

The Shape of a Prescription Drug Peace Treaty

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The easiest problem to solve

- Health costs are again rising rapidly
- Hospitals continue to close; surviving hospitals can't find enough nurses
- Insurance premiums are skyrocketing
- Long-term care crises loom
- And prescription drugs are increasingly unaffordable-- Why is this the easiest problem to solve?

Overview

Problems

Causes

Today's solutions

Possible futures

A peace treaty

Problems

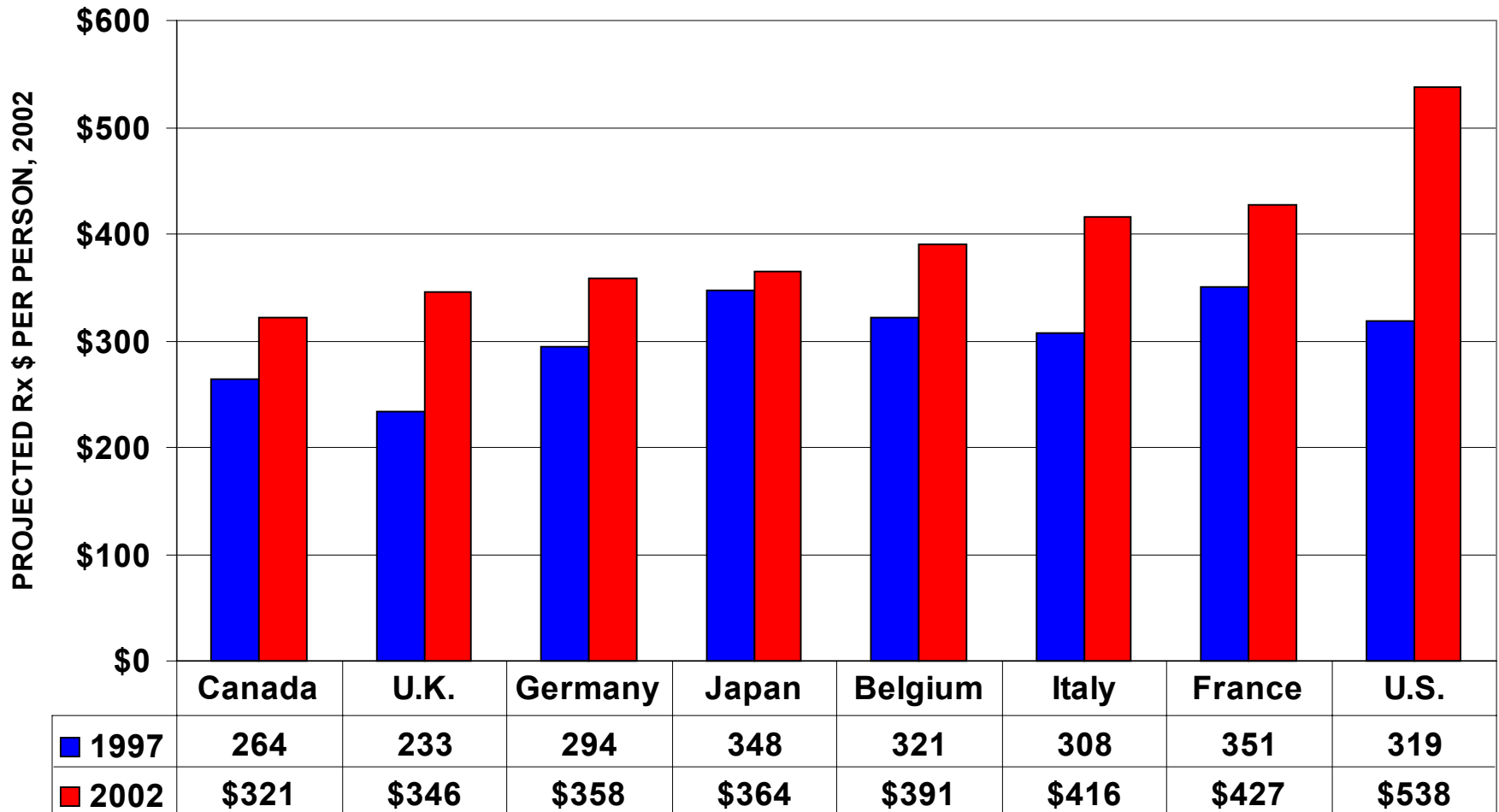
Spending

Prices

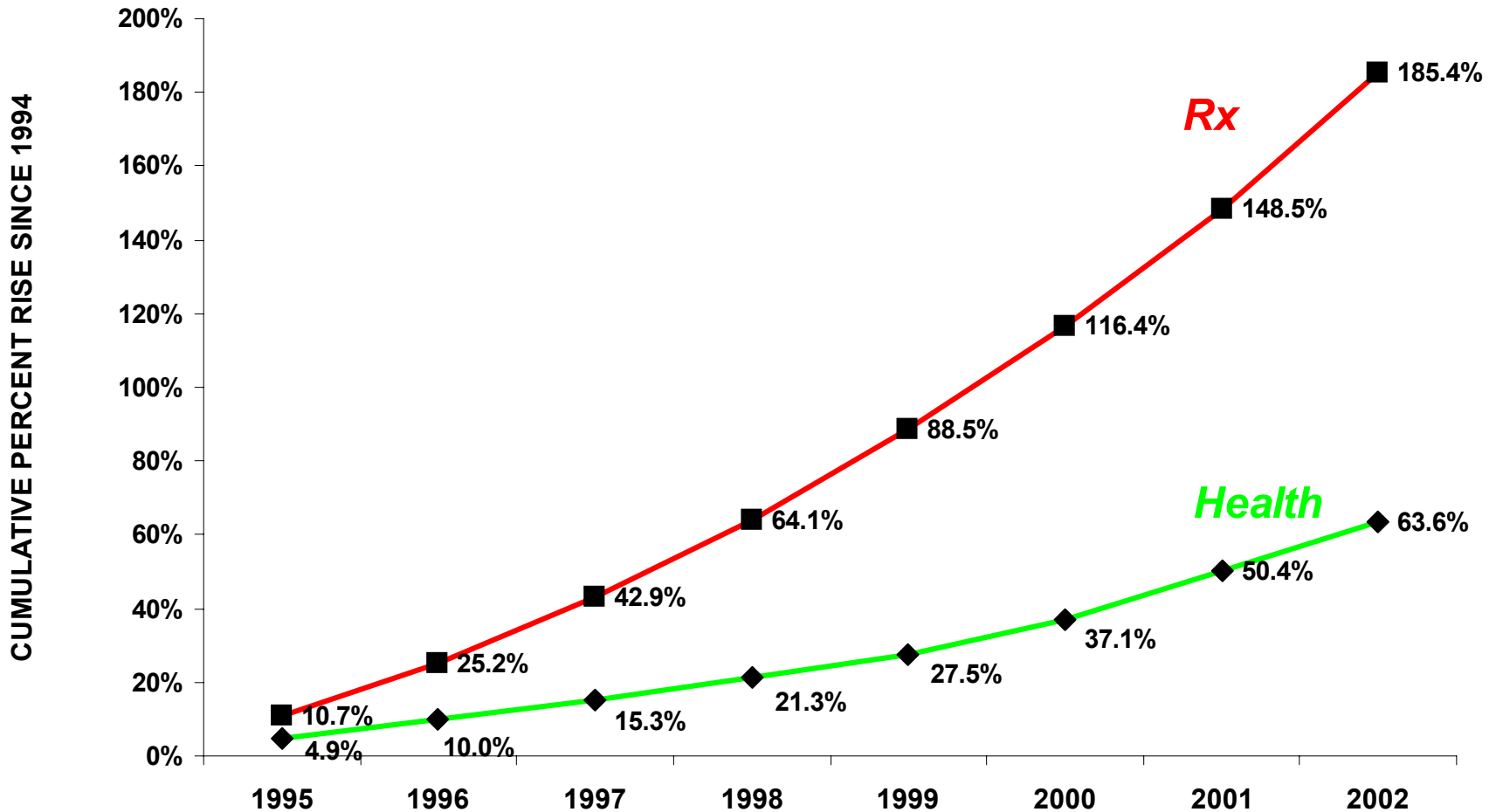
Waste

Suffering

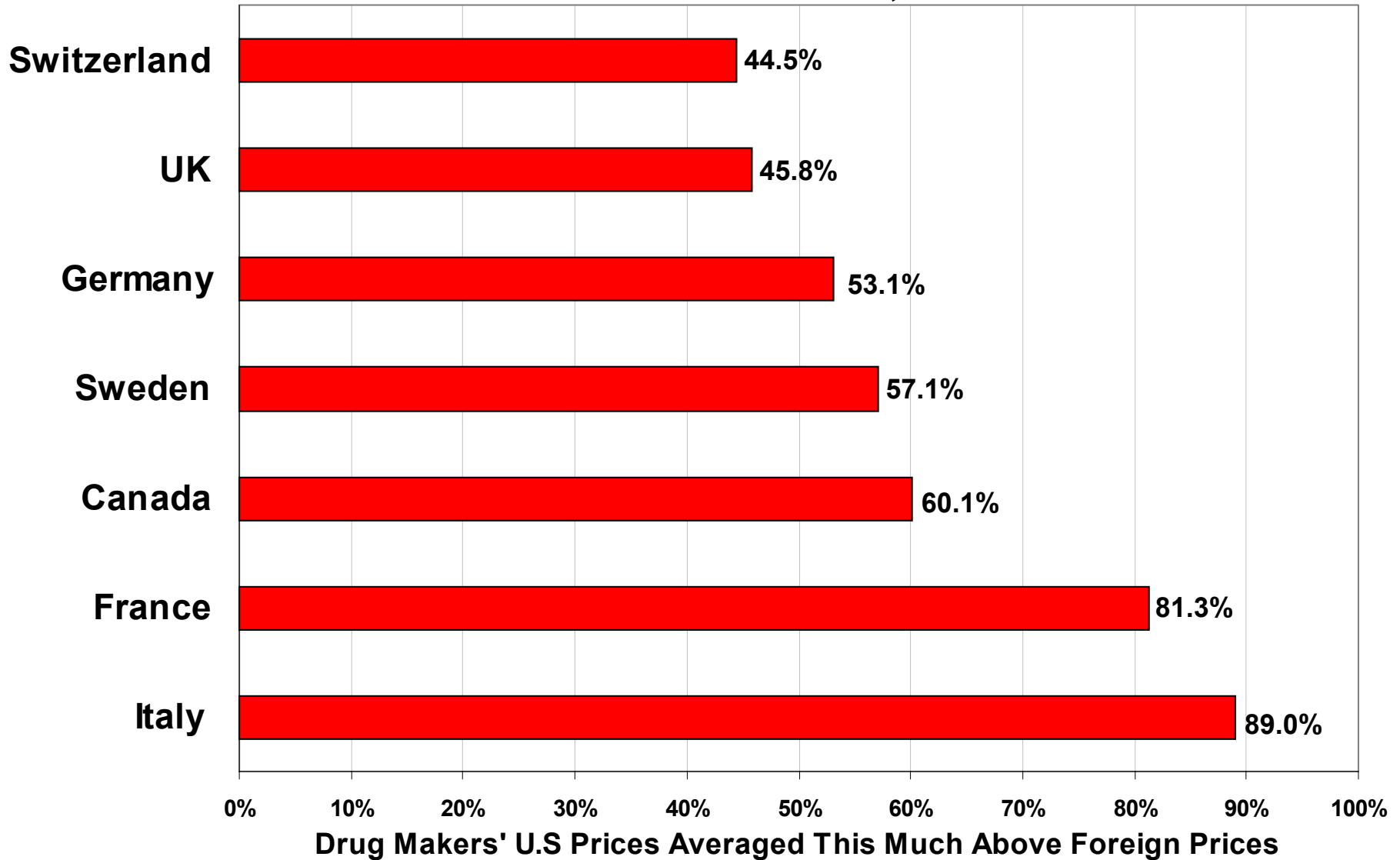
PRESCRIPTION DRUG SPENDING PER PERSON, 1997 + 2002 (projected)



