

**NOTICE SEEKING CLEARANCE IN RESPECT OF THE PROPOSED ACQUISITION BY CENTRAL
HEALTHCARE OPERATIONS LIMITED OF AORANGI HOSPITAL LIMITED PURSUANT TO SECTION 66 OF
THE COMMERCE ACT 1986**



31 October 2022

The Registrar
Business Acquisitions and Authorisations
Commerce Commission
PO Box 2351
WELLINGTON

Pursuant to s 66(1) of the Commerce Act 1986 notice is hereby given seeking **clearance** of a proposed business acquisition.

1. EXECUTIVE SUMMARY

- 1.1 This notice seeking clearance is given by Central Healthcare Operations Ltd (**CHOL**, or the **Applicant**) in relation to its proposed acquisition of 100% of the shares in Aorangi Hospital Limited (**Aorangi**, or **Target**) from Southern Cross Healthcare Limited (**SCHL**) (the **Proposed Transaction**), and associated ancillary agreements described in this application.
- 1.2 Aorangi is a shareholder in Crest Hospital Ltd, the agent for the Crest Hospital Partnership (the **Crest JV**). The Crest JV is a 50/50 joint venture between Aorangi and SCHL's subsidiary, Southern Cross Hospitals Palmerston North Partnership Limited (**SCHPNPL**). The Crest JV operates a private hospital and specialist centre in Manawatū at the Crest Hospital (**Crest Hospital**).
- 1.3 The Proposed Transaction will be implemented through two inter-conditional agreements. First, SCHPNPL will acquire from the current Aorangi shareholders the remaining shares in Aorangi it does not already hold, then SCHPNPL will sell 100% of the shares in Aorangi to CHOL.
- 1.4 The parties want to provide for succession and renewal of the Crest JV by bringing the mid-career surgeons and specialists that are shareholders in CHOL into the Crest JV. CHOL can also facilitate future opportunities for growth of the Crest JV to meet the needs of the local community by accessing potential new healthcare facilities at the nearby land on Milson Line owned by Central Healthcare Ltd (**CHL**, a sister company of CHOL with identical shareholding as CHOL) (**Milson Line**).
- 1.5 The Proposed Transaction does not give rise to any adverse competition effects. []
- 1.6 Instead, the Proposed Transaction is likely to give rise to material efficiencies and public benefits, as the Proposed Medical Facility's development of consulting and specialist rooms, to meet the Manawatū local community incremental demand over time, optimises efficient capacity expansion and utilisation. The common ownership link between Crest Hospital and the development at Milson Line is likely to lead to much more efficient consulting and referral experience for all users of private healthcare services in the local community and wider Manawatū region.

PART A: PARTIES TO THE PROPOSED TRANSACTION**2. THE APPLICANT: CENTRAL HEALTHCARE OPERATIONS LTD****The Applicant's Contact Details**

2.1 This notice seeking clearance is given by CHOL.

2.2 The contact details for the Applicant are:

Colin Hutchison
Managing Director
Central Healthcare Operations Limited
c/- Sheperd Hensman Ltd,
107 Market Street South,
Hastings, 412
Phone: []
Email: []

2.3 All correspondence and notices in respect of the application for the Applicant should be directed in the first instance to:

Sarah Keene, Barrister
Level 1, 27 Chancery Street
Auckland, 1010

Telephone: 027 535 5034
Email: sarah@keene.co.nz

Description of the Applicant

2.4 CHOL is owned by a group of 39 shareholders associated with healthcare practitioners including surgeons and specialists practicing in the Manawatū area. A list of the shareholders in CHOL is included in the document set filed with this clearance application (**Clearance Application Bundle**, or **CAB**) (**CAB.001**).

2.5 Further details regarding the Applicant's New Zealand activities are provided in section 8.

3. THE TARGET: AORANGI HOSPITAL LIMITED**The Target's Contact Details**

3.1 The target is Aorangi, a limited liability company incorporated in New Zealand, currently owned by SCHL through SCHPNPL (approximately 15% of shares), together with a group of 11 surgeons and specialists (current and retired) operating in the Manawatū area (approximately 85% of shares).

