

[NON-CONFIDENTIAL VERSION]

**COMPETITION AND MARKETS AUTHORITY INVESTIGATION
UNDER THE ENTERPRISE ACT 2002 (PART 3)**

**OF THE PROPOSED ACQUISITION
BY OMNICELL, INC./MTS MEDICATION TECHNOLOGIES, INC.
OF SURGICHEM LIMITED**

SUBMISSION

TO THE COMPETITION AND MARKETS AUTHORITY

BY OMNICELL, INC. AND MTS MEDICATION TECHNOLOGIES, INC.

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BY OMNICELL, INC. AND MTS MEDICATION TECHNOLOGIES, INC.
PROPOSED ACQUISITION BY OMNICELL, INC. OF SURGICHEM LIMITED

Please note:

In this submission, references to the OFT's Decision are to the OFT's Decision of 14 March 2014 referring the proposed acquisition by Omnicell, Inc. of Surgichem Limited to the Competition Commission, now the Competition and Markets Authority.

1. OVERVIEW

This paper sets out the initial submissions of Omnicell, Inc. and MTS Medication Technologies, Inc. to the Competition and Markets Authority concerning Omnicell's planned acquisition of Surgichem Limited. These submissions are structured on the lines requested in the Competition Commission's letter of 14th March 2014.

Accordingly, this paper will cover the following: the background concerning Omnicell (section 2), information on the present transaction (section 3), the relevant markets and the overlaps between the parties' supplies (section 4), barriers to entry (section 5), the counterfactual (section 6), and the competitive effects of the merger (section 7). This paper will also explain the efficiencies and other benefits resulting from the planned merger (section 8) and will set out the parties' conclusions (section 9).

These submissions will explain that there are no competition concerns arising from the planned merger except in relation to supplies of adherence packaging products to pharmacies. It will be explained that in relation to supplies of adherence packaging to large pharmacy chains by tender, there will be no loss of competition because Surgichem is not currently a supplier in relation to this sector of the market and because it is not likely to enter this sector because it does not have a card-based adherence packaging product, and a prototype developed for it has been shown to be not economically viable to supply at the price levels typically required to win such tenders. No large pharmacy chains raised any concerns to the OFT with regard to the merger.

In relation to supplies to other pharmacies not purchasing by tender, there will be no significant loss of competition because there are various alternative suppliers and various potential competitors all of which will constrain any market power of the merged entity to raise prices, and because there are no significant barriers to entry or expansion in markets for adherence packaging products. Further, most pharmacies which are not part of a large pharmacy chain are members of a buying group (and those which are not already, could become members). Buying groups provide protection against price rises and indeed secure favourable prices for their member pharmacies from an appointed supplier. Moreover, buying group prices become known in the market and provide a benchmark for individual price negotiations by pharmacies.

Omnicell's mission is to introduce innovative solutions for medication management and administration, for the benefit of patients, by introducing monitoring and analytics to improve medication adherence in primary healthcare settings, in particular in the

domiciliary and care home sectors, building on its innovative analytic and monitoring solutions provided in hospital and acute settings in the USA. The acquisition of Surgichem will enable an accelerated introduction of such solutions, because the acquisition will allow the critical mass and in particular a larger revenue base from which to fund the required investments in such innovations.

The parties believe that any concerns regarding loss of competition as a result of the proposed merger, are unfounded. This submission will explain why the planned merger will not result in any substantial lessening of competition ("SLC").

2. BACKGROUND ON OMNICELL

Omnicell, Inc will, through its wholly-owned subsidiary, MTS Medication Technologies, Inc., purchase the entire issued share capital of Surgichem Limited from BUPA Care Homes (CFG) plc. Omnicell is a NASDAQ listed provider of medication and supply management systems. The Omnicell group is active, through subsidiaries, in the UK, France, Germany, Australia, Hong Kong, China and The United Arab Emirates, in addition to the USA. An organisational chart of the Omnicell group was provided at tab 8 of the information submitted to the CMA on 21 March 2014.

A copy of the form 10-K for Omnicell, Inc, which includes its annual accounts, was provided at tab 20 of the information submitted on behalf of Omnicell on 21 March. Omnicell's total revenue for 2013 was \$381 million.

Omnicell purchased MedPak Holdings, Inc in May 2012. MedPak is the parent company of MTS Medication Technologies, Inc., an international provider of adherence packaging, adherence support products for patients/carers and technological solutions that support the dispensing process in pharmacies.

MTS Medication Technologies, Inc. operates in the UK through its subsidiary MTS Medication Technologies Limited ("MTS"). MTS has approximately [X] key staff in the UK with facilities in Leeds comprising warehouse space of approximately [X] square feet and office space of approximately [X] square feet. MTS's adherence packaging is manufactured by MTS Medication Technologies, Inc. in facilities in the USA. MTS's total sales for the financial year ended 31 March 2013 was approximately £6.9 million. In the calendar year 2013, MTS's sales in the UK were approximately £[X], including sales of adherence packaging in the UK of approximately £[X]. MTS also sells semi-automated filling machines (for filling its packaging), deblistering machines (for extracting oral medications from the manufacturer's packaging) and heat-sealing machines (for sealing its adherence packaging) and also a range of adherence support products (including medication of administration record sheets, trolleys, dividers, hangers and other products), but the sales of all of these products are relatively low. Specific sales figures for the calendar year 2013 (and for the previous calendar years 2010 to 2012) are set out at tab 11 of the information submitted to the CMA on 21 March 2014.

Omnicell provides medication and supply management solutions to healthcare providers including hospitals and acute care providers in the USA, focusing on improvements to patient safety in hospitals by ensuring that the correct medications are given to the appropriate patients by the appropriate clinician at the correct doses and at the correct times Through MTS Medication Technologies, Inc. and its subsidiaries, Omnicell has extended such medication management solutions across the continuum of care, providing the same benefits of ensuring correct medication administration, in care homes and in domiciliary (community) settings.

Omnicell has introduced an innovative electronic solutions platform, Pandora Analytics, which allows hospitals and acute care providers in the USA to optimise medications inventories and ensure correct medication administration. [REDACTED] through the [REDACTED]. Omnicell's mission is to introduce such innovative solutions for the benefit of patients, by [REDACTED]. The acquisition of Surgichem will enable an accelerated introduction of such solutions, including [REDACTED] because the acquisition will allow the critical mass and in particular a larger revenue base from which to fund the required investments in such innovative solutions. This is explained further in section 8.1 below.

Omnicell's plans following completion of the acquisition of Surgichem include the [REDACTED]. This would further enhance the efficiency of its operations, with the possibility (subject to raw material price increases) of cost reductions for products [REDACTED]. This is explained further in section 8.2 below and in the relevant Appendix.

3. INFORMATION ABOUT THE TRANSACTION

The vendor is Bupa Care Homes (CFG) Plc (company no. 01969735) of Bridge House, Outwood Lane, Horsforth, Leeds LS18 4UP. Bupa is selling the entire issued share capital of its Surgichem Limited ("Surgichem"). The consideration is £12,000,000 subject to certain adjustments.

The purchaser is MTS Medication Technologies, Inc. of 2003 Gandy Blvd. North, St Petersburg, FL 33702, USA. It is a subsidiary of Omnicell, Inc. ("Omnicell") of 590 E. Middlefield Road, Mountain View, CA 94043-4008, USA [REDACTED].

[REDACTED]

In addition, it should be noted that Surgichem's parent company BUPA has elected to sell Surgichem as adherence packaging is not core to its strategy. The merged entity will be better placed to consider capital investments to meet the evolving expectations of the market and to benefit pharmacies and ultimately carers and patients.

The parties signed Heads of Terms on 23 September 2013 (as attached at Appendix 1 to this submission) and an electronic data room (the "Data Room") containing both commercial and financial information was opened on the same day. Access to the Data Room was controlled by BUPA's solicitors and users were required to acknowledge a statement when logging-in that they were deemed to have agreed with the data room rules. The Data Room remained open until 6 December 2013 when access was terminated. The Share Purchase Agreement ("SPA") for the sale and purchase of Surgichem was then signed on 6 December 2013. Information provided in the Data Room which the vendor disclosed against the warranties was provided to the purchaser on exchange of contracts.

A copy of the SPA, as signed on 6 December 2013, was provided in Omnicell's response to the Competition Commission's request for initial information, submitted on 21 March 2014, at tab 1. Completion is subject to conditions precedent in the SPA to ensure that the merger is cleared under the Enterprise Act 2002, as explained below. Completion will take place once the merger clearance conditions precedent are satisfied. The transaction was announced on 9 December 2013. Omnicell's press release of 9 December 2013 was provided in response to the CMA's initial request for information, submitted on 21 March 2014, at tab 5.

Completion will take place once the merger control condition precedent is satisfied. This provides, so far as relevant following the referral of the merger by the OFT to the Competition Commission, that completion is subject to one of the following being satisfied:

- i. Clearance by the CMA following the reference from the OFT; or
- ii. Acceptance, at Omnicell's discretion, of undertakings that remedy or prevent any lessening of competition identified by the CMA.

4. RELEVANT MARKETS

4.1 Product categories

MTS submits that there are three product categories relevant to the merging parties' business activities albeit that, for the reasons that follow, it is only adherence packaging that should be of relevance to the CMA's investigation. The OFT concluded in its Decision that no competition concerns arise in relation to other products.¹ The product categories are as follows:

- Adherence packaging (**market 1**) - to the extent that there is a market of adherence packaging products it would include both the packaging itself and the associated components necessary to enable pharmacies to fill and use the adherence packaging. It includes both card and plastic products, and disposable and reusable products. It includes cards, blisters, plastic pill dispensers, automatic dispensers (such as the Pivotell product which is a cassette with 28 slots that automatically rotates and indicates when medicines are to be taken), plastic trays, pouches, pods and other medical compliance aids as well as label flaps, repair patches, rollers, templates and paddles.
- Dispensing support for pharmacies (**market 2**) - MTS supplies dispensing support for pharmacies. This market covers all technological solutions that support the dispensing process in the pharmacy including automation, de-blistering and sealing equipment. Surgichem does not currently provide any products or services in Market 2 although it is developing a filling and heat sealing machine.
- Adherence support products for patients / carers (**market 3**) – this includes all products that support patients and carers in medication adherence. These include SMS/mobile/web applications, [⌘], patient reminders, labels, packaging dexterity aids, storage bags, dividers, hangers, sleeves, pill cutters and crushers, MAR sheets /folders and software (including e-MAR and consolidated label software) and also trolleys, cabinets and fridges. This list is not however exhaustive but describes the main product areas currently available in the UK market. Generally, customers (pharmacies) decide separately on the purchasing of adherence packaging products and adherence support products for patients and carers. However, each of MTS and Surgichem generally (although with individual exceptions) supply adherence support products only to customers purchasing the company's adherence packaging products and not normally separately.

4.1.1 Market 1 - Adherence Packaging

Adherence packaging comes in two forms, 'single dose' and 'multi-dose'. Single dose contains one type of medication only to be taken by the patient at the relevant time whereas for multi-dose the packaging will contain multiple medications to be taken at the same time. Pharmacies supply those domiciliary patients who use adherence packaging with multi-dose packaging. There are still a significant number of domiciliary patients who continue to receive their medications in the original manufacturers' packaging i.e. who do not use

¹ Paragraphs 35 and 37.

adherence packaging. A number of such patients would benefit from using adherence packaging. Pharmacies mainly use single-dose packaging for supplies to care homes although multi-dose packing is also used. For instance Surgichem supplies multi-dose packaging to care homes (namely their *Nomad MDS* product). Protomed's *Biodose* product (which can be used for solid and liquid medicines and is used in care homes) is also multi dose.

