

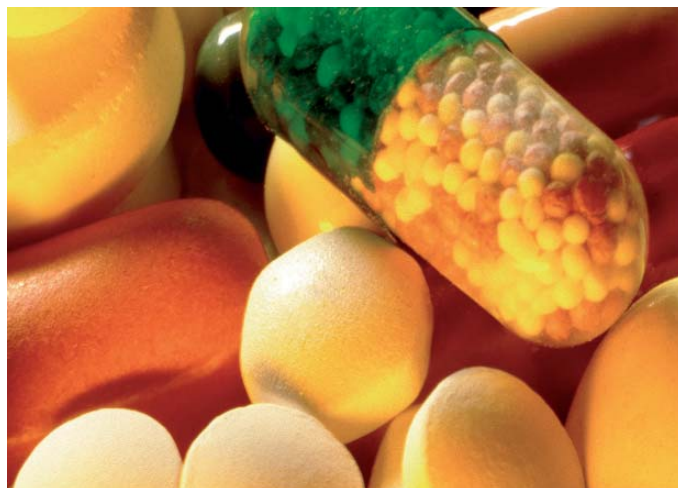
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Procuring medicines

— key issues for all pharmacy staff

By Allan Karr, MBA, MRPharmS

Budgetary pressures in the NHS mean that clinical pharmacists and other pharmacy staff may need to develop an understanding of drug procurement principles. This article describes some of these principles, including factors that affect the price of medicines



All pharmacy staff may find that they need to develop a basic understanding of the key drug procurement processes and the medicines supply chain in the NHS. With current budgetary pressures in mind, clinical pharmacists, in particular, are now more frequently asked questions about medicines supply and drug costs. Queries about the comparative costs of medicines, cost pressures (ie, volume change multiplied by price change), dates of patent expiries of branded medicines, changes in product selection and annual use are becoming common. The challenges faced in managing the “Payment by results” systems look set to increase the need for this knowledge.

Hospital medicine expenditure in the NHS is approximately £2.8bn per year, so a small percentage discount can potentially release significant savings for hospital trusts. There is a need for clinical pharmacists to add “cost efficiency” skills to their existing portfolio of clinical and other skills.

Procurement practices have always had the potential to impact on the work of clinical pharmacists since they affect the supply of medicines to wards and patients. However, the focus of trusts on saving money means that procurement services

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seem, at last, to have come of age. NHS managers are now seeing effective medicines contracting, in particular, as a key practice in their armoury to reduce overspent budgets.

Who procures medicines?

Experience has shown that an in-depth knowledge of medicinal products, suppliers, stakeholders and the clinical market is essential in order to take maximum commercial advantage of any potential medicines contract. Therefore trusts and regions currently employ specifically trained or experienced pharmacy procurement staff to ensure that this important pharmacy service is undertaken in a professional and competent manner and within trust clinical networks. It is worth noting that many independent consultancy firms and other organisations have seen an opportunity to capitalise on the demand for savings and are trying to establish if further savings can be made. So far it appears that they have identified limited, if any, savings to be made. This may be because of the skills of procurement staff and the effectiveness of existing systems which have already been in place at local, regional and national level for many years.

The medicines market is complex as there are many stakeholders involved who can all potentially affect the supply chain. A selection of issues are discussed in this article, to illustrate the complexity of medicines procurement and the supply chain and to help clinical pharmacists gain the knowledge they look set to need to know.

Contracting for medicines

The contracting process that trusts use will differ depending on whether the medicine is generic or branded.

Generic medicines Generic medicines can be defined in several ways. They can, for example, be described as products that have “lost their patent and are manufactured in large volume and at low cost”. These medicines are characterised as being in a competitive market and should consequently, in theory, have many suppliers. Recently, the NHS has been fortunate to have seen a number of major branded medicines lose their patents (eg, clozapine, paclitaxol, simvastatin and omeprazole). Branded products have a 20-year patent period so there will always be new generics entering the market and savings released. Whether or not these savings should offset the cost of the new branded products that are regularly entering the market is regularly debated.

Past and existing generic contracting arrangements aim to maximise purchasing power by developing collective arrangements between trusts. Over the past few years, procurement tendering at a regional level has been superseded by tendering at a national level under the direction of the Supply Chain Excellence Programme (SCEP) which was instigated by the Department of Health (see p397).

In England, the SCEP generic contracts are administered by the NHS Purchasing

and Supply Agency (NHS PASA). Tenders from suppliers hoping to sell medicines to the NHS are administered by NHS PASA. Regional pharmacy procurement staff adjudicate the contracts, together with quality assurance pharmacists, on behalf of individual trusts. Adjudication of tenders, although mainly based on the tendered price, also takes into account other factors such as packaging and labelling and the efficiency of the supplier's customer support services.

Such is the effectiveness of the nationally co-ordinated generic contracting process, that the prices offered can occasionally be driven too low, which can force suppliers out of the market or make the market unattractive for new entrants. The national Pharmaceutical Market Support Group (PMSG) has systems in place that aim to ensure that a sufficient number of suppliers are in the market for each product and that competition is fair and appropriate.

