone of health care antitrust policy? Does

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(the "integration of resources: that follows when collaborating firms "contribute assets such as capital, technology, or production facilities to a common endeavor."); William J. Kolasky, Jr., Prepared Testimony Before the FTC Hearings on Joint Ventures, 85 (July 1, 1997) (urging a broad view of integrative efficiencies looking to whether firms are "bringing together complementary, productive resources and using them in a way jointly that will allow them to do something that neither firm could do individually or do it more efficiently") (transcript available at <http://www.ftc.gov/opp/jointvent/kolasky.htm>).

136. FTC Enforcement Policy on Physician Agreements to Control Medical Prepayment Plans, 46 Fed. Reg. 48,982 (1981).

137. Robert F. Leibenluft, Remarks Before the American Hospital Association, (Oct. 10, 1996) (transcript available in 1996 WL 595823 (F.T.C.)).

138. 457 U.S. 332 (1982).

139. *Id.* at 356-57.

140. *Id.* at 332.

Maricopa provide support for such a wide-ranging public policy decision to focus critically on financial risk-sharing, or to invariably apply the per se rule where that risk-sharing is absent? As a matter of jurisprudence, many courts and commentators have observed how difficult it is to reconcile the Court's decisions in *BMI* and *Maricopa*.[141]

As Justice Powell noted in his dissent in *Maricopa*, there was very little difference between the arrangements in *BMI* and *Maricopa* in that each: (1) involved competitors and resulted in cooperative pricing activities among those competitors; (2) was prompted by the need to provide better service to consumers; and (3) apparently made possible a new product by reaping otherwise unattainable efficiencies.[142] The dissent observed that the Foundation's agreement foreclosed no competition, since the participating physicians could associate with other insurance plans or treat patients from these plans. The Foundation simply created a novel way to provide health care services and the "freedom to compete, as well as the freedom to withdraw, [was] preserved."[143] The dissent concluded that the foundations had "set up an innovative means to deliver a basic service—insured medical care from a wide range of physicians of one's choice—in a more economical manner."[144]

The history of the case does not support a per se approach. The fee schedules established by the foundation were maximum prices, not minimum.[145] The district court concluded that the price setting should be analyzed under the

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141. *See* National Bancard Corp. (NaBANCO) v. Visa, U.S.A., Inc., 779 F.2d 592, 601 (11th Cir. 1986), *cert. denied*, 479 U.S. 923 (1986). "The Court apparently abandoned its BMI standards and followed a formalistic approach which indicated that all price fixing was per se violative even if it created efficiencies." *Id.* One commentator maintained that the Court's position in *Maricopa* "made it impossible for the majority to articulate a principled explanation of the Court's unanimous decision in *Broadcast Music* . . . ." WESLEY J. LIEBELER, ANTITRUST ADVISOR: 1983 CUMULATIVE SUPPLEMENT § 1.29 (2d ed. 1984). *See also* Greaney & Sindelar, *supra* note 134; Frank H. Easterbrook, *Maximum Price Fixing*, 48 U. CHI. L. REV. 886 (1981); Peter M. Gerhart, *The Supreme Court and Antitrust Analysis: The (Near) Triumph of The Chicago School*, 1982 SUP. CT. REV. 319 (1982).

142. *Maricopa*, 457 U.S. at 364-65 ("the foundations provide a 'different product' to precisely the same extent as did *Broadcast Music*'s clearinghouses. The individual sellers—the rights to use individual compositions.") Just over a year after *Maricopa* was decided, the Fifth Circuit noted that the case already had criticism. *See* St. Bernard General Hosp. v. Hospital Service Ass'n of New Orleans, 712 F.2d 978, 986 (5th Cir. 1983), *cert. denied*, 466 U.S. 970 (1984). "It is clear that the refusal of the Supreme Court [in *Maricopa*] to look beyond the surface effect of the pricing arrangements and examine instead the underlying competitive effects prohibits potentially beneficial as well as blatantly monopolistic restraints on pricing." *Id.*

143. *Maricopa*, 457 U.S. at 360.

144. *Id.* at 365 n.12. *See also* Easterbrook *supra* note 141, at 898-99 (observing that a maximum fee schedule may reduce insurers' transaction and search costs and create a "new product" as in *BMI*).

145. *Maricopa*, 457 U.S. at 335.

rule of reason.[146] The Ninth Circuit, at that time including Justice Kennedy, upheld the price setting because the foundations were non-exclusive and there was no evidence that they kept other managed care arrangements out of the market.[147]

Is *Maricopa* truly a per se case? Professor Havighurst observes that *Maricopa* is a rather peculiar application of the per se rule.[148] Whereas application of the rule typically eschews analysis of market power and efficiencies, in *Maricopa* the Court relied on both factors to find a per se violation. In particular, the majority relied on the large market share of the foundation and the lack of any credible efficiencies in finding a violation. "Such a consulting of the record to see whether a presumption of illegality might be successfully rebutted demonstrates that the presumption was not conclusive; as a per se rule would be."[149] Havighurst ultimately concludes that invariably following the dicta to require financial risk sharing in *Maricopa* would not be sound public policy:

> [T]he agencies' job is not to prosecute every case they might win on the basis of questionable dicta or precedent. Instead, it is to employ their expertise and fact-finding capability to prevent true restraints harmful to competition and consumer welfare while encouraging arrangements that create efficiencies.[150]

Havighurst recommended that the agencies move away from relying on *Maricopa* and generally apply the rule of reason to health care joint ventures.[151]

Professor Herbert Hovenkamp takes a contrary view of *Maricopa*, but still finds that the Court's analysis falls far short of the mark.[152] First, he observes that application of the per se rule was inappropriate because if the maximum price schedules were really disguised minimum prices, why did the insurance companies agree to participate?[153] Second, he observed that it would have been worthwhile for the Court to compare the prices charged by the doctors in foundations, to those outside the foundations.[154] If nonparticipating doctors charged more, then the arrangement was probably efficient. Finally, the fact that the foundations were non-exclusive was "absolutely inconsistent with the economics of cartelization: no cartel could restrict its output and raise price if it

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146. Arizona v. Maricopa County Med. Soc'y, 1979-1 Trade Cases (CCH) ¶ 62,694 (D. Ariz. 1979).

147. Arizona v. Maricopa County Med. Soc'y, 643 F.2d 553 (9th Cir. 1980).

148. Havighurst, *supra* note 8, at 82-83.

149. *Id.* at 83.

150. *Id.* at 84.

151. *Id.* at 88.

152. HERBERT HOVENKAMP, FEDERAL ANTITRUST POLICY: THE LAW OF COMPETITION AND ITS PRACTICE § 5.6 (1994).

153. *Id.*

154. *Id.*

permitted its members freely to come and go, or to make unlimited 'non-cartel' sales, especially if the cartel's members numbered in the thousands."[155] Hovenkamp concludes that the venture should have been upheld under the rule of reason because it reduced transactions costs and was non-exclusive.[156]

Professor Edward Correia makes a similar criticism of *Maricopa*. He observes that as a general matter, using integration as the sine qua non of a legitimate joint venture runs the risk of condemning new capacity or new products.

> The Supreme Court made this mistake in *Maricopa*. By focusing too much on the precise degree of integration, the Court failed to give adequate weight to the fact that the medical association had introduced a new insurance plan to the Phoenix area. When collaborators are bringing a new product or new capacity to the market, the rule of reason should be applied, without regard to some particular integration threshold.[157]

Correia suggests that a physician network should qualify for the rule of reason treatment if it is non-exclusive and can be characterized as offering a new form of health insurance plan to the market.[158]

A recent speech by FTC Commissioner Starek questions whether *Maricopa* continues to provide a vital basis for the use of the per se rule in health care antitrust enforcement.[159] He noted that the agreement appeared to be a

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155. *Id.*

156. *Id.*

157. Edward Correia, Prepared Testimony Before the FTC Joint Venture Project 29 (December 4, 1997) (transcript available at <http://www.ftc.gov/opp/jointvent/correia.htm>).

158. *Id.* Professor Stephen Ross observes that application of the per se rule in *Maricopa* seems inconsistent with the Court's jurisprudence. The maximum fee schedules did not facially appear to be invariably anticompetitive, and at most posed a risk of being anticompetitive. STEPHEN F. ROSS, PRINCIPLES OF ANTITRUST LAW 140 (1993).

159. Roscoe B. Starek, III, *Reinventing Health Care Antitrust Enforcement*, Speech before the Antitrust Common Ground Conference, 1996 WL 313476 (F.T.C.). Neither the Supreme Court nor the lower courts have relied much on *Maricopa*. In the four horizontal restraint cases decided by the Supreme Court since *Maricopa* and *NCAA* (Northwest Wholesale Stationers, Inc. v. Pacific Stationery and Printing, 472 U.S. 284 (1985); Federal Trade Comm'n v. Indiana Fed'n of Dentists, 476 U.S. 447 (1986); Federal Trade Comm'n v. Superior Court Trial Lawyers Ass'n (SCTLA), 493 U.S. 411 (1990); Jay Palmer v. BRG of Ga., 498 U.S. 46 (1990)) only two, *Northwest* and *SCTLA*, even cite *Maricopa*, and then only for the proposition that per se rules provide administrative simplification. When the court deals with the issues of modes of analysis, the scope of the per se rule, or other horizontal restraint questions, it consistently relies on *NCAA*, rather than *Maricopa*.

