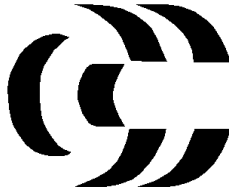


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COMMERCE COMMISSION Decision No. 407

Determination pursuant to the Commerce Act 1986 in the matter of an application for clearance of a business acquisition involving:

THE SOUTHERN CROSS MEDICAL CARE SOCIETY

AND

AETNA HEALTH (NZ) LIMITED

The Commission: M J Belgrave (Chair)
M N Berry
E C A Harrison

Summary of Proposed Acquisition: The Southern Cross Medical Care Society (or a direct or indirect subsidiary) has sought clearance to acquire all the issued share capital in Aetna Health (NZ) Limited.

Determination: Pursuant to section 66(3)(a) of the Commerce Act 1986, the Commission determines to give a clearance for the proposed acquisition, subject to a written undertaking given by The Southern Cross Medical Care Society pursuant to section 69A of the Commerce Act.

Date of Determination: 13 October 2000

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THE PROPOSED ACQUISITION

- 1 Pursuant to section 66(1) of the Commerce Act 1986 (“the Act”), The Southern Cross Medical Care Society (“Southern Cross”) gave notice to the Commission on 18 September 2000 (“the current notice” or “the current application”) seeking clearance for the proposed acquisition by it, or a direct or indirect subsidiary of Southern Cross, of all the issued share capital in Aetna Health (NZ) Limited (“Aetna”). The proposed acquisition is subject to a written undertaking given by Southern Cross pursuant to section 69A of the Act. The undertaking states that Southern Cross will execute the Deed of Undertakings (“the Deed”) within seven days of the Commission granting clearance for the proposed acquisition and duly carry out all of its obligations under the Deed. A copy of the undertaking including the Deed as attached to the undertaking is contained in the Appendix.
- 2 The current notice repeats sections 5 to 16 (inclusive) and Annex A of a notice given by Southern Cross under section 66(1) of the Act on 18 July 2000 (“the first application”). Under the first application, the proposed business acquisition was the same as under the current application, but was not subject to an undertaking. On 25 August 2000, the Commission made a determination declining to give a clearance for the proposed acquisition as detailed in the first application.¹
- 3 Following the Commission declining to give a clearance in respect of the first application, Southern Cross gave a further notice under section 66(1) of the Act on 30 August 2000 (“the second application”) seeking clearance for a business acquisition as proposed in the first application and the current application. The acquisition proposed in the second application was, however, subject to a written undertaking given by Southern Cross pursuant to section 69A of the Act. On 13 September 2000, the Commission made a determination declining to give a clearance for the proposed acquisition as detailed in the second application.² The current application follows the Commission’s determination set out in *Decision No. 404*.
- 4 Southern Cross made several amendments to the Deed during the course of the Commission’s consideration of the current application. The Deed now sets out an undertaking by Southern Cross to divest “[]” certain assets following its acquisition of Aetna. Specifically, the Deed refers to, *inter alia*, Southern Cross selling or procuring “... the sale of all of the medical insurance policies of insured members of Aetna (“Policies”) to [] purchaser who is not an interconnected body corporate (as defined by section 2(7) of the Act) or an associated person (as defined by section 47(3) of the Act) of Southern Cross or Aetna” As to the timing of the divestment, Southern Cross commits in the Deed to using “... all reasonable endeavours to complete the sale of the Policies [] of the Commission granting the clearance application to which this deed relates. The Commission will allow Southern Cross a further [] period to complete the sale of the Policies if the sale has not been completed [] period, if Southern Cross can show that [

¹ Commerce Commission, Decision No. 399, 25 August 2000 (“*Decision No. 399*”).

² Commerce Commission, Decision No. 404, 13 September 2000 (“*Decision No. 404*”).