Following adjudication, NHS PASA provides details of the contract and any subsequent amendments electronically so that they can be used by trusts to update their pharmacy computer systems. Updating can take a considerable time, because of the potential number of changes to suppliers and prices that need to be incorporated. Delays in doing this, however, can cause unnecessary invoice queries and can result in trusts not taking advantage of new lower prices. Therefore it is important that trusts have adequate staff resources within their pharmacy department to complete this task within the agreed time frames.

All trusts should adhere to generic medicine contracts. Failure to do so will result in reduced volumes being sold by suppliers and thus increased prices.

From experience, fragmented procurement arrangements also serve to confuse suppliers and to increase risk to trusts, because adequate product quality assurance support may not be in place. Non-adherence to generic contracts is therefore being monitored by the PMSG. A data monitoring system called PharmEx has been developed by NHS PASA, which is able to collect purchasing information directly from hospital pharmacy computer systems on a monthly basis. Benefit tracking and contract adherence tables can then be provided to every hospital's purchasing department for monitoring purposes and to enable auditing.

Some trusts also undertake their own local validation of the data generated by PharmEx to calculate annual savings. This approach will ensure improved data accuracy, especially if the data is to be used directly to impact on medicines budgets or be added to procurement saving targets.

Branded medicines Contracting for branded (ie, patented) medicines is perhaps more complicated than generic tendering. A number of patented products have no

competition (ie, they have a monopoly) or have limited therapeutic competition (ie, they are in an oligopoly). Those involved in contracting for branded medicines will need to ensure that prescribers and other key stakeholders are an integral part of the decision-making process or are, at least, willing to comply with the adjudication decision. In light of the difficulty of getting consensus views with many prescribers, adjudication for branded medicines tends to take place at local or consortia level.

When contracting for branded medicines it is important to establish the extent to which different products can be used to treat the same clinical condition (ie, the level of interchangeability). Close negotiations are required with stakeholders such as the pharmaceutical industry, prescribers, the clinical directorate, primary care trust and formulary pharmacists. A clear understanding of medicines management, stakeholders views, clinical issues and industry marketing practices, such as product differentiation techniques, will assist NHS staff in this type of contracting process.

Public procurement law The procurement by public bodies (ie, NHS hospitals) of products or services that are valued above a certain amount is regulated. The law is intended to ensure that the EU's public procurement contracts are not constrained by national policies and are open to the widest competition.

The threshold for EU contracting rules is approximately £100,000 depending on the pound to Euro exchange rate. Amounts below this threshold still need to be tendered in line with general EU principles (including non-discrimination, transparency and proportionality). Trusts will therefore have developed their own local standing financial instructions or orders to ensure compliance with all of the relevant public procurement regulations.

Contracts subject to EU regulation are advertised by the form of an EU notice. This states which of the three main award procedures applies: open procedure, restricted procedure or negotiated procedure. Each of these procedures has its own rules and contract time frames.

Those without experience of EU procurement laws may view them as daunting. However, they can be simplified if the key principles can be understood. The key principles are:

- Be open and transparent and explain to suppliers what you are going to do and how you will do it
- Ensure that suppliers are treated equally — all suppliers should have a fair and equal chance of winning a contract
- Be consistent with any action and do what you said you would do

— Stock holding

Although "just in time" delivery systems may have proved useful for some manufacturing industries, demand and supply must be totally predictable for these systems to work effectively — a situation not found in the medicines supply chain where, for example, supplier product shortages are common.

There is a need for stocks of medicines to be stored in appropriate facilities in dispensaries and wards to ensure that patients receive these critical supplies when needed. Items of stock are treated by trust accountants as though they are "cash" because they are not fixed assets. Pressure may therefore be exerted to keep stock holding to a minimum. Stock levels should be reviewed regularly, especially those relating to slow-moving (ie, infrequently used) bulky, expensive or short-dated items.

The average stock holding for the hospital pharmacy sector appears to be about one month's supply. This figure can also be expressed as a stock turnover of 12 times per year. Experience has shown that reducing stock levels below this, and therefore increasing the frequency of stock turnover, may help the cash flow position but can be detrimental in other ways (eg, resulting in increased orders, more invoice queries and an increased risk of becoming out of stock, particularly if a shortage occurs).

— Medicine pricing

Branded medicines The national prices of all new branded medicines are established at their launch as part of the Pharmaceutical Price Regulation Scheme (PPRS). This voluntary scheme is managed by a section of the DoH following five-yearly negotiations between the Government and the Association of the British Pharmaceutical Industry. PPRS is intended to balance the needs of a variety of stakeholders:

- Pharmaceutical companies — want to cover their research and development costs and generate profit for shareholders and for further research to bring more medicines onto the market
- Government — wants pharmaceutical companies to invest in UK facilities and, for example, to receive taxes from enhanced export sales
- NHS — wants to obtain affordable new medicines

The UK is often used as a reference source for other EU countries' pricing systems. Pricing in the UK can therefore be critical to a supplier. After product launch, any price increase can only be obtained by a manufacturer following agreement with the DoH. Manufacturers can modulate prices between products in their portfolio to achieve their market objectives.

