ISSN 1178–2560
Decision Series
Project no. 11.04/PRJ0046251

PUBLIC version

Determination

Central Healthcare Operations Limited and Aorangi Hospital Limited [2022] NZCC 40

The Commission:	Sue Begg Dr Derek Johnston Vhari McWha
Summary of application:	An application from Central Healthcare Operations Limited seeking clearance to acquire 100% of the shares in Aorangi Hospital Limited from Southern Cross Healthcare Limited.
Determination:	Under section 66(3)(a) of the Commerce Act 1986, the Commerce Commission gives clearance to the proposed acquisition.
Date of determination:	12 December 2022

Sensitive material in this report has been removed. Its location in the document is denoted by [ ].

The proposed acquisition

1. On 2 November 2022, we registered an application (the Application) from Central Healthcare Operations Limited (Central Healthcare)[1] seeking clearance to acquire 100% of the shares in Aorangi Hospital Limited (Aorangi) from Southern Cross Healthcare Limited (Southern Cross) (the Proposed Acquisition).

2. Currently, Southern Cross and Aorangi each have 50% ownership in Crest Hospital Limited (Crest Hospital), which is the only private hospital[2] in the Manawatū region. Southern Cross also has approximately a 15% share in Aorangi.

3. To facilitate the Proposed Acquisition, Southern Cross would first purchase the shares in Aorangi that it does not already own.

4. The Proposed Acquisition would result in Central Healthcare acquiring a 50% share in Crest Hospital, with Southern Cross retaining ownership of the remaining 50% of Crest Hospital.

Our decision

5. The Commission gives clearance to the Proposed Acquisition as it is satisfied that the acquisition will not have, or would not be likely to have, the effect of substantially lessening competition in a market in New Zealand.

6. The key focus of our investigation was the assessment of the counterfactual and whether, absent the Proposed Acquisition, Central Healthcare would be likely to construct and operate a private hospital in competition with Crest Hospital.

7. We consider that in the counterfactual it is unlikely that Central Healthcare would compete with Crest Hospital. Accordingly, we are satisfied that there is unlikely to be a loss of competition arising from the Proposed Acquisition.

Our framework

8. Our approach to analysing the competition effects of mergers is based on the principles set out in our Mergers and Acquisitions Guidelines (our guidelines).[3]

9. We assess mergers using the substantial lessening of competition test. We determine whether a merger is likely to substantially lessen competition in a market by comparing the likely state of competition if the merger proceeds (the scenario with the merger, often referred to as the factual), with the likely state of competition if the merger does not proceed (the scenario without the merger, often referred to as the counterfactual).[4]

---

1 Central Healthcare is also used in this document to refer to Central Healthcare Limited, which is described in the Application at [1.4] as a sister company of Central Healthcare Operations Limited with identical shareholdings.

2 We discuss the types of services provided at private hospitals further below in the Background section.

3 Commerce Commission, *Mergers and Acquisitions Guidelines* (May 2022).

4 *Commerce Commission v Woolworths Limited* (2008) 12 TCLR 194 (CA) at [63].

10. As something can be likely even when the chance of it occurring is less than 50%, there may be multiple scenarios that are likely without the merger (and with the merger).[5] We first assess the possible scenarios that might arise without the merger and discard those that are unlikely.[6] As a practical matter, we usually focus our analysis on the likely without-the-merger scenario we consider the most competitive.[7]

11. Where a market is likely to undergo changes that will affect competition in the without-the-merger scenario, we take these changes into account.[8] For example, if, without the merger, one of the merging entities was planning to enter or expand in a market to compete with the other merging entity(s), the state of competition without the merger should reflect this.[9]

The parties and the proposed acquisition

The applicant (Central Healthcare)

12. Central Healthcare comprises a group of investors and shareholder surgeons, many of whom work at Crest Hospital.

13. Central Healthcare was formed in early 2020 with the intention of building[10] a private hospital to compete with Crest Hospital. However, it has not built a private hospital and does not currently provide any services, so there is currently no competitive overlap between it and Crest Hospital.

The target (Aorangi)

14. Aorangi has a 50% shareholding in Crest Hospital. The shareholders in Aorangi (other than Southern Cross) are a group of surgeons that are based in the Manawatū region.

