

13 November 2015

Att: Sam Campbell
Australian Competition & Consumer Commission (ACCC)
mergers@acc.gov.au

Dear Mr Campbell

Submission re: Sonic/APP

The National Coalition of Public Pathology (NCOPP) represents public pathology services across Australia and would like to comment on the proposed acquisition by Sonic Healthcare (Sonic) of Adelaide Pathology Partners (APP) (the proposed acquisition).

Description of organisation

NCOPP represents public pathology services throughout Australia. Our members are the major government owned and operated pathology services in each State and Territory in Australia. They provide the vast majority of pathology services in Australia's public hospitals, service a number of private hospitals, and operate community based collection services for patients upon request from GPs and Specialists.

In addition to diagnostic services, NCOPP members conduct research and teaching in the areas of new and existing diseases, tests and treatments, and collaborate closely with colleagues in all areas of patient care, with many pathologists also performing clinical roles. Their laboratory testing and medical consultation services play a crucial role in timely clinical diagnosis, in monitoring therapy and in prevention of disease in individuals and the community. This work is supported by earnings generated by public pathology's community pathology practice.

NCOPP has been a co-signatory to previous Pathology Funding Agreements between the Australian Government and the pathology profession. These Agreements managed pathology use and expenditure under the Medicare Benefits Schedule (MBS) to ensure that pathology services are of high quality, accessible and affordable. Specific objectives under these agreements have included maximising competition in the pathology sector, providing stability of the regulatory and funding environment and recognising diversity in the practice of pathology to ensure sustainability in the sector.¹ It is important to note that the pathology sector is not currently operating under a Pathology Funding Agreement.

SA Pathology is a member of NCOPP and has a presence in the community pathology market. SA Pathology will be liaising directly with the ACCC in relation to the proposed acquisition. NCOPP makes this submission in light of its national view of changes to competition practice in the pathology sector over the last decade.

NCOPP does not have any formal relationship, commercial or otherwise with Sonic or APP, but interacts from time to time with employees of Sonic and APP in meetings convened by the Australian Department of Health and the Royal Australasian College of Pathologists (RCPA) concerning funding under the Medicare Benefits Schedule (MBS) and other aspects of pathology practice.

¹ Australian Government, Pathology Funding Agreement, 2011-2016, Clause 2.

Reason for interest

NCOPP believes it is important that the ACCC consider the proposed acquisition not only in the light of the provision of pathology services (in terms of quality, access and competition), but in the broader context of the health care sector and in particular the potential effects on the publicly funded health system.

Relevant markets

Competition between community pathology service providers occurs on the basis of the locations of collection centres rather than laboratories. Providers tend to operate an economies of scale business model and rely on throughput of higher volume and less complex tests to generate a profit. As such, providers compete to service areas where a high volume of routine test requests and specimens can be collected. These tests are then sent for processing by a central laboratory.

APP's market presence is in metropolitan Adelaide. SA Pathology a statewide service which operates across the metropolitan, regional and rural areas of South Australia.

Competition between service providers differs for the supply of clinical pathology services compared to the supply of anatomical pathology services. The latter tends to be more complex and less profitable work. NCOPP understands that APP originated as a boutique anatomical pathology provider, and then broadened its scope to include more routine diagnostic testing. To fairly assess the impact of the proposed acquisition, the reduction in competition specifically in anatomical pathology should be considered.

Impact on competition

NCOPP is unable to comment on the exact nature of competition between Clinpath and APP. However, the proposed acquisition will decrease competition in South Australia. Public pathology is already limited in the ability to fairly compete with the private sector as it:

- does not pay above market rents for Approved Collection Centres to secure volumes as occurs in the private sector;
- receives lower fees payable by Medicare per pathology episode (the public sector receives a flat \$2.40 Patient Episode Initiation (PEI) fee whereas private sector PEIs range from \$2.40 to \$17.70 depending on where the specimen collection is performed);
- carries higher operating costs due to teaching and research, and the requirement to operate 24 hours, 7 days per week;
- undertakes the full spectrum of testing, including higher cost, complex esoteric tests.

Private pathology companies can alter their billing policies as they deem appropriate to meet their corporate objectives. For instance, Sonic's billing practice is to charge and not bulk bill non-concession card holders for pathology tests. A reduction in competition may reduce the rates of bulk billing in the private sector. This in turn can result in more patients generally or more patients with a particular condition incurring out of pocket expenses. Patients who cannot afford these costs may forgo testing (and hence timely diagnosis and treatment) and present to the South Australian public health system at a more advanced stage of disease. Unlike private providers, SA Pathology's billing practices are constrained by government policy which limits out of pocket expenses. Patients are largely unaware that they are free to choose their pathology provider, and tend to only go to the provider listed on the pathology request form. Hence a reduction in bulk billing by a private provider would not necessarily drive patients to find another bulk billing provider.

Private pathology providers predominantly rely on Commonwealth funding through the Medicare Benefits Schedule (MBS) as their primary source of revenue. The MBS does not encourage patient-centred, outcomes based pathology testing and it does not reflect the costs of providing pathology tests. MBS fees are generally well above cost for routine tests and well below costs for more complex tests. Private providers tend to cherry pick the routine profitable tests and refer the more complex tests to public pathology providers. In addition, application of coning rules (which limit MBS funding to the three most expensive tests requested by a General Practitioner), influences referral of unpaid work to public pathology providers. A decrease in competition may see a propagation of this type of activity. Alternatively, there may be a greater number of tests referred to Sonic's larger laboratories on the eastern seaboard of Australia and this could significantly increase turn-around times for important pathology tests.

The barriers to entry in the pathology market are significant. No single private small provider has grown to a national level in the last 10-15 years. In that timeframe, entities have only grown considerably by mergers and acquisitions. This indicates that it is unlikely for new small practices to grow quickly to fill the absence of competition. Following the deregulation of Approved Collection Centre numbers, the larger corporate entities such as Sonic, Primary and Healthscope have saturated the market with collection centres. These organisations can afford to pay well beyond market rent for prime collection space to secure referral streams. While this is contrary to the spirit of relevant regulations, the Australian Department of Human Services / Department of Health have been unable to enforce appropriate behaviour due to the lack of definition of what constitutes market rent in the regulations.

The proposed acquisition could further increase Sonic's purchasing power and strengthen their bargaining position with regard to equipment, reagent and consumable supply. Sonic already uses its global strength to negotiate favourable pricing. Removal of a competitor could see a reduction in the viability of some suppliers and could lead to other pathology providers, especially the public providers, paying higher prices for equipment, reagents, consumables and service, thus effectively subsidising Sonic's increased profits.

NCOPP trusts that these comments are of assistance to the ACCC in relation to the proposed acquisition by Sonic of Adelaide Pathology Partners. For any points of clarification or further information, please contact NCOPP CEO Jenny Sikorski at ceo@ncopp.org.au.

Yours sincerely



Ms Jenny Sikorski, CEO