PUBLIC VERSION

COMMERCE ACT 1986: BUSINESS ACQUISITION SECTION 66: NOTICE SEEKING CLEARANCE

23 December 2004

By email: registrar@comcom.govt.nz

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

THE SOUTHERN CROSS HEALTH TRUST: AUCKLAND SURGICAL CENTRE LIMITED

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

PART I: TRANSACTION DETAILS

1. The business acquisition

1.1 Clearance is sought for the proposed acquisition by The Southern Cross Health Trust or its interconnected body corporate ("the Trust") of the assets of Auckland Surgical Centre Limited ("ASC").

2. The person giving notice

2.1 This notice is given by:

The Southern Cross Health Trust
181 Grafton Road
Private Bag 99934
Auckland

Attention: Terry Moore
Telephone: (09) 356 0917
Facsimile: (09) 366 1423

2.2 Correspondence and inquiries should in the first instance be addressed to:

Minter Ellison Rudd Watts
Lawyers
Bank of New Zealand Tower
125 Queen Street
PO Box 3798
Auckland

Attention: Andrew Matthews / Melanie Tollemache
Telephone: (09) 353 9700
Direct dial: (09) 353 9847 / (09) 353 9793
Facsimile: (09) 353 9701
Email: andrew.matthews@minterellison.co.nz
melanie.tollemache@minterellison.co.nz

3. **Confidentiality**

3.1 Confidentiality is not claimed for the fact this notice is made.

3.2 Confidentiality is sought for that information included in square brackets. A copy of this notice with the confidential information deleted is provided for the Commission's assistance.

3.3 Confidentiality is sought until the confidentiality request is withdrawn.

3.4 This request is made because the information is commercially sensitive and disclosure would be likely unreasonably to prejudice the commercial position of the parties. This request is made initially under section 100 of the Commerce Act 1986 and subsequently under section 9 of the Official Information Act 1982.

4. **Details of the participants**

4.1 The acquirer is the Trust. Contact details are set out in paragraph 2.1.

4.2 The target:

Auckland Surgical Centre Limited
C/- Reeder Smith
Level 3, 60 Parnell Road
Parnell
Auckland

Attention: Philip Leightley
Telephone: (021) 775 504/(09) 523 3580
Facsimile: (09) 520 0124

4.3 Correspondence and inquiries should in the first instance be addressed to:

Russell McVeagh
Lawyers
48 Shortland St
PO Box 8
Auckland

Attention: Sarah Keene
Telephone: (09) 367 8000
Direct dial: (09) 367 8133
Facsimile: (09) 367 8163
Email: sarah.keene@russellmcveagh.com

5. **Parties interconnected to or associated with each participant**

5.1 Acquirer group/associates:

(a) The Trust is the acquirer.

(b) The Trust is a charitable trust, established for the purposes of providing hospital care to the general public, the beneficiaries of which are effectively all New Zealanders. The Trustees of The Trust are registered as a Board under the Charitable Trusts Act 1957. The Trust owns 9 hospitals[1] and has partnerships in another four[2]. These

[1] Brightside, Christchurch, Hamilton, Invercargill, New Plymouth, North Harbour, Palmerston North, Rotorua and Wellington.

hospitals are used by independent surgeons to provide a range of surgical services (including otolaryngology, ophthalmology, general surgery, gynaecology, orthopaedic, plastic, urology and endoscopy).

(c) In *Southern Cross Oxford Hospital Limited/Oxford Clinic*, Decision No. 537 ("*Oxford Clinic*") the Commission concluded that, for the purposes of considering the acquisition in that case, it would proceed on the basis that the Trust and The Southern Cross Medical Care Society ("The Society") were "associated persons" within the meaning of s47(3) of the Commerce Act.

(d) The Trust does not agree with the Commission's conclusion on association. However, the Trust does not propose to pursue this issue in this application as it does not consider that the Commission's view affects the analysis of the proposed acquisition.

5.2 Target group/associates:

The target is ASC. ASC's shareholding is attached as Appendix 1.

6. Inter-participant interests

6.1 No participant has any beneficial interest in any other participant.

7. Inter-participants links

7.1 There are no existing links between the Trust and ASC or ASC's shareholders except that some of the shareholders of ASC operate at the Trust's Auckland hospitals from time to time. In addition, the Trust's contract with ACC (which covers all three facilities) is held jointly with [ ].

8. Common directorships

8.1 None of the trustees of the Trust are directors or trustees of any hospitals other than those owned by the Trust.

9. Business activities

The Trust

9.1 The Trust owns two hospital facilities in Auckland, Southern Cross Brightside Hospital ("Brightside") and Southern Cross North Harbour Hospital ("North Harbour"). It also has a 50% joint venture interest in Gillies Hospital Limited ("Gillies") (the other 50% share is owned by Surgical Group Limited). Secondary elective procedures are performed on both a day-stay and in-patient basis at all three facilities[3]. The Trust does not employ surgeons or contract surgeons to provide any surgical services.

