COMPETITION TRIBUNAL
REPUBLIC OF SOUTH AFRICA

Case no.: 32/LM/Jun03

In the large merger between:

Liberty Group Limited

and

Investec Employee Benefits Limited

Reasons for Decision

APPROVAL

1. On 05 August 2003, we issued a merger clearance certificate approving unconditionally the merger between Liberty Group Ltd ("Liberty") and Investec Employee Benefits Ltd ("Investec"). The reasons for our decision appear hereunder.

THE PARTIES

2. The acquiring firm is Liberty Group Limited ("Liberty"), a registered long-term insurer active in the retirement fund industry. Liberty is a public company listed in the life assurance sector on the JSE Securities Exchange South Africa. However, its controlling shareholder is the Standard Bank Group Limited ("STD Group Limited")[1].

3. The target firm is Investec Employee Benefits Limited ("IEB"), a long-term insurer registered as such in terms of the Long-Term insurance Act No. 52 of 1998, as amended. IEB is also, as submitted by the parties, active within the retirement fund industry. IEB is a wholly owned subsidiary of Investec Employees Benefits Holdings Limited, which in turn is controlled (100%) by Investec Limited, a public company listed in the financial bank sector on the JSE Securities Exchange.

The Transaction

4. This transaction basically entails Liberty Group's proposed acquisition of Investec Employee Benefits' business of marketing, underwriting and administering certain insurance policies, as well as the subsequent rights and obligations of these policies. The transaction will be effected by way of a transfer agreement[2] entered into between Liberty and IEB.

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[1] It should be noted that the Standard Bank Group, a part of the acquiring firm by virtue of its indirect controlling interest in Liberty, does not operate within any of the overlapping product markets of the parties identified hereunder.

[2] In terms of the Long-Term Insurance Act, as amended, the transfer agreement requires court approval before it may be implemented of which the merging parties are uncertain as to when such approval will be obtained.

5. In terms of the proposed transaction, Liberty will, as outlined in their transfer agreement, acquire from IEB the business of marketing, underwriting and administering certain insurance policies issued by IEB (the "business")[3]. The latter three services relate to a part of its long-term investment and risk policies issued to pension funds where Investec is appointed as the administrator of the funds ("Fully Administered Retirement Fund Business"); and part of long-term policies in terms of which it is liable to pay disability benefits ("Disability Claimant Business").

6. Liberty will acquire IEB's rights and obligations in terms of the policies being transferred; the business assets used by IEB in the conduct of the business; and the policy assets, being assets required to support the liabilities of the business.

7. To minimise the risks, market disruptions and other adverse effects on the business being transferred (due to the time delays with regard to such transfer) the parties further agreed to enter into a reinsurance agreement and an administrative agreement. The reinsurance agreement is related to the transfer agreement, but is independent in that it will be effective even if the transfer agreement is not approved.

8. It is imperative for Liberty, as envisaged in the reinsurance agreement, to reinsure certain liabilities of IEB under certain long-term policies that will be transferred to Liberty under the transfer agreement. As a prerequisite for the reinsurance agreement, Liberty furthermore agreed to administer the business in accordance with the administrative agreement.

9. Liberty will, prior to the proposed transaction, exercise control over the business being purchased in terms of the administration agreement while post the proposed transaction it will own the business being acquired.

Rationale for the transaction

10. The rationale from the acquiring firm's perspective, in concluding the transaction is that Liberty has invested heavily in systems infrastructure in the past three years for it to become a competitive and efficient retirement fund administrator. To that effect Liberty requires increased volumes of business to achieve the intended economies of scale.

11. The IEB's strategy, as submitted by the parties, does not include the administration of retirement funds and provision of investment policies thereto as a core competency. Rather, as the Investec Group has key strengths in risk management, it has defined the core business of IEB as risk underwriting. IEB will focus on the provision of risk underwriting services in the future, which includes the provision of risk policies to retirement funds.[4]

[3] The parties submit that these policies are principally long-term policies which provide for IEB to administer the retirement fund obligations of the policyholder (usually a retirement fund itself) and also provide for the payment of policy benefits to the policyholder.

[4] The parties submitted that the proposed transaction only relates to the non-industrial fully administered retirement fund business of IEB. By March 2004, IEB will have exited the fully administered retirement fund business in all respects and be able to focus on its core business being risk management.

12. In addition, Liberty considers retirement fund administration as a core part of its business, which it wants to grow. It is submitted that IEB's customers will, as a result of this transaction, be offered the greater degree of product flexibility and transparency that Liberty's systems cater for. This would, as submitted by the parties, provide enhanced benefits for customers.