The last round of PPRS negotiations achieved an overall medicines price reduction of 7 per cent for the NHS. Any hospital contracting needs to be considered in light of these negotiations.

Unlike Drug Tariff prices in primary care, Hospitals' medicine prices include VAT. This cost variation may immediately disadvantage the hospital sector if they do not receive similar or greater discounts from suppliers.

Price discounts Pharmaceutical companies are sometimes prepared to offer a range of discounts to hospitals and primary care trusts in order to promote their products and increase sales. Discounts may increase the market size for the supplier or take market share from their competitors. The discounting mechanism should, under EU procurement law, be transparent and be applied to all purchasers in a market segment. Examples of the types of discounts offered include:

- Settlement discounts (price reductions given for timely payment)
- Quantity discounts (reductions for ordering large volumes)
- Seasonal discounts (eg, to meet a supplier's year-end targets)
- Loss-leader pricing (very low prices offered to break into new markets)
- Sliding-scale discounts (variable pricing depending on the quantity purchased)
- Captive-product pricing (eg, discounts given on a blood glucose meter to encourage purchase of the blood glucose strips)
- Discount to compete against parallel imports

"What is the price of a medicine?" is the most frequently asked question by trust managers. A medicine may have many different prices (see Panel 1).¹ A clear understanding of what price is required and where the pricing data can be found is essential to answer this question properly.

Stock valuation Medicine prices are not always fixed.² Product prices vary over time. A lower price may become available through favourable contracting or prices may increase. It is therefore important to establish what the value of a product is if the stock has been purchased at different times with different prices.

There are two legal methods of valuing the stock due to price variations. These are:

- AVCO (average cost)
- FIFO (first-in, first-out)

For the AVCO method, the average value of all stock is established. This price may not reflect any of the purchase prices and is automatically calculated using trusts' com-

Panel 1: Different prices of medicines

- Price with or without VAT
- Standard hospital discount price
- Special contracted hospital price
- NHS tariff price with or without VAT
- Standard monthly pack price or other pack type (eg, bulk pack)
- Prepack or overlabeled pack price with the cost of this overhead included
- Price with or without dispensing fee and other overhead cost
- Home delivery price
- Average stock value or first-in stock price
- Price during clinical evaluation of product or clinical trial

puterised stock management systems. Sometimes AVCO prices take several months to settle down to match the true purchase cost, especially if infrequent bulk purchasing occurs. Average prices often include VAT.

For the FIFO method, the price follows the stock through the supply chain. The first stock issued to a cost centre will not be the same price as that of the last stock purchased. Stock issued from different pharmacy areas, such as distribution and the dispensary, may therefore have different prices for the same product.

Benchmarking Benchmarking is a useful practice to compare the procurement efficiency of different organisations. However, a thorough knowledge of the causes of price variances is necessary. Also, the accuracy of comparator price data needs to be established to adequately benchmark prices between any two organisations. In the past, common errors in benchmarking practices have been made. Some of these have been made by experienced management consultancies.³ These can give the wrong impression of the efficiency of the pharmacy service. These common benchmarking errors include:

- Using the wrong price, for example, using the "off-contract" price (caused by suppliers' failure to supply), instead of the contract price
- Not taking the timing of contracts and market changes into account
- Not taking into account low use of a product versus the benefits of a contract
- Not being aware of whether or not prices include VAT
- Not comparing different pack sizes and presentations of medicine accurately
- The AVCO price being mistakenly compared with the FIFO price

Management and financial accounting

All purchased products or services are managed by the financial accounting team within a trust. The responsibility of this team is to ensure that the externally-based financial systems of a trust, such as those with their suppliers and purchasers, are both accurate and appropriate. Financial management systems will focus on a trust's year-end financial reports. The yearly pharmacy medicine stock take and invoice matching processes are important issues for the financial accounting systems.

Once funds become available to the trust through the financial systems, senior managers decide how the funds should be applied to the different cost centres. Management accountants assist senior managers by the allocation of monthly pay and non-pay budgets. These budgets can be altered according to the business needs of the trust and are applied not just to pharmacy but to all significant cost centres.

A financial coding system, which may incorporate specialist centres, consultants, wards and departments can be used to ensure that internal medicines charges are transferred to specific budget holders. As trusts change their clinical structures, their coding systems will alter. It is therefore important that pharmacists ensure that accurate medicine charges, part of the directorates/consultants' non-pay costs, are made to the correct cost centres through the right coding structure.

Conclusion

Procurement and supply chain management may not be high on the priority list of clinical pharmacists, but it does appear to be of great importance to trust managers. In order to achieve beneficial financial savings for trusts, a close partnership between clinical pharmacists and pharmacy procurement professionals is essential. Such a working relationship may already exist in some trusts. Other trusts may look to developing this cultural relationship.

Clinical pharmacists will also need to extend their existing skills base and take the time and trouble to understand more about procurement and the supply chain. The new learning required by clinical pharmacists in this speciality is fast becoming an essential requirement to satisfy the cost-efficiency demands as well as the clinical effectiveness demands of the new NHS.

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