Adherence packaging typically takes the form of a single-use adherence pack. Adherence packs are either card or plastic based. There is little functional difference between plastic and card based adherence packs. MTS supplies card based adherence packs whereas Surgichem supplies plastic based adherence packs; in essence they are undifferentiated. Surgichem has however obtained a prototype for a card based adherence pack that will be manufactured in China. This prototype has not been further developed and is not supplied to the market. However, HD Medi, for instance, provide a different product which is referred to as blister pouch adherence packaging (unlike a blister pack the pouch is small bag). Further, for supply to care homes, Manrex supplies a re-usable plastic frame that holds a disposable plastic blister pack and is sealed with foil.

Surgichem has also established a product known as *Nomad Multimed*s. Promotion of these products started in April 2013 and Surgichem is so far supplying it to [§<]. Currently it is only used for solid medications. It is a multi-dose product predominately used in care homes. Surgichem considers that the product could be developed for use with liquid medications however it has not yet started to develop the product to do so. MTS does not supply packaging for liquid medications. Rather than constituting a separate segment of the market, adherence packaging for liquid medications is, in MTS's view, an additional feature of a relevant supplier's adherence packaging for solid oral medications. Such packaging is only used in care homes and volumes used are small compared to the overall volumes of adherence packaging. All patients who use adherence packaging for liquid medications are likely to also use adherence packaging for solid oral medications.

As noted above, adherence packaging comes in two forms, 'single dose' and 'multi-dose'. Single dose packaging contains one type of medication only to be taken by the patient at the relevant time whereas for multi-dose the packaging will contain multiple medications to be taken at the same time. MTS submits that single dose and multi-dose packaging form part of the same market for at least the following reasons:

- Although pharmacies mainly use single-dose packaging for supplies to care homes, multi-dose packing is also used. For instance Surgichem supply multi-dose packaging to care homes (namely their *Nomad MDS* product) and Protomed's *Biodose* product (which can be used for solid and liquid medicines and is used in care homes) is also multi dose;
- There is, generally, substitutability of supply between multi-dose and single dose adherence packaging;
- There are no significant barriers to switching between supplying single dose packaging and multi-dose packaging and most suppliers provide both single dose and multi-dose packaging; and
- Most pharmacies use both single dose and multi-dose packaging.

Note that whilst the separate customer group (explained below) concerns supplies for domiciliary patients only, who are supplied with multi-dose adherence packaging, this does not mean that such packaging forms a separate market to single dose packaging.

As noted above, the market for adherence packaging includes the associated components necessary to make the adherence packaging. In this regard, adherence packaging packs are either heat-sealed or pressure sealed. The majority of suppliers use pressure sealing. Pressure-sealing allows pharmacies to provide a community service with little outlay or expense. Heat-sealing is ideal for pharmacies who plan to make a large number of adherence packs as use of the heat-seal packs saves time and expense. Heat sealing can be used for both plastic based and card based adherence packaging. For example Protomed's *Biodose* plastic-based product is heat-sealed. For heat-sealing a heat- sealing machine is required. Details of MTS's heat sealing machines are set out in section 4.1.2 below. It is particularly easy for pharmacies to switch between suppliers of different pressure-sealed adherence packaging products as no heat- sealing machine is required, however even switching to heat-sealing products is relatively straightforward.

The vast majority of adherence packaging sold by MTS are pressure sealed. All of Surgichem's adherence packaging packs are pressure sealed as are those of the competitors Shantys and Dosebliss, whilst Venalink uses both heat and pressure seal. Recent trends suggest that the market is moving towards pressure seal. Rollers and platens are needed to pressure seal the adherence packaging packs. Whilst the rollers are fairly standard across suppliers the platens are bespoke to the type of adherence packaging being used. Different shaped platens are needed for the different types of adherence packaging packs. Without the correct shaped platen the adherence packaging pack will not seal properly. In order to prepare MTS pressure seal adherence packs the pharmacy would require: the MTS Easyblister cards; the blisters; the filling template (platens); and a roller. Platens need to be replaced fairly regularly whilst rollers can last a number of years. For pressure seal adherence packaging (for which a roller is used) MTS will typically supply the customer with the platens [X] when it supplies the adherence packaging.

As noted above, in order to prepare heat seal adherence packs the pharmacy will need heat seal paddles or platens and a heat sealing machine. Generally heat sealing machines are purchased for use with the same suppliers' packaging. As is explained further below it is however technically possible for a pharmacy for instance to purchase an MTS heat sealing machine and then to use it to seal blister packs from other suppliers. To do so the pharmacy would however need to purchase the platen from the supplier of the blister pack as the platen must match the blister pack supplied. As is evidenced below, MTS [X].

4.1.2 Market 2 - dispensing support for pharmacies

Dispensing support for pharmacists covers all technological solutions that support the dispensing process in the pharmacy including automation, de-blistering and sealing equipment. MTS supplies a number of products in this market whereas Surgichem currently does not. Surgichem is however developing a filling and heat sealing machine. The CMA will however note in this regard the OFT's conclusion that there is no realistic prospect of a substantial lessening of competition in the supply of adherence packaging machines.²

The three types of machine that MTS supplies are as follows: heat sealing machines; filling machines; and de-blistering machines.

MTS UK product list:

² Paragraph 35 of the Decision.

Product	Description	Speed of machine	List price
Heat sealing machinery			
MTS Easy Seal Auto	A compact all electric heat sealer which can be used for monthly or weekly pill packs with the largest size blister.	Approximately [X] seconds to seal each card. Exact time is dependent on the machine.	[X]
MTS Easy Seal	A compact heat sealer.		[X]
Filling and sealing machine - single dose cards			
MTS 350	A semi-automated machine that fills medium to large volumes of the same drug into monthly care packs. Sealing is by way of heat seal.	Between [X] unit dose cards per minute.	[X]
Filling machine - multi-dose cards			
On demand multi-med (OD 400)	A semi-automated packaging system for multi-dose, patient friendly packs. This uses heat-sealing.	[X] patient cards per week (dependent on hours operated). [X] multi-dose cards per hour.	[X]
De-blistering machine			
BD500 de-blistering machine	De-blisters [X] tablets per minute.	[X] tablets / capsules per minute.	[X]

Heat sealing machines

MTS supplies two heat sealing machines: the MTS Easy Seal Auto; and the MTS Easy Seal. Heat sealing is used only in relation to [X] proportion of MTS's sales of adherence packaging. In 2013, [X] MTS customers purchased only heat seal cards and [X] customers purchased both heat and pressure seal cards. For those customers which purchased both heat and pressure seal cards the sales of pressure sealed cards far outweighed those of heat seal cards. [X] pressure seal cards were sold to such customers as compared with [X] heat seal cards. Overall last year MTS sold [X] heat seal cards.

As noted above, it is technically possible to use one manufacturer's heat sealing machine with another manufacturer's adherence packaging. Where this is done the only switching cost is the purchase of a new platen as these are bespoke to each supplier's adherence packaging. The cost of a new platen is low, at around £15-20. There are also no contractual restraints in relation to the use of the heat sealer. For instance MTS does not contractually require that only MTS consumables are used with the MTS heat sealing machines.

Other suppliers provide heat sealing equipment. However, demand is moving away from heat-sealing processes and equipment to pressure sealing equipment.

Taking into account all the factors explained above, the use of heat sealing machines does not in any way limit a pharmacy customer's options for adherence packaging or choice of adherence packaging supplier. The vast majority of adherence packaging cards supplied by MTS are sealed using pressure sealing, for which no machinery is required, and not heat sealing; [X] cards supplied annually by MTS are used for heat sealing in comparison to total cards supplied by MTS of over [X] in 2012 and over [X] in 2013 in the UK. Further, MTS's revenue from the sale of heat sealing equipment represents less than [X] of its turnover in the UK. [X]. Further, [X], and the machines can be, and MTS believes are, used in this way.

Filling machines

Automated filling and packaging is mainly used by the large pharmacy chains. For instance, Lloyds Pharmacy uses automation equipment for supplies to domiciliary patients whilst Boots uses automation equipment for supply to care homes but not domiciliary customers. For supplies to care homes, Boots fill their blister cards (supplied by Manrex) on an industrial scale using machines supplied by Illseemann. Such machines are similar to those used for packaging on an industrial scale in the pharmaceutical sector. Boots fill the cards at a central location before delivering them to dispensing hubs and then onwards to care homes.

MTS supplies two filling machines in the UK: the MTS 350 machine which is used for single dose adherence packaging used in care homes; and the On-demand Multi-med 400 which is used for filling and sealing multi-dose adherence packaging used in the community. Sales volumes of these machines [X].

[X]. The volume of consumables (adherence packaging) sold to customers of these machines (which may include consumables not used with these machines) in comparison with MTS's overall sales of consumables is [X] amounting to only [X] of overall sales in 2013. As the table below illustrates sales of adherence packaging to MTS 350 customers as a % of total MTS sales of adherence packaging have remained [X] throughout the last five years.

Sales of adherence packaging to MTS 350 customers as a % of total MTS sales of adherence packaging

Year	2009	2010	2011	2012	2013	Total
Percentage	[X]	[X]	[X]	[X]	[X]	[X]

The OD 400 machine is only compatible with MTS consumables. In addition, the cards used in these machines are adapted for heat sealing and include a barcode which is used to for audit purposes. Customers that purchase an MTS filling machine will [X] typically use the machine for servicing a [X] percentage of their customers and will use adherence packaging manually for the rest of their customers. Therefore to the extent that such customers are tied to using MTS consumables when using the MTS filling machine this does not permit MTS to raise prices because the customer would typically use other suppliers' adherence packaging manually, reducing their usage of MTS's filling equipment, in response to such a price increase. For instance [X] have purchased four OD 400 filling machines from MTS, but those machines are only used in relation to about [X]% of [X] requirements for its multi-

dose business. In 2013 MTS provided [X] with [X] cards for use with the On-demand 400 machine compared with [X] non-machine cards for the same period. In the [X] supply contract MTS was contractually committed to supply consumables at a specified price for a specified period (the return on investment period).

Surgichem does not currently sell these types of dispensing support products. All of its adherence packaging is pressure sealed which does not require machinery. However, as noted above Surgichem has developed a pharmacy heat sealing and filling machine. The prototype of the machine is currently with the manufacturer and developing and testing was completed in September 2012. Surgichem estimate that the cost of manufacture of this machine is approximately [X] and the next stage of the process will be to pilot the machine with a customer. [X] As automation is at an early stage of evolution, it is likely that Surgichem will work with other organisations in order to bring this machine to market. [X]

For the reasons given above, the use of MTS's automated filling machines does not in any way limit or constrain the pharmacy customer's adherence packaging operations or their choice of adherence packaging supplier. [X] In any event, as regards both the multi-dose filling and single dose filling (for which MTS's relevant equipment is the 350 machine), the vast majority of filling is conducted by pharmacies manually. [X] units in total of the multi dose (OD400) machine are in use in the market, [X] of which are owned by [X], but [X] use of these machines accounts for approximately [X]% of [X] adherence packaging, the rest being carried out manually. As regards the single dose filling machines, the 350 machines, [X] have been supplied, [X]. Therefore if a pharmacy customer were dissatisfied with the terms or basis of use of either type of filling machine, it could simply reduce its use of the machine and increase its manual filling and packaging.

Moreover the supplies of MTS's multi-dose and single dose machines respectively each account for less than [X] of MTS's total turnover in the UK. Accordingly the actual usage of the filling machines is [X] effect on pharmacies' choice of adherence packaging supplies. Moreover, such machines are mostly supplied to large pharmacy chains which, the OFT noted in its Decision, did not raise concerns about the proposed merger.³

De-blistering machines

The de-blistering machine removes solid oral medications from the original manufacturer's packaging. A pharmacy could use any manufacturer's de-blistering machine irrespective of the choice of supplier of adherence packaging.

