

# **Would Price Transparency for Retail Generic Drugs Lower Costs?**

Steven M. Lieberman and Paul B. Ginsburg

Center for Health Policy  
The Brookings Institution

June 14, 2017

# Table of Contents

**Overview**

**Background**

**Proposal: Tell Plans Average Net Generic Costs**

**PBM's Role and Information Asymmetry**

**Effects of Limited Generic Cost Disclosure**

**Conclusion**

# Overview of Paper: Retail Generic Drugs

- 4 billion generic prescriptions = \$100 billion (2016)
  - Average reimbursement: \$26 (Rx cost:  $< \frac{1}{3}$ ; Pharmacy:  $> \frac{2}{3}$ )
- Generic manufacturer rebates flow to pharmacies
- Published prices  $\neq$  actual net ingredient costs
  - Exclude rebates to pharmacies
- PBMs 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

	<b>Average Wholesale Price (AWP)</b>	<b>Wholesale Acquisition Cost (WAC)</b>	<b>National Average Drug Acquisition Cost (NADAC)</b>	<b>Average Sales Price (ASP)</b>	<b>Average Manufacturer Price (AMP)</b>
<b>List or Net Price</b>	List	List	Hybrid	Net	Net
<b>Confidential or Public</b>	Public	Public	Public	Public	Confidential
<b>Discounts or Rebates Included</b>	Excluded	Excluded	Off-Invoice/ Transfer Pricing Excluded	Included	Included

# Background: Current Retail Drug Market

- Markets for generic and brand drugs differ sharply

	# of Prescriptions	% of Total Prescriptions	% of Total Spending	Average Cost
Generics	4.0 billion	89 %	27 %	\$26
Brands	0.5 billion	11 %	73 %	\$308

- 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

- PBMs determine what plans pay to pharmacies
- PBMs also operate large mail order pharmacies
- Does dual role of PBMs cause conflict of interest?
  - Do PBMs link payment for mail order generics to retail payment?
- Does information asymmetry increase plan cost?
  - PBMs know cost of generic drugs—unlike (most) plans
  - PBMs 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