Lower Courts have been similarly silent on *Maricopa*. Even in the few cases that have declared horizontal restraints per se illegal (General Leaseways, Inc., v. National Truck Leasing Ass'n, 744 F.2d 588 (7th Cir. 1984); COMPACT v. Metropolitan Gov't of Nashville & Davidson County, 594 F. Supp. 1567 (M.D. Tenn. 1984); Regents of Univ. of California v. American Broad. Co., Inc. 747 F.2d 511 (9th Cir. 1984)) have not even cited the case. Like the Supreme Court, the Courts follow *NCAA* even though *Maricopa* would have provided a road map for rather naked price fixing arrangement, and it was clear the foundation, with seventy percent of the physicians in the market had market power.[160] He observed that most importantly the decision:

> provides little guidance for harder — and perhaps more typical—cases in which the evidence of agreement is uncertain, smaller percentages of the physicians in a relevant market are involved, and the doctors can plausibly claim some type of financial risk-sharing.... [The] 1982 decision predates much of the near-transformation of health care financing that has stemmed from the explosion of managed care.[161]

He also observed that it is far from certain that the current Supreme Court would apply the same analysis and reach the same result if presented with a more challenging and equivocal physician network case.[162] *Maricopa* was decided by a four to three vote, and three of the four Justices who voted in the majority are no longer on the Court.[163] Finally, he observed that although *Maricopa's* per se analysis receives some attention in the antitrust agencies' Health Care Policy Statements and the academic literature, no other court has relied upon it in declaring a health care joint venture illegal.[164]

Perhaps one way to look at *Maricopa* is to view it as a narrow exception that permits per se condemnation for sham joint ventures. *Maricopa* is the progeny of earlier Supreme Court joint venture cases in which the Court condemned certain joint venture restraints as per se illegal.[165] All of these cases displayed three unifying characteristics: (1) the practices examined were related to the market in such a way that if they were to have any effect at all it would be on price formation; (2) the practices lacked any degree of integration of functions among the competitors; and (3) the arrangements were not ones which helped to make or improve a market by facilitating trading, reducing transactions costs, exchanging information, standardizing products or the

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condemnation. The only case in which a horizontal restraint has been struck down that cited it was Premier Electrical Constr. Co., v. National Electrical Contractors Ass'n, Inc., 814 F.2d 358 (7th Cir. 1987). In that case an association placed a "union bargaining fee" of one percent of all industry sales, regardless of whether the seller was a member of the association. It is only cited once for the proposition that unintegrated sellers can not price fix. *Id.* at 370. There was no integration whatsoever. It was naked price fixing agreement. *Id.*

Thus the courts appear reluctant to rely on, or even apply *Maricopa*, except in the most egregious situations.

160. Starek, *supra* note 159, at 3.

161. *Id.*

162. *Id.*

163. *Id.*

164. *Id.* at 5 n.14.

165. *See, e.g.*, Timken Roller Bearing Co. v. United States, 341 U.S. 513 (1951) (stating that labeling a horizontal arrangement as a joint venture will not immunize the arrangement from per se treatment). *See also* 1 ANTITRUST LAW DEVELOPMENTS (FOURTH), *supra* note 72, at 395-96.

like.[166] Each of these characteristics were indicative that the venture was a sham. Since price formation was affected, if there was any consequence at all, it was entirely fair and functionally accurate for courts and enforcement agencies to treat arrangements like these as naked restraints.

Although the application of *Maricopa* may have missed the mark, more generally useful integration may be indicia of the legitimacy of joint venture. Where joint venture partners make significant investments and create new productive output, there is a strong likelihood it is not a smokescreen for a cartel. Where *Maricopa* may have been misinterpreted is on a simplistic search for certain forms of integration, e.g., financial risk sharing. As explained in the next section, by broadening the definition of integration beyond risk sharing, the antitrust agencies may have brought *Maricopa* types of analyses within mainstream antitrust jurisprudence.

b. Health Care Policy Statements and Integration

In order to provide guidance to the health care marketplace the Antitrust Division of the Justice Department and the FTC have issued three sets of Health Care Policy Statements—in 1993, 1994 and 1996.[167] Based on the dicta in *Maricopa*, the first two iterations of the Policy Statements focused almost exclusively on certain forms of financial risk sharing as the path to integration. They explained that sufficient integration was present:

> (a) when the venture agrees to provide services to a health benefits plan at a "capitated" (or per subscriber) rate; or
>
> (b) when the venture creates significant financial incentives for its members as a group to achieve specified cost-containment goals, such as withholding from all members a substantial amount of the compensation due to them, with distribution of that amount to the members only if the cost-containment goals are met.[168]

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166. Professor Pitofsky makes a similar observation about *Maricopa* and *Socony-Vacuum*: "In each of these cases, there was little or no integration, no real improvement in the functioning of the market, nor any increase in firm or group efficiency. As a result, anticompetitive effects should have been and were enough to lead to a finding of illegality." Robert Pitofsky, *A Framework for Antitrust Analysis of Joint Ventures*, 54 ANTITRUST L.J. 893, 908 (1985).

167. Department of Justice and Federal Trade Commission, Statements of Enforcement Policy and Analytical Principles Relating to Health Care and Antitrust (1993, 1994, and 1996), *reprinted in* 4 Trade Reg. Rep. (CCH) §§ 20,500-835, ¶¶ 13,150-53.

168. *Id.* at ¶ 13,152 (1994 Policy Statement No. 8). A capitated payment is based on a fixed periodic rate for a defined patient population and does not vary with the amount of services provided. Carl H. Hitchner et al., *Integrated Delivery Systems: A Survey of Organizational Models*, 29 WAKE FOREST L. REV. 273, 278 n.18 (1994). Consequently, physicians assume the risk for utilization of services above the capitated rate. Capitation may raise certain types of legal and regulatory problems. *See* Andrew Ruskin, *Capitation: The Legal Implications of Using Capitation to Affect Physician Decision-Making Processes*, 13 J. CONTEMP. HEALTH CARE POL'Y

As one enforcement official observed "[t]he key to integration is that providers have assumed the substantial risk of the venture's economic success or failure, so that they will no longer act solely as independent economic actors and will have the incentive to attain any efficiencies that may flow from integration."[169]

The existence of financial risk sharing, in terms of withholds and capitation, was frequently the crucial element in advisory opinions and business review letters issued by the agencies. In fact, it often was the sole issue discussed.[170] Both the 1994 Policy Statements and several business review letters were very specific about the appropriate level of financial withhold necessary to show sufficient integration.[171] In these letters the agencies specified certain acceptable levels of integration in terms of financial withholds for meeting cost containment goals. Regardless of whether such an approach was sound policy, it gave the impression that the agencies were engaging in unwarranted regulation of these ventures.[172]

In 1994, for example, the Montana Medical Association presented a proposal to the FTC staff for review.[173] The proposed PPO was non-exclusive and there was no suggestion that it could exercise market power.[174] It would have performed utilization and quality-assurance reviews. It sought to meet the risk-sharing criterion by withholding fifteen percent of physicians' fees as a form of budgetary discipline.[175] Only if the cost containment goals were met would physicians receive the withhold.[176] Participating doctors would have been required to accept no more than eighty-eight percent of customary charges.[177] But the FTC staff concluded that the PPO was engaging in per se illegal price fixing, even though different doctors would have charged different fees.[178] Joint price setting was not justified because the withhold level was too small to change the physician's incentives: "a 15% withhold from charges

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391 (1997).

169. Prepared Remarks of Mark D. Whitener before the Charles River Associates, Apr. 28, 1994.

170. *See Capitation is Seen as Brightest Line in Quest for Sufficient Integration*, 68 Antitrust & Trade Reg. Rep. (BNA) 1702, at 295 (Mar. 2, 1995).

171. *Id.*

172. *Id.*

173. Advisory Opinion Letter from Mark J. Horoschak, Assistant Director for the Bureau of Competition, *Federal Trade Commission*, to Paul W. McVay, President, *ACMG, Inc.* (July 5, 1994)(on file with the Federal Trade Commission). *See also* Advisory Opinion Letter from Mark J. Horoschak, Assistant Director for Bureau of Competition, *Federal Trade Commission*, to George Q. Evans, Esquire, *Wise Carter Child & Caraway* (July 5, 1994) (on file with the Federal Trade Commission).

174. *Id.*

175. *Id.*

176. *Id.*

177. *Id.*

178. Letter from Horoschak, *supra* note 173.

may not be enough to affect each physician's normal incentive to maximize his or her income by increasing the number of services provided to enrolled patients."[179]

One could question the focus on financial risk-sharing from several perspectives. Although commitment to reducing or controlling health care costs is a laudable health care goal, is it a goal of the antitrust laws? There are few, if any examples, where the antitrust laws seem to be applied to meet some other public policy objective. Moreover, by making the level of withholds the critical element, the agencies may appear to be regulating the price and profitability of these ventures. In addition, by focusing so strongly on cost containment, the agencies appeared to treat to a disadvantage certain alternatives such as a high quality, high cost provider sponsored venture. Certain specialty networks may decide for many reasons not to engage in substantial risk sharing as defined by the guidelines. Consumers may prefer fee-for-service medicine to capitation, and physicians may not know the risks of capitation or may be unwilling to assume either the financial risk of loss or the legal risk for inappropriate underutilization.[180]

As Professor Havighurst notes, by establishing such a high threshold to avoid per se condemnation, the agencies in effect appeared to be regulating physician networks by evaluating the merits of the products they offered and allowing only those networks perceived to be of sufficient value to be legal.[181] In doing so, some perceive the agencies as acting in place of the market by determining which products have merit.[182] Such actions are inconsistent with the goals of antitrust, which seeks to create the widest variety of alternatives for consumers. It does not seek to prejudge market outcomes or favor one form of organization over another.[183]

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179. *Id.*

180. *See* Dennis Yao, *Antitrust and Managed Competition for Health Care*, ANTITRUST BULL., Summer, 1994, at 6-10 (discussing consumer preferences); Bronow, *HMO Physicians' Shared Risk Pools Are Dangerous to Patients' Health*, 10 HEALTHSPAN 9 (Jan. 1993) (arguing that capitated risk pools may lead to malpractice claims for underutilization and patient exploitation).