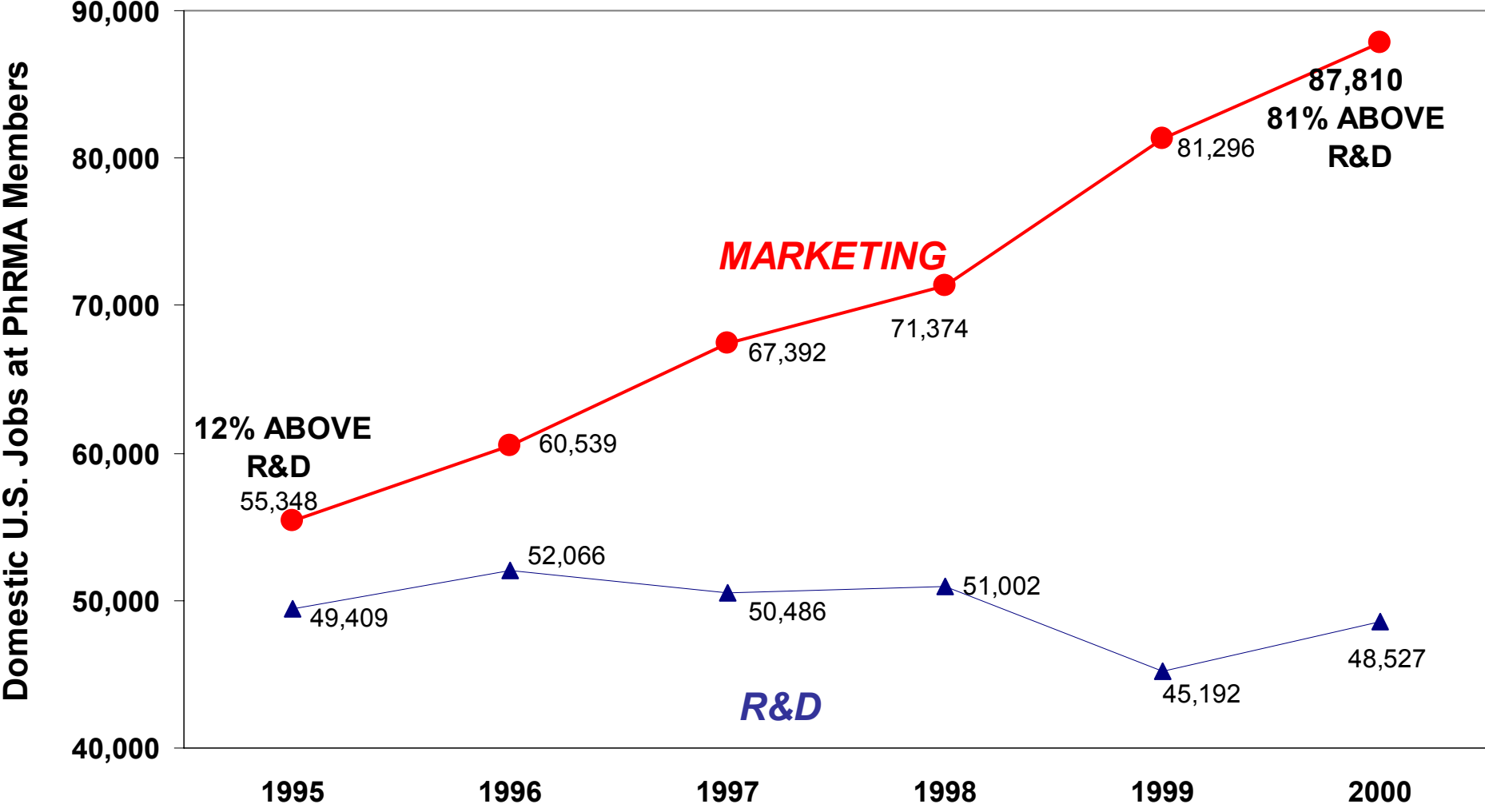
CUMULATIVE RISE IN RETAIL Rx + TOTAL HEALTH SPENDING, 1994 - 2002