4.1.3 Market 3: Adherence support products

MTS and Surgichem provide a range of products that support patients and carers in medication adherence. The OFT however had no concerns in relation to the supply of such products in the UK.⁴

It is not possible for the parties to assess the market separately by reference to the additional products provided as part of adherence support for patients/carers. The parties have no visibility as to the volume of sales by competitors and as the additional products can be sourced from providers other than the providers of the adherence packaging (for example, Beaucare Medical Ltd and Confrerie Clinique, as set out at Appendix 4) it is very difficult to estimate the overall size of the market and thus the share of supply of the parties. Further, the parties do not sell all of the numerous different products that are within the ancillary

³ See paragraph 98.

⁴ Paragraph 37 of the Decision.

products market. However, the parties generally do not supply such products other than to their customers for adherence packaging, so their respective shares of supplies of such products will be the same as or lower than their shares of supplies of adherence packaging.

4.1.4 Trolleys and cabinets

Both MTS and Surgichem supply medicinal trolleys and cabinets. However, the OFT identified no concerns in relation to the supply of such products in the UK.⁵ Whilst this is a major area of business for Surgichem, it is a negligible area for Omnicell's subsidiary MTS. Surgichem is a leading supplier of trolleys and cabinets and fridges to pharmacies who supply these products to pharmacy customers. Surgichem provides *Nomad* medication cabinets for the safe, secure storage of medication in both the care home and pharmacy environments.

MTS's supplies of trolleys and cabinets are by comparison negligible, amounting to [redacted] for year ended December 2012 and £[redacted] for 2013 as compared with [redacted] (for trolleys, cabinets and fridges) for Surgichem for the same period. Further, MTS only supplies trolleys and cabinets when a specific request is made from a customer, and when it does so the trolleys and cabinets are manufactured by [redacted]. MTS's sales figures for cabinets are even lower than those for trolleys.

Omnicell's distributor Avantec (in which Omnicell has a minority shareholding) does however sell cabinets (but not trolleys) to hospitals in the UK, typically around [redacted], with a value of approximately [redacted] per annum. However, the cabinets supplied by Avantec contain various electronic value-added features with the result that in terms of their price level and characteristics, they can be regarded as not being in the same market as the cabinets supplied by MTS and Surgichem. Those supplied by Avantec are [redacted] times more expensive than those of MTS and Surgichem.

The cabinets and trolleys supplied by each of the parties are similar to the types of products used in hospitals and such products would fall within the same market. Neither MTS nor Surgichem currently supplies these products to hospitals. However, Surgichem is intending to supply products including drugs trolleys, cabinets, medical fridges, infection control products and bins to hospitals. It has sourced most of the products from the Far East and has started to position itself well for instance by obtaining ISO 9001 accreditation. There are a large number of suppliers of such equipment to hospitals and Surgichem believes that competition between suppliers of trolleys and cabinets is fierce. Bristol Maid is a strong competitor and has reduced prices in recent years.

In the Information Memorandum prepared by Deloitte on behalf of BUPA concerning the sale of Surgichem, a copy of which is included at Appendix 2, Surgichem have estimated that they hold a [redacted] share of supply for trolleys to care homes. However, supply to care homes is merely a part of the broader market for supply of such products to the health care sector including hospitals (both private and NHS). On that broader market Surgichem's share of supply would be considerably lower. There are several actual or potential suppliers of trolleys and cabinets. For estimates of Surgichem's share of supply for trolleys, fridges and cabinets, please see [redacted]

⁵ Paragraph 37 of the Decision.

4.2 Overlaps of supplies by the parties

The primary area of overlap between the parties', and that to which MTS submits is of relevance to the CMA's investigation, are supplies in the UK of adherence packaging. However, the overlap is not as significant as may otherwise be the case due to the following factors:

- A separate customer group within the adherence packaging market can be identified by reference to large pharmacy chains which hold formal tenders in order to appoint suppliers of adherence packaging for domiciliary patients, namely (currently) the [X] chains and NHS Scotland. Surgichem does not supply domiciliary care adherence packaging to the relevant large chains to any significant extent and currently does not supply such packaging at all pursuant to tenders to the large chains. Therefore in such separate customer group in respect of such large chains, the activities of MTS and Surgichem do not overlap as regards supplies pursuant to tenders. Further, the large chains typically specify a requirement for a card-based product, and although Surgichem has developed a card based product, it has never launched that product and, in MTS's view, could not economically compete with MTS and others in the tender market with that product, as is explained in section 6 below.
- Large pharmacy chains, together with sales through buying groups, accounts for approximately [X] of MTS's revenues. Therefore, the extent to which it competes with [X] of MTS's sales, is limited. MTS understands that the majority of Surgichem's sales are made to independent pharmacies [X].
- Outside of the tender segment, as is evidenced below the parties compete much less closely than would be suggested by their market share figures alone.

4.2.1 Separate customer group – large pharmacy chains purchasing by tender

A separate customer group within the adherence packaging market can be identified by reference to large pharmacy chains which hold formal tenders in order to appoint suppliers of adherence packaging for domiciliary patients. The OFT considered that the conditions of competition may differ sufficiently between customers who tender for their requirements and the other customers for it to consider the effects of the merger on these two customer groups separately.⁶ MTS agrees with this assessment. This separate customer group currently comprises the [X] chains and NHS Scotland. NHS Scotland is akin to a large pharmacy chain in the sense that it purchases on behalf of numerous pharmacies in Scotland albeit that it does not itself run the pharmacies in question. Under the NHS Scotland Framework, each individual Scottish Health Board has the option to subscribe to the arrangements for the provision of adherence packaging by or at the cost of NHS Scotland, but not all of the Health Boards have chosen to do so; the framework has resulted in approximately [X] of pharmacies in Scotland participating.

The separate customer group concerns supplies for domiciliary patients only. For domiciliary patients it is the pharmacy that decides which packaging would best suit its patients' needs. For long term care, the pharmacies' decision as to which packaging to purchase are influenced by the preference of the care homes. This is why some suppliers, including *Biodose*, approach the care homes directly who in turn can require the pharmacies to use a particular manufacturer's adherence packaging. The [X] contract that MTS has acquired is for [X]. The [X] contract is focused mainly on [X]; however, in relation to long term care

⁶ Paragraph 46 of the Decision.

[X] use a number of different suppliers other than MTS whereas for domiciliary it only uses MTS products. This is because different care homes require different manufacturers' packaging. Further, the NHS Scotland Framework is for multi-dose (domiciliary care) products but not single dose products as used in care homes. It is possible that a pharmacy participating in the NHS Scotland Framework could obtain its domiciliary care adherence packaging under the framework (supplied by MTS or Venalink) and obtain their single dose adherence packaging for care homes from a different supplier.

The following further factors distinguish this separate customer group of pharmacies:

- The contracts resulting from such tenders tend to be at [X], in particular as regards the large pharmacy chains, than the supplies agreed without a formal tender. By way of illustration the average price per card for key accounts (MTS's top 11 customers which includes [X]) is [X] per card whilst for all other accounts the average price per card is [X]. Further, [X] pays [X] per card. When [X] moved to purchasing by way of tender in [X] MTS [X] its price from approximately [X] does not currently tender for supplies of adherence packaging, although it has indicated that it soon will do so, and this is reflected by the fact that it [X]. NHS Scotland pays [X]. This is because NHS Scotland has established a framework agreement [X]. Further, as there is flexibility in the framework terms for deliveries to be made to either a central hub or to individual pharmacies (as opposed to delivery only to a central hub) the costs of supply [X]. Higher supply chain costs are associated with deliveries to individual pharmacies. [X].
- All such customers purchase card-based adherence packaging. Customers who purchase by way of tender informed the OFT⁷ that they have demanded card based products in their recent tenders and that they have historically used card-based products. MTS submits that this is largely because card based adherence packaging, when purchased in significant volumes, tends to be cheaper than plastic based adherence packaging. Therefore Surgichem, or indeed any other supplier, is unlikely to be able to compete for the business of the large pharmacy chains for supplies to domiciliary patients by offering plastic based adherence packaging. For further details please see section 6 below concerning the counterfactual.
- [X]
- Supplies are in all cases, other than NHS Scotland, made to a central depot. The customer then delivers the adherence packaging to its individual pharmacies. For NHS Scotland supplies for some Health Boards are made to a central NHS depot and then redistributed, however, in other cases supplies are made direct to the pharmacy in question which can then reclaim the cost of the packaging from NHS Scotland.
- Further, some large pharmacy chains which typically tender their requirements, have the alternative, which is not open to independent pharmacies, of insourcing their requirements for adherence packaging. Lloyds Pharmacy has previously insourced its requirements of adherence packaging (using bought-in components). This is explained later in this section 4.2.1.

The market for supplies by tender to large pharmacy chains appears to be expanding. Through discussions with customers, MTS understands that [X] are planning to run tenders for adherence packing during the course of this year.

⁷ Paragraph 23 of the Decision.

Having regard to the criteria set out in the OFT's and Competition Commission's Merger Assessment Guidelines at paragraph 5.2.28, it can be said that competition for customers differs significantly as regards domiciliary care supplies as between the large chains which generally appoint suppliers by tender and other pharmacy customers. The scale of the large pharmacy chains' requirements enables them, through tendering, to obtain better terms for their adherence packaging requirements (see paragraph 5.2.29 of the OFT's and Competition Commission Merger Assessment Guidelines).

Surgichem does not supply domiciliary care adherence packaging to the relevant large chains to any significant extent and does not currently supply such packaging at all pursuant to tenders to the large chains. [X] Therefore in relation to the separate customer group in respect of such large chains pursuant to tenders, the activities of MTS and Surgichem do not overlap. When the data for this distinct customer group is extracted the aggregated share of supply of the parties to customers in the general adherence packaging market for 2013 falls from [X]% to [X]%. (Please see the shares of supply data set out in more detail in section 4.2.2 below.)

Large customers have additional possibilities to obtain adherence packaging, apart from purchasing the products. They can purchase the component items themselves (for example foils and blisters) and have them contract manufactured or produce the packaging themselves in house. The Boots/Manrex arrangement is an example of this, and Lloyds Pharmacy, previously in-sourced its requirements for adherence packaging. This possibility of in-sourcing or self-supply by large pharmacy chains imposes competitive constraints on MTS and will likewise do so on the merged entity.

The parties are also aware that Chemistree (<http://www.chemistree.co.uk/>), which is a specialist provider of pharmaceutical services to the NHS and care home sector, has recently produced a plastic-based adherence packaging product which bears its name. Although relatively little is known about this product, which appears (at least at this stage) to be used by Chemistree for internal supply, Surgichem believes that Chemistree sourced this product from China. The apparent ease with which Chemistree has sourced this product underscores the low barriers to entry and expansion including, in particular, the lack of any significant regulatory or intellectual property barriers and the fact that there are numerous thermoformer suppliers (both in the UK and overseas) which are available to supply adherence packing products to customers in the UK (and will remain available to supply these products following the merger).

In any event present levels of competition in relation to large pharmacy chains are sufficient and will not be reduced by the merger. These large pharmacy chain customers are sophisticated customers with strong buying power. Even without Surgichem as a bidder, in the tenders so far conducted they have [X]. Further, the other leading chains have likewise used their buying power to negotiate [X] as compared with the retail list price of 39 pence per pack.

For supplies to this distinct large pharmacy chain customer group (purchasing domiciliary packaging supplies by tender), MTS holds a share of supply of approximately [X]% for 2013 whilst for 2012 it held a share of supply of [X]%. Also, the shares of supply would change significantly if a supplier other than MTS were to be successful in any future tender as was seen when [X] (which resulted in the significant increase in MTS's share of supply in 2013). Further, the parties believe that, apart from MTS and Venalink, other suppliers, in particular Manrex and Dosebliss, have the necessary production capacity to tender for and perform large scale supply contracts for the supply of adherence packaging to the large pharmacy chains. (Please see the details of competing suppliers set out at 4.3.1 and in Appendix 4).

