



Public Competition Assessment

28 August 2013

Sonic Healthcare Limited - proposed acquisition of pathology businesses of Healthscope Limited in Queensland, Western Australia and the Australian Capital Territory (including the Southern Tablelands region of New South Wales)

Introduction

1. On 11 October 2012, the Australian Competition and Consumer Commission (**ACCC**) announced its decision:
 - to oppose the proposed acquisition by Sonic Healthcare Limited (**Sonic**) of the pathology business of Healthscope Limited (**Healthscope**) in Queensland (the **Queensland proposed acquisition**), since it would be likely to have the effect of substantially lessening competition in the market for the supply of community pathology services in Queensland, in contravention of section 50 of the *Competition and Consumer Act 2010* (**the Act**); and
 - to not oppose Sonic's proposed acquisition of the pathology business of Healthscope in Western Australia (the **WA proposed acquisition**), since it would not be likely to have the effect of substantially lessening competition in any relevant market.
2. Subsequent to its decision regarding the Queensland and WA proposed acquisitions, Sonic provided a submission seeking informal clearance of its proposal to acquire the pathology business of Healthscope in the Australian Capital Territory (the **ACT**) and the Southern Tablelands region of New South Wales (the **ACT proposed acquisition**). On 31 January 2013, the ACCC announced its decision to not oppose the ACT proposed acquisition, since it would not be likely to have the effect of substantially lessening competition in any relevant market.
3. The ACCC made its decision on the basis of the information provided by the merger parties and information arising from its market inquiries. This Public Competition Assessment outlines the basis on which the ACCC reached its

decisions in relation to the proposed acquisitions, subject to confidentiality considerations.

Public Competition Assessment

4. To provide an enhanced level of transparency in its decision making process, the ACCC issues a Public Competition Assessment for all proposals where:
 - an acquisition is opposed;
 - an acquisition is subject to enforceable undertakings;
 - the parties to the acquisition seek such disclosure; or
 - an acquisition is not opposed but raises important issues that the ACCC considers should be made public.
5. This Public Competition Assessment has been issued because the Queensland proposed acquisition was opposed by the ACCC.
6. By issuing Public Competition Assessments, the ACCC aims to provide the public with a better understanding of the ACCC's analysis of various markets and the associated merger and competition issues. It also alerts the public to circumstances where the ACCC's assessment of the competition conditions in particular markets is changing, or likely to change.
7. Each Public Competition Assessment is specific to the particular transaction under review by the ACCC. While some transaction proposals may involve the same or related markets, it should not be assumed that the analysis and decision outlined in one Public Competition Assessment will be conclusive of the ACCC's view in respect of other transaction proposals, as each matter will be considered on a case-by-case basis.
8. Public Competition Assessments outline the ACCC's principal reasons for forming views on a proposed acquisition at the time the decision was made. As such, Public Competition Assessments may not definitively identify and explain all issues that the ACCC considers arise from a proposed acquisition. Further, the ACCC's decisions generally involve consideration of both non-confidential and confidential information provided by the parties and market participants. In order to maintain the confidentiality of particular information, Public Competition Assessments do not contain any confidential information or its sources.

The parties

The acquirer: Sonic Healthcare Limited

9. Sonic provides pathology and radiology services in Australia and overseas. It also offers medical centre management services in Australia through its subsidiary company Independent Practitioners Network. In the 2012 financial year, Sonic had revenue of \$3.4 billion from its worldwide business, \$1 billion (or 30%) of this was contributed by its Australian pathology business. Sonic is listed on the Australian Securities Exchange.

10. Sonic operates the following pathology businesses in Australia:

- Queensland: Sullivan Nicolaides Pathology.
- Western Australia: Clinipath/Bunbury Pathology.
- Australian Capital Territory: Capital Pathology.
- Victoria: Melbourne Pathology.
- New South Wales: Douglass Hanly Moir Pathology (including Barratt & Smith Pathology), Southern Pathology and Sullivan Nicolaides Pathology.
- South Australia: Clinpath Laboratories.
- Tasmania: Launceston Pathology, Hobart Pathology and North West Pathology.

The target: Healthscope Limited

11. Healthscope operates private hospitals, medical centres and pathology businesses in most states of Australia as well as pathology businesses in New Zealand, Singapore, Malaysia and Vietnam.

