Public Competition Assessment

30 July 2014

Sonic Healthcare Limited – proposed acquisition of assets of Delta Imaging Group

Introduction

1. On 17 January 2014, the Australian Competition and Consumer Commission (**ACCC**) announced its decision to oppose the proposed acquisition of Delta Imaging Group by Sonic Healthcare Limited (**proposed acquisition**). The ACCC decided that the proposed acquisition would be likely to have the effect of substantially lessening competition in the markets for the supply of MRI services in Newcastle and Maitland, and the supply of general diagnostic imaging services in Maitland, in contravention of section 50 of the Competition and Consumer Act 2010 (**the Act**).

2. 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 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 opposed;
   - a merger is subject to enforceable undertakings;
   - the merger parties seek such disclosure; or
   - a merger is not opposed but raises important issues that the ACCC considers should be made public.

4. This Public Competition Assessment has been issued because Sonic Healthcare Limited's proposed acquisition of Delta Imaging Group was opposed by the ACCC.

5. 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.

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. 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 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.

The parties

The acquirer: Sonic Healthcare Limited

8. Sonic is an Australian Securities Exchange listed company. It provides diagnostic imaging services in Australia and New Zealand, as well as pathology services in Australia, New Zealand, Europe and the United States and medical centre management services in Australia.

9. In Newcastle and the Hunter region of New South Wales, Sonic provides diagnostic imaging services through its subsidiary, Hunter Imaging Group Pty Ltd (**Hunter Imaging**). Hunter Imaging operates a number of clinics in the region, providing a range of general x-ray, ultrasound, computed tomography (**CT**) (collectively, general diagnostic imaging), magnetic resonance imaging (**MRI**) and nuclear medicine services.

10. Relevant to the assessment of the proposed acquisition, Hunter Imaging operates the radiology practices in Newcastle and Maitland (located approximately 32km from the centre of Newcastle) listed in Table 1 below.

Table 1 – Hunter Imaging radiology practices in Newcastle and Maitland

Location	Services provided
Newcastle	
Charlestown	• General diagnostic imaging • MRI
Cardiff	• General diagnostic imaging • MRI
Gateshead	• General diagnostic imaging
Broadmeadow	• General diagnostic imaging
Belmont	• General diagnostic imaging
Wallsend	• General diagnostic imaging
Toronto	• General diagnostic imaging
Maitland	
Maitland	• General diagnostic imaging
East Maitland	• General diagnostic imaging • MRI
Rutherford	• General diagnostic imaging

The target: Delta Imaging Group

11. The Delta Imaging Group was established in 2009 and consisted of two radiology practices, located in Charlestown (Newcastle) and Maitland. Both practices provided general diagnostic imaging services (including, x-ray, ultrasound and CT) and MRI services.

12. The Delta Imaging Group ceased trading on 9 July 2013 and was placed into liquidation.

Other industry participants

13. As explained further below, the areas in which Sonic and the Delta Imaging Group overlap is in the supply of general diagnostic imaging services and MRI services. Other suppliers of these services in Newcastle and Maitland are set out in Table 2.

Table 2: Suppliers of diagnostic imaging other than Hunter Imaging and the Delta Imaging Group

Supplier	Locations	General diagnostic imaging	MRI	Public Hospital/Private Radiology Practice
NEWCASTLE				
Primary	Charlestown	✓		**Private Radiology Practice**
	Merewether	✓	✓	**Private Radiology Practice**
Hunter Radiology	Newcastle	✓		**Private Radiology Practice**
	Glendale	✓	✓	**Private Radiology Practice**
Newcastle Radiology	Adamstown	✓		**Private Radiology Practice**
In Focus Radiology	Warners Bay	✓		**Private Radiology Practice**
Newcastle X-ray	Edgeworth	✓		**Private Radiology Practice**
Newcastle X-ray and Ultrasound	Charlestown	✓		**Private Radiology Practice**
HNEI: Calvary Mater Hospital	Waratah	✓	✓	**Public Hospital**
HNEI: John Hunter Hospital	New Lambton	✓	✓	**Public Hospital**
MAITLAND				
Greenhills X-ray	Maitland	✓		**Private Radiology Practice**
HNEI: Maitland	Maitland	✓		**Public Hospital**

Supplier	Locations	General diagnostic imaging	MRI	Public Hospital/Private Radiology Practice
Public Hospital				

The proposed acquisition

14. Sonic's proposal was to acquire assets of the Delta Imaging Group, primarily consisting of radiology equipment for the supply of x-ray, ultrasound, CT and MRI services.

