



Public Competition Assessment

14 March 2007

Mater Misericordiae Hospital - proposed acquisition of the Wesley Hospital, Townsville

Introduction

1. On 7 March 2007, the Australian Competition and Consumer Commission (ACCC) announced its decision not to oppose the proposed acquisition of The Wesley Hospital by the Mater Misericordiae Hospital (**proposed acquisition**). The ACCC was of the view that the proposed acquisition would be unlikely to have the effect of substantially lessening competition in the markets for the supply of private hospital services to health funds and the Repatriation Commission/Department of Veterans' Affairs (DVA) and to patients in the Townsville and surrounding region in contravention of section 50 of the Trade Practices Act 1974 (the **Act**).
2. The ACCC formed its view 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 has reached its decision on the proposed acquisition, subject to confidentiality considerations.

Public Competition Assessment

3. To provide an enhanced level of transparency and procedural fairness in its decision making process, the ACCC issues a Public Competition Assessment for all transaction proposals where:
 - a merger is rejected;
 - a merger is subject to enforceable undertakings;
 - the merger parties seek such disclosure; or
 - a merger is approved but raises important issues that the ACCC considers should be made public.
4. This Public Competition Assessment has been issued because the Mater Misericordiae Hospital's proposed acquisition of the Wesley Hospital is considered to raise issues of interest to the public.

5. By issuing Public Competition Assessments, the ACCC aims to provide the market with a better understanding of the ACCC's analysis of various markets and the associated merger and competition issues. It also alerts the market to the circumstances where the ACCC's assessment of the competition conditions in particular markets is changing, or likely to change, because of developments.
6. 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 its own merits.
7. Many of the ACCC's decisions will involve consideration of both non-confidential and confidential information provided by the merger 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. While the ACCC aims to provide an appropriately detailed explanation of the basis for the ACCC decision, where this is not possible, maintaining confidentiality will be the ACCC's paramount concern, and accordingly a Public Competition Assessment may not definitively explain all issues and the ACCC's analysis of such issues.

The parties

The acquirer: Mater Misericordiae Hospital (Mater)

8. The Mater is a 165 bed, acute care facility, owned and operated by the Townsville Congregation of the Sisters of Mercy. The Mater is a major referral hospital offering a range of medical and surgical services including oncology, urology, gastroenterology, gynaecology and obstetrics, orthopaedic and ophthalmology among others. The Mater also offers acute care services such as intensive care, coronary care and cardiac surgical services.

The target: The Wesley Hospital (Wesley)

9. The Wesley is an 80 bed acute medical surgical hospital owned by Uniting Church in Australia Property Trust (Qld) (Uniting Church), a group of six not-for-profit hospitals formed in 2001. The Wesley offers a range of services including:
 - a 34 bed medical /surgical unit catering for orthopaedics, plastics, general surgery and urology;
 - a women's unit offering IVF services, gynaecology, and obstetrics for antenatal classes, birth and postnatal care (5 level 2 nursing cots); and
 - a 14 bed day surgery unit and endoscopy suite.

Market background

10. The ACCC understands that the population of Townsville is approximately 160 000 and it is currently growing at an annual rate of around 2.5%.
11. There are currently only two private hospitals in Townsville; the Mater and the Wesley. There is also the public Townsville Hospital operated by Queensland Health, and two day surgeries located in metropolitan Townsville – Townsville Day Surgery and North Queensland Day Surgical Unit.
12. Post-acquisition, there will be two overnight hospitals in the city of Townsville – the public Townsville Hospital and the merged hospital (which will operate across two campuses).

The proposed transaction

13. On 9 January 2007, the Mater announced its proposal to acquire the Wesley and sought informal clearance from the ACCC. The proposed acquisition has not yet been completed and is subject to ACCC approval.
14. The sale agreement provides that the Mater will acquire the Wesley as a going concern.