12. Healthscope was previously a public company listed on the Australian Securities Exchange. In October 2010, Healthscope was acquired by Asia Pacific Healthcare Group Pty Ltd, a company owned by funds advised and managed by The Carlyle Group and TPG Capital.

13. Healthscope's pathology operations generally use the brand name 'Healthscope Pathology', but are still known amongst some industry participants as 'Gribbles', which was Healthscope's former brand name in some states.

Industry background

Pathology testing

14. Pathology is the branch of clinical medicine concerned with studying the nature, diagnosis and causes of diseases. Pathology testing involves the analysis of medical samples, for example blood cell counts, which are collected from patients.

15. Pathology testing can be divided into the following four broad categories and relevant sub-specialties:

- biochemistry (chemical pathology, immunology and infertility and pregnancy tests);
- haematology;
- microbiology; and
- histopathology and cytopathology (sometimes referred to as histology and cytology).

16. Some pathology providers also perform genetic testing.
17. The testing for different sub-specialties is automated to varying degrees. Microbiology, biochemistry and haematology (sometimes collectively described as 'clinical pathology') tend to be more highly automated and generate the highest pathology test volumes. Consequently, there are significant economies of scale associated with performing these tests. Histology and cytology tend to require greater manual preparation of samples, analysis and interpretation of test results.

Pathology collection

18. Pathology samples are collected from patients via various channels, including at Approved Collection Centres (**ACCs**), by doctors (including specialists) at medical practices (**'doctor collects'**), at hospitals and at patients' homes.
19. Although obtaining pathology samples solely from doctor collects may be a viable option for a niche pathology provider focussing on fields such as histology and cytology, having ACCs is a critical part of any full service pathology provider's business. This is because a significant proportion of pathology test volumes are generated at ACCs. ACCs can be 'co-located' at medical practices (by sub-leasing part of a medical practice) or 'standalone' at an independent site.

Pathology funding

20. Most pathology testing is funded in one or more of the following ways:
 - **Commonwealth government** – the Commonwealth Government (**Government**) funds the majority of pathology tests through Medicare rebates on a fee-for-service basis, in some cases supplemented by out-of-pocket expenses paid by patients (see further below).
 - **Health funds** – for private in-patients with private health insurance, a private health fund will cover the gap (see further below) for privately billed patients. For this purpose, private health funds seek to enter into Medical Provider Purchase Agreements (**MPPAs**) with pathology providers.
 - **State governments** – the pathology expenses of public in-patients at public hospitals are generally covered by a State-based funding system covering all services provided during a hospital stay.
21. The mechanism for billing pathology tests, except for public in-patients covered by a State-based funding system, is described below.
22. A pathology provider can choose whether to receive only the applicable Medicare rebates for services it provides (**'bulk bill'**) or to impose an additional charge to patients, known as an 'out of pocket' expense or 'gap' (**'privately bill'**). This decision is influenced by a range of factors, including whether the patient is a concession card holder, the preference of the doctor as expressed on the referral form, the billing policy of competing pathology providers and the complexity of the test. The pathology pricing is implemented through the billing policy of each pathology provider.
23. When a pathology provider chooses to bulk bill its patients, the pathology provider obtains payment directly from the Government. The result is that the services are

effectively free to the patient and the pathology provider is exposed to minimal credit risk.

24. When a pathology provider chooses to privately bill, the patient may pay the whole amount charged by the pathology provider and obtain reimbursement of the applicable Medicare rebate from the Government. Alternatively, the patient may pay only the 'gap' to the pathology provider, in which case the patient must obtain a cheque from the Government for the applicable Medicare rebate and forward it to the pathology provider. In effect, when a pathology provider chooses to privately bill, the Government and the patient share the cost of the patient's pathology tests.
25. A pathology provider may be able to obtain substantially greater revenue if it privately bills patients, who must then pay out of pocket expenses. However there is a materially greater credit risk associated with invoicing and seeking payment from out-patients relative to seeking payment directly from Medicare, as it relies on the patient paying the out-of-pocket expense and may also require the patient to pass on the applicable Medicare rebate to the pathology provider.¹ The size of the out-of-pocket expense is generally set at a level that is sufficient to mitigate this risk.
26. In this Public Competition Assessment, references to 'price increases' should be read as including both or either of:
 - a decision to privately bill for the supply of pathology services that would previously have been bulk billed; and/or
 - an increase in the gap for privately billed pathology services.
27. A patient must obtain a referral from a medical practitioner for a pathology test. Pathology providers provide branded referral forms to medical practitioners, which patients then take with them to an ACC. Since 11 December 2010, patients have been free to take these forms to any pathology provider, regardless of the branding on the form, unless a particular provider is specified by the referring medical practitioner on clinical grounds. The medical practitioner may express a preference on the referral form for the patient either to be bulk billed or privately billed; however, a pathology provider can choose to disregard such a request.

