

Abbott drug shake-up to save \$1bn

- Compensation for chemists
- Pressure to use generics

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The federal government will be forced to compensate pharmacists for losses they suffer under an overhaul of the pharmaceutical benefits scheme designed to save \$1 billion by making generic medicines the preferred drugs for all Australians.

Health Minister Tony Abbott will today put a reform package to the pharmaceutical industry that requires chemists to disclose the margins they make on sales of generic drugs and cuts the amount the government pays for subsidised medicines once new copycat drugs enter the market.

By reducing the amount the government pays for many medicines, the reforms are likely to hurt pharmacists and drug manufacturers while having little impact on consumers.

The changes could also raise the stakes in the debate over the effect of the United States free-trade agreement on the local pharmaceutical

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sector, amid concerns "big pharma" — the companies that develop new drugs — could use the deal to block generics entering the market.

But *The Australian Financial Review* has learnt the government will move to placate developers of new drugs by giving patented drugs a two-year exemption from the price cuts that come into effect once generics hit the market.

While the package tries to offer something to each of the other

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Abbott targets \$1bn savings in drug plan

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industries affected, elements of it are likely to draw fire from pharmacists, drug companies and doctors.

Last week's budget showed the government had successfully reined in the cost of the \$6 billion PBS through a number of measures, including increasing patients' co-payment and a 12.5 per cent drop in prices once copycat versions of a drug become available.

After recording double-digit growth for much of the past decade — and attracting Treasurer Peter Costello's attention as one of Canberra's fastest-growing sources of spending — the cost of the PBS is expected to fall marginally this year, before growing at 5.6 per cent a year in real terms over the following three years.

Pharmacists said the budget result meant there was little justification for any radical overhaul of the system, which they fear could cut their profits.

But Mr Abbott indicated last week he still saw room for improvement.

"While growth has been slow in the current year, the forward estimates are still for quite high growth and there is quite a long queue of new drugs that will soon be coming [up] for evaluation," he said.

In a sign of the importance of the issue to the sector, the Pharmacy Guild of Australia last week announced that Kieren Schneemann, chief executive of Medicines Australia — which represents the companies that develop new drugs — would take over the top job at the guild from July.

The government will be hoping to wrap up discussions with the sector well before next year's federal election, amid concerns among some senior coalition MPs about the risk of a protracted dispute with the powerful pharmacy industry.

Under the PBS, patients pay \$29.50 for most drugs listed on the scheme — or \$4.70 for concession cardholders — and the government picks up the remainder of the cost.

EXPENSIVE HABIT

What the reforms mean

1 Higher subsidies for some branded drugs

Under so-called reference pricing, all drugs with similar health outcomes are offered at the same price. When any original or branded drug in that group has its patent expire, copycat versions will enter the market, meaning all the drugs within the group would have to be offered at the lower price of the generics. But under the government's reforms, other branded drugs in the group, which would still be on patent, could apply to wait two years before dropping their price.

Outcome: The taxpayer pays more and innovator drug companies earn more for some branded drugs. Some customers may pay more for branded drugs but government wants them to shift to generics.

2 Generics become default drug of choice

If a generic version of a drug is available, doctors must prescribe it unless they can show there is a clinical reason for choosing the branded drug.

Outcome: Use of cheaper generics increases, saving the taxpayer money. But innovator drug companies would lose sales. Doctors are likely to resist the move and medicine wholesalers, which make money from sales of branded drugs, could also suffer.

3 Pharmacists' margins revealed

The government pays pharmacists a set amount for the drugs they sell to customers. But there are concerns that pharmacists are reaping big margins by buying generics at a price well below the amount they receive from the government. The government therefore wants to require pharmacists to disclose these discounts, opening the way for their margins to be squeezed.

Outcome: Pharmacists potentially make smaller profits on generics while taxpayers pay less. Generics manufacturers would also suffer.

4 Lower subsidies for generics

Once a branded drug in a reference pricing group comes off patent, the price of all drugs in the group falls by 12.5 per cent as soon as the first generic version becomes available. The government now wants to take this further, reducing the price by a further 5 per cent for every additional generic that enters the market.

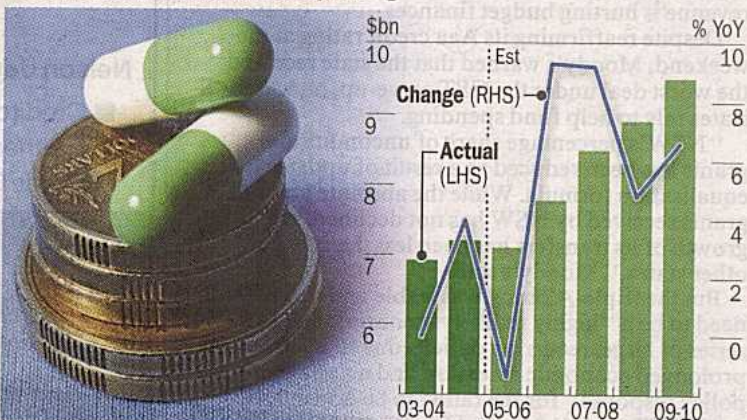
Outcome: Pharmacists' margins are squeezed and drug companies earn less but taxpayers make savings. Generics manufacturers would also be hit.

5 Compensation

Cascading reference prices and having to disclose their margins mean pharmacists are likely to lose profits.

Outcome: The government plans to pay compensation to offset these losses.

Federal govt pharmaceutical spending



Source: Budget papers

A central plank of the government's bid to cut the cost of the PBS is to promote the use of cheaper generic drugs that enter the market once a more expensive branded medicine comes off patent.

Under the plans to be put to the industry today, where a generic version of a drug is available, doctors will be required to prescribe it unless they can show there is a good clinical reason for choosing the branded drug.

The proposal is likely to encounter resistance among doctors. The Australian Medical Association has previously rejected any measures that would compel doctors to favour one type of drug over another.

The government is also concerned that pharmacists reap big margins by buying generics at a price well below the amount the government eventually pays for them.

Mr Abbott will therefore push pharmacists to disclose these discounts, opening the way for the government to make savings by renegotiating the amount it pays for generic drugs under the PBS.

But because lower prices would squeeze margins right down the supply chain, the move is likely to be opposed by pharmacists and generic drug manufacturers.

Under measures that came into force last year, the price of all drugs in a so-called reference pricing group — meaning medicines that produce a similar

“It is likely to encounter resistance among doctors.”

health outcome — are required to drop 12.5 per cent once one of them comes off patent and the first copycat version becomes available.

In a move that is likely to encounter resistance right across the pharmaceutical sector, the government now wants this “reference price” to drop a further 5 per cent every time a new generic enters the market.

In recognition of the impact

that this measure and the new disclosure rules are likely to have on pharmacists, the government is putting together a compensation package for the pharmacy sector, although the likely size of the deal is unclear.

Although big pharma is likely to be worse off as a result of the cuts to reference prices and the push towards generics, it will benefit from other changes to the reference pricing system.

While the price of all drugs in the group would automatically drop 12.5 per cent once one branded pharmaceutical comes off patent and a generic version becomes available, other branded drugs in the group that are still under patent would not have to lower their prices for two years.

The biggest attempt to date to rein in costs of the PBS occurred in the 2002-03 budget, when Mr Costello increased the PBS customer co-payment as part of his intergenerational reforms.

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