15. All of the assets could be used to provide a full-service radiology business at the former premises of the Delta Imaging Group in Maitland and Charlestown. Alternatively, some of the assets could be redeployed to other existing practices of Sonic with Sonic supplying only a limited range of radiology services from the former Delta Imaging Group practices.

16. The ACCC considered both possibilities in assessing the potential competitive effects of the proposed acquisition. The ACCC concluded that the proposed acquisition was likely to result in a substantial lessening of competition, regardless of whether Sonic were to continue to operate the former Delta Imaging Group practices or whether Sonic were to redeploy some of the equipment.

Review timeline

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

Date	Event
15-Oct-2013	ACCC commenced review under the Merger Process Guidelines.
28-Oct-2013	Closing date for submissions from interested parties.
21-Nov-2013	ACCC awaiting information from Sonic. Former provisional date for announcement of findings (28th November) delayed.
27-Nov-2013	ACCC received further information from merger parties. ACCC amended former provisional date for announcement of findings (28th November).
05-Dec-2013	ACCC published a Statement of Issues outlining preliminary competition concerns.
20-Dec-2013	Closing date for submissions relating to Statement of Issues.
17-Jan-2014	ACCC announced it would oppose the proposed acquisition.

Market inquiries

18. The ACCC conducted market inquiries with a range of industry participants, including competing radiology practices in the Newcastle and Maitland areas, radiology practices operating Medicare funded MRI units outside of Maitland and Newcastle, referring medical practitioners, industry bodies and alternative bidders for the Delta Imaging Group assets.

Statement of Issues

19. The ACCC published its Statement of Issues on 5 December 2013 identifying the following concerns:

MRI services

- The proposed acquisition would result in Hunter Imaging being the only supplier of Medicare eligible MRI scans other than the public hospital in Newcastle (under a narrow geographic market definition), or Newcastle and Maitland (under a broad market definition).

  The ACCC was concerned that post-acquisition, the only other supplier of Medicare eligible MRI services, the public hospital, would not provide a sufficient constraint on Hunter Imaging to prevent a substantial lessening of competition.

- The proposed acquisition would result in Hunter Imaging being the only supplier of MRI services in Maitland (under a narrow geographic market definition).

  The ACCC was concerned that relative to the counterfactual of another radiology company providing MRI services from an unfunded MRI unit at Maitland, the proposed acquisition may result in a substantial lessening of competition through a deterioration of service levels for the supply of MRI services.

General diagnostic imaging services

- The proposed acquisition would result in Hunter Imaging being one of three suppliers of general diagnostic imaging services in Maitland (the other suppliers being Greenhills Radiology and the Maitland Public Hospital). Hunter Imaging would operate three out of four private radiology practices.

  The ACCC was concerned that the proposed acquisition may result in a substantial lessening of competition because the existing private radiology competitor, Greenhills Radiology, and the Maitland Public hospital would not provide a sufficient constraint on Hunter Imaging's pricing and service offerings post-acquisition.

Future with/without test

20. 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 a 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.

21. In this case, the ACCC considered that if the proposed acquisition did not proceed, another radiology company would be likely to acquire the Delta Imaging Group's assets and operate full-service radiology practices at the former Delta Imaging Group sites.

Industry background

22. Radiology is a medical specialty that employs the use of medical imaging to both diagnose and treat human injuries and illnesses.

23. Radiologists are doctors who specialise in the interpretation of diagnostic images, and provide clinical reports. Sonographers and radiographers (medical imaging technologists) are medical professionals who operate the relevant diagnostic imaging machinery.

24. Diagnostic imaging involves a variety of modalities, including x-ray, ultrasound, fluoroscopy, bone mineral densitometry, mammography, fine needle aspiration biopsy, CT, MRI and nuclear medicine / position emission tomography (PET).