Industry participants

28. Sonic, Primary Healthcare Limited (**Primary**) and Healthscope together process the vast majority of the pathology specimens in Australia, and are sometimes referred to as the 'corporate' pathology providers. Each of these pathology providers operates in all mainland states and territories of Australia. The corporate pathology providers operate 'hub and spoke' business models. This consists of at least one large 'central' laboratory and a network of regionally located laboratories.
29. Primary trades as Laverty Pathology in NSW and the ACT, QML Pathology in Queensland and Western Diagnostic Pathology in WA.

¹ There is relatively little credit risk involved with privately billing insured in-patients who are covered by health insurance.

30. St John of God Pathology (**SJOG**) is a significant pathology provider with multiple laboratories and ACCs in Western Australia and Victoria. It is a not-for-profit company.
31. There are a number of smaller, full service pathology providers who operate in just one state in Australia, typically with one laboratory. Their ACCs tend to be concentrated in metropolitan areas. There are also several very small pathology providers who either have limited ACC networks and/or operate laboratories which focus on providing pathology services in specific categories (**'niche' providers**).
32. Public pathology providers have laboratories based in public hospitals which are their primary source of demand. These providers are required to provide the full range of pathology services on a 24 hours, 7 days a week basis, including complex tests. Public pathology providers generally also provide pathology services to patients referred by GPs and specialists, with some having ACCs in the general community, usually in the area surrounding the public hospital.

Competition in the supply of pathology services

33. The ACCC found that competition between pathology providers may be manifested in one or more of the following ways:
 - **Bulk billing levels:** The proportion of patients being bulk billed, which depends on a pathology provider's billing policy.
 - **Prices to privately billed patients:** The amount of the gap set by pathology providers for privately billed patients.
 - **Health funds:** The rates negotiated under MPPAs between pathology providers and private health funds. These rates are reflected in insurance premiums.
 - **Service levels:** Non-price aspects of pathology services. The ACCC considered that while pathology providers must comply with minimum standards imposed by the National Association of Testing Authorities (**NATA**), the authority for accrediting laboratories in Australia, pathology providers compete on a number of other service-related aspects, such as the number and convenience of ACC locations, opening hours of ACCs, range of tests and customer service.

The proposed transaction

34. Sonic initially proposed in May 2012 to acquire the pathology businesses of Healthscope in New South Wales (including the ACT), Western Australia and Queensland. The ACCC commenced a public review of these three proposed acquisitions. However on 17 September 2012, Sonic announced that it no longer intended to acquire Healthscope's pathology businesses in New South Wales, so the ACCC did not proceed to a decision regarding the NSW proposed acquisition.
35. Sonic subsequently advised the ACCC that it proposed to acquire the pathology business of Healthscope in the ACT and the Southern Tablelands region of New South Wales. The ACCC commenced a public review of that proposed acquisition on 2 January 2013, drawing on information and documents gathered during the earlier review.

Review timeline

36. The following table outlines the timeline of key events in this matter.

Date	Event
Queensland, WA and NSW proposed acquisitions	
16 May 2012	ACCC commenced review under the Merger Review Process Guidelines.
6 June 2012	Closing date for submissions from interested parties.
3 July 2012	ACCC requested further information from the merger parties. ACCC timeline suspended.
27 July 2012	ACCC received submissions from the merger parties. ACCC timeline recommenced.
2 August 2012	ACCC published a Statement of Issues outlining preliminary competition concerns.
16 August 2012	Closing date for submissions relating to Statement of Issues.
27 August 2012	ACCC requested further information from the merger parties. ACCC timeline suspended.
14 September 2012	ACCC received further information from the merger parties. ACCC timeline recommenced.
17 September 2012	Sonic announced that it no longer proposed to acquire Healthscope's pathology businesses in New South Wales.
11 October 2012	ACCC announced it would oppose the Queensland proposed acquisition and would not oppose the WA proposed acquisition.
ACT and Southern Tablelands region of NSW proposed acquisition	
2 January 2013	ACCC commenced review under the Merger Process Guidelines.
31 January 2013	ACCC announced it would not oppose the ACT proposed acquisition.

