



April 16, 2007

Honorable Debbie Stabenow
United States Senate
Washington, DC 20510

Dear Senator:

This letter responds to your question about the effect that changes to Part D of the Medicare program would have on drug pricing for other purchasers, including the Medicaid program, the Department of Veterans Affairs (VA), and private purchasers. As a general rule, any effects on non-Medicare purchasers of drugs would depend on the specific changes made to Part D and the extent and nature of their impact on Medicare spending.

The Congressional Budget Office (CBO) anticipates that S. 3, the Medicare Prescription Drug Price Negotiation Act of 2007 (as reported by the Finance Committee on April 13th), would not have an effect on drug prices for other purchasers. That bill would repeal section 1860D–11(i) of the Social Security Act, which is commonly known as the “noninterference provision” because it prohibits the Secretary of Health and Human Services from interfering in the negotiations between drug manufacturers, pharmacies, and sponsors of the prescription drug plans that deliver the Part D benefit. CBO anticipates that simply removing that provision would have a negligible effect on Medicare spending across a broad range of drugs and would not have an effect on drug prices paid by other purchasers.

By contrast, Part D could be modified to include a “best price” system similar to the one used by the VA and Medicaid. As I indicated during the Finance Committee’s deliberations, CBO would expect such a change to generate significant cost reductions for drugs purchased under Part D. Such an approach, however, would put upward pressure on prices paid by the VA, Medicaid, and private purchasers. Medicaid and the VA are required by law to receive price discounts that at least equal the largest private-sector discounts that drug manufacturers provide. Expanding that requirement to the Medicare benefit, which accounts for a larger share of total drug spending, would encourage drug manufacturers to reduce the private-sector discounts on which the VA’s and Medicaid’s prices are partially based; that effect would probably offset a small share of the expected savings for Medicare.

The expected effects of other proposals that result in cost savings for Part D would vary. The more direct the connection is between pricing under Part D and prices paid by the VA and Medicaid (or the private-sector prices on which discounts for the VA and Medicaid are based), the more upward pressure would be placed on VA and Medicaid prices. Approaches that yielded savings for Medicare but did not link Part D prices to the prices paid by other purchasers would not be expected to have an effect on those other prices. S. 3 would not establish any such

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connection, and CBO estimates that it would not have an impact on prices paid by other purchasers.

If you would like additional information on this subject, CBO would be happy to provide it. The staff contact for this analysis is Philip Ellis.

Sincerely,

A handwritten signature in black ink, appearing to read "Peter R. Orszag". The signature is fluid and cursive, with the first name "Peter" and last name "Orszag" clearly distinguishable.

Peter R. Orszag
Director

cc: Honorable Max Baucus
Chairman
Committee on Finance

Honorable Charles E. Grassley
Ranking Member