9.2 The Brightside facility has 4 operating theatres and 53 in-patient beds and is used to carry out general surgery, orthopaedics, gynaecological, urological, plastics and ear, nose & throat ("ENT"). The hospital is best known for its gynaecological, orthopaedics, general surgery, oral and maxillofacial and urological care. About [ ] of the procedures are performed on a day-stay basis.

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[2] Gillies Hospital (Auckland), Mercy Angiography Unit (Auckland), Norfolk Southern Cross Hospital (Tauranga), and Southern Cross Oxford Hospital (Christchurch).

[3] The only exception being certain ACC surgery, and DHB arrangements.

9.3 The North Harbour facility has 4 operating theatres and 63 beds and is used to carry out a wide range of procedures including general surgery, orthopaedics, gynaecological, plastics and ENT. It is best known for its general, gynaecological, orthopaedics, plastics and ENT surgery. About [%] of its procedures are performed on a day-stay basis.

9.4 The Gillies facility has 3 operating theatres and 20 beds. It is best known for its ENT work. It is primarily a day-stay facility with about [%] of its procedures being on a day-stay basis.

The Auckland Surgical Centre

9.5 ASC is primarily a day-stay facility (day-stay surgery comprises about [%] of ASC's procedures) at which orthopaedic, plastic, gynaecological, ENT, oral, paediatric, breast, urology and general surgery is performed, with a strong focus on orthopaedic procedures.

10. **Reasons and intentions**

10.1 The Trust sees the acquisition as a way to [

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PART II: IDENTIFICATION OF MARKETS AFFECTED

11. **Horizontal Aggregation**

11.1 The acquisition will result in aggregation in the provision of hospital facilities and related non-specialist services for elective secondary services in the Auckland region. There will be no aggregation in the provision of surgical services as the Trust only provides facilities[4].

Hospital facilities versus separate public and private hospital facilities

11.2 With one exception[5] the Commission has adopted separate markets for the provision of hospital facilities and related non-specialist services for elective secondary surgery to private and public patients. The Trust agrees with the Commission's approach in earlier decisions of categorising separate secondary elective and tertiary surgery markets, and treating the services provided by hospitals (i.e. the provision of its facilities and related non-specialist services) as one product market.

11.3 The Trust disagrees with the Commission's view that the product market is limited to private patients or facilities. The High Court has also recently accepted that public and private hospitals compete in the provision of cataract surgery in Southland[6].

11.4 The Trust considers (as did the Commission, for example, in *Ascot/Mercy*[7]) that public hospitals impose a constraint on the private market by providing a choice for patients, by contracting out work to the private sector, and by having the potential (subject to political priorities) to undertake private work.

11.5 The issue of patient choice was highlighted by the High Court in the *Ophthalmologists* case:

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[4] Subject to the limited exception described in paragraph 9.1 and footnote 3 above.

[5] *Eastbay Health Limited and Western Bay Health Limited*, Decision 331, 19 November 1998.

[6] *The Commerce Commission v The Ophthalmological Society of NZ Ltd*, 1/3/2004, Gendall J, Wellington, paragraph 192 ("*Ophthalmologists* case").

[7] *The Ascot Hospital and Clinics Limited/Mercy Hospital Auckland Limited*, Decision No. 449, paragraphs 49-52.

> ...the relevant market is for cataract surgery ("routine"...elective") including pre-assessment and follow-up, provided to people in the Southland area. I find that cataract surgery is a distinct product market.
>
> That market includes all of those customers (patients) who require surgery for the eye condition whether they are able to pay for it themselves, personally or through health insurance, so that it may be performed privately, or whether they are required to have the surgery performed in public without cost to them. **If waiting times in the public sector are short, less may be willing to pay for private surgery. If private surgery prices are reduced it is likely that more may opt for that service.** ... Private and public routine cataract surgery is in the same market.[8]

11.6 One of the reasons given by the Commission in *Southern Cross Oxford Hospital Limited/The Oxford Clinic*[9] ("*Oxford Clinic*") for its conclusion that the constraints it referred to in *Ascot/Mercy* were not sufficient for public and private hospitals to be in the same market, was that government policy since 2000 was focussed on reducing waiting lists so that public providers were discouraged from seeking private business.

11.7 However, while that policy may have limited the ability of public providers to seek private business, it has led to an increase in the contracting out of work to the private sector. In *Oxford Clinic* the Commission referred to the fact that most work undertaken by private hospitals is privately funded, with only 6% of their funding coming from DHBs.[10]

11.8 The Trust considers that a funder providing 6% of its revenue to be a significant constraint. Moreover, there is significant geographical variation in the percentage of private hospital revenue comprised by DHB funding, depending on specific local conditions. Current conditions in Auckland, for example, have meant a substantial increase in the amount of public work contracted out to the private sector.

11.9 For example Waitemata DHB has recently run open tenders for gynaecology, general surgery and joint replacement in order to reduce its waiting times and to cope with theatre constraints caused by major refurbishment at the North Shore hospital. Auckland DHB has run open tenders for hernias, joint replacement and general surgery as has Counties Manukau DHB for joint replacement surgery (the successful tenderer in relation to the joint replacement surgery for both Counties Manukau and Auckland DHB's was MercyAscot). The level of this contracting out to the private sector is such that these DHB contracts constitute about [%] of North Harbour's and Brightside's revenue at present.