Market inquiries

37. The ACCC conducted market inquiries with a range of interested parties, including other pathology providers, referring practitioners, private health funds and industry associations.

With/without test

38. Section 50 of the Act prohibits mergers or acquisitions that would have the effect or be likely to have the effect of substantially lessening competition in any market. In assessing a proposed acquisition pursuant to section 50 of the Act, the ACCC considers the effects of the acquisition by comparing the likely future competitive environment post-acquisition if the acquisition proceeds (the "with" position) to the likely future competitive environment if the acquisition does not proceed (the "without" position) to determine whether the proposed acquisition is likely to substantially lessen competition in any relevant market.

39. As regards the Queensland and WA proposed acquisitions, the ACCC considered that the likely future competitive environment absent the proposed acquisition would be the status quo, that is, Healthscope would continue to operate as an independent, viable and effective competitor. As regards the proposed acquisition in the ACT and Southern Tablelands region of NSW, the ACCC considered that Healthscope was likely to provide a weaker competitive constraint in the future absent the proposed acquisition.

Market definition

40. The relevant markets were considered to be:

- the market for the supply of community pathology services in Western Australia;
- the market for the supply of community pathology services in Queensland; and
- the market for the supply of community pathology services in New South Wales / ACT.

Product dimension

41. Pathology services consist of a number of integrated services, including collecting pathology samples, transporting them to an Accredited Pathology Laboratory (APL), processing (testing) the samples, generating and delivering reports and discussing with the referring medical practitioner, where necessary.

42. Since these activities are integrated, and the ACCC is not aware of companies active in only one component,² the ACCC considers it appropriate to regard them as forming part of an overall product of providing pathology services.

43. There are three key sources of demand for pathology services:

- out-patients referred by general practitioners and specialists;
- private in-patients at public and private hospitals; and
- public in-patients at public hospitals.

44. Pathology services provided to the first two sources of demand attract a Medicare rebate and are described as 'community pathology'.

45. Pathology services provided to public in-patients are covered by a State-based funding system and are described as 'public hospital pathology'. Public hospital pathology services are generally carried out either in-house or by private sector pathology providers who have been appointed on a long term contract. Public in-patients are not contestable to pathology providers operating outside of these arrangements.

² The ACCC recognises that there is some scope for third parties such as courier companies to be engaged to provide transportation. However this does not appear to occur on any material scale.

46. Private and public pathology providers do compete in relation to the supply of community pathology services.³ Some pathology laboratories of public hospitals are used to provide community pathology testing services and several of these have established ACCs in the community.
47. The ACCC's view, therefore, is that the supply of pathology services to public in-patients does not fall within the supply of community pathology services. However, public pathology providers should be included as actual or potential competitors in relation to the supply of community pathology services to out-patients.
48. Pathology providers also compete to provide pathology services to corporate and government customers (**corporate and government pathology services**), typically to perform tests on current and potential employees. Whilst some corporate customers might require or prefer to engage a pathology provider with a national presence, market inquiries have indicated that a national presence is not required in most cases. In addition, in some specialised areas of testing, pathology providers may compete with a range of potential suppliers that are not active in the wider community pathology markets. Nonetheless, corporate and government pathology services may be regarded as forming part of the same market as community pathology services.
49. In light of the above, the ACCC's view is that the product dimension of the relevant markets is the supply of community pathology services.

Geographic dimension

50. Market inquiries indicated that it is often necessary for a pathology specimen to be tested within approximately four hours of being collected from a patient. This time constraint means that APLs are typically located close to population centres and specimens are generally tested in the same state or territory in which they are collected. The ACCC is aware of exceptions to this, for example specimens collected on the north coast of New South Wales may be tested in Brisbane.
51. For the purposes of its review of the proposed acquisitions, the ACCC treated each of Western Australia, New South Wales (including the ACT) and Queensland as separate markets. However, the ACCC noted that the geographic dimension of these markets may not exactly mirror state boundaries, reflecting efficiencies in collection coverage and testing locations, and that there is the potential for more localised effects.