Activities of the parties to this transaction

Liberty

13. As a long-term insurer, Liberty's products and services include long-term insurance, asset management, retail investment management and healthcare services. According to the parties, long-term insurance products (inclusive of both individual and group products) are provided through Liberty Corporate Benefits, Liberty Personal Benefits and Charter Life. These products and/or services, depending on the nature of each, are provided to individual and/or corporate clients.

14. *Individual products* are assurance and investment products offered to individuals. These products include life and disability insurance options, local and offshore investment plans, retirement savings plans, preservation schemes and annuities.

15. *Group products*[5] being retirement fund products and risk benefits (other than health) offered to employers, retirement funds and other groups. The products include insurance policies issued to retirement funds as an integrated product (i.e. packaged solution). Elements of this product are investment management, risk underwriting and administration, also marketed and sold separately.

Investec

16. Investec's primary products and services include long-term insurance policies (segmented into individual and group products) and annuities (being the administration of annuitants who retire from retirement funds).

17. *Individual products* are assurance and investment products offered to individuals. These products include life annuities, offshore trenches and individual life policies.[6]

18. *Group products*[7] are retirement fund products in respect of which a full spectrum of retirement fund products are provided including policies of insurance (incorporating both investment and risk cover as well as administration services) to retirement funds, which operate exclusively by means of these policies (i.e. funds that purchase "packaged" retirement products).

19. Both the Commission and the merging parties were emphatic in their papers and at the hearing that Investec's individual products and annuities do not form part of the

[5] The Commission indicated in its recommendation (page 9) that group products constitute 95% of Liberty's retirement fund business.
[6] Investec's individual products business has been, as submitted by the parties, reinsured with Capital Alliance Life Limited.
[7] It has been indicated in the Commission's recommendations that group products constitute 93% of Investec's retirement fund business.

current transaction. Only group products (Audit Exempt Funds) are the relevant products for purposes of the current transaction.

The Standard Bank Group

20. As indicated above, Standard Bank Group does not operate within any of the overlapping product markets. It is, however, involved in banking and insurance activities in South Africa and abroad.

An overview of the retirement fund industry

21. It is therefore clear from the above that the merging parties operate within the retirement fund industry.

22. As a precursor to defining the relevant product market in order to assess the impact of the proposed transaction on competition, it is necessary to give an overview of the various players, and their functions, in the retirement industry.

23. The primary functions of a retirement fund are administration, investment and risk underwriting. These functions can either be undertaken by the fund itself or the fund can outsource one or more of them to a professional administrator, investment manager and/ or risk underwriter.[8]

Types of retirement funds

24. The retirement funds are classified within this industry as either Self Administered Funds or Audit Exempt Funds (Section 2(3)(a) Exempt Funds)[9].

25. Self Administered Funds are funds that either perform all the functions themselves or that outsource one or more of these functions. A fund may, in terms of the Self Administered Fund, invest members' contributions in investment and/or risk policies issued by insurers. The insurer, as a professional administrator, may undertake administration functions or they may outsource administration to other professional administrators.

26. Sections 2(3)(a) Exempt Funds are funds that operate exclusively by means of policies of insurance. Such a retirement fund purchases an insurance policy, which provides cover in respect of investment and risk benefits and includes administration services as part of the package in the form of a "packaged" retirement fund product.

27. In terms of section 2(3)(a) of the Pensions Fund Act[10] these funds are exempted from the obligation to produce audited financial statements on the basis that its administration and accounting functions are performed by a regulated insurer. Save for the above regulatory classification, there is no significant distinction between the two types of retirement funds.

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[8] The appointment of these entities is subject to regulatory requirements, for instance registration with the Financial Services Board ("FSB"), etc.
[9] It is important to note that this classification is based on the performance of the abovementioned operating functions of a retirement fund.
[10] Pensions Fund Act No. 24 of 1956, as amended.

28. When considering whether to outsource the functions of investment management, risk and administration respectively, retirement funds consider the regulated groups of service providers including, *inter alia*, asset managers, retirement fund administrators, and long-term insurers.

29. Long-term insurers are service providers who assume risk in return for a premium and issue a long-term policy to that effect. Retirement fund administrators include long-term insurers and specialist administrators.

30. In addition to the abovementioned service providers there are brokers who act as intermediaries between retirement funds and insurers. These include large insurance brokers such as Alexander Forbes, NMG, NBC, Wynn Jones, Tennant, Ten-50-Six, ABSA Employee Benefits and Robson Savage.

31. These brokers offer packaged retirement fund products to small and medium-sized retirement funds by bundling investment and risk insurance cover as well as administration services sourced from different long-term insurers and administration service providers. The brokers are classified into administrative and non-administrative brokers with the latter not performing any of the above functions but outsource them all.

