IN THE COMPETITION APPEAL COURT

CASE No.: 55/CAC/Sept05

In the matter between:

MEDICROSS HEALTHCARE GROUP (PTY) LTD — **First Appellant**

PRIME CURE HOLDINGS (PTY) LTD — **Second Appellant**

and

THE COMPETITION COMMISSION — **Respondent**

JUDGMENT

MHLANTLA, AJA: A.

INTRODUCTION

[1] On 15 September 2005 the Competition Tribunal ("the Tribunal") prohibited a merger between the first and second appellants on the basis that the said merger was likely to lead to a substantial lessening of competition. The appellants immediately noted an appeal to this Court against the said decision. The appeal was heard on 7 December 2005. On 31January 2006 the appeal was upheld. This Court set aside the order of the Tribunal and replaced it with an order that the merger be approved unconditionally. I now set out the reasons for the order.

B. FACTUAL BACKGROUND

[2] The primary acquiring firm is Medicross Healthcare Group (Pty) Ltd, the first appellant herein. The shares in the first appellant are owned by Network Healthcare Holdings Limited (80%) and Netpartner Investments Limited (20%). The primary target firm is Prime Cure Holdings (Pty) Ltd, the second appellant. Its shareholders are Brait Private Equity (34,2%); Praxis Private Equity (29,30%); CDC Financial Services Mauritius Ltd (11, 3%); Total Support Management (Pty) Ltd (8,22%) and other minority shareholders (16,95%). The first appellant intends to acquire the entire issued share capital (together with the shareholders' claim and loan claims against) in the second appellant. The total purchase consideration is R85 million.

[3] On 5 March 2005 the merger was notified to the Competition Commission in terms of section 13A of the Competition Act 89 of 1998 ("the Act") as a large merger. On 30 June 2005 the Commission recommended to the Tribunal that the proposed merger be prohibited. A hearing before the Tribunal was conducted where various witnesses were called by the appellants, the respondent as well as the Tribunal respectively. At the end of the hearing the Tribunal concluded that the horizontal dimensions of the merger were likely to lead to a substantial lessening of competition in the relevant market. It is against this decision that the appellants have appealed to this Court.

[4] It is apposite at this stage to set out the relevant provisions dealing with mergers. Section 12A of the Act provides:-"(1) Whenever required to consider a merger, the Competition Commission or Competition Tribunal must initially determine whether or not the merger is likely to substantially prevent or lessen competition, by assessing the factors set out in ss (2); and-(a) if it appears that the merger is likely to substantially prevent or lessen competition, then determine-(i) whether or not the merger is likely to result in any technological, efficiency or other pro-competitive gain which will

> be greater than, and offset, the effects of any prevention or lessening of competition, that may result or is likely to result from the merger, and would not likely be obtained if the merger is prevented; and
>
> (ii) whether the merger can or cannot be justified on substantial public interest grounds by assessing the factors set out in subsection (3); or

(b) Otherwise, determine whether the merger can or cannot be justified on substantial public interest grounds by assessing the factors set out in subsection (3).

(2) When determining whether or not a merger is likely to substantially prevent or lessen competition, the Competition Commission or Competition Tribunal must assess the strength of competition in the relevant market, and the probability that the firms in the market after the merger will behave competitively or co-operatively taking into account any factor that is relevant to competition in that market, including/-(a) the actual and potential level of import competition in the market;

b)the ease of entry into the market, including the tariff and regulatory barriers;
c)the level and trends of concentration, and history of collusion, in the market;
d)the degree of countervailing power in the market;
(e) the dynamic characteristics of the market, including growth, innovation, and product differentiation;
(f) the nature and extent of vertical integration in the market;
(g) whether the business or part of the business of a party to the merger or proposed merger has failed or is likely to fail; and

(h) whether the merger will result in the removal of an effective competitor.

(3) When determining whether a merger can or cannot be justified on public interest grounds, the Competition Commission or Competition Tribunal must consider the effect that the merger will have on:-(a) a particular industrial sector or region;

(b) employment;

c)the ability of small businesses, or firms controlled or owned by historically disadvantaged persons, to become competitive; and

d)the ability of national industries to compete in international markets.

C. **RECOMMENDATIONS OF THE RESPONDENT.**

[5] After analysing the submissions by the parties as well as additional information, the respondent identified only three firms that were competing in the market for managed care services that have a national network of service providers namely, Prime Cure, Medicross and Carecross. It did not support the parties' contention of the existence of other players and their ability to enter the market with ease.