3.2 A list of the surgeons that are shareholders in Aorangi is at **CAB.001**. CAB.001 also details Aorangi's understanding of the working status of the shareholding surgeons and specialists.
[]

3.3 SCHL is a 100% subsidiary of Southern Cross Health Trust, a registered charitable trust under the Charitable Trusts Act 1957. The business assets of SCHL include 10 wholly owned private hospitals, and (via partnerships and/or partial ownership) shareholdings in six private hospital joint venture companies, including Crest Hospital Limited.

3.4 The contact details for Aorangi are:

Matthew McIlroy
General Counsel
Southern Cross Healthcare Limited

Telephone: []

Email: []

Description of the Target

3.5 Further details regarding the Target's New Zealand activities are provided in section 8.

3.6 Pre- and post-transaction structure charts for the Crest JV and related companies are provided at **Appendix A**.

PART B: TRANSACTION DETAILS

4. OVERVIEW OF THE PROPOSED TRANSACTION

Description of the Proposed Transaction

- 4.1 The current shareholders in Aorangi agreed to sell to SCHL the remaining shares that it does not already own by heads of agreement dated [] (**Aorangi HOA**).
- 4.2 The Aorangi HOA is conditional on:
- (a) []
 - (b) []
 - (c) []
 - (d) []
- 4.3 CHOL agreed to acquire, and SCHL agree to sell, 100% of the shares in Aorangi by heads of agreement dated [] (**CHOL HOA**).
- 4.4 The CHOL HOA is conditional on [.]
- 4.5 The net effect of the acquisition and sale of the Aorangi shares by SCHL will be that CHOL will control 50% of Crest Hospital. This is a marginally higher share than the Aorangi shareholders currently have, and reinstates the clinician shareholding level approved by the Commission in 2011, as described further at paragraph 7.4 below.

Transaction documents

- 4.6 Copies of the Aorangi HOA and the CHOL HOA are at **CAB.002** and **CAB.003**.

5. RATIONALE FOR THE TRANSACTION

- 5.1 The parties want to provide for succession and renewal of the Crest JV by bringing the mid-career surgeons and specialists that are shareholders in CHOL into the Crest JV. CHOL can also facilitate future opportunities for growth of the Crest JV to meet the needs of the local community by accessing potential new healthcare facilities at Milson Line.

PART C: COUNTERFACTUAL**6. COUNTERFACTUAL****CHOL**

- 6.1 If the Proposed Transaction does not proceed, [] Of the surgeons under 55 years old operating in the private sector in the Manawatū area, [] are shareholders in CHOL.
- 6.2 In the Counterfactual, CHL (CHOL's sister company) may continue to develop the Milson Line site, as is proposed in the Factual, to provide out patient suites for CHOL's core clinicians, who operate in the specialties of urology, orthopaedics, ENT, cardiology, general surgery, and gynaecology. Some of the suites will be run as standalone suites, for one speciality group, others will be run as "hot desks" and the rooms used across multiple disciplines, depending on the requirements of the relevant specialty. Alongside the outpatient rooms, CHL is proposing to also provide a dental suite and a radiology department, including CT, PET CT, MRI, USS, plain film ("**Proposed Medical Facility**"). [] In summary, the Proposed Medical Facility will provide facilities that are complements to, not substitutes for, Crest Hospital's facilities.
- 6.3 There is also a possibility in the Counterfactual that if the Proposed Transaction does not proceed, [].
- 6.4 []
- 6.5 []. Further detail on why that is the case, with reference to the relevant documents, is attached at **Appendix B**.

SCHL and Aorangi

- 6.6 If the Proposed Transaction does not proceed, then the status quo will prevail. []
- 6.7 []
- 6.8 []
- 6.9 []
- 6.10 []
- 6.11 []
- 6.12 [] If Crest Hospital could relocate the specialist centre in the Proposed Medical Facility, this could allow for the site to be more optimally configured.

