

ANNEXURE 5.3 CONGLOMERATES AND OWNERSHIP STRUCTURES

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Introduction

1. The HMI assessed the structural relationships between various players in the private healthcare market and, in particular, how these relationships influence the competitive dynamics and market outcomes. The HMI published a research note titled “Cross-ownership and Cross-directorship in the South African Private Health Sector”¹ and invited comments on it.² This note identified possible competition problems related to cross-ownership whereby firms may use their ownership structures to act anti-competitively. In particular the note identified that cross ownership and cross directorship could result in unilateral and coordinated effects amongst competitors. It could also influence the strategic decisions individual firms make so that they do not commercially harm other firms within the conglomerate.
2. For purposes of this analysis, the HMI looked specifically at Remgro Ltd (Remgro) and Afrocentric Investment Corporation Ltd (Afrocentric). The inquiry selected these two groups because the scale and scope of their investment in the private healthcare sector. These two firms may allow the groups to influence the commercial and strategic decisions the management of the firms within the conglomerate take.
3. Remgro forms part of a complex group of companies that have ownership of both MMI Holdings Ltd (MMI Holdings) and Discovery Ltd. These two companies have shareholdings in medical scheme administrators: Discovery Health (Pty) Ltd (Discovery Health) (within the Discovery Group) and Metropolitan Health Corporate (Pty) Ltd (Metropolitan Health), Methealth (Pty) Ltd (Methealth), MMI Health (Pty) Ltd (MMI Health) and Providence Healthcare Risk Managers (Pty) Ltd (Providence Healthcare) within the MMI Group. They are also active in the managed care and broker markets. In addition to this, the Remgro conglomerate has shareholdings in the facility group, Mediclinic International Ltd (Mediclinic).
4. The Afrocentric group owns the administrator, Medscheme Holdings (Pty) Ltd (Medscheme), as well as several managed care companies, pharmaceutical

¹ Research Note published on the HMI website titled ‘Cross-ownership and Cross-directorship in the South African Private Health Sector’.

² The HMI received responses to its research note published on this topic from Afrocentric, ENS Africa on behalf of Discovery Health, Helen Suzman Foundation, MMI Health, RMI and the SA Pharmacy Council.

manufacturers, other medical product manufacturers, distributors of medical products and retail pharmacy outlets.³

5. In this Annexure, the HMI provides a summary of stakeholder comments to the research note and the HMI's findings on the ability of firms to act anti-competitively from cross ownership and cross directorship. We also provide stakeholder comments and the HMI's findings on unilateral conduct, exchange of commercially sensitive information and the change in incentive structures and strategic decisions.

Ability to act anti-competitively from cross ownership and directorship

Stakeholders' views:

6. Stakeholders sought to demonstrate that they did not have the ability to act anti-competitively. MMI Health explained that both MMI Group and Discovery Ltd have numerous subsidiary companies, each with their own board. Each of these companies operate without influence from the holding company. Furthermore, there is no direct shareholding in firms competing in healthcare and that indirect shareholding in healthcare is small and there is therefore no material influence.⁴
7. ENS Africa, who submitted a response on behalf of Discovery Health, stated that neither Remgro nor its subsidiary, Rand Merchant Investment Holdings (RMI), have control over Discovery Health or MMI Group and, because of this, Remgro and RMI did not have the ability to act anti competitively.⁵
8. ENS Africa provides a breakdown on the level of control per shareholder and company. According to ENS, RMI does not control Discovery Ltd as it only holds 25% of its shares. Furthermore, none of Mediclinic's directors serve on the boards of Discovery Life, Discovery Health or MMI.⁶
9. RMI went further to say that it only had a few directors on the boards of MMI (2 of 16) and Discovery Ltd (2 of 22) and that they therefore did not have control over these

³ Research Note published on the HMI website titled 'Cross-ownership and Cross-directorship in the South African Private Health Sector', pg 7.

⁴ MMI Health response titled "*Comments on HMI research note: cross-ownership and cross-directorships in the South African private health sector*" dated 22 June, pg.7.

⁵ ENS Africa's response titled "*Proposed response to the HMI Regarding cross-shareholding and directorship*"¹² June 2017, Submitted on behalf of Discovery Health, pg. 2.

