The Daily Dish

Developments in Proposed Part D Reform

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Eakinomics: Developments in Proposed Part D Reform

Reforms to reduce the cost — or slow the growth of the cost — of prescription drugs are at the top of the agenda at the White House and in Congress. Among them are potential reforms to the Medicare prescription drug program, or Part D. Ideas in the mix include the proposal by AAF's Tara O'Neill Hayes, the heart of which is three changes. The first is to institute an absolute maximum that any beneficiary will pay for Part D drugs. The second is to improve incentives by changing the *way* (not the amount) that the pharmaceutical industry pays in the program. Specifically, its contribution would be concentrated above the catastrophic maximum to reduce the incentive to produce high-cost drugs that push beneficiaries into the catastrophic region. Finally, the prescription drug plans would pick up a greater fraction of the catastrophic costs to improve their incentives to negotiate strongly for lower cost drugs.

Now variations on the theme are beginning to appear, and Hayes has a nice discussion of the tradeoffs involved in three areas:

- Setting the out-of-pocket (OOP) cap lower is good for more high-cost beneficiaries, but would mean higher premiums;
- Forcing drug manufacturers to pay only in the catastrophic region sharpens incentives, but helps a limited number of beneficiaries — there may be pressures to provide help more broadly;
- The legislative reform could be done at the same time as the proposed "rebate rule"; this could lead to even higher premium increases and interacts with setting the OOP cap.

The substantial focus on the impact on premiums reflects accepted political wisdom, but I think is misdirected in two ways. First, the whole goal is to change the pace of drug price growth. Since premiums are set to cover the cost of drugs, sharp incentives are a way to lower premiums overall — this needs to be taken into account. Second, a monomaniacal focus on keeping premiums down can lead to real policy errors. After all, if the insurance doesn't cover anything, the premium will be zero. Pressure to keep premiums down can lead to high deductibles, high co-insurance, and large amounts of out-of-pocket expenses. Is that really a good idea?

The are also recent press reports of Senators contemplating an inflation penalty in Part D. Specifically, manufacturers would be obliged to pay an additional rebate (i.e., tax) if a drug's price rises faster than the rate of inflation. The problem is that I have no idea what that means in Part D. The essence of Part D is negotiation between plans and manufacturers. The essence of the reform is to sharpen the incentives for strong negotiations. If the negotiated price is above some target (say inflation), why not blame the plans for poor negotiation and make them pay? More generally, an inflation-based rebate/tax is a form of government price-setting that is the antithesis of the foundations of the program.

Reform is a real opportunity to address drug prices. But there will be a lot of tough choices on the road to any finished legislation.