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Regulatory Update

Post-COVID Checkup: Current FDA Due Diligence Considerations

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The COVID-19 pandemic highlighted both the incredible promise and challenges for life science companies developing and manufacturing drugs, biological products, and devices that enhance our lives. As the public health emergency in the United States and elsewhere has ended, it is critical that life science companies, and their investors and lenders, consider the changing FDA regulatory and compliance landscape.

During the pandemic, the FDA focused its resources and priorities on issues related to COVID-19. In many cases, the pandemic paused important agency activities, such as inspections of manufacturing establishments. In other cases, the FDA applied its enforcement resources to combating fraudulent COVID-19 "treatments" or ensuring the quality of hand sanitizers used by millions of Americans. Now that the pandemic is subsiding and the public health emergency orders have ended, FDA inspection and enforcement patterns are returning to more traditional patterns. The FDA is once again conducting on-site inspections at manufacturing facilities and issuing Warning Letters at a rate that is more commensurate with past practice. But it would be wrong to think that the pandemic has not also affected the FDA's approach and practice. And these effects have important implications for both healthcare investors and lenders in the life sciences and healthcare sectors.

1. COVID-19 Created a Significant Inspection Backlog at the FDA

The FDA generally uses a risk-based approach to inspecting drug manufacturing establishments. Although during the pandemic the FDA sought to use alternative compliance tools, such as remote interactive evaluations and record requests, it frequently could not conduct on-site inspections and, thus, currently faces a large backlog of inspections. Additionally, the FDA faces increasing review demands (as the number of cell and gene therapy applications increase) while struggling to hire reviewers (as the FDA's focus on COVID-19 vaccine approvals and regulation during the pandemic has stretched existing resources). For investors and lenders conducting due diligence, this means that typical inspection results and feedback are not available yet, and critical quality issues that might otherwise arise during such inspections may be otherwise latent. Depending on the situation, it may be prudent to examine additional quality system metrics, such as related to deviations and complaints, or other information to get more insight into a target's compliance status, such as internal reports or third-party reports.

2. The FDA Relies on an Expanding Set of Compliance Tools

FDA compliance tools have grown over time, and the pandemic was the impetus for the FDA to explore and implement the use of these tools more regularly. For example, the FDA has long had the authority to request manufacturers' records in lieu of or in support of an inspection. The agency began making more significant use of these requests during the pandemic when it could not conduct on-site inspections. In the post-pandemic environment, it has continued to use these requests and, in some cases, has initiated import alerts and Warning Letters because of a company's response. Due diligence practices need to increasingly be attuned to these types of requests and the consequences that poor responses may generate.

3. Attention Increasing on Supply Chain

The pandemic highlighted, of course, weaknesses in many supply chains. But in addition to the disruption and delays that might result from the supply chain, the FDA has also focused its attention on potential safety and quality issues related to raw materials and issues in the drug manufacturing process. For example, multiple companies have initiated recalls after identifying nitrosamines in their products stemming from active pharmaceutical ingredients ("API") or other sources. The FDA has also issued import alerts and guidance on high-risk components that might lead to the presence of ethylene glycol and diethylene glycol in pharmaceutical products. Due diligence efforts need to pay increasing attention to supplier management programs and the risk assessments that companies perform to evaluate (a) the potential for these issues to occur with their products, and (b) depending upon a company's risk assessment, potential alternative sources of raw materials.

4. Quality-Related Issues are Increasingly Surfacing in Company's Compliance Programs

In addition to FDA oversight, more and more companies have developed compliance programs, and the effectiveness of such programs is critical to the U.S. Department of Justice ("DOJ") when it considers resolution of any potential issue before DOJ. Companies also realize that an effective compliance program adds real value by preventing some issues altogether and stopping other issues from becoming more significant. These compliance programs routinely focus on identifying and escalating potential issues, and so despite the FDA backlog, in many cases, quality or FDA-related issues are being flagged more often in companies' compliance systems. This is particularly true as companies facing cost pressures have streamlined staffing and attempted to do more with less. It is becoming increasingly critical as part of due diligence to understand whether such internal compliance reports have been generated and substantiated by third parties, such as outside counsel or other consultants, as these reports sometimes lead to whistleblower suits and other government investigations. Moreover, these internal reports might, in some cases, highlight matters bearing on the company's financial performance.

Concluding Thoughts

As always, it is important to take a methodical approach to FDA compliance due diligence to identify and evaluate the impact on a company's financial performance and mitigate against the risk that healthcare investors or lenders face. The COVID-19 pandemic accelerated the development of new drugs, vaccines, and devices but also impacted FDA regulatory approaches with continuing effects. Consequently, healthcare investors and lenders must continue to consider pandemic approaches as part of their ongoing due diligence activities now that the worst has subsided.

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