

Who Makes Money on Epidemics of HIV/AIDS and Tuberculosis in Ukraine



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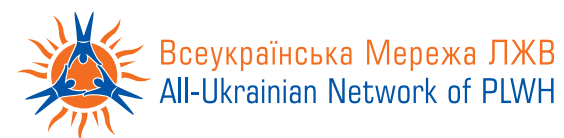
The AntAC welcomes any comments from the government agencies and entities mentioned in the report, shall they find any evidential inaccuracies.

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The book is issued in English and Ukrainian in print and electronic versions. The electronic version of the publication is presented on the AntAC website: <http://antac.org.ua>. The printed book is distributed free of charge. Reference to AntAC is obligatory if using the texts of the report.



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WHO MAKES MONEY ON HIV/AIDS AND TUBERCULOSIS EPIDEMICS IN UKRAINE?

Interim Report. November, 2013. Kyiv

Corruption, staged competition, abuse of commercial secrets, and speculations over the official status prevent Ukraine from overcoming the epidemics of HIV/AIDS and tuberculosis (TB), both of which have threatened the country's national security. This is the conclusion analysts at the Anticorruption Action Centre (AntAC) came to after monitoring the public procurement of medicines for HIV/AIDS and TB in 2013.

According to the Constitution, the government of Ukraine is responsible for ensuring that all citizens have access to effective and affordable medical care. Despite this obligation, the government does not provide adequate funding to purchase essential HIV/AIDS and TB medications. Moreover, the government uses limited existing resources to purchase medications at prices above market value. As a result, thousands of critically ill Ukrainians do not receive the necessary therapy they need to survive.

While most medications for HIV/AIDS and TB are produced by foreign companies, neither the producers nor their authorized representatives take part in government tenders. In 2013, only 6 out of 6,500 pharmaceutical companies authorized for trading participated in the public procurement of antiretroviral agents (ART), sharing among themselves the market of \$30.9 million USD¹.

There are no occasional winners of public procurement tenders for HIV/AIDS and TB medicines. Intermediaries (“shell companies”) participate in a number of schemes to ensure they win bids, often in collaboration with the Ministry of Health of Ukraine (MoH), law enforcement and regulatory agencies. These companies stage competition in order to profit from multi-million government tenders. Moreover, after receiving payment, shell companies often do not supply medications in time, which disrupts therapy regimens and endangers the lives of patients.

This report from the AntAC describes in detail four ways by which taxpayers' money ends up in the private pockets of pharmaceutical company owners in Ukraine:

1. Staging tenders among multiple companies controlled by one actual (beneficial) owner
2. “Cartel agreements” between companies that belong to different beneficial owners but collude to win bids and increase profits
3. Conversion of the state pharmaceutical factory “Indar” into a shell company that purchases pharmaceuticals from offshore companies and sells them to the MoH at unreasonably high prices
4. Use of the Register of Bulk Release Prices, which serves to regulate drug prices, to overestimate tender prices.

The scale of fraud affecting the public procurement of medicines in Ukraine is impressive, even to experienced anti-corruption experts. For example, a ten-month old company “Sky Pharm” managed to win government tenders worth \$7.3 million USD for supplying ART and TB agents. Another company “Indar” got half of the funds that were allocated for state procurement of medicines (\$21.7 million USD) immediately after entering the market. If the current public procurement process does not change soon, the lives of hundreds of thousands of people living with HIV/AIDS and TB will be at risk. Thus, AntAC advocates for amending legislation to close loopholes and stronger civil society monitoring of public procurement procedures.

AntAC experts suggest a series of comprehensive solutions at the local, national and international levels that will help reduce prices for medicines in Ukraine and improve access to therapy for patients. These suggested measures are described in this report. Proposed legislative changes include a review of the system used for regulating the prices of medicines, reforming public procurement laws and creating a register of beneficial owners of companies.

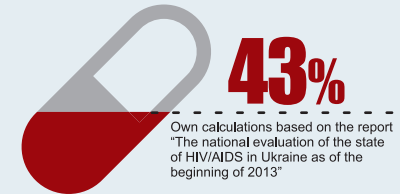
Furthermore, legislation amendments should focus on the creation of more favorable conditions for civil society monitoring and control over public procurement as this tool already proved its efficiency. For example, over the last six months, AntAC has successfully reduced the value of public procurement tenders of the State Penitentiary Service (SPS) by 2.5 times, saving Ukrainian taxpayers' \$0.2 million USD on the purchase of medicines. AntAC lawyers, in cooperation with Members of Parliament (MPs) representing the Global Organization of Parliamentarians Against Corruption (GOPAC)², also initiated two criminal proceedings and seven investigations of suspected fraud. Therefore, it is important that international organizations combating HIV/AIDS and TB make a special effort to encourage civil society oversight for the public procurement of medicines.

This report contains the interim results of AntAC's monitoring activities and analysis of the drug procurement process in Ukraine. Certain questions in this report are left open-ended in order to facilitate discussion. This report aims to draw attention to the abusive practices of various parties (e.g. MoH officials, law enforcement, regulatory agencies, pharmaceutical shell companies and beneficial owners) with respect to the public procurement of medications. The goal of the report is to reduce over-inflated prices for essential medicines by eliminating shadow schemes of public procurement of ART and TB agents. Corruption in health care is particularly detrimental to the health of the population; abusive procurement practices must be eliminated in order to prevent more lives from being lost.

AntAC is open to amending this report if any concerned parties can present evidence contrary to our findings.

Drug supply for patients

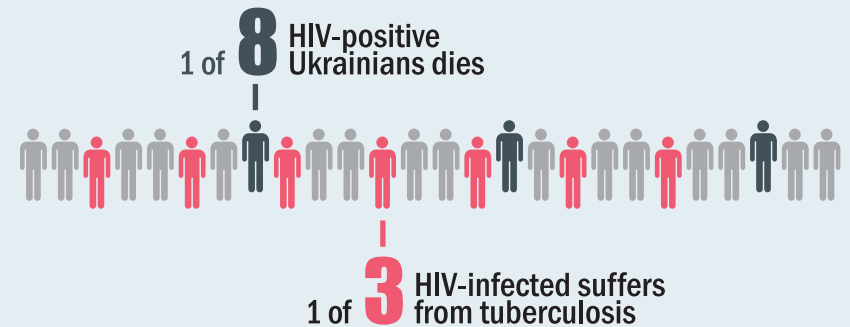
HIV/AIDS



Tuberculosis

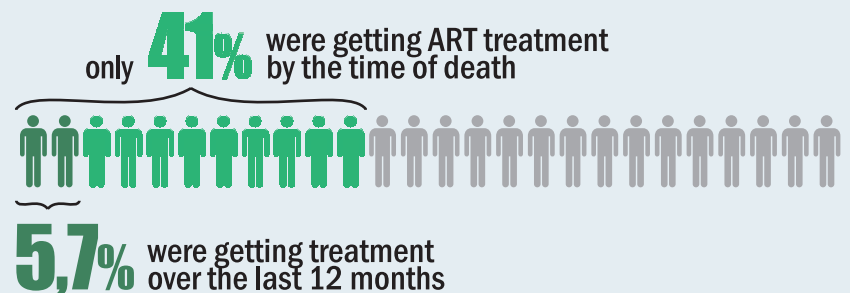


Mortality from HIV/AIDS



Mortality and Treatment

Among 100% of HIV-positive who died in the first half of 2013



1.

EPIDEMICS THAT KILL: THE SPREAD OF HIV/AIDS AND TB IN UKRAINE

The spread of HIV/AIDS in Ukraine is one of the fastest-growing epidemics in Europe. Various estimates indicate that 0.6-1% of the population is infected; only Russia have a higher percentage of people living with HIV³. Similarly, the spread of TB in Ukraine is the second highest in Europe after Russia⁴.