Summary

- 6.13 In short, there is no material negative effect on competition when comparing the factual and the counterfactual. The factual is pro-competitive, as the common ownership links between Crest JV and the Proposed Medical Facility should provide incentives within the CHOL shareholders to ensure that capacity expansion is in fact undertaken and that it is done in the way that is most efficient, incremental, and best meets the needs of the local community.

PART C: THE INDUSTRY

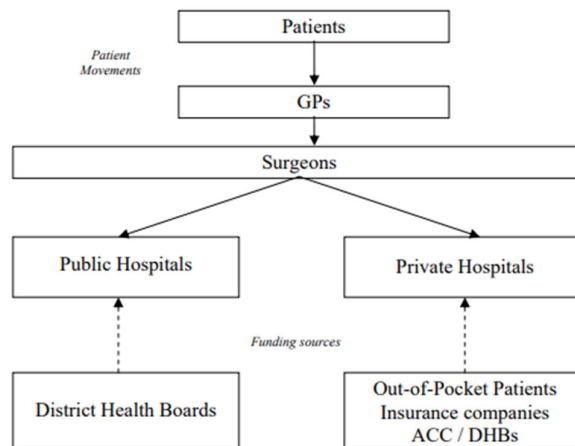
7. BACKGROUND TO THE INDUSTRY

Healthcare Facilities in Manawatū

- 7.1 The Proposed Transaction concerns the ownership structures in respect of the supply of private healthcare facilities in the Manawatū region.
- 7.2 In *Southern Cross Health Trust/Aorangi Hospital Limited*, 4 September 2008, Decision 650 (**First Aorangi Decision**), the Commission outlined the way that private hospital services are procured and delivered in the Manawatū area. That description is set out below¹. The relevant dynamics remain materially the same.

In New Zealand, healthcare is provided by a range of medical practitioners and facilities. The main industry participants relevant to this proposed acquisition are shown in the diagram below.

Figure 1: Main Industry Participants in Healthcare



There is a relatively complex set of relationships leading to a particular patient being operated on by a particular surgeon in a particular hospital. As shown in Figure 1, patients are first seen by a primary healthcare provider (usually a GP). If surgery is warranted, or specialist consultation is required, the patient will be referred to a surgeon.

When a surgeon recommends private elective surgery the decision as to which private hospital will be used will be heavily influence by the hospital (or hospitals) where that surgeon normally operates. Typically, patients will follow their surgeon's recommendation about where the surgery is to be performed.

Factors that influence surgeons' choice of hospital include:

- (i) whether or not they have a shareholding in a facility (as is the case with Aorangi)²;

¹ First Aorangi Decision, paras 19-24, pp 3-5.

² Note that this consideration is subject to managing appropriately any relevant conflicts of interest.

- (ii) the ability to schedule surgery at a convenient time for the surgeon at a particular private hospital; and
- (iii) the particular private hospital's charges for the provision of the necessary facilities.

Private hospitals provide facilities, namely, patient rooms and medical equipment, as well as the related non-specialist services such as administration staff and nursing staff. Private hospitals typically do not provide surgeons or the ancillary specialist skills such as the anaesthetists or physiotherapists. These medical professionals contract directly with the patient and therefore bill the patient separately.

Private hospitals focus almost exclusively on providing elective surgery. Elective surgery is defined as non-emergency treatments (including diagnostic 5 services) where the condition is not life threatening and does not require immediate surgery.

7.3 In summary, the choice of hospital will depend on the funding model engaged, as follows:

- (a) For public patients – Te Whatu Ora (Health NZ), together with the surgeon, will decide whether the patient is treated at PN or Crest Hospital;
- (b) For ACC patients – where any elective surgery is carried out will be a decision made in a discussion between the patient and their surgeon, depending on availability and capability for the procedure. Crest Hospital has an ACC contract for elective surgery;
- (c) For private patients – private patients' expectation is that they will be treated privately. Occasionally, patients with private insurance will have elective procedures in a public hospital, that would have been covered by their insurance.