Statement of Issues

52. The ACCC published a Statement of Issues on 2 August 2012 identifying a number of competition issues relating to the WA proposed acquisition and the Queensland proposed acquisition. The ACCC stated its preliminary view that these proposed acquisitions may raise competition concerns in the relevant community pathology services markets.

³ Public pathology providers may provide pathology services to private in-patients in public hospitals on a non-contestable basis under authorised or notified exclusive dealing arrangements. For instance, pathology services for private in-patients in NSW public hospitals must be provided by pathology providers appointed by NSW public health organisations, unless it is not in the patient's best interest. This arrangement is subject to exclusive dealing notifications lodged with the ACCC in 2009.

53. The ACCC identified the following key issues of concern:

- Whilst Sonic's closest competitor appears to be Primary, Healthscope is the next largest pathology provider in Queensland, and is the fourth largest behind SJOG in Western Australia. Other pathology providers did not appear to be as close competitors as Sonic, Primary, Healthscope and SJOG (the latter in Western Australia only).
- Healthscope's ownership of hospitals and medical centres in Western Australia and Queensland and its strong position in other pathology markets including in Victoria, South Australia and New South Wales are likely to make it a particularly vigorous and effective competitor in the relevant markets.

54. The ACCC stated that competition concerns were unlikely to arise in relation to the supply of pathology services to corporate and government customers.

Competition analysis

55. The ACCC found that the competition analysis applying to each of the proposed acquisitions shared a number of common features relating to the closeness of competition between the corporate pathology providers (i.e. Sonic, Primary and Healthscope), the significance of barriers to entry and expansion and the potential for localised competition effects. Those common features are therefore discussed first, followed by competition analysis relating to each of the proposed acquisitions.

56. The ACCC obtained a range of data relating to pathology providers' testing activities to assess their respective positions in the relevant markets. This data cannot be disclosed since it is confidential. However, Medicare publishes statistics relating to the number of ACCs owned by each pathology provider. These are used in the discussion below, to provide an approximation of their market shares. The number of ACCs reflects a pathology provider's collection capacity relating to out-patients – i.e. not including doctor collects and not accounting for the actual volume of specimens collected.

Closeness of competition between corporate pathology providers

57. The ACCC found that the corporate pathology providers generally constitute each other's closest competitive constraint in most states and territories of Australia. This is because they have established:

- wide coverage of their ACCs;
- wide coverage of their courier networks;
- a full range of pathology testing capability;
- networks of laboratories, including in regional centres; and
- widespread recognition of their brands.

Barriers to entry and expansion

58. The ACCC considered whether, following the proposed acquisitions, another pathology provider might be capable of entering and expanding its presence to replicate the competitive constraint currently imposed by Healthscope. The ACCC considered whether such entry or expansion would be likely, timely and sufficient to deter any potential price or non-price effects that might otherwise result from the proposed acquisitions.
59. The ACCC found that there are material sunk costs associated with establishing and expanding a referral base and testing capacity and that there are economies of scale, both in collecting and processing specimens. This deters small scale entry, except on a 'niche' basis, as described at paragraph 31. In addition, the ACCC found that pathology providers face substantial impediments to timely expansion of their referral base, which is necessary for any investment in pathology collecting and testing capacity to be viable.
60. The ACCC identified four main categories of obstacles relating to pathology providers expanding their referral base:
- **Misalignment of incentives** – the person receiving the pathology services, the person selecting the pathology provider and the person paying for the pathology services are often not the same. This means that there may be some misalignment of incentives between them, resulting in dampened sensitivity to changes in price and/or service levels.
 - **Switching costs** – although medical practitioners (and therefore patients) do not make any formal commitment to a pathology provider that they will use their services, there were costs associated with switching between pathology providers, including uncertainty in the quality of service provided by an alternative pathology provider and dependence on, or familiarity with, a pathology provider's software, IT systems or reporting format.
 - **Establishing reputation and relationships** – significant time and effort needs to be expended over a substantial period of time to establish a reputation and personal relationships with referring medical practitioners, which assist with retaining and broadening a referral base. Therefore incumbent pathology providers may hold an advantage over new entrants seeking referrals or pathology providers seeking to expand their referral base, who must contest strong, established relationships between existing pathology providers and medical practitioners. As a result, expansion of a referral base tends to be gradual and incremental.
 - **Collection centres** – pathology providers that do not rely on doctor collects need to establish ACCs in locations that are convenient for patients and likely to deliver sufficient referral volumes, taking into account rental levels. Following the removal of regulations limiting the number of ACCs that could be operated by a given pathology provider on 1 July 2010, there was a rapid increase in the number of ACCs. The ACCC found that most of the new ACCs that were established at that time were 'defensive' – i.e. established to support an existing referral base rather than to capture additional volume. The ACCC therefore considered that the rapid expansion of ACCs that occurred immediately following deregulation was

