
Completed acquisition by Southern Cross Healthcare Group Limited of Cannon Capital Ventures Limited

The OFT's decision on reference under section 22(1) given on 16 December 2005. Full text of decision published on 3 January 2006.

Please note that square brackets indicate that information has been excised or replaced by a range at the parties' request.

PARTIES

1. **Southern Cross Healthcare Group Limited (SX)** operates 375 care homes across the UK. In addition, through its affiliate, NHP, it owns a portfolio of 357 homes. Most of these are operated by SX, although 57 are operated by third parties, of which Ashbourne, owned by Cannon Capital, operates 22. SX and NHP are wholly owned by Blackstone Group.
2. **Cannon Capital Ventures Limited (Cannon)** operates a portfolio of 208 care homes across the UK, mainly through Ashbourne. In addition, its SunChoice division supplies dry consumables (towels, linen, crockery etc.) primarily to Ashbourne, although about 20 per cent of its sales are to third parties. Its UK turnover in the financial year to 31 May 2005 was £[> 70] million.

TRANSACTION

3. This transaction qualified for investigation under the EC Merger Regulation¹ (ECMR), but was referred to the UK in accordance with Article 4(4) ECMR on 24 October 2005. The transaction was completed on 4 November 2005.
4. The statutory timetable in accordance with Article 4(4) ECMR expires on 6 January. The 40-working-day administrative deadline expires on 22 December 2005.

¹ Council Regulation (EC) No 139/2004.

BACKGROUND

5. On 5 April 2005, the OFT cleared the completed acquisition by the Blackstone Group of NHP plc.² Like the current transaction, this acquisition concerned the supply of (residential and nursing) care home services in the UK. Notwithstanding substantial shares in some areas, the OFT believed that there existed specific constraints in the form of pricing restrictions and overcapacity in those areas. Moreover, it was considered that barriers to entry were low and local funding authorities exercised a sufficient degree of countervailing buyer power to counteract any potential competition concerns.

JURISDICTION

6. As a result of this transaction SX and Cannon have ceased to be distinct. The UK turnover of Cannon exceeds £70 million, so the turnover test in section 23(1)(b) of the Enterprise Act 2002 (the Act) is satisfied. The OFT therefore believes that it is or may be the case that a relevant merger situation has been created.

RELEVANT MARKET

Product market

7. The parties have submitted that the relevant product frame of reference for this assessment should comprise the supply of care home services to the elderly in general. However, in previous cases³ the OFT has further divided this market into services provided by (i) residential care homes and (ii) nursing care homes (see below regarding EMI). While residential care consists of the provision of personal care for the elderly, nursing care caters for persons suffering from sickness, injury or infirmity, and requires the presence of staff with specific nursing/medical qualifications. The funding of this care is either done by the local authority ('local funding authority') or by, or on behalf of, the resident themselves (so called 'self-funders'); however, residents may also decide to top-up the local authority funding where this does not meet the whole of the cost of a particular care home.
8. On the *demand side*, it is considered that individuals requiring high levels of care could not readily substitute their need for nursing care. The additional care required for nursing as opposed to residential care is reflected in prices for the former being on average £151 per week higher than for residential care.⁴ However, the parties

² Available at <http://www.offt.gov.uk/nr/exeres/c62451ec-546e-4ed7-bcd9-2750a96a57da.htm>

³ Acquisition by Takecare PLC of Court Cavendish Group PLC (1997); Proposed Acquisition by the British United Provident Association Ltd of Care First Group PLC (1997); *Blackstone/NHP*.

⁴ Average weekly fees are £496 for private nursing care for elderly people and £345 for private residential (personal) care. (Source: Care of Elderly People, UK Market Survey 2004, Laing & Buisson).

have submitted that on the part of local funding authorities some substitution between nursing and residential care could exist, because local funding authorities seek to place people in (less expensive) residential care rather than nursing care whenever possible.

9. For those requiring residential care, nursing care may provide a substitute, although residents may not necessarily want to be surrounded by substantially less able individuals. Care at home supported by other local authority services could also to some extent be considered an alternative for residential care and it is currently government policy to promote this option.
10. In terms of *supply side* substitution, to start providing nursing care, a residential home would have to hire additional nursing staff in order to provide 24 hour nursing cover and register with the Commission for Social Care Inspection.
11. The OFT has also considered whether care for the elderly mentally infirm (EMI) including dementia care could be considered separately from other nursing care provision. It has been submitted that to accept individuals with dementia, an authorisation is required and a fee of approximately £950 is incurred. The entire process would take between six and ten weeks. According to the parties, nursing care homes are required to employ a registered mental health nurse if they intend to offer EMI care. For the purpose of this assessment, EMI including dementia care has therefore been considered separately.
12. The above considerations suggest that there may currently exist at least a degree of demand and supply-side substitution between residential and nursing care homes. However, given that this might not apply to all customers and that most third parties considered the two forms of care to be distinct, they have been considered separately. In view of the lack of competition concerns arising from this transaction even on the narrowest frame of reference, it was not necessary to conclude on the product frame of reference.