In any event, most importantly, there is no significant overlap between the parties in relation to supplies of adherence packaging to the relevant large chains and no overlap between the parties in supplies to large chains pursuant to tenders. Also, as already mentioned, the OFT noted in its Decision that large customers that tender their requirements expressed no concerns in relation to the proposed merger.

4.2.2 Pharmacies not purchasing by tenders

In this section MTS sets out estimated shares of supply for the supply of adherence packaging excluding the distinct group of customers who make large scale purchases of adherence packaging by tender for domiciliary patients. Therefore estimated shares of supply excluding these customers for the year ending 31 December 2013 and 31 December 2012 are set out below. The underlying workings and assumptions are provided in Appendices 5 and 6. The methodology for the shares of supply at Appendix 5 reflects all sales prior to adjustment to exclude such supplies by tender.

Also, details of MTS's share of supply to the distinct group of customers who make large scale purchases of adherence packaging by tender for domiciliary patients is provided.

At Appendix 7, MTS provides the methodology and figures that were used to calculate the market shares in the Information Memorandum, prepared by Deloitte, as well as a brief summary of why those figures do not provide an accurate estimate of market shares.

The parties have supplied certain data about which pharmacy stores they supply to PricewaterhouseCoopers ("PwC"), who have aggregated this data. Since half of this data is confidential to each of the respective parties, the aggregation of the two parties' data must also remain confidential. Accordingly the estimates of market share from this methodology are set out in confidential Appendices 8 and 9. Appendix 8 summarises the results of the data analysis by PwC whose report is included in Appendix 9.

It must be emphasised that the parties have limited definitive information about supplies of adherence packaging by third parties and there is therefore considerable uncertainty about the figures now provided in respect of third parties' sales. However, MTS maintains that there is or should be a strong presumption that all pharmacies (or virtually all pharmacies) in the UK purchase adherence packaging, and that the average levels of requirements for adherence packaging for all types of pharmacies taken together is the same for all categories (for example, large chain outlets, multiples and independents) and that there is no bias in terms of levels of requirements as between different types of pharmacy outlet. Therefore in the absence of further or more reliable data, MTS believes that its estimations of the market should be accepted. MTS's calculations of the estimated size of the market and the various assumptions included in them, are explained in Appendix 6.

The market share figures in the following tables are as previously submitted to the OFT except for an adjustment (an increase) in respect of the supplies by Protomed in each table (for 2012 and 2013). This is based on a published article in 2012 of Protomed's product Biodose being used by 45,000 UK patients in care homes and the domiciliary care sector.⁸ MTS has assumed a growth in demand for the product of approximately 10% in 2013, in the table for 2013 below.

⁸ *Packaging the problem of patient adherence*: article dated 26 March 2012 on www.pharmaceutical-technology.com.

ESTIMATED SHARES OF SUPPLY FOR ADHERENCE PACKAGING (EXCLUDING LARGE SCALE PURCHASES THROUGH TENDERS FOR DOMICILIARY CARE)

Year ended 31 December **2013**:

	Surgichem	MTS	Protomed	Venalink	Manrex	HD Medi	Dosebliss / Medimax (Medidos)/ Pivotell / Shantys / others	Total market
Number of patients serviced	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
% share of supply	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]

Based on **2012** year ending 31 December:

	Surgichem	MTS	Protomed	Venalink	Manrex	HD Medi	Dosebliss / Medimax (Medidos)/ Pivottell / Shantys / others	Total market
Number of patients serviced	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
% share of supply	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]

MTS's share of supply for supply to those entities that make large scale purchases of adherence packaging for use by domiciliary patients through tenders is estimated at [X]% for 2013 and [X]% for 2012. These figures have been calculated using the figures in the tables above. Whilst the share of supply for 2013 is high, as is noted at above, Surgichem does not supply adherence packaging to these customers pursuant to tenders and as such the merger will not result in any increment to these figures.

The OFT sets out its conclusion on shares of supply at paragraphs 59-78 and 89-91 of the its Decision. The OFT considered that the parties' methodology may have over-estimated the size of the supply of adherence packaging in the UK attributing a large share (around [X]%) to the 'others' category.⁹ However, the OFT goes on to acknowledge that it was unable to obtain responses from all of the competitors that the parties had identified.¹⁰ Further, the OFT excluded sales made by Manrex from the market share figures on the basis that it treated Boots' supplies of Manrex products to care homes as self-supply by Boots, and that it had received insufficient evidence that Manrex acts as a constraint on the merging parties.¹¹ However, the OFT made clear that it was doing so on a 'cautious basis'.¹² It should be noted that the above estimated shares of supply data provided by MTS treat Boots' adherence packaging for care homes as being supplied by Manrex; if the OFT is correct that such products are self-supplied by Boots, then the shares of supply in the above tables would need to be recalculated accordingly. In any event MTS submits that actual or potential self-supply of adherence packaging by large pharmacy chains imposes a competitive constraint on suppliers and will do so on the merged entity. MTS submits that the parties faces genuine competition from the Manrex system, as Manrex is the originator of Boots' supplies of adherence packaging to care homes and Boots also actively markets Manrex products to other pharmacies.

4.2.3 The parties' strategies for the supply of adherence packaging are entirely different

MTS focusses its sales efforts for adherence packaging on the large pharmacy chains and buying groups. The majority of its sales, approximately [X]% by value are to such customers. In contrast, Surgichem's strategy is to focus its sales and promotion efforts on individual independent pharmacies (from which Surgichem derives a large proportion of its turnover). MTS's and Surgichem's promotional efforts are also differentiated in that MTS uses telesales techniques whereas Surgichem relies more on individual pharmacy visits using its direct sales team. As a result of these different strategies, MTS and Surgichem are only to a limited extent in direct competition with each other in the supply of adherence packaging. The parties therefore compete much less closely than would be suggested by their market share figures alone. MTS's sales activities are focused on the large pharmacy chains and buying groups and only to a much lesser extent on independent pharmacies. Surgichem does not supply any of the large pharmacy chains through tenders and has opted not to compete for buying group bids. Finally, Surgichem supplies other large customers only to a very limited extent [X]. Surgichem has dedicated and experienced sales representatives dealing directly with individual pharmacies, and MTS does not have this type of resource.

The parties' internal sales records show that they lose business to the other or are compelled to adjust their prices to compete with the other to a much lesser extent in proportionate terms than would be suggested by their respective market shares. Please see Appendix 10 which summarises the position with regard to customers lost by MTS over the previous six months as at November 2013 and Appendix 11 which sets out details of MTS's customers which have been lost, in December 2013 and January 2014, to smaller competitors (i.e. customers other than Venalink or Surgichem).

As noted above, the parties have supplied certain data about which pharmacy stores they supply, to PwC. PwC's resulting analysis is summarised in confidential Appendix 8 and PwC's report is reproduced in confidential Appendix 9. This analysis, which aggregates

⁹ Paragraph 60 of the Decision.

¹⁰ Paragraph 65 of the Decision.

¹¹ Paragraph 64 of the Decision.

¹² Paragraph 64 of the Decision.

confidential data of the two parties, provides empirical evidence on the extent to which MTS and Surgichem compete with each other, and should be read in conjunction with the evidence in this section.

It must also be noted that insofar as Surgichem's prices are generally higher than MTS's the planned merger is clearly not a case of an acquisition being made to remove lower-priced competition.

4.3 Competition issues in relation to customers not purchasing by tender

For the reasons given in section 4.2.1 above the merger will not result in any SLC in relation to large pharmacy chains which purchase their requirements by tender. This section explains why the merger will not give rise to any SLC in relation to customers not purchasing by tender, including the independent pharmacies. In summary:

- There are numerous credible suppliers of adherence packaging apart from the merging parties.
- Even small pharmacies exert significant buyer power in their own right and strong buyer power through the buying groups.
- Price levels for adherence packaging are falling due to fierce competition and the merged entity will be unable to increase prices.
- The market is expanding, which given the low barriers to entry explained in section 5 below, makes it attractive to new entrants.
- The productive capacity used (but not owned) by Surgichem will not exit the market through the merger because Surgichem out-sources all of its production.

4.3.1 Competition from other suppliers

There are various strong suppliers competing to supply smaller customers, all of whom have comparable quality products to those of the merging parties. They exert a real competitive constraint on the parties and they will continue to do so in relation to the merged entity. These competitors include not only Venalink and Protomed (the supplier of *Biodose*), but also Shantys (supplier of *Pillmate*), HD Medi, Medi-Clear and Manrex (through Boots). Appendix 12 contains screenshots of their respective websites. These website extracts clearly demonstrate a focus on actual supplies in the UK. Competition is provided by these and a range of further competitors, all of whose details are set out in Appendix 4, including for example Medication Systems Limited /Caremeds (who are part of the same group) which supplies the *Multimed*s product. Boots is actively supplying Manrex adherence packaging to pharmacies in competition with each of MTS and Surgichem. This does not appear to be limited to areas where such pharmacies are not in competition with Boots. Therefore Manrex/Boots impose a further competitive constraint on the parties, whether the Manrex/Boots arrangement is viewed as supply by Manrex to Boots or as self-supply by Boots.

Venalink benefits from the resources of a larger group, Jones Packaging which has its own manufacturing capabilities and can readily expand their operations. Venalink is a subsidiary of Jones Packaging, a major packaging supplier. A large part of the cost of the packaging, around [X] is the raw material. Given that Jones Packaging purchases large quantities of raw material (across its packaging operations) it is likely to be able to source the raw material at a lower cost than MTS is able to giving it a competitive advantage.

Further, Dosebliss has demonstrated its readiness to supply adherence packaging in the UK. Dosebliss is part of Ecobliss, a significant Netherlands-based supplier of adherence packaging which has its own manufacturing capabilities and can expand its operations into the UK.

Protomed's sales have increased rapidly in recent years and Shantys is believed to have [REDACTED]. That Shantys is a credible supplier active in the UK is also evidenced by the fact that it supplies the [REDACTED].

HD Medi has established a presence on the UK market and Dosebliss is ready to supply in the UK (if it is not already doing so) having established a UK sales team and having invested in establishing its brand in the UK through participation in the Pharmacy Show (a trade show in Birmingham) in 2013. Both of them are very strong suppliers on mainland Europe.

By way of further detail, the screenshots contained in Appendix 12 make it clear that these competitors are serious, credible and well-resourced. For instance:

- Protomed's *Biodose* is described as *'Tried and tested in the market – first install over two years ago, now being used by many thousands of service users across the UK.'*
- Protomed state that *Biodose* has been *'Voted by 85% of pharmacies as 'better' or 'much better' than any other medication management device.'*
- More generally, Protomed's annual reports and accounts show that it has experienced significant growth in turnover from £56,651 in 2008 to £2.98 million in 2012 (it may be noted that this is equal to almost [REDACTED] of MTS's turnover).
- Such is the success of Protomed's *Biodose* product its Managing Director (Ian Pearce) has recently commented *'The care sector's unwavering demand for Biodose is such that we have invested heavily in expanding our sales and support team.'*
- HD Medi state that they are the leader in Europe for blister packaging solutions.
- HD Medi is a joint venture backed by two successful shareholders, Dijkstra Vereenigde from the Netherlands and JVM from Korea.
- HD Medi has its own office in the UK and operates across numerous markets including Germany, Austria, Switzerland, Spain, Portugal and Belgium.
- The HD Medi pouch system is suitable for large and small customer bases. HD Medi state that it has solutions appropriate for a patient base of just 100.
- W&W Medsystems are an established player having been in the market since 1980.
- It is clear from the Shantys' website that they are active in the UK (in addition, as mentioned above, [REDACTED]).
- Dosebliss operates in the UK and is actively marketing in the UK for instance it attended the Pharmacy Show 2013 in Birmingham.
- Through global production and supplier networks Dosebliss can provide cost effective solutions for both very small and large volumes of blister packs. It offers a card based

adherence packaging product that would be suitable for the large chains. As such it is a credible supplier for both large pharmacy chains and independent pharmacies.