181. Havighust, *supra* note 8, at 81.

182. *Id.* at 82.

183. This criticism appears to have resonated with the enforcement agencies. In releasing the 1996 Policy Statements, FTC Chairman Robert Pitofsky said:

> It is not the goal of the agencies to enforce the antitrust laws in a way that determines the kind of physician networks that will develop in the marketplace. We leave it to the market to develop particular frameworks that best meet consumer needs. On the other hand, the antitrust law enforcement agencies will continue to police the marketplace to protect consumers against price fixing among competing health care providers that has no redeeming competitive effects . . . .

Federal Trade Commission, Justice Department Revise Policy Statements on Health Care Anti-

In response to these concerns, the standards for integration were revised and broadened in the 1996 Policy Statements. The Statements now recognize other forms of integration, and not just financial risk sharing such as capitation and withholds. Clinical integration can be demonstrated by "significant utilization management and quality assurance programs."[184] The Statements stress that these "are not, however, the only types of arrangements that can evidence sufficient [clinical] integration to warrant rule of reason analysis," and that "substance, rather than form, [will be determinative] in assessing a network's likelihood of producing significant efficiencies."[185] In addition the 1996 Statements recognize cost containment incentives other than withholds (such as financial rewards).[186]

c. Application of Risk Sharing Standards to PBM Joint Ventures

A PBM joint venture could attempt to meet the specific standards of the Health Care Policy Statements. Many ventures involve a substantial financial investment. Another approach could be to enter into capitated contracts, or contracts with withholds. There is some evidence that PBMs, like other health care intermediaries, are beginning to enter into capitated arrangements.[187]

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trust Enforcement, FTC NEWS (Federal Trade Commission, Washington, D.C.), Aug. 28, 1996 (FTC press release including Robert Pitofsky's, FTC Chairman, written statement).

184. According to the 1996 guidelines,

> Such integration can be evidenced by the network implementing an active and ongoing program to evaluate and modify practice patterns by the network's physician participants and create a high degree of interdependence and cooperation among the physicians to control costs and ensure quality. This program may include: (1) establishing mechanisms to monitor and control utilization of health care services that are designed to control costs and assure quality of care; (2) selectively choosing network physicians who are likely to further these efficiency objectives; and (3) the significant investment of capital, both monetary and human, in the necessary infrastructure and capability to realize the claimed efficiencies.

1996 POLICY STATEMENTS, *supra* note 4.

185. *Id.*

186. The standards on clinical integration have raised new questions and there have been no business review letters applying these standards. The AMA recently testified before the FTC that "[u]nfortunately, there is substantial confusion about what constitutes sufficient clinical integration for a fee for service network to qualify for rule of reason analysis." Thomas R. Reardon, M.D., Statement before the FTC Joint Venture Project, July 1, 1997 at 8. The statement also notes that there is only limited use of the expanded treatment of financial risk, such as cost or utilization targets. *See also* Greaney, *supra* note 9, at 309 ("Less clear . . . is how much clinical integration is required. This is likely to be a point of contention and debate in the coming years.").

187. *See* Robert McCarthy, *Is It Risky to Ride with a Drug Company?*, 14 BUS. & HEALTH 30 (1996); Anita R. McGahan, *Industry Structure and Competitive Advantage*, HARV. BUS. REV., Nov.-Dec. 1994, at 115; *Capitation: However You View It, It's a Potent New Force*, DRUG TOPICS, Jan. 23, 1995, at 40.

For discussions of various capitation models, *see generally* Douglas G. Cave, *Today's*

But even if there is some use of financial risk sharing among some PBMs, that does not mean it should be a requirement for all PBMs. There are strong arguments that risk-sharing should not be applicable to PBM joint ventures, or perhaps other health care settings. As FTC Commissioner Azcuenaga has observed:

> Instead of attempting to transplant the emphasis on capitation and risk-sharing from the market for physician services to other markets, it may be more useful to examine the market context in which the venture is being formed, including the likely market power of the venture.[188]

Whether the requirement of risk-sharing should be extended outside the physician joint venture context raises important policy questions.[189] Financial risk-sharing as an indicia of integration was adopted for physician joint ventures only after several years of government investigations, enforcement actions, academic commentary,[190] and a lengthy dialogue with the industry.

Moreover, the reasons for these particular standards may be inapplicable in the pharmaceutical context. For example, the Policy Statements standard requires financial incentives to meet cost-containment goals because of the concern that a physician member may attempt to free-ride on the venture and overprescribe treatment.[191] This objective seems inappropriate in the pharmacy setting since pharmacists do not prescribe treatment.

The purpose of these integration standards, in part, is to assure that the venture member is fully committed to the success of the venture by changing its incentives. In a situation like a PBM joint venture, where the venture is producing something its members could not produce individually, their incentives have already changed. There is no need to provide an additional guarantee to insure their commitment to the success of the venture. Moreover, phar-

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Managed Care Market-Developing Capitation Rates for Disease Management Programs, COMPENSATION & BENEFITS MGMT., (Winter 1996); Joseph S. Coyne and Stuart D. Simon, *Capitation: Selecting the Method, Determining the Rates*, HEALTH CARE FIN. MGMT., Aug. 1996; Robert Fromberg, *Capitation is Coming*, HEALTH CARE EXECUTIVE, Jan./Feb. 1996.

188. Remarks of Commissioner Azcuenaga, *supra* note 132.

189. *Id.* The revised Policy Statements observe that the physician joint venture standards are not necessarily applicable to other forms of joint ventures.

190. Although there have been studies of the effect of capitation and withholds on physician behavior, no such studies have been conducted in the PBM market. *See, e.g.*, Gordon & Herman, *Appropriate Reimbursement Methodologies for Managed Care Systems*, *in* MAKING MANAGED HEALTHCARE WORK: A PRACTICAL GUIDE TO STRATEGIES AND SOLUTIONS (P. Boland ed. 1991) (if physicians do not expect a return of the withhold, they may view it as a discount and increase the volume of services in order to increase total reimbursement); Hillman et al., *How Do Financial Incentives Affect Physician's Clinical Decision and the Financial Performance of Health Maintenance Organizations*?, 321 N. ENG. J. MED. 86, 90 (1989) (presence of a higher proportion of HMO patients in a physician's practice may increase his or her awareness of the HMO's imperatives).

191. 1996 POLICY STATEMENTS, *supra* note 4.

macies have another interest which assures their commitment to the venture—to prevent the erosion of retail pharmacies and increase the volume of traffic through their stores. Thus, the likelihood that they will use a network to mask sham activity is probably slight.

If one takes a broader view of integration, a PBM joint venture probably will be sufficiently integrated. A venture which creates additional productive capacity through the formation of a new producing organization, the development of a new product or technology, or the entry into a new market would meet this test. A PBM network involves a significant investment in terms of, for example, creating the necessary infrastructure, promoting the product, developing relationships, creating an electronic payment system and establishing a formulary.

Financial risk sharing should not be a necessary feature where these factors are present. There was no financial integration in *BMI*, yet the lack of integration was not even at issue.[192] In other cases, such as *NCAA*, and in the numerous cases involving the NFL,[193] rule of reason treatment has been accorded even though there was no financial integration or risk sharing of any consequence.[194] Each of the network joint ventures described earlier were apparently found sufficiently integrated, even though the investments by any member were relatively minor. In some of these cases, the courts specifically refused to apply *Maricopa* and subject the ventures to per se condemnation.[195] Numerous other ventures with relatively little integration have been approved by the Justice Department.[196] As a leading article on the subject observes

192. It would be difficult to argue that the Court applied the rule of reason to the *BMI* licensing arrangement because the songwriters were engaged in the type of risk-sharing and economic integration mentioned in *Maricopa* as factors distinguishing price-fixing conspiracies from procompetitive pricing agreements. The BMI songwriters were not joint owners or contributors of risk capital. Integration was limited to sales, monitoring and enforcement against unauthorized use. *BMI*, 441 U.S. at 20. *See also NaBanco*, 779 F.2d at 599. "The blanket license in *BMI* was a practical necessity because it was virtually impossible for thousands of composers to negotiate individually over the use of each song, for each user to report the amount of use, and for each composer to police the use of his works by authorized and unauthorized users." *Id. See also* Richard D. Raskin, *Antitrust Issues for Independent Health Care Providers: 'Integration' and the Per Se Rule, in* ANTITRUST AND EVOLVING HEALTH CARE MARKETS: A SYMPOSIUM FOR HEALTH CARE INDUSTRY PARTICIPANTS, COUNSEL & POLICYMAKERS 85 n.7 (1995). "The price agreement at issue in *BMI* did not involve financial integration." *Id.*

193. *See, e.g.*, Los Angeles Memorial Coliseum Comm'n v. National Football League, 726 F.2d 1381, 1395-98 (9th Cir.), *cert. denied*, 469 U.S. 990 (1984).