Southern Cross

15. Southern Cross has a 50% shareholding in Crest Hospital and a 15% shareholding in Aorangi. As well as its shareholding in Crest Hospital, Southern Cross operates several other private hospitals across New Zealand either directly or via joint ventures.

The proposed acquisition

16. The Proposed Acquisition would result in Central Healthcare replacing Aorangi as a 50% shareholder in Crest Hospital, with Southern Cross retaining their 50% share of

---

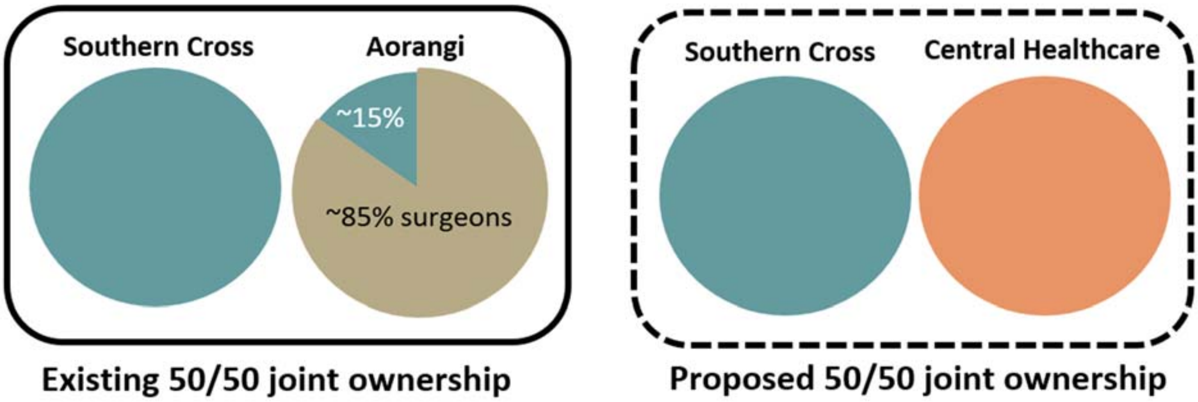
5 *Mergers and Acquisitions Guidelines,* above n 3, at [2.30].
6 *Mergers and Acquisitions Guidelines,* above n 3, at [2.31].
7 *Mergers and Acquisitions Guidelines,* above n 3, at [2.33].
8 *Mergers and Acquisitions Guidelines,* above n 3, at [2.36].
9 *Mergers and Acquisitions Guidelines,* above n 3, at [2.38].
10 The building of a private hospital is used in this document to refer to both the initial construction and subsequent operating of a private hospital.

Crest Hospital (but not their current 15% share in Aorangi). The proposed change in shareholding is shown below in Figure 1.

16.1 To facilitate the Proposed Acquisition, Southern Cross would initially acquire 100% of the shares in Aorangi (of which it currently owns approximately 15%).

16.2 Once Southern Cross owns all of the Aorangi shares, it would then sell these shares to Central Healthcare.

Figure 1: Existing and proposed shareholding in the Crest Hospital



Source: Commission estimates from Application

Background on private hospitals and elective surgery

17. The Proposed Acquisition concerns ownership of a private hospital.

18. A private hospital in the context of the Proposed Acquisition is a full service secondary elective surgical hospital with operating theatres, where work is performed for fee-paying patients. We consider the functions of a private hospital fall within both markets referred to below in the market definition section.

19. While a public hospital may provide for similar (and in some instances more complex) work than a private hospital, it does this for the public healthcare system through Te Whatu Ora - Health New Zealand (Health NZ).[11]

20. Medical facilities without operating theatres, such as radiology practices, general practice clinics and dentist facilities are not considered private or public hospitals

[11] Health NZ was established on 1 July 2022 to run the health system in New Zealand. District Health Boards have been disestablished and subsumed into Health NZ. The region most relevant to the Application is part of Health NZ – MidCentral District. This area was previously administered by MidCentral District Health Board.