- Dosebliss is a proven reliable partner to many customers around the globe. It also has experience of many years in the industry.

Robotik's website describes blister trays by Biodose, Surgichem, Venalink, MTS etc as old technologies compared to pouch based systems. It is of note that pouch based systems are prevalent in Europe and it is likely that the competitive pressure from such systems will increase in the future. MTS is aware, for instance, that trials of pouch based systems have been conducted at [X]. MTS understands that such pouches were accepted by the care homes and other organisations. Further, Pivotell have recently run a successful West Midlands and Manchester pilot of their product.¹³ This demonstrates that they are credible player. Pivotell's website states that they are '*looking for pharmacy involvement nationwide*'.

At a minimum the actual or potential competition provided by smaller-scale suppliers (e.g. HD Medi, Protomed and Shantys) and by potential entrants (e.g. Dosebliss) is in effect at the very least equivalent to an extra established competitor although MTS submits that this significantly understates the competitive pressure that such suppliers exert.

All of the above suppliers can be expected to take advantage of the change of control of Surgichem through the merger as the reduction in the number of larger suppliers will create increased opportunities for other competitors. MTS would not be able, following the merger, to introduce above-inflation price increases, because this would result in demand being switched to the alternative suppliers described above.

4.3.2 Buying power of small pharmacies independently and through buying groups

Independent small pharmacies possess a significant amount of buying power both directly and indirectly. This results to a large extent from buying groups which serve to protect the pharmacies against price increases and they will continue to do so after the merger. However, even outside the buying groups, independent pharmacies are able to negotiate discounts off the retail list price. This is shown by MTS's actual average sales prices to independent pharmacies other than buying group customers, by reference to MTS's retail list price of 39 pence per pack, in that MTS's average sales price to such customers was [X] in 2013 (and in 2012 it was [X]). Further, the prices negotiated by buying groups have a wider effect on the market, in that they become known by pharmacies and then serve as a benchmark for pharmacies' negotiations of prices with suppliers. This results in a spill-over effect of downward pressure on adherence packaging prices as a result of the special prices agreed by buying groups originally for the benefit of their members.

Independent pharmacies have the motivation and means to test the market with adherence packaging suppliers and obtain the best possible price. In making their purchasing decisions pharmacies tend to be very price driven as adherence packaging is largely seen as a commodity product. There are however some differences between the different products offered by each supplier and some pharmacies for instance prefer card over plastic and vice-versa. For instance some pharmacies who manually fill their cards prefer the clear plastic based cards so that they can see the pills throughout the process. Ultimately however price will form a major part in a pharmacy's decision as to which packaging to purchase.

¹³ <http://www.pivotell.co.uk/downloads/authorities/West-Midlands-Automated-Pill-Dispenser-Pilot-Cuts-Hospital-Admissions.pdf>

Whilst product quality is an important minimum requirement in a pharmacy's choice, price is the most important factor. This is clearly demonstrated by the Health Advances survey results follow-up slides (provided in connection with the present transaction) which are included in Appendix 13. These show that cost is the predominant factor in the switching of adherence packaging purchases, measured either as the single most important factor or as part of the three most important factors to the pharmacy concerned). Adherence packaging is a cost factor to pharmacies' business, for which they are not reimbursed, whilst their average revenues per prescription item are under downwards pressure (please see the data provided in Appendix 14).

Pharmacies can and do switch between different suppliers including between suppliers of plastic based blister packs and those that supply card based blister packs and vice-versa. There are no technical issues or costs associated with switching. As the table below indicates, customers regularly switch to and from MTS. In each of the last 12 months MTS has [X].

At Appendix 15 MTS supplies a chain of E-mails in relation to pricing for [X] indicates that MTS is required to reduce its prices to match those of a competitor in order to retain its business [X]. The negotiation of these supply arrangements with [X] and this is in effect the tendering process for adherence packaging that MTS refers to at 4.2.1 above. Further, at Appendix 16 please find MTS's price approval forms from approximately the last 2-3 months. These give an indication as to how prices are agreed with both new and existing customers and where relevant, these indicate that prices are [X] in response to prices of competitors. The merged entity will still have to limit prices to gain or retain business after the merger.

Please also see the Surgichem Confidential Annex [X]

CUSTOMER SWITCHING

<u>New/Lost Customer Summary – 2013 (UK Customers (excl Key accounts))</u>														
	Jan-13	Feb-13	Mar-13	Apr-13	May-13	Jun-13	Jul-13	Aug-13	Sep-13	Oct-13	Nov-13	Dec-13		
Live Customers @ start of month	[X]	[X]	[X]											
NEW Customers sold to in the month	[X]	[X]	[X]											
Re-Activated Customers in the month	[X]	[X]	[X]											
LOST Customers in the month	[X]	[X]	[X]											
Live Ship-To's @ end of month	[X]	[X]	[X]											
Net Gain or (Loss) in the month	[X]	[X]	[X]											
Cumulative Gain or (Loss) since 1.1.13	[X]	[X]	[X]											

[X]

Buying groups provide a high degree of pricing protection to independent pharmacies and will continue to do so after the merger. For instance [X] members receive a [X]% discount on the list price for products purchased through the members' account. Apart from any pricing benefits offered at present by buying groups to their members, buying groups will react and find alternative sources of adherence packaging for their members should the merged entity attempt to increase prices post-merger. It would be relatively easy for a buying group to switch to competitors such as Venalink (who are very price competitive for instance having outbid MTS in the NHS Scotland tender) or Shantys who are already a supplier to [X]. Further, the smaller players in the market and potential entrants are likely to take advantage of any price increases to gain market share.

There are numerous buying groups, including nine of which MTS is aware, with very large aggregate memberships, as follows:

<i>Buying group:</i>	<i>Approximate membership:</i>
Numark	[X]
Avicenna	[X]
Cambrian	[X]
Albapharm	[X]
Edinpharm	[X]
Nupharma	[X]
Pharma Plus	[X]
Pharmaco	[X]
Propharm	[X]

These buying groups aggregate the purchasing power of their members, in order to obtain better prices (discounts) for their members usually by way of a rebate and so obtain some of the benefits of a larger business. [X] are known to have concluded arrangements with a supplier for supply of adherence packaging at reduced prices; [X] have made such agreements with MTS and [X] has done so with Shantys.

MTS's arrangements vary as between these buying groups. [X], but for Avicenna's member pharmacies, the rebates are operated on a more flexible basis. Buying groups do not operate formal tenders but appoint a supplier based on consideration of business proposals. They take a commission on each product that is sold by their members through them, but do not hold any stock themselves as orders by members are placed with and dispatched by the suppliers.

The buying groups typically negotiate prices from an adherence packaging supplier which are significantly below the retail list price, through a bidding process which has the same pricing effects as tendering by large pharmacy chains. The screenshots provided at Appendix

17 from various buying groups' websites demonstrate their ability to exert buyer power on behalf of their members. For example, [X] agreed price for purchases by their members from MTS for the MTS adherence packaging product mentioned above with a retail list price of [X] per pack, is [X]. [From this price it is further necessary to deduct an additional[X]%(X)equating to approximately [X] and the [X] equating to approximately [X] per pack, resulting in an equivalent net price of approximately [X] pence per pack.]

The total memberships listed above amount to over 6,000 pharmacies, possibly many more, which are members of buying groups (it is unusual for a pharmacy to be a member of more than one buying group). Of these, over [X] are members of buying groups which currently have arrangements in place for the supply of adherence packaging. This amounts to the vast majority of pharmacies in the UK which are not included within the large customers category. Moreover, any independent pharmacy which is not already a member of a buying group could easily become a member and thereby gain the benefits of the buying group's negotiated prices. Joining a buying group is quick and easy and relatively inexpensive. At the same time, member pharmacies are free to purchase adherence packaging from a different supplier to the one appointed by the buying group where they wish to exercise choice of supplier, for whatever reason, rather than take advantage of the discount negotiated by the buying group.

4.3.3 Price levels are falling due to competition

Adherence packing is a low value product. Therefore sufficient volumes must be sold in order to generate sufficient gross margin to cover the costs (fixed and variable) associated with the supply chain, transport and infrastructure and other operational costs, and thus achieve a positive net margin. Given that adherence packaging is largely viewed as a commodity input product it is very difficult for suppliers to raise prices since products are largely undifferentiated. Attempts to raise prices could lead pharmacies to switch to an alternative supplier. For instance in typical tenders and negotiations MTS's prices have regularly been [X]. At Appendix 18, MTS has provided details of the outcome of tenders over the last five years. In no cases was MTS [X] and in numerous cases prices have [X]. In each of the tenders MTS's tender bid price was [X]) and MTS was nonetheless unsuccessful in some cases

Price lists for most of Surgichem's products have been kept steady over the past two years. The Information Memorandum (Appendix 2) refers to a price increase in October 2012 in relation to *Nomad Clear*. However, in fact this was not a simple price increase as Surgichem also introduced a lower cost variant of the product at a price lower than the previous price. Whilst the list price of *Nomad Clear* increased from £92.45 per box to £99.95, at the same time Surgichem launched its less expensive *Nomad Clear 2* product, priced at the reduced price of £91.20 per box. The *Nomad Clear* and *Nomad Clear 2* products are similar, however the lid for the *Nomad Clear 2* product is made from card rather than plastic, which helps reduce the cost. Through this dual pricing approach, Surgichem was able to retain customers despite the introduction of an increased price for the higher quality version of the product. [X]

[X] has recently lost to MTS the major contract with [X] for supplies of adherence packaging for domiciliary use. As a result of this [X] has a significant amount of spare capacity which it is likely to seek to utilise by winning market share through aggressive pricing to restore its prior position. MTS believes that [X] capacity utilisation may have fallen to levels at which its ability efficiently to spread its costs will be impaired, meaning that [X] can be expected to be particularly pro-active in reducing prices to gain new business to replace the lost [X] contract in order to increase its capacity utilisation.

The ease with which pharmacies can switch suppliers of adherence packaging, and thereby maintain downward pressure on prices, is reflected in the fact that pharmacies do not generally enter into contracts with suppliers of adherence packaging which commit them to purchase any particular quantities or even to continue purchasing for any significant period of time from a supplier. Surgichem does not for instance have any supply contracts in place with any of its customers and MTS only have supply contracts in place with [X]. In relation to the [X] tender won by MTS [X].

4.3.4 The market is growing

The market is growing (Omnicell estimates at approximately [X] per annum for domiciliary care and [X] per annum for long term care). The lower growth rate in relation to long term care customers reflects the greater levels of adherence packaging penetration in relation to such customers in contrast to domiciliary care patients and the fact that there are a greater proportion of domiciliary patients who are not yet using but can benefit from adherence packaging as compared to long term care patients). The number of drugs being prescribed is increasing year on year. In 2010, 927 million prescription items were dispensed in England which was an increase of 68 per cent on 2000.¹⁴ The ONS has found that between 1995 and 2009 the volume of drugs prescribed by GPs more than tripled, with growth averaging 8.6 per cent per year.¹⁵

There are a significant number of patients who are not currently provided with their oral medications in adherence packaging but for whom such packaging would be beneficial. Indeed there is published evidence that as many as 50 per cent of prescribed medicines, taken by older people, are not taken in compliance with dosage regimes.¹⁶ The estimated drug cost of unused or unwanted medicines in the NHS is large at around £100 million annually.¹⁷

Adherence packaging is particularly useful for older patients whose numbers are growing. One in six people in England and Wales is now aged over 65 which equates to 9.2 million people. This is an increase of more than 10 per cent in the last decade.¹⁸ The 65+ population is expected to more than double to 24.2 million by 2081. Further, it is estimated that around 75% of all drugs used in an individual's lifetime are required after the age of 65.¹⁹

There is published evidence that the number of persons in the UK living with long term conditions is increasing. The number of individuals with multiple long term conditions is set to rise from 1.9 million in 2008 to 2.9 million in 2018.²⁰ Jeremy Hunt, Secretary of State for Health, has stated in relation to such persons that "*We must provide a seamless service*

¹⁴ <http://www.dailymail.co.uk/health/article-2019327/Number-prescriptions-given-soars-70-decade.html>

¹⁵ <http://www.telegraph.co.uk/health/healthnews/8421673/Amount-of-drugs-prescribed-by-GPs-triples-over-15-years.html>

¹⁶ <http://www.scie.org.uk/publications/briefings/files/briefing15.pdf> The World Health Organisation also reports that 30% and 50% of patients do not take or use their prescribed medicines as recommended by their prescriber. See World Health Organization (2003) Adherence to long-term therapies: evidence for action. Geneva: WHO.

