NATIONAL CENTER FOR POLICY ANALYSIS

Proposed Drug Plan Legislation Could Hurt Oklahoma Consumers, Raise Costs

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An estimated 70 percent of Americans are enrolled in a prescription drug plan through their employer, health insurer or Medicare Part D. Millions more have joined discount drug card programs. When hundreds of thousands of Oklahomans enrolled in drug plans walk into their neighborhood drugstore, they receive discounted drug prices that have been negotiated on their behalf. However, uninsured consumers and those enrolled in health plans with insurance deductibles that have not been met must bear the cost of drug purchases out of their own pockets. Rising drug prices have prompted some ill-conceived legislative proposals that should raise some concerns — and could boost costs for Oklahomans.

Our Generic Drug Approvals. Over the past several years, there has been a surge in abbreviated new drug applications at the U.S. Food and Drug Administration from firms applying to produce generic drugs. The backlog of FDA applications grew to nearly 4,000 by mid-2015. The extensive backlog and resulting lengthy period to get competing drugs approved has allowed some generic drug makers to temporarily jack up their prices exorbitantly — often with little notice.

High drug costs are a problem that ultimately affects consumers and their drug plans, but can also impact drugstores by temporarily reducing profit margins on a few drugs. In an attempt to insulate their industry from the effects of rising wholesale drug prices, and boost profits, drugstores are lobbying Oklahoma lawmakers to allow pharmacies to ignore negotiated discounts and pass the price hikes on to consumers in violation of contractual agreements.

How Generic Drug Prices Are Set. The wholesale cost of generic drugs can vary tremendously from one manufacturer to the next, and one supplier to the next. Maximum allowable cost (MAC) price lists are a tool health plans, drug plans and discount card sponsors use to place an upper limit on how much they pay for a given drug. Pharmacies have agreed to abide by these terms; contracts are negotiated annually with drugstores, or with the Pharmacy Services Administrative Organization to which they belong. With no limits, pharmacies would have little reason to hold prices down because they could merely pass on higher costs to consumers.

An existing law in Oklahoma already requires weekly updates to MAC lists and allows pharmacies to contest MAC prices they feel are inaccurate or unfair. The existing law was passed because the drug store lobby argued that prices for a few generic drugs were rising faster than MAC lists were being updated. This is no longer an issue, now that the FDA has sped up its approval process and is working through its application backlog. As the figure shows, the average acquisition cost of generic drugs was about as likely to fall as it was to rise in the second quarter of 2015 (the latest period for which data is available).

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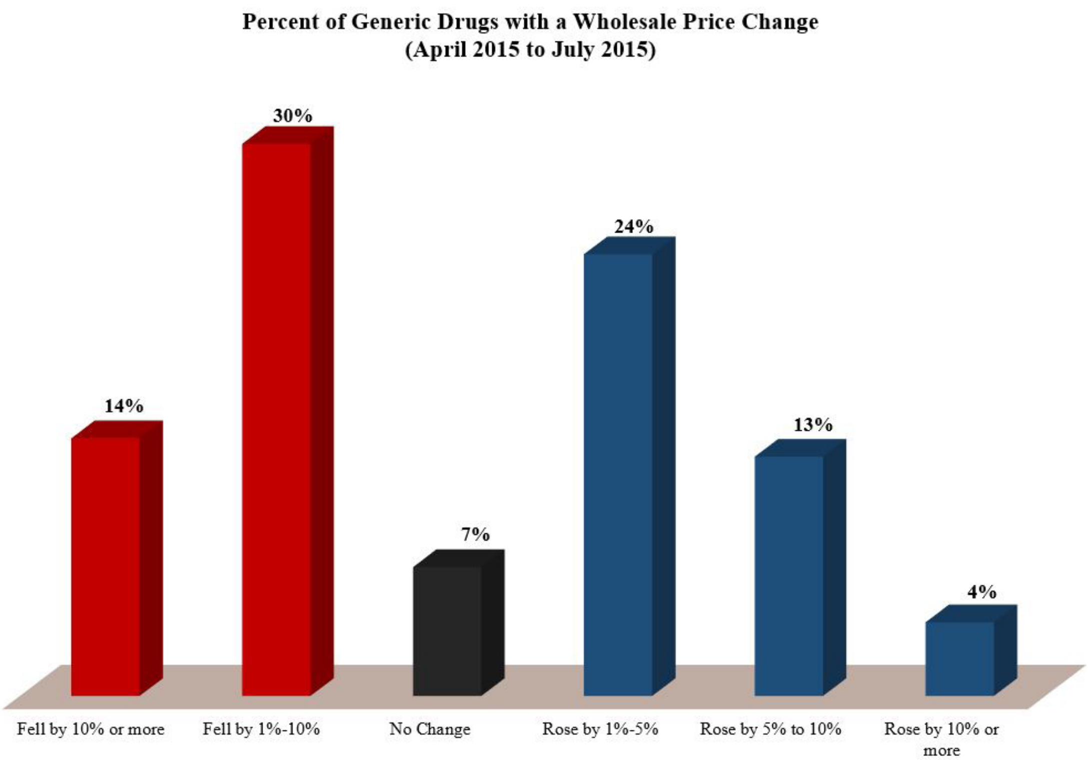