11.10 For the reasons set out above the Trust is of the view that the constraints provided by public hospitals are such that they should be treated as falling within the same market as private hospitals. However, for the purposes of this application, the Trust has followed the Commission's market definition and has provided market share information relating only to private hospital facilities.

Private hospitals v separate day-stay and in-patient hospitals

11.11 The Commission has previously concluded that all hospitals, including those limited to day-stay, are within the same market, but that the in-patient facilities could be considered closer substitutes than the day-stay facilities.[11]

11.12 However, in its most recent decision on hospital mergers, *Oxford Clinic*, the Commission, while "acknowledging that there are arguments in favour of both a narrow and broad product market"[12] adopted even narrower market definitions for the purposes of that

[8] *Ophthalmologists* case at paragraph 192, emphasis added.

[9] Decision No. 537, paragraph 67.

[10] Paragraph 63.

[11] For example, *Ascot/Mercy* at paragraph 97.

[12] Paragraph 90.

application, separating in-patient and day-stay markets. The relevant product markets adopted by the Commission were the provision of private:

- day-patient hospital facilities and related non-specialist services for elective secondary surgery;
- in-patient hospital facilities and related non-specialist services for elective secondary surgery.

11.13 Subject to the Trust's comments in paragraph 11.3, the Trust's view is that the appropriate market is the provision of private hospital facilities and related non-specialist services for elective secondary surgery, encompassing both day-stay and in-patient facilities. Given the changing nature of surgical technology and advances in anaesthesia which are constantly expanding the range of procedures which can be performed on a day-stay basis, a fixed distinction between day-stay and in-patient facilities is artificial. This is illustrated by the fact that while there are procedure rooms which perform only day-stay surgery, most hospital facilities provide a range of both in-patient and day-stay surgical procedures.

11.14 This means that for many procedures, in-patient hospital facilities and day-stay facilities are close substitutes. Procedures which do not require the cutting of tissue can be carried out either at a procedure room or at a hospital facility (ie day-stay or in-patient), and in both cases on a day-stay basis (examples of such procedures are endoscopy, minor gynaecological surgery and removal of skin lesions).

11.15 Those procedures that require the cutting of tissue have to be carried out in a fully-sterile theatre[13], but whether that is done on an in-patient or day-stay basis will depend on the complexity of the procedure involved which will determine the recuperation and medical supervision needs of the patient. Moreover, whether a patient stays in a facility overnight or not is often a function of the time of day when the operation is conducted, and not the nature of the surgery itself. Furthermore, an overnight stay is not determinative of the surgery being in-patient since day-stay facilities will often include 23 hour beds.

11.16 In conclusion, the Trust's view is that there is a continuum of surgical procedures which can be performed in facilities ranging from procedure rooms to day-stay theatres to in-patient facilities.

Geographic scope of the market

11.17 In *Ascot/Mercy* the Commission concluded that one of the relevant markets (hospital facilities and related non-specialist services for elective surgery to private patients) was limited to the Auckland region. The Trust agrees with this as the geographical scope of the market.

Differentiated Product Markets

12. Characterisation of the relevant products as standardised or differentiated

12.1 As the Commission referred to in *Ascot/Mercy* there is some variation in the degree to which in-patient and day-stay facilities are substitutes for each other[14].

13. For differentiated product markets

13.1 The Trust's view is that there are some distinctions between facilities which provide only day-stay surgery and those providing a mixture of in-patient and day-stay surgery, but not to the extent that they fall within separate facilities markets. The main distinctions between

[13] All of the 53 theatres set out in Appendix 2 are fully sterile and are equipped to perform surgery under general anaesthetic.

[14] Paragraph 90.

facilities solely providing day-stay and those providing day-stay and in-patient procedures, are the nature of the theatres and the extent of infrastructure such as bathrooms, kitchens and laundries necessary for in-patient services.

13.2 Despite the differentiation in the private hospitals facilities market, the merged entity will continue to be constrained by other suppliers, both those providing a mixture of in-patient and day-stay surgery, and those providing only day-stay surgery.

14. Vertical Integration

14.1 The proposal will not result in any vertical integration.

15. Previous acquisitions

15.1 On 8 October 2003 Southern Cross Oxford Hospital Limited, which is owned 50% by a subsidiary of the Trust, notified the Commission of its proposed acquisition of the assets of the Oxford Clinic in Christchurch. Clearance for that acquisition was granted on 11 November 2004 in *Oxford Clinic*.

15.2 There are no previous acquisitions notified by ASC.

PART III: CONSTRAINTS ON MARKET POWER BY EXISTING COMPETITION

16. Existing competitors

16.1 Existing competitors in the Auckland region comprise the 53 private facilities owned by 24 providers, specialist procedure rooms, and the facilities of three DHBs, Auckland, Waitemata and Counties Manukau. Private suppliers of facilities are:

(a) **The Trust's facilities**:

- Information about the Brightside, North Harbour and Gillies facilities is set out above in 9.1-9.4.

