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OPINION

Drug shortages? Look to the middleman

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When you try to solve a problem you don't understand, you run a serious risk of making that problem worse. Congress may be in the process of doing this right now. A new bill would require drug manufacturers to notify federal officials of a disruption to a drug supply six months in advance.

"What we're trying to find out is whether there's a pattern behind the shortages that we can address," said Sen. Richard Durbin, D-Ill. "We've got to get down to what is really behind it and try to solve it."

Administration an opportunity to prevent the shortage, notify health care providers and develop a contingency plan. In reality, though, that's never been the problem.

The unreported problem is the role of group purchasing organizations. GPOs control the purchasing of more than $200 billion in drugs, devices and health care supplies annually for about 5,000 private, acute care hospitals nationwide. The good news is that they keep costs low. The bad news is that they are also permitted by law to charge a fee to hospital suppliers based on percentage of sales volume for a particular product.

Often, the fee is rather hefty -- as high as 25 percent of cost. That certainly throws a wrench into an already low-margin supply-and-demand proposition. For many of the suppliers, the accumulation of six months' supply at ever-lower margins becomes a nonstarter. Such a requirement would exacerbate the problem of shortages rather than solving it.

The GPO market is nearly a monopsony (a buyer's monopoly). Ninety percent of GPO-hospital purchasing is dominated by six firms. The power of these organizations is such that they can often dictate which drugs, devices and supplies are used in hospitals, and which companies are allowed to sell them. One of the unintended consequences is that incentives to manufacture low-margin products become smaller for large manufacturers and vanish for smaller ones.

As a result, drugmakers have little incentive to update old manufacturing facilities or build new ones. When a facility suddenly goes offline because of quality concerns (the major cause of supply line disruption) or is retooled for a different (and more profitable) use, shortages can occur.

The GPOs use a variety of practices that enhance their profits but exacerbate the problem of drug shortages. For example:

• Exclusionary, sole-source, long-term contracts;

• Tying and bundling product lines to give the advantage to large incumbent suppliers and discourage competition from smaller, entrepreneurial companies with fewer products;

• A byzantine system of manufacturers' rebates to large, favored distributors that ensures that only those distributors can sell to GPO-member hospitals.

These practices have created a concentrated market that excludes other existing and would-be suppliers and distributors. With no other suppliers able or available to fill the gap, increases in demand for generic drugs have resulted in shortages and surging prices. It is no coincidence that the problem of shortages is generally limited to generics sold to health care facilities through GPO contracts rather than directly to consumers through retail pharmacies. As former Wall Street Journal reporter Phil Zweig put it, "[T]hese cartels have undermined the laws of supply and demand in this critical industry."

While earlier and more robust communications between drug manufacturers (largely generic manufacturers of hospital injectables) and the FDA is important, the lack of such interaction is not the issue.

We applaud Durbin for striving to solve an important problem. We urge him to include not only drug manufacturers and the FDA in potential solutions -- but also our nation's giant group purchasing organizations.

Peter J. Pitts is president of the Center for Medicine in the Public Interest and a former Food and Drug Administration associate commissioner.

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