Medical practitioners – referral practices

25. Doctors, including General Practitioners (**GPs**) and various other medical specialists, refer patients to radiology service providers. When making referrals, doctors select a radiology practice based on a range of factors including quality, convenience, price, location, services available and clinical relationship with the reporting radiologist.

26. Although patients are given a referral slip for a particular radiology practice or company, patients are free to go to radiology practices other than the practice their medical practitioner refers them to. However, market inquiries have indicated that patients rarely attend radiology practices other than those they are referred to.

27. Market inquiries also indicated that many doctors prefer to refer to radiology practices which are full service: that is practices which offer all general diagnostic imaging modalities and MRI, and have a radiologist present at the radiology practice. There are several reasons for this preference, including:

    - a full service practice provides expertise in multiple modalities and is therefore perceived by doctors as being able to provide a higher quality of service;

    - referring doctors often request several diagnostic imaging investigations to diagnose patients, and on-site radiologists with expertise in several modalities are able to provide advice on the most appropriate methods based on the results of the preliminary diagnostic image;

    - referring doctors often develop ongoing professional relationships with on-site radiologists who consistently produce high quality reports on which referring doctors can rely. Practices without an on-site radiologist may not use the same radiologists to produce reports and therefore referring doctors can be reluctant to refer patients to such practices.

Medicare eligibility of MRI scans

28. The Australian Government regulates Medicare funding of MRI services by entering into a Deed of Undertaking with certain accredited MRI service providers. The Deed of Undertaking permits specific MRI units to supply Medicare MRI eligible scans (i.e. MRI scans which attract a Medicare rebate). These deeds of undertakings define MRI units as either:

    - fully funded – these units can supply the full range of Medicare eligible MRI scans under the MBS when referred by a specialist, surgeon or GP; or

- partially funded – these units can supply a selected number of Medicare eligible scans under the MBS when referred by a GP and for certain breast scans.

Table 3 below summarises the Medicare eligible scans which can be provided by fully and partially funded MRI units.

Table 3: Summary of Medicare eligibility on funded and unfunded MRI units.

Referrer	Fully funded MRI unit	Partially funded MRI unit	Unfunded MRI unit
Specialist or surgeon	All Medicare eligible MRI scans.	Certain breast scans.	Nil
GPs	• Select MRI scans for patients under 16 years of age with certain symptoms for scans of the head, spine, ankle, knee, hip, elbow and wrist. • Select MRI items for patients over 16 years of age with certain symptoms for scans of the head, neck or knee.	• Select MRI scans for patients under 16 years of age with certain symptoms for scans of the head, spine, ankle, knee, hip, elbow and wrist. • Select MRI items for patients over 16 years of age with certain symptoms for scans of the head, neck or knee.	Nil

29. MRI units without a deed of undertaking are ‘unfunded’. While these units can supply all types of MRI scans, these scans will not attract a Medicare rebate and patients can be charged substantial out of pocket fees.

30. Prior to 1 November 2012, only patients referred by specialists or surgeons for MRI scans listed under the MBS were eligible for the Medicare rebate. Additionally, to receive the Medicare rebate for these scans, patients would have needed to be referred to fully funded MRI units, of which there were only 125 throughout Australia.

31. On 1 November 2012, the Australian Government increased the number of MRI items under the MBS which could attract the Medicare rebate if supplied by a funded MRI unit. These items related to MRI scans for patients under 16 years old, referred by a GP. The Australian Government also increased the number of fully funded MRI units and introduced partial funding of MRI units. There are now 169 partially funded MRI units and 168 fully funded MRI units throughout Australia.

32. On 1 November 2013, the Federal Government further increased the number of MRI items which can be referred by a GP to a fully or partially funded MRI unit and attract the Medicare rebate. These items related to MRI scans of the head, neck and knee for patients over 16 years old.

Market definition

33. The parties overlapped in the supply of general x-ray, ultrasound, CT and MRI in Newcastle and Maitland.

Product dimension

34. In previous matters the ACCC has considered that all diagnostic imaging modalities, except for MRI and nuclear medicine, fall within the same product

dimension. The ACCC did not receive any submissions to indicate a different approach should be taken in this matter.

35. In most cases, there is limited substitutability between the various diagnostic imaging modalities, as they offer different functionalities to diagnose a variety of injuries or ailments. However, based on information obtained in market inquiries, the ACCC believes it is appropriate to consider the supply of general diagnostic imaging services, including x-ray, ultrasound and CT, as one product dimension because radiology practices tend to supply these modalities together.