(b) **MercyAscot**:

- **Ascot Hospital** provides a broad range of surgical, medical and related services with facilities ranging from day stay to longer stay services for very complex procedures. It houses the consulting rooms of surgical and medical specialists and has 12 state-of-the-art operating theatres, 68 single in-patient rooms, a dedicated 5 bed Intensive Care Unit, a 5 bed Coronary Care Unit, a 6 bed short-stay unit with single bedrooms and a day surgical facility with accommodation for up to 26 patients at a time.

- **Mercy Hospital** is a 155 bed hospital providing a broad range of surgical, medical and related services with facilities ranging from day-stay, an overnight service and a longer stay service for more complex cases. Many specialists consult in practice rooms near to or within Mercy Hospital. Over 100 on-site specialists provide services and on-site surgeons perform surgery in 7 state-of-the-art operating rooms.

(c) **The Auckland Surgical Centre** is primarily a day-stay facility (day-stay surgery comprises about [%] of ASC's procedures) at which orthopaedic, plastic, gynaecological, ENT, oral, paediatric, breast, urology and general surgery is performed.

(d) **The Northern Clinic** provides a wide range of procedures at its 2 theatres on both an in-patient and day-stay basis.

(e) **Quay Park Surgical** provides a range of urology, oral and maxillofacial and plastic surgery at its 2 theatres and 1 procedure room on both a day-stay and in-patient basis.

(f) **Navy (Devonport)** provides facilities for private elective patients as well as for the military at its 2 theatres, and has recently been contracted by Waitemata DHB to provide some limited DHB procedures.

(g) **Shore Surgery Limited** provides a range of surgery at its 2 theatres on a day-stay.

(h) **The Eye Institute** provides a range of ophthalmological procedures at its theatre on a day-stay basis.

(i) **Laparoscopy Auckland** provides a range of general surgery at its 1 theatre on a day-stay basis.

(j) **Manukau Health Trust** provides a range of surgery at its 1 theatre and 1 procedure room on a day-stay basis.

(k) **St. Marks Eye Hospital/Auckland Eye** provides ophthalmology surgery at its 1 theatre on a day-stay basis.

(l) **243 Surgical Centre Limited** provides a range of plastic surgery at its 1 theatre on a day-stay basis.

(m) **Auckland Gynaecology Group** provides gynaecology surgery at its 1 procedure room on a day-stay basis.

(n) **Auckland Plastic Surgical Centre** provides plastic surgery on a day-stay basis at its 1 theatre.

(o) **Auckland Theatre Services** provides plastic surgery at its 1 theatre on a day-stay basis.

(p) **The Elliot Trust** provides plastic surgery at its 1 theatre on a day-stay basis.

(q) **Endoscopy Auckland** provides endoscopy services at its 1 theatre on a day-stay basis.

(r) **The New Zealand Institute of Plastic Surgery** provides plastic surgery at its 1 theatre on a day-stay basis.

(s) **Remuera Surgical Centre** provides plastic surgery at its 1 procedure room on a day-stay basis.

(t) **Skin Institute Limited** provides plastic surgery at its 1 theatre on a day-stay basis.

(u) **Skin Specialist Centre** provides plastic surgery at its 1 theatre on a day-stay basis.

(v) **Surgery on Shakespeare** provides gynaecology surgery at its 1 theatre on a day-stay basis.

(w) **Urology 161** provides urology surgery at its 1 theatre on a day-stay basis.

(x) **Bracken Medical Centre** provides a range of plastic surgery at its 1 theatre on a day-stay basis.

(y) the procedure rooms set out in Appendix 2 provide a range of surgery on a day-stay basis, including gynaecology, plastic surgery and endoscopy.

Hospital facilities for elective secondary services for private patients

16.2 In *Oxford Clinic* the Commission concluded that, for the purposes of evaluating Southern Cross Oxford Hospital Limited's acquisition of the assets of the Oxford Clinic business in Christchurch, it would adopt separate product markets for in-patient and day-patient surgical facilities.

16.3 The Trust's view is that the appropriate hospital facilities market is one which encompasses both in-patient and day-stay facilities. As referred to above, none of the Trust's own or joint venture hospitals collects market share figures based on separate day-stay and in-patient categories.

16.4 While there is uncertainty about the market share data, the Trust believes that post-acquisition it would not exceed the Commission's lower safe harbour. The Trust's view is that post-acquisition, its facilities would be likely to have approximately [%] of the market for private hospital facilities and related non-specialist services for elective secondary surgery in the Auckland region.

16.5 In estimating market shares, the Trust has followed the Commission's approach in *Ascot/Mercy* to using theatres as the appropriate measure of market share:

> It is acknowledged that operating theatres are not a perfect measure of market share. Surgical procedures vary considerably by complexity, time and cost, so the output of one theatre may be very different from the output of another. Similarly, the theatres may have different equipment or be set up with different procedures in mind. However, to the extent that surgical facilities can be used across a variety of branches of medicine (notwithstanding the distinction between secondary and tertiary care) the number of theatres is a useful proxy to market share.[15]

16.6 Post-acquisition, the parties will be constrained by a number of factors including:

(a) a very strong competitor in MercyAscot which will remain by far the largest competitor in the market;

(b) a number of other competitors, including day-stay (including 23 hour stay) and in-patient facilities and specialist procedure rooms;

(c) the threat of new entry (see below);

(d) the countervailing power of:

(i) the ACC;

(ii) the three DHBs;

(iii) insurance companies; and

(iv) surgeons.[16]

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[15] *Ascot/Mercy* at para 98.