¹⁷ NCCPC (2009) Medicines Adherence: involving patients in decisions about prescribed medicines and supporting adherence.

¹⁸ Figures from the census 2011 quoted by the Daily Telegraph <http://www.telegraph.co.uk/earth/greenpolitics/population/9403470/Census-2011-one-in-six-people-in-Britain-now-over-65.html>

¹⁹ Information Memorandum (Deloitte) (see Appendix 2)

²⁰ <https://www.gov.uk/government/publications/integrated-care>

focussed on the individual within their own home."²¹ Assistive technology, including adherence packaging, can support such persons.²²

Further there will be market growth as medication regimes are becoming more complex, with more drugs per patient prescribed. For example the average number of prescriptions per patient is expected to grow from [X] by 2016.²³ As a result of these factors, the numbers of prescriptions and as a consequence the required volumes of adherence packaging, are increasing. This is explained by Dr Laurence Buckman, Chairman of the British Medical Association's GPs Committee, who is reported as stating "*There are many reasons why prescribing rates have risen. Our population is growing, we can treat more illnesses than ever before, we are getting older and, as a result, the number of people with multiple long-term conditions is also on the rise. It's not unusual now to find a patient with an array of prescriptions to treat their various conditions.*"²⁴ The vast majority if not all UK community pharmacies provide adherence packaging at least to some extent although this is not necessarily the case for all NHS hospital pharmacies. Further, it may be considered a requirement for them to do so due to disability discrimination legislation.

The Pharmaceutical Services Negotiating Committee ('PSNC'), which promotes and supports the interests of all NHS community pharmacies in England, has provided guidance on this issue. In summary, the Equality Act 2010 sets out the framework which requires providers of goods and services not to discriminate against persons with a disability. If a person is disabled, the provider of the service must consider whether a feature of the way in which he provides the service means that the disabled person would not be able to access the service, whereas a non-disabled person would. The provider of the service must then consider whether an adjustment could be made which would overcome the obstacle to providing the service. Such an adjustment may be the provision of medication in adherence packaging. The PSNC Guidance Paper is available here: <http://psnc.org.uk/wp-content/uploads/2013/08/PSNC-Briefing-084.13-Equality-Act-2010-August-2013.pdf>

The number of UK pharmacies has grown year on year from approximately [X] pharmacies in 2009 to over [X] pharmacies by 2013.²⁵ This indicates a growth in the number of customers for adherence packaging suppliers and therefore a growth in sales opportunities. However, the overall size of the market is best measured in terms of the prescriptions, especially where multiple prescriptions are issued to the same patient. On this basis, the market is growing because of the demographic, social care and prescription rate factors explained above.

For these reasons, the adherence packaging market is expected to expand considerably making it attractive to new entrants particularly given the low barriers to entry described below.

4.3.5 Productive capacity

The productive capacity used (but not owned) by Surgichem will not exit the market through the merger because Surgichem out-sources all of its production. [X]. Moreover Surgichem's third party suppliers will be motivated to diversify their customer base in order to reduce

²¹ Ibid

²² Ibid, page 35

²³ Health Advances Presentation dated 31 October 2013, page 14

²⁴ <http://www.telegraph.co.uk/health/healthnews/8421673/Amount-of-drugs-prescribed-by-GPs-triples-over-15-years.html>

²⁵ Source: Binley's (Wilmington Healthcare Limited) data: [X] pharmacies in January 2009 and [X] in October 2013.

their dependence on a customer that, post-acquisition, would have access to its own production assets in the USA.

Thus the productive capacity that would previously have been used by Surgichem can then be used by other suppliers to compete in the market. The proposed merger involves no acquisition of productive capacity. In addition, suppliers can increase their productive capacity with relative ease. For example, a thermoformer can purchase additional machines where it expects to increase the volume of products that it supplies.

5. BARRIERS TO ENTRY OR EXPANSION

Barriers to entry are relatively low at least in so far as concerns the supply of adherence packaging other than to the large pharmacy chains by way of tender. This is particularly the case for suppliers of packaging (not necessarily adherence packaging) although it is also true for suppliers who are not currently active in packaging at all. There are numerous suppliers of adherence packaging who currently supply outside the UK but for whom it would be relatively easy to enter the UK market. In particular, the capital costs of entry into the market are relatively low as will be explained below. Also intellectual property rights are not a significant barrier to entry and there are no regulatory requirements for adherence packaging.

In addition, it is relatively easy for new entrants to expand their position in the UK market, because it is relatively easy for pharmacy customers to switch supplier. The various competitors described in section 4.3 above are all capable of expanding their position, taking into account the factors explained in section 4.3.1 above, if independent or other pharmacies were to wish to switch suppliers (taking into account also the factors in section 4.3.2 above). Indeed Surgichem itself was a small competitor which has swiftly and progressively expanded its position in the UK market. Other new entrants have followed Surgichem's model, for example Shantys and Medi-Clear, as explained in section 4.3.1 above.

5.1 Supply other than to large pharmacy chains by way of tender

It is relatively easy for a new-entrant to enter the market by sub-contracting the manufacture of the adherence packaging to a third party. This is the method by which Surgichem has its plastic based adherence packaging produced. Further, Protomed's *Biodose* product is manufactured by a third party manufacturer in the UK. Protomed has, within the last five years, established its *Biodose* product in the market by persuading many care homes to insist that pharmacies use *Biodose*. Protomed markets its products into care homes and then finds a pharmacy to service those care homes with its *Biodose* product. Further examples include HD Medi, which has achieved sales of an innovative pouch-based variation of adherence packaging, and Dosebliss who has entered the market in approximately the last two years. Dosebliss is a large Dutch company with over 300 employees which supplies basic card packs as well as a card pack that contains electronic circuits, used to send messages when an individual has taken their medication.

Sub-contracting production of adherence packaging to a third party manufacturer is relatively simple and does not require significant up-front capital investment. In order to supply plastic based adherence packaging a new entrant would need to approach one of the numerous thermoplastic suppliers, for instance William Beckett Plastics or MHP, and contract with them to produce the packaging. The new entrant would be expected to pay upfront for the tooling to be used in the thermoforming machines. For a machine that produces sufficient volumes of plastic based adherence packaging to enter the market Omnicell estimates that the tooling would cost in the region of £15,000 – 20,000.

There are numerous thermoplastic suppliers who the parties believe could supply a new entrant adherence packaging supplier. Details of three such thermoplastic suppliers are provided in Appendix 19.

The out-sourcing of production of card-based adherence packaging may be less economically viable for the purpose of supplies to large pharmacy chains at the prices that result from tender awards (as suggested by Surgichem's experience of its development of a card-based product using a Chinese manufacturer). However, for supply of card based adherence packaging products to independent pharmacies, a third party card supplier could be approached (for example any one of a number of Chinese suppliers). The blisters on the card based adherence packaging are made from plastic and so a thermoplastics company would need to be approached as well (and the tooling would need to be purchased).

For both card based adherence packaging and plastic based adherence packaging the upfront capital costs are low. The production processes themselves are not technologically complex and rely on old technology.

Further, container shipping costs are low and so suppliers can manufacture their adherence packaging outside the UK. At Appendix 20 MTS provides a [X] shipping invoice dated 13 December 2013. The invoice shows the freight cost of £[X] for a 40' container from the United States to the UK. Such a container would contain approximately [X]. For such cards the shipping costs are therefore minimal at only [X] pence per card. As such, shipping costs do not constitute a barrier to entry.

For information concerning Surgichem's shipping costs, please see [X]. Further, the OFT concluded that it did not consider it necessary for a supplier to manufacture in the UK given that one of the merging parties is not currently manufacturing in the UK but supplies there.²⁶ The majority of third parties who responded to the OFT's market investigation confirmed the parties' view that geographic location within the UK is not an important factor when choosing a supplier of adherence packaging. One customer explained that location within the UK was not important at all as all the adherence packaging products are delivered by courier and another supplier stated that location did not matter so long as the supplier could deliver nationally (in the UK).²⁷

Furthermore, it is straightforward for a new entrant to build a database of potential customers as such information is publicly available on the internet from multiple sources. In addition to approaching the pharmacies a new entrant could also consider approaching the care homes. For instance Protomed marketed its *Biodose* product direct to care homes who have then in turn requested the *Biodose* product from the pharmacies. The *Biodose* product is innovative in that it can be used for liquid oral medications as well as solid oral medications, and also in that it allows for the routine application of the name of the medication to the seal of each pod in the blister pack. Surgichem's *Nomad Multimed*s product, explained above, has been developed by a third party and could provide a further liquid medications adherence packaging product.

Intellectual property rights do not act as a significant barrier to entry. Certain features of some suppliers' products are protected by intellectual property, for instance, the seal on Surgichem's pressure seal adherence packaging is patented, however other suppliers use other methods of sealing the packaging that are outside the scope of that patent. Protomed's *Biodose* product has some intellectual property right protection, but this does not appear to

²⁶ Paragraph 54 of the Decision.

²⁷ Paragraph 56 of the Decision.

have prevented Medication Systems Limited from operating in the market by offering a product similar to *Biodose*.²⁸

There are no regulatory standards for adherence packaging or for the products ancillary to the adherence packaging and this further contributes to the ease of entry. This point was confirmed to the OFT by the Medicines and Healthcare products Regulatory Agency.²⁹

A new-entrant would however need to gain credibility in the market. In order to obtain around a 5% share of supply a new entrant would need to establish a presence through winning accounts with independent pharmacies. In order to build up a customer base of independent pharmacies, a new entrant would need to invest as follows. First it would need office and potentially warehouse space particularly if it intends to import its adherence packaging. MTS estimates office and warehouse space and rates may cost no more than £[redacted] per annum. As noted above the new entrant would need to pay for the tooling, which MTS estimates would cost in the region of £15,000 – 20,000. The new entrant would also need to invest in building a sales team and in marketing. MTS estimates that the annual cost for a sales team capable of achieving a 5% share of supply of adherence packaging to be at most between £[redacted]. This would cover the cost of two sales representatives, an office assistant, as well as a manager. In addition the marketing spend may be at most between £[redacted]. Marketing spend may for instance include attendance at trade fairs. The fact that, as already mentioned, MTS's sales teams make telesales, rather than making personal visits to pharmacies, makes clear that suppliers can become established in the market by means of distance selling without needing to incur the costs of establishing a field sales force. New entrants would be able to copy this model of sales at low cost.

However, potential entrants may already be producing related products such as other packaging products and in such cases the costs of entering the adherence packing market may be lower than as indicated above.

For example, suppliers such as Shantys, Pivotell and Medimax have gained credibility in the UK market for instance as a result of appearing at exhibitions in the UK and Dosebliss has done likewise. Further, the low barriers to entry are illustrated by the introduction to the market of Protomed's *Biodose* product which is gaining market share.