Areas of overlap

15. The Mater and the Wesley each offer a range of different hospital services, with a number of these services provided by both private hospitals. The main specialties where there is some overlap between the hospitals include:
 - Obstetrics and Gynaecology;
 - Orthopaedics;
 - General surgery;
 - Oncology;
 - Urology; and
 - Paediatrics.

Timing

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

Date	Event
09-Jan-2007	ACCC commenced review under the Merger Review Process Guidelines. Market inquiries commenced
24-Jan-2007	Closing date for submissions from interested parties
07-Feb-2007	Timeline extended due to the need to conduct further market inquiries. Further market inquiries commenced
16-Feb-2007	Closing date for submissions from interested parties in response to further market inquiries
07-Mar-2007	ACCC announced its decision not to oppose the proposed acquisition

Initial market inquiries

17. Initial market inquiries commenced on 9 January 2007. The ACCC conducted an initial round of market inquiries with a range of industry participants, including health funds, public and private hospital operators, day surgeries, industry bodies, doctors (specialists) and other interested parties. Submissions were sought in relation to the substantive competition issues.

Further market inquiries

18. Further market inquiries commenced on 7 February 2007. The ACCC conducted further extensive market inquiries with a range of industry participants; in particular doctors (specialists), and other interested parties.

19. More specifically, submissions were sought in relation to:

- Extent of competition between the Mater and the Wesley in specialties where the hospitals overlap;
- Potential competition between the Mater and the Wesley in non-overlap specialties;
- Extent of competition between the Mater and the Wesley for doctors, which may lead to better outcomes for patients; and
- Impact of the proposed acquisition on prices to uninsured patients.

With/without test (Counterfactual)

20. In assessing a merger pursuant to section 50 of the Act, the ACCC must consider the effects of the transaction by comparing the likely competitive environment post-merger if the transaction proceeds (the “with” position) to the likely competitive environment post-merger if the transaction does not proceed (the “without” position or “counterfactual”).

21. Market inquiries revealed a widespread view in the market that the Wesley has been declining in terms of occupancy rates, standard of facilities, and financial viability for several years. Following discussions with market participants and examination of confidential documents provided by the merger parties, the

ACCC formed the view that in the absence of the merger, the Wesley is not likely to continue operating in its present form and will not be a vigorous and effective competitor to the Mater in future.

22. Market participants also noted the Mater's advanced plans for a redevelopment, which would add 60 beds to its existing capacity, if the proposed acquisition does not proceed, with most considering that this would exacerbate the Wesley's difficulties.

Market definition

23. The ACCC considers that the following broad markets are relevant to the assessment of this proposed acquisition:
 - (a) Market one – The Townsville and surrounding region market for the supply of private hospital services to health funds and the DVA; and
 - (b) Market two – The Townsville and surrounding region market for the supply of private hospital services to patients (with doctors acting as agents).
24. The ACCC notes that although some market participants indicated that for certain specialties, the geographic market may be broader than Townsville and the surrounding region, this appears to apply to only a small minority of specialties and patients, and the degree of substitutability does not appear to be sufficiently strong to justify a broader geographic market for private hospital services.

Market One - The Townsville and surrounding region market for the supply of private hospital services to health funds and the DVA

Competition analysis

25. Health funds negotiate Hospital Purchaser Provider Agreements (HPPAs) with hospitals to set the rates their members pay for services.¹ Effectively, members of individual health funds are collectively negotiating with hospitals, with the health fund acting as an agent. The DVA enters into arrangements similar to HPPAs with private hospitals for the provision of hospital care to veterans and entitled persons. Health funds also fully or partially pay the price they negotiate with hospitals and receive premiums from their members in return (in this way, the costs of treating illness and injury are spread across a health fund's membership). The DVA enters into arrangements similar to HPPAs with private hospitals for the provision of hospital care to veterans and entitled persons.
26. In making this assessment, the ACCC took into account the counterfactual referred to above (i.e. likely extent of future competition between the hospitals in the absence of the merger).