Official statistics indicate that there were 219,862 people living with HIV⁵ and 61,749 people living with TB⁶ in Ukraine in 2012-2013. In sum, this is equal to the populations of such Ukrainian oblast centers as Zhytomyr, Ivano-Frankivsk or Poltava.

One of eight HIV-positive in Ukraine dies⁷, and one out of three HIV-positive patients also has tuberculosis⁸. The HIV/AIDS epidemic reached its concentrated stage 16 years ago⁹. According to international criteria, the concentrated stage of an HIV epidemic is characterized by steady virus expansion of at least 5% in one or more at-risk social group¹⁰. Although official publications declare that the rate of transmission among general population has declined, studies indicate a dangerous trend: increasing HIV transmission through sexual contact among the general population. This way of transmission is slower, but it is more dangerous because it involves a larger number of people¹¹. In other words, once the epidemic breaks away from at-risk groups and spreads to the general population, strategies for fighting and preventing HIV/AIDS will become more complex.

The epidemic of TB in Ukraine began in 1995. Since then the number of people with TB has tripled¹². One TB-infected patient can infect 10-15 persons in one year¹³; making TB a serious threat to the national security of Ukraine¹⁴. High rates of HIV/AIDS and TB transmission not only constitute a significant threat to the population of Ukraine but also neighboring countries.

Timely and effective treatment for HIV/AIDS and TB

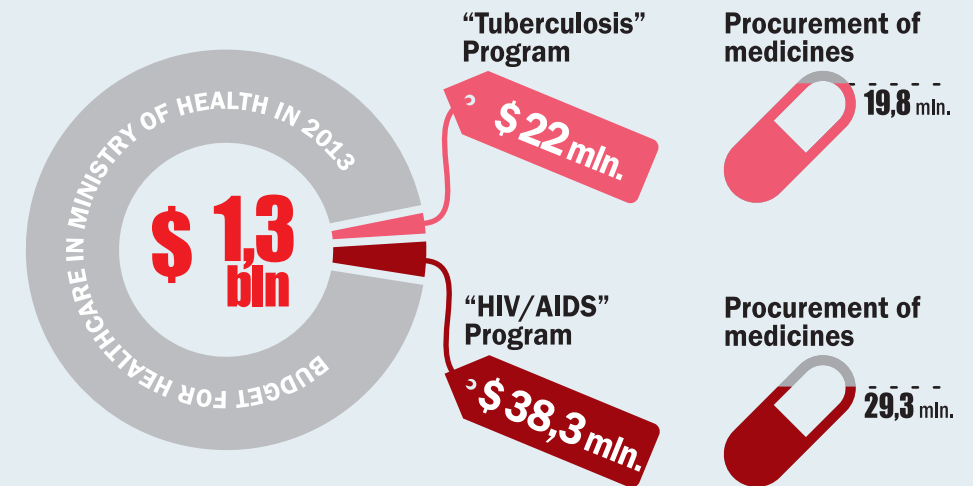
is the key to preventing the spread of both epidemics. In both cases, therapy is contingent upon patients' continuous access to quality medications.¹⁵ In Ukraine, the government is fully responsible for the provision of such medications, as the Constitution guarantees every citizen the right to free medical services.¹⁶

Despite this, Ukraine provides only 43% of necessary medications for HIV patients¹⁷ and 88.3% for TB patients¹⁸. Moreover, medications purchased by the government are often not delivered in time, causing a delay in therapy.¹⁹ Statistics indicate that, among all HIV-positive people who died in the first half of 2013, only 5.7% were continuously receiving ART treatment over the last 12 months, and only 41% were receiving ART treatment at the time of their death²⁰.

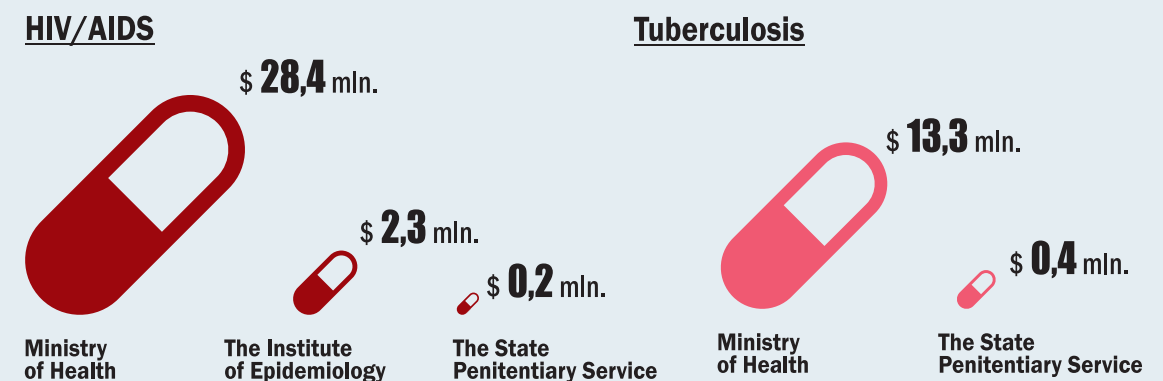
In the structure of Government, the MoH is responsible for the provision of medications in Ukraine.²¹ In 2013, the overall budget for health care in MoH was over \$1.3 billion USD.²² The allocated budgets for HIV/AIDS and TB were \$38.2 and \$21.9 million USD, respectively. Specifically, \$31.8 and \$19.8 million USD of these totals were spent on drug procurement.²³ However, funding is still not enough to provide therapy to all HIV/AIDS and TB patients in Ukraine due to unreasonably high prices of public procurement. The current system of public procurement and distribution of medications across governmental agencies is partly responsible for this situation.

The high spread of HIV/AIDS and tuberculosis in Ukraine has increased epidemiological risk to the general population not only in Ukraine but also in the neighboring countries.

Funds for treatment in Ministry of Health



Who procured medicines in 2013



The Institute of Epidemiology – the government institution "L.V.Gromashevsky Institute of Epidemiology and Infectious Diseases"

2.

SUMMARY OF ANTAC ACTIVITIES: CIVIL SOCIETY CONTROL OVER PUBLIC PURCHASES

The MoH regularly claims that the budget for programs targeting HIV/AIDS and TB is insufficient.²⁴ However, inefficient use of available resources is also a very important factor. In particular, appropriated funds disappear at the stage of purchasing medicines. As a result, patients do not receive life-saving treatment, allowing HIV/AIDS and TB to continue to spread. At the same time, money ends up in the pockets of private parties who benefit from these epidemics. Experts of the AntAC came to this conclusion after thoroughly analyzing the public procurement of medicines for HIV/AIDS and TB.

In early 2013, the AntAC initiated civil society oversight over the public procurement of medicines. Efforts were directed toward monitoring the process of public procurement of medicines for HIV/AIDS and TB, challenging discovered violations and cases of inefficient spending from the state budget, and examining the structure of pharmaceutical company-supplier ownership. Assisted by members of the national chapter of GOPAC, AntAC experts demanded that law enforcement and regulatory agencies react to these alleged violations.²⁵

AntAC lawyers monitored the procurement of HIV/AIDS and TB medicines by designated institutions, specifically the MoH, SPS, and the government institution “L.V.Gromashevsky Institute of Epidemiology and Infectious Diseases” (the Institute of Epidemiology). As of 30 September 2013, these institutions spent \$49 million USD on the procurement of drugs, which comprises 87% of all resources allocated to purchase of medicines for HIV/AIDS and TB in the 2013 state budget.²⁶

Public procurement is an open process and information is available to a wide audience. In

most cases it includes the following stages: announcing a competitive bid, accepting applications, defining and announcing a winner of the competitive bid, and signing a contract with a winner. The main criterion when selecting the winner is the lowest offered price.²⁷ The information and the supporting documentation related to public procurement are published on the official web portal for public procurement issues.²⁸

To collect additional information on some bidders, AntAC’s analysts addressed companies such as “Indar” closed-JSC, “Abbot Laboratories”, and profile state institutions.²⁹ With a separate appeal AntAC’s analysts also managed to receive the reports of the Accounting Chamber of Ukraine.³⁰

AntAC lawyers systematically analyzed all documents published at every stage of the competitive bidding process (39 public procurement biddings in total).

