Would Price Transparency for Retail Generic Drugs Lower Costs?

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Overview of Paper: Retail Generic Drugs

- 4 billion generic prescriptions = $100 billion (2016)
  - Average reimbursement: $26 (Rx cost: < $1/3; Pharmacy: > $2/3)

- Generic manufacturer rebates flow to pharmacies

- Published prices ≠ actual net ingredient costs
  - Exclude rebates to pharmacies

- PBM's have dual—and conflicting—roles
  - As contracted agent of plans, negotiate pharmacy reimbursement
  - As mail order pharmacies, profit from high generic reimbursement

- Proposal: tell plans average actual generic costs
  - CMS collects data; limited disclosure to plans
  - Likely to lead to lower payment rates by plans
  - Every $1 (4%) reduction in average generic reimbursement saves $4 billion
Background: Current Retail Drug Market

• Growth of generic drugs
  – 89% of all prescriptions with 98% generic substitution

• Changes in pharmacy market
  – Shift to narrow networks of preferred pharmacies (Medicare Part D)
  – Advent of “$4 generics” (Walmart) vs $11 estimated dispensing cost
  – Other changes (e.g. growth of specialty drugs)

• Pharmacies contract with wholesalers
  – Wholesalers negotiate pharmacy rebates for generic drugs

• Plans contract with PBMs for:
  – Pharmacy network, claims payment, formulary & cost sharing
  – Negotiating pharmacy reimbursement
Background: Current Retail Drug Market

• Drug distribution is complex and not transparent
  – System of manufacturers, wholesalers, plans, PBMs and pharmacies
  – Net price paid by pharmacies (generics) & plans (Brands) unknown

• AWP and WAC: markedly overstated list prices
  – NADAC overstates actual prices: excludes rebates; fatally flawed
  – Medicare ASP: aggregated average prices only for Part B drugs
  – AMP: confidential, trade secret generic and brand prices (all rebates)

• Prescription drugs differ from standard markets
  – Consumer choice strictly limited by physician prescribing
  – Formularies and differential cost sharing (tiers) steer patient choice
  – Actual cost (prices) masked from patients:
    • Third parties (plans) pay most of total reimbursement
    • Same cost sharing at network pharmacies even if plan cost differs
## Background: Drug Price Measures

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<tr>
<th>List or Net Price</th>
<th>Average Wholesale Price (AWP)</th>
<th>Wholesale Acquisition Cost (WAC)</th>
<th>National Average Drug Acquisition Cost (NADAC)</th>
<th>Average Sales Price (ASP)</th>
<th>Average Manufacturer Price (AMP)</th>
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Background: Current Retail Drug Market

• Markets for generic and brand drugs differ sharply

<table>
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<tr>
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<th># of Prescriptions</th>
<th>% of Total Prescriptions</th>
<th>% of Total Spending</th>
<th>Average Cost</th>
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<tbody>
<tr>
<td>Generics</td>
<td>4.0 billion</td>
<td>89 %</td>
<td>27 %</td>
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<tr>
<td>Brands</td>
<td>0.5 billion</td>
<td>11 %</td>
<td>73 %</td>
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• Generic rebates lower pharmacy drug cost; brand rebates lower plan drug cost
• WAC (published list price) excludes rebates
  – Brand drugs: pharmacy actual ingredient cost ~ WAC
  – Generic drugs: pharmacy actual ingredient cost ~ WAC-70%
• Plans mainly pay pharmacies based on WAC or AWP
  – Generic reimbursement: pharmacy retains >2/3; drug costs < 1/3
  – Brand reimbursement: pharmacy retains~5%; drugs~95%
• Pharmacy profits greater on generics than brands
Proposal: Tell Plans Average Generic Costs

• Require wholesalers to report to CMS net prices paid by retail pharmacies for 11-digit NDCs
  – Make condition of wholesaler licensing (P.L. 113-54)
  – Leverage sophisticated wholesaler IT systems

• CMS to collect, aggregate, and de-identify information
  – Averages reported at ingredient/dosage/strength/route of admin
  – HHS Secretary would issue necessary regulations
  – Participating plans finance through user fees

• Restrict disclosure only to participating plans
  – Averages confidential “trade secrets” (similar to Medicaid AMPs)
  – Report biweekly
  – Options to increase/decrease transparency of reported averages
PBM’s Role and Asymmetric Information

• PBM’s determine what plans pay to pharmacies
• PBM’s also operate large mail order pharmacies
• Does dual role of PBM’s cause conflict of interest?
  – Do PBM’s link payment for mail order generics to retail payment?
• Does information asymmetry increase plan cost?
  – PBM’s know cost of generic drugs—unlike (most) plans
  – PBM’s profit from high generic reimbursement
• Risk from selectively increasing transparency?
  – What is downside if plans already know generic ingredient cost?
Effects of Limited Generic Cost Disclosure

• Knowing seller’s cost structure may assist buyer in consolidated markets
  – Little economic research to inform analysis
  – 3 examples of positive effects of increased price transparency: collective bargaining, auto buying, and hospitals purchasing stents

• Price reporting would inform plans—but not PBMs

• Risks of higher prices to manufacturers can be limited
  – Disclose only national averages
  – Can increase/decrease transparency by adjusting policy “dials”
  – Pursue demonstrations with selected drugs with multiple competing manufacturers
Conclusion

• Complexity, information asymmetry, and role of PBMs appear to overpay pharmacies for generic drugs
  – 4% ($1) reduction in average generic drug reimbursement saves $4BN

• Reporting actual average prices would inform plans
  – Would informed plans negotiate lower pharmacy reimbursement?
  – If yes, purchasers and patients would pay lower prices
    • PBM profits and pharmacy retention would fall

• Proposal to collect, aggregate, and report data
  – Averages strictly confidential and could not be re-identified

• Analysis suggests selective reporting would not impair manufacturer competition or facilitate price collusion