⁶ ENS Africa's response titled "*Proposed response to the HMI Regarding cross-shareholding and directorship*"¹² June 2017, Submitted on behalf of Discovery Health, pg. 7.

boards. However, RMI also stated that it has some influence over high-level commercial and strategic decisions of its investee companies. This, RMI cautioned, does not result in an ability to control decisions on strategy as the ultimate decision makers are the boards. Further RMI does not exercise any operational, financial or strategic control over Discovery Ltd or MMI.⁷

HMI analysis on the ability of stakeholders to act anti competitively

10. Section 12(2) of the Competition Act no 89 of 1998 states that

“A person controls a firm if that person-

(a) Beneficially owns more than one half of the issued share capital of the firm

(b) Is entitled to vote a majority of the votes that may be cast at a general meeting of the firm, or has the ability to control the voting of a majority of those votes, either directly or through a controlled entity of that person;

(c) Is able to appoint or to veto the appointment of a majority of the directors of the firm;

(d) Is a holding company, and the firm is a subsidiary of that company...

(g) has the ability to materially influence the policy of the firm in a manner comparable to a person who, in ordinary commercial practice, can exercise an element of control referred to in paragraphs (a) to (f).⁸

11. While ENS Africa argues that RMI’s shareholding of Discovery Ltd is sufficiently low at 25.01%, the HMI found that the next largest shareholder is the GEPP which holds 8.41%, and the third largest is Adrian Gore at 7.66%. So while 25% is not controlling in the sense or representing a majority, it is significantly larger than the next shareholder. In fact, after RMI, the four largest shareholders combined have around 24% which is less than RMI’s shareholding on its own. It is worth noting that Adrian Gore, together with RMI were founders of Discovery Ltd.

12. Since this is not a competition investigation, but rather an inquiry into the features of the market that affect competition, the HMI has focused on the question of whether the cross-shareholdings, as they are, might provide an opportunity and an incentive to influence decisions in an anticompetitive manor.

⁷ RMI response titled “*Response to the Competition Commission’s cross-ownership and cross-directorships in South Africa private health sector research note*” 30 June 2017, pg.5.

⁸ Competition Act (1998).

Unilateral conduct:

13. This possible competition concern relates to unilateral conduct whereby cross ownership may change the incentive structures of the management of the firms. Firms might voluntarily refrain from fierce competition in order to please the largest shareholder.⁹

Stakeholders views on unilateral conduct:

14. The stakeholders stated that they compete for market share through various means including through their wellness programs, MMI Multiply (Pty) Ltd (Multiply) and Discovery Vitality (Pty) Ltd (Vitality).¹⁰ Afrocentric sought to illustrate the extent of competition between the administrators by pointing to its complaint it made to the Competition Commission and then the Competition Tribunal in relation to Discovery Health and tariff negotiations.¹¹

15. MMI Health stated that if the HMI's cross directorship note was correct, then we would not see such competition between MMI Group and Discovery Health through the tender process. MMI Health went on to say that Metropolitan Health lost its administration contract with Bankmed to Discovery Health and the impact of this was significant.¹² Both RMI and ENS Africa provided examples to illustrate why they believe unilateral conduct was unlikely to be a concern. RMI explained that the boards of directors are the ultimate decision makers and RMI has no control of boards. There could be a concern if, for example, MMI group had a financial interest in the performance of Discovery Ltd and/ or vice versa.¹³ ENS stated that tendering for restricted medical scheme business is fiercely contested by numerous administrators and that there was no certainty that either MMI or DH would secure the contract.¹⁴ RMI pointed out that if Discovery Health or administrators within the MMI group lost a

⁹ Research Note published on the HMI website titled 'Cross-ownership and Cross-directorship in the South African Private Health Sector', pg 5.

¹⁰ MMI Health response titled "*Comments on HMI research note: cross-ownership and cross-directorships in the South African private health sector*" dated 22 June, pg.4.

¹¹ "*Afrocentric Investment Corporation Ltd's representations to the Health Market Inquiry of the Competition Commission re Research Note on Cross-Ownership and Cross-Directorships*", pg. 21 and 22.

¹² MMI Health response titled "*Comments on HMI research note: cross-ownership and cross-directorships in the South African private health sector*" dated 22 June, pg.5.

¹³ RMI response titled "*Response to the Competition Commission's cross-ownership and cross-directorships in South Africa private health sector research note*" 30 June 2017, pg.5.