36. Further, with the exception of MRI services, the training and qualifications of medical imaging technicians and radiologists allow these practitioners to provide diagnostic imaging services on several modalities.

37. In contrast, radiologists and medical imaging technicians require additional training and qualifications to provide MRI services. The ACCC therefore considers that the supply of MRI services to be in a separate product dimension to general diagnostic imaging services.

Radiology services provided by hospitals

38. Radiology practices compete for referrals of outpatients. These are patients who are not admitted to a hospital to obtain radiology or any other medical services. Radiology services are provided to outpatients by private radiology practices, private hospitals and public hospitals.

39. Services provided to hospital in-patients by public or private hospitals are not included within the relevant markets. This is primarily because in-patient services require a patient to be admitted to hospital and this is unlikely to be substitutable on either the demand or supply-side to any material extent.

Geographic dimension

General diagnostic imaging services

40. Market inquiries indicated that radiology patients in Newcastle and Maitland generally seek to obtain general diagnostic imaging services in their local area, which may include the five or six suburbs surrounding their home or the location of their doctor. The ACCC therefore concluded that there are separate Newcastle and Maitland markets for the supply of general diagnostic imaging services.

Newcastle

41. The ACCC did not receive any third party submissions, in response to the Statement of Issues, suggesting that the geographic boundary for the supply of general diagnostic imaging services extends beyond Newcastle.

42. In Newcastle, most of the competing radiology practices are located within 10km of each other. While Hunter Imaging has practices at multiple locations in Newcastle, some practices are located further from the central Newcastle area, such as Toronto (which is located approximately 17km from the target site in Charlestown). Market inquiries indicated it is unlikely that significant numbers of patients would travel beyond 10km from the more central parts of Newcastle, particularly to obtain the relatively routine general diagnostic imaging modalities (i.e. x-ray and ultrasound).

43. Nevertheless, even if Hunter Imaging's Toronto practice were included as a competitor in the Newcastle market, this would not impact the ACCC's analysis.

Maitland

44. Some submissions were made to the ACCC stating that the relevant market should be broadened beyond Maitland to include practices in Cessnock. If a broader market definition was adopted, Valley Imaging and Local X-Ray at Cessnock (approximately 30km from the target site in Maitland) would be included as competing private radiology practices. Sonic does not have a radiology practice in Cessnock.

45. Information from market inquiries following the release of the Statement of Issues revealed that some Cessnock residents attend radiology practices in Maitland for general diagnostic imaging services. However, these were primarily patients who work or attend specialist appointments in the area.

46. Cessnock is a smaller centre than Maitland and is not on any through route for Maitland patients. In contrast, Maitland is a large centre with a larger hospital and medical precincts with resident specialists which Cessnock patients may attend. Market feedback was that Cessnock has a very small hospital and medical precinct with very few resident specialists. It would therefore be unlikely that significant numbers of Maitland residents would travel to Cessnock for diagnostic imaging services in response to a price increase or service deterioration in Maitland.

47. Prior to the release of the Statement of Issues, the ACCC did not include Rutherford as part of the Maitland market for general diagnostic imaging services. However, market feedback following the release of the Statement of Issues was that given its close proximity to Maitland (approximately 5km), radiology practices in Rutherford should be included as competitors in the market. This resulted in the addition of another Hunter Imaging practice to the Maitland market, which supplied general diagnostic services (x-ray and CT).

MRI services

48. The preliminary view in the Statement of Issues was that there are likely to be separate local markets for the supply of MRI services in Newcastle and Maitland.

49. Following the release of the Statement of Issues, information from market participants indicated patients are willing to travel up to 50km for MRI services. This is mainly because it is less common for radiology practices to offer MRI services than other general diagnostic imaging services, making it necessary for many patients to travel longer distances to acquire them.

50. The ACCC therefore concluded that the geographic dimension of the market for MRI services should encompass both Newcastle and Maitland.

Conclusion on relevant markets

51. The ACCC concluded the following markets to be relevant to the assessment of the proposed acquisition:

- The supply of general diagnostic imaging services to outpatients in Newcastle.
- The supply of general diagnostic imaging services to outpatients in Maitland (including Rutherford).

