

OPEN THE FLOODGATES: U.S. SUPREME COURT DECIDES ERISA DOES NOT PREEMPT ARKANSAS STATE LAW REGULATING PBMS

On December 10, 2020, the Supreme Court of the United States (the "Supreme Court") unanimously overturned an Eighth Circuit decision in the case of *Rutledge v. Pharmaceutical Care Management Association*. In the case, the Supreme Court held that an Arkansas law known as **Act 900**, which regulates the rates at which pharmacy benefit managers ("PBMs") reimburse pharmacies for prescriptions covered by prescription drug plans, was not preempted by the Employee Retirement Income Security Act of 1974 ("ERISA"). Many view the ruling as a blow to PBMs, as PBMs have often taken the position that ERISA preempts the myriad of state laws seeking to regulate PBM practices, particularly with respect to PBMs' negotiated rates with pharmacies. This decision will likely pave the way for a flood of new state-level PBM regulating legislation in 2021 and beyond. In the meantime, the Supreme Court's decision in this case is instructive when analyzing whether ERISA preempts certain state laws regulating PBMs.

BACKGROUND

PBMs act as intermediaries between pharmacies and prescription drug plans. In addition to providing other administrative services, PBMs negotiate the rates at which pharmacies are reimbursed for the prescriptions the pharmacy fills for prescription drug plan members, through PBM-established maximum allowable cost ("MAC") lists. Some pharmacies, especially small, independent and rural pharmacies, have challenged the PBM reimbursement methodology, as the reimbursement a pharmacy receives from a PBM for a particular drug can sometimes be lower than the pharmacy's cost (i.e., what was paid to purchase the drug from a wholesaler).

In 2015, the Arkansas legislature passed Act 900, which sought to address the concerns of Arkansas pharmacies by regulating certain PBM reimbursement practices within the state. In a nutshell, Act 900 requires PBMs to reimburse Arkansas pharmacies at a price equal to or higher than the price a pharmacy paid to buy the drug from a wholesaler. Specifically, Act 900 requires:

1. PBMs operating in Arkansas to timely update their MAC lists whenever a drug wholesaler increases the price of a drug, so as to ensure that pharmacies are being reimbursed at or above the wholesale cost.
2. PBMs to create an administrative appellate procedure whereby pharmacies can challenge MAC reimbursement rates that are below the pharmacy acquisition cost. If a pharmacy can prove that it could not have acquired the drug from a wholesaler at a lower price, the PBM must increase its reimbursement rate to, at a minimum, cover the pharmacy acquisition cost.
3. PBMs to permit pharmacies to decline to fill prescriptions for plan beneficiaries if the PBM reimbursement rate is less than the pharmacy's acquisition cost.

CASE HISTORY

Act 900, like other similar state laws, was immediately challenged by Pharmaceutical Care Management Association ("PCMA"), a professional PBM association that represents the 11 largest PBMs in the country, on the basis of ERISA preemption. In brief, under 29 U.S.C. §1144(a), ERISA expressly preempts any and all state laws insofar as they relate to an employee benefit plan that is subject to ERISA (an "ERISA plan"), such as self-funded health plans offered by employers. However, the scope of ERISA preemption is not unlimited, and history has shown that the boundaries can be challenging to determine. Generally, a state law that has indirect impact on the benefits provided by an ERISA plan or the administration thereof has been sufficient to support ERISA preemption in past Supreme Court decisions, while laws that only have economic effects have not been preempted. Since PBMs are frequently utilized by ERISA plans to administer prescription drug benefits, PBMs have historically argued that PBM operations are closely tethered to ERISA plans to support ERISA preemption of state laws that look to regulate how PBMs operate.

In *Rutledge v. Pharmaceutical Care Management Association*, PCMA contended that Act 900 has "an impermissible connection with an ERISA plan because its enforcement mechanisms both directly affect central matters of plan administration and interfere with nationally uniform plan administration." PCMA further detailed how, if Act 900 were to go into effect, it would create operational inefficiencies with PBMs and ERISA plans, that would result in increased costs and potentially decreased benefits to ERISA plan beneficiaries. The Eighth Circuit Court

sided with PCMA, holding that Act 900 was preempted by ERISA. The Attorney General of Arkansas appealed the case to the Supreme Court.

THE SUPREME COURT'S DECISION

The Supreme Court unanimously overturned the Eighth Circuit's decision, holding that Act 900 is not preempted by ERISA. Specifically, the Court found that Act 900 does not relate to an ERISA plan because it (1) does not have an impermissible connection with an ERISA plan, and (2) does not "refer to" ERISA.

The Supreme Court noted that "not every state law that affects an ERISA plan or causes some disuniformity in plan administration has an impermissible connection with an ERISA plan." The Supreme Court also reasoned that Act 900 is not connected with an ERISA plan because it does not govern central matters of plan administration or interfere with nationally uniform plan administration. The Supreme Court explained that Act 900 is merely a form of cost regulation, and therefore does not dictate ERISA plan choices or administration. PCMA argued that Act 900 is connected with ERISA plans because Act 900 will inevitably lead to a pass-through of PBM costs to ERISA plans and such cost-shifting will ultimately require ERISA plans to potentially alter the administration of their plans and benefits offered. The Supreme Court refuted this argument by stating that, "PBMs may well pass those increased costs on to plans, meaning that ERISA plans may pay more for prescription drug benefits in Arkansas than in, say, Arizona. But cost uniformity was almost certainly not an object of preemption." (internal quotations omitted).

Next, the Supreme Court directly stated that Act 900 does not "refer to" ERISA. A law refers to ERISA if it "acts immediately and exclusively upon ERISA plans or where the existence of ERISA plans is essential to the law's operation." The Court noted that Act 900 applies to PBMs whether or not they manage an ERISA plan. Further, the Court stated that Act 900 will only affect ERISA plans in so much as PBMs pass along higher pharmacy rates to ERISA plans, which is not sufficient to preempt the law.

PRACTICAL TAKEAWAYS

The practical implications of this case extend well beyond Arkansas' regulation of PBMs. PBMs operating in all states should take notice of this legal development, as should pharmacies and health plans that contract with PBMs. Likewise, this decision could open the door for state cost regulation of other service providers for ERISA plans, including third-party administrators, in the future.

For years, PBMs have believed they were immune to state laws that attempted to interfere with their rate-setting because their rates were tethered to ERISA plans. This Supreme Court decision turns that longstanding idea on its head. Consequently, it is likely that this case will lead to an uptick in new state legislation affecting PBMs' negotiated rates and other aspects of the PBM/pharmacy relationship. In light of this decision, we recommend that PBMs and pharmacies with operations in Arkansas ensure that their contracts and operations are structured to comply with Act 900. More broadly, all PBMs, pharmacies and health plans should consider the Supreme Court's decision in this case when analyzing whether ERISA preempts current and future state laws regulating PBMs.

If you have any questions on the Supreme Court's decision in this case and its potential implication on your operations, please contact:

- **Julie Lappas** at (317) 977-1490 or jlappas@hallrender.com;
- **Calvin Chambers** at (317) 977-1459 or cchambers@hallrender.com;
- **Matt Reed** at (317) 429-3609 or mreed@hallrender.com; or
- Your primary Hall Render contact.

Hall Render blog posts and articles are intended for informational purposes only. For ethical reasons, Hall Render attorneys cannot—outside of an attorney-client relationship—answer specific questions that would be legal advice.