

Completed acquisition by IDEXX Laboratories Limited of Vetlab Services Limited

The OFT's decision on reference under section 22 given on 23 November 2005. Full text of decision published 7 December 2005.

Square brackets indicate information replaced by a range at the parties' request.

PARTIES

1. **IDEXX Laboratories Limited (IDEXX)** is active in the sale of diagnostic testing solutions for the detection of diseases and conditions in animals, including in-hospital testing and outside of hospital reference laboratory services (referred to as 'reference laboratory services'). It provides these solutions for use by animal veterinarians on companion animals (dogs, cats and horses) and for use by animal health laboratories on production animals (such as cattle, swine and poultry). IDEXX also provides tests for the dairy and water sectors. In addition, IDEXX produces and sells digital radiography instruments, telemedicine services and diagnostic instrument maintenance to companion animal veterinarians in the UK.
2. **Vetlab Services Limited (Vetlab)** provides reference laboratory services for use by animal veterinarians on companion animals from its reference laboratory. It is not active in in-hospital testing. Vetlab's turnover for the year ended on 31 December 2004 was approximately £1.7 million.

TRANSACTION

3. On 29 July 2005 IDEXX acquired the veterinary diagnostic testing business of Vetlab Services Limited.
4. The OFT administrative timetable expires on 23 November 2005 and the statutory deadline for referral of the merger is 28 November 2005.

JURISDICTION

5. As a result of this transaction IDEXX and Vetlab have ceased to be distinct enterprises. The parties overlap in the supply of companion animal diagnostic testing services in the UK with a share of supply in reference laboratory services in this sector estimated at approximately [30-50] per cent. While the parties question this figure, the OFT takes the considered view, which is supported by the majority of third party comments on this issue, that it may be the case that the share of supply test in section 23 of the Enterprise Act 2002 (the Act) is met. The OFT therefore believes that it may be the case that a relevant merger situation has been created.

RELEVANT MARKET

Product market

6. The parties overlap in the supply of companion animal diagnostic testing services in the UK. Their customers are generally veterinary surgeries and hospitals (referred to as veterinary hospitals in this Decision) that provide healthcare for household pets. The provision of such services is split within the following segments:

- (i) the supply of instruments and test kits to veterinary hospitals for in-hospital testing; and
- (ii) (ii) the provision of reference laboratory services (or external testing).

While IDEXX is active in (i) and (ii), Vetlab is active only in (ii). The parties therefore only overlap in the supply of reference laboratory services for companion animals.

7. There is a large range of tests for evaluation of different health parameters and diagnosis of many different companion animal diseases. For the more basic and common tests, companion animal hospitals will have the choice of carrying out the tests in-house (using either in-house equipment or single-use kits) or sending the sample out to a reference laboratory. IDEXX provides instruments and kits to carry out a wide range of tests in-hospital.
8. All tests carried out in-hospital can also be carried out at a reference laboratory. In addition, reference laboratories also carry out more complicated tests that cannot be done in-hospital. These additional services generally require a specialist veterinary pathologist. Therefore, while there is demand-side substitutability between in-hospital and reference laboratory testing, there are certain tests which can only be carried out by reference laboratories and some occasions where it is

preferable for tests to be carried out at reference laboratories rather than in-hospital.

9. Third parties have submitted that while in-house test results can be obtained faster, reference laboratories generally provide more accurate and reliable information. When choosing whether to use in-hospital or reference laboratory testing, a trade-off therefore exists between the speed and the accuracy of the test results. However, reference laboratories can provide a next-day and sometimes same-day service. Moreover, veterinarians will sometimes carry out an in-hospital test for an immediate result while simultaneously sending a sample to a reference laboratory for a more detailed analysis and/or for confirmation of the results obtained in-hospital.
10. Given that in-hospital testing cannot be substituted for all laboratory tests, it could be argued that the appropriate product scope might, therefore, be as narrow as companion animal testing at reference laboratories.
11. It could be suggested that the appropriate product market might be narrower still, depending on the nature of testing services provided. However, third party responses have indicated that the product scope should not be narrowed to only those laboratories that provide a full range of tests since such a service can be obtained by using a number of different laboratories. All veterinarians that responded submitted that they currently use more than one laboratory for their diagnostic testing needs. Additionally, third parties did not consider that the product scope should be narrowed to particular types of test.
12. While there is some indication that the relevant frame of reference is reference laboratory services, it has for the assessment of this transaction not been necessary to conclude on this matter because, as outlined below, a realistic prospect of a significant lessening of competition is not raised on the basis of either reference laboratory services or companion animal diagnostic testing services in general.

Geographic market

13. The parties submitted that the relevant geographic frame of reference would be the UK. While there is some evidence that veterinarians use reference laboratories outside the UK to a limited degree, this tends to be for specialized services. Some third parties mentioned the German lab Vet Med Labor as an example of an independent overseas reference laboratory that provided services to the UK market until it was recently acquired by IDEXX. As no competition concerns arise on a UK basis, it has not been necessary to conclude on the issue of whether

overseas suppliers provide a constraint.