32. The parties further submit that by offering customers “packaged” retirement fund insurance products and administrative services in this way, insurance brokers introduce direct competition between “packaged” retirement fund insurance products offered to Audit Exempt Funds and Self Administered Funds and indirect competition between “packaged” and “unpackaged” retirement fund products.

33. It is asserted further that a retirement fund’s choice for performing or acquiring investment, risk underwriting and administration products/services depends largely on its size. Large funds are more likely to perform all three required functions themselves or to outsource only one or two of them. Smaller to medium-sized funds are more likely to outsource these all three functions as a package in that they are unable to achieve critical mass in any one function and they might not meet the minimum threshold requirements of a provider of one or three services. As a result of the cost efficiency and effortless management obtained in respect of “packaged” retirement fund products, they opt for “packaged” retirement products.

34. In addition, these “packaged” retirement products can be provided by either administrative brokers, non-administrative brokers or insurers. Retirement funds purchasing these “packaged’ products may either be Self-Administered Funds or Audit Exempt Funds.

The relevant product market

35. In analyzing the transaction the Commission identified the relevant product market where the overlap occurs as the market for the provision of group investment, risk underwriting and administration services to Self Administered Funds and/or Audit Exempt Funds. The merging parties only provide these services to the latter two funds.

36. IEB also conducts the Disability Claimant Business, which relates only to the performance by IEB of its obligations under an existing policy[11]. On that basis, the Disability Claimant Business cannot be considered to be a product on its own and therefore a market (or even a part of the market) for the purposes of this transaction.

The relevant geographic market

37. There is no dispute as to the area where consumers can practicably turn for supply or where competitors face competition (i.e. the geographic market).

38. Both merging parties and their competitors (being long-term insurers) provide their products and services throughout South Africa. We therefore agree with the Commission that the relevant geographic market is national.

Impact on competition

Market shares

39. According to the market shares figures (all based on the contribution of members in the market for the provision of services to Section 2(3)(a) Exempt Funds) supplied by the parties, Liberty has 13,9% while IEB has 4,1%. Post-merger, the parties will have a combined market share of 18%[12] in the national market.

40. This 18% reflects the merged entity's post-merger market share for the provision of group investment, risk underwriting and administration services in this market.

41. There are many large players active in the long-term retirement insurance market including, *inter alia*, Old Mutual, Sanlam, Momentum, Sage, Metropolitan, Discovery and various small and large independent brokers. These are the players from which the merged entity face competition.

Countervailing power

42. The Pensions Fund Act entrenches the independence of pension funds and their trustees, and they can change the providers of administrative functions at any time if they so wish provided they give a sufficient written notice. There is often a link between administrative services, and investment management and risk underwriting services. The termination of administrative services could result in the termination of the latter two services, especially when a long-term insurer provides it. This significantly strengthens the countervailing power of pension funds.

43. This independence also applies to areas such as product innovation and differentiation (due to the large number of registered long-term insurance companies, including brokers), which enhances countervailing power. A wide variety of products are offered as a result of the number of competitors in the market with the prices

[11] This is merely, as submitted by the parties, the payment of benefits, which have already been claimed under a long-term policy with no concomitant receipt of contributions.
[12] The parties consider this to be a narrowly defined market overstating their actual market share in the relevant markets.

becoming low, and funds are at liberty to seek business from competitively low prices.

44. According to the parties the market is intermediated with the result that information with regard to the market and its players is relatively public. In addition, the brokers increased competition in the market between long-term insurers in that brokers negotiate best products and ultimately lowest prices with insurers in order to market a best product to retirement funds. The above ensures that brokers possess a strong degree of countervailing power over other providers in this market.

Barriers to entry

45. According to the parties there are various categories of providers of administration, investment management and risk underwriting services to retirement funds and, depending on the category, the barriers to entry vary from relatively high to significantly low.

46. In terms of regulation a long-term insurance service provider must be registered as such in terms of the Long-term Insurance Act, as amended, or have access to an insurance licence. An administrator must also be registered as such with the Financial Services Board. In both situations there are, however, specific requirements, which providers have to adhere to.

47. The barriers are in place to enforce adherence to regulatory requirements and to monitor the activities of long-term insurance service providers. Brokers are able to enter and compete in the market without any significant capital, regulatory or other requirements. The parties further submitted that there are no barriers to entry if the products are provided as a Non-Administrative broker, other than accreditation requirements shortly to become prerequisites in terms of the Policyholder Protection Rules and Financial Advisors and Intermediary Services.

48. The Commission further indicated the entry figures on