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Turing Pharmaceuticals: The Ethics of Drug Pricing[[1]](#endnote-1)

Shernaz Bodhanwala and Aakash Bothra wrote this case solely to provide material for class discussion. The authors do not intend to illustrate either effective or ineffective handling of a managerial situation. The authors may have disguised certain names and other identifying information to protect confidentiality.

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Turing Pharmaceuticals AG (Turing), a privately held, New York-based biopharmaceutical company, came under fire in the third quarter of fiscal year (FY) 2015/16 for increasing the price of one of its drugs, Daraprim (pyrimethamine), from US$13.50[[2]](#endnote-2) to $750.00 a pill. Martin Shkreli, the founder and former chief executive officer (CEO) of Turing, was subjected to scrutiny and outrage-inducing media headlines, such as one by *Vice News*—“This Is How Drug Companies Jack Up Their Prices and Hurt Patients”[[3]](#endnote-3)—and another by *USA Today*—“Company Hikes Price 5,000% for Drug That Fights Complication of AIDS, Cancer.”[[4]](#endnote-4) The media circulated many emotional stories of affected patients, including that of Isla Weston.

Isla, a four-month old girl born to Shannon Weston and her husband, Joshua, was diagnosed with congenital toxoplasmosis, a parasitic infection that had occurred during pregnancy.[[5]](#endnote-5) Isla was asymptomatic at birth, but without immediate treatment, she would have likely experienced brain damage and blindness. When their insurance company refused to cover the needed medication, Isla’s parents considered taking a second mortgage on their home, cashing in their retirement plan, and finding a benefactor to help provide the $360,000 needed for Isla’s year of treatment. The University of North Carolina was able to help the Westons, providing them with Daraprim for $48 a month.[[6]](#endnote-6) In a testimony before the U.S. Congress, Shannon expressed her gratitude: “I am so grateful that this option was found before it was too late for my daughter.”[[7]](#endnote-7)

The high cost of health care in the United States could be attributed to the rising cost of medications; for Isla, the rising cost was a single price increase of more than 5,000 per cent in the price of Daraprim.[[8]](#endnote-8) The drug, which had been on the market for decades and went off-patent in 1970, was primarily used to treat toxoplasmosis—a parasitic disease easily contracted by patients suffering with weakened immune systems due to HIV/AIDS,[[9]](#endnote-9) cancer, pregnancy, or organ transplant.[[10]](#endnote-10)

In 2015, Turing acquired the manufacturing and commercialization rights to Daraprim in the United States from Impax Laboratories for $55 million. Shortly after the deal, Turing raised the price of the drug from $13.50 to $750.00 a pill, and moved to a more tightly controlled distribution model. Shkreli, in the face of a public outcry, defended the decision, pointing to the need for the company to turn profits, modernize the 1953 drug, and develop refined versions of the drug (“next generation” drugs) with fewer side effects and better efficacy. According to Shkreli, the increased price for the drug would support the needed research and development. He argued that the increase in the price of Daraprim was warranted because the drug was highly specialized. He likened Daraprim to an Aston Martin previously being sold at the price of a bicycle.[[11]](#endnote-11) How should Turing respond to the public outcry? Should Turing stand by the increased price for Daraprim? How could it handle the outcry from the patient groups that needed Daraprim?

Martin Shkreli

Shkreli was born in April 1983, and grew up in a working-class neighbourhood in Brooklyn, New York. As a young child, Shkreli was interested in playing chess, and attributed his interest to a man called Marty, who lived in Shkreli’s building. At an age when children usually played with toys, Shkreli began an investment-related education about public listed company stocks with the help of Marty. Shkreli remarked, “I kept thinking even as a young kid—at 10 or 11 years—I could have a company as big as Eli Lilly or Merck.” Recalling his early days in an interview with CNN Money, Shkreli said, “As a kid, my friends knew all the Yankees and Mets players’ batting averages and how many home runs they hit. I knew everything about all the public companies.”[[12]](#endnote-12)