7.4 In terms of the hospitals available to the Manawatū community, since the Commission granted authorisation for SCHL to acquire Aorangi Hospital in its subsequent decision, *Southern Cross Hospitals Limited/Aorangi Hospital Limited*, 28 July 2011, Decision 729 (**Second Aorangi Decision**), Aorangi Hospital was closed and Southern Cross' Palmerston North hospital was renamed Crest Hospital. Crest Hospital remains the only private hospital in Manawatū.

Crest Hospital

7.5 Private hospitals undertake elective surgery that is funded by ACC, Te Whatu Ora (Health NZ) (as the successor organisation to the District Health Boards, effective 1 July 2022, under the Pae Ora (Healthy Futures) Act 2022), private health insurers and self-paying patients, as described above. The key private health insurers are Southern Cross Medical Care Society, nib Health Insurance, Unimed Insurance and AIA. In terms of the split of revenue sources, for FY22 Crest Hospital's revenue was³:

- (a) [] Private Insurance;

³ It should be noted that some of the revenue received from various funders reflects fees that are then paid to related providers (i.e. surgeons and anaesthetists) whereas some revenue solely relates to hospital charges. This impacts the net revenue received by Crest Hospital.

- (b) ACC;
- (c) Health NZ; and
- (d) Self Pay.⁴

7.6 The effects of Covid-19 materially affected the number of surgeries undertaken in both private and public facilities between 2020 and 2022, but all facilities are expected to increase utilisation to meet demand and clear public waiting lists.

PN Hospital

7.7 PN Hospital is a fully equipped publicly owned and operated regional general hospital and the only other hospital in the Manawatū. It currently has 7 operating theatres, and a number of procedure rooms. PN Hospital is also currently building a further two new operating theatres, to bring the total to 9, and is adding 2 extra general procedure rooms and a cardiac catheterisation lab. CHOL understands that all new theatres and procedure rooms are scheduled to be open and fully operational by July 2023. PN Hospital also has a host of consulting rooms spread over its campus. All major services are provided from the hospital except neurosurgery and cardiothoracic surgery.

The future direction of health delivery

7.8 Globally, the direction of travel for elective surgical procedures is for less invasive and therefore shorter stay hospital visits. Rehabilitation in the home and for many muscular-skeletal issues non-surgical interventions. As such, over time, there will be less need for full-service non-emergency hospital capacity.

⁴ Note: some of the self-funded revenue includes individuals who paid for the surgery but were later reimbursed from an insurance company. SCHL has no visibility of what proportion of this amount is truly self-funded.

PART D: RELEVANT MARKETS**8. ACTIVITIES OF THE PARTIES IN NEW ZEALAND****CHOL**

- 8.1 CHOL represents in its shareholder base a large majority of the surgeons and anaesthetists under the age of 55 years operating in the Manawatū area. CHOL's shareholders are also shareholders in CHL, which owns a site at Milson Line in Palmerston North.
- 8.2 By press release dated 28 January 2022, CHL announced that it would develop a world class healthcare facility at Milson Line in Manawatū. The release noted that the *“first stage of the project would include a full radiology suite, specialist consultation suites, an interventional cardiology laboratory, and a large dentist practice”*.
- 8.3 In terms of the timeframe for the build project, the expectation was that the build would take about 24 months so was planned (at that time) to open in July 2024. The release noted that a second stage was still under development and that the development will be undertaken to complement the existing healthcare providers in the region, including a collaboration with Crest, as follows:

“the group, which represents over 30 senior doctors, looked forward to working in collaboration with existing local healthcare providers to help meet the growing demand for healthcare within Manawatū. He said that discussions were already underway with Mid-Central DHB and Southern Cross (the co-owners of the CREST facility) to ensure the new healthcare facility on Milson Line will complement other secondary care facilities in the region.”

- 8.4 In summary, CHOL is a group of surgeons and anaesthetists who have an interest in owning and operating healthcare facilities where they also work.

