The Daily Dish

CBO on Pelosi and Drugs

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Eakinomics: CBO on Pelosi and Drugs

Friday the Congressional Budget Office (CBO) released "Effects of Drug Price Negotiation Stemming From Title 1 of H.R. 3, the Lower Drug Costs Now Act of 2019, on Spending and Revenues Related to Part D of Medicare" — CBO is ruthless about hooking you with pithy titles — its take on the implications of the Pelosi bill on drug prices. Specifically, it is a preliminary analysis focused on the requirement that manufacturers negotiate prices with the Secretary of Health and Human Services, subject to the limitation that the price cannot exceed 120 percent of the average price in other developed countries. The incentive to negotiate is that if a manufacturer does not, it will be subject to an excise tax of up to 95 percent of the sales receipts. The tax is non-deductible, so the total tax rate will be over 100 percent.

Now, if you do a little price-fixing (120 percent of the international average) followed by a little extortion (negotiate or face a confiscatory tax), you can save some money. CBO estimates that the savings to Medicare Part D will be $345 billion, roughly 25 percent. But it is easy to save budget dollars — just don't pay for things. The real impacts are what happens to the industry when these prices are applied across the board (Medicare, Medicaid, commercial insurance, etc.). As the CBO dryly puts it: "The lower prices under the bill would immediately lower current and expected future revenues for drug manufacturers, change manufacturers' incentives, and have broad effects on the drug market."

Indeed, the real concern is the impact on innovation and the quality of therapies in the United States: "In the short term, lower prices would increase use of drugs and improve people's health. In the longer term, CBO estimates that the reduction in manufacturers' revenues from title I would result in lower spending on research and development and thus reduce the introduction of new drugs." The short-run impact is often overlooked, and the long-run impact is at the center of the concern.

CBO notes that: "CBO's analysis of the bill is not complete; its preliminary estimate is that a reduction in revenues of $0.5 trillion to $1 trillion would lead to a reduction of approximately 8 to 15 new drugs coming to market over the next 10 years. (The Food and Drug Administration approves, on average, about 30 new drugs annually, suggesting that about 300 drugs might be approved over the next 10 years.) The overall effect on the health of families in the United States that would stem from increased use of prescription drugs but decreased availability of new drugs is unclear."

Losing roughly 5 percent of innovative drugs is nothing to sneeze at, but I think this is the tip of the iceberg. The real issue is that the drug industry would be much, much less attractive as a location for risk capital, so that the lost revenues is the lower bound for the loss of innovation finance.

Title 1 of H.R. 3 is a bad idea. Period. But the concern is that people will conclude it is not *too* bad.