Surgichem's own experiences confirm ease of entry. For instance, when Surgichem launched *Nomad Clear*, it did not need to spend significant amounts on marketing as it was able to simply send a sample of the product to all UK pharmacies together with a response card. New entrants could adopt a similar approach to keep marketing spend low. Surgichem's start-up costs are low across the range of its blister pack products.

For Surgichem's total annual marketing expenditure, please see [redacted] MTS has provided details in Appendix 21 details of its annual marketing spend which is low at only approximately £[redacted] in total.

In conclusion, the costs of entry into the adherence packaging market in the UK for supply other than to large pharmacy chains by way of tender are relatively low. The estimated investment costs to produce tooling capable of enabling supplies to independent pharmacies is relatively limited (no more than £20,000) and various thermoplastics suppliers could provide the products, either in the UK or in the Far East, and the cost of transportation is, based on the example mentioned above, small ([redacted]). Also it is possible to compile a database of pharmacies and to market those pharmacies at low cost, and relatively limited

²⁸ <http://www.multimedcs.co.uk/protomed-lose-in-court-of-appeal>

²⁹ Paragraph 115 of the Decision.

investment in personnel would be required. The success of various new entrants in becoming established or at least gaining credibility on the UK market in recent years, in particular Shantys, Dosebliss, Pivotell and Medimax, demonstrates this scope for entry.

[REDACTED]

5.2 Supply to large pharmacy chains by way of tender

As noted above present levels of competition in relation to large pharmacy chains are sufficient and will not be reduced by the merger. As is explained in section 6 below, experience shows that it would not be possible for Surgichem (or indeed any other supplier) to contract out production of a card based product at a price low enough to compete in the large pharmacy tender market. However there are suppliers who manufacture their own adherence packaging that could compete in that market. Dosebliss for example manufactures its own card based product and, as already mentioned, could tender for supplies and supply such adherence packaging to a large pharmacy chain.

6. THE COUNTERFACTUAL

6.1 Large customers which purchase by tender

Large pharmacy chains are unlikely to regard Surgichem as a potential supplier of adherence packaging because these customers generally require card-based products, and Surgichem does not have a card-based product. A prototype card-based product made for Surgichem in 2013 cannot be supplied (MTS understands) sufficiently cost-effectively to be realistic competition. Omnicell believes there is no realistic prospect that Surgichem would have the ability to supply card-based products and tender to supply such products, absent the merger.

The OFT's Decision asserted that, absent the merger, Surgichem would provide additional competition as it would launch the card-based adherence packaging product that it has had developed. However, this product, though developed, has not been launched. Moreover the cost price for the product means that Surgichem would not be able to supply the product sufficiently economically and cost-effectively to be a realistic competitor by means of this product, for future tenders to large customers absent the merger. Therefore the counterfactual should not include the availability of Surgichem's card-based product, which means that there will be no loss of potential competition as a result of the merger in relation to large customers which tender their requirements.

MTS has its card-based adherence packaging products manufactured and transported to it by its parent company in the USA on a more cost-effective basis than can be offered by Surgichem's supplier. The marginal cost of production per pack for MTS's products supplied to [REDACTED] are [REDACTED] and the costs per pack for MTS's products supplied to [REDACTED] are [REDACTED]. These costs cover production and transportation and there are no import duties involved. Also it may be concluded from this that there are efficiency benefits from the merger whereby MTS could offer a more cost-effective card-based alternative to the plastic-based products currently supplied by Surgichem.

Even if such evidence were not accepted by the CMA in relation to the costs of Surgichem's card-based product and the potential for Surgichem to supply such a product, nevertheless there is in any event no loss of actual competition through the merger in relation to large customers which tender their adherence packaging requirements, because to date Surgichem does not have a card-based product. Therefore the conclusion can be drawn that there will be no *substantial* loss of competition as a result of the merger in relation to such customers.

Further, Omnicell believes that the increased size of the tender market will constrain the competitive threat of Surgichem absent the merger for as long as it does not have a card-based product.

6.2 Customers which do not purchase by tender

In MTS's view, the proposed merger will create opportunities for new entrants and smaller competitors to gain business from pharmacies in the supply of adherence packaging through the removal of a significant independent supplier. A greater diversity of suppliers may develop following the merger than would otherwise be likely if Surgichem were to continue supplying independently as at present.

7. COMPETITIVE EFFECTS OF THE MERGER

The parties consider that the proposed merger will not result in a *substantial* lessening of competition in relation to either to large pharmacy chains which tender their requirements for adherence packaging, or in relation to smaller chains or independent pharmacies which do not tender their requirements.

7.1 Overview

In relation to other products, the parties consider that there will be no substantial lessening of competition ("SLC") because, as regards automated filling machines and heat sealing machines, there is no overlap or virtually no overlap between the parties' supplies. As regards trolleys, MTS is not a manufacturer but buys and resells a small quantity of trolleys, and any incremental market share in relation to Surgichem's is minimal, whilst in any event Surgichem's and the parties' combined market shares in relation to trolleys are low. As regards adherence support products, there is no data on the overall size of the market but there are numerous sources of supplies for all types of product and there is no indication that the proposed merger would in any way restrict competition in relation to such products.

Further, it should be noted that the OFT's Decision indicated that there is no competition concern as regards the proposed merger, in relation to the supply of adherence packaging machines, the supply of trolleys and cabinets or the supply of adherence support products (paragraphs 35 and 37 of that Decision).

7.2 No loss of competition in relation to large customers for adherence packaging

Large pharmacy chains are sophisticated customers with strong buying power who through tenders have gained substantial reductions in prices. Other leading chains such as [X] have likewise successfully used their buying power to negotiate reductions in price.

In any event, Surgichem is not a competitor in relation to large pharmacy chains which tender their requirements for adherence packaging, because such chains have specified their requirements to be for card-based adherence packaging products whereas Surgichem currently does not have a card-based product available. As explained above and in more detail by Surgichem, the prototype card-based product which Surgichem arranged to develop, was found (MTS understands) not to be economically viable on the basis of the cost of production and the typical sales price at which contracts for supply of adherence packaging to the large chains (in particular [X]) have been awarded, pursuant to tender.

MTS understands that Surgichem has therefore declined to pursue further or launch any such card-based product and that it does not regard itself as a competitor in this sector.

Further, large customers also have the option of self-supplying their requirements of adherence packaging by purchasing components themselves and having them contract manufactured or doing the manufacturing in-house. Arguably the current arrangement between Manrex and Boots is an example of this. Lloyds Pharmacy previously arranged for its adherence packaging requirements to be insourced. The possibility of such self-supply or insourcing represents an ongoing constraint on MTS and will do so on the merged group, in relation to supplies to large pharmacy chains, and this will continue despite the merger.

Accordingly, the proposed merger cannot be regarded as resulting in any loss of competition in relation to large customers which tender their adherence packaging requirements.

7.3 No SLC in relation to customers which do not currently tender their requirements

Despite the fact that the parties will together have relatively high market shares for the overall adherence packaging market and also for the sector of the market comprising customers which do not currently tender their requirements, the proposed merger will not result in any *substantial* lessening of competition.

This is due to a combination of factors. First, there is a range of competing suppliers of adherence packaging, including HD Medi, Protomed and Shantys, all of which have established a foothold in the market and which already represent credible alternative sources of supply of adherence packaging. For example, Protomed is recognised as a successful entrant having gained approximately 5% market share in 2013 and Shantys and HD Medi are already well established on the UK market. In addition, there are a range of established suppliers on mainland Europe which supply or have clearly indicated their readiness to supply in the UK, including Dosebliss which is part of a large Dutch-based group Ecobliss. Such smaller competitors and potential entrants are described further below; they can be expected to take the opportunity to enter the market (if they do not already have plans in place) if the merged entity were to attempt to increase prices post-merger.

Second, in relation to any such potential price increases by the merged entity, independent pharmacies benefit from a high degree of protection afforded by buying groups. In the event of such a post-merger price increase, the buying groups can be expected to react and find alternative sources of adherence packaging for their members.

[X] buying groups are known to have secured favourable arrangements for the supply of adherence packaging by the appointed suppliers at discounted prices. These include [X], all of which have arrangements with MTS for supplies at reduced prices, and Cambrian, [X]. These buying groups together account for over 5,600 pharmacies as explained in section 4.3.1 above:

Buying group:	Approximate membership:
[X]	[X]

Thus the memberships of these buying groups account for over 5,600 pharmacies, possibly more. It should also be noted that the large pharmacy chains account for over 6,000 pharmacies. These comprise Boots (approximately 2,500 pharmacies), Lloyds Pharmacy (approximately 1,400 pharmacies), NHS Scotland (approximately 450 pharmacies), the Co-Operative (approximately 800 pharmacies) and Rowlands (approximately 600 pharmacies), Day Lewis (approximately 220 pharmacies) and PCT Healthcare (approximately 100 pharmacies). Since there are approximately 14,000 pharmacies in the UK, those that are not members of a large chain or a buying group are in a minority, and any independent pharmacy that is not already a member of a buying group could easily join one.

Buying groups typically negotiate prices from an adherence packaging supplier which are significantly below the retail list price, through a bidding process which has the same pricing effects as tendering by large pharmacy chains. For example, [X] agreed price for purchases by their members from MTS for MTS adherence packaging products with a retail list price of [X] per pack, is [X]. [From this price it is further necessary to deduct an additional [X]% [X] equating to approximately [X] and the [X] equating to approximately [X] per pack, resulting in an equivalent net price of approximately [X] per pack.]

There are various suppliers competing to supply smaller customers, all of whom have comparable quality products to those of the parties. They exert a competitive constraint on the parties and they will continue to do so in relation to the merged entity. These competitors include Venalink and Protomed (the supplier of *Biodose*) and also Shantys (supplier of *Pillmate*) and HD Medi . Shantys is (as already mentioned) the appointed supplier of the [X] and HD Medi has established a presence on the UK market (with a new UK accounts director). Dosebliss is ready to supply in the UK having established a UK sales team and having invested in establishing its brand in the UK, partly through participation in the Pharmacy Show (a trade show in Birmingham) in 2013 (please see the above screenshots). Both of them are very strong suppliers on mainland Europe.

Appendix 12 contains screenshots of their respective websites. These website extracts clearly demonstrate a focus on actual supplies in the UK. Competition is also provided by a range of further competitors whose details are set out in Appendix 4, including for example Medication Systems Limited / Caremeds which supplies the *Multimed*s product.

Protomed's sales have increased rapidly in recent years and Shantys is believed to have [X]. Shantys is the supplier appointed by the [X] for adherence packaging.

All of the above suppliers can be expected to take advantage of the change of control of Surgichem through the merger. The reduction in the number of larger suppliers will create increased opportunities for other competitors.

Also, Boots is actively supplying Manrex adherence packaging to pharmacies in competition with each of MTS and Surgichem. Also this does not appear to be limited to areas where such pharmacies are not in competition with Boots. Therefore Manrex/Boots impose a further competitive constraint on the parties, whether the Manrex/Boots arrangement is viewed as supply by Manrex to Boots or as self-supply by Boots.

Thus the aggregate or combination of smaller competitors, the ease of entry and expansion on the part of such competitors and the important role of buying groups, together mean that any lessening of competition that may result from the merger will not be substantial.

7.4 Competition concerns in relation to independent customers

The proposed merger will not give rise to any competition concerns in relation to independent customers for the following reasons. First, MTS's sales strategy focuses on large pharmacy chains and buying groups rather than individual independent pharmacies. Surgichem, by contrast, focuses its sales activities on independent pharmacies. There is therefore limited overlap between the two parties' sales and supplies of adherence packaging. Whilst definitive information is scarce, the parties consider that their competitive interactions with each other are lower than might be expected given their market shares.