Simultaneously, AntAC analysts examined the ownership structure of the companies participating and winning tenders for the procurement of HIV/AIDS and TB agents. We analyzed information published in the Ukrainian and foreign media databases³¹, as well as investigative reports by journalists, particularly those of Nashi Groshi³². Preliminary results of the analysis indicate that most public purchases of HIV/AIDS and TB agents were staged by a limited number of companies that allegedly coordinate their actions.

Monitoring resulted in an unveiling of a series of systematic problems, including alleged “cartel agreements” and inflated prices of ART and tuberculosis medications. With the assistance

of MPs-members of GOPAC, the AntAC submitted 60 claims to different law-enforcement and regulatory bodies (such as the State Financial Inspection of Ukraine, Antimonopoly Committee of Ukraine, the Ministry of Economic Development and Trade of Ukraine, and the Prosecutor General’s Office of Ukraine) challenging alleged violations of public procurement law and laws on conflicts of interest.³⁴ Additionally, AntAC’s lawyers submitted 37 information inquiries to regulatory agencies and government institutions that procure drugs.

3.

THE PROBLEM OF OVERPRICING

During monitoring, the AntAC identified two important and interconnected problems in the field of public procurement of ART and TB agents: (1) most purchases were made at over-inflated prices due to a lack of competition, and (2) alleged secret deals took place between tender bidders.

The problem of government institutions purchasing medications at over-inflated prices has been relevant to Ukraine for a long time. The prices for particular medicines purchased by the MoH in 2012 were 150-300% higher as compared to prices for similar medicines purchased by patients' organizations (e.g. the charity foundation "the All-Ukrainian Network of PLWH"). The AntAC determined that \$4.9 out of \$21.9 million USD were wasted on over-inflated prices in 2012. In 2013, \$2 out of \$7.3 million USD were wasted.^{35 36}

It is also important to note that patient organizations in Ukraine purchase a limited number of medicines; therefore, the AntAC cannot conduct a whole-scale price comparison. However, in every case examined, the government grossly overpaid for medications when compared to non-governmental organizations (NGOs). This indicates that government tenders are likely to have over-inflated prices in cases of other ART and TB agents, too.

One of the reasons why the prices are over-inflated for public procurement tenders is the absence of competition. The circle of tender winners of all ART agents purchased this year is restricted to only six companies that divided among themselves the market worth of \$30.9 million USD.³⁷ Similarly, the tenders for TB agents totaling \$13.6 million USD were won by only eight companies. This system is unacceptable, especially considering that there are 6,500 companies authorized for wholesale and retail pharmaceutical trade. Since only a limited number of companies participate in tender procedures, they can control the prices of medications purchased by the government with money from Ukrainian taxpayers.

Furthermore, even though there are 116 pharmaceutical companies authorized for producing medications³⁸, the manufacturers are virtually not represented in the list of tender winners. National pharmaceutical producers have not won a single tender for ART agents. Similarly, three Ukrainian manufacturers of TB medications received only 9% of all relevant public procurement tenders organized by the MoH this year.³⁹

Most HIV/AIDS and TB medications purchased by government are produced by foreign companies.⁴⁰ None of these producers or their authorized dealers participates in Ukrainian tenders⁴¹ because they do not want to run the risk of being associated with corrupt practices, which will damage their reputation and necessitate international sanctions. For this reason, foreign manufacturers sell medicines to intermediary shell companies that are familiar with doing business in Ukraine, specialize in winning public procurement tenders, and can properly prepare bidding applications in Ukrainian.

Intermediary companies control pharmaceutical procurement in order to provide their owners with super-profits. Owners collude with other organizations to divide the market, stage competition and win bids. Thus, the winners of the tenders are determined in advance.

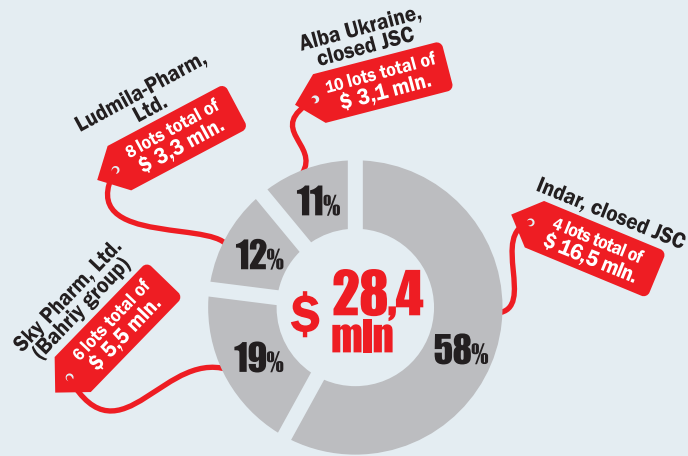
AntAC experts have defined four ways in which companies game the drug procurement system in order to win bids:

- a) "competition" among companies registered by one actual (beneficial) owner;
- b) staged competition among companies that compete for tenders with predetermined outcomes (called "cartel agreements");
- c) intermediary companies claiming national producer's status ;
- d) using the State Register of Wholesale Prices for Medicines as justification for submitting bids with intentionally over-inflated prices for medicines

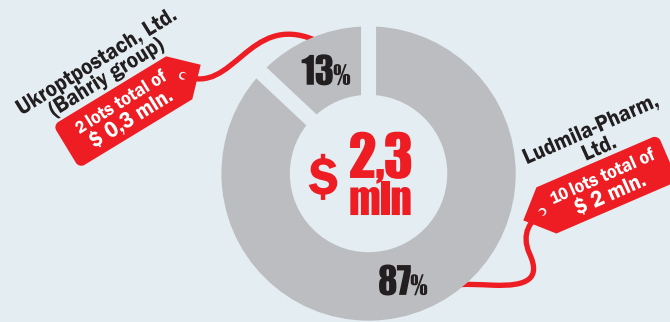
Details about each of the schemes above are discussed in the following sections below.

Public Procurement Priorities for ART Agents

Public Procurement by the Ministry of Health



Public Procurement by the Institute of Epidemiology

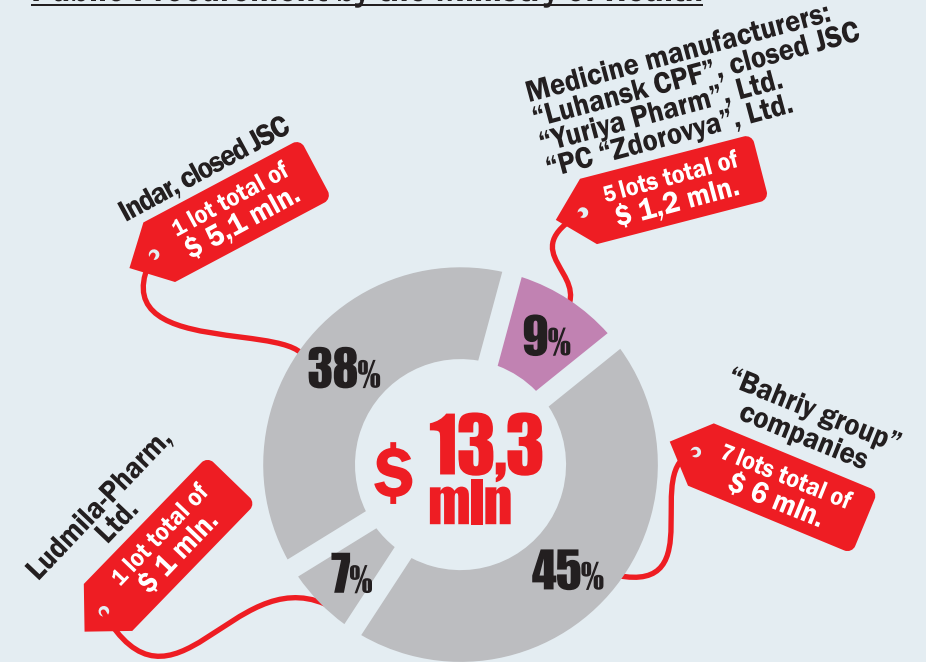


Public Procurement by the State Penitentiary Service



Public Procurement Priorities for Tuberculosis Agents

Public Procurement by the Ministry of Health



Public Procurement by the State Penitentiary Service



4.

