30 June 2014

Ms Itebogeng Palare
Competition Commission
Office of the Commissioner
3rd Floor
Mulayo Building
The DTI Campus
Pretoria

By email: ItebogengP@compcom.co.za

Dear Ms Palare

Market Inquiry into the Private Healthcare Sector –
Comment on Draft 'Statement of Issues' and 'Guidelines for Participation'

INTRODUCTION

1. Discovery is most appreciative of the open and consultative stance adopted by the Panel of aforementioned Inquiry. We believe this augurs well for the process of conducting the Inquiry as well as the formulation of the final recommendations.

2. It is in this spirit that Discovery Health (Pty) Ltd (herein referred to as "Discovery") hereby submits the following comments on the Draft 'Statement of Issues' and 'Guidelines for Participation' issued on 3 May 2014.

3. The comments below serve to draw the attention of the Panel to potential areas of concern that we respectfully submit may not be fully recognised or dealt with in these documents, or to request clarity on certain aspects contained therein.

PART A – Comment on 'Statement of Issues'

4. Discovery is in broad agreement with the general approach of the Panel in developing a "Statement of Issues" to convey potential theories of harm, and with the overall scope of matters addressed in the Statement of Issues. We agree that the inclusion of non-medical scheme health insurance and the public sector would allow the Panel to understand broader relationships and factors influencing costs other than those contained within medical schemes and medical scheme administrators.

5. The framework adopted in paragraphs 5 to 9 of this document, segments the healthcare market into three sub-markets (healthcare financing, healthcare providers and consumables) and seeks to investigate four potential sources of harm to competition, namely market power, barriers to entry into a market, imperfect

information and the regulatory framework. Discovery is in agreement herewith. However we do wish to note that we see the Panel's focus on the features of the private healthcare sector that prevent, distort or restrict competition as a necessary but not sufficient perspective in understanding the "level of prices, expenditure and costs in the sector as well as the reasons for the above-inflation increases in prices in healthcare" (see paragraph 15).

6. Competition, or lack thereof, is but one of several factors that may influence the functioning of healthcare markets and hence healthcare costs and inflation. For instance, supply side factors such as the introduction of new healthcare technologies may drive up costs, without necessarily resulting from factors that prevent, distort or restrict competition. Similarly, demand side factors such as a deterioration in the demographic profile and an increasing disease burden in the insured population due to underlying epidemiological factors could likewise be a critical factor in explaining cost increases, but may not be at all related to competitive forces or factors. For these reasons, we believe that it is essential that, in addition to the current envisaged approach, the Inquiry also seek to investigate the impact of the structure of healthcare delivery in the SA private healthcare system, the regulatory framework for healthcare financing, and the incentives of various role players and stakeholders within private healthcare, over and above competition related issues. We believe that only once this broader picture is understood will the Panel be in a position to accurately understand all of the drivers of healthcare cost levels and inflation, as well as to evaluate the specific contribution of competition, or lack thereof, to these costs and inflation.

A suggested addition to the current approach

7. Our interpretation of the Terms of Reference, read together with the additional document from the Panel, is that the Panel will allow considerable scope for investigation into all of the factors affecting the level of prices and inflation, and will not solely focus on competition issues. We welcome this approach, and believe it to be essential to the success of the Inquiry.

8. In the document from the Panel there are requests for advice on the prioritisation of investigations and efforts. The approach outlined in paragraph 19 makes sense, namely to adopt a prioritisation on criteria which involve the relative importance of factors explaining costs, affordability, access, innovation and quality, as well as the promotion of competition and sustainability in the sector, in addition to practical resource requirements and the availability of data and information.

9. Our suggestion in this context is that the explicit initial focus of the Panel be on answering questions about inflation in the cost of medical scheme cover, and the various factors driving this. In our view this will give immediate guidance on the relative importance and contribution to inflation of different elements of healthcare delivery and financing. This in turn, will assist greatly in prioritising investigations, as mentioned in paragraph 38. An understanding of why the graph on page 6 of the document from the Panel looks the way that it does will highlight not only inflationary and competitive factors within medical schemes, but also relevant nodes of interaction and influence with and by external sectors, such as health insurers not registered as medical schemes, the public sector and regulators. It will also highlight how consumers' out

of pocket expenses interact with the inflationary factors inherent within medical schemes. In addition, the explanation of inflation will also highlight how the structure of healthcare delivery and financing, as well as the regulatory framework, impact on costs and competition.