Source: Authors calculations using Pembroke Consulting's analysis of data files from Center for Medicare and Medicaid Services. For the original graphic see Adam Fein, "Generic Drugs, Change in NADAC per Unit, 2015:Q2 (April 2015 vs. July 2015)," Drug Channels Institute, August 25, 2015.

Arbitrarily Raising Prices. The Oklahoma Senate is now considering a proposal that amends and greatly expands the scope of existing law by adding vague language that would give drugstores more power to raise prices arbitrarily. The Oklahoma Senate already considered and rejected similar language in House Bill 2799; subsequently, the rejected language was attached to SB 1150 and passed by the House. SB 1150, as amended, would grant pharmacies the right to contest not only the MAC list price of any drug they dispense, but also contest other contractual arrangements — long after agreements have been signed.

For instance, the amendment language replaces the term "maximum allowable cost" with the term "reimbursement amounts." *Reimbursement amounts* is so broadly defined that it includes not just MAC prices, but also customer copays. In theory, this could allow drugstores to raise prices by some arbitrary amount and balance bill consumers for the difference between the reimbursement they agreed to and the higher price they wish to charge. This is unprecedented pricing power for a pharmacy to wield over drug plan enrollees.

Moreover, this broadens the scope of the existing law to the extent that it could also be used by pharmacies to demand higher fees for brand-name drugs whenever a pharmacy decides prices are too low. Increased regulations on the use of MAC lists would inhibit use of a tool that drug plans use to promote competition among pharmacies and drug wholesalers.

The legal right to ignore prior contractual agreements and renegotiate existing contracts at any time could cost Oklahomans a bundle. The purpose of this legislation is to boost the prices of the drugs sold by pharmacies to drug plan members. According to one estimate, this law would raise taxpayers' cost by up to $8 million per year for the state employee health plan. Other Oklahoma consumers would also find their drug costs and premiums rising.

Conclusion. Today, nearly all health plans include some level of prescription drug benefits. When drug plans create pharmacy networks, they negotiate the lowest possible prices. Negotiated prices are the result of bargaining power — the ability of the drug plan to steer business to a firm that offers the most favorable bid. As a result of drug plans and competition among pharmacies, relatively few patients are unable to afford their medications. Indeed, three-fourths of retail prescriptions cost the patient $10 or less. But this could all change if new laws allow drugstores to renege on negotiated contractual arrangements prior to the expiration of contracts. Consumers, employers and taxpayers will be the ultimate losers in that deal. SB 1150 as amended is a bad deal for Oklahoma consumers, employers and taxpayers.

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