“COMPETING WITH MYSELF”: COMPETITION AMONG THE COMPANIES OF THE “BAHRIY GROUP”

In 2013, 19.4% of public procurement tenders for ART agents (totaling \$6 million USD) were won by three companies: “Ukroptpostach” Ltd, “Sky Pharm” Ltd, and “Pharmadis” Ltd. These same companies also won almost a half (47%) of tenders for TB agents (totaling \$6.4 million USD).⁴²

These three companies are controlled by one person, Mr. Petro Bahriy, who presides over the Ukrainian Association of Medicines Producers and is also a member the Council of Entrepreneurs by the Cabinet of Ministers of Ukraine.⁴³

In 2008, Mr. Petro Bahriy and the companies he controls were referenced in a controversial report prepared by Mr. Volodymyr Konovaliuk commissioned by the Verkhovna Rada Committee on Health Care (hereafter called Konovaliuk’s report). Konovaliuk’s report describes in detail how, between 2005 and 2007, nearly half of funds budgeted for health care were allegedly stolen and laundered by Mr. Bahriy. According to the report, the companies controlled by Mr. Bahriy carefully controlled their actions and had a collaborative action plan for the public procurement of medicines. As a result, the price of TB agents was 2-3 times as high (and sometimes as much as 22 times as high) as prices in similar neighboring countries.⁴⁴

Since 2008, the situation has not changed much: Mr. Bahriy’s companies still bid with over-inflated prices and keep winning ART and TB tenders with the MoH, SPS, and Institute of Epidemiology. Occasionally, Mr. Bahriy changes names of the companies or creates new ones to provide the illusion of competition in public procurement tenders.

The results of the AntAC’s investigation as well as journalists investigations demonstrated⁴⁵ that “Pharmadis” Ltd, “Ukroptpostach” Ltd, and “Sky Pharm” Ltd registered between 2010 and 2012⁴⁶ are controlled by Mr. Bahriy. They are also connected to the companies that were referenced in Konovaliuk’s

report as those controlled by Bahriy: “HANSA” Ltd, “Regional Pharmaceutical Drugs” Ltd, and “Sumy Pharmacy Company” Ltd.

“Pharmadis” Ltd. has the same phone number as “HANSA” Ltd founded in 1991 by Mr. Petro Bahriy himself.⁴⁷ Moreover, “Pharmadis” Ltd was founded by Mr. Serhiy Siora. Mr. Siora used to be one of formal owners of “Sumy Pharmacy Company” Ltd, which was officially registered as a company founded by “HANSA” Ltd until 2006.⁴⁸ In 2013, “Pharmadis” Ltd won 4 out of 14 MoH tenders for procurement of TB agents after competing with “Ukroptpostach” Ltd, another member of Bahriy’s group.⁴⁹

“Ukroptpostach” Ltd was founded in January 2011.⁵⁰ Until April 2012, the company was registered at 100-b Kirovohradska Street, Kyiv.⁵¹ Previously, this address was also used by other companies from the same group, including “Lumier Pharma” Ltd and “Regional Pharmaceutical Drugs” Ltd.⁵² Between March 2012 and September 2013, these companies won tenders worth \$26.6 million USD.⁵³ “Ukroptpostach” Ltd competed exclusively with other companies representing Bahriy’s group, including “Pharmadis” Ltd.⁵⁴

In September 2012, “Sky Pharm” Ltd was founded by a citizen of Russia, L.O. Kuzmin, with a statutory capital of 100,000 USD.⁵⁵ Within one year, “Sky Pharm” Ltd won public tenders totaling \$9.3 million USD, including \$7.3 million USD for HIV/AIDS and TB agents. “Sky Pharm” Ltd took part in nine tenders for ART and TB agents and won all of them; the company’s one and only competitor was “Pharmadis” Ltd.⁵⁶

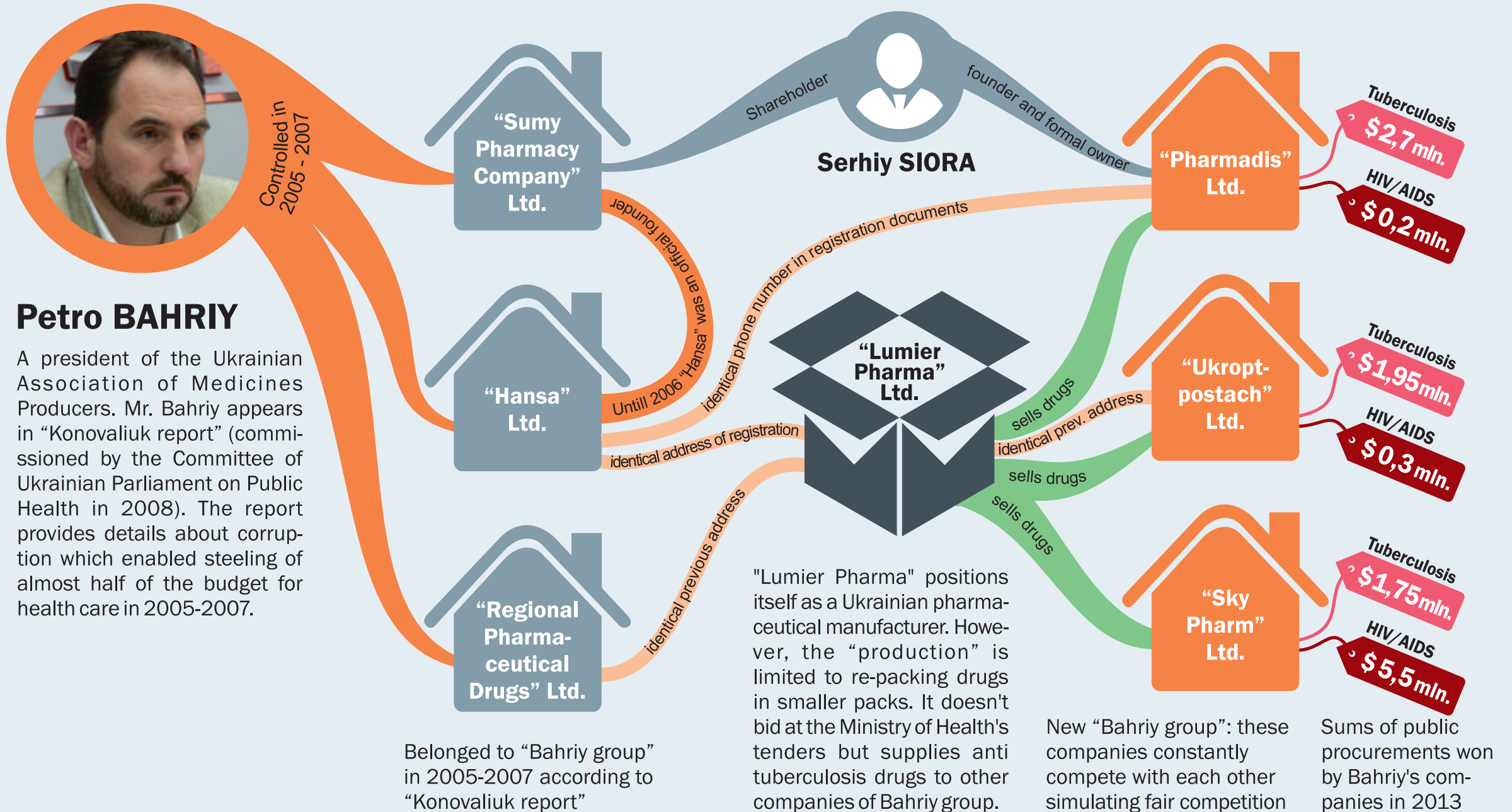
In many cases, Bahriy’s intermediary companies are bidding with the medicines “produced” by “Lumier Pharma,” which belongs to Mr. Bahriy and is registered as a pharmaceutical manufacturer.⁵⁷ Ukrainian legislation allows companies that re-pack medicines to be defined as manufacturers.⁵⁸