Crest Hospital

- 8.5 The Crest Hospital is a joint venture between SCHL and Aorangi. Crest Hospital is a full service hospital, with four operating theatres, and a fifth theatre due to be opened in November 2022, one procedure room, 10 bed recovery room, 30 inpatient beds and 21 day stay beds/chairs. Specialties performed at Crest Hospital include Orthopaedics, Urology, Gynaecology, General Surgery, Ophthalmology, Otolaryngology, Endoscopy, Oncology and Oral Surgery.
- 8.6 In terms of its outpatient facilities, Crest Hospital has recently developed consulting space in the front of the hospital, consisting of 12 consulting rooms and one procedure room. Beyond that, Crest Hospital has site constraints, with a retirement village and care home next door also expanding its services competing for similar land proximate to the hospital.

Conclusion on the Parties' overlapping activities

- 8.7 The parties' activities are complementary and do not overlap. The surgeons and anaesthetists who are shareholders in CHOL are also users of the Crest Hospital's facilities. They currently do not own or operate healthcare facilities.
- 8.8 To the extent that CHOL proposes to support CHL's development of its site to provide outpatient services and consulting rooms, in both the factual and the counterfactual, those services are likely to be complementary to, and will likely be utilised by, Crest Hospital and the surgeons and anaesthetists who operate there.
- 8.9 There are no material barriers to entry or expansion in the development of land and buildings for consulting rooms and outpatient services, other than access to land proximate to the Crest and PN Hospitals, and to finance.

9. MARKET DEFINITION

- 9.1 In the First Aorangi Decision, the Commission defined separate markets for:
- (a) the provision of private short-stay (less than 24 hours) hospital facilities and related non-specialist services for elective surgery in the MidCentral DHB region (the short-stay market) and
 - (b) the provision of private in-patient hospital facilities and related non-specialist services for elective secondary surgery in the MidCentral DHB region (the in-patient market).
- 9.2 It considered closely whether the market for private hospital services was wider than the DHB region but ultimately found there were not sufficient patients that had or exercised the choice to obtain their private hospital services outside of the region to justify a wider geographic market.
- 9.3 In the Second Aorangi Decision, the Commission authorised the establishment of the Crest Hospital Partnership, having undertaken an analysis of the efficiencies of the proposed joint venture (primarily cost savings) and found they outweighed any calculated efficiency losses arising from the lessening of competition it found may arise in the First Aorangi Decision.
- 9.4 Finally, with reference to the short stay market, in *Southern Cross Health Trust / Auckland Surgical Centre Limited*, 17 February 2004, Decision 546 (ASC Decision) the Commission cleared the merger of short stay facilities on the basis that there was sufficient excess capacity and barriers to entry in the short stay market are low.
- 9.5 Although the parties remain of the view that any market for elective surgery is likely to be wider than the Manawatū region, it is also of the view that it is not necessary for the purposes of this application to consider a different market definition than was adopted in the Commission's previous decisions.

10. COMPETITIVE EFFECTS

No competitive overlap

- 10.1 As noted above, the parties are of the view that there is no competitive overlap in their respective activities in the factual or counterfactual.
- 10.2 In respect of private elective surgical facilities, in both the factual and the counterfactual there will be two fully functional hospitals in the Manawatū region, the privately owned Crest Hospital and publicly owned PN Hospital.

Health NZ outsourcing

- 10.3 To the extent that PN Hospital will need to outsource some of its publicly funded elective surgery volume, as its two new operating theatres are constructed and commissioned, it will outsource that to Crest Hospital. [] After that timeframe, the PN Hospital's own theatres will be operational, and the parties expect the combination of PN Hospital and Crest's own additional theatre to absorb all likely demand for operating theatres in the Manawatū region over the foreseeable future.
- 10.4 The demand in the Manawatū region continues to only be sufficient to support one private hospital, as the Commission concluded in the Second Aorangi Decision.
- 10.5 At the time of the Second Aorangi Decision in 2012, Crest Hospital was doing little public work. The four theatres and one procedure room were more than adequate. [] Surgeons at Crest Hospital are operating on a number of public patients within their private lists (under a different contract), so more private lists are needed. [] is still more than adequate for the local demand for private surgery in the Manawatū.
- 10.6 Based on patient numbers, which have fluctuated over time, the non-public work at Crest Hospital has grown only a net [] between the first year of the merger (FY2013) and FY2022. A [] increase in private patient numbers still would not have made two private hospitals viable, confirming the Commission's Second Aorangi Decision.
- []
- 10.7 When public work is included, patient numbers at Crest []. Crest Hospital now has a [] contract in place with Health NZ []. However, any additional capacity required to support public work is [].
- []
- 10.8 Even with the public work, theatre utilisation at Crest is [] The statistics on Crest Hospital's private and public patient numbers and theatre utilisation from 2018 to 2021, are set out below for reference.
- []
- 10.9 Finally, as the Commission recognised in the First Aorangi Decision, Health NZ contracts cannot be relied on for any particular volume of work, as they are ad hoc, and often at a low level of profitability.