[16] The influence of the ACC, insurance companies and surgeries have all been noted as strong constraints in the Commission's previous decisions.

Existing competition

16.7 As can be seen from the theatre-based information set out in Appendix 2, post-acquisition MercyAscot would still be the most significant competitor in the Auckland market and there are many other theatre facilities and specialist clinics which compete either across all specialities or in focussed areas.

The threat of new entry

16.8 Given that the barriers to entry (particularly in day-stay) are low, the threat of entry is a real constraint.[17] The Commission has concluded that there "*are no structural or regulatory barriers that constitute a material barrier to new entry*", that "*the capital costs of establishing a new hospital are not sufficiently high to constitute a material barrier . . . and that the low return on capital is correctly regarded as a sign of a competitive market*"[18]. The Commission has pointed to the growth of day-stay surgery due to technological advances and the particular ease of entry for day-stay surgeries.[19] The Commission also noted:

> *Boulcott considered that a new day surgery could be operational within 6-12 months with capital costs of approximately $1 million. However, facilities and equipment can be leased, thus reducing the capital cost associated with them. The experience of Ascot in Auckland suggests that de novo entry of a significant scale can be accomplished within two years of planning being commenced. Furthermore, the experience in Auckland in the last 6 years where there has been entry by four surgical centres indicates that entry into the secondary surgical market is not slow.*
>
> . . .
>
> *The Commission concludes that the barriers to entry are low and the prospect of entry in the event of the merged entity attempting to exercise market power is sufficiently tangible to be a constraint on the merged entity in the post-acquisition market".*[20]

16.9 The Commission's comments in *Oxford Clinic* are relevant as in that case (as here) the facility being acquired conducted primarily day-stay procedures. In *Oxford Clinic*, the Commission concluded that overall, it considered the capital costs of setting up private day patient hospital facilities to be low[21]. In applying the LET test the Commission also noted that some GPs have begun to enter the day surgery market in Christchurch market and that "a number of GP clinics in Auckland already perform some day procedures, such as hernia operations and vasectomies"[22].

16.10 In noting the increasing popularity of day surgeries made possible by technological advances, the Commission noted that:

> *A new day surgery is most likely to occur in the secondary market where the volume of operations is high and the degree of sophistication is low; such as for endoscopy, low complexity orthopaedic, general surgical and hernia procedures. In some cases procedures may be undertaken in a surgeon's consulting room.*[23]

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[17] *Ascot/Mercy*, at para 151.

[18] *Wakefield/Bowen*, at paras 157, 158.

[19] *Wakefield/Bowen*, for example, at paras 168, 169.

[20] *Wakefield/Bowen, at* paragraphs 175 and 177.

[21] Paragraph 134.

[22] Paragraph 154.

[23] *Oxford Clinic* at paragraph 158.

16.11 Surgical, anaesthetic and technological advances now mean that a wide variety of procedures can be conducted on a day-stay basis. All of ASC's cases would fit this description. Therefore ease of entry in these areas of procedure is high. With surgical support, ASC's operation could be replicated within 6-12 months.

ACC

16.12 ACC was recognised by the Commission in *Wakefield/Bowen* as having "significant" countervailing power.[24] In *Oxford Clinic* the Commission noted that ACC contracts provide a "*significant sum of funding for some private hospitals*".[25] This is certainly the case with ASC. Approximately [%] of ASC's revenue comes from ACC. This contract commenced on [ ] and runs for two years.

16.13 The Trust's current ACC contract is in the name of [ ]. It runs from July 2004 until July 2006. ACC funding comprises approximately [%] of the Trust's revenue in Auckland.

16.14 Clearly ACC is a powerful constraint in relation to both the Trust's and ASC's revenue. The ACC's power to influence where surgery is conducted is illustrated by the fact that until [ ], when the [ ] contract with ACC began, no orthopaedic work was carried out at Brightside. However, a movement in that funding to another provider (particularly if ACC's proposed surgeon-based funding model eventuates) could leave Brightside without orthopaedic work.

16.15 While the current ACC model is based on contracts with facilities, it is possible that ACC may propose a revision of its model which may open this funding up to more potential providers.[26] Hospitals may have access agreements with ACC and supply ACC with a list of specialists who perform surgery at that facility and specialists could then appear on multiple facility contracts. In addition, the existing capping of budgets (which does not apply to the DHBs), which limits how much work a facility with an ACC contract can undertake, may end. Under this proposed change, as long as the work being undertaken falls within ACC's specifications, ACC would pay for it. This has a significant potential to increase the level of ACC funding which the DHBs and the private sector compete for.[27]

DHBs

16.16 In addition to competing with private hospitals for ACC funding, the Auckland-based DHBs (Auckland, Waitemata and Counties Manukau) also pose a constraint through their ability to contract work out to the private sector. Both Brightside and North Harbour have recently undertaken short-term contracts for the DHBs in Auckland as set out below:

[

[24] *Wakefield/Bowen*, at paragraph 184.

