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Selecting the Right Price Indicator for Pharmaceutical Cases

Analyzing drug pricing are a crucial part of antitrust cases and securities litigation involving pharmaceutical companies. This analysis can be complicated, however, because the pharmaceutical industry has multiple pricing mechanisms. Expert analysis is critical to correctly identify the which price metric is appropriate for a given analysis. This article discusses the various price metrics used in the industry, how they relate to one another, and some considerations to keep in mind when selecting the appropriate price metric for the analysis.

List Prices

Drug pricing between manufacturers and their customers in the U.S. is complicated and opaque.[1] While some government-funded programs involve high levels of price regulation, private contractual relationships govern most private sector drug transactions in the U.S. These contractual relationships can vary by customer and the parties involved usually keep such information in confidence.[2] At the same time, pharmaceutical companies will make the "list prices" of particular drugs available to reporting services.

These list prices, which do not reflect contractually negotiated discounts and rebates, are distinct from the prices customers actually pay. However, list prices still bear a strong relationship to the latter because contracts usually contain a benchmark establishing a direct relationship between the list price and the price the customer pays.

Thus, list prices provide a useful, albeit rough, measure of what pharmaceutical companies charge for specific drugs. As such, they are often monitored by competing firms and can provide useful insights into pharmaceutical pricing patterns.

Average Wholesale Price (AWP) and Wholesale Acquisition Cost (WAC)

Historically, the Average Wholesale Price, or AWP, was the most commonly used list price. However, in recent years, it has largely fallen out of favor as it has less relevance for actual pricing.

Instead, the standard list price for U.S. pharmaceuticals today is the Wholesale Acquisition Cost, or WAC, defined in regulations as the "the manufacturer's list price for the drug or biological to wholesalers or direct purchasers in the United States" excluding discounts, rebates or

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[1] Lieberman, Steven M., and Paul B. Ginsburg. "Would Price Transparency for Generic Drugs Lower Costs for Payers and Patients?" *The Brookings Institution* (June 2017). <https://www.brookings.edu/wp-content/uploads/2017/06/es_20170613_genericdrugpricing.pdf> (accessed May 5, 2021): 1-17 at 1.
[2] *Id.*

reductions."[3] The WAC is based on data from the most recent month available[4] and WAC data is generally shared with commercial data providers, such as Symphony, who then make the information available for a fee to subscribers.

Post-Discount Prices

Starting from the list price, manufacturers deduct discounts, rebates, chargebacks, and other concessions to arrive at the "post-discount price" or "net price." For example, a contract might specify that a customer will pay list price minus a certain percentage.[5] Larger customers, such as major chain pharmacies and leading wholesalers that control greater market volume, can generally negotiate larger discounts than can smaller customers. Despite this general tendency, list price increases are often borne by all customers, albeit to varying degrees depending on each customer's negotiating power.

Apart from the discounts negotiated with customers, generic pharmaceutical drug contracts also often contain provisions that create disincentives for manufacturers to increase prices. For instance, contracts may include automatic penalties triggered by price increases. Such penalties can potentially be imposed and payable to customers immediately, even if the price increases do not take effect until after a mandatory notice period. After a large price increase, penalties could temporarily exceed the revenue received on sales of a drug, in which case the firm would attribute negative revenues to the drug for the affected period. Depending on whether such penalties are reflected in the post-discount price indicator being analyzed, the indicator might show negative customer pricing in the immediate aftermath of a list price increase.

Pros and Cons of Various Price Indicators

Companies might maintain different internal estimates or measurements of the final price paid by customers, reflecting various discounts, rebates, fees, and other price adjustments. Because different measurements of post-discount prices may not reflect all discounts, penalties, and other pricing factors, it is essential to assess each indicator carefully before determining which is the most appropriate for use in the analysis at hand.

For instance, in studying long-term pricing patterns, using an indicator that includes temporary penalties and chargebacks may introduce an unnecessary source of "noise" into the analysis. On the other hand, if the objective is to analyze company revenues, it may be more appropriate to use an indicator that includes all discounts, penalties, fees, and other adjustments to get the most accurate picture of the amounts the company actually received. It is also worth noting that different pharmaceutical companies may have different internal uses for different indicators, rendering certain indicators more valuable for analyzing the behavior of a particular company.

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[3] 42 U.S.C. § 1395w-3a(c)(6) (2011).
[4] *Id.*
[5] *See, e.g.*, McKesson Corporation and ANIP Acquisition Company. "Supplier Agreement - Multisource and OneStop Generics Program." *Securities and Exchange Commission* (Nov. 1, 2010). <https://www.sec.gov/Archives/edgar/data/1023024/000104746912011161/a2211561zex-10_56.htm> (accessed Apr. 30, 2021) at Section 2.2.

It may also be appropriate to analyze list prices instead of—or in conjunction with—post-discount prices. Analyzing list prices may be particularly useful in cases with a comparative focus. In analyses in which overall pricing behavior is more relevant than customer-specific pricing, list prices provide a useful starting point for analyzing similarities or differences between pricing behaviors of multiple companies.

Moreover, because post-discount prices are typically not disclosed to competitor firms and list price is the only indicator that is commonly observable to competitors, analyzing list prices may also be informative from the perspective of analyzing firm behavior, conditional on observable market information.

Due to these complex considerations, the choice of an appropriate price indicator requires familiarity with the pros and cons of the prevailing price indicators. In this respect, an expert combining domain knowledge with quantitative expertise can be invaluable, not only in selecting the appropriate indicator but also in generating the most useful insights from that indicator.

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