¹ The *Veterans' Entitlement Act 1986* (Cth) and the *Military Rehabilitation & Compensation Act 2004* (Cth) empower the Repatriation Commission of the Department of Veterans' Affairs to enter into arrangements similar to HPPAs with private hospitals for the provision of hospital care to veterans and entitled persons.

Countervailing power of health funds

27. The ACCC considered, among other things, whether any increased bargaining power would be held by the merged hospital post-acquisition relative to the countervailing power currently held by the health funds and the DVA in HPPA negotiations.
28. Some market participants expressed the view that the proposed acquisition may lead to a small increase in bargaining power of the merged hospital in its negotiations with some health funds, but generally considered that this would be due to the improved level and range of services available at the merged hospital rather than a lessening of competition in the relevant market. Further, some health funds did not appear to consider the Mater and the Wesley to be close competitors for the purpose of HPPA negotiations.

Portfolio effects as a result of the proposed acquisition

29. During its investigation, the ACCC examined whether there would be any portfolio effects as a result of the proposed acquisition; that is, any increased ability of a group of private hospitals to use their collective bargaining strength (where they have a number of private hospitals in their network) in their negotiations with health funds and the DVA to extract higher prices. Fundamental to the discussion of the portfolio effect is the level of bargaining power held by the relevant private hospital group when compared to that of the health funds and the DVA.
30. Market inquiries indicated that it is unlikely that there would be any significant portfolio effects as a result of the proposed acquisition of the Wesley by the Mater. Although the Mater is a member of the Catholic Negotiating Alliance (CNA), the ACCC understands that the hospital typically acts autonomously and negotiates prices independently of the CNA (and only some terms and conditions as a group). In any case, the Mater's portfolio post-acquisition will be small relative to other private hospital groups.

Ability to influence the range and service level at hospitals

31. Market inquiries confirmed health funds and the DVA have limited ability to influence the range and service level at the hospitals, beyond ensuring that at least a certain standard is met (the minimum threshold is determined by HPPA contracts and the relevant legislation). This appears unlikely to be affected by the proposed acquisition.

Market One - Conclusion

32. The ACCC concluded that the proposed acquisition was unlikely to result in a substantial lessening of competition in the Townsville and surrounding region market for the supply of private hospital services to health funds and the DVA, particularly given the counterfactual identified in paragraph 21.

Market Two – The Townsville and surrounding region market for the supply of private hospital services to patients (with doctors acting as agents)

Competition analysis

33. In conducting this assessment, the ACCC took into account the counterfactual (i.e. likely extent of future competition between the hospitals in the absence of the merger) discussed in paragraph 21.

Extent of competition between the Mater and the Wesley in specialties where the hospitals overlap

34. With some exceptions, the Mater and the Wesley do not currently compete vigorously in most specialties.
35. In those specialties where the merger parties do overlap, market inquiries indicated that the main area of competitive concern was in obstetrics and gynaecology. Market participants considered that the Mater and the Wesley both currently provide these services to a high standard, and in comparable numbers. Similar concerns were also raised in respect to the provision of neo-natal paediatric services.
36. The concerns expressed by some market participants in relation to obstetrics and gynaecology included:
- (a) the loss of choice of hospital for patients (including delivery methods);
 - (b) the likelihood that the bargaining power of doctors would be lessened post-acquisition;
 - (c) the view that the quality of care may be at risk for some specialties post-acquisition (including the lack of immediate access to Intensive Care (ICU) facilities for those specialties relocated to the Wesley, since the ICU will remain at the Mater campus); and
 - (d) transitional issues, such as the current lack of capacity at the Wesley to accommodate a merged obstetrics/gynaecology workload as planned (including the timing of the construction of new consulting suites adjacent to the Wesley).
37. However, the majority of market participants expect that a better standard and quality of services will be available overall at the planned women's and children's hospital at the Wesley site post-acquisition. Further, although some market participants had concerns about the proposed acquisition, generally they were not opposed to it, with many noting the counterfactual when making their submissions.
38. The ACCC is of the view that, given the counterfactual and the views of most specialists that the standard of care will not be affected and may improve in some areas, any lessening of competition in obstetrics and gynaecology as a result of

the proposed acquisition is unlikely to constitute a substantial lessening of competition pursuant to section 50 of the Act.