194. Greaney & Sindelar, *supra* note 134, at 573 n.243.

195. *See, e.g.*, National Bancard Corp. ("NaBanco") v. VISA U.S.A., Inc., 779 F.2d 592 (11th Cir.), *cert. denied*, 479 U.S. 923 (1986); *In re* Arbitration Between First Texas Savings Ass'n and Financial Interchange, Inc., 55 Antitrust & Trade Reg. Rep. (BNA) No. 1380, at 349 n.11 (Aug. 25, 1988).

196. *See, e.g.*, Business Review Letter to Newspaper Ass'n of America, Dec. 10, 1993 (joint

"[j]oint enterprises falling far short of full integration [as set out in *Maricopa*] have *without exception* qualified for the 'safe harbor' of the rule of reason."[197]

Moreover, not applying the per se rule is consistent with the purpose of the sham inquiry—the search for cartel arrangements. The antitrust enforcement agency's underlying concern is whether a PBM joint venture could facilitate cartel behavior, by providing independent competitors the opportunity to collude under the cover of a joint venture umbrella. This could be very difficult unless the venture possessed both: (1) "a mechanism for preventing cheating on the cartel by individual members of the cartel[; and (2)] a sufficiently large share of the market so that limiting output will have the prospect of raising prices."[198] Unless those factors are present, it will be difficult for the venture to police and enforce the cartel price.

Assume for the sake of argument that the level of integration is less significant. What if the PBM simply serves as a bargaining agent for a large group of pharmacies but does not provide any additional service? Certainly the arrangement has some efficiencies since it reduces the transactions costs of plan sponsors which seek to form a group of pharmacies for a PBM. During the Congressional debate on the Policy Statements, some advocated for recognition of transactions costs as integrative efficiencies, but they are not discussed in the revised Statements. There may be circumstances in which transactions cost savings alone could warrant treating such arrangements under the rule of reason, and the revised Statements do not preclude such treatment. The agencies may have been reluctant to acknowledge this because this type of efficiency raises complicated issues, as transactions cost savings may provide cover for cartel behavior, and some transactional efficiencies are present in every price fixing arrangement, including naked cartels. Moreover, it is argued that there is some risk that more explicit treatment of transactions costs efficiencies at the characterization stage (they are addressed in the rule of reason) could have been read as a signal that the agencies are retreating from enforcement in this area.[199]

However, there is probably some point, especially when dealing with large numbers of providers, where these transactions costs are so significant, espe-

venture network for selling advertising space for national advertising campaigns); Business Review Letter to Affiliated Distributor, May 5, 1992 (creation of joint venture to provide national accounts program); Business Review Letter to Independent Drug Wholesalers Group, May 21, 1987 (same). In each of these letters, the Department approved price setting by the venture to third parties.

197. Popofsky, *supra* note 134, at 1142. (emphasis added).

198. United States v. Columbia Pictures Indus., 507 F. Supp. 412, 429 n.47 (S.D.N.Y. 1980) (citing Antitrust Division's brief), *aff'd mem.*, 659 F.2d 1063 (2d Cir. 1981). In *Columbia Pictures* the court found each of these factors present and condemned a joint venture's price and output restraints as per se illegal.

199. Greaney, *supra* note 9, at 309 (applying rule of reason whenever transactions costs savings are present "would seriously hamper effective antitrust enforcement.").

cially if supported by testimony from buyers, that they should support a finding that the venture is legitimate. The example of a PBM of numerous independent pharmacies would seem to be such an example. Absent the joint venture, the transactions costs are so significant that these pharmacies are often excluded from the network, or are included only at a lower price. As noted earlier, in response to this problem of exclusion, independent pharmacies have successfully lobbied for any willing provider legislation in over thirty states. The courts have readily acknowledged the existence of transaction costs efficiencies, in *BMI* and *NaBanco*, in finding ventures legitimate.[200] Greater sensitivity to transaction cost efficiencies would further a sensible public policy.

Identifying the appropriate integration standard is not a simple task. The courts have been silent, and both the courts and enforcement agencies often appear to assume its existence.[201] The carefully measured standards in the Health Care Policy Statements appropriately assist in identifying sham conduct by health care providers.[202] Although financial risk sharing may be a valuable indicia in that context, without further industry-specific experience, it should not be extended to pharmaceutical networks. Rather, relatively minimal integration, like the earlier joint ventures which were not challenged by the Antitrust Division, should be considered sufficient.

B. *Policy Reasons to Refrain From Per Se Analysis*

Even if a "formalistic" per se approach might be valid in these circumstances, there are several policy reasons to refrain from such an approach. These reasons counsel for, at most, a limited rule of reason analysis of either the creation of a PBM joint venture, or any restraints established by the venture.

First, as discussed earlier, the structure of these ventures and the market makes cartel behavior unlikely. If the underlying concern is that the pharmacy-owned PBM might act as a cartel, so long as the venture is nonexclusive, cartel behavior seems unlikely. Moreover, prices are easily observable and plan sponsors are generally well-informed buyers that possess substantial buying power.[203] In addition, the creation of a new entrant in the PBM market does not appear, on its face, to have any anticompetitive impact.

Second, there appear to be significant procompetitive benefits from the creation of a PBM joint venture. If the per se rule is applied, none of these will be considered in the decision to take enforcement action. In the PBM market, a pharmacy joint venture increases competition by providing a new entrant. A

200. *Broadcast Music*, 444 U.S. at 24; *NaBanco*, 779 F.2d at 601.

201. *Id.*

202. 1996 POLICY STATEMENTS, *supra* note 4.

203. *See* National Cable Television Ass'n v. BMI, 772 F. Supp. 614, 639-40 (D.D.C. 1991) (discussing the relevance of buyers power argument to the validity of a blanket license).

PBM joint venture may enable small pharmacies to bear the transactions costs internalized in the structure of a chain pharmacy. Absent a PBM joint venture, these independent pharmacies might be unable to participate in a PBM. Perhaps as important, consumers who would prefer to use their independent pharmacy would have less choice. Consumers may prefer the personal contact they receive at an independent pharmacy.

A PBM joint venture may also improve competition in the pharmacy market. Access to a PBM is increasingly crucial for the competitive viability of a pharmacy. PBMs serve an important role in directing consumers to preferred pharmacies. In addition, PBMs provide important cost savings to pharmacies, in terms of group purchasing.[204]

A PBM joint venture may also improve the efficiency and competitiveness of its members by aggregating buying power of both the pharmacies and the plan sponsors. These savings could not be achieved by a joint buying group alone because only a PBM has the power to solicit discounts based on share shifting (e.g., preferential listing on the formulary). Because of the savings from the joint buying arrangement small pharmacies are able to compete more effectively.

Third, applying the per se rule may implicitly condemn the ability of independent pharmacies to act collectively to attain the efficiencies of a chain drugstore. Such a decision has important public policy ramifications because it implies that independent pharmacies cannot imitate chain drugstores by agreeing to jointly bid on third party plans. Since the majority of pharmaceuticals are purchased under third party plans currently and this percentage continues to grow, deciding on a per se basis that independent pharmacies are prevented from offering the services that third party payers desire and chain drugstores, by virtue of their control/ownership of multiple locations provide, may competitively disadvantage independent pharmacies substantially. If the antitrust laws prevent independent pharmacies from organizing in a way that mimics chain drugstores without allowing them to exercise market power, a decision that this method of organization is per se illegal simply asserts that one form of corporate organization, multiple pharmacy locations jointly owned (i.e. a chain drugstore) will be competitively favored over another, multiple pharmacy retail locations independently owned.[205]

Fourth, PBMs owned by independent entities (*i.e.*, not owned by pharmaceutical manufacturers) may serve important competitive interests. As described earlier, acquisitions of PBMs by pharmaceutical manufacturers raise

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204. *Cf.* GAO REPORT, *supra* note 16.

205. Congress has expressed its intent in the NCPRA, that the law should not inhibit small businesses from joining together to effectively compete with their larger counterparts. Absent observable anticompetitive effects, there is no reason to condemn such a venture. S. Rep. No. 51, 103d Cong., 1st Sess. at 16 (1993).

concerns of foreclosure and collusion.[206] The existence of independent PBMs may partially ameliorate these concerns by providing another means of access.

For example, manufacturer-owned PBMs might attempt to foreclose the drugs of their competitors. Each of the manufacturer-owned PBMs could enter into a reciprocal arrangement to exclude the drugs of competing manufacturers.[207] Pharmacy owned PBMs would have no incentive to engage in such reciprocal foreclosure.

In addition, independent PBMs, especially those owned by pharmacies, are less likely to raise concerns that the PBM is serving as the agent of the manufacturer, and is improperly "pushing" the manufacturer's drugs.[208] Finally, because a pharmacy-owned PBM has different incentives than one owned by a pharmaceutical manufacturer it is less likely that it would engage in collusion or oligopolistic behavior.

