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WHY PRICE CONTROLS ON PRESCRIPTION DRUGS WOULD HARM SENIORS

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Price controls do not work. In fact, they invariably worsen the very problems they are designed to solve. Nonetheless, politicians from Hammurabi the Great to President Richard Nixon have stubbornly implemented price controls as policy. And many Members of Congress today are sounding the siren song of price controls by supporting legislation that promises to make cut-rate prescription drugs available to Medicare beneficiaries. The tacit assumption is that government price controls would lower drug prices without increasing the cost of prescription drugs for senior citizens and others. That assumption is wrong.

After Representative Tom Allen (D–ME) introduced the Prescription Drug Fairness for Seniors Act (H.R. 664) on February 10, 1999, it quickly amassed over 100 sponsors. This bill would force prescription drug manufacturers to sell their products to retail pharmacies at a price equal to the lower of:

- The lowest price paid by any agency or department of the U.S. government; or
- The manufacturer's best price for the covered outpatient drug, as defined in section 1927(c) of the Social Security Act.

The price control regulation embodied in this bill would not lower costs. Instead, it would wreak havoc on the prescription drug market and result in higher costs and the reduced availability of new prescription drugs for all Americans. The reasons:

- **It would discount drugs for pharmacies but not seniors.** Representative Allen suggests that enacting H.R. 664 would result in a 40 percent reduction in the price of prescription drugs to the elderly. Because pharmacies would receive the discount, there would be no guarantee, legal or otherwise, that they would pass on their savings—in whole or in part—to a needy patient. Without that guarantee, the expected savings for seniors could not be determined.
- **It would increase costs for taxpayers.** Under the proposals in H.R. 664, drug manufacturers would find every excuse and legal loophole to charge higher prices to the government. If a drug developer were forced to sell that drug to pharmacies at a price linked to what it charged the federal government, then the developer

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would simply charge the government more. This higher price would be passed on to either Medicare beneficiaries—in the form of higher co-payments, monthly premiums, or deductibles—or to the taxpayer.

- **It would combine bad economics with a reduction in supply.** Under the "Findings" section of H.R. 664, the authors demonize prescription drug companies by stating that "manufacturers of prescription drugs engage in price discrimination practices." This is not the kind of argument that Members of Congress normally use to describe how other products are marketed in the economy. An apple grower, for example, rarely is charged with "price discrimination" when his product is sold at a higher price in a country store instead of in a busy downtown supermarket that buys apples in larger volume. The price paid at the country store is higher as a result of special shipping and packaging costs, not some conscious effort by the producer to soak the "little guy." If the government fixes a price that is unprofitable to a supplier, then the supplier is less likely to sell apples, or any other product, to small retailers. The same is true for prescription drugs.

- **Research and development on tomorrow's cures would decline.** The authors of the bill declare that drug manufacturers make an annual profit of $20 billion, and they imply that these companies earn unreasonably high profits. Certainly automobile, aerospace, and computer manufacturers, among others, make similar profits, but no one in Congress accuses them of price gouging for their vital products. Although it is true that some drug companies are financially successful, profits are spread very unevenly throughout the pharmaceutical industry. For every manufacturer that makes huge profits off a blockbuster drug like Viagra, there are numerous other companies that are less profitable and still others that lose money (the latter group, by the way, does not count against the $20 billion figure cited in the bill).

  Pharmaceutical research is a very risky business. A number of independent studies have found that between 5,000 and 10,000 compounds are tried on average for every 1 that makes it into a neighborhood pharmacy. And that one may be for a very tiny niche market. The incentive to engage in such intense research and development is the potential for large profits on the few drugs that are successful. If the government limited profits on the successes, then there would be fewer resources devoted to research and development. This would translate into a reduced likelihood that tomorrow's cures will be developed. Last year, U.S. pharmaceutical manufacturers invested $24 billion of their revenues to research new drugs. Jeopardizing such massive expenditures in the search for new medications quite literally would threaten the health of America's seniors.

CONCLUSION

Congress needs to develop a sound prescription drug policy for seniors enrolled in the Medicare program. Almost two-thirds of Medicare enrollees buy prescription drugs through the private market. The task is to find a way to help those seniors in need to purchase their prescription drugs affordably. Bills like H.R. 664 that focus on price controls would do nothing to address the real problem: the lack of outpatient prescription drug coverage for needy seniors. Worse, policies like those contained in H.R. 664 are fraught with unintended consequences. They would harm not only those seniors Congress wants to help, but also the pharmaceutical research base that is necessary to find cures and treatments to combat disease and improve the quality of life for millions of Americans.

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