- The supply of MRI services to outpatients in a combined Newcastle/Maitland market.

Competition analysis

Supply of MRI services in Newcastle and Maitland

52. The ACCC concluded that the proposed acquisition would be likely to result in a substantial lessening of competition in the market for the supply of MRI services in Newcastle and Maitland taking into account the following factors:

    - Post-acquisition, Hunter Imaging would be the only private radiology company capable of providing Medicare eligible MRI services.
    - As Medicare eligible MRI scans are the key source of demand for MRI services, Primary and Hunter Radiology would not impose a sufficient competitive constraint on Hunter Imaging to prevent a substantial lessening of competition, given that they do not offer Medicare eligible MRI services.
    - The only other supplier of Medicare eligible MRI services is the public hospital provider, HNEI, which must prioritise services to in-patients and is capacity constrained. Market inquiries indicated that HNEI would not be likely to impose a sufficient competitive constraint on Hunter Imaging post-acquisition to prevent a substantial lessening of competition.
    - Barriers to entry are high and there is no credible threat of new entry.

53. The ACCC concluded that in the absence of the proposed acquisition, an alternative acquirer would be likely to operate a full-service radiology practice at the former Delta Imaging Group sites. This would enable the supply of MRI services using two partially funded MRI units (both in Newcastle) and one unfunded MRI unit (Maitland) in competition with other service providers in Newcastle. These assets would enable particularly close competition with Hunter Imaging's partially funded MRI unit at Charlestown and fully funded MRI units at Cardiff and East Maitland.

Significance of changes to Medicare eligibility of MRI since 1 November 2013

54. The key sources of demand for MRI services are:

    - patients referred for scans by specialists and surgeons, the bulk of which are Medicare eligible;
    - patients referred for scans by a GP, of which a selected number of items are Medicare eligible; and
    - patients referred for scans by any medical practitioner for injuries covered under workers' compensation schemes (these scans do not attract a Medicare rebate).

    Market participants consistently stated that Medicare eligible MRI scans account for the vast majority of the demand for MRI services.

55. Despite the introduction of the GP-referrable Medicare eligible MRI scans being very recent, information obtained in market inquiries demonstrated there has already been a significant increase in the number of GP referrals for Medicare eligible MRI scans.

56. Radiology companies which operate partially funded MRI units outside of the relevant market provided data indicating increases in the number of Medicare-eligible MRI scans conducted by these units since 1 November 2013, ranging from 30-80%.

57. Further, Medicare data show that in the first two months that the Medicare eligible GP referred adult MRI scans were available, the number of GP-referred scans increased by 23%. As a proportion of total Medicare eligible MRI scans conducted, these scans increased from 20.1% (November 2013) to 24.95% (December 2013). These data are summarised below at Table 4.

58. These data indicate that the newly introduced GP-referred MRI scans are likely to account for a significant proportion of demand for MRI services. However, as the new items have only been available for referral since November 2013, it is too early to identify the full impact the expansion will have on demand for services from partially funded MRI units. The ACCC found that GP awareness of the changes to Medicare eligibility was relatively low. As GP awareness increases, this is likely to further significantly increase the number of GP referrals to both partially funded and fully funded MRI units.

Table 4 – November and December Medicare data for MRI

Type of scan	**November 2013**		**December 2013**		**Medicare eligible on fully or partially funded MRI units**
	Number of scans	**Percentage of total**	**Number of scans**	**Percentage of total**	
GP referred (under 16 years old)	1,803	2.6%	1,329	1.93%	Both
GP referred (over 16 years old)	12,099	17.5%	15,835	23.01%	Both
GP referred (all)	13,902	20.1%	17,164	24.95%	Both
Certain breast scans	947	1.36%	343	0.5%	Both
Other specialist referred scans	54,298	78.5%	51,298	74.55%	Fully funded units only

Source: https://www.medicareaustralia.gov.au/statistics/mbs_group.shtml

59. The number of GP referrals for MRI scans to funded MRI units is expected to increase because of the following factors:

- The availability of Medicare rebates on certain GP referred scans enables GPs to refer patients directly for MRI scans without needing a prior referral to a specialist. This will reduce waiting times for receiving diagnoses. The ACCC obtained data from the 2012/2013 financial year which showed that specialist referred MRI scans equivalent to the newly introduced GP referred MRI scans accounted for a high proportion of Medicare eligible MRI scans overall. The ACCC considered this indicated significant potential for substitution of GP referrals for specialist referred Medicare eligible MRI scans where the services to be provided to patients are equivalent as between GPs and specialists.