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THE PROCEDURES

- 5 The Commission on 18 September 2000 registered the current notice. Section 66(3) of the Act requires the Commission, within 10 working days after the date of registration of a notice, or such longer period agreed to by the Commission and the person giving a notice, to either give a clearance or decline to give a clearance for the acquisition proposed. The tenth working day after the registration of the current notice was 2 October 2000. By agreement between the Commission and Southern Cross, the deadline for a determination of the Commission was extended by 9 working days. Accordingly, a determination of the Commission is required by 13 October 2000.
- 6 Southern Cross did not request confidentiality from the Commission for the fact of the current application. It did, however, request confidentiality for specific information contained in and relating to the current application (including in respect of certain information contained in the Deed) on the grounds that the information is commercially sensitive and disclosure would be likely unreasonably to prejudice the commercial position of the parties to the current application. The Commission, in accordance with section 100 of the Act, made Confidentiality Orders on 20 September and 12 October 2000 prohibiting the publication or communication of specific information until 20 working days from the Commission’s determination of the current application. When the Confidentiality Orders expire, the provisions of the Official Information Act 1982 will apply to the information.
- 7 The Commission’s determination is based on an investigation conducted by its staff, and their subsequent advice to the Commission. The majority of the investigation work was carried out in respect of the first application and is relevant to the current application. As indicated above, the essential difference between the first application and the current application is that in the latter case the proposed acquisition, which is identical in both instances, is subject to a written undertaking given by Southern Cross pursuant to section 69A of the Act.
- 8 In the course of their investigation of the acquisition proposed by Southern Cross under the first application, Commission staff had discussions with and sought the views and comments of a number of parties. The parties included insurance companies, insurance brokers, the New Zealand Treasury, the Health Funds Association of New Zealand and the New Zealand Private Hospitals Association. In addition to discussions held, a number of written submissions were received in respect of the first application. Staff have sought and obtained the views and comments of a number of industry participants in relation to the current application, and the Commission has received a number of written submissions on the current application. Furthermore, the Commission obtained expert advice in respect of the process for the divestment contained in the Deed, the undertakings contained in clause 6(c) of the Deed, and information technology related issues.

THE PARTIES

Southern Cross

9 Southern Cross is a “not for profit” health care organisation incorporated as a friendly society under the Friendly Societies and Credit Unions Act 1982. The current application states that Southern Cross has four discrete activities:

- the provision of indemnity health insurance;
- ownership of 13 hospitals, which are operated on an arm’s length basis by The Southern Cross Hospital Trust;
- travel insurance, through its wholly owned subsidiary Southern Cross Benefits Limited; and
- workers’ compensation claims processing, injury prevention and case management activities carried out by Southern Cross Benefits Limited and its 51% owned subsidiary, GMV Associates Limited.

Aetna

10 Aetna is a health risk management services company which is ultimately wholly owned by Aetna Inc., located in Connecticut, United States of America. Aetna is being sold as part of an international reorganisation by Aetna Inc. of its operations. The main business activities of Aetna are:

- the provision of private indemnity health insurance and programmes designed to help manage work place injury and absenteeism; and
- the provision of health management services in the publicly funded primary care market, through its wholly owned subsidiary First Health Limited and its interest in PrimeHealth Limited, a 50/50 joint venture with a network of Tauranga physicians (through the company PrimeHealth Network Limited). Both these companies have management contracts with the Government’s Health Funding Authority to provide patient services in their region on a capitation basis.

OTHER RELEVANT PARTIES

11 Apart from Southern Cross and Aetna, major parties relevant to the Commission’s consideration of competition for health or medical insurance services in New Zealand were identified as part of the investigation of the first application. These parties, which are listed in *Decision No. 399*, mainly included insurance providers. Some such providers offer only general insurance products, while others offer both general and medical insurances or only medical insurance.

BACKGROUND TO HEALTH INSURANCE

12 In *Decision No. 399* the Commission provided a brief background to health insurance. The background covered the function of health insurance, the principal types of health

insurance, general methodologies used by health insurers to price their products, some statistical trends in health insurance, the regulatory environment within which insurance providers in New Zealand must operate, and the role of brokers.

MARKET DEFINITION

- 13 Market definition is an important first step in the process of assessing competition and market dominance. As the Commission stated in *Decision No. 399*, “The purpose of defining a market is to provide a framework within which the competition implications of a business acquisition can be analysed. The relevant markets are those in which competition may be affected by the acquisition being considered, and in which the application of section 47(1) of the Act can be examined.” The Commission briefly outlined in *Decision No. 399* the relevant principles relating to defining markets for the purposes of competition analysis.
- 14 As the Commission noted in *Decision No. 399*, the only area where the acquisition proposed by Southern Cross would result in significant aggregation of activities carried out by both Southern Cross and Aetna is for the provision of indemnity health or medical insurance. Accordingly, in that determination the Commission considered that the only relevant market for the purposes of competition analysis was “the market for the provision of medical insurance in New Zealand”. In respect of assessing the current application, the Commission sees no reason to depart from the relevant market definition in *Decision No. 399*.³
- 15 The effect of the undertakings contained in the Deed is that there will, following the divestment referred to in the Deed, be no aggregation of activities in the medical insurance market.