HORIZONTAL ISSUES

Shares of supply

14. The OFT has received varied calculations and estimates for shares of supply from IDEXX and third parties. In the absence of any publicly available data for total supply or individual shares, it has not been possible to verify this information from independent sources.
15. The parties estimated their combined share of total supply of companion animal diagnostic testing, which includes both the supply of instruments and test kits to veterinary hospitals for in-hospital testing and the provision of outside reference laboratory services to be [20-30] per cent with an increment of [less than 5] per cent and their combined share of testing in reference laboratories to be [10-20] per cent with an increment of [less than 5] per cent. These calculations differ markedly from information received from the majority of competitors, who estimated the parties' combined share of supply of reference laboratory services for companion animals at approximately [30-50] per cent with an increment of between 10 and 20 per cent. (As noted at paragraph 5 the OFT has taken the view that the share of supply test may be met in respect of this transaction).

Non-coordinated effects

16. Responses received from veterinary hospitals indicate that customers had no competition concerns and considered several other players as viable alternatives should the merged entity's prices rise as a result of the merger. Named alternatives include Axiom and NWL who offer a full service (or 'one stop shop') covering the full range of laboratory disciplines for which testing is required (the type of service which IDEXX and Vetlab offer), and a number of companies such as Abbey Veterinary Services, BioBest and Greendale Vet Diagnostics which have a more limited range of tests on offer. Customers also commented that they could relatively easily switch suppliers of reference laboratory services. Moreover, they believed that larger laboratories offer a type of service that could be substituted with a combination of laboratory services from several other laboratories.

Barriers to entry and expansion

17. Third parties have given a number of examples of recent entrants in this sector, in particular CTDS, BattLabs, Cytopath and CSL. As mentioned above, Vet Met Labor is an example of a recent overseas entrant (albeit later acquired by IDEXX). Third parties did however mention a shortage of qualified veterinary pathologists

as the main barrier to entry in this sector, but some also submitted that veterinary pathologists could leave their employer to start up their own laboratory and so offering another route of potential entry. Furthermore, customers mentioned that veterinary schools currently offer a specialist commercial service and that this service also has the potential for expansion suggesting entry is possible using already existing expertise in the sector.

18. The parties have submitted that the capital cost of entry and expansion into the laboratory testing sector is relatively low. The main cost is the cost of specialised laboratory testing equipment. This ranges from £25,000 to £120,000 depending on the service provided. One competitor estimated the cost of employing a veterinary pathologist at approximately £40,000 per annum.

Buyer power

19. While a small number of larger veterinary groups tend to negotiate yearly contracts with laboratories, only one customer respondent submitted that they carried out a formal tendering process. Most veterinary practices appear to be too small to exert any influence on laboratories' prices, and it would appear, therefore, that there is no significant buying power in any of the markets under consideration.

VERTICAL ISSUES

20. No vertical competition issues arise as a result of this transaction.

THIRD PARTY VIEWS

21. While none of the veterinary hospitals contacted raised any concerns about this transaction, competitors claimed that post-merger the parties might be able to price smaller laboratories out of the market and so lead to a reduction in choice in the sector. It was suggested that the parties could potentially offer a 'one-stop-shop' service at lower prices than if the individual components such as haematology or cytology were purchased separately. Respondents were unable to provide evidence to substantiate these claims, which, if correct, suggest that rivals fear greater competition from a more efficient competitor.
22. In any event, responses from veterinarians contacted indicated that they did not share the competitor's concerns. They did not believe there to be a separate segment for 'one-stop-shop' services but instead submitted that the full range of services could be provided by using a combination of several laboratories to provide the range of services required. Customers also submitted that, even if the

parties were able to offer lower prices, other smaller laboratories could still compete on service quality.

23. Some competitors raised concerns about the parties' post-merger ability to use its power in in-house testing instruments to leverage their position into laboratory services. It was submitted that the parties might offer in-house testing instruments at a lower price when purchased together with reference laboratory services. However, IDEXX's potential to engage in such practices has not been affected by the merger: even assuming IDEXX has market power, in in-house testing, this acquisition does not increase it. Nor is there evidence to suggest that IDEXX was engaging in anti-competitive bundling of these products and services pre-merger, although competitors allege it already had a substantial (30-40 per cent) pre-merger share of reference laboratory services.

ASSESSMENT

24. The parties overlap in the supply of reference laboratory services for companion animal diagnostic testing. Notwithstanding the variations in share of supply estimates, the parties are regarded by many in the sector as two of the main providers of reference laboratory services. The OFT's investigation has, however, revealed that several other players will remain in this sector post-merger and customers have confirmed that they will remain able to switch between laboratories where necessary.
25. While competitors raised some concerns about this transaction, it appears on closer examination that these concerns relate to the increased competitive threat posed by the parties rather than to any substantial lessening of competition that might be expected to result from the merger.
26. 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

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