Crest Hospital outsourcing

- 10.10 Crest Hospital itself will require further space in the near future. [].
- 10.11 [] The Proposed Medical Facility due to be constructed by CHL will therefore provide opportunities for Crest Hospital to more optimally utilise its own capacity.

No other competitive effects

- 10.12 The parties are confident that the Proposed Transaction does not give rise to any substantial lessening of competition in any market in New Zealand by way of any other competitive effects, such as coordinated, conglomerate or vertical effects.

11. CONCLUSION

- 11.1 For the above reasons, the Applicant is confident that the Proposed Transaction does not give rise to any substantial lessening of competition in any market in New Zealand.

12. FURTHER DOCUMENTATION / INFORMATION**The Applicant**

Names and contact details of in-patient and out-patient healthcare facility operators in Manawatū

Healthcare facility operator	Contact Details
Te Te Pae Hauora o Ruahine o Turaroa MidCentral (PN Hospital)	Jeff Brown, Interim District Director Te Te Pae Hauora o Ruahine o Turaroa MidCentral
Crest Hospital	Lorna Grove, CEO Crest Hospital Limited []

Key customers in New Zealand

Crest Hospital's top 5 customers FY22

Customer	Contact Details	Annual value
[
]

Key suppliers in New Zealand

Crest Hospital's top 5 suppliers FY22

Supplier	Contact Details	Annual expenditure
[
]

Trade or industry associations*CHOL*

- 12.1 CHOL, or its shareholders, are registered with the appropriate medical and surgical colleges of New Zealand based on their clinical practice and the Medical Council of New Zealand.

SCHL/Aorangi

- 12.2 In addition to the above associations (as applicable) SCHL and Crest Hospital are members of:

(a) New Zealand Private Hospitals Association

- 12.3 The current Aorangi shareholders are members of:

(a) Medical Council of New Zealand;

(b) Australasian Royal College of Surgeons.

Copies of most recent financial statements

- 12.4 Copies of CHOL and CHL annual financial statements for FY21/22 are included at **CAB.004**.

PART E: CONFIDENTIALITY**13. REASONS FOR SEEKING CONFIDENTIALITY**

- 13.1 Confidentiality is sought in respect of the information in this application that is contained in square brackets (with confidentiality indicated by the coloured highlighting). Confidentiality is sought for the purposes of s 9(2)(b) of the Official Information Act 1982 on the grounds that:
- (a) The information is commercially sensitive and valuable information which is confidential to the parties; and
 - (b) Disclosure would be likely to unreasonably prejudice the commercial position of the parties, as the entities providing the information.
- 13.2 The parties request that they are notified of any request made to the Commission under the Official Information Act 1982 for release of the confidential information. The parties also request that the Commission seek and consider the Applicant's or the Target's views, as the case may be, as to whether the information remains confidential and commercially sensitive at the time responses to such requests are being considered.
- 13.3 The foregoing equally applies in respect of any additional information provided to the Commission that is expressed to be confidential.

PART F: DECLARATION

I, Colin Hutchison, have supervised the preparation of this notice seeking clearance.

To the best of my knowledge, I confirm that:

- all the information specified by the Commission has been supplied;
- if the information has not been supplied, reasons have been included as to why the information has not been supplied;
- all information known to me that is relevant to the consideration of this notice has been supplied; and
- all information supplied is correct as at the date of this notice.

I undertake to advise the Commission immediately of any material change in circumstances relating to the notice.