“Lumier Pharma’s” website says that the company only packages and re-packages medicines,⁵⁹ and that one of their main partners is “Hansa” Ltd.⁶⁰ Additionally, as of 18 September 2013, the registered address of “Lumier Pharma” coincides with that of “Hansa” Ltd. and “Regional Pharmaceutical Drugs” Ltd.⁶¹

Three companies mentioned above - “Ukroptpostach” Ltd, “Sky Pharm” Ltd, and “Pharmadis” Ltd - have taken leading positions in the market of ART and TB agents almost immediately after registration. They do not manufacture any medicines and compete exclusively with themselves. The role of second competitor is formal. According to Ukrainian legislation, a minimum of two bidders is necessary for the bidding process to be valid. How can we talk about fair competition if the two competing companies have the same beneficiary owner?

Under such conditions, national and international manufacturers are out of public procurement of medications in Ukraine. As a result, taxpayer money is directed into the pockets of a limited group of selected persons by means of corrupt schemes.

“Bahriy Group”: Pseudo Competitors in Public Procurement



Competitive Bidding for Public Procurement

in HIV/AIDS and TB among “Bahriy group” companies

Sky Pharm,
Ltd

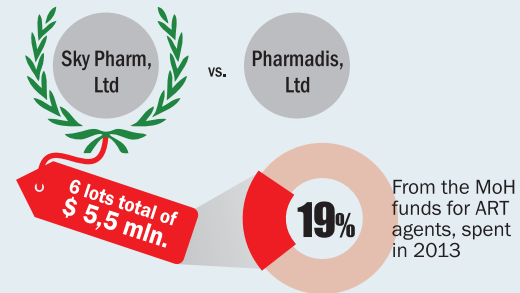
Pharmadis,
Ltd

Ukropt-
postach,
Ltd

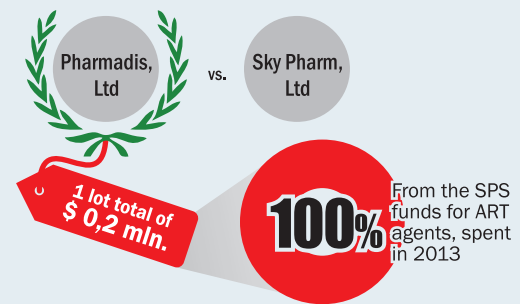
Three clones companies controlled by Mr. Petro Bahriy regularly participate in public procurement bidding for ART and TB agents. By faked in competition they divide a part of tenders between themselves.

HIV/AIDS Medications

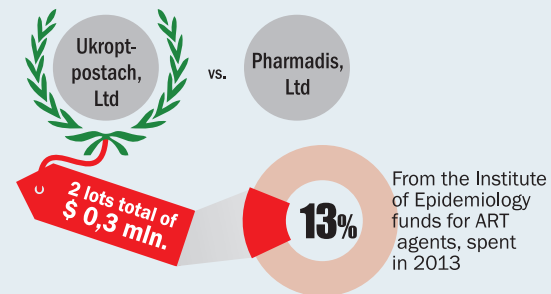
Public Procurement by Ministry of Health



Public Procurement by the State Penitentiary Service

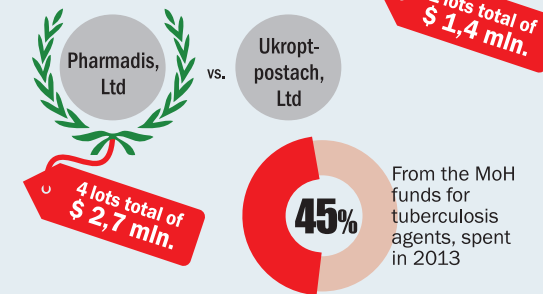
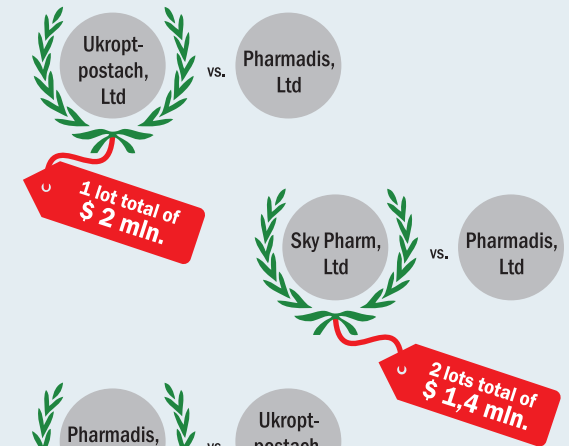


Public Procurement by the Institute of Epidemiology

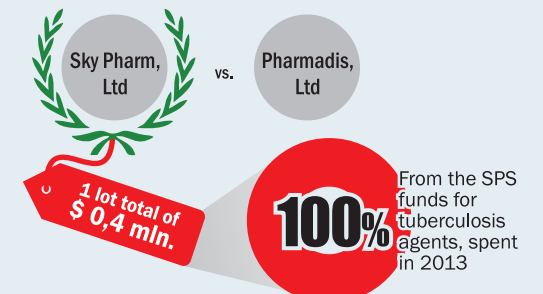


Tuberculosis Medications

Public Procurement by Ministry of Health



Public Procurement by the State Penitentiary Service



5.

THE GIVEAWAY GAME: STAGED COMPETITION BETWEEN “ALBA UKRAINE” CLOSED-JSC AND “LUDMILA-PHARM” LTD

The list of companies taking leading positions at government tenders for the procurement of ART and TB agents also includes “Alba Ukraine” closed-JSC and “Ludmila-Pharm” Ltd. In 2013 these two companies won governmental contracts for ART totaling \$8.4 million USD, which accounts for 27% of all public procurement of ART. Their share in public procurement of TB agents is worth \$1 million USD, which is 7% of the total value of all purchases.⁶²

AntAC experts have identified several consistent trends concerning public procurement procedures involving “Alba Ukraine” and “Ludmila-Pharm”. First, there are rarely more than two tender competitors (the minimum according to Ukrainian legislation) when one of these companies participates in the bidding process. Second, “Alba Ukraine” competes exclusively with “Ludmila-Pharm” when it participates in tender bidding. Third, when “Ludmila-Pharm” competes with a third company (e.g., “BADM” Ltd, “Medpharcom-Center” Ltd, or “Apopharm” Ltd) “Ludmila-Pharm” wins a tender. Fourth, the prices for the medicines offered by these “competitors” mostly vary within 1% or 0.1 to 2.5 US cents per item from the price proposed by the “opponent” company.⁶³