10. Our recommendation is therefore that medical inflation and its driving factors, defined in the first instance as the rate of increases in medical scheme contributions, be investigated as a first priority, and that this in turn will help to prioritise the rest of the investigation into all of the other matters of interest to the Panel.

11. In terms of the six theories of harm as considered by the Panel, our comments above indicate that serious consideration should be given to other structural facets of this system that lead either to high pricing levels or high rates of increase in prices. While such features may not in themselves lead to a direct impact on market power, barriers to entry or other competition consequence, they do directly and indirectly influence both levels of prices and their rates of increase, sometimes via competitive effects and at other times through other systemic effects.

12. In the light of this, Discovery proposes that a seventh theory of harm be added to give appropriate consideration to the structural peculiarities of the South African healthcare market, where these give effect to a price-inflationary effect in the market, without necessarily having a direct impact on any of the four categories of potential sources of harm. This theory of harm could be named "structural factors in the healthcare system".

13. This aspect was explicitly recognised by the Commission in the Terms of Reference, and recognition of it does appear in some sections of the Statement of Issues, but at the same time Discovery believes it is appropriate that the Statement of Issues highlights this as a fundamental aspect affecting competition and medical inflation, through designating this as a potential theory of harm.

14. Some examples of structural issues are -

    14.1 the market entry, uptake and utilisation of high-technology devices or new medicines. Over the last decade there have been an increasing number of high-technology biological medicines and new devices which although beneficial for individual patients, are adding significant cost pressures for medical schemes, and are therefore having a significant inflationary impact in the market.

    14.2 the specific modalities of delivery of hospital care (strong bias towards all purpose inpatient hospitals, relatively few day surgery and specialised high volume surgery centres), and the history of how private hospital care developed in South Africa.

    14.3 the role of GPs in healthcare delivery, and how they interact with Specialists, and how the relative role of these two categories of health professional have changed over time.

    14.4 the dynamics within and between corporatized specialist services, such as radiology and pathology, and other specialist services.

14.5 the role of logistics fees, marketing and related fees, and dispensing fees within the Single Exit Price for medicines.

15. Both the Terms of Reference (section 3 entitled *"Rationale for a Market Inquiry"*) and the Statement of Issues (paragraphs 14 -16) are strongly premised on the theory that possible barriers / inefficiencies in competition have led to high medical inflation in the private sector. In our view, this makes it imperative that the Inquiry informs itself of the full range of drivers of inflation in this sector; in order to "arrive at a factual basis to make evidence-based recommendations" on competition as such. Inclusion of an investigation into structural factors such as mentioned above, and an initial focus on the explanation and understanding of medical inflation, will help greatly in constructing an appropriate framework for the evaluation of the role of competition.

Specific Comments on the 'Statement of Issues' document

16. Paragraph 43 defines pharmaceuticals and other medical products as part of one category, named "consumables". Further paragraphs within the Theories of Harm seek to understand the relationship between different segments of the healthcare market and the suppliers of consumables. Discovery believes that this approach is not adequate to fully probe the possible impediments to efficient market functioning and competition within the pharmaceutical sector. The Commission should explicitly seek to understand the inter-relationships in the supply chain for pharmaceuticals and other medical products, including the role of logistics fees, marketing and related fees, and dispensing fees.

17. Paragraph 51 invites stakeholders to make submissions on appropriate techniques to be employed in the division of markets and the analysis of competition. It is not clear if these submissions are to be made prior to the August 1 period for formal submissions, or at the same time. As an example, Discovery has developed a methodology for defining health regions based on patterns of consumption of health services by Discovery clients. These are not co-terminous with the geographic definition of provinces, nor service delivery regions as defined by the Department of Health. Instead, they are based on analysis of data on where individual patients access primary and tertiary care in the private sector. It is agreed that the definition of relevant markets is an important first step (paragraph 48); hence it would seem advisable that questions of methodology are addressed early on in the Inquiry. This technique of defining health regions may play an important part in the analysis of inflation and cost differentials between these different regions, and as such is an integral part of an explanation of inflationary factors – and in our view another reason for an initial focus on inflation.