- GPs will refer patients for MRI scans, which is often a more clinically appropriate test, rather than CT scans for certain symptoms. CT scans have previously been used instead of MRI scans because they were Medicare eligible.

- An organic increase in demand for MRI scans.

60. The ACCC was therefore satisfied that the newly introduced GP referrable Medicare eligible MRI scans represented a significant proportion of the demand for MRI services and this was expected to increase. The funded MRI units formerly owned by the Delta Imaging Group would therefore be a significant constraint on Hunter Imaging if operated by an alternative acquirer.

Competitive constraints

61. The following MRI units are located in the Newcastle and Maitland areas:

Table 5 – Providers of MRI services (funded and unfunded) in Newcastle and Maitland

Provider	Location	Medicare eligibility
NEWCASTLE		
Hunter Imaging (Sonic)	Cardiff	Full
Hunter Imaging (Sonic)	Charlestown	Partial
Delta Imaging Group	Charlestown	Partial
Delta Imaging Group	Charlestown	Partial
HNEI	John Hunter Hospital	Full
HNEI	John Hunter Hospital	Partial
HNEI	Calvary Mater Hospital	Partial
Hunter Radiology	Glendale	None
Primary Healthcare	Merewether	None
MAITLAND		
Sonic	East Maitland	Full
Delta Imaging Group	Maitland	None

62. As noted above, the proposed acquisition would result in Hunter Imaging being the only private radiology practice with partially or fully funded MRI units in the Newcastle and Maitland areas.

Constraint from the public hospital provider

63. Market participants expressed significant concerns regarding HNEI's ability to competitively constrain Hunter Imaging.

64. Although HNEI supplies Medicare eligible MRI services to out-patients, its capacity to accommodate significantly more out-patient referrals is limited.

65. The primary business of public hospitals is to provide services to in-patients. Because public hospitals have an obligation to prioritise services to in-patients over out-patients, they cannot choose to switch to providing services to out-patients, rather than in-patients, in response to an increase in out-patient demand.

66. Hospital in-patients commonly have serious illnesses which may be more progressed and complex, therefore requiring more time and resources for the provision of services. Public hospitals also focus time and resources on hospital clinics and training of medical staff. These factors can result in poor accessibility for out-patients in terms of long wait times for appointments and, diminished service through inconvenience and potential delays in providing reports for images.

67. Further, out-patients acquiring MRI services from HNEI are often previous hospital in-patients or referred from specialist clinics within the hospital, rather than external doctors. Patients of these specialists are likely to have specialist appointments and imaging services provided on the same day.

68. On the basis of these factors, the ACCC concluded that if the proposed acquisition proceeded, the funded MRI units at the John Hunter and Calvary Mater hospitals in Newcastle would not impose a sufficient constraint on Hunter Imaging to prevent a substantial lessening of competition.[1]

Constraint from unfunded MRI units

69. Market inquiries indicated that radiology practices with unfunded MRI units are not a strong competitive constraint on radiology practices with funded MRI units, particularly with respect to pricing competition. While practices operating unfunded MRI units provide some competition, practices operating partially or fully funded MRI units compete more closely on price as they have the ability to charge no or lower fees to patients for Medicare eligible scans, which account for the vast majority of MRI scans supplied.

70. Market participants consider that Hunter Imaging is the leading provider of MRI services in the Newcastle and Maitland areas. Market participants stated that its position is, to a large extent, because it operates the only fully funded MRI units outside of the public hospital system.

71. Although demand for MRI services is increasing, MRI scans are relatively expensive tests, generally costing patients between $200 and $800 per scan (without a Medicare rebate). Referring doctors, particularly GPs, are often reluctant to refer patients to practices where patients cannot receive the Medicare rebate for MRI scans. Therefore, many referring doctors refer patients to radiology practices with funded MRI units for Medicare eligible scans. As GP referrals are becoming a much more significant source of referrals for MRI services, the acquisition by Sonic of the former Delta Imaging Group MRI units would enable Hunter Imaging to further entrench its position as the principal supplier of MRI services.