Fifth, requiring financial risk-sharing raises important policy issues. Whether capitation or financial withholds are appropriate for pharmacy networks is an extremely open and uncertain question. The purpose of those tests is to assure the commitment of the members to the venture.[209] Other productive network ventures, such as those described earlier, reach these goals through a wide variety of means. Without further empirical experience it would be imprudent to condemn as per se illegal one form of organization. The Supreme Court observed in *Continental Television v. GTE Sylvania*, that the per se doctrine should not be extended to restraints of trade that are of ambiguous effect; "[any] departure from the rule of reason standard must be based upon demonstrable economic effect rather than . . . upon formalistic line drawing."[210]

Finally, considering the youth and continually evolving structure of the PBM industry, per se condemnation would be particularly inappropriate. As the Supreme Court stated in *United States v. Topco*: "it is only after considerable experience with certain business relationships that courts classify them as per se violations."[211] The guidance of the Eighth Circuit when it looked at the infant credit card industry is on point:

> The bank card industry is a relatively new one and, with over eight billion dollars in annual business, a very large and important segment of our economy. Considering the importance of the industry and the lack of definitive information relating to competition therein, it would be a mistake to determine this case of first impression on a per se basis. This is especially true where it

206. *See* GAO REPORT, *supra* note 16.

207. *Id.*

208. This has been a significant consumer protection concern. *Id.*

209. *Cf. Capitation is Seen as Brightest Line in Quest for Sufficient Integration*, 68 Antitrust & Trade Reg. Rep. (BNA) NO. 1702, at 295 (Mar. 2, 1995).

210. Continental T.V. v. GTE Sylvania Inc., 433 U.S. 36, 58-59 (1977).

211. United States v. Topco Assoc., 405 U.S. 596, 607-08 (1972).

> may result in the dilution of competition or the elimination of one of the two competitors where this is not an aggregate of illegal restraints such as price fixing or exclusive territorial allocations and where the initial purpose in forming the joint venture, to produce a national credit card, is obviously not illegal.[212]

C. *Are the Price Restraints Reasonably Necessary?*

Once the joint venture itself survives per se condemnation, any collateral restraints imposed by the venture are analyzed. This may be two separate inquiries or may be merged into a single inquiry. A PBM joint venture has arguably established a price restraint by setting the price that the venture will bid for contracts with plan sponsors and PBMs. In the typical joint venture arrangement, one might be cautious about calling this agreement a "restraint" where: (1) the venture does not restrict its members from entering into contracts with other PBMs (and in fact the members belong to other PBMs); and (2) members can decide to individually reject a contract.

Antitrust analysis of collateral restraints imposed by joint ventures and other partial integrations among competitors begins with *United States v. Addyston Pipe & Steel Co.*,[213] where Judge Taft drew a sharp distinction between those restraints characterized as "naked" (*i.e.*, "having for their sole object the restraint of trade"), and those ancillary to the primary and lawful purpose of the parties' agreement.[214] Ancillary restraints were to be judged under a standard of reasonableness, with the central inquiry being whether the restraints at issue exceeded "the necessity presented by the main purpose" of the contract.[215]

In modern terms, the focus under an *Addyston Pipe* standard is on whether the restraint is *reasonably necessary* to the attainment of the efficiencies which justify the venture in the first instance.[216] As former-Judge Bork defined the standard for evaluating collateral restraints:

> To be ancillary, and hence exempt from the per se rule, an agreement eliminating competition must be subordinate and collateral to a separate, legitimate transaction. The ancillary restraint is *subordinate and collateral in the sense that it serves to make the main transaction more effective in accomplishing its purpose*. Of course, the restraint imposed must be related to the efficiency sought to be achieved. If it is so broad that part of the restraint suppresses

212. Worthen Bank & Trust Co. v. National BankAmericard, Inc., 485 F.2d 119, 129-30 (8th Cir. 1973), *cert. denied*, 415 U.S. 918 (1974). *See also Broadcast Music*, 441 U.S. at 9.

213. 85 F. 271 (6th Cir. 1898), *modified and aff'd*, 175 U.S. 211 (1899).

214. *Id.* at 283.

215. *Id.* at 282.

216. *See, e.g.*, United States v. Realty Multi-List, Inc., 629 F.2d 1352, 1375 (5th Cir. 1980); National Bancard Corp. v. VISA USA, Inc., 596 F. Supp. 1231, 1257 (S.D. Fla. 1984), *aff'd*, 779 F.2d 592 (11th Cir. 1986), *cert. denied*, 479 U.S. 923 (1986).

competition without creating efficiency, the restraint is, to that extent, not ancillary.[217]

Thus, if restraints are both related to and necessary to achieve the efficiency-enhancing goals of the joint venture, they should be analyzed under the rule of reason. A restraint is reasonably necessary if it is "substantially related to the efficiency-enhancing or procompetitive purposes" of the venture,[218] and the efficiencies cannot be reasonably attained through means that are less restrictive of competition.[219] This "reasonably required" approach was incorporated into the National Cooperative Production Amendments of 1993.[220]

When a PBM joint venture bids on behalf of its members it is acting as a joint sales agent. Price setting by a joint sales agency is typically analyzed under the rule of reason.[221] The Supreme Court has observed that certain joint selling arrangements "may be so efficient that [they] will increase the sellers' aggregate output and thus be procompetitive."[222] Moreover, the Court observed that "a joint selling arrangement may 'mak[e] possible a new product by reaping otherwise unattainable efficiencies.'"[223] Both *BMI* and *NCAA* provide guidance on how price setting by a joint sales agent is analyzed. In both cases, the exclusivity or non-exclusivity of the joint venture proved to be the critical factor, along with whether the restraint was necessary to produce the product.

1. *BMI*

After the Court determined that the BMI venture was not per se illegal, the

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217. *Rothery*, 792 F.2d at 223-24 (emphasis added).

218. Northwest Wholesale Stationers, Inc. v. Pacific Stationery & Printing Co., 472 U.S. 284, 296 n.7 (1985).

219. *See, e.g.*, Chicago Prof'l Sports L.P. v. National Basketball Ass'n, 961 F.2d 667, 676 (7th Cir. 1992), *cert. denied*, 506 U.S. 954 (1992); Los Angeles Memorial Coliseum Comm'n v. National Football League, 726 F.2d 1381, 1395-98 (9th Cir. 1984) (rule effecting territorial allocation was not justified where less restrictive alternative was available), *cert. denied*, 469 U.S. 990 (1984); United States v. Realty Multi-List, 629 F.2d 1351 (5th Cir. 1980); *Financial Interchange*, 55 Antitrust & Trade Reg. Rep. (BNA), at 365 ("[a]n interchange fee agreement with a surcharge/rebate option is significantly less restrictive than [one] without such an option, and would not violate Section 1 of the Sherman Act"). *See generally* Thomas L. Greaney, *Is Antitrust Anti-Autonomy?*, 6 HEALTH MATRIX 129, 136 (1996); Kevin J. Arquit & Joseph Kattan, *Efficiency Considerations & Horizontal Restraints*, 36 ANTITRUST BULL. 717, 729-31 (1992).

220. *See* 15 U.S.C. § 4301(b)(3) (1988); Pub. L. No. 103-42, 107 Stat. 117, § 3(c)(5) (1993), *to be codified in* 15 U.S.C. §§ 4301(b)(5), 4301(b)(8) (excluding certain restraints from Act's protection unless "reasonably required" to attain specified efficiencies); S. Rep. No. 51, 103d Cong., 1st Sess. at 16 (1993) (ancillary restraints "must be reasonably required to accomplish legitimate goals").

221. *See generally*, 1 ANTITRUST LAW DEVELOPMENTS (FOURTH), *supra* note 72, at 406-07.

222. *NCAA*, 468 U.S. at 104.

223. *Id.* at 113 (quoting Arizona v. Maricopa County Medical Soc'y, 457 U.S. 332, 365 (1982) (Powell, J., dissenting) (footnote omitted)).

question became one of whether the setting of the price was reasonably necessary for the sale of the blanket license.[224] While recognizing that this collective fee setting was price-fixing in a "literal sense," the Court concluded that the blanket licensing agreement was not per se illegal but should be subjected to a broad rule of reason inquiry.[225] The restraint was not "naked," but accompanied a partial integration of those participating in the licensing organizations.[226] By eliminating these transaction costs, the blanket licensing agreement increased efficiency.[227] The Court stressed that such a license was reasonably necessary to achieve these efficiencies, and that a "necessary consequence" of a blanket license was the establishment of a price.[228] In addition, the Court noted that the blanket license was not mandatory and that individual copyright owners could negotiate separately with respect to their own compositions.[229] Accordingly, the Court held that the blanket license was not per se illegal, but rather "should be subjected to a more discriminating examination under the rule of reason."[230]

On remand, the Second Circuit did not conduct a full rule of reason analysis. It upheld the price setting based on a single issue—the blanket license was nonexclusive, hence there could be no restraint of trade.[231] Under the license, individual composers retained the right to negotiate fees for their own compositions outside the framework of the blanket license.[232]

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224. *Broadcast Music*, 441 U.S. at 23. *See supra*, notes 90-99 and accompanying text.

225. *Id.* at 23-24.

226. *Id.* at 20.

227. *Id.* at 20-21.

228. *Id.* at 21.

229. *Broadcast Music*, 441 U.S. at 24.