18. Paragraph 52 -54 proposes six theories of harm to be used in assessing competition in private healthcare. It is proposed that this guideline be supplemented with a seventh category of issues, which for expediency may be referred to as "Structural issues in the healthcare system", by which we mean the current structure of private healthcare delivery and the history of how it developed into its current state.

19. Paragraph 58 suggests that health financing market power relations could include the market power of medical scheme administrators over medical schemes. It seems incomplete not to also list the market power of medical schemes over medical scheme administrators. In the same paragraph, there is also no reference to health insurers, and in particular the way in which various health insurance products could result in distortions in the healthcare market.

20. Paragraph 59 suggests an examination of market power of health facilities in relevant geographic markets. It is recommended that this definition be cognisant of relevant health regions as derived from analysis of patients' regional access to primary and tertiary health facilities.

21. Paragraph 60 lists the potential distortions of competition in relation to healthcare facilities. It is recommended that this section includes the provision of "other distortions which include a misalignment of incentives between facilities and consumers" (as contained in paragraph 57). A similar additional clause is required for paragraph 61, relating to healthcare practitioners.

22. Paragraph 61 should include the following additional bullet points -
    - Market power of corporate specialist practitioner practices.
    - Distortion of competition due to practice models that support undue fragmentation of care.

23. Paragraph 63 and 65 should each include the bullet point below -
    - Contractual or informal arrangements between healthcare facilities / healthcare practitioners and suppliers of medicines and medical devices.

24. Paragraph 67 should include a bullet point on imperfect information as it relates to consumer wellness, as suggested below -
    - Consumer information relating to wellness and avoidable medical intervention.

25. Paragraph 69 should be explicit about the priority regulatory areas to explore for possible distortions in competition. These include the Ethical Rules of the HPCSA; Prescribed Minimum Benefits and solvency regulations under the Medical Schemes Act and Regulations; and the lack of a completed legal framework for open enrolment and social solidarity in the medical schemes environment. An important area to explicitly include in this paragraph is the Single Exit Price legislation and its possible unintended consequences in reducing competition.

PART B – Comment on "Guidelines for Participation"

26. At the outset we advise that we consider the Guidelines to be sensible and procedurally fair.

27. We note that it is not intended for the Inquiry to be an adversarial process. Rather, participants will provide written and oral submissions to the Panel, who may then ask various questions (again in writing or orally). It is noteworthy, however, that, although the questions directed towards a witness will largely be from the Panel itself, paragraph 23.9 of the Guidelines provides that the Chairperson may allow participants to question witnesses, directly or through the Chair as the Chairperson considers appropriate in the

circumstances, in order to allow for proper ventilation of information on contested issues. Leave to question a witness must be sought on sufficient and reasonable notice to the Chairperson, stating the reasons for the request. In this regard we consider it appropriate that the document be amended to set out a procedure including timelines incorporating advanced warnings to answer questions and a procedure for identifying the subject matter of the question(s) and identity of the person/entity posing the question(s).

28. In addition it is noted that parties will be able to address issues raised by other participants through their own submissions. It is for this reason that we recommend that the Guidelines include specific provision for public access to the written submissions of other parties (having removed confidential information before making same available) immediately upon closing of the date for submissions.

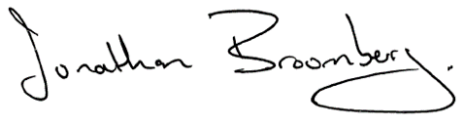
29. Consideration should also be given, in our view, to permit parties to submit supplementary submissions at a convenient point in proceedings, possibly before the Panel adjourns to compile its provisional report. We believe that this will enrich the process.

30. Finally, we note that the Panel intends to publish provisional findings and recommendations during October 2015. Given the gravity and potential implications thereof it is recommended that the Guidelines make provision for a period for comment on the provisional findings before they are made final.

CONCLUSION

31. We trust that these comments are helpful to the Inquiry and advise we are available for further elaboration should the need arise.

Yours sincerely



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