I understand that it is an offence under the Commerce Act to attempt to deceive or knowingly mislead the Commission in respect of any matter before the Commission, including in these documents.

I am a director/officer of the company and am duly authorised to submit this notice.

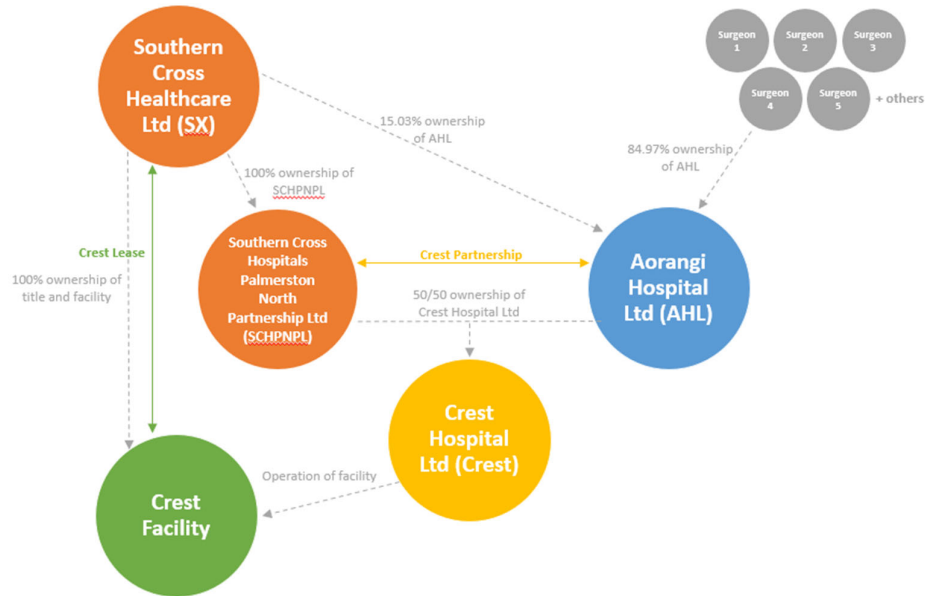
Colin Hutchison
Director of Central Healthcare Operations Limited

Signature

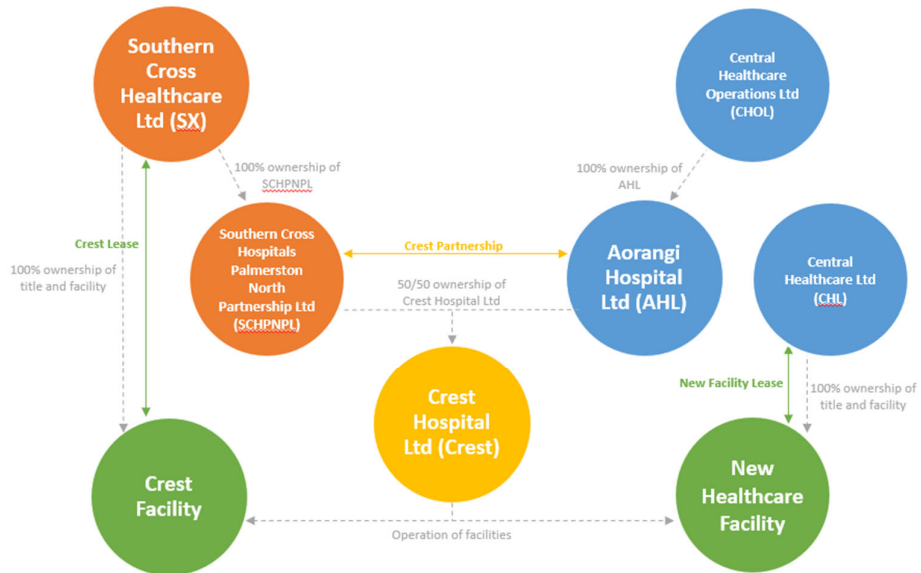
Date

APPENDIX A: Pre- and post-transaction corporate structure diagrams

Current structure



Proposed new structure



APPENDIX B: Confidential appendix relating to CHOL Counterfactual

1.1 []