230. *Id.*

231. Columbia Broadcasting Sys., Inc. v. ASCAP, 620 F.2d 930, 935 (2d Cir. 1980), *cert. denied*, 650 U.S. 970 (1982).

232. *Id.* (blanket license not a restraint where opportunity to purchase performing rights to individual songs is fully available), *cert. denied*, 450 U.S. 970 (1982). *See also* Stratmore v. Goodbody, 866 F.2d 189, 193 (6th Cir. 1989) (restriction on auctions were not considered a restraint since seller had alternative means to reach customers), *cert. denied*, 490 U.S. 1066 (1989); Buffalo Broadcasting Co., Inc. v. ASCAP, 744 F.2d 917, 925 (2d Cir. 1984) ("blanket license" offered by a group of copyright owners not an antitrust violation because copyright owners had the ability to enter into separate arrangements; noting that "the opportunity to acquire a pool of rights does not restrain trade if an alternative opportunity to acquire individual rights is realistically available"), *cert. denied*, 469 U.S. 1211 (1985). *Cf. NCAA*, 468 U.S. at 114 n.54 (freedom of individual participants to increase their own output central to evaluation of venture); National Bancard Corp. v. VISA, U.S.A., Inc., 596 F. Supp. 1231, 1254 (S.D. Fla. 1984) (stressing availability of alternative arrangements), *aff'd*, 779 F.2d 592 (11th Cir. 1986), *cert. denied*, 479 U.S. 923 (1986); *In re* Matter of First Texas and Fin. Interchange, 55 Antitrust & Trade Reg. Rep. 340, 365 (Aug. 25, 1988) (noting that "if ATM operators are free to impose surcharges or rebates on PULSE transactions, virtually all of the adverse effects [of a collectively set interchange fee] . . . disappear").

Exclusivity was a crucial factor because such a restriction would be necessary to facilitate a cartel arrangement.[233] Absent exclusivity, members of the cartel could cheat on the cartel when the opportunity arose. Similarly, if BMI set prices at non-competitive levels, buyers could enter into alternative arrangements with individual members of the venture.

2. *NCAA*

In *NCAA*,[234] the Court after declining to condemn the NCAA venture under the per se rule, analyzed whether the NCAA's restraints on the output and price of college football telecasts was reasonably necessary to its objective of promoting intercollegiate football games. The NCAA retained exclusive rights to the marketing of televised college football, including setting the "minimum, maximum and actual price which will be paid to the schools"[235] for television appearances. These restraints had anticompetitive consequences, including higher prices and lower output for televised college football.[236]

The Court rejected NCAA's arguments that the restraints were reasonably necessary to the production of college football.[237] Moreover, the Court rejected the argument that the restraints were necessary to promote athletic parity, since there were less restrictive means, such as differences in the number of athletic scholarships permitted that could have achieved the same goal.[238] The output restraints were not justified on the basis of a transaction cost efficiency because, unlike the situation in *BMI*, the NCAA members were able to negotiate on an individual basis because of the relatively small number of games involved.[239] Moreover, unlike *BMI*, the Court found, an individual producer (i.e., a school) could enhance the volume of output beyond that established by the restrictions of the joint venture.[240] Because of the exclusivity in the NCAA's television plan, individual schools could not offer alternative

233. In all the recent cases condemned as per se illegal the venture precluded its members from dealing outside the venture. *See* COMPACT v. Metropolitan Gov't, 594 F. Supp. 1567, 1574 (M.D. Tenn. 1984) (agreement by black-owned architectural firms not to bid individually on projects on which they were bidding jointly was per se illegal); United States v. Columbia Pictures Indus., Inc., 507 F. Supp. 412 (S.D.N.Y. 1980) (restrictions on competitive bidding facially illegal), *aff'd mem.*, 659 F.2d 1063 (2d Cir. 1981).

234. 468 U.S. 85 (1984).

235. *Id.* at 106 n.30 (quoting the District Court).

236. Despite the fact that the Court easily observed anticompetitive effects of the television restrictions, it rejected the NCAA's argument that it did not possess market power, holding that "[a]s a matter of law, the absence of market power does not justify a naked restriction on price or output." *Id.* at 109. The Court then noted that the NCAA did have market power. *Id.* at 111.

237. *NCAA*, 468 U.S. at 114-115.

238. *Id.* at 119.

239. *Id.* at 114 n.53.

240. *Id.* at 114-115.

competition.[241] Accordingly, the NCAA plan was held unlawful on the ground that it had "curtail[ed] output and blunt[ed] the ability of member institutions to respond to consumer preference."[242]

3. Application to a PBM Joint Venture

In both *BMI* and *NCAA* the Court declined to invalidate the venture, but reached different conclusions on whether the price restraint was naked or ancillary. The *NCAA* plan was held unlawful while the *BMI* blanket license was upheld because: (1) the price restraint was found necessary to market the joint venture product in *BMI*,[243] and (2) each BMI member, unlike the NCAA schools, remained free to sell its own product.[244]

The answer for a PBM joint venture depends upon the type of pricing involved. Assume for the moment that the PBM sets prices not only to plan sponsors, but also the prices of other non-PBM products to consumers outside the network. It is difficult to imagine how price setting to consumers would be reasonably necessary to the effective functioning of the joint venture, rather, this seems like garden variety price fixing, which should be condemned as per se illegal.[245]

The joint venture's price to the plan sponsor should pass muster under the rule of reason, especially where the venture is non-exclusive.[246] Joint price setting appears to be reasonably necessary in order for a PBM joint venture to bid on contracts with plan sponsors. Plan sponsors could reasonably require that a bidder specify certain specific prices and a certain level of geographic coverage. If a PBM joint venture was unable to specify a certain price or level of coverage, its bid might not be accepted. That is why many PBMs have established standing networks of available pharmacies. Like the price of the blanket licenses in *BMI*, price setting is necessary for the effective sale of the product, since it reduces the substantial transaction costs involved in selling the product. Thus, joint price setting is "subordinate and collateral" in the sense

241. *Id.* at 115.

242. *NCAA*, 468 U.S. at 120.

243. *Broadcast Music*, 441 U.S. at 20-21.

244. *Id.* at 23.

245. *See* 1 ANTITRUST LAW DEVELOPMENTS (FOURTH), *supra* note 72. A recent FTC enforcement action provides an example of the application of the ancillary restraint doctrine. A group of urologists in Chicago formed a joint venture to provide an outpatient lithotripsy procedures—a non-surgical shock wave treatment for kidney stones. There are three services that must be billed for lithotripsy treatment—a facility fee, an anesthesiologist fee, and the urologist's professional fee. In this case the joint venture collectively set each of these fees. Although setting the facility fee probably was reasonably necessary, the collective setting of the professional fee was not. The FTC secured a proposed consent which prohibits the joint venture from collectively setting the professional fee. *See In the Matter of* Urological Stone Surgeons, No. 931-0028 (Jan. 6, 1998).

246. *See supra* notes 240-41 and accompanying text.

that it enables a PBM joint venture to compete in the market for PBM services.[247]

Determination of reasonable necessity requires consideration of whether there are substantially less restrictive alternatives which can achieve comparable efficiencies. Under this analysis, a restraint may still be "reasonably necessary" despite the existence of alternative arrangements less burdensome to competition. A restraint need only contribute substantially to the efficacy of the arrangement.[248] The courts have held that consideration of alternatives should be used in evaluating competitive benefits against risks, but should not bind the courts to condemn ventures anytime a somewhat superior alternative is identified.[249]

The Intellectual Property Guidelines, issued by the Justice Department and the FTC, pose the appropriate scope of analysis:

> The existence of practical and significantly less restrictive alternatives is relevant to a determination of whether a restraint is reasonably necessary. If it is clear that the parties could have achieve similar efficiencies by means that are significantly less restrictive, then the Department will not give weight to the parties' efficiency claim. In making this assessment, however, the Department will not engage in a search of a theoretically least restrictive alternative that might be easier to construct in hindsight that in the practical prospective business situation faced by the parties.[250]

Arguably one might consider that a "messenger model" arrangement might be a less restrictive alternative.[251] Under a messenger model a PBM joint venture would simply convey offers to its members, which could inde-

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247. In the SFY business review letter, the Division observed that the "negotiation of price is not necessarily anticompetitive, even though the members are otherwise competitors and the PPO is provider-controlled. [The] negotiation of price can be an integral part of a demonstrably procompetitive PPO."

In a Business Review Letter, the Division found that joint price setting by a joint venture which created a national network to sell newspaper advertising space was "reasonably" related to its function as a joint sales agent. *See* Business Review Letter to The Newspaper Association of America (Dec. 10, 1993).

248. *See* 1 ANTITRUST LAW DEVELOPMENTS (FOURTH), *supra* note 72, at 416-22.

249. *Rothery*, 792 F.2d at 227-28.

> We do not believe ... that, in choosing the words it did, the Supreme Court intended that lower courts should calibrate degrees of reasonable necessity. That would make the lawfulness of conduct turn upon judgments of degrees of efficiency. There is no reason in logic why the question of degree should be important.

Id.

250. JOINT U.S. DEP'T OF JUSTICE & FEDERAL TRADE COMM'N, ANTITRUST GUIDELINES FOR THE LICENSING OF INTELLECTUAL PROPERTY(1995), *reprinted in* 4 Trade Reg. Rep. (CCH) ¶ 13,132, at 20,743.

