Prescription Drug Pricing

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On Monday the Supreme Court sent a request to the Justice Department asking for their input on New Mexico's lawsuit against Colorado for a mine waste spill in 2015. The request comes as the Supreme Court considers taking up the case. Acting Solicitor General Ian Gershengorn is unlikely to be able to fulfill the Supreme Court's request in the final days of the Obama Administration so it is likely the responsibility will fall to whomever President-elect Trump chooses as his solicitor general. While the Environmental Protection Agency (EPA) has taken the blame for the spill, New Mexico argues Colorado shares the blame as their state officials were involved in the planning of the operation which led to the toxic spill.

Last week the Obama Administration published $174 million in regulatory burdens, with $159 million in annual costs. Additionally, 44 new rules were proposed and there were 85 new final rules released bringing the total regulatory burden costs for 2016 to $153.1 billion in final rules and an additional $47 billion in proposed rules. According to a calculation from the Congressional Research Service, all regulations submitted to Congress or published (whichever is later) after May 30, 2016 will be subject to the Congressional Review Act's disapproval process next year.

Eakinomics: Prescription Drug Pricing

The rollout and cost of new drugs like Sovaldi, the pricing revelations at Turing Pharmaceuticals, and the Epipen episode have fed two related phenomena: a) concerns about drug pricing and b) problematic proposals to address these worries. Seventy five percent of Americans say they want more government action on drug prices, but to my eye we simply have not witnessed the sort of fundamental market failure that would justify proposals for aggressive government intervention.

The first important fact to consider is that, with a few exceptions, prescription drug price growth is no faster than that of inflation (just under two percent). In fact, prescription drug spending as a percent of National Health Expenditures has remained steady at about 10 percent since the 1960s. Unfortunately, burdensome restrictions on insurance plans mandated by the Affordable Care Act (ACA) give insurers incentives to limit the drugs they cover and increase the patients' share of the price. This means that patients pay more money for more drugs more often, even though the actual sale price of most drugs has increased relatively little.

Consider the contrast between the ACA and the most successful entitlement program: the Medicare Part D prescription drug program. In the latter private drug plans and pharmacy benefit managers (PBMs) compete to achieve lower costs, promote use of generics, use formularies to promote more affordable brand options, and offer other beneficiary-friendly and cost-savings tools. This – the power of effective private sector negotiation and competition – is why the Medicare prescription drug plan has come in well below its original projected cost and still receives beneficiary satisfaction ratings of 85 percent or more. It is also why calls for the government to "negotiate" drug prices are misguided. Genuine government negotiation would have no real impact. PBMs and private plans can use a formulary to reward low-priced drugs, while the government cannot. In effect, the private sector already has all the market-based leverage available.

That doesn't mean that inventive politicians can't think of ways to make things worse, ranging from calls for "transparency" in those private negotiations (the Congressional Budget Office (CBO) concluded this would raise the overall cost of the program) to Medicaid-style rebates in Part D. Imposing rebates in Part D could of course result in higher prices, since the cost of a mandated rebate would have to come from somewhere. The most dramatic thing the government could do is to impose price controls.

There is no need to turn to price setting schemes. Instead, it is instructive to recall that the moment Sovaldi faced competition from new entrants, the drug's price dropped precipitously. The key to good public policy is to continue to harness the effectiveness of private negotiation and competition among manufacturers, drug plans, PBMs, and employers.