Passionate about a career in investments, Shkreli dropped out of school at the age of 16 and began to work as an intern at Cramer, Berkowitz & Co.[[13]](#endnote-13) Shkreli continued his education later and pursued his business degree at New York’s Baruch College. Shkreli’s working career included brief stints at UBS and Intrepid Capital Management. In 2006, he started his own hedge fund, Elea Capital Management (Elea). At Elea, Shkreli lost his investors’ money and the fund closed a year later.[[14]](#endnote-14) Shkreli’s second hedge fund venture was MSMB Capital Management.[[15]](#endnote-15)

Retrophin LLC (Retrophin), a Delaware-based company, was the first biotech firm Shkreli founded, in 2011. In 2014, Shkreli was removed from Retrophin’s board due to alleged improper handling of legal settlements, and siphoning Retrophin’s money to compensate for the loss suffered by MSMB’s investors.[[16]](#endnote-16) Denying the allegations, Shkreli said in an interview with the *New York Times*, “They are sort of concocting this wild and crazy and unlikely story to swindle me out of the money.”[[17]](#endnote-17)

After the legal dispute at Retrophin, Shkreli moved on in February 2015 to form another biopharmaceutical firm: Turing. The intent was to focus on providing treatment for serious diseases. Turing had two medications in its product offerings: Daraprim, used to treat toxoplasmosis, and Vecamyl®, used to treat hypertension.

In November 2015, being true to his entrepreneurial spirit, Shkreli bought ailing KaloBios Pharmaceuticals (KaloBios). The pharmaceutical firm had acquired worldwide ownership rights to the drug benznidazole, which was primarily used to treat Chagas disease, a parasitic disease that could lead to cardiac and digestive issues. Soon after Shkreli took over KaloBios, the company’s shares soared 400 per cent.[[18]](#endnote-18) However, in December 2015, after Shkreli had been arrested in a securities fraud case, he was fired from his position as CEO at KaloBios, and the company eventually filed for bankruptcy.[[19]](#endnote-19) At the same time, Shkreli resigned as CEO of Turing, after which Ron Tilles, then chairman of the board, was appointed interim CEO.

Inside Turing

Many senior officials at Turing were unhappy with the sudden increase in the price of Daraprim, and were concerned about the negative impact on Turing’s reputation. Company officials had to face not only the media scrutiny, but also inquiries from several U.S. senators demanding that pricing decisions be explained. On March 17, 2016, in a testimony before the United States Senate’s Special Committee on Aging, Howard Dorfman, who had been senior vice-president and general counsel at Turing, said he and other members of Turing’s management committee raised objections to the price increase. He explained that there was no formal study protocol in place at Turing to develop a next generation toxoplasmosis therapy.[[20]](#endnote-20)

Dorfman further explained that Daraprim was distributed through a closed or “controlled” system; it could not be obtained through normal hospital or pharmacy channels, but through a direct dispensing and case management program run by Turing. This tightly controlled drug distribution system excluded the entry of a potential “second generic competitor”—an approved substitute for the specific branded drug—which enabled Turing to enjoy a monopoly power for at least three years.[[21]](#endnote-21) Dorfman justified Turing’s distribution strategy by saying, “[I]t is important to understand how that closed distribution system plays a role in maximizing the returns on a drug such as Daraprim.”

During an interview with Fox5 in New York, Shkreli explained that the company invested all of its cash and all of its “extra” profit in research and development (R&D).[[22]](#endnote-22) Contradicting Shkreli’s statement, Nancy Retzlaff, Turing’s chief commercial officer, testified in a Congressional hearing that only 60 per cent of the company’s net revenue was used in R&D. She added that Turing was running the Daraprim program at a financial loss, revealing that gross sales for 2015 were approximately $98 million and net sales for the same period were $20 million.[[23]](#endnote-23) At the same time, the company was increasing salaries, according to a board agenda for October 14, 2015 (see Exhibit 1).[[24]](#endnote-24) When asked whether she was planning any future price increases, Retzlaff replied, “No, I am not.”[[25]](#endnote-25)