COMPETITION ANALYSIS

Introduction

- 16 In *Decision No. 399* the Commission considered the impact on the medical insurance market of the acquisition proposed by Southern Cross in the first application. Taking into account various factors, the Commission concluded in *Decision No. 399* that it was not satisfied that the proposed acquisition would not result, or would not be likely to result, in any person acquiring or strengthening a dominant position in the medical insurance market. Accordingly, the Commission made a determination declining to give a clearance for the proposed acquisition.
- 17 As a result of the Commission declining to give a clearance in *Decision No. 404*, Southern Cross has for the third time sought a clearance for its proposed acquisition of Aetna by filing with the Commission the current application. As stated previously, the proposed acquisition is subject to a written undertaking given by Southern Cross pursuant to the Act whereby, as with the second application, Southern Cross commits to

³ Hereafter also referred to as “the medical insurance market”.

executing and carrying out the obligations contained in a deed requiring, amongst other undertakings, the divestment of certain assets. However, the undertakings set out in the Deed are substantially different from those included in the divestment deed which accompanied the second application.

- 18 The Commission's objective under the competition analysis section is to assess the impact of the proposed acquisition, as specified in the current application, including the undertaking given, on the medical insurance market.
- 19 Section 69A(2) of the Act prohibits the Commission from accepting an undertaking in relation to the giving of a clearance under section 66 of the Act other than an undertaking given under section 69A(1) of the Act. Section 69A(1) provides that, in giving a clearance under section 66 of the Act, the Commission may accept a written undertaking given by or on behalf of the person who gave a notice under section 66(1) of the Act to dispose of assets or shares specified in the undertaking.
- 20 The Commission notes that the decision as to whether to accept an undertaking under section 69(A)(1) of the Act is a discretionary matter for the Commission. As the Court of Appeal said in *Goodman Fielder Ltd & Wattie Industries Ltd v Commerce Commission* (1987) 2 TCLR 270 at p. 279:

“When a proposal, original or revised, includes some divestment, it will be for the Commission to decide the bearing of that element in determining whether in its opinion the proposal would result or be likely to result in market dominance or, if so, would result or be likely to result in any outweighing public benefit. The decision must be a discretionary one for the commission. For instance, it may be satisfied with a contract, to be settled after clearance, or it may insist on completed divestment before clearance. Or it may be satisfied with an undertaking, having regard to factors including the terms of the undertaking and its confidence in those who have proffered the undertaking.”

Deed of Undertakings

- 21 The Commission considers that the undertakings contained in the Deed, taken together, address the concerns that it had in respect of the divestment undertaking that accompanied the second application. They address the following key areas:
- Ring fencing of the operational control or management of Aetna's Medical Insurance Business during the divestment period referred to in the Deed. This includes the appointment of a person, having no association with Southern Cross, to independently supervise the Medical Insurance Business of Aetna, and the appointment of independent directors to the Aetna board.
 - Preventing Southern Cross from having access to the confidential and commercially sensitive information of Aetna's Medical Insurance Business.
 - Otherwise putting in place procedures and controls to preserve the Medical Insurance Business, including [] and retaining for the Medical Insurance Business the brandname “Aetna” during the divestment period.

- []

Conclusion

- 22 Having regard to the various elements of section 3(9) of the Act, and all the other relevant factors, the Commission concludes that it is satisfied that the proposal, including the written undertaking given by Southern Cross pursuant to section 69A of the Act, would not result, or would not be likely to result, in any person acquiring or strengthening a dominant position in the market for the provision of medical insurance in New Zealand.

DETERMINATION ON NOTICE OF CLEARANCE

- 23 Accordingly, pursuant to section 66(3)(a) of the Commerce Act 1986, the Commission determines to give a clearance for the proposed acquisition by The Southern Cross Medical Care Society, or a direct or indirect subsidiary of Southern Cross, of all the issued share capital in Aetna Health (NZ) Limited, subject to a written undertaking given by Southern Cross pursuant to section 69A of the Commerce Act, a copy of which is contained in the Appendix to this determination.

Dated this 13th day of October 2000

M J Belgrave
Chair