(although minor procedures may be undertaken at such facilities) for the purposes of our analysis.[12]

21. There are two types of elective surgery that contribute to demand for private hospitals, being:

 21.1 private elective surgery, which is funded by health insurers, the Accident Compensation Corporation and/or patients themselves; and

 21.2 public elective surgery. Although this is most commonly performed in public hospitals, public hospitals may commission private hospitals to perform publicly funded surgery if they are short on capacity. However, industry participants informed us that private hospitals do not tend to rely on this type of work in their business planning.[13]

Market definition

22. As discussed further below, the key focus of our assessment of the Proposed Acquisition is the counterfactual and so we have not considered it necessary to reach a definitive view on market definition. Nevertheless, consistent with the submissions from the Applicant and Southern Cross, as well as previous Commission decisions, we have undertaken our analysis with reference to markets for:[14] [15]

 22.1 the provision of private short-stay (less than 24 hours) hospital facilities and related non-specialist services for elective surgery in the Health NZ – MidCentral District region; and

 22.2 the provision of private in-patient hospital facilities and related non-specialist services for elective secondary surgery in the Health NZ – MidCentral District region.

With and without scenarios

23. With the Proposed Acquisition, Central Healthcare and Southern Cross would jointly operate Crest Hospital.

24. Central Healthcare submitted that there would be no material difference between the Proposed Acquisition and any without-the-acquisition scenario because Crest Hospital would continue to be the only existing operator of a private hospital in the Manawatū region with or without the Proposed Acquisition. Because of this, Central

---

12 Consistent with feedback we received in interviews with
[ ]

13 Commerce Commission interviews with
[ ]

14 *Southern Cross Health Trust/Aorangi Hospital Limited*, 4 September 2008, Decision 650; *Southern Cross Health Trust/Aorangi Hospital Limited*, 28 July 2011, Decision 729; the Application at [9.1]-[9.5] and Commerce Commission interview with Central Healthcare [28 November 2022).

15 We consider the functions of a private hospital fall within both of these markets.

Healthcare considers the Proposed Acquisition is unlikely to raise any competition concerns in any relevant market.[16]

25. As there can be multiple scenarios that are likely without a merger, we assessed whether there would be any likely scenarios where there would be a material difference in the level of competition with and without the Proposed Acquisition. We consider there are no such scenarios and we set out our reasoning for this assessment below.

Assessing the likely counterfactual scenario(s)

26. In assessing the likely counterfactual scenarios, we considered whether any entity, but particularly Central Healthcare,[17] would likely build a private hospital in competition with the Crest Hospital in the foreseeable future.

27. In particular, over an approximately 18-month period beginning in 2020, Central Healthcare took steps towards building a private hospital in the Manawatū region. These steps included preparing a business case, obtaining shareholder interest and purchasing suitable land on Milson Line in Palmerston North.

28. The first public announcement of these steps was on 28 January 2022 when Central Healthcare announced plans to build a new medical facility on Milson Line.[18] The first phase of this development would include radiology, consultation, cardiology and dentist facilities.[19] The announcement also mentioned a potential second phase of the development.

29. Details of any second phase were not announced but, if progressed, it is possible that Central Healthcare's Milson Line development may have included building a private hospital in competition with the Crest Hospital, which would be consistent with the rationale behind Central Healthcare's formation.

30. However, Central Healthcare's ability, incentives and intentions to build a private hospital changed over time after receiving additional information and assessing the business case further. Central Healthcare submitted that:[20]

---

16 The Application at [6.2] and [6.13].

17 We consider that, in the counterfactual, Central Healthcare would be the most likely of any entity (however unlikely) to build a private hospital in competition with Crest Hospital. This is because the majority of surgeons in the Manawatū region are shareholders in Central Healthcare and we are not aware of any other entity having signalled a viable intention to build a private hospital in the area. Hence, our analysis focuses on Central Healthcare.

18 Scoop*, New State Of The Art Healthcare Facility Announced For Manawatū,* 28 January 2022 (link available here).

19 We do not consider this first phase is likely to raise competition concerns as it is falls outside the markets applicable to the Proposed Acquisition; involving facilities that complement, rather than compete with, Crest Hospital.