[6] The respondent found that the proposed merger would strengthen the Netcare group and will reduce the number of players from three to two. According to the respondent the proposed merger would significantly concentrate the market for the provision of managed care services and eliminate a likely potential entrant into the bottom segment of the market. This would reduce the choice of medical aid schemes to enter into capitation agreements with managed care companies. The respondent concluded thus:

> "[T]he market in which the parties compete is highly concentrated. The barriers to entry into this market are immensely challenging and

> according to Prime Cure extremely high. Sustainable and successful market participants are few and far between. According to the Commission the likely entry into the market by other firms are highly speculative and unlikely to occur. Considering all of the above the Commission is of the view that the transaction is likely to substantially prevent or lessen competition in the manager healthcare market with a national network of service providers."

[7] The respondent went on to say:

> "Furthermore, the Commission is of the view that the transaction raises significant public interest concerns relating to the industry as a whole and the effect that the transaction is likely to have on small business and businesses controlled by historically disadvantaged persons."

[8] The respondent then considered the efficiency defences raised by appellants. It concluded that these did not outweigh the effects of the likely prevention or lessening of competition. It also considered the public interest issues and concluded that the transaction could not be justified on public interest grounds .

[9] The respondent thus recommended that the merger be prohibited.

D. **FINDINGS OF THE TRIBUNAL**

[10] It has not proved easy to isolate the essential reasoning upon which the Tribunal's determination is predicated. The following summary seeks to read its key findings in the best possible light. The Tribunal commenced its determination of whether the merger was likely to substantially prevent or lessen competition (s 12A (2)(e) of the Act) with an analysis of the "general state of healthcare provisioning in South Africa the policy objectives of the South African government in the realm of healthcare provision, the mechanisms whereby government intends achieving those objectives and the place and role of the private section…".(para 51). It concluded its analysis thus:

> " It is our view then, that in this extremely fluid context , the absence of an established and stable regulatory framework for this embryonic market as well as for some related and long-standing markets (for example, pharmaceuticals) demands that we adopt a particularly cautious and circumspect approach to private interventions, such as this merger, that will inevitably impact on the development of the market under consideration. Public interest considerations impinging on the outcome of interventions in this area- be they interventions by the State, by regulators or by private market participants- are, for unimpeachably good reason unusually intense and this also predisposes us to particular circumspection."

[11] The Tribunal found that the relevant product market was that for the provision of capitated primary managed health care products with a national geographic market. The definition of capitated managed primary care employed by the Tribunal was "a method of payment for health services in

which a provider is paid a fixed, per capita, amount in advance for each enrolee without regards to the actual number of nature of services provided to each member in advance. This involves a great deal of risk sharing" (para 109)

[12] The Tribunal thereafter examined the impact of the merger on competition and found that the horizontal dimensions of the merger were likely to lead to a substantial lessening of competition in the relevant market. In particular, it held that the barriers to entry were formidable. The merger would serve to increase concentration, and in effect reducing the three viable competitors to two, being first and second appella nts and Carecross. Accordingly, the Tribunal found that "the removal of a rival – Prime Cure – to Netdirect and Medicross, increases the likelihood of a relationship between Netcare, on the one hand, and Mediclinic and Life Healthcare on the other and certainly aggravates our concerns regarding the future state of competition in a vital related healthcare market". (para 188). The Tribunal went on to hold that the merger stood to be prohibited on its horizontal dimensions which were likely to lead to a substantial lessening of competition in the relevant market. It found however that there was insufficient evidence to establish that 'the vertical integration that characterises Netcare distorted referrel patterns were sufficient to justify a conclusion that a substantial lessening, of competition would occur on vertical grounds.

[13] The Tribunal prohibited the merger, having found that the claimed efficiency grounds did not outweigh the costs competitive effects of the merger.

E. **<u>SUBMISSIONS BY THE PARTIES.</u>**

[14] At the hearing of the appeal, Mr Unterhalter, who appeared with Mr Cockrell for the appellants, submitted that the Tribunal misdirected itself in that it adopted a "cautious and circumspect approach" to the merger; that is it had conflated public interest grounds with its primary task, that is an enquiry as to whether there was a likelihood that the merger would substantially lessen competition.