[25] *Wakefield/Bowen*, for example, at paras 168, 169.

[26] ACC has also introduced national, as opposed to regional, pricing.

[27] This competition between the DHBs and the private sector was recognised by the Commission in *Oxford Clinic* at para 63 where it referred to its previous conclusion that "for publicly funded operations, public and private institutions are in the same market".

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16.17 New Zealand-wide, funding from DHBs comprises about [%] of the Trust's revenue. In the Auckland region, this funding comprises about [%] of revenue for the Trust.

Insurers

16.18 The role of insurers as a constraint on hospitals has been recognised by the Commission. For example, in *Wakefield/Bowen* the Commission commented that:

> The Commission considers that the constraints that buyers can effect in the market are significant. These constraints arise from the role of ACC and insurance companies as significant purchasers and funders in the market, and the potential competition from public hospitals. Surgeons and other healthcare providers also have a degree of countervailing power. ... These constraints are difficult to quantify in terms of their ability to constrain an increase in price. However, the cumulative impact of these constraints, coupled with low entry barriers, will be an effective constraint to prevent the merged entity from exercising market power.[28]

16.19 In *Ascot/Mercy* the Commission also stated that "health insurance will make many patients less price sensitive, but in turn heightens the price sensitivity of the insurer".[29] In *Oxford Clinic* the Commission concluded that:

> On the whole [it] considers that health insurance companies provide an important source of revenue and are likely to provide some constraint on the proposed joint venture and this is unlikely to be affected by the proposed joint venture.[30]

16.20 The Trust's view is that the constraint imposed by insurance companies on the Trust's facilities, both at present and post-merger, is considerable (and is one of only a number of constraints). Nor does it believe that this constraint is at all lessened by the Commission's conclusion in *Oxford Clinic* that the Trust and the Society are associated. In order to meet its obligations to its members, the Society is highly motivated to ensure that all suppliers of services to its members provide the highest quality services at the most competitive prices.

Surgeons

16.21 In *Oxford Clinic* the Commission discussed the role of surgeons in the hospital facilities markets. It noted that surgeons can impose a constraint on hospital facility pricing by choosing a cheaper hospital where the patient is paying for the surgery themselves[31]. And in general, surgeons guard the right to direct patients to the facilities of their choice. In addition, surgeons will exercise their ability to switch between private hospitals in the event of increased hospital charges or reduced quality of service, as this would reflect poorly on the surgeon.[32]

16.22 There is no aggregation of surgical services and the Trust does not consider that the acquisition will result in any material effects in relation to surgical services. The shareholders of ASC will be free to operate at any facility [

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[28] *Wakefield/Bowen* at paragraphs 182 and 189.

[29] *Mercy/Ascot*, at paragraph 124.

[30] *Oxford Clinic*, at paragraph 177.

[31] *Oxford Clinic*, at paragraph 179.

[32] *Oxford Clinic*, at paragraph 179.

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Other Considerations

16.23 The Trust notes:

(a) regardless of whether public hospitals are included in the market, they represent a significant constraint;

(b) barriers to entry are low and the threat of new entry is particularly high in respect of day-stay facilities which is the principal focus of ASC;

(c) recent examples of new entry occurred in Hamilton, where a group of clinicians established their own facility, the Bridgeway Day Surgery, in a short period of time, and the establishment of Quay Park Surgery in Central Auckland, and the Northern Clinic on Auckland's North Shore.

17. Conditions of expansion

17.1 The Trust considers that constraints imposed by existing competitors are sufficient to ensure that the acquisition would not result in a substantial lessening of competition. MercyAscot remains the largest hospital facility in the region and existing competitors can readily increase their supply by increasing utilisation of existing capacity or expanding capacity.

17.2 Expansion can be undertaken swiftly – this could occur in as little as 6-12 months. MercyAscot has the ability to add further theatres to increase its existing capacity should it wish. Further, given the low barriers to entry, the threat of new entry is a strong constraint, as recognised by the Commission[33] and demonstrated by the entry of facilities such as Quay Park Surgical and the Northern Clinic and the growth of procedure rooms performing day-stay surgery.

17.3 The merged entity could not have the power to sustainably increase prices and/or to reduce quality of its services relative to what would have occurred in the absence of the acquisition.

Co-ordinated Market Power

18. The Trust notes that the Commission has previously accepted that collusion is unlikely as the industry structure does not enable discipline due to the low barriers to entry, and the close monitoring of price and the countervailing power of insurance providers and ACC.[34] That observation was made in the context of a much more highly concentrated market, and the Trust agrees that this conclusion is even more relevant in the competitive Auckland environment.

19. In *Oxford Clinic* the Commission confirmed that any collusion between hospital providers would be easily detected by patients, surgeons, insurance companies and the ACC. The

[33] *Oxford Clinic* at paragraph 163.