not likely to be repeated and that the viability of establishing new ACCs in future was likely to be far more marginal.

61. The gradual and incremental nature of the expansion of pathology providers' referral base has an impact on their geographic coverage. Pathology providers other than the corporate pathology providers cover only certain regions within the relevant state or territory. As they expand, they tend to do so by incrementally expanding around their existing geographic coverage. In other words, a pathology provider would be far more likely to start servicing an area that is adjacent to the areas that it already services than an area hundreds of kilometres away. This means that some pathology providers that are active in a certain market (i.e. a certain state) do not pose an immediate competitive constraint in some regions of that market and may not be sufficiently likely to expand into those regions in a sufficiently timely manner to be relevant to the competitive process there.
62. The ACCC found that a new entrant or existing pathology provider seeking to expand may be able to gain referrals relatively rapidly as a result of a change of billing policy by a rival pathology provider or by offering bulk billing to patients that are currently privately billed. However, in these circumstances a smaller pathology provider may be deterred from incurring the costs associated with establishing or expanding its collection and testing capacity due to the prospect of rapidly losing any additional referral base that it gains through these means. This is because an incumbent could utilise its established collection and testing capacity, reputation and professional relationships to regain its lost customer base rapidly, and at little cost, by reversing such a change in policy or by responding on a targeted basis, for example by altering its billing policy at relevant ACCs. Such a change of billing policy, including a subsequent reversal, occurred in Queensland in 2009. This event is described in the competition analysis section for Queensland below.

Localised competition effects

63. The ACCC considered that competition effects may arise on a localised basis within a given market (i.e. within a given state). This is because patients are willing to travel only a limited distance to visit an ACC. Notwithstanding the presence of multiple pathology providers in a given state, there are areas covered only by a subset of those pathology providers (i.e. areas where only some pathology providers have ACCs and/or provide doctor collects). This may facilitate localised competition effects arising from an acquisition.
64. The ACCC identified several geographic areas where Sonic and Healthscope were the only pathology providers with an ACC. In those areas, the number of corporate pathology providers with ACCs would decrease from two to one following the proposed acquisitions. However, the ACCC considered that Primary would be likely to establish a local ACC relatively quickly if Sonic were to increase prices or decrease service levels in those areas, given Primary's presence across the relevant states and established reputation in the relevant markets.
65. The ACCC therefore primarily considered whether the aggregation of two of the three corporate pathology providers in each of the relevant markets would result in a substantial lessening of competition, taking into account:
 - the level and significance of the competition provided by Healthscope in the relevant markets for community pathology that would be lost post-acquisition; and

- whether the competition provided by Healthscope in each market could be replaced by another existing or potential pathology provider post-acquisition in a timely way.

66. In particular, given the on-going competitive constraint provided by Primary in the relevant markets, the ACCC considered whether any coordinated effects were likely to arise from the proposed acquisitions.

Competition analysis – Queensland

67. The Medicare figures relating to the number of ACCs held by each pathology provider in Queensland were as follows:

Pathology provider	Share of ACCs (21 May 2012)
Primary (QML Pathology)	~50%
Sonic (Sullivan Nicolaides Pathology)	~35%
Healthscope	~10%
Mater Pathology	~4%
Coastal Pathology	~1%
Pathology Queensland	~1%
Other	~1%

Competitive constraint imposed by Healthscope

68. Information and documents obtained by the ACCC following publication of its Statement of Issues indicated that, although Sonic and Primary are likely to be the closest competitors of each other in Queensland, there was evidence of a substantial degree of rivalry between Sonic, Primary and Healthscope.