There is a degree of indirect competition between MTS and Surgichem in relation to members of buying groups who purchase or consider purchasing adherence packaging outside of the relevant buying group's arrangements where MTS is the buying group's selected supplier with whom it has agreed discounts for its members. However, after the merger, MTS will not be able to increase its prices for buying groups to narrow the difference between its and Surgichem's prices, because this would be likely to result in MTS losing its status as the relevant buying groups' appointed supplier, in favour of another supplier offering better discounts, such as possibly Venalink. These factors already apply at present irrespective of the merger and will not be changed by the merger.

Conversely, it would not be economically rational for MTS to increase the prices charged by Surgichem to its customers after it has acquired control of Surgichem. This would test the loyalty of, and risk losing to alternative (less expensive) suppliers, the very customer relationships that MTS hopes and expects to gain through the merger with Surgichem.

Insofar as Surgichem's prices are generally higher than MTS's, the planned merger is clearly not a case of an acquisition being made to remove lower-priced competition. MTS intends to maintain the customer relationships developed by Surgichem and the proposed merger will not result in any adverse effects for such pharmacy customers.

The extent of competition between MTS and Surgichem is also analysed in Confidential Appendices 8 and 9, which should be read in conjunction with this section. These Appendices, already mentioned, rely on confidential data from the parties aggregated by PwC, and shed light on whether the extent to which the parties take business off each other is as significant as might be expected given their market shares.

In the light of the above factors, the merger will be at least a six to five merger in a very open market. Insofar as the smaller competitors such as Protomed, HD Medi and Shantys would not be regarded as equivalent to a well established competitor, in the parties' view they nonetheless represent a range of alternative source of supply which together are approximately equivalent to an established competitor. In addition, the potential competing suppliers, such as Dosebliss, that would be likely to enter the UK market in the event of a price increase post merger, and also the protection offered by buying groups, provide additional competitive forces constraining any market power of the merged entity. Further, there will be no acquisition of productive capacity through the merger and the third parties which produce Surgichem's products will be available to provide products to other competing suppliers. In these circumstances, if the merger were said to result in a lessening of competition, this would not be a *substantial* lessening of competition.

8. EFFICIENCIES AND OTHER BENEFITS RESULTING FROM THE MERGER

8.1 Innovations

As explained in section 2 above, Omnicell aims to ensure the same level of medication monitoring in non-acute sectors, to that achieved by its innovative electronic solutions

platform which allows hospitals and acute care providers in the USA to optimise medications inventories and ensure correct medication administration. [X] The acquisition of Surgichem will enable an accelerated introduction of such solutions because it will allow the critical mass and in particular a larger revenue base from which to fund the required investments in such innovations.

MTS is currently at an early stage in the development of [X] Moreover it is intended that the [X] will be applied to both card-base and plastic-based adherence packaging products, meaning that as a result of the merger such technology could be achieved more rapidly for the benefit of users of both types of product.

[X] It will assist [X] giving the right medication at the right time to the right person and will include safeguards to prevent administration errors. The commercial model has not yet been decided upon but the software will support the dispensing process in relation to care homes and allow the pharmacy to improve its offering to care homes.

The merger will enable the parties to pool their resources in relation to [X] so as to be able to adopt and implement such technology and to develop a better product, ultimately for the benefit of [X] patients, faster than would be possible absent the merger. The merged entity will be able to increase capital investments in such developments as it will generate revenue from a larger customer base across which to spread the costs of such investments. [X] can be expected to bring about results earlier than would be the case absent the merger.

8.2 Production efficiencies

The enlarged customer base that will result for the merger may make it economic for [X].

[X] will create efficiencies and give the merged entity improved control over its unit costs in the face of increasing raw material costs.

[X].

9. CONCLUSIONS

9.1 Innovations resulting from the merger

The proposed merger will enable Omnicell to bring forward significant planned innovations to improve medication adherence, by providing the critical mass necessary to spread the investment costs across wider patient base and revenue streams. These innovations include [X]. MTS's current work on such innovations is described in section 8 above. The acceleration of such innovations will result in significant healthcare benefits, [X]. These innovations and benefits would not be possible within a similar time scale absent the merger.

9.2 Competition in relation to adherence packaging and heat sealing machines, adherence support products and trolleys and cabinets

The proposed merger will not give rise to any competition concern in relation to automated filling machines or heat sealing machines for adherence packaging. As regards automated filling machines, [[X] such products have been supplied by MTS] and the amounts and proportion of adherence packaging which are filled using such machines are [X]. There are in practice no ties on the customer regarding the use of the adherence packaging of a supplier of such a machine because customers fill most of their adherence packaging manually and can readily switch to using a competing supplier's packaging irrespective of whether or not they use such a machine. Moreover the OFT concluded in its Decision that

the merger will not give rise to any concerns in relation to the supply of adherence packaging machines. Also as regards heat-sealing equipment, in the parties' view no competition concerns arise because most adherence packaging, indeed increasing proportions, are sealed using pressure sealing which does not require such machinery, the proportions of MTS's packs which are heat-sealed are [3<] and to some extent its heat sealing machines can be used to seal other suppliers' packaging (provided the customer provides the relevant platen, which is not an expensive item).

No competition concerns arise in relation to adherence support products, which are merely an incidental and minor part of the parties' respective UK operations. MTS's supplies of trolleys and cabinets are minor and will result in an insignificant enhancement of Surgichem's share of supplies of such products, for which the relevant market must be regarded as comprising all supplies to hospitals as well as care homes throughout the UK. Moreover, the OFT also concluded that no competition concerns arise as regards the merger in relation to trolleys, cabinets and adherence support products.

9.3 Supplies of adherence packaging to large pharmacy chains which tender their requirements

As regards adherence packaging, the proposed merger will not result in any SLC in relation to large pharmacy chains which tender their requirements.

Large pharmacy chains are sophisticated customers with strong buying power who through tenders have gained substantial reductions in prices. Other leading chains have likewise successfully used their buying power to negotiate reductions in price. Surgichem is not a potential competitor in relation to large pharmacy chains that tender their requirements because these customers generally require card-based products and Surgichem's card-based product has not been launched, and (MTS understands) cannot be supplied sufficiently cost-effectively to be realistic competition. Therefore there is no actual or potential overlap in supplies by the parties in relation to the large pharmacy customers tender segment.

Further, large customers can also self-supply by purchasing components themselves and having them contract manufactured or manufacturing themselves. The Boots/Manrex arrangement for the care home sector is arguably an example of this, and Lloyds Pharmacy has also previously insourced its requirements for adherence packaging and could do so again. Such a possibility of insourcing or self-supply by the large pharmacy chains imposes a competitive constraint on MTS and will continue to do so on the merged entity.

MTS expects tendering by pharmacy chains to increase in 2014 onwards and that this will counter-balance any increased market power of the merged entity. Moreover, in the counterfactual, such increased size of the tender market will constrain the competitive threat of Surgichem absent the merger for as long as it does not have a card-based product.

9.4 Supplies of adherence packaging to pharmacy customers which do not tender their requirements

As regards the supply of adherence packaging to pharmacy customers which do not currently tender their requirements, there is sufficient existing competition for other suppliers irrespective of the merger and a strong degree of potential competition. There are no significant barriers to entry in terms of the costs of entry or in terms of intellectual property, technological or regulatory requirements (as explained in section 5 above). Also, the size of the market is increasing not just in terms of the number of pharmacies but more importantly in terms of the increasing numbers of mostly elderly patients receiving multiple medications who are likely to benefit from adherence packaging and who are likely to give rise to

increasing demands for the use of adherence packaging by the pharmacy sector across the UK. These factors give strong incentives to adherence packaging suppliers to enter or expand their operations in the UK adherence packaging sector.

At the same time, adherence packaging represents a cost factor to pharmacies for which they are not reimbursed and which they cannot recharge to their customers. Therefore pharmacies are strongly incentivised to ensure that the prices they pay for adherence packaging are kept to a minimum. The evidence shows that whilst product quality is important to pharmacies, price is more important (see the health Advances survey data provided at Appendix 13). It is easy for pharmacies to switch suppliers of adherence packaging (there are no barriers to them doing so), to ensure a strong price to quality ratio and such switching by customers is a regular feature of MTS's and Surgichem's current and recent experiences in the market place. Indeed the experience of both parties shows that independent small pharmacies possess significant buying power. This will continue after the merger.

There are a significant number of actual and potential competing suppliers of adherence packaging. The current competitors include Venalink and various smaller scale competitors, mainly Protomed, Shantys and HD Medi. In addition, Manrex/Boots impose further competitive constraints on the parties because Boots is actively supplying Manrex packaging to pharmacies pursuant to its licence or distribution agreement with Manrex.

There are various potential competitors which are strong suppliers on mainland Europe and which could readily enter the market or expand their supplies in the UK in response to price increases by the merged entity, such as Dosebliss as well as HD Medi, both of which have already established their brand on the UK market. The actual or potential competition provided by these suppliers and potential entrants is in effect at least equivalent to an extra established competitor. These smaller scale competitors (for example Protomed, Shantys and HD Medi) and the potential entrants (such as Dosebliss) will take the opportunity to enter the market, if the merged entity were to attempt to increase prices post-merger.

The merged entity will therefore be constrained by potential competition within the meaning of paragraphs 5.8.14 and 5.8.15 of the OFT's and Competition Commission's Merger Assessment Guidelines. The merged entity will not be able to exploit any increased market power gained through the merger because of the threat of new entry. Moreover this threat is a realistic constraint because such entry could occur without substantial sunk costs as the production could be outsourced if production capacity is not already owned by the competitor, and the entry could be achieved within a period of a year.

The buying power of independent pharmacies and the competitive constraints imposed by the current small scale competitors and by potential entrants are supported and reinforced by the activities of buying groups. Buying groups will continue to provide a high degree of pricing protection for their members after the merger. Buying groups' members include over 6,000 pharmacies and those which have concluded arrangements for the supply of adherence packaging at favourable prices account for over [X] pharmacies. Therefore the vast majority of pharmacies that are not part of large pharmacy chains are members of a buying group. Other pharmacies could easily join a buying group. Buying groups negotiate reduced prices on behalf of their member pharmacies through bidding processes similar in effect to competitive tendering. Apart from any pricing benefits offered at present by buying groups to their members, buying groups will react and find alternative sources of adherence packaging for their members if the merged entity were to attempt to increase prices post-merger.

The parties' sales strategies for adherence packaging are entirely different. MTS focuses on large pharmacy chains and on arrangements with buying groups, whilst Surgichem focuses on direct supplies to independent pharmacies. As a result there is only limited overlap between them in the pharmacy outlets that they supply or have supplied or to which they have provided formal price quotations in recent years. Moreover, the parties' sales records show they lose business to the other, or are compelled to adjust their prices to compete with the other, to a much lesser extent than would be suggested by their market shares.

Insofar as there is a degree of indirect competition between MTS and Surgichem in relation to members of buying groups, after the merger MTS will not be able to increase its prices for buying groups, because this would result in MTS losing its status as the relevant buying group's appointed supplier. This factor will continue irrespective of the merger. Also MTS could not increase prices charged by Surgichem after the merger because this would risk losing the very customer relationships that MTS expects to gain through the merger.

The merger will also enable the benefit of increased choice to pharmacies and their patients in that the merged entity will supply or offer to supply both MTS's card-based adherence packaging products and Surgichem's plastic based products to pharmacies. Therefore a pharmacy could offer both types of product to cater to the preferences of individual end users (patients and carers) without needing to dual-source their adherence packaging requirements.

Further, please see the confidential Appendix 8 which summarises the results of the PwC report in the confidential Appendix 9.

Overall the merger will be at least a six to five or seven to six merger in a very open market, with no takeover of productive capacity. The merged entity will be strongly constrained by the ease of switching by pharmacy customers, the ease of entry or expansion by competitors, and in particular by potential competition from existing fringe competitors and new entrants in the UK market. In these circumstances, the merger cannot be said to be likely to result in a *substantial* lessening of competition.