CVS Caremark to cut off Walgreen from network

CVS Caremark Corp. said Wednesday it will end rival Walgreen Co.'s participation in its retail pharmacy network starting in a month.

The move would mean that people whose prescription drug benefits are handled by Caremark would not be able to be reimbursed for prescriptions filled at Walgreen pharmacies. Walgreen said it expects most of its 7,500 stores to be out of Caremark's commercial network in 30 days. Some Walgreen stores won't be cut off as quickly because of state laws or client contracts.

The Woonsocket, R.I., pharmacy benefits manager also said it will end Walgreen's participation in its Medicare Part D retail pharmacy network on Jan. 1.

Walgreen, based in Deerfield, Ill., is the largest U.S. drugstore chain based on locations and revenue, slightly ahead of CVS Caremark. Caremark is one of the largest pharmacy benefits management networks. It negotiates contracts with employers and handles the drug benefit part of their health plans, paying pharmacies to fill prescriptions. It saves money by negotiating volume discounts.

Walgreen wants to be paid more for filling prescriptions, while Caremark makes money by reducing costs for plan members and sponsors. The companies had been in negotiations for months, although CVS now says Walgreen refused to negotiate in good faith.

According to Citi Investment Research analyst Garen Sarafian, about 13 percent of drugstores nationwide are run by Walgreen. The company said it fills almost 20 percent of all retail prescriptions in the U.S.

Sarafian and other analysts think the companies will eventually renegotiate their reimbursement rates because Walgreen does not want to lose the revenue it gets from Caremark, and Caremark does not want to lose contracts to other PBMs. However, a resolution might take months, and Caremark's biggest rivals, Medco Health Solutions Inc. and Express Scripts Inc., will get more business from clients who decide not to participate in a network that excludes the biggest drugstore chain the country.

Sarafian thinks Medco, in particular, will benefit from the split, which comes as the pharmacy benefits managers are trying to secure contracts that will start in 2011.

Earlier this week, Walgreen said it would not do any new business with Caremark because it wants better prices and objects to policies that drive customers to CVS stores. Walgreen said it would honor any current contracts, however, so customers would have felt few effects until 2012.

CVS Caremark said that move was a transparent attempt to raise reimbursement rates. It said consumer access to pharmacies won't be much changed even without Walgreen.

"We've seen Walgreen use this approach in the past, targeting employers, health insurers, government entities and other plan sponsors," said Per Lofberg, president of CVS Caremark's pharmacy benefits business, in a statement from the company. "We believe this approach is totally contrary to the needs of our clients who are all struggling to keep pharmacy health care affordable in today's challenging environment."

Walgreen gets about 7 percent of its revenue from Caremark prescriptions, or about $4.5 billion in its last fiscal year. Caremark handled almost 660 million prescriptions in 2009.

So far, Wall Street appears to believe that CVS has more to lose in the dispute, as its shares are down almost 8 percent this week and Walgreen shares have fallen less than 1 percent. But Moody's Investors Service reduced its outlook on Walgreen's credit to 'negative' from 'stable,' and did not change its view on CVS Caremark.

Moody's said Walgreen could lose customers, which would reduce its pharmacy revenue and sales of other items. The firm said Walgreen may have trouble making up for lost Caremark revenue, which would hurt its credit.

In a statement, Walgreen said in response to the CVS announcement that it was "disappointed but not surprised" by the decision. Walgreen said the move confirms its view that doing business with Caremark was not in its best interest. It said it is confident its business will continue to grow as it participates in PBM networks and provides other services directly to employers.

Walgreen shares fell 49 cents to $30.12 in Wednesday afternoon trading, while CVS shares dropped 36 cents to $30.80.

Associated Press Writer Tom Murphy in Indianapolis contributed to this story.

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