[15] Mr Unterhalter contended that the misdirection vitiated the Tribunal's decision and that the appeal should succeed. He submitted that there was no textual support in the Act for a conflation of public interest considerations with the predictive task mandated by the Act. He contended that the need to consider "public interest grounds" comprises a separate and subsequent enquiry to the primary determination as to whether or not the relevant merger is likely to substantially prevent or lessen competition. Referring to paragraph 71 of the Tribunal's reasons where it was stated that "public interest considerations" predisposed the Tribunal to particular circumspection when considering this merger, he submitted that the Tribunal at no stage had proceeded to a detailed "second order analysis" in order to consider whether the merger could or could not be justified on public interest grounds within the meaning of section 12A(3) of the Act. On the contrary, the Tribunal had regard to public interest considerations *at the first stage of analysis* for the purposes of determining whether the merger is like ly to substantially prevent or lessen competition.

[16] Mr Unterhalter further contended that the public interest grounds which the Tribunal purported to consider in its determination did not fall within the ambit of sectio n 12A(3). The Tribunal had noted "Pertinent to our consideration of the general state of healthcare provisioning in South Africa, the policy objectives of the South African government in the realm of healthcare provision, the mechanisms whereby government intends achieving those objectives, and the place and role of the private sector, including the merging parties and many others who participate in these hearings, in this wider context" (para 51). Mr Unterhalter submitted that the public interest concerns which appear to have coloured this approach were not concerns which the Tribunal was mandated to consider at this stage of its enquiry. The mechanisms by which Government intends to achieve its policy objectives and the place and role of the private sector in these objectives are issues which fall within the purview of Parliament and the Executive; they are not issues that fall within the remit of the competition authorities.

[17] Mr Berger, who appeared on behalf of the respondent, submitted that the Tribunal had conducted a careful and detailed analysis of the evidence. The Tribunal did not purport to adopt an approach that assessed whether the merger was likely to substantially prevent or lessen competition against the factors set out in section 12A(3) of the Act or any other public interest considerations. He thus contended that no misdirection had been committed by the Tribunal, alternatively; if such misdirection was found, this Court

ought to assess the evidence placed before the Tribunal and make an order in terms of section 17(2) and/or section 17(3) of the Act.

[18] Accordingly the question arises as to the proper approach to the enquiry mandated by s 12A of the Act. In Schuman Sasol SA (Pty) Ltd v Price's Daelite (Pty) Ltd [2001-2002] CPLR 84 (CAC) at 90d this Court said the following:

> "The approach which this Court adopts to an appeal against the decision of the Tribunal in respect of a merger should take cognisance of the composition and role of the Tribunal as a specialist body which consists not only of lawyers but also of members possessed of the necessary financial and economic knowledge and thorough grasp of the relevant policy issues required in these kind of deliberations. Section 12A requires that the Tribunal make a determination after a holistic inquiry into whether the proposed merger is likely to substantially prevent or lessen competition. In assessing such a decision, this Court should take account of the composition and expertise of the Tribunal as well as the nature of the enquiry which entails an element of probabilistic investigation into the effect of the proposed merger .... In its decision as to whether to set aside, amend or confirm the decision of the Tribunal, this Court must be cautious before imposing its own conception of the policy considerations upon the decision adopted by the Tribunal . The Court should seek rather to examine and test rigorously the justifications offered by the Tribunal for the decision to which it has arrived before it invokes its power in terms of section 17."

This **dictum** made it clear that this Court recognizes the expertise of the Tribunal with regard to the evaluation of economic evidence and the development of a sound policy framework which informs this evaluation. However, recognition of the specialist role of the Tribunal does not mean that the Court should not test whether the evidence led can justify the

conclusion reached by the Tribunal nor should this Court be deferential to the manner in which the Tribunal engages with the interpretation of the structure of the Act or the mandated legislative tests.

[19] Within the context of mergers, section 12A provides for a two stage analysis. The first phase involves the determination by the Tribunal whether the merger is likely to substantially lessen or prevent competition, having regard to the evidence and argument presented before it by the respondent and the parties. The inquiry is conducted by assessing the factors set out in section 12A(2). The word likely has its prime meaning of "probability" whilst the word "substantially" means materially or considerably in amount or duration.