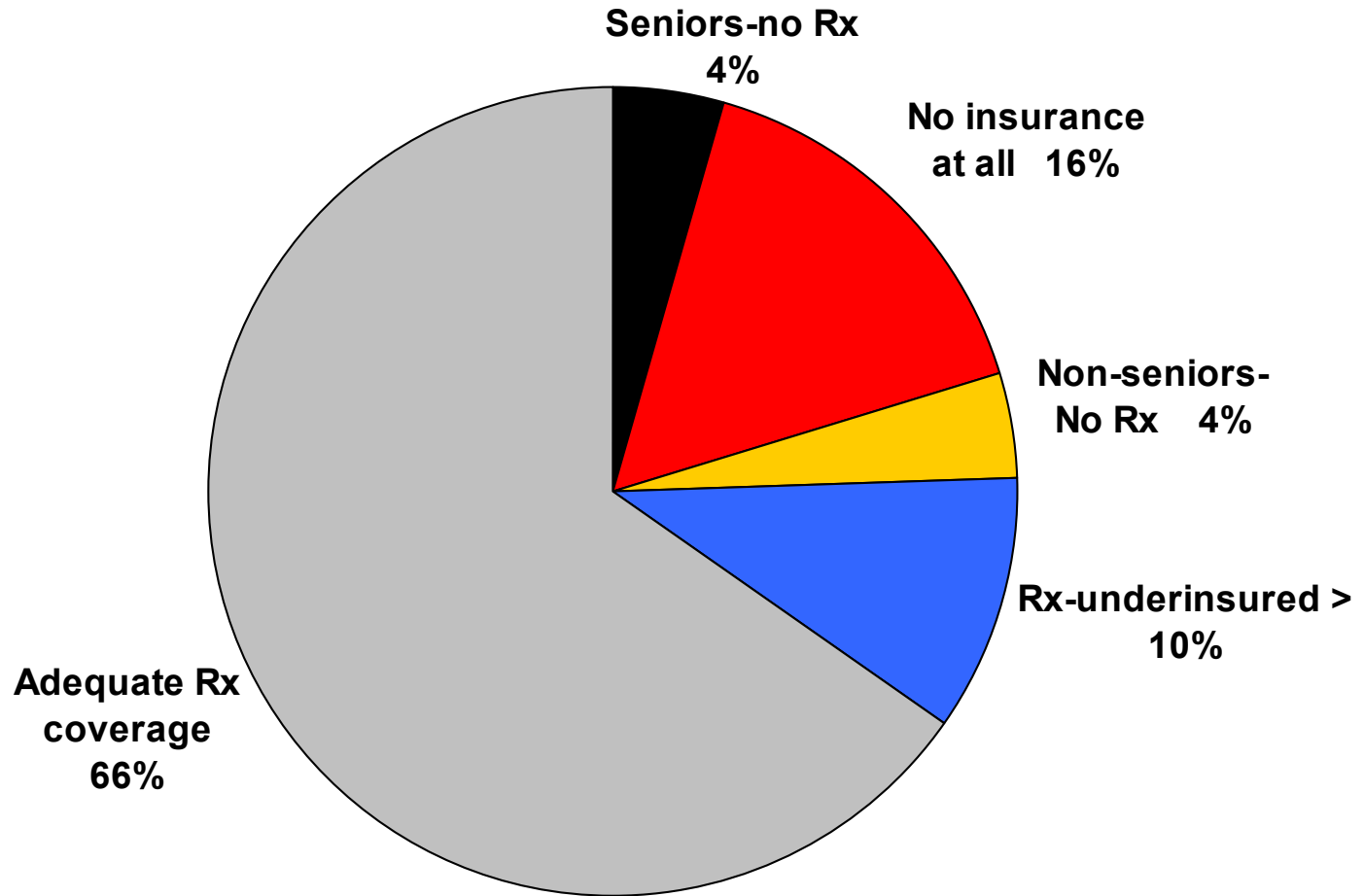
U.S. EXCESS ABOVE 7 NATIONS' FACTORY DRUG PRICES, 2000



BRAND NAME DRUG MAKERS' MARKETING AND R&D JOBS, 1995 - 2000



98 MILLION LACKED PRESCRIPTION DRUG FINANCIAL SECURITY IN 2000



Three choices

- **Continued suffering** and dying for lack of needed drugs. Intolerable.
- **Paying much more** public and private money for needed drugs. Unaffordable.
- **Changing our ways**, to secure needed drugs at small additional costs while rewarding innovation. Unavoidable.