[34] *Wakefield/Bowen*, for example, at paragraphs 140, 141.

Trust is also of the view that the DHBs would closely monitor any potentially collusive behaviour.

20. The Trust does not consider that the market is susceptible to collusion, but otherwise agrees with the Commission's comments. Given the above, the Trust briefly reproduces the Commission's criteria below,[35] but does not deal further with them here.

21. Table 4: Testing the Potential for Collusion

Factors conducive to collusion	Presence of factors in all relevant markets
High seller concentration	No
Undifferentiated product	Partially (there is further differentiation between public and private facilities)
New entry slow	No
Lack of fringe competitors	No (specialist procedure rooms and the public system)
Price inelastic demand curve	In *Ascot/Mercy* the Commission stated that it did not view demand for these services as inelastic and the Trust agrees that demand is relatively elastic.
Industry's poor competition record	No
Presence of excess capacity	Variable
Presence of industry associations/fora?	Yes

22. **Table 5: Testing the Potential for Discipline**

Factors conducive to discipline	Presence of factors in all relevant markets
High seller concentration	No
Sales small and frequent	No
Absence of vertical integration	Yes[36]
Demand slow growing	Varies across market and depends on government policy, but growth in day-stay procedures is high
Firms have similar costs	Yes (varies again when take public system into account)
Price transparency	Variable

23. The acquisition will not increase the risk of co-ordinated behaviour in the relevant markets due to the large number of market participants, the role of the public health sector, the lack of barriers to entry/expansion and the strong incentive on surgeons, public funders (ACC and the DHBs) and health insurers to resist any attempts at co-ordination.

[35] The Trust notes that the Commission's Mergers & Acquisitions Guidelines refer to retaliation as part of this analysis. The Trust does not view that distinction as adding further to the analysis in this case.

[36] The Trust is not vertically integrated (cf. Table 3, para 128 and para 131 of *Wakefield/Bowen*).

24. **PART IV: CONSTRAINTS ON MARKET POWER BY POTENTIAL COMPETITION**

25. The Trust considers that the constraint imposed by MercyAscot and other smaller surgical facilities and specialist clinics is sufficient to ensure that competition will not be lessened. Further significant constraints come from the public hospitals and the countervailing power of surgeons, the ACC, insurers and the DHBs.

26. In addition, there are new facilities planned in Auckland, which would compete with the merged entity. The Trust is aware that the new Albany facility, called the Apollo Hospital, is in advanced stages of planning.

27. Given the above factors, and the Commission's clear statements about the low barriers to entry, the Trust does not consider it necessary to focus on potential competition.

This notice is given by Terence David Moore, Southern Cross Health Trust. I confirm that:

(a) all information specified by the Commission has been supplied; and

(b) all information known to the applicant(s) which is relevant to the consideration and determination of this application/notice has been supplied; and

(c) all information supplied is correct as at the date of this application/notice.

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

DATED this day of 2004

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Terence David Moore

I am an officer of Southern Cross Health Trust and am duly authorised to make this application.

APPENDIX 1

Auckland Surgical Centre Limited Shareholders			
Group	**Name**	**Shareholding**	**%**
Anaesthetist	S V Mayadeo Trust	147,870	3.9%
Anaesthetist	John McDougall Family Trust	140,000	3.7%
Anaesthetist	The Blyth Family Trust	120,000	3.1%
Anaesthetist	Dr Joseph Edmund Petoe	120,000	3.1%
Anaesthetist	Dr Rajpal Sarath Gooneratne	90,000	2.4%
Anaesthetist	The Krupa Trust	75,000	2.0%
Anaesthetist	Dr Malcolm Edward Futter	70,000	1.8%
Anaesthetist	Elias Family Trust	53,010	1.4%
Anaesthetist	The Nevyne Trust	50,000	1.3%
Anaesthetist	Dr David Michael Chamley	49,000	1.3%
Anaesthetist	Jonathon Cross Investment Trust	45,000	1.2%
Anaesthetist	Knarston Trust	40,000	1.0%
Anaesthetist	Kaye Ottaway Investment Trust	32,500	0.8%
Anaesthetist	Dr Graeme Andrew Crooks	32,320	0.8%
Anaesthetist	Gunn Family Trust	25,000	0.7%
Anaesthetist	Dr Neil G Middleton	25,000	0.7%
Anaesthetist	Dr C R Varad Raj	23,000	0.6%
Anaesthetist	Baker Family Trust	22,320	0.6%
Anaesthetist	Dr John Edward Blackburn	20,000	0.5%
Anaesthetist	Clovelly Trust	20,000	0.5%
Anaesthetist Total		**1,200,020**	**31.4%**
Dermatologist	Vista trust	20,000	0.5%
Dermatologist Total		**20,000**	**0.5%**
General Public	Dr Phillip Lowe	126,250	3.3%
General Public	J G Smith Family Trust	120,000	3.1%
General Public	Mr Kerry Edgar Clark	116,600	3.0%
General Public	Mr Raymond George Woolford	108,500	2.8%
General Public	Dr Alan Geoffrey Bowers	103,790	2.7%
General Public	Brown Family Trust	98,500	2.6%