This scheme of predetermined bidders organized by “Alba Ukraine” and “Ludmila-Pharm” has existed for more than a year. Until 2011, “Alba Ukraine” was regularly staging competition with “BADM”.⁶⁴ In 2011, the Antimonopoly Committee fined both organizations for coordinated anticompetitive behavior in public procurement tenders.⁶⁵ Both “Alba Ukraine” and “BADM” were founded by Cyprus-based offshore companies registered in the same building.⁶⁶ “Alba Ukraine” belongs to the Cypriot company “Laona Investments Limited”. 85% of stock in “Laona Investments Limited”⁶⁷ is held by four former classmates:⁶⁸ Roman Yefymenko, Volomymyr Chumel, Volodymyr Dzhus and a current MP of Ukraine Volodymyr Dudka.⁶⁹ The Dnipropetrovsk-based “BADM” Ltd is entirely owned by the Cypriot company “Liorco Investments Limited”.⁷⁰

When the Antimonopoly Committee unveiled the collusion between “BADM” and “Alba Ukraine”, the latter expanded the circle of tender partners. In 2011, “Ludmila-Pharm” Ltd, owned by siblings Kosiantyn Hroshev and Olena Myronova, joined the group of “Alba Ukraine’s” competitors. Similarly, “BADM” has become the formal competitor of “Ludmila-Pharm”.⁷²

AntAC experts assume that the other companies competing with “Ludmila-Pharm” submit their bids to create the illusion of fair competition. For example, “Medpharcom-Center” (a company that often competes with “Ludmila Pharm”) is controlled by the Swiss offshore company “PALMA GROUP SA” headed by Director Francois Zurcher.⁷³ Mr. Zurcher, who has the exclusive right to sign all documents for “PALMA GROUP SA”, also works for 63 other companies.⁷⁴

Thus, these companies win public procurement tenders through “choreographed” competition among themselves. Necessarily, they must coordinate their participation in public procurement tenders in advance of bidding. The European Commission defines such actions as a “cartel agreement”. A cartel is a group of independent manufacturers that work in the same field and coordinate their actions with regard to pricing policy and market division. Such coordinated actions aim to increase the income of individuals by weakening competition.⁷⁵

Cartel agreements in public procurement tenders are largely ignored by the the MoH, as well as law enforcement and regulatory agencies. This scheme allows two intermediary companies to control a major share of the market, causing over-inflated prices for life-saving medications and undermining quality and delivery.

Cartel Agreement between “Alba Ukraine” and “Ludmila-Pharm”

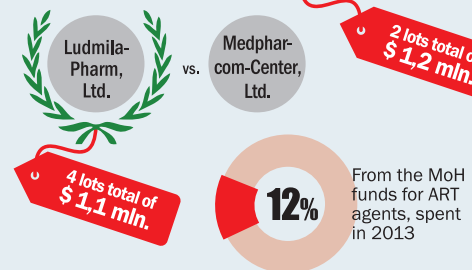
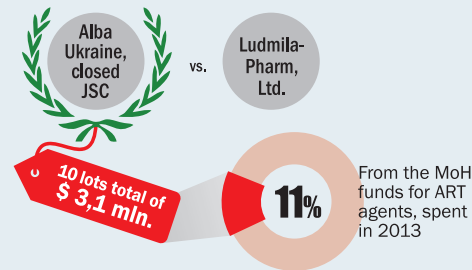
Alba Ukraine, closed JSC

Ludmila-Pharm, Ltd.

The AntAC experts have identified several consistent trends concerning public procurement bidding involving “Alba Ukraine”, closed JSC and “Ludmila-Pharm”, Ltd. Firstly, if one of the companies participates in bidding, there is never more than two competitors in that bidding. This is minimal number of tender competitors to meet the formal conditions of the Ukrainian legislation. Secondly, “Alba Ukraine” competes exclusively with “Ludmila-Pharm”. Thirdly, when “Ludmila-Pharm” participates in a tender with a third company, “Ludmila-Pharm” wins it. Fourthly, the prices for the medicines offered by these “competitors” mostly vary within 0,8 to 2,5 cents per item from the price.

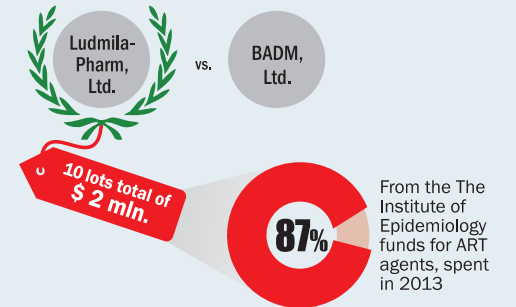
HIV/AIDS Medications

Public Procurement by the Ministry of Health



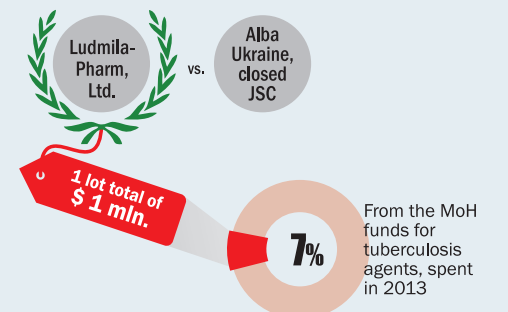
HIV/AIDS Medications

Public Procurement by the Institute of Epidemiology



Tuberculosis Medications

Public Procurement by the Ministry of Health



6.

THE PRETENDER: THE TRANSFORMATION OF STATE INSULIN MANUFACTURER “INDAR” CLOSED JSC

According to information provided on the official web portal for public procurement, state-owned insulin manufacturer “Indar” closed JSC is the biggest provider of HIV/AIDS and TB medicines in Ukraine. Immediately after entering the market in 2013, Indar won 58% of the public procurement tenders for ART (totaling \$16.5 million USD) and 38% of TB tenders (totaling \$5.1 million USD).⁷⁶

“Indar” was created in 1997 on the resource basis of a pig farm.⁷⁷ Initially, the company specialized in producing cheap and affordable insulin. However, in 2012, “Indar” began to successfully bid in MoH tenders for medications the company had never produced before. In 2013, ART and TB agents were included on the extended list of “Indar’s” products.⁷⁸ This expansion of the company’s products was accompanied by public statements made by Indar’s CEO, Ms. Vyshnevskaya. According to Ms. Vyshnevskaya, localizing production of ART would help to gradually reduce the price for HIV/AIDS agents by 40%.⁷⁸ She announced that the factory had successfully passed the inspection by “Abbott Laboratories”, a US-based pharmaceutical corporation specialized in manufacturing ART.⁸⁰ Meanwhile, neither “Indar”, nor “Abbott Laboratories”, based in Chicago, officially confirmed this information.⁸¹

Rather than providing answers, Ms. Vyshnevskaya’s statements only raise more questions. First, according to information included in the State Register of Medical Agents of Ukraine, “Indar” does not manufacture any of the pharmaceutical drugs it sells to the MoH.⁸² AntAC lawyers, with assistance from MP Lesya Orobets (Vice-President of the Ukrainian chapter of GOPAC), sent a deputy’s information request to Ms. Vyshnevskaya in order to clarify whether “Indar” indeed has its own facilities for producing ART agents as claimed.⁸³ MP requests require a mandatory response. Despite this, Ms. Vyshnevskaya ignored the AntAC’s request for a list of medicines produced at the factory and supplied to the MoH.⁸⁴ Such behavior warranted

opening a criminal case⁸⁵ against Ms. Vyshnevskaya, who can face up to three years in prison.⁸⁶ Second, the price of Aluvia, an ART agent, was only reduced by 0.06 US cent (0.12%) compared to the previous year,⁸⁷ which contradicts “Indar’s” intentions of significantly reducing prices through localized production of ART.

Moreover, many hidden pitfalls were found in the ownership structure of “Indar” and its relations with government officials, including representatives of the MoH. While “Indar” is a private company, the state-owned joint-stock company “Ukrmedprom” owns 70.7% of “Indar’s” stock.⁸⁸ “Ukrmedprom” is a part of the MoH structure.⁸⁹ This, however, is only part of the intricate relationship between “Indar” and the MoH.