Causes of High Spending and Prices

Government failure to contain prices,
resulting from

- industry pressures
- claims that research would suffer
- claims that free market justifies high prices
- belief in free lunch

Causes of waste

- Weak evidence on who needs which Rx
- Is marketing more secure than innovating?
- Copy-cat drug research: better to steal an idea? (attributed to Jack Welch)
- Oligopoly means lack of free market discipline

Causes of Suffering

- Stunted empathy
- “High prices are essential to innovation.”
- Inertia
- Lack of imagination
- The difficulty of crafting something better
- Loss of retiree and HMO Rx coverage
- High Rx prices make better coverage too costly

Solutions that enjoy good political currency today

To lower prices or spending

To expand coverage

To lower prices or spending

- PBMs
- formularies
- counter-detailing
- drug discount cards
- greater use of generics
- importing from Canada/Mexico
- de-insure patients--make them pay more
- fragmented public and private demands for discounts

Today's solutions to high prices/spending

- Probably won't work
- If they do work, and therefore cut drug use and spending, they may well cut dollars drug makers say are needed to finance research

To expand coverage

- “Reform Medicare,” enroll elders in competing HMOs, and let those HMOs worry about Rx coverage
- legislate Medicare Rx benefit without substantial price controls

Today's ways to expand coverage

- Neither likely to be enacted
- Neither likely to work if enacted
- Medicare HMOs hard to save
- Medicare Rx without lower prices = high premiums and subsidies but low benefits
- Ten-year federal cost of modest plan:
 - \$118 B in June 1999
 - \$318 B in June 2001
 - \$500 B+ in spring 2002

Possible futures and probabilities

- More money for business as usual 5%
- More co-pays, formularies to cut use 20%
- Costly coverage improvements,
leading to pressure to cut prices 20%
- Radical new Congress guts prices 20%
- Other 35%

Peace treaty aims

- **Short-run:** To finance and deliver all existing medications to all Americans who need them, at the lowest possible spending increase consonant with protecting manufacturers' research and profits
- **Long-run:** To increase financing of breakthrough research, cut waste, get right medications to the patients who need them

Why a peace treaty?

- ~ \$200 B for Rx in 2002 should be enough
- Protect patients, payors, and drug makers
- Marginal cost of medications is usually tiny
- Pre-empt windfall profits from higher use
- Pre-empt devastating price cuts
- Higher factory prices spur cuts in use
- Lower factory prices permit all needed use
- Total revenue = price * quantity (!)
- Need package deal to align lower prices with higher volume, to protect total revenue, profits, and research

Peace treaty provisions

1. Legislate Canadian-level factory prices for brand-name drugs, cutting manufacturers' revenues by ~ \$44 B in 2002
-- if do nothing else
2. Replace much or most of lost revenue through higher private market volume responding to lower prices (extent depends on price-elasticity of demand)

Peace treaty provisions

3. Provide the rest of the revenue needed to maintain pre-reform return on equity, for each drug maker, via publicly-subsidized purchases for people who can't afford even the newly-discounted private prices.

Peace treaty provisions

4. To maintain return on equity, publicly subsidized prices would be set to replace that share of the \$44 B in lost revenue not recouped privately (in step 2), plus the small marginal cost of new volume. The upper limit on revenue replacement would be that required to maintain return on equity, allowing for reasonable cost rises.