General Public	Dr William Max Morrris	91,500	2.4%
General Public	Dr Kevin John McKerrow	75,000	2.0%
General Public	Dr Robert Graham Hay	72,540	1.9%
General Public	The Bijur Trust	70,000	1.8%
General Public	Dr Ashwin Chunilal	51,000	1.3%
General Public	Dr Gerald Wong	50,200	1.3%
General Public	Mr Alan Robert McKenzie	49,500	1.3%
General Public	Mr Donald Evan Murray MacCormick	45,000	1.2%
General Public	Turner Family Trust	45,000	1.2%
General Public	Guise Family Trust No. 1	35,000	0.9%
General Public	Dr Robert John Anderson	30,500	0.8%
General Public	Dr Alan Forbes Merry	22,500	0.6%
General Public	Highgate Trust	22,310	0.6%
General Public	Dr Colin Stuart Barber	20,000	0.5%
General Public	Dr Barnaby Clark	20,000	0.5%
General Public	Mr Jacob Johannes de Geus	20,000	0.5%
General Public	Mrs Susan Young	10,000	0.3%
General Public	Miss Christine Mac Donald	8,380	0.2%
General Public Total		**1,412,070**	**36.9%**
General Surgeon	The Innes Trust	122,000	3.2%
General Surgeon	David & Lien Morris Family Trust	75,890	2.0%
General Surgeon	Charlesworth Family Trust	70,000	1.8%
General Surgeon	Dr Belinda Mary Denise Scott	20,000	0.5%
General Surgeon Total		**287,890**	**7.5%**
Gynaecologist	Catabrian Trust	160,000	4.2%
Gynaecologist Total		**160,000**	**4.2%**
Orthopaedic Surgeon	Mr Leslie John Tonkin	167,500	4.4%
Orthopaedic Surgeon	Mr Barry Ross Tietjens	85,000	2.2%
Orthopaedic Surgeon	M&S Caughey Family Trust	84,460	2.2%
Orthopaedic Surgeon	E A Hardy Investment Trust	82,500	2.2%
Orthopaedic Surgeon	Dr Stuart John Walsh	40,000	1.0%
Orthopaedic Surgeon	Dr Karen Lesley Smith	20,000	0.5%
Orthopaedic Surgeon	Dr Richard John Street	20,000	0.5%

Orthopaedic Surgeon	Dr Josie Sinclair	10,000	0.3%
Orthopaedic Surgeon Total		**509,460**	**13.3%**
Paediatric Surgeon	Dr Anne Kolbe	20,000	0.5%
Paediatric Surgeon Total		**20,000**	**0.5%**
Plastic Surgeon	Mr Stephen Thomas James Gilbert	100,440	2.6%
Plastic Surgeon	Dr Martin James W Rees	50,000	1.3%
Plastic Surgeon	Mr Gary Glynne Mellow	20,000	0.5%
Plastic Surgeon Total		**170,440**	**4.5%**
Urologist	The Bassam trust	45,000	1.2%
Urologist Total		**45,000**	**1.2%**
Grand Total		**3,824,880**	**100.0%**

Appendix 2: Private Hospital and Specialist Clinic Facilities - Auckland

Facility	Specialty	Theatres	Procedure Room
243 Surgical Centre Limited (Remuera)	Plastic Surgery	1	
Ascot (Remuera)	All	12	
Auckland Eye (Remuera) / St Marks Eye Hospital	Ophthalmology	1	
Auckland Gynaecology Group (Parnell)	Gynaecology		1
Auckland Plastic Surgical Centre (Remuera)	Plastic Surgery		1
Auckland Surgical Centre (Remuera)	All	4	
Auckland Theatre Services (Epsom)	Plastic Surgery		1
Bracken Medical Centre	Plastic Surgery	1	
Brightside (Epsom)	All	4	
Elliot Trust (Remuera)	Plastic Surgery		1
Endoscopy Auckland (Epsom)	Endoscopy		1
Eye Institute (Remuera)	Ophthalmology	1	
Gillies Hospital (Epsom)	All	3	
Laparoscopy Auckland (Epsom)	General Surgery	1	
Manukau Health Trust	All	1	1
Mercy (Epsom)	All	7	
Navy (Devonport)	Plastic Surgery, Orthopaedics	2	
New Zealand Institute of Plastic Surgery	Plastic Surgery	1	
North Harbour (North Shore)	All	4	
Northern Clinic (North Shore)	All	2	
Quay Park Surgical (Auckland City)	Urology, Oral & Maxillofacial, Plastic Surgery	2	1
Remuera Surgical Centre (Remuera)	Plastic Surgery		1
Shore Surgery Limited (Milford)	All	2	
Skin Institute Limited (Takapuna)	Plastic Surgery	1	
Skin Specialist Centre (Remuera)	Plastic Surgery	1	
Surgery on Shakespeare (Milford)	Gynaecology	1	
Urology 161 (Epsom)	Urology	1	
TOTAL		**53**	**8**