AMERICANS for TAX REFORM

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Re: ATR Opposition to H.R. 107 (Lifting the 100 Percent Rebate Cap for Medicaid Outpatient Drugs)

Jan 16, 2019

Dear Member of Congress:

I write in opposition to H.R. 107, legislation sponsored by Congressman Michael Burgess (R-Texas). This legislation removes the existing 100 percent rebate cap that currently exists for outpatient drugs prescribed under Medicaid.

This legislation would create a perverse system where manufacturers pay Medicaid to supply their drugs to the states. This would create incentives within the Medicaid system that could encourage gaming of the system and higher prices in Medicaid and the private market.

The Medicaid rebate is currently calculated through a two-step process.

First, Medicaid is entitled to a "basic rebate" which is the greater of 23.1 percent of the Average Manufacturer Price (AMP) or the difference between AMP and "best price." AMP is calculated as the average price of selling to retail community pharmacies and wholesalers but excluding rebates and discounts negotiated by Pharmacy Benefit Managers, among others.

Second, the manufacturer is required to provide an inflation penalty rebate calculated based on the extent to which the drug's price increases exceed the Consumer Price Index for all Urban Consumers (CPI-U).

This formula results in manufacturers providing roughly $42 billion every year in discounts to state Medicaid programs, but also contains a cap that prevents the discount exceeding 100 percent of AMP, a situation where the product is free for Medicaid. There are currently over 2,500 drugs that are at 100 percent of AMP.

A rebate above 100 percent of AMP, as H.R. 107 would allow, would create numerous instances where the manufacturer is paying Medicaid to supply the drug.

It is important to note that participation in Medicaid is not optional. Manufacturers must take part in the system as a condition of participating in other federal programs including Medicare Part B and Veterans Affairs healthcare.

As a result, this reform would not cause manufacturers to leave Medicaid. Instead, it would likely create perverse incentives within the market.

For instance, the proposal could result in higher prices in the commercial market because manufacturers would be incentivized to reduce rebates and discounts in order to avoid further decreasing "best price." While this would reduce the Medicaid rebate, it would increase costs for plans and consumers. In turn, this would result in new medicines being launched at higher prices due to the subsidies required by Medicaid.

Lifting the cap would also encourage gaming of the system by turning a product into a revenue stream for the federal government and the states. In fact, the bill effectively creates slush funds for the states as there are no restrictions on how they can utilize funds generated from payments above 100 percent of AMP.

The current 100 percent rebate cap is a reasonable safeguard for manufacturers to ensure the subsidies they pay Medicaid are no higher than the price of the drug. Removing this cap, as H.R. 107 proposes, would create a perverse system where manufacturers are forced to pay the government every time they supply their product to Medicaid, a situation that will distort the market and incentivize higher prices.

Onward,

Grover G. Norquist
President, Americans for Tax Reform