[20] The manner in which the Tribunal justifies its finding on the evidence before it is of critical importance. In Mondi Ltd and Kohler Cores and Tubes v Competition Tribunal [2003] 1 CPLR 25 (CAC) at 33c, this court said:

> " The decision required by section 12A(1) must be made on evidence which is available to the Tribunal. In other words the Tribunal cannot base its decision upon speculation of a kind which cannot be attributed to any evidential foundation placed before the Tribunal. But the prohibition against unjustified speculation should not be confused with the need for a predictive judgment. The section enjoins the Tribunal to forecast a likely possibly, that is, it makes a predictive judgment, based on evidence which has been placed before it."

[21] It follows therefore that if the Tribunal finds on the evidence available that the merger is capable of having the anti-competitive effect

contemplated, the test would have been satisfied. However, the Tribunal can only move to the second stage after it has made this finding.

[22]In the present case, the Tribunal adopted a "cautious and circumspect" approach based, to a considerable extent, on public interest considerations. As the Tribunal observed:

> "we are, to state the obvious, dealing with a transaction in a market that is central to the interests of the state, to the private sector and to ordinary consumers. It may well be that in a year's time, or, more likely, in five years' time, the regulatory framework and the parameters of the markets implicated in this transaction will be more certain and that the consideration of an identical or similar transaction will produce a different outcome. However, it is in the nature of merger analysis that changing eras and contexts produce different outcomes. There is no single answer that stands for all time" (at para 72).

[23] It is extremely difficult to determine the weight which the Tribunal gave to these public interest grounds. in its probabilistic enquiry. But, as I have already said, these issues should have been of no relevance to the first stage of its enquiry which needed to examine the evidence relating to the proposed merger's impact upon competition. These public interest considerations would have been more appropriately considered during the second phase in terms of section 12A(3), as the need to consider public interest grounds is a separate and subsequent enquiry to that of the primary determination.

[24] In the result, the Tribunal misdirected itself by adopting an incorrect test when assessing the evidence. It failed to engage fully with the probabilistic enquiry of the evidence presented before it. It failed to apply the test set out in section 12A(1) and (2) before considering the public interest grounds. In the result, this Court is at large to assess the evidence that was placed before the Tribunal and make an order in terms of section 17 of the Act. It is to that evidence that I now turn.

Definition of the relevant market

[25] The assessment of the effects of the merger on competition must be preceded by a proper definition of the relevant market. The need for market analysis must be viewed within the context of the S 12A(1) of the Act which uses the phrase 'likely to substantially present or lessen competition' In this case, the Tribunal found that there would be a 'lessening of competition'. Such a conclusion requires a full market analysis. By contrast, 'preventing competition appears to concern impediments or hindrances which retard or keep back that which might otherwise have happened. An enquiry about impediments may well have allowed the Tribunal to escape an engagement with a comprehensive market analysis. However its finding was based on a lessening of competition; hence an analysis of the market is essential to this enquiry.

[26]There is a dispute between the parties in regard to the definition of the market. The Tribunal found that the relevant product market is the market for the provision of capitated primary managed healthcare products. Mr

Unterhalter submitted that the Tribunal restricted the market definition to the provision of capitated primary managed health care products and failed to recognise that a number of other primary managed care options are substitutable for managed care options . He contended that the Tribunal ought to have found that the relevant market is the market for the provision of primary managed healthcare products for low cost medical schemes, irrespective of whether or not the products are capitated. Mr Berger on the other hand argued that the focus ought to be on the contractual arrangements between managed care organisations and medical schemes when defining the relevant market.

[27] It is apposite at this stage to provide a brief overview of the medical schemes environment before determining the definition of the relevant market.

[28] Regulations made in terms of the Medical Schemes Act 131 of 1998 (the "Medical Schemes Act") make provision for managed health care. Regulation 15 defines managed health care as:-" Clinical or financial risk assessment and management of health care with a view to facilitating appropriateness and cost effectiveness of relevant health services within the constraints of what is affordable, through the use of rules based and clinical management based programmes."

[29] A health care provider concludes a contract with a medical scheme in terms of Regulation 15A and undertakes to provide a relevant health service to the beneficiaries of the medical scheme concerned. There are two sorts of managed health care arrangements envisaged by the Regulations:

a)the medical scheme may choose to render managed healthcare to its member " in house" in which case the medical scheme (or administration) will enter into contractual arrangements directly with a network of participating health care providers.
b)A medical scheme may choose to outsource the provision of its members' managed healthcare." In this case the scheme enters into a contractual arrangement with a managed healthcare organisation. The latter then enters into contractual arrangements with a network of participating healthcare providers.