Geographic market

13. The parties submitted that while the conditions for operating a care home are broadly similar across the UK, there are some elements of local competition
14. From the demand side it appears that many residents (whether funded by the local authority or self funded) opt for a care home that is close enough to relatives or friends to maintain regular contact. It was accepted in *Blackstone/NHP* that the narrowest possible geographic frame of reference should be a 15-20 minute drive time within a given location. This corresponds to radii of three to ten miles,

depending on the nature of the area (rural or urban).⁵ In addition (and again in line with *Blackstone/NHP*) the merger's impact on competition at a local authority level has also been considered.

15. The parties have argued that self-funding residents may have a wider geographic scope. However, the customer survey conducted as part of a recent OFT market study⁶ ('OFT care home study') suggested that self-funders are even more likely to be influenced by locational factors than publicly funded residents. The OFT therefore does not consider that this case would merit deviating from the geographic frame of reference established in *Blackstone/NHP*.
16. For the purpose of this assessment, the OFT therefore considered i) three-to-ten-mile-radii (corresponding to 15-20 minutes drive time) and ii) overlaps on the basis of local funding authorities.

HORIZONTAL ISSUES

Shares of supply

17. On a national basis, the provision of care home services post-merger remains characterised by very low levels of concentration. The parties' post-merger national shares amount to [0-10] per cent on the basis of the number of beds and [0-10] per cent on the basis of the number of homes and no competition concerns are considered to arise on a national level.
18. On a local basis, there are 22 areas where the parties' joint share of supply exceeds 25 per cent on a radius basis and 27 areas where the parties' joint share of supply exceeds 25 per cent on a local authority basis. Table 1 below contains key areas for which a more in-depth assessment was carried out.

⁵ *Blackstone/NHP*, at paragraph 12.

⁶ Care homes for older people in the UK. A market study. May 2005, OFT 780.

Table 1: HHI calculations, potentially problematic areas by share of supply figures⁷

	Type of Care	Fascia numbers	Combines %Share (beds)	% increment (beds)	HHI post-merger	HHI increment
By radius						
The Sycamores/ The Poplars	Nursing	7-6	[45-55]%	[15-25]%	3103	1197
The Sycamores/ The Poplars	EMI	12-11	[35-45]%	[15-25]%	2098	761
Riverside	Nursing	22-21	[30-40]%	[5-15]%	1458	415
Falstone	Nursing	8-7	[35-45]%	[10-20]%	3330	806
Cranford	Nursing	8-7	[30-40]%	[10-20]%	2312	403
Chester House	EMI	12-11	[50-60]%	[5-15]%	3515	900
Wickwar	Nursing	5-4	[40-50]%	[10-20]%	3566	660
Barnes Court	Nursing	10-9	[35-45]%	[15-25]%	2816	719
By LA						
Bridgend	Nursing	6-5	[45-55]%	[10-20]%	3224	972
Nottingham City	EMI	9-8	[30-40]%	[10-20]%	2245	646
Tameside	Nursing	12-11	[25-35]%	[10-20]%	1653	508
Salford	Nursing	14-13	[25-35]%	[5-15]%	1379	376
Sunderland	Nursing	14-13	[30-40]%	[10-20]%	2262	640
Caerphilly	Nursing	10-9	[45-55]%	[10-20]%	2589	887
Southwark	Nursing	8-7	[40-50]%	[15-25]%	2812	886
South Tyneside	Nursing	7-6	[30-40]%	[10-20]%	2413	563

19. While these areas also show high post-merger HHIs and HHI increments⁸, it should be noted that these shares of supply relate to capacity. Capacity allocation was carried out assuming that *all* beds in a care home offering nursing were allocated to nursing care. However, insofar as some beds in nursing and residential homes are currently allocated to residential care (and similarly only some beds in nursing homes are devoted to EMI care), the ability of the larger providers to exert market power may already be constrained by competitors' ability to switch capacity from residential to nursing care and from non-EMI to EMI care. Competitors could therefore relatively easily make additional capacity for nursing care available.

20. With regard to self-funders, a survey conducted as part of the OFT care home study found that 88 per cent of residents looked at four homes or less before making their choice. It is noted that according to the data in Table 1 above, the number of care home operators ('fascia') in an area will remain significantly above that number in almost all areas.