Since March 2012, Mr. Roman Bohachov, Deputy Minister of Health, has been the Head of the Public Procurement Committee for the MoH.⁹⁰ According to the official duties order, Mr. Bohachov also controls and coordinates the activities of “Ukrmedprom”.⁹¹ Dmytro Politiko is a Head of “Ukrmedprom”.⁹² He is Mr. Bohachov’s classmate and close friend,⁹³ as well as a member of “Indar’s” Supervisory Board⁹⁴ (allowing him access to internal affairs at the company). This conflict of interest creates conditions that might cause the transfer of classified information from the MoH to “Indar”, enabling them to coordinate their actions at competitive bidding.

To illustrate this, consider the following facts. First, “Indar” started to participate and win MoH public procurement tenders in June 2012, soon after Mr. Bohachov was appointed in his current post.⁹⁵ Second, “Indar” wins all tenders it bids for.⁹⁶ Third, when “Indar” was supplying the MoH with test strips for glucometers in 2012, it contracted with a UK-based offshore company called “Altona” (which also appears to be a shell company). “Altona” signed a contract with “Indar” on the same day that the MoH made the announcement of public procurement tender – long time before the participants of the

tender submitted their proposals and result of tender was announced. Remarkably, the value of the contract was exactly the same as the announced public tender from the MoH as of “Indar” was confident about the results of the tender.⁹⁷

Therefore, ownership structure of “Indar” and its close connections to the MoH give the AntAC reason to believe that “Indar” has access to classified tender information, which constitutes a breach of national legislation. This conflict of interest violates the basic principle of public procurement: a “level field” for all participants.

Finally, “Indar,” like the majority of other companies participating in MoH public procurement tenders, has no “un-staged competitors”. In two out of six tenders,⁹⁸ “Indar” competed with “MBB Instruments” Ltd, a company connected with “Indar”. The Antimonopoly Committee has started an investigation of this connection as a result of claims by AntAC lawyers and MPs.⁹⁹

Instead of localizing production to reduce drug prices for consumers, “Indar” speculated over its manufacturer status to benefit from local producer status. Furthermore, “Indar’s” top management allegedly abused their connections with MoH officials and entered into cartel agreements to distort the competitiveness of public procurement tenders. The illicit profits received from multi-million contracts with the MoH were transferred to the accounts of offshore companies with complex ownership structures,¹⁰⁰ while “Indar” declared its loss-making balance. In other words, a state-owned company (and the principle government supplier of ART and TB agents in 2013) was converted into a shell company used for laundering Ukrainian taxpayers’ money.

7.

STATE REGULATION OF DRUG PRICES AS A GREEN LIGHT FOR SUPER-PROFITS

It looks like Ukraine has created all conditions to reduce the price of drugs purchased by the government. First, medicines are exempt from VAT.¹⁰¹ Second, there is the State Register of Wholesale Prices for Medicines,¹⁰² which fixes the upper ceiling of prices for medicines.¹⁰³ However, the imperfect pricing system enables manufacturers to consciously inflate prices in the Register.¹⁰⁴

Holders of registry certificates can abuse the Register by making an agreement with the MoH to declare over-inflated prices. First, a manufacturer (or their authorized representative) gets a special certificate from the State Drug Service, which operates under the MoH. The holder of the certificate then submits a declaration with the pre-determined wholesale price to the MoH according to the standard formula.¹⁰⁵ After winning a tender, bidders split the profits with the MoH.

Pricing formulas are different for domestic and foreign drugs.¹⁰⁶ The price of imported drugs is based on the value indicated on the customs declaration form, which is issued to companies when pharmaceuticals enter Ukraine. The MoH does not require a copy of the customs declaration. In fact, the customs database is classified and only available to the Ministry of Revenue and Duties.¹⁰⁷

A report by the Parliamentary Temporary Investigative Commission indicated that offshore companies are often used for over-inflating drugs prices. Ukrainian shell companies fictitiously import drugs from foreign offshore companies to justify the inflated price on their customs declaration. In reality, however, medications come directly to the buyer without any additional transactions but are much more expensive.¹⁰⁸ Taking into consideration that importers of drugs enjoy certain tax privileges, they often abuse the procedure and declare higher prices. This gives them an opportunity to withdraw shadow cash abroad and to artificially minimize their tax liability in Ukraine. The profit from these

shadow operations, in turn, ends up in the pockets of offshore and shell companies' beneficial owners.

Domestic manufacturers can also easily inflate drug prices in the State Register. The certificate holder simply submits a claim that indicates the wholesale price the holder charges all buyers.¹⁰⁹ The MoH does not require any supporting documentation to justify the wholesale price from a domestic manufacturer. Furthermore, the State Pricing Inspection does not check or request any supporting documents even though they have a right to so.¹¹⁰

The AntAC has repeatedly asked the State Pricing Inspection to request an audit of the over-inflated prices in the State Register. In response, the State Pricing Inspection repeatedly states that an audit would be impossible because there are no standard formulas used to calculate the price of drug production. In fact, domestic manufacturers can essentially declare any price for their drugs. On several occasions, the State Pricing Inspection has requested that the MoH introduce an obligatory formula for calculating drug prices, but this request has yet to be fulfilled.¹¹¹

AntAC experts also approached the Antimonopoly Committee of Ukraine regarding this challenge. The Antimonopoly Committee confirmed that drugs prices are over-inflated in the State Register. The Committee confirmed that the problem of over-inflated prices does exist. They also informed that they are working on regulating price calculations, but it is still unclear when there will be any progress in this domain.¹¹²

In some cases, pressure from regulatory agencies and the public can force institutions to purchase drugs at prices that are much lower than those fixed in the State Register of Wholesale Prices. A recent tender organized by the SPS provides one successful example of how civil society can help reduce the price of drugs purchased with taxpayer money. In April 2013, the SPS announced a public

tender for purchasing ART, TB agents and basic antiseptics for a total of \$0.7 million USD.¹¹³ A study by AntAC indicated that the SPS was expecting to pay 20% more compared to similar MoH contracts, and two times more compared to charity foundations.¹¹⁴ After an appeal of the AntAC and MPs,¹¹⁵ the SPS canceled its previous tender, and announced a new one.¹¹⁶ The bidder who won the new tender was the same as in the previous one, but the value of the contract was decreased by \$0.2 million USD.¹¹⁷

The Register has turned into an instrument for justifying over-inflated prices for drugs purchased by the MoH and other governmental institutions. Neither the Register nor the intervention of law enforcement agencies helped save taxpayers' money; only pressure from civil society assisted by MPs achieved the desired results.

8

HOW TO RESOLVE THE PROBLEMS?

In countries where medicines are procured by state, it is possible to reduce prices for essential drugs if the government has enough political will to do so. In countries where corruption is the rule rather than the exception, however, such political will may be hard to come by. In Ukraine, many companies with strong relationships to the MoH form partnerships to divide the market of publicly procured medicines among themselves. Companies enter into “cartel agreements” and speculate over the status of a domestic manufacturer. Companies transfer taxpayer money to offshore accounts and abuse the State Register of Wholesale Prices to justify over-inflated prices. Thousands of critically ill Ukrainians are denied life-saving medications as a result of this corrupt system.

Under such conditions, the only solution is to provide constant public, media and parliamentary oversight over the public procurement of medications, as well as make systematic amendments to legislation. Civil society control of and advocacy for legislative amendments are the daily focus of the AntAC and the Ukrainian chapter of GOPAC.

After analyzing the most common corrupt schemes used in the public procurement of medicines, AntAC experts have identified that changes should be introduced on three levels: sectoral, inter-sectoral and international levels.