[30] The proper approach to the definition of a market is set out by Brassey *et al*, Competition Law (2002) at 183 thus:

> " The market does not define itself…... The approach that is ordinarily adopted by economists to define the market is the hypothetical monopolist test, [commonly known as the SSNIP test] which is of a piece with the definition of the market in merger control. The relevant market is best defined according to the 1992 United States Department of Justice Guidelines as follows:-' A market is defined as a product or group of products and a geographical area in which it is produced or sold such that a hypothetical profit-maximising firm, not subject to price regulation, that was the only present and future producer or seller of those products in that area, likely would impose at least a "small but significant and non-transitory" increase in price, assuming the terms of the sale of all other products are held constant."

Massimo Motta Competition Policy: Theory & Practice (2004) at 102-103 provides a useful example of the SSNIP test:

> "Suppose that there exists a hypothetical monopolist that is the only seller of bananas. Would this hypothetical monopolist find it profitable to increase the price of bananas above the *current* level in a non-transitory way, say by 5-10% Imagine that the answer to this question is yes, that such a price rise would be

> profitable. This will mean that bananas do not face significant competitive constraints from other products, that is there are no other products that substitute enough for bananas for the hypothetical monopolist to lose much demand when it raises the prices of bananas. Accordingly, bananas should be considered as a separate market, and the test has already given its response.
>
> Suppose now instead that the hypothetical monopolist would not find it profitable to increase prices by that amount, for instance because after the price rise a significant part of demand is redirected from bananas to kiwi fruits and to a lesser extent to pineapplies and other fruits. Then this will imply that bananas should not be considered as a separate market on their own, as their exist other products that exercise a competitive constraint on sellers of bananas. The test should then continue, to consider a wider market, for instance bananas and kiwi fruits together. Would a hypothetical monopolist that is the only seller of banana and kiwi fruits find it profitable to increase the price of these fruits above their current level by 5-10%. Again, if the price rise is profitable the relevant market for our investigation will be found. Otherwise, the test should continue to include those products/fruits that exercise a constraint on bananas and kiwi fruits, and so on until a separate market has been found."

In short, a market does not define itself. It is determined by the demand side substitution and the supply side substitution of customers and producers respectively. In so assessing the scope of the referral market, there is a need to enquire as to the extent to which customers may switch to alternate products in the event of a price increase and the ability of competing producers to other alternate product offerings employed by the Tribunal in arriving at its finding. Hence there is a need to enquire into the evidence employed by the Tribunal in arriving at its finding.

[32] Mr Berger contended that the appellants seek to widen their market definition. It was his contention that appellants should be bound to their

original statements of the merger information filed of record, where they had described the relevant market as 'the administration of capitated managed care options'. He further submitted that the evidence that was placed before the Tribunal established, on a balance of probabilities, that capitated managed care is the only effective arrangement of providing affordable medical insurance to the poorest of the employed.

[33] It does appear that the appellants may have created the confusion when they stated in their original statements of the proposed merger that the relevant market was described as "administration of capitated managed care options." The Tribunal's reliance upon the initial filing does run the risk of elevating the CC 4(2) form to the status of pleadings It also ignores subsequent exchanges between the parties. By the time the respondent submitted its recommendation on 30 June 2005, the information provided by the merging parties extended far beyond the initial merger filing – particularly in relation to the definition of the product market. That this had been imparted to respondent is borne out by the recommendation itself, where the respondent concluded that the relevant product market is "the market for the provision of managed care services with a national network of service providers."

[34] It must also be borne in mind that regard must be had to the totality of the evidence as well as the applicable principles set out above in determining the market. That evidence includes the testimony of witnesses called by the Tribunal and respondent, which evidence reveals that capitation is but a model used by a party within a market.

Mr Dorfling, who testified on behalf of appellants said:

"I think capitation is normally sort of seen as managed care and I think that's an incorrect perception. As I said, capitation is only one of the tools. It's sort of the impression that's been given is that capitation equals managed care due to the American experience and the Kiaza, the Kiaza, which is one of the big managed care models in America, which primarily used capitation."