69. Despite Healthscope's relatively small market share, the ACCC reached the view that it provides an appreciably stronger level of competition relative to other pathology providers in the Queensland market other than Sonic and Primary. In particular:

- Healthscope's ACCs are located across multiple regions within Queensland and it has more than double the number of ACCs in Queensland compared to the next largest competitor, Mater Pathology. Healthscope's ACCs are located across Queensland rather than being concentrated in a particular region;
- Healthscope runs a hub and spoke laboratory network in Queensland, which allows it to maximise the efficiency of its pathology testing, unlike the smaller pathology providers;
- Healthscope has been steadily growing its pathology referral volumes; and

- while Healthscope must compete to obtain referrals by tendering or leasing sites for ACCs within medical centres owned by third parties, its ownership of several medical centres and private hospitals in Queensland provides it with access to convenient locations from which to compete for referrals without having to incur the high costs of renting space for ACCs.

The 2009 Queensland event

70. The ACCC considered an event in 2009 relating to Sonic's billing policy in Queensland to be particularly relevant to its assessment of the likely effect of the Queensland proposed acquisition.
71. In 2009, each of the corporate pathology providers sent a series of letters to medical practitioners informing them that it was not sustainable for pathology services to continue to be bulk billed and encouraging them only to request bulk billing for financially disadvantaged patients. In July 2009, Sonic changed its billing policy in Queensland so that it would privately bill a much greater proportion of patients. As a consequence, Sonic rapidly lost referrals until it reversed this change of billing policy in early 2010. Sonic then rapidly regained much of its lost referral volumes. This appeared to be due to its established relationships and reputations, and the short period in which the policy change was in place.
72. The ACCC obtained documents and information from the merger parties and third parties relating to the 2009 Queensland event. Due to confidentiality restrictions, the ACCC cannot provide any detail regarding those documents and information. However, based on these, the ACCC concluded that Healthscope had played a significant role in disrupting a potentially broader move by Sonic and Primary to privately bill a larger proportion of patients in Queensland.

Significance of other pathology providers

73. As outlined above, the ACCC considered that smaller pathology providers face significant hurdles to expanding their presence. The ACCC concluded that none of the remaining pathology providers in Queensland were likely – in a timely manner – to replicate the competitive constraint currently provided by Healthscope. In particular, the ACCC noted:
- Mater Pathology is a not-for-profit pathology provider affiliated with the Mater Hospitals in Brisbane. It does not have the same commercial drivers as a private pathology provider. It has less than half the market share of Healthscope and does not appear likely to expand its presence very substantially in the short to medium-term.
 - Coastal Pathology has a very small market share and is focussed on providing a local service on the Sunshine Coast.
 - Pathology Queensland is a public pathology provider, currently experiencing cuts to its budget. It is focussed on providing pathology services to in-patients and has only two ACCs in the community.
74. The ACCC therefore concluded that the remaining pathology providers in Queensland (or potential new entrants) were not likely to provide a comparable level of competitive constraint to Healthscope in a timely manner, post-acquisition.

Conclusion

75. The ACCC concluded that the Queensland proposed acquisition would result in the removal of a significant competitive constraint in the Queensland market that was not likely to be replicated by any existing or new pathology providers post-acquisition, and therefore would be likely to result in a substantial lessening of competition.
76. The ACCC considered that the events surrounding Sonic's change of billing policy in Queensland in 2009 were a strong indication of the level of inter-dependence of the billing policies of the corporate pathology providers in Queensland. The ACCC therefore considered that the Queensland proposed acquisition was likely to increase the prospect that a change of billing policy by either Sonic or Primary would be accommodated by the other and not disrupted by any existing or new pathology provider, resulting in more patients being privately billed.
77. The ACCC further considered that a substantial lessening of competition in the Queensland market may also be manifested in aspects of pathology providers' price and service offering other than their bulk billing policies.