39. In the other areas of overlap, market inquiries indicated that either the extent of competition between the Mater and the Wesley in these overlap specialties was limited (in some instances, due to the differences in the facilities and equipment available at the Mater and the Wesley). In some other specialties, the procedures can be provided in a day surgery, which means that in these specialties, day surgeries are likely to act as a constraint on the merged hospital. Therefore, it was considered unlikely that the proposed acquisition would lead to a substantial lessening of competition in respect of any of these other specialties where the hospitals overlap.

Potential competition between the Mater and the Wesley in non-overlap specialties

40. Market inquiries indicated that there is limited, if any, potential competition in most services where the Wesley is not currently active, since there is no credible threat of the Wesley expanding into these specialties in competition with the Mater, either because of prohibitive costs or because of the need to have an on-site ICU facility in conjunction with certain specialties. Market participants noted that given the Wesley's recent decline, the prospect of it expanding into new specialties appears unlikely.
41. Based on available information, the ACCC formed the view that the proposed acquisition is unlikely to result in any significant elimination of potential future competition between the Mater and the Wesley in those non-overlap specialties where the parties do not currently compete.

Extent of competition between the Mater and the Wesley for doctors, which may lead to better outcomes for patients

42. Competition between hospitals for doctors may have benefits not only for doctors but also for patients, if it leads to hospitals offering, for example, better equipment, training or improved ancillary services.
43. Market inquiries indicated that both the Mater and the Wesley, due to the consistent shortage of specialists in regional areas, actively seek appropriately qualified specialists. Responses from market participants supported the view that given this shortage of specialists in regional areas, the merged hospital would still have an incentive to attract and retain doctors in Townsville, and may even be in a better position to do so, post-acquisition.
44. Market inquiries also indicated that the Mater offers attractive conditions to some doctors in certain specialities (such as well appointed consulting rooms at relatively low rents and/or the provision of ancillary services) to encourage them to establish their practices at the Mater. However, competition for doctors between the Mater and Wesley is more limited than in some other regional areas due to the differences between the two hospitals. Specifically, the Wesley is far smaller than the Mater and offers fewer specialties, and has been experiencing falling occupancy levels as well as declining support from doctors in a number of

specialties in recent years. Almost every doctor with visiting rights at the Wesley also has visiting rights at the Mater.

45. In respect of potentially better outcomes for patients as a result of competition between hospitals for doctors, initial market inquiries generally supported the view that doctors are primarily responsible for maintaining the level of services at the Mater and the Wesley, including having a large say over a number of services which are not provided by doctors.
46. A small number of market participants indicated that as part of this process, some doctors have tried to play the Mater and the Wesley off against one another in the past, by approaching both hospitals requesting new equipment/machinery. Some market participants expressed concern that the incentive for the Mater and the Wesley to fulfil such requests would be lessened post-acquisition.
47. Market inquiries indicated that the Mater and the Wesley are both receptive to purchasing new equipment (including the Mater even in those non-overlap services where the Wesley does not currently compete) and that competition between these two hospitals is generally not a critical factor in determining whether new equipment is provided. The majority of market participants were of the view that the proposed acquisition would not lessen the quality of services offered to private patients in the Townsville and surrounding region, and that it may even lead to benefits such as higher quality services offered by the merged hospital.
48. The ACCC considers that, given the limited extent of competition between the Mater and the Wesley for doctors, and lack of evidence to suggest that doctors playing the hospitals off one another is a significant factor in the provision of new equipment or the level of patient care in these two hospitals, it is unlikely that these factors would lead to the proposed acquisition resulting in a substantial lessening of competition.