¹⁴ ENS Africa's response titled "*Proposed response to the HMI Regarding cross-shareholding and directorship*"¹² June 2017, Submitted on behalf of Discovery Health, pg. 6.

sale, there was no guarantee that the lost sale would divert to the other and the lost sale could go to Medscheme. Furthermore, there was no guarantee that any gains from their behaviour would flow to RMI or other shareholdings. The listed entity could hold the gains or use them elsewhere in the business. Similarly, RMI would be unable to increase prices or restrict output at MMI Group and Discovery Ltd simultaneously as RMI does not have the required level of control over both to achieve this.¹⁵

16. Both MMI Health and ENS Africa spoke about MMI Health and Discovery Health's relationship with Mediclinic. MMI Health explained that there were no common directors between it and Mediclinic. MMI and ENS Africa argued that Remgro and RMI have no influence in the various negotiations with Mediclinic and that they procured services from Mediclinic based on a competitive rate after intense negotiations.¹⁶ Discovery Health's key objective is to get the lowest possible price for its open medical scheme, Discovery Health Medical Scheme (DHMS), in order to be more competitive in the open medical scheme market.¹⁷

The HMI's analysis on unilateral conduct:

17. The HMI agrees with the stakeholders that Discovery Health, MMI Group and Medscheme compete to attract members to their open medical schemes and to win restricted schemes' tenders to provide administration/ MCO services. As discussed in Chapter 5 titled "Funders" many medical schemes can and some do switch between administrators. When Metropolitan Health lost the South African Service Medical Scheme (Polmed) contract to Medscheme, RMI (as a conglomerate) lost the revenue that Polmed generated. Furthermore, the HMI found that the loss of Polmed and Bankmed has had a significant impact on Metropolitan Health's business.
18. The HMI is of the view that the risk for Discovery Health or MMI Group of losing medical schemes to Medscheme or, for that matter another administrator, is true in the case of restricted medical schemes. In the open medical scheme environment, the strong relationship between Discovery Health and DHMS makes it very unlikely that DHMS will switch administrators, even if Discovery Health increases its

¹⁵ RMI response titled "*Response to the Competition Commission's cross-ownership and cross-directorships in South Africa private health sector research note*" 30 June 2017, pg 6.

¹⁶ MMI Health response titled "*Comments on HMI research note: cross-ownership and cross-directorships in the South African private health sector*" dated 22 June: pg.4 and ENS Africa's response titled "*Proposed response to the HMI Regarding cross-shareholding and directorship*" 12 June 2017, Submitted on behalf of Discovery Health, pg 6.

¹⁷ ENS Africa's response titled "*Proposed response to the HMI Regarding cross-shareholding and directorship*" 12 June 2017, Submitted on behalf of Discovery Health: pg. 6.

administration fees beyond a competitive level. Similarly, Momentum Health is very unlikely to leave MMI Health and neither MMI Health nor Discovery Health are likely to take on another open medical scheme. The HMI is of the view that it is likely these administrators are already charging the maximum administration fee that they can. Therefore the ownership link to RMI is unlikely to have a significant influence when it comes to open medical schemes.

19. When considering the incentives for RMI to influence the behaviour between MMI Group, Discovery Health and Mediclinic, the inquiry had to consider how and why this would happen. Firstly, the shareholders of Mediclinic would be able to increase its profit if it could charge higher prices to the MMI/ Discovery Health medical schemes. This would result in the medical schemes increasing their membership premiums. In the restricted medical scheme market, some of the schemes may switch to Medscheme or another administrator. The gains in profit for Mediclinic would be lost through loss of medical schemes. In the open medical scheme market, we know that DHMS will not change administrators. But DHMS/ Momentum Health members may switch to open medical schemes. Bear in mind that the second largest scheme is Bonitas, whose administrator is Medscheme, and Bestmed is the fourth largest open medical scheme and neither are within the Discovery Health / MMI Group conglomerate. If enough members switch, then the group as a whole will lose revenues.
20. Another scenario could be that Mediclinic gives Discovery and MMI Group lower tariffs than the other medical schemes and administrators. The idea here is that consumers' benefit through lower monthly premiums and the administrators benefit from more members joining their medical schemes and that they win more tenders. Ultimately this would benefit the consumers so would not be a concern to the HMI.

Exchange of commercially sensitive information:

21. The HMI's research note stated that cross ownership of firms with related commercial interests may increase the risk of exchange of competitively sensitive information. This may facilitate price collusion.¹⁸ The stakeholders sought to illustrate why anticompetitive information exchange is unlikely.

¹⁸ Research Note published on the HMI website titled 'Cross-ownership and Cross-directorship in the South African Private Health Sector', pg 4.