Competition analysis – Western Australia

78. The Medicare figures relating to the number of ACCs held by each pathology provider in WA were as follows:

Pathology provider	Share of ACCs (21 May 2012)
Primary (Western Diagnostic Pathology)	~28%
Sonic (Clinipath/Bunbury Pathology)	~25%
SJOG	~15%
Healthscope	~13%
Perth Pathology	~10%
PathWest	~7%
Other	~1%

Competitive constraint imposed by Healthscope

79. The ACCC considered that Healthscope's presence in the WA market imposed a material competitive constraint on the other pathology providers in terms of price and service offerings for community pathology. In this regard, the ACCC noted:
- Healthscope had considerably expanded its ACC network and had the testing and collection capacity to take significant volumes of referrals from its rivals.
 - Market inquiries indicated that Healthscope was aggressively competing for co-located ACCs at medical centres by paying high levels of rent.

- Healthscope’s ownership of medical centres and the Mount Hospital provided a strong pathology referral stream.

Significance of other pathology providers

80. The ACCC considered whether the remaining pathology providers in WA would provide a level of competition post-acquisition that was comparable to Healthscope.
81. Market inquiries indicated that the market shares in WA are more evenly distributed among a larger number of full service pathology providers with significant geographic coverage of WA. In particular, PathWest and SJOG have a greater presence than Healthscope in WA. Market inquiries with medical practices indicated that there are a number of alternative pathology providers available if the merged firm were to privately bill or change its service offering.

Conclusion

82. The ACCC therefore considered that, although the WA proposed acquisition was likely to remove a significant player, it was not likely to substantially lessen competition in the WA market, given that:
- a number of pathology providers would remain in the WA market that would continue to provide a comparable level of competition; and
 - although Healthscope appeared to be a strong competitor winning market share from Sonic, Primary and others, the competitive constraint offered by Healthscope, and likely to be offered by Healthscope in the future without the proposed acquisition, did not appear to be significantly different or superior to that of other competitors in the WA market, such as SJOG and PathWest.

Competition analysis – ACT and Southern Tablelands

83. The ACCC considered the ACT proposed acquisition in the context of the market for the supply of community pathology services in New South Wales / ACT. The ACCC found that pathology providers not servicing the ACT or Southern Tablelands region provided very little competitive constraint in relation to the Healthscope pathology business that Sonic proposed to acquire. As such, and given that the Southern Tablelands region is immediately adjacent, the ACCC assessed the competitive effects of the proposed acquisition primarily in the ACT.
84. The Medicare figures relating to the number of ACCs held by each pathology provider in the ACT were as follows:

Pathology provider	Share of ACCs (21 May 2012)
Sonic (Capital Pathology)	~41%
Primary (Lavery Pathology)	~25%
Healthscope	~18%
ACT Pathology	~16%

Competitive constraint imposed by Healthscope

85. Market inquiries indicated that while Healthscope was competitive in the ACT, it did not appear to be a particularly significant competitor.
86. The ACCC also formed the view that Healthscope was likely to impose a weaker competitive constraint in the ACT in the event that the ACT proposed acquisition did not proceed.

Significance of other pathology providers

87. The ACCC found that two other full-service pathology providers would remain in the ACT market to constrain Sonic post-acquisition: Primary and ACT Pathology.
- ACT Pathology is a public pathology provider with a significant presence in the ACT and has a policy always to bulk bill. The ACCC considered ACT Pathology to be a viable alternative to Sonic but noted the limitations on ACT Pathology's ability to expand and take on substantial referral volumes.
 - Primary has a smaller presence in the ACT than in other states but market inquiries indicated that Primary is well-placed to expand its presence in the ACT to constrain Sonic, particularly if Sonic were to increase prices or decrease service levels post-acquisition.

Conclusion

88. The ACCC concluded that the ACT proposed acquisition was not likely to substantially lessen competition in the ACT, given that:
- Sonic would continue to be constrained by Primary and the public provider, ACT Pathology; and
 - Healthscope did not appear to be a particularly strong competitor and was likely to impose a weaker competitive constraint in the ACT in the event that the proposed acquisition did not proceed.

Conclusion

89. On the basis of the above, the ACCC formed the view that:
- the Queensland proposed acquisition would be likely to result in a substantial lessening of competition in the market for the supply of community pathology services in Queensland in contravention of section 50 of the Act;
 - the WA proposed acquisition would not be likely to result in a substantial lessening of competition in the market for the supply of community pathology services in WA; and
 - the ACT proposed acquisition would not be likely to result in a substantial lessening of competition in the market for the supply of community pathology services in New South Wales (including the ACT).