[35]The following exchange between Dr Stillman and Mr Berger was also relevant to this determination, particularly in the light of the importance placed by the Tribunal and Mr Berger upon Dr Stillman's memorandum of 20 June 2000 in arriving at its conclusion about the referral market:

"ADV BERGE R: According to Dr Nauta and I believe Dr Walters, the aim of such an environment is to move towards capitating the service provider as well, but that's not necessarily the position. In Carecross for example some of the doctors are paid on a capitated basis, other doctors are not paid on a capitated basis. Do you understand that?

DR STILLMAN: My understanding is that when it comes to the providers, that there are various kinds of models that are used and in some cases the provider has to bears and in other cases the provider is on a fee-for-service basis."

[36] In its determination, the Tribunal also relied upon the evidence of Mr Strauss of Discovery Health who testified on behalf of respondent but with regard to this key question of the market, nowhere did Mr Strauss gainsay

the evidence of Dorfling and Stillman that capitation was but one of a variety of managed care techniques.

A further exchange between Mr Berger and Dr Stillman reveals the approval adopted by the latter to capitation:

"Yes, but Dr Stillman, you will forgive me. I am concentrating on the capitated managed care market.

DR STILLMAN**:** But I don't understand what you mean by that.

ADV. BERGER: Well I thought we had gone through that, but let me try again The capitated managed care market is the market where a managed care organisation takes the risk, assumes the risk from the scheme in return for a capitation fee.

DR STILLMAN**:** That is a business model. That doesn't make it a market."

The distinction between a market and a business market was never adequately gainsayed by other witnesses. The Tribunal's use of evidence in support of its conclusions at least in part, somewhat problematic. For example, the Tribunal employed the evidence of Dr R Nauta, the founder of Carecross, to justify its conclusion that *"much of the evidence before us regards capitation as an essential element of a managed care product directed at providing health insurance for low-income consumers. This is not to deny Dr Walters' contention that full capitation lies at th e end of a long journey that may begin with varying mechanisms for managing a fee-for-service arrangement and that ultimately ends with full risk transfer, (in the form of capitation) is required if healthcare provision is to be extended*

on a significant scale to low-income earners. Dr Nauta contends that the transfer of risk "…is really critical too the success in this market. You've got to ultimately transfer risk from you as entity in the middle, that buys this from various options and various schemes, to the doctor" (para 113).

In context, this passage of Dr Nauta's evidence reads:

> "Are you aware of any other managed care companies that have attempted or companies that have attempted to enter this capitated managed care market?
>
> DR NAUTA**:** Yeah, no, I think it's true what I heard earlier. There are…many people enter this. They go as fast as they come. It's not difficult to enter this market. You basically need to have a spreadsheet and a few bop in your pocket, because to say I'm going to do this and then the examples of that and the skeletons, you know, in the past are there. We only think that there are about 3 of us that got enough lives and members to retain the attention of the doctor and of the member, so that members didn't churn, what we say in the medical industry – in other words, come and go and come and go – which is normally a broker induced thing if there's unhappiness in a particular scheme or platform."

This is hardly a definitive statement in support of the Tribunals caution regarding capitation as a market.

[37] In summary, the evidence shows that a capitation agreement which is a subset within the range of managed healthcare is an arrangement entered into between a medical scheme and a person in terms of which the medical

sche me pays to such a person a pre-negotiated fixed fee in return for the delivery or arrangement for the delivery of specified benefits to some or all of the members of the medical scheme. Apart from capitation, there are many options by which the provision of managed healthcare can be achieved. These include risk-adjusted global fee for service; risk-adjusted fee for service; performance-based re-imbursement of global fee for service; peer review management, preferred provider accreditation and benefit design.

[38] The Tribunal's own approach is also not free of contradiction. In its market definition, the Tribunal concluded that the relevant market included firms that provide capitated primary managed care options for both low-income and high/middle-income options. In short, the defined market was not qualified by income sectors. When analysing barriers to entry however, the Tribunal changed the scope of its analysis and deferred the market as the provision of managed care options to the low income sector only. In other words, the Tribunal now imposed a further restriction and excluded the high-income and middle-income sectors. Thus it states at para 162:

> "We note that the schemes which Walters claims are about to desert Prime Cure and Carecross in favour of Solutio, appear to fit this profile. If one accepts that much of the growth in the low -income market is going to be in large, national open schemes, this does not, on its own, suggest a significant future role in the relevant market for Solutio."