72. Additionally, because doctors typically refer to a single radiology practice for all imaging services, it is anticipated that GPs who refer patients for Medicare eligible scans to practices with a funded MRI unit are also likely to refer patients to the same practices for non-Medicare eligible MRI scans. It is therefore anticipated that for radiology practices with funded MRI units, there will not only be a significant increase in GP referrals to these practices for Medicare eligible MRI scans, but also for non-Medicare eligible scans.

73. In this context, the acquisition by Sonic of the partially funded MRI unit would be likely to significantly increase Hunter Imaging's market share for the supply of MRI services through an increase in referrals from GPs Medicare eligible MRI scans as well as ancillary referrals from GPs.

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[1] The Maitland public hospital does not have an MRI unit.

74. For the reasons outlined at paragraph 59, radiology businesses operating both within and outside of the relevant markets consistently stated that in light of the expansion of Medicare eligibility of GP-referrable MRI scans, partially funded units are now capable of winning significant market share from fully funded and unfunded MRI units. Therefore, the relatively weak constraint previously imposed by unfunded MRI units on funded MRI units prior to the Medicare expansion on 1 November 2013 has been further diminished. The ACCC considered that since the expansion of Medicare eligibility, the partial funding status allocated to the MRI units formerly owned by the Delta Imaging Group had the potential to be a source of significant competitive constraint against Hunter Imaging's funded units, but that unfunded MRI units were not likely to competitively constrain a merged Sonic-Delta entity to a significant extent.

75. The acquisition of the former Delta Imaging Group practices by an alternative purchaser would allow that purchaser to operate a full-service practice, which would competitively constrain Hunter Imaging in the supply of MRI services in Newcastle and Maitland. Without the constraint of an alternative private radiology practice capable of supplying Medicare eligible services, Hunter Imaging would have the ability to increase prices and reduce service levels for the supply of MRI services, in particular, the supply of MRI scans attracting a Medicare rebate.

Barriers to entry

76. Barriers to establishing a radiology practice in Newcastle and Maitland are significant. This is discussed further at paragraphs 86 to 99. For the supply of MRI services, the ACCC found that potential entrants face the following additional barriers to entry and expansion:

- Investment in MRI equipment requires significant capital investment and sunk costs.
- It is very difficult to recruit skilled staff needed to operate MRI units to Newcastle and Maitland as there is a shortage of skilled staff. Market inquiries revealed examples of radiology practices being unable to enter the Newcastle and Maitland market as a result of this issue.
- Market participants stated that having a Medicare eligible MRI unit has the potential to attract much higher volumes of referrals and associated revenue than an unfunded unit. Without a Medicare eligible MRI unit, radiology practices are at a high risk of not making a return on their investment.
- The Commonwealth Government is unlikely to grant full or partial funding status to additional MRI units in the foreseeable future.
- Funding status of MRI units is tied to their location. As such, it is unlikely that an existing or potential competitor could relocate a funded MRI unit from another area to the Newcastle or Maitland areas.

77. Given these barriers, the ACCC considered that Hunter Imaging would not be constrained by the threat of new entry for the supply of MRI services in the Newcastle and Maitland area post-acquisition. In particular, there is no credible threat of a new entrant capable of providing Medicare eligible MRI services and replicating the constraint that would be imposed by the Delta Imaging Group funded MRI units.

Supply of general diagnostic imaging services in Maitland

78. Post-acquisition, Hunter Imaging would operate four out of five private radiology practices in Maitland if it continued to operate the Delta Imaging Group practice, or three out of four practices if it chose not to operate the Delta Imaging Group practice. This contrasts with the likely future without the acquisition, where an alternative acquirer would operate the relevant assets in competition with Hunter Imaging and the other providers.

79. The ACCC formed the view that the only other private radiology practice, which only provides x-ray and ultrasound services and is not a full-service practice, would impose a limited competitive constraint on Hunter Imaging post-acquisition. Similarly, the public hospital provider, HNEI, is unlikely to impose a sufficient constraint in this market.