At the sectoral level, it is paramount to change the system that regulates the prices of medicines. Currently, the only entity regulating drug prices is the State Register of Wholesale Prices for Medicines, which has proven to be inefficient. It is necessary to develop a transparent and economically justified standard for calculating drug prices. Such an assessment must include an analysis of referral prices. AntAC, with the assistance of the Charity Foundation the “All-Ukrainian Network of PLWH,” has already begun to develop a price observatory

for procurement prices in Ukraine, neighboring countries and the national NGOs. This online platform will soon be available to the general public.

As for inter-sectoral reform, it is important to make a series of amendments to public procurement legislation. These amendments will have a positive effect on all spheres of public procurement.

First, although current legislation already has a model for conducting tenders through requesting quotes, there is still room for improvement. Under the current process, governmental institutions must request at least three quotes per one tender. Based on these quotes institution picks the most economically reasonable and selects the supplier. Since the pool of pharmaceutical manufacturers who produce drugs registered in Ukraine,¹¹⁸ AntAC believes that this system would be appropriate for the procurement of medications. Moreover, state institution should send their requests for quote to local and international pharmaceutical companies (including international non-governmental distributors like IDA Foundation¹¹⁹). On the other hand, the law stipulates that the ceiling price for one bid cannot exceed \$25,000 USD.¹²⁰ This restriction should be lifted.

Second, since most ART and TB agents are produced abroad,¹²¹ it is necessary to simplify the tender documentation package in order to level the field for both domestic and foreign producers. This will facilitate more direct purchases from foreign manufacturers. Currently, foreign manufacturers have problems completing all the necessary tender documents and certificates in Ukrainian. It is also takes a lot of time and efforts for them to legalize all relevant documents and certificates at the delegations of correspondent embassies in Ukraine.¹²² These challenges encourage collaboration with shell companies specialized in preparing and submitting all public procurement tender documenta-

tion. This involvement of corrupt intermediaries is one key reason why the prices for medicines are over-inflated in Ukraine.¹²³ Experts at AntAC believe that it is necessary to reduce the number of required documents and make up a final list of documents for participating in public procurement. Also, it is important to allow foreign manufacturers to submit documents in English.

Third, all public procurement tender documentation submitted by bidders must be available to a wider public when applications are opened. AntAC’s investigation uncovered evidence that suggests that documents of the “preliminarily defined winners” may undergo editing when opening tender applications and post factum.¹²⁴ The Antimonopoly Committee of Ukraine (AMCU) also found similarities among competitors’ applications during monitoring. In certain cases, applications contained the same linguistic and spelling mistakes in all documents of the pseudo-competitors;¹²⁵ indicating that all applications were likely prepared by the same person or company. Tender applications are currently classified, which restricts the possibility of civil society oversight over the bidding process.¹²⁶

Fourth, it is important to add patients, consumers, general public to the list of people who can request an investigation by the AMCU concerning the unveiled facts of anticompetitive actions. Namely, it is necessary to include the ultimate consumers into the list of the parties concerned. Moreover, regulatory bodies such as the State Price Control Inspection should be able to initiate and conduct unbiased monitoring of price calculations in the State Register.

Fifth, it is vital to expand convenient access to the database of the procurement budget, which is located on the web portal of public procurement, for common users of the web portal. Currently searching for information of just one purchase may take up to several hours, which complicates oversight of public procurement and significantly reduces the possibility of public control over the expenditure of funds of Ukrainian taxpayers.

Sixth, it is important to make information about drug procurement by state companies more transparent. This would include disclosure of informa-

tion about various goods and services purchased by state-owned companies, as well as relevant prices and suppliers.¹²⁷ State companies often have privileges in public procurement given their structure (including connections to Ministries) and taking several positions in adjacent offices by the same people. It allows them to take advantage of the system. Making information more transparent would prevent great share of abuses by companies like “Indar”.

Finally, on the international level, it is necessary to identify the beneficial owners for various companies. This can be done by creating a public register of beneficial owners, and would help reduce staged competition between groups of companies with one mutual beneficial owner. It will also reduce the transfer of funds to offshore companies by identifying their beneficial owners.

A number of influential NGOs specializing in anti-corruption and anti-money laundering have united their efforts to organize an international advocacy campaign for piercing the veil of beneficial ownership.¹²⁸ This initiative has recently received approval from the Prime Minister of the United Kingdom, Mr. David Cameron.¹²⁹ Strong international movement can facilitate the advocacy campaign of a public register of beneficial owners in Ukraine.

Another way to reduce corruption in public procurement of medicines in Ukraine is to use the international instruments for anticorruption actions more efficiently. Such tools include the “Foreign Corrupt Practices Act” (FCPA), a law that forbids companies listed on the American Stock Exchange from bribing foreign officials and politicians.¹³⁰ Violating this law can result in considerable financial punishment, up to 5 years imprisonment, and a number of other economic and political sanctions.¹³¹ The Ukrainian experience demonstrates that companies develop partnerships with local intermediaries in order to avoid the consequences of being associated with corrupt activities. Shell companies bear the burden of risk when communicating with governmental officials and politicians. As a result, these intermediaries guarantee themselves the victory in public procurement tenders by applying shadow schemes. In our opinion, FCPA and other

international anticorruption laws could also be applied to foreign pharmaceutical manufacturers in cases of “veiled” corruption.

International NGOs that finance anticorruption projects relating to HIV/AIDS and TB should advocate for the development of international policy and review their approach to implementing projects at the local level.

All legislative amendments and initiatives should concentrate on two key principles: (1) civil society oversight at every stage of the public procurement process and legislative amendments, and (2) ensuring an unrestricted flow of information. Ukraine’s experience indicates that the most progressive bills do not get implemented without public oversight. Meanwhile, creative officials and corrupt-minded entrepreneurs find loopholes in existing regulations where there is no civil society control. Furthermore, the opportunities for civil society monitoring are seriously impeded if there is no access to information and primary documents.

The above recommendations should significantly reduce prices for essential medicines, giving hope to those in need of high-quality and affordable therapy. Most importantly, successful implementation of these suggested measures may eventually help overcome the epidemics of HIV/AIDS and TB in Ukraine.

LIST OF ACRONYMS

ART – antiretroviral therapy

AMCU – Antimonopoly Committee of Ukraine

AntAC – non-governmental organization Anticorruption Action Centre

HIV/AIDS – human immunodeficiency virus infection / acquired immunodeficiency syndrome

Institute of Epidemiology – the government institution “L.V.Gromashevsky Institute of Epidemiology and Infectious Diseases”

MoH – the Ministry of Health of Ukraine

MP – member of parliament

SPS – the State Penitentiary Service of Ukraine

TB – tuberculosis

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15. Community consensus statement on the use of antiretroviral therapy as prevention for people living with HIV. Available at: <http://www.aidsmap.com/tasp-statement>
16. The Constitution of Ukraine. Art. 49. Available at: <http://zakon1.rada.gov.ua/laws/show/254%D0%BA%96-%D0%B2%D1%80>
17. Own calculations. According to the report "The national evaluation of the state of HIV/AIDS in Ukraine as of the beginning of 2013", 48,430 HIV infectees were getting ART therapy. At once, 111 393 HIV infectees were in need of therapy.
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The Anti-corruption Action Centre (AntAC) is a Ukrainian civil society organization, which unites experts from legal, media and civic-political sectors fighting corruption as a root cause of the key state-building problems in Ukraine.

Why AntAC is focused on grand political corruption?

AntAC aims at curtailing grand political corruption, which occurs on the stage of making policy decisions by officials. Political corruption within a captured state, such as Ukraine, becomes a root cause of governance problems. Political corruption significantly increases the level of administrative corruption and gives rise for petty corruption. Political corruption washes up billions of state budget funds and drains natural resources of the country depriving its people from fundamental human rights.