In my view it is inconsistent for the Tribunal to rely on a market definition including "capitated primary managed healthcare" generally (which market includes first appellant) and then later in the same determination to insist that the relevant barriers ar e those in respect of entry into the lower income sector (a sector in which first appellant does not operate),

[39] For these reasons, the Tribunal erred in its definition of the product market. To return to the Tribunal's approach regarding market definition, there is an unfortunate absence of a rigorous exercise to determine the scope and nature of the market. The Tribunal did not perform any of the traditional exercises used for determining the dimensions of product market. There is no analysis in its determination which sector to compare prices of competing products or the functionality of those products from a consumer perspective. No customer substitution test was performed: that is an analysis of price substitutability or functional substitutability. On the available evidence, the relevant product market appears to be the provision of primary managed healthcare products for low cost medical scheme options.

Competitors.

[40] The next question that has to be determined is the identification of the competitors. The evidence reveals that there are various entities which competed with second appellant, including third party managed care organisations, ("the MCO'S") , the medical scheme administrators as well as the independent practitioners' associations commonly known as IPA's.

[41] In regard to the managed care organisations, the evidence revealed that Carecross as well as Faranani compete with the second appellant. Dr Nauta

testified that Faranani was established by IPA members and has fewer lives than Carecross and the second appellant, but continues to compete in the same market. He then went on to testify as follows:

> "Mr Unterhalter: But let's just examine some of the facts. I was asking you a question as to who you would think your competitors are and I think we had got to, well, you don't think Medicross, you do think Prime Cure. Who else? Is that it?
>
> DR NAUTA: No, look I think there are probably let's say a new world that you may have in your mind somewhere there, that I don't really see as a competitor, but they are the managed care entities within administrators. The ones that jump to mind immediately would be Qualsa, who have in fact poached 920 lives from us and then sent a letter to all our doctors and that was a little (inaudible) group. So we were a bit vulnerable there. There is the Solutio Group, who look at hospital risks and they're part of the medscheme stable and then you have a lot of little ones.

[42] The medical scheme administrators also compete in the same market, some of which provide the service "in house". Dr Strauss testified that Discovery had previously engaged the second appellant and Carecross to provide all primary health care benefits on their behalf. Subsequently Discovery has terminated that contract and intends to render the service on its own from 1 January 2006. Significantly, it has 90 000 of the 342 000 lives which comprise the number of lives covered by capitated options.

[43] Solutio is the managed care division of Medscheme. Dr Walters testified that Solutio has since 2002 contracted 4000 practices to its network. Some of these practices have two to three doctors. Furthermore, twelve schemes have contracted with Solutio to gain access to its network of medical practitioners. Dr Walters testified that Solutio regarded the second appellant, Carecross, Faranani, Discovery and Qualsa as its competitors and that it has on certain instances been appointed to provide services which had been previously provided by the second appellant.

[44] Qualsa is a managed healthcare organisation within the Metropolitan Health Group. It provides primary care services for Wooltru, previously provided by Carecross and the second appellant. It has 40 000 lives. Mr Dorfling testified that Qualsa also provides managed care services to the Pick 'n Pay Medical Scheme. Mx Health is a large administrator that has a managed care division, thus providing similar services provided by the second appellant. Enablemed has recently been awarded a contract in respect of the Nissan Medical Scheme involving 6000 lives. This scheme was previously handled by the second appellant .

[45] The Independent Practitioners Associations also have a national footprint. Mr Singh testified that the IPA's are all doctors and the location of their practices is convenient for the member and his or her family. The IPA's have organised themselves as businesses in order to provide managed care services to medical schemes. In this regard Sizwe Medical Fund has concluded contractual arrangements with the IPA's only .

[46] It is evident that there are a number of organisations with financial resources and administrative networks in the market, whilst some are

preparing to enter the market. In my view, the Tribunal did not attach sufficient we ight to this evidence. It is highly unlikely that Discovery, an experienced administrator, will encounter any major difficulties when it commences providing the service "in house" from January 2006. It has the financial means and network, and furthermore has 90 000 lives with which to commence with. Indeed respondent's own expert, Mr J Hodge, conceded that Discovery was 'a real competitor'. Similarly, Solutio is a competitor of the second appellant. Dr Walters provided evidence that Solutio had entered the market to provide primary care services for managed care options and had done so in competition with second appellant and Carecross.