Impact of the proposed acquisition on prices to uninsured patients

49. Some market participants expressed concern about the possibility that prices to uninsured patients may increase post-acquisition. This issue appeared to be most relevant to specialties such as elective plastic surgery, where the majority of procedures are not covered by insurance.
50. The ACCC understands that, generally speaking, the Mater and the Wesley's charges to uninsured patients are at least the same as, and in some cases higher than, the highest fee that has been contracted with a health fund. This appears to be consistent with the pricing practices of other private hospital operators and day surgeries.
51. However, market inquiries supported the view that the cost of services is not the only factor that uninsured patients take into consideration when deciding whether to be admitted to the Mater or the Wesley. Past experiences and other factors such as the complexity of the procedure (in which case doctors refer patients to the Mater) also influence this decision.

52. The ACCC considers that many uninsured patients are likely to consider the public Townsville Hospital to be a realistic alternative to the private hospitals (taking into account access and price), whereas insured patients are less likely to consider using the public hospital. Uninsured patients may weigh up the option of paying the full cost of an immediate private procedure against waiting for a public procedure at low or zero cost. In contrast, an insured patient, whose insurer will pay for the private procedure at a time of the patient's choosing, is far less likely to consider using the public system, since there is no significant cost saving to them for doing so.
53. Further, some specialists have operating lists at the Townsville Hospital so, in some cases, would be able to offer their uninsured patients admission to the public hospital as private patients. Although patients would still be required to pay for the specialist's services, they may face lower hospital fees compared to being admitted to one of the private hospitals. One specialist indicated a willingness to treat uninsured patients at the public hospital if cost was a significant issue.
54. Overall, taking into account the counterfactual, the ACCC considers that the proposed acquisition is unlikely to substantially lessen competition for the provision of private hospital services, including services to uninsured patients.

Barriers to entry for private hospitals and day surgeries

55. The ACCC considers that barriers to entry for a new private hospital are relatively high and the establishment of a new private hospital in the Townsville region is unlikely in the near future.
56. Market inquiries did indicate, however, that barriers to entry for a new day surgery facility are much lower, as demonstrated by recent entry. However, the ACCC notes that day surgeries only provide a competitive constraint in relation to certain specialties and are not sufficiently close substitutes across the range of specialties to form part of the relevant market.

Availability of reproductive services (including IVF) post-acquisition

57. Early in the ACCC's investigation, concerns were expressed by market participants in relation to the availability of reproductive services post-acquisition, given that the acquirer is a Catholic organisation whose beliefs do not permit certain procedures.
58. Following extensive market inquiries, the ACCC was satisfied that reproductive services, including IVF, would continue to be available at similar levels to patients in Townsville and the surrounding region post-acquisition. The ACCC understands that the Queensland Fertility Group, which currently offers IVF services at the Wesley and some services at Townsville Day Surgery, is proposing to transfer all its services to the Townsville Day Surgery with minimal, if any, interruption to services. The Queensland Fertility Group will operate separately from, and in competition with, Monash IVF, a competitor which already operates at Townsville Day Surgery.

Elimination of tubal ligation in conjunction with a Caesarean delivery post-acquisition

59. Tubal ligation performed in conjunction with a Caesarean delivery is uncommon among private patients in Townsville – the ACCC’s inquiries revealed that only a very low number of these procedures were performed at the Wesley in the past two years. The discontinuation of this procedure post-acquisition, due to the acquirer being a Catholic hospital, was an issue of concern for a small number of private patients. However, the option to undergo these procedures separately will continue to be available post-acquisition. On the basis of this information, and the counterfactual, the ACCC does not consider the discontinuation of this procedure at the Wesley post-acquisition constitutes a substantial lessening of competition.

Conclusion

60. On the basis of the above, in light of the counterfactual, the ACCC concluded that the proposed acquisition of the Wesley Hospital by the Mater Misericordiae Hospital is not likely to result in a substantial lessening of competition in any relevant market in contravention of section 50 of the Act.