251. The Antitrust Division approved the SFY PBM even though it was not a messenger model.

pendently decide whether to participate.[252]

A messenger model may not be an effective alternative especially where there are a large number of pharmacies. It may be more uncertain and time consuming for a messenger model to aggregate and convey bids. It may not be feasible for a PBM to submit each potential contract and reimbursement rate to each pharmacy to determine whether it wishes to participate. There may be insufficient time between a request for proposal and the time a proposal is submitted to generate a network. The initial offer by the insurer or purchaser must be accepted by a sufficient number of providers. Otherwise, the insurer or purchaser would have to change the terms of its offer, and the process would be repeated. As a result, the messenger model is often not particularly attractive to providers.[253]

D. Analysis Under the Rule of Reason

Once a venture is determined legitimate, the analysis of the venture and its restraints is under the rule of reason. An inquiry under the rule of reason should focus on exclusivity and market power.[254]

1. Exclusivity

Exclusivity is a critical factor in rule of reason analysis. Numerous courts have held that a rule of reason violation can not be found unless the venture prohibits its members from acting outside the venture.[255] As the court in *NaBanco* observed "a practice is not unlawful per se where . . . there is no legal, practical or conspiratorial impediment to making alternate arrangements."[256] Where exclusivity is not required, each joint venture member is able to participate in any PBM.[257] Where a joint venture permits its members to participate in other networks and a large portion of members do participate in more than one network, that fact alone may suggest that the network lacks market power.[258]

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252. *See* Health Choice of Northwest Mo., Inc., 60 Fed. Reg. 51,809 (Dept. Justice 1995) (Proposed Final Judgment and Competitive Impact Statement).

253. Julie Y. Park, *PHOs and the 1996 Federal Antitrust Enforcement Guidelines: Ensuring the Formation of Procompetitive Multiprovider Networks*, 91 NW. U. L. REV. 1684, 1708 (1997) (noting criticism of cases where DOJ imposed messenger model and ownership restrictions as relief); *Law Firm Warns of FTC's and DOJ's Increased Focus on Messenger Model*, 4 Health L. Rep. (BNA), at 603 (Apr. 29, 1995) (a messenger model "is cumbersome to implement and adds significant costs to the operation of the network because the model requires numerous individual transactions and negotiations.").

254. 1996 POLICY STATEMENTS, *supra* note 4.

255. *See supra* note 232.

256. National Bancard Corporation v. Visa U.S.A., Inc., 596 F. Supp. 1231, 1254-55 (S.D. Fla. 1984), *aff'd*, 779 F.2d 592 (11th Cir. 1986), *cert. denied*, 479 U.S. 923 (1986).

257. *Id.*

258. *Id.*

The critical nature of non-exclusivity is suggested by the FTC's one enforcement action involving a PBM joint venture. In 1996 the Commission entered a consent agreement with RxCare, a joint venture PBM network which included practically every pharmacy in Tennessee.[259] Although the joint venture appeared to have a one hundred percent market share the Commission chose to challenge just one aspect of its contracts—a most favored nations ("MFN") clause.[260] The MFN provision provided that pharmacy members could participate in other networks but only if they charged the same prices they charged RxCare.[261] RxCare compelled its member pharmacies to agree to an MFN clause, which required an RxCare pharmacy that accepted a reimbursement rate lower than the RxCare rate to accept the lower reimbursement rate for all its RxCare business.[262]

Most important, the MFN provision acted as a de facto exclusivity provision. RxCare's business is a large percentage of the pharmacies' third-party business. As a result, the clause made it very expensive for pharmacies to participate in other lower priced networks and they rarely did so. To participate in lower priced networks would force members to lower their RxCare price.

One might ask why the FTC did not seek to dissolve the network or restrict its size. First, the arrangement seemed efficient in many respects. As Commissioner Varney noted when the proposed consent was issued: "joint ventures by retail pharmacists can be procompetitive by injecting new competition into the market for pharmacy benefit management services."[263] Perhaps more important, once the de facto exclusivity provision was eliminated, the pharmacy members would no longer face the strong disincentive to participate in other networks. Thus, without exclusivity even a network with an apparently large market share might not raise market power concerns.

Although proclaiming a network "non-exclusive" may be relevant to an analysis of exclusivity, that factor is not dispositive. The agencies have significant experience with ventures, like RxCare, that were allegedly non-exclusive, but used a variety of other mechanisms to enforce exclusivity. The 1996 Policy Statements caution that some arrangements that appear to permit participating providers to contract individually may nevertheless prove to be exclusive in operation.[264] Among the factors that the agencies consider to determine whether a network is "non-exclusive in fact and not just in name" are whether there are "viable competing networks or plans" in the market: whether providers in the network actually participate in other networks or

259. *In re* RxCare of Tenn., Inc. No C-3664 (Federal Trade Comm. June 10, 1996).

260. *Id.*

261. *Id.*

262. *Id.*

263. *Id.* (Statement of Comm. Christine V. Varney, File No. 951 0059).

264. 1996 POLICY STATEMENTS, *supra note 4*

contract individually; and whether network providers earn substantial revenue outside the network.[265]

Some of the factors the agencies consider in determining whether a particular exclusive arrangement raises antitrust concerns include: "the market share of the providers subject to the exclusivity arrangement; the terms of the exclusive arrangement, such as its duration and providers' ability and financial incentives or disincentives to withdraw from the arrangement; the number of providers that need to be included for the network and potentially competing networks to compete effectively; and the justification for the exclusivity arrangement."[266]

Although non-exclusivity may provide a safe harbor from market power concerns, that does not mean that a venture necessarily must be non-exclusive. The Policy Statements note that exclusivity is not necessarily anticompetitive. It may, for example, increase providers' incentives to promote the network and help "create a favorable market reputation."[267]

Exclusivity provisions are common in network industries, such as ATM and credit card joint ventures. In *National Bank of Canada v. Interbank Card Association*, a MasterCard rule that barred Canadian licensees from issuing competing credit cards survived challenge.[268] The court found the restraint reasonable because MasterCard had adopted the ban upon entering the market, to protect new members' start-up costs in the venture, and had limited it to eight years, the anticipated time needed to recover the start-up costs.[269] Thus, even an absolute prohibition of competition with a joint venture may survive antitrust review if it is necessary to ensure the viability of the venture. Similarly, even an agreement restricting competition among joint venturers themselves may survive antitrust scrutiny where it is necessary for the creation of the joint venture's product.[270]

Ultimately, the goals of integration and non-exclusivity may not coincide. The integration analysis really looks to indicia of a strong commitment to a network—significant investment, commitment to a network's cost containment goals, financial risk sharing, and other factors.[271] The exclusivity analysis on the other hand, focuses on the ability of members to participate in other networks, and rewards the lack of integration and commitment.[272] To the extent the agencies require nonexclusivity, health care providers will have less incen-

265. *Id.*

266. *Id.*

267. *Id.*

268. National Bank of Canada v. Interbank Card Ass'n 507 F. Supp. 1113, 1115-16 (S.D.N.Y. 1980).

269. *Id.* at 1122-23.

270. *See* Polk Bros., Inc. v. Forest City Enterprises, Inc., 776 F.2d 185 (7th Cir. 1985).

271. 1996 POLICY STATEMENTS, *supra* note 4.

272. *Id.*

tive to financially integrate their operations—particularly since some members will continue to serve other PBM networks.[273]

It may be difficult to resolve the fact that these two goals seem to move the structure of health care ventures in opposite directions. Perhaps this is another factor that counsels for a fairly light handed approach to analysis of integration.

2. Market Power

Even where a venture is legitimate, the enforcement agencies continue to analyze whether there is the potential for the exercise of market power that could ultimately lead to higher prices to consumers.[274] While judicial standards and appropriate yardsticks for market power are often unclear, market power serves as a meaningful indicator of potential competitive effects. The standard for market power articulated in *NCAA* is "the ability to raise prices above those that would be charged in a competitive market,"[275] but this definition ignores the ability to prevent decreases in price, which similarly results in reduced consumer welfare.[276] Instead, the standard for market power should incorporate the broader definition of *United States v. E.I. du Pont de Nemours & Co.*, which refers to the "power to control prices or exclude competition."[277]

The market power concern would be that a PBM joint venture, by combining an overly inclusive group of pharmacies, might inhibit the formation of competing PBMs or prevent payors who wish to deal with pharmacists individually, rather than through the venture, from being able to enter and operate in the market.[278] Two important factors in determining the likelihood of the

273. Provider exclusivity may serve to strengthen the network's procompetitive efficiencies. For providers joining an unlimited number of networks or plans, the incentive to share substantial risk or to provide volume discounts to any one network or plan may be limited. Instead, providers may become fickle and join many nonexclusive networks and plans simply to cover their bases. Moreover, providers are more likely to undertake fundamental and enduring changes in medical practice within a specialty group in which they are vested.

274. 1996 POLICY STATEMENTS, *supra* note 4

275. *NCAA*, 468 U.S. at 109 n.38.

276. *See, e.g., Judge Halts Proposed Merger of Staples and Office Depot*, 73 Antitrust & Trade Reg. Rep. (BNA) No. 1818, at 6 (July 3, 1997).