[47] Th e Tribunal erred in rejecting this evidence without justification. It erred in its identification of the competitors of the second appellant. It is evident that the competitors of Prime Cure, the second appellant, consisted of various entities namely, Carecross, Solutio, Discovery, Qualsa, Enablemed, Faranani, Mx Health as well as the IPA's.

[48] Having defined the product market and identified the competitors, I turn to deal albeit, briefly, with the remaining issues raised by the parties. These related to the findings by the Tribunal on price sensitivity; switching between medical schemes; competition in the market as well as barriers to entry.

(i) Price sensitivity

[49] In regard to price sensitivity the evidence clearly reveals that the low income members are sensitive to price increases and that members will

migrate if there was any mention of a price increase, however minute. This view was held by various witnesses, including Mr Van der Heever called by the Tribunal who replied to a question of sensitivity to price changes as follows:

> 'I think that yes, I think that looking at the sort of absolute levels, the sort of price elasticity at the lower end, I would expect they would be very price sensitive to changes as well to the absolute level of cost at this point in time. Mr Hodge's testimony in this regard is particularly telling. We also acknowledge this is a price sensitive market, as a low-income market, but what the parties are actually suggesting is that it's perfectly price sensitive, which is a completely different game and from our perspective, if we are going to take pr ice sensitivity on the low-income market to its logical conclusion, then we wouldn't be hearing cases in the Competition Tribunal on low-income products.'

To elevate the indicated test to that of perfect price sensitivity is to construct a test in favour of respondent which in practice will hardly, if ever be met!

[50] Mr van der Heever's concession was wisely made. Members or consumers with very little disposable income are likely to remain sensitive to price increases. If the price is increased, they may not be able to afford membership of the scheme and this will cause them to move or switch to a medical scheme that will suit their needs and pockets. Any attempt by the appellants to increase the price if the proposed merger is granted may well be met by an exodus of members who are price sensitive. This prediction finds clear support in the evidence of Dr Nauta who conceded under the cross examination that low income earners would 'simply move away' if

price was increased significantly. It follows therefore that the Tribunal erred when it found that the low income consumers become insensitive to price once they have joined the scheme.

(ii) Switching between medical schemes

[51] The Tribunal found that the members are unlikely to switch from one medical aid to another due to price increases. In my view there is no clear impediment precluding the members from switching. They do not forfeit any money if they move but may be required to wait for a period before the benefits accrue to them. In any event this finding by the Tribunal is not clearly supported by any evidence.

(iii) Barriers to entry

[52] The Tribunal concluded that the entry barriers are formidable. It is difficult to comprehend how that finding was made when regard is had to the evidence. There are competitors in the market. The evidence of Dr Nauta on whom the Tribunal relied was that it was not difficult to enter the market. Dr Nauta's evidence is revealing.

As noted, when he was asked the question: "Are you aware of any other managed care companies that have attempted or companies that have attempted to enter this capitated managed care market?", Dr Nauta replied that entry into the market is easy; the difficulty of being successful was another matter.

But, Discovery has a good network and sound financial backing with 90 000 lives and would not face any barriers upon entry. Solutio has more than

4000 practices in its network. Old Mutual has the financial and administrative resources necessary to enter the market. It has also acquired Sizwe Medical Scheme, which has an arrangement with IPA's.

In coming to its conclusion the Tribunal sought to circumvent Dr Nauta's evidence by emphasizing the tests of continued presence in the market as opposed to focusing upon entry. But as I have noted, not even that predictive conclusion has been justified nor is there a basis to conclude with confidence that it can be sustained on the evidence. The Tribunal accordingly erred in finding that there were significant barriers to entry.

Conclusion.

[53] It follows therefore that this was not a "three to two merger" as found by the Tribunal. There are other competitors with sound financial and administrative networks. Some of the competitors have managed to secure market share which had previously been held by the second appellant. The evidence has clearly established that there is aggressive competition, that each player has to provide good if not excellent service, in order to keep its contracts. On the evidence presented to the Tribunal there was an insufficient basis to conclude that the horizontal dimensions of the merger would result in a lessening of competition in the deferred market.

[54] It follows that the appeal was upheld and the order approving the merger was granted.

MHLANTLA AJA

DAVIS J P AND SELIKOWITZ JA AGREED