⁷ Please note that figures may not always add up due to rounding.

⁸ OFT, Mergers Substantive Assessment Guidance, at paragraph 4.3.

Barriers to entry and expansion

21. The key entry requirements are a suitable property and the need to obtain registration from the relevant authorities. In some of the areas listed in Table 1 above, e.g. Southwark, Nottingham City and possibly Salford, the cost of land may be higher than average. However, none of the local funding authorities in these areas considered entry to be difficult.
22. With regard to the registration requirements, the parties have submitted that while the Department of Health's National Minimum Standards of Care need to be met, new care homes are currently being developed, especially by the main national chains. SX submitted that it has [] new developments planned for 2006, which will be built by third parties. The parties have also given examples of entry by other providers, in particular entry sponsored by local funding authorities. National competitors, such as BUPA, Four Seasons, Barchester and Craegmore, have said that they are in a stage of developing (building and refurbishing) more homes.
23. In addition, it should be noted that the national minimum standards applicable in this area are not retrospective in that a residential care home seeking to re-register as a nursing care home would not have to meet certain specifications to the premises of the home which would be required of a new build and which might otherwise have resulted in substantial additional costs.
24. It appears that many care homes dedicated as 'nursing care homes' currently also offer places to residential customers in order to maximise the use of existing capacity. However, this capacity that is currently used for residential care could easily be re-allocated and used for nursing care when becoming available.⁹ This is in addition to the [] per cent overall spare capacity that SX homes in the areas in Table 1 are operating on.
25. As regards the supply of nursing staff in the UK, none of the third parties indicated that this would be a problem. The parties have suggested that there may be a trend towards migrant workers in the nursing profession.
26. On the basis of the above evidence, the OFT considers that new entry (or expansion), most likely from established care home groups and often sponsored by local funding authorities, would provide a sufficient competitive constraint in the areas listed above in Table 1.

⁹ [].

Buyer power

27. Local funding authorities pay around two thirds of all care fees, which suggests that they hold some negotiation strength. However, their buyer power might be restricted by their legal obligation to find a place in a care home for people who meet their published criteria. Moreover, health authorities can impose financial penalties on local funding authorities that fail to move people from hospitals into care homes within a specified time period.
28. However, the OFT considers that the available evidence demonstrates that local funding authorities use their buyer power effectively. Third party evidence suggests that budgetary constraints sometimes result in cuts in demand until existing capacity is freed up. Moreover, the parties have provided documentary evidence to demonstrate that many local funding authorities only engage in limited negotiations with care home providers, and instead apply uniform charges.
29. In addition, funding authorities have the option of self-supply and in some of the high-concentration overlap areas, such as Nottingham City and Sunderland, local funding authorities run their own homes. A number of local funding authorities submitted that they have in the past promoted entry through the use of block contracts.

VERTICAL ISSUES

30. Cannon's share of consumables used by care homes is less than 15 per cent. Third parties did not raise any vertical concerns. No vertical competition issues are therefore considered to be raised by this transaction.

THIRD PARTY VIEWS

31. Third parties were in general unconcerned by the merger. Some residents groups, competitors and local funding authorities felt that the merger represented a trend of consolidation towards larger care home groups, which would eventually reduce customer choice. In general, however, this particular merger was not seen to tip the balance, or to itself raise competition concerns.

ASSESSMENT

32. The parties overlap in the local supply of nursing care home services (of which EMI and dementia care may be distinct elements) and residential care home services.
33. On the narrowest possible frame of reference, of nursing/EMI care separately, post-merger HHIs and HHI increments are substantial in some local areas. However, for

the purpose of this assessment it is considered that barriers to entry and expansion are sufficiently low for new entry to constrain the parties post-merger. There is evidence that national care home providers are currently developing new care homes and also evidence of sponsored entry by local funding authorities as well as self-supply by Local Authorities. Moreover, it would be possible to re-allocate capacity within homes designated as nursing homes that was being used to provide residential care back to providing nursing care. Also, homes currently providing residential care could relatively easily re-register to offer nursing care.

34. There is evidence to suggest that the local funding authorities that finance around two thirds of all care fees will, post-merger, continue to use their resulting buyer power effectively. The budgetary constraints local funding authorities face mean that many apply uniform charges which, first, leaves care homes little room for price increases and, second, appears to result in a policy whereby a new resident is only placed in a home once a place has become available.
35. Third parties were generally unconcerned by the merger.
36. Consequently, the OFT does not believe that it is or may be the case that the merger has resulted or may be expected to result in a substantial lessening of competition within a market or markets in the United Kingdom.

DECISION

37. This merger will therefore **not be referred** to the Competition Commission under section 22(1) of the Act.