The burden of the increased drug price fell on insurance companies, who in turn charged their members higher insurance premiums. Retzlaff clarified that the $750 price for Daraprim was primarily borne by commercial insurers, who represented the minority of patients. The majority of patients received Daraprim through public programs that purchased Daraprim at a reduced cost, or through a patient assistance program run by Turing. The price of Daraprim in other countries was significantly lower than in the United States (see Exhibit 2). Retzlaff defended the price increase, arguing that because only 3,000 patients annually needed Daraprim, the budget impact on health care insurance premiums was almost negligible.[[26]](#endnote-26)

Many medical practitioners and hospitals considered prescribing alternative products, and warned Turing about the negative impact of the massive increase in price. On September 30, 2015, a sales account manager at Turing sent an email describing a recent meeting with Massachusetts General Hospital, writing, “One of the things we discussed was Mass[achusetts] General’s internal analysis of the impact of Daraprim’s new price on their inpatient pharmacy budget, which they have determined to be prohibitively expensive. Against their clinical convictions, they are currently switching patients to Bactrim.”[[27]](#endnote-27)

Industry

The *Rx Price Watch Report*, released in 2016 by the AARP Public Policy Institute, claimed that from 2006 to 2015 the prices for prescription drugs increased every year at a rate substantially higher than the general inflation (Exhibit 3).[[28]](#endnote-28) This difference was more pronounced in the last three years of analysis (2013–2015), when the retail prices for widely used prescription drugs increased by an average of over 15 per cent compared to the general inflation rate, which ranged from 0.1–1.6 per cent. The AARP study showed that the annual cost for drug therapy in 2015—$26,000—was much greater than the median annual income for Medicare beneficiaries.[[29]](#endnote-29) The impact of a substantial rise in the retail prices of prescription drugs was borne by almost all consumers, with the major financial burden on private health care insurance users.[[30]](#endnote-30)

Horizon Pharma PLC increased the price of its Vimovo (naproxen and esomeprazole magnesium)[[31]](#endnote-31) pain tablets by 597 per cent right after they purchased the drug from AstraZeneca in 2013. The revenue generated by Vimovo increased from $20 million in 2013 to $163 million in 2015. Valeant Pharmaceuticals increased the price of Nitropress (nitroprusside), a drug used to treat high blood pressure, more than three times immediately after the company acquired the rights for the drug from Marathon Pharmaceuticals LLC (Exhibit 4).[[32]](#endnote-32) Mallinckrodt PLC increased the price of H. P. Acthar Gel (repository corticotropin injection) from $40 per vial in 2001 to $38,000 per vial in 2016. According to the Medicare Drug Spending Dashboard for 2015, the average cost of Acthar to Medicare was $162,371, making it the single most expensive drug on a per patient basis.[[33]](#endnote-33) In yet another case, Mylan Inc. increased the price of EpiPens, a medical device used to automatically inject a measured dose of epinephrine, from $100 for a package of two in 2007 to $600 in 2016—an increase of 500 per cent for a device used by millions to counter life-threatening allergic reactions.[[34]](#endnote-34)

During a hearing of the Full House Committee on Oversight and Government, U.S. Representative (R-TX) Blake Farenthold questioned Keith Flanagan, a director from the Food and Drug Administration (FDA). Farenthold challenged Flanagan about the FDA’s delay in approving generic drugs: “You’re saying you’re getting down to 10 and 15 months, but you’ve basically created a 10- and 15-month monopoly for anybody who’s a single source of a generic drug, [and] who do that kind of price increase.”[[35]](#endnote-35)

Conclusion

Industry stakeholders questioned whether the development and approval of generic drugs, which cost approximately 80 per cent less than their branded equivalent, should be sped up.[[36]](#endnote-36) Others argued, as suggested in 2014 by the Tufts Center for the Study of Drug Development, that pharmaceutical companies incurred huge costs in R&D to bring a new drug to the market. In general, the drug development and approval process was long, often with a low success rate. For these companies to sustain their business, the price of drugs needed to support reasonable profits. But if that were the case, was it justifiable to prioritize a company’s profits over drug availability?[[37]](#endnote-37)

Dr. Rima McLeod, the medical director of the toxoplasmosis centre at the University of Chicago, had previously defended Turing’s actions, describing the situation as “workable” despite the price increase.[[38]](#endnote-38) Later, however, she wrote in an email to Eliseo Salinas, Turing’s president of R&D:

I understand, I know nothing of what makes Turing solvent and able to do research and of course I value that a lot too. . . . However, Martin [Shkreli] did say that he had to maximize profit for investors and that was why [the] price is high. He did not say that it was for research primarily that it was a high price. He called that the “dirty secret” of pharma.[[39]](#endnote-39)

Was Shkreli an aberration in the pharmaceutical industry? And was the industry’s pricing structure its only “dirty secret”? Generally, any business would charge a customer more if it could. When companies held calls with investors and analysts to discuss drug costs, Mick Kolassa, a former director of pricing policy for the drug industry, noted that participants would ask, “Why didn’t you price it higher?” Kolassa remarked, “I’ve never heard anybody say, ‘Why don’t you price it lower?’”[[40]](#endnote-40)

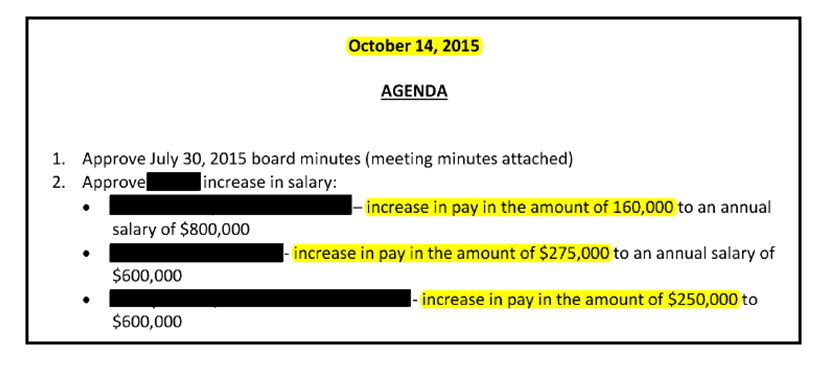
Pharmaceutical pricing had become a question of how much higher the prices could go until the pricing model became unethical. But it was a question ripe with subjectivity. Who should be responsible for upholding ethical pricing in the pharmaceutical industry? Was the company responsible to a wider group of stakeholders than just the shareholders?

Tilles and his team needed to answer some tough questions posed by Turing’s customers, Congress, and the media. How could they maintain Turing’s reputation and quell the increasing public criticism?

If there is nothing to morality but expressions of will, my morality can only be what my will creates. There can be no place for such fictions as natural rights, utility, the greatest happiness of the greatest number. I myself must now bring into existence “new tables of what is good.”

Friedrich Nietzsche[[41]](#endnote-41)

Exhibit 1: Salary Increases at Turing on Agenda



Source: *Developments in the Prescription Drug Market, Before the Full House Committee on Oversight and Government Reform*, 114th Cong. (2016) (related document “Turing Pharmaceuticals Salary Increases”), accessed January 27, 2017, https://oversight.house.gov/wp-content/uploads/2016/02/Salaries.png. Reproduced under 17 U.S. Code §105.

Exhibit 2: Approximate Price of Pyrimethamine in different countries

|  |  |
| --- | --- |
| Countries | Price (US$) |
| United States | 750.00 per tablet |
| Canada | 2.78 per tablet (imported from United Kingdom) |
| United Kingdom | 18.68 for 30 tablets\* |
| India | 0.04—0.10 for a pack of two tablets |
| Australia | 9.75 for 50 tablets\*\* |

Notes: \* £13 converted using exchange rate of £1 = US$1.4370 (effective date March 31, 2016); \*\*AUS$12.99 for 50 tablets converted using exchange rate of AUS$1 = US$0.75067 (effective date March 27, 2016).

Source: Created by the case authors from Karthick Arvinth, “Daraprim: Generic Version of Drug Costs Less than £0.07 in India,” *International Business Times*, September 25, 2015, accessed October 24, 2017, www.ibtimes.co.uk/daraprim-like-drug-costs-less-0-07-india-1521144; Michelle Roberts, “What’s a Fair Price for a Drug?,” BBC News, September 22, 2015, accessed October 24, 2017, www.bbc.com/news/health-34322720; “Daraprim 25 mg and/or Equivalents,” Canada Drugs, accessed October 24, 2017, www.canadadrugs.com/products/daraprim/25mg; “Daraprim 25 mg Tablets 50,” Chemist Warehouse, accessed October 24, 2017, www.chemistwarehouse.com.au/Buy/56166/Daraprim-25mg-Tablets-50.