20 Commerce Commission interview with Central Healthcare (28 November 2022). The decision to not build a private hospital [ ]

30.1 it made a decision not to build a private hospital that would have competed with Crest Hospital; and

30.2 it does not have the means, or the intention, to change this decision.

31. We investigated and evaluated Central Healthcare's position and, while it is possible that Central Healthcare might revisit its decision not to build a private hospital, we do not consider this to be likely. To this extent, we consider that in the counterfactual scenario, Central Healthcare is unlikely to build a new private hospital that would compete with the Crest Hospital. There are three main reasons for this assessment.

31.1 The costs involved in constructing a private hospital are high relative to likely returns and these costs have significantly increased since the formation of Central Healthcare. We consider it unlikely that such costs would decrease within the foreseeable future.

31.1.1 Central Healthcare's original business plan in 2020 estimated the initial build cost of a new hospital would be in the order of [ ] and, with the related facilities, the total project cost over time would be in the order of [ ].[21]

31.1.2 However, Central Healthcare obtained an estimate of [ ] from its designer in mid-2021 which indicated costs would be significantly higher than initially anticipated and outside its means. Central Healthcare then sought a scaled back design but the costs for this revised option remained out of reach.[22]

31.2 There is insufficient demand (contrary to Central Healthcare's initial estimates) in the Manawatū region to justify the building of a second private hospital. This demand is not expected to significantly increase within the foreseeable future.[23] For example:

31.2.1 we received feedback that the number of patients requiring surgery in a private hospital is expected to remain relatively constant for the foreseeable future;[24]

---

21 [ ]

22 [ ]

23 [ ]

24 [ ]

31.2.2 existing private hospital operating theatre capacity recently increased, with the Crest Hospital opening a fifth operating theatre; and

31.2.3 Crest Hospital obtained an outsourcing contract with the then MidCentral DHB,[25] which has significantly reduced Health NZ – MidCentral District as a potential source of revenue for any new private hospital.[26]

31.3 Central Healthcare lacks the ability to finance the building and operation of a new private hospital. This ability is not expected to change in the foreseeable future. For example:

31.3.1 Central Healthcare's revenue and profitability forecasts appear unfavourable due to the estimated construction costs and insufficient demand outlined above;[27]

31.3.2 in order to cover construction costs, Central Healthcare would need to obtain significant funds from investors and from its bank and it appears unlikely Central Healthcare could obtain sufficient funds to finance a private hospital build;[28] and

31.3.3 the associated costs in financing a private hospital build would likely be disproportionate to any potential investment return.[29]

Conclusion on the likely counterfactual scenarios

32. For the reasons set out above, we consider that, absent the Proposed Acquisition, it is unlikely that Central Healthcare, or another entity, would build a private hospital within the foreseeable future that would compete with Crest Hospital.

33. Rather, the likely counterfactual scenarios would see Central Healthcare either:

33.1 develop its Milson Line property into a medical facility that complements the current services provided at the Crest Hospital (so the facility would not be a private hospital competing with the Crest Hospital); or

---

25 The contract is now with Health NZ.

26 [ ]

27 [ ]

28 [ ]

29 [ ]

33.2 sell the Milson Line site it previously purchased.

34. In both these scenarios, Central Healthcare would not be in competition with the Crest Hospital in any potentially relevant market and so there would be no material difference between the factual scenario and a likely counterfactual scenario.

Overall conclusion

35. When Central Healthcare was formed, circumstances appeared favourable to it building a new private hospital in Palmerston North. However, the evidence before us indicates that circumstances subsequently changed such that we do not consider there is a likely scenario where Central Healthcare would compete with Crest Hospital in the counterfactual. As such, the Proposed Acquisition is unlikely to remove any existing or potential competition between the merging parties.

36. Accordingly, we are satisfied that the Proposed Acquisition will not have, or would not be likely to have, the effect of substantially lessening competition in any relevant market.

Determination on notice of clearance

37. Under section 66(3)(a) of the Commerce Act 1986, the Commerce Commission determines to give clearance to Central Healthcare Operations Limited to acquire 100% of the shares in Aorangi Hospital Limited from Southern Cross Healthcare Limited.

Dated this 12th day of December 2022

____

Sue Begg
Deputy Chair