80. The proposed acquisition would therefore significantly increase market concentration in the supply of general diagnostic imaging services in Maitland, where Hunter Imaging already has a high share of the market, and would not be constrained by the threat of new entry.

Sonic is unlikely to be constrained by existing competitors in Maitland

81. Before the Delta Imaging Group was placed into liquidation, its Maitland practice was the only other private, full-service practice which operated in competition with Hunter Imaging's Maitland practices. The ACCC considered that the former Delta Imaging Group assets have the potential to offer significant competition against Hunter Imaging in the supply of general diagnostic imaging services in Maitland in the future without the proposed acquisition.

82. Hunter Imaging currently has a significant presence in the market for general diagnostic imaging services in Maitland, operating three out of four private radiology practices. The proposed acquisition would have the effect of reinforcing its already substantial presence and would prevent a competing full-service radiology practice from being established at the former Delta Imaging Group site in Maitland.

83. As Table 2 indicates, the only other radiology practices in Maitland are Greenhills Radiology and HNEI.

84. Greenhills Radiology, the only other private radiology practice in Maitland, does not offer a full service practice (it also does not supply all general diagnostic imaging modalities) and does not have a radiologist present on site. As noted in the industry background section, market inquiries have indicated that an on-site radiologist is often important for a radiology practice's ability to provide high levels of service to referring doctors. Consequently, it is unlikely that Greenhills Radiology would provide a sufficient constraint to prevent Hunter Imaging from increasing prices or reducing service levels.

85. For the reasons outlined at paragraphs 63 to 68 above, public hospitals provide a limited constraint on private radiology practices. Market inquiries revealed significant concerns about the current effectiveness of HNEI as a competitive constraint upon private radiology practices and its ability to increase the level of constraint that it provides in the market in the foreseeable future.

Barriers to entry

86. The ACCC considered whether, following the proposed acquisitions, another radiology practice might be capable of entering the market for general diagnostic imaging services in Maitland. The ACCC considered whether any 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 acquisition.

87. The ACCC found that potential entrants would face significant barriers to establishing a radiology practice in Maitland, including the following:

    - There is a shortage of skilled labour.
    - There is a shortage of suitable sites. Radiology equipment consumes high levels of electricity relative to many businesses, which often requires upgrading the electricity connection to a given site, to obtain adequate supply. These arrangements can be time consuming and very costly.
    - There are considerable lead times and sunk costs involved in establishing a new radiology practice.
    - It can be difficult to build up a referral base from medical practitioners. This can pose a particular barrier when the market is already served by multiple existing radiology practices (particularly if they include a scaled incumbent like Sonic/ Hunter Imaging).

88. For these reasons, the ACCC concluded that there was little prospect of a radiology practice (and in particular, a full-service radiology practice) entering the market in the foreseeable future other than through the acquisition of the Delta Imaging Group site in Maitland. The ACCC considered that through the acquisition of the Delta Imaging Group's site, a new owner would overcome a number of these barriers.

89. The ACCC therefore concluded that the proposed acquisition would be likely to substantially lessen competition in the market for the supply of general diagnostic imaging services in Maitland.

Supply of general diagnostic imaging services in Newcastle

90. The proposed acquisition would result in Hunter Imaging operating eight out of 16 private radiology practices in Newcastle.

91. The ACCC considers that existing competitors in this market would be likely to impose a sufficient competitive constraint on Hunter Imaging post-acquisition. Hunter Imaging is unlikely to have the ability or incentive to raise its prices or reduce its service levels as it would risk losing business to other practices, most of which bulk bill all general diagnostic imaging examinations. Additionally, Primary and Hunter Radiology operate full service practices in competition with Hunter Imaging's Newcastle practices.

92. The ACCC therefore concluded that it is unlikely that the proposed acquisition would result in a substantial lessening of competition in the market for the supply of general diagnostic imaging services in Newcastle.

Conclusion

93. On the basis of the above, the ACCC formed the view that the proposed acquisition of assets of the Delta Imaging Group by Sonic Healthcare Limited would be likely to result in a substantial lessening of competition in the markets for supply of MRI services in Newcastle and Maitland and, the supply of general diagnostic imaging services in Maitland, in contravention of section 50 of the Act.