Exhibit 3: Average Annual Increase in Branded Drug Prices and General Inflation

Note: CPI-U = consumer price index for all urban consumers

Source: Created by the case authors from Stephen W. Schondelmeyer and Leigh Purvis, *Rx Price Watch: Brand Name Prescription Drug Prices Increases by Double-Digit Percentage for Fourth Straight Year* (Washington, DC: AARP Public Policy Institute, December 2016), accessed January 13, 2017, www.aarp.org/rxpricewatch.

Exhibit 4: Price Spikes after Major Drug Deals

|  |  |  |  |
| --- | --- | --- | --- |
| **Drug** | **Acquirer** | **Price Change** | **Inflated Price (US$)** |
| Nitropress | Valeant Pharmaceuticals | >300% | 806/vial |
| Deflazacort | Marathon Pharmaceuticals | 6,000% | 89,000 |
| Ofirmev | Mallinckrodt Pharmaceuticals | >229% | 1,020 per 24 vials |
| Isuprel | Valeant Pharmaceuticals | 525% | 1,347 per vial |
| Vimovo | Horizon Pharma | >1,200% | 1,678 per 60 tablets |
| EpiPens | Mylan Inc. | 500% | 600 per pack of two |

Source: Created by the case authors from Jonathan D. Rockoff and Ed Silverman, “Pharmaceutical Companies Buy Rivals’ Drugs, Then Jack Up the Prices,” *Wall Street Journal*, April 26, 2015, accessed October 24, 2017, www.wsj.com/articles/pharmaceutical-companies-buy-rivals-drugs-then-jack-up-the-prices-1430096431; Matthew Herper, “Why Did That Drug Price Increase 6,000%? It's The Law,” *Forbes*, February 10, 2017, accessed March 31, 2017, www.forbes.com/sites/matthewherper/2017/02/10/a-6000-price-hike-should-give-drug-companies-a-disgusting-sense-of-deja-vu/#57bebc1d71f5; Michael Hiltzik, “Another Reason to Hate Mylan, Which Jacked Up the Price of Life-Saving EpiPens: It's a Tax Dodger,” *Los Angeles Times*, August 23, 2016, accessed September 2, 2017, www.latimes.com/business/hiltzik/la-fi-hiltzik-mylan-inversion-20160823-snap-story.html.

ENDNOTES

1. This case has been written on the basis of published sources only. Consequently, the interpretation and perspectives presented in this case are not necessarily those of Turing Pharmaceuticals or any of its employees. [↑](#endnote-ref-1)
2. All dollar amounts are in US$ unless otherwise stated. [↑](#endnote-ref-2)
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9. HIV/AIDS referred to human immunodeficiency virus (HIV) and the illness it caused, acquired immune deficiency syndrome (AIDS). [↑](#endnote-ref-9)
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13. Ibid. [↑](#endnote-ref-13)
14. Zoe Thomas and Tim Swift, “Who is Martin Shkreli—‘The Most Hated Man in America’?,” BBC News, September 22, 2015, accessed March 25, 2017, www.bbc.com/news/world-us-canada-34331761. [↑](#endnote-ref-14)
15. Ibid. [↑](#endnote-ref-15)
16. Ibid. [↑](#endnote-ref-16)
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24. Ibid. [↑](#endnote-ref-24)
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26. Ibid.; *Developments in the Prescription Drug Market* (statement of Nancy Retzlaff), op. cit. [↑](#endnote-ref-26)
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39. Democratic Staff, op. cit. [↑](#endnote-ref-39)
40. Rockoff and Silverman, op. cit. [↑](#endnote-ref-40)
41. Friedrich Nietzsche, *The Will to Power: An Attempted Transvaluation of All Values*, rev. ed. (1901; repr., New York, NY: Knopf Doubleday Publishing Group, 2011). [↑](#endnote-ref-41)