Weekly Checkup

Price Controls Can't Control Drug Prices

JOHN WALKER | JULY 12, 2024

Earlier this week, the Senate Health, Education, Labor, and Pensions Committee hosted a hearing entitled "Everyday Expenses and Everyday Americans: How High Costs Impact Children and Families." The committee did indeed discuss the problem of rising prices but, rather than address their actual causes, largely opted instead to credit corporate greed. High prices are a problem that has long afflicted the health care industry, of course. Roughly half of U.S. adults say it is difficult to afford health care costs and 21 percent report to have forgone prescription medications for over-the-counter alternatives. While it's easy, not to mention popular, for Congress to lay blame at the foot of the pharmaceutical industry, which generated roughly $364 billion in revenue in 2022, **lawmakers would be wise to shift their focus to correcting policies that would actually assist in reducing drug prices: taking another look at the dysfunctional price controls in both the Inflation Reduction Act (IRA) and 340B Drug Pricing Program.**

Packaged among a host of clean energy tax credits, the IRA authorized the secretary of the Department of Health and Human Services (HHS) to "negotiate" a select number of prescription drug prices directly with participating manufacturers on behalf of Medicare. As explained at length in previous American Action Forum insights and Weekly Checkups, **this "negotiation" labeling is deceptive.** In practice, HHS was tasked with implementing the well-worn and crude federal tool of price controls, along with a 95 percent tax on all non-compliant manufacturers and announcing it would bar any manufacturers from selling to Medicare should they refuse to comply with its negotiations. In crafting the health care provisions of the IRA, lawmakers were of course addressing the very real problem of high health care prices. But **as with other finite goods, there are only two ways to lower costs: increase supply or reduce demand. Because the former would require real political solutions and the latter would be**

dimwitted, lawmakers reached for the blunt instrument of simply capping prices. So, while Medicare will face drastically lower drug prices, it will come at the cost of driving up those costs for private insurers, employers, and uninsured patients at the pharmacy counter, as well as hampering future drug innovation.

The 340B Drug Pricing Program (340B), too, relies on the use of ham-fisted price controls. While 340B was intended to provide better access to quality care at a reduced cost for patients and the federal government, the program has become a federally mandated revenue stream for covered entities such as hospitals and for-profit pharmacies. **What's important to understand about 340B is that it establishes manufacturer ceiling prices that cap the total amount a manufacturer can charge a covered entity for a drug.** The covered entity is then supposed to pass these lower prices on to patients or sell the drug at market prices and use the additional funds to improve patient services. **Yet there remains little to no oversight or transparency to ensure that covered entities do so (and even if there were, there is no statutory language requiring as much).** As shown by an analysis published in the New England Journal of Medicine and a study in the Journal of the American Medical Association, there is scant evidence to support that these funds are re-invested appropriately or that they serve vulnerable communities. Some evidence also suggests that 340B's structure incentivizes covered entities to sell drugs at prices higher than set by the manufacture ceiling, putting upward pressure on launch prices. Here again, **faced with the cold, hard reality of supply and demand, lawmakers apparently chose the politically convenient but economically ineffective option.** Perhaps more concerning, even with its apparent faults, the 340B Program continues to grow at unmanageable rates and is on track to eventually surpass Medicare Part D spending, becoming the largest federal prescription drug program.

There are indeed a few ways for lawmakers to lower health care costs. The best route, of course, is to raise supply – something that can be accomplished by, for example, lowering regulatory barriers to entry or expansion. **We may be a long way from arriving at that conclusion and, in the meantime, it seems we're left with price controls – which ramp up demand without increasing supply, all while reducing drug innovation.**