277. United States v. E.I. du Pont de Nemours and Co. 351 U.S. 377, 391 (1956).

278. *See* Health Choice of Northwest Mo., Inc. 60 Fed. Reg. 51,815 (Dept. Justice 1995) (Proposed Final Judgment and Competitive Impact Statement); Healthcare Partners, Inc., 60 Fed. Reg. 52020 (Dept. Justice 1995) (Proposed Final Judgment and Competitive Impact Statement); Business Review Letter from Justice Department, Antitrust Division, to Children's Healthcare, P.A. (March 1, 1996) (announcing Department's intention to challenge formation of over inclusive pediatric network). *Cf. In re* Matter of Home Oxygen, Medical Equipment, No. C-3530 (Federal Trade Commission Sept. 14, 1994); *In re* the Matter of Homecare Oxygen & Medical Equipment Co., No. 911-0020 (Federal Trade Commission July 28, 1992), (consent

exercise of market power are (1) whether the joint venture is exclusive—whether its members are permitted to compete separately with the venture, either individually or through a competing venture; and (2) whether the venture is overinclusive, in that it includes such a high proportion of competing providers in the market that a sufficient number of other actual or potential providers are not available to form competing arrangements. Where both of these factors are found—overinclusiveness and exclusivity—the risks of the exercise of market power may be especially pronounced.[279]

The question of whether a firm can exercise market power, depends upon a number of factors including the number and size of competitors, exclusivity, and the existence of entry barriers.[280] These factors do not point in a single direction, although they generally suggest that a pharmacy joint venture PBM should usually pass muster. Perhaps the most important factor is the existence of other competitors. Here, where there are large dominant PBMs owned by pharmaceutical companies—DPS, PCS, and MEDCO—the pharmacy-owned PBMs may have quite a struggle to reach the level of size or significance that they will have power over price as PBMs.

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orders issued for public comment Nov. 2, 1993) (Commissioner Azcuenaga concurred with separate statement, Commissioner Starek dissented). Professor Greaney has observed that overinclusive provider networks threaten competition by "lessening price or quality rivalry among physicians or hospitals that contract with [managed care organizations] or employers to deliver services . . , [and] by reducing the feasible number of viable plans and hence increase the risk of oligopolistic behavior." Thomas L. Greaney, *Managed Competition, Integrated Delivery Systems and Antitrust*, 79 CORNELL L. REV. 1507, 1534 (1994).

279. *See* United States v. Health Choice of Northwest Missouri, Inc., Case No. 95-6171-CV-SJ-6 (W.D. Mo.; filed Sept. 13, 1995), 60 Fed. Reg. 51808, 51815 (Oct. 3, 1995); United States and State of Connecticut v. HealthCare Partners, Inc., Case No. 395-CV-01946-RNC (D. Conn.; filed Sept. 13, 1995), 60 Fed. Reg. 52018, 52020 (Oct. 4, 1995); Business Review Letter from Justice Department, Antitrust Division, to Children's Healthcare, P.A. (Mar. 1, 1996)(announcing Department's intention to challenge formation of overinclusive pediatric network); Justice Department, Antitrust Division, Press Release, Oct. 12, 1983 (announcing Department's intention to challenge creation of Stanislaus Preferred Provider Organization, Inc.; 50 to 90% of the providers in the relevant market were members of the PPO); *See also* Business Review Letter from Justice Department, Antitrust Division, to First Priority Health System (Nov. 3, 1997) (where exclusive venture had approximately 30% of providers there were sufficient uncommitted providers in the market for alternative ventures); Business Review Letter from Justice Department, Antitrust Division, to Donald H. Lipson (July 7, 1997) (announcing that Department could not approve a merger of three gastroenterologist practices, which accounted for 12 of the 14 gastroenterologists in the market). *See generally* Federal Trade Commission, *supra* note 124, at 48,990-91 ("serious antitrust concerns might arise if the formation of a plan appeared to eliminate a significant amount of 'potential competition'. . . . If the formation of a plan . . . makes impracticable the formation of other plans that would otherwise be likely to enter the market, potential competition from those plans may be eliminated and enforcement action may be warranted.").

280. *See* U.S. DEP'T. OF JUSTICE MERGER GUIDELINES (1992), *reprinted in* 4 Trade Reg. Rep. (CCH) ¶ 13,104, at 20,571.

In terms of market power, the Health Care Policy Statements provide some guidance. Those statements provide safe harbors for certain physician network joint ventures. The Statements provide that the federal antitrust enforcement agencies will not challenge, absent extraordinary circumstances, an exclusive physician network joint venture comprised of twenty percent or less of the physicians in each physician specialty, or a nonexclusive joint venture with no more than thirty percent of the physicians.[281] The enforcement agencies have approved other physician joint ventures with market shares above these thresholds.[282]

More significant concerns may be raised when the joint venture brings together competing pharmacy chains each of which may serve as the anchor in a PBM network. Pharmacy chains have an advantage over independent pharmacies in PBM networks.[283] PBMs generally seek to have at least one large pharmacy chain in a metropolitan area to "anchor" their PBM network.[284] Once the pharmacy chain is selected the PBM may then "fill in" the network with additional independent pharmacies or smaller chains.[285] Since the bid for the anchor chain may set the price for the entire network, competition for the anchor position in the PBM is very important for controlling costs.

Where a joint venture brings together two or more chains that might serve as an anchor in an individual geographic market, competitive concerns are present. This is illustrated by the proposed 1996 merger between Rite Aid and Revco, the two largest pharmacy chains in the U.S. The FTC challenged the merger on the theory that it would have permitted the merged firm to raise prices to PBMs by combining the two firms that otherwise could have served as anchors in several metropolitan areas.[286]

Assume there is a metropolitan area where third party plans and their subscribers demand the convenience of broad coverage of their market—for example, participation by sixty percent of all local pharmacies. A hypothetical joint venture PBM includes two pharmacy chains, each of which has twenty percent of the stores in the market. Assume further that the venture is also ex-

281. 1996 POLICY STATEMENTS, *supra* note 4.

282. *Id.*

283. Cary, *supra* note 35.

284. *Id.* at 3, 4.

285. *Id.* at 3.

286. *Id.* at 3, 4.

> [I]f the largest two competitors merge, leaving only smaller less cost effective competitors, the merged entity can also withhold its participation in the network except at higher prices than each would have been willing to participate at premerger. The network simply will not get enough participation at a low price because higher-cost stores will not participate; the network will therefore have to increase the price it is offering in order to induce the participation of the large merged chain, or higher cost competitors.

Id.

clusive. Because the joint venture has a significant market share, it could make a higher all-or-nothing offer than either joint venture member would have been able to do individually. The third party plan would have two choices. It could reject the higher joint venture all-or-nothing offer and go deeper and deeper into higher cost independent pharmacies in order to retain its sixty percent coverage, which would, in effect, raise the PBM's costs of doing business. Alternatively, it could cave in and accept the higher joint venture price.

Even outside the Health Care Policy Statement thresholds, there are several ways in which a venture can avoid antitrust risk, especially if it is non-exclusive. First, a PBM joint venture can be structured as a "messenger model,"—an intermediary between plan sponsors and pharmacies. As a messenger model the PBM would form a potential panel of willing pharmacies and communicate requests for proposal from plan sponsors. The PBM then communicates back to the plan sponsor which pharmacies are willing to communicate in the network. Since the PBM joint venture does not actually set the price, concerns over market power are not present. Thus, the agencies have approved various health care networks under a messenger model, without concerns over size.[287]

Second, a PBM joint venture can be structured using another model that limits the size of the ownership of the network. For example, the Department of Justice has entered into consent orders that permit a network to include a relatively large proportion of physicians in a relevant market where the percentage of physicians with an ownership interest in the network is strictly limited, and the network subcontracts with additional physicians under terms that create a sufficient divergence of economic interest between the subcontracting physicians and the owner physicians so that the owner physicians have an incentive to control the costs to the network of the subcontracting physicians.[288] Thus, the focus of whether the joint venture can exercise market power depends not only upon the size of the venture, but also the incentives of its members. In this model, since the non-owner members have the incentive to participate in other networks, the concern over the exercise of market power is reduced.[289]

287. Health Choice of Northwest Mo., Inc., 60 Fed. Reg. 51,809, 51,815 (Dept. Justice 1995) (Proposed Final Judgment and Competitive Impact Study).

288. *See, e.g.*, Health Choice of Northwest Mo., Inc. 60 Fed. Reg. 51,815 (Dept. Justice 1995) (Proposed Final Judgment and Competitive Impact Statement); Healthcare Partners, Inc., 60 Fed. Reg. 52020 (Dept. Justice 1995) (Proposed Final Judgment and Competitive Impact Statement); For a description of the relief in these cases, see Richard D. Raskin, "Blaming the Messenger (Model): Antitrust Challenges to Physician-Hospital Organizations," 29 J. HEALTH & HOSP. LAW 129 (1996); Greaney, *supra* note 219, at 143.

289. Health Choice of Northwest Mo., Inc., 60 Fed. Reg. 51816 (Dept. Justice 1995) (Proposed Final Judgment and Competitive Impact Statement).

V. CONCLUSION

Pharmacies play an important role in the health care system. The emergence of PBMs has dramatically changed the environment of the distribution of pharmaceuticals. Enabling pharmacies to form joint venture PBMs may provide an important new competitive force in this market. This article attempts to explain how these ventures can be created without running afoul of the antitrust laws. Application of the rule of reason to these ventures should improve the opportunity for new competition in this market.

This example illustrates the importance of the debate over the Health Care Policy Statements. Antitrust has played an important role in opening up markets to managed care. The question faced by Congress was whether antitrust was improperly foreclosing these providers from entering into the managed care environment. The 1996 revisions to those Policy Statements open up the possibility that a broader range and number of health care providers can compete as managed care entities without facing per se antitrust condemnation. Making it clear that the rule of reason is the rule of law will enable new forms of competition to arise.