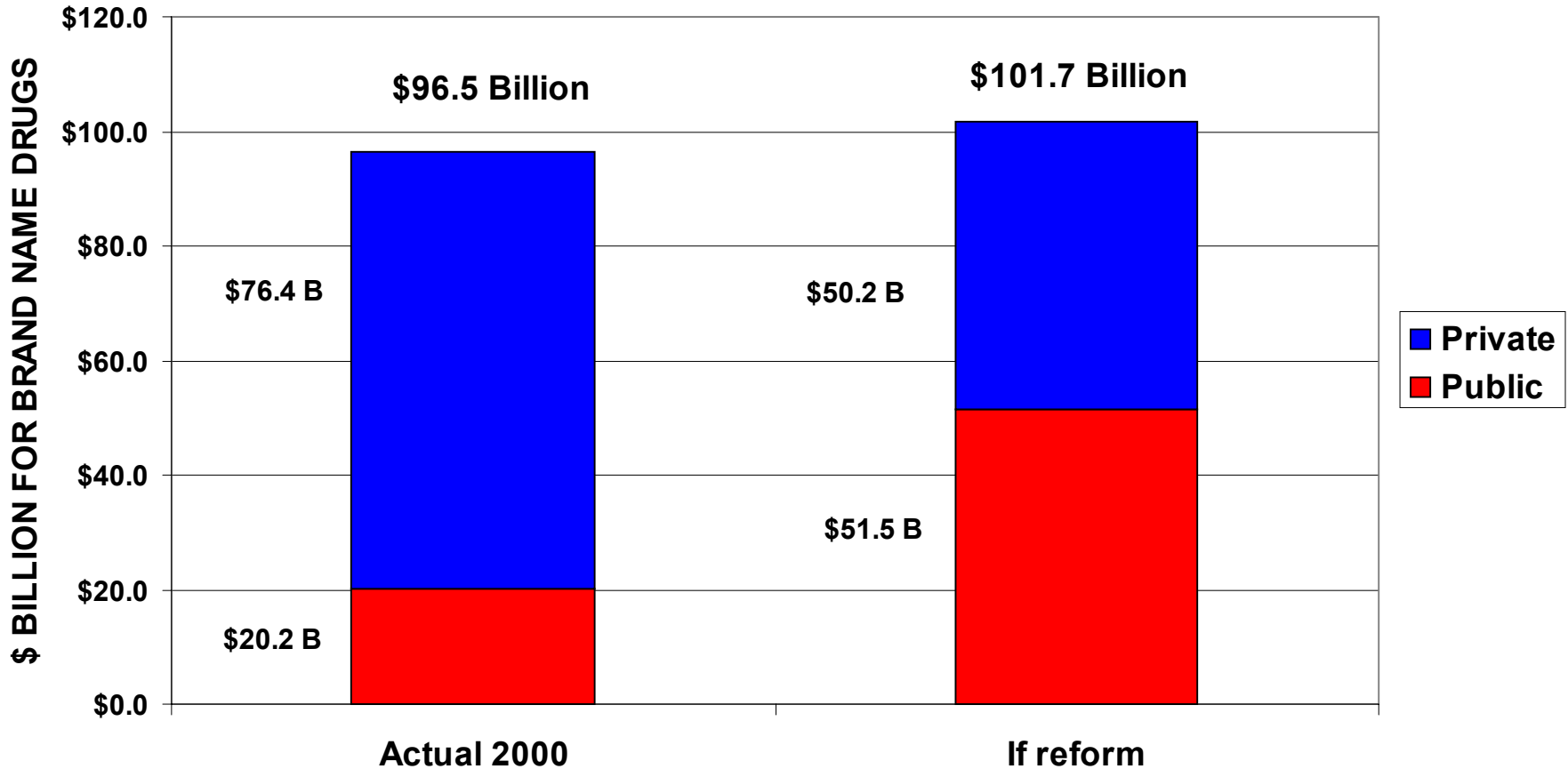
Strengths of short-run elements

- All needed prescriptions are filled
- Each manufacturer is financially whole: maintain returns on equity (though not on revenue) at pre-reform levels for, say, 5 years--for drugs available at outset
- Incremental cost to payors < \$10 B yearly
- Buys time to develop and disseminate data to guide better prescribing

Complications and problems

- Public share of Rx cost rises visibly and private share falls somewhat less
- Asymmetry between pain and gain: private parties who pay less may be less vocal than taxpayers who pay more
- Absent good clinical standards, lower prices and better coverage could lead to unnecessary use
- Possible risk to research

ILLUSTRATIVE PUBLIC AND PRIVATE Rx PAYMENTS, BEFORE AND AFTER REFORM, FACTORY PRICES



Dealing with Complications

- We can learn from other nations' regulatory experience, such as U.K.'s profit regulations
- Researchers will find gainful employment measuring marginal costs and needed revenue
- Building a trusting private-public partnership is key to peace treaty.

Dealing with Complications

- Competition and regulation are allies, not antagonists.
 - Competition and adequate financing will spur innovation.
 - Regulation to lower price and achieve universal coverage will sustain political and financial support.

Inevitable limitations of short-run peace treaty

- While peace treaty makes today's meds affordable for all,
- It does little to slow rise in drug spending
- It does little to squeeze out waste
- Alone, it may sustain today's level of innovation but does not spur greater innovation

Peace treaty provisions

long-run elements

1. Raising the money
2. Paying for medications
3. Identifying and rewarding good innovation
4. Financing research
5. Protecting competition
6. Ending marketing waste
7. identifying and promoting affordable drugs and prescribing patterns

Winning Durably Affordable Medications for All

- A peace treaty will be difficult to negotiate and implement
- But if more money for business as usual is unaffordable and unsustainable, what is the alternative?