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Drug Makers Raise Prices in Face of Health Care Reform

By DUFF WILSON

Even as drug makers promise to support Washington’s health care overhaul by shaving $8 billion a year off the nation’s drug costs after the legislation takes effect, the industry has been raising its prices at the fastest rate in years.

In the last year, the industry has raised the wholesale prices of brand-name prescription drugs by about 9 percent, according to industry analysts. That will add more than $10 billion to the nation’s drug bill, which is on track to exceed $300 billion this year. By at least one analysis, it is the highest annual rate of inflation for drug prices since 1992.

The drug trend is distinctly at odds with the direction of the Consumer Price Index, which has fallen by 1.3 percent in the last year.

Drug makers say they have valid business reasons for the price increases. Critics say the industry is trying to establish a higher price base before Congress passes legislation that tries to curb drug spending in coming years.

“When we have major legislation anticipated, we see a run-up in price increases,” says Stephen W. Schondelmeyer, a professor of pharmaceutical economics at the University of Minnesota. He has analyzed drug pricing for AARP, the advocacy group for seniors that supports the House health care legislation that the drug industry opposes.

A Harvard health economist, Joseph P. Newhouse, said he found a similar pattern of unusual price increases after Congress added drug benefits to Medicare a few years ago, giving tens of millions of older Americans federally subsidized drug insurance. Just as the program was taking effect in 2006, the drug industry raised prices by the widest margin in a half-dozen years.

“They try to maximize their profits,” Mr. Newhouse said.

But drug companies say they are having to raise prices to maintain the profits necessary to invest in research and development of new drugs as the patents on many of their most popular drugs are set to expire over the next few years.

“Price adjustments for our products have no connection to health care reform,” said Ron Rogers, a spokesman for Merck, which raised its prices about 8.9 percent in the last year, according to a stock analyst’s report.

This year’s increases mean the average annual cost for a brand-name prescription drug that is taken daily would be more than $2,000 — $200 higher than last year, Professor Schondelmeyer said.

And this means that the cost of many popular drugs has risen even faster. Merck, for example, now sells daily 10-milligram pills of Singulair, the blockbuster asthma drug, at a wholesale price of $1,330 a year — $147 more than last year. Singulair is now selling at retail, on drugstore.com, for nearly $1,478 a year.

The drug companies “can charge what they want — it’s not fair,” Eric White, the 42-year-old owner of a small jewelry store in Queens, said as he left a pharmacy recently.

Despite having drug insurance, Mr. White says he now pays $110 a month out of pocket for two brand-name allergy medicines, even as he has cut prices in his jewelry store by at least 40 percent to keep customers coming through the door.

He shook his head. “What can I do?” he said. “I need my medicines.”

The drug industry has actively opposed some of the cost-cutting provisions in the House legislation, which passed Nov. 7 and aims to cut drug spending by about $14 billion a year over a decade.

But the drug makers have been proudly citing the agreement they reached with the White House and the Senate Finance Committee chairman to trim $8 billion a year — $80 billion over 10 years — from the nation’s drug bill by giving rebates to older Americans and the government. That provision is likely to be part of the legislation that will reach the Senate floor in coming weeks.

But this year's price increases would effectively cancel out the savings from at least the first year of the Senate Finance agreement. And some critics say the surge in drug prices could change the dynamics of the entire 10-year deal.

"It makes it much easier for the drug companies to pony up the $80 billion because they'll be making more money," said Steven D. Findlay, senior health care analyst with the advocacy group Consumers Union.

Name-brand prices have risen even as prices of widely used generic drugs have fallen by about 9 percent in the last year, Professor Schondelmeyer said. But name brands account for 78 percent of total prescription drug spending in this country. And as long as a name-brand drug still has patent protection it faces no price competition from generics.

Ken Johnson, senior vice president of the industry association — the Pharmaceutical Research and Manufacturers of America — criticized the analysis Professor Schondelmeyer had conducted for AARP, saying it was politically motivated.

"In AARP's skewed view of the world, medicines are always looked at as a cost and never seen as a savings — even though medicines often reduce unnecessary hospitalization, help avoid costly medical procedures and increase productivity through better prevention and management of chronic diseases," he said.

But Professor Schondelmeyer's analysis — which found prices for the name-brand drugs most widely used by the Medicare population rising by 9.3 percent in the last year, the fastest rate since 1992 — is in line with the findings of a leading Wall Street analyst, too.

Catherine J. Arnold, a drug industry analyst at Credit Suisse, said her latest study of the nation's eight biggest pharmaceutical companies showed markedly similar results: list prices rising an average of 8.7 percent in the 12 months ending Sept. 30 — the highest rate of growth since at least 2004.

As does Professor Schondelmeyer, Ms. Arnold based her price calculations on reported wholesale prices and a formula that puts more emphasis on each company's best-selling drugs.

Ms. Arnold said the prospect of cost containment under health care reform, as well as the tougher business environment, entered into the decisions of manufacturers to raise prices this year.

The industry stands to gain about 30 million customers with drug insurance from the legislation pending in Congress. But the industry also faces the prospect of tougher negotiations from both public and private buyers as the government tries to squeeze savings out of the health system.

“If you’re going to take price increases,” Ms. Arnold said, “here and now might be the place to do that, because the next year and the year after that might be tough.”

Mr. Johnson did not dispute the Credit Suisse study or deny Ms. Arnold’s finding that American drug makers have raised prices at the fastest rate in five years.

He said both studies were incomplete by failing to include rebates that drug makers give distributors. But Ms. Arnold, Professor Schondelmeyer and a 2007 Congressional study of Medicare said the rebates often accrue to the middlemen, not consumers, and higher manufacturer prices lead to higher retail prices.

And the drug industry’s own major consulting firm, IMS Health, has also reported a significant run-up in prices. Back in April, IMS predicted that United States drug sales might actually decline this year.

Billy Tauzin, president of the industry’s trade association, highlighted the gloomy prediction in a June 1 letter to President Obama shortly before striking the deal to cut drug costs by $80 billion. In negotiating the deal, the drug makers argued that they could not afford to give up more than that.

But in October, IMS made an unusual change in the middle of its forecasting cycle, saying it now believed United States sales would grow at least 4.5 percent in 2009 — or $21 billion more than expected six months earlier.

A major reason, IMS said, was higher-than-expected price increases for drugs in the United States.