Stakeholders views on the exchange of commercially sensitive information:

22. Afrocentric argued that information sharing and collusion was unlikely in the administrator market due to the high contestation in terms of delivering the best service and value for money.¹⁹
23. MMI Health said that there were no common directors between competing firms so they could not exchange competitively sensitive info. Furthermore, MMI Holdings and Discovery Ltd are listed companies and are subject to strict rules and the King IV Code on Corporate Governance.²⁰ RMI and ENS Africa explain that the type of information that board members get was not of the nature that would facilitate collusion or restrain capacity and volumes.²¹

HMI analysis of exchange of commercially sensitive information:

24. The HMI found that, as discussed already, the administrators within the same conglomerate compete against each other to win tenders to provide administration services. For example, Discovery Health and the administrators within the MMI group compete to win tenders for restricted medical scheme business. These administrators also compete to attract potential members to their open medical schemes within their administration. As such, the HMI is of the view that it seems unlikely that they would engage in collusive behaviour.

Change in incentive structure and strategic competitive decisions:

25. The research note's third theory of harm is that that "cross-ownership structures may increase the ability to influence or control the strategic competitive decisions of a (partially) co-owned firm".²² Financial investors with minority holdings may influence the decisions of the management of firms even without representation on the respective boards.

¹⁹ "Afrocentric Investment Corporation Ltd's representations to the Health Market Inquiry of the Competition Commission re Research Note on Cross-Ownership and Cross-Directorships", pg. 20.

²⁰ MMI Health response titled "Comments on HMI research note: cross-ownership and cross-directorships in the South African private health sector" dated 22 June, pg. 6.

²¹ RMI response titled "Response to the Competition Commission's cross-ownership and cross-directorships in South Africa private health sector research note" 30 June 2017: pg. 10, and ENS Africa's response titled "Proposed response to the HMI Regarding cross-shareholding and directorship" 12 June 2017, Submitted on behalf of Discovery Health, pg. 7.

²² Research Note published on the HMI website titled 'Cross-ownership and Cross-directorship in the South African Private Health Sector', pg. 5.

Stakeholders views on change in incentive structure and strategic competitive decisions

26. RMI said that it has some influence over high level commercial and strategic decisions of its investee companies. RMI also argued that this influence does not result in its ability to control decisions on strategy as the board of directors were the ultimate decision makers.²³ Furthermore, the board of directors of listed companies do not make decisions regarding competitive strategy at the level of pricing, products and value propositions.

The HMI's analysis on changes in incentive structures and strategic decisions:

27. The HMI found that stakeholders did not elaborate much on this point of possible strategic effects of cross-ownership and cross-directorship structures in their responses. Also in our multiple engagements with the administrators, we found that funders focus on the downstream (consumer) market. Funders' innovations seem to focus on strengthening the corporate brand and target the younger and healthier members. In a competitive third party payer system, where consumers are able to fully compare product offerings, the HMI would expect to find significant strategic innovative initiatives that focus on improving the value of the funder's offering on healthcare to the benefit of the members. These initiatives, for example, could focus on more cost effective formulas of the provision of healthcare such as the introduction and large-scale implementation of performance (costs, quality) related remuneration models.

28. As another example, large medical schemes could have been expected to integrate into the provision of healthcare on a non-profit basis, as we have seen in international markets in Europe and the US. Also we would have expected medical schemes and administrators to endorse the provision of integrated care around maternity or eye-care as we have witnessed in countries like India.²⁴

29. Other types of strategic decisions administrators and facility groups could make is around ARMS and entering into different innovative types of models to purchase healthcare which are well established in international markets. While there are some alternative and risk sharing reimbursement models in South Africa, by far most reimbursement tends to be fee-for-service. The HMI interprets this as a signal of a

²³ RMI response titled "Response to the Competition Commission's cross-ownership and cross-directorships in South Africa private health sector research note" 30 June 2017, pg 2.

²⁴ Transcript, 03 May 2016, pg 10-12.

lack of appetite from both providers and funders in this regard. The HMI is therefore of the view that companies may behave strategically so as to not upset the overall balance in the conglomerate.

Conclusion on cross ownership and cross directorship

30. The HMI has not found any concrete anticompetitive conduct stemming from the ownership structures. However the structure of cross holdings carries some risks for the long-term development of a healthy competitive environment. This is particularly a concern where MMI Health and Discovery Health may lack incentives to pursue innovative long term strategies in their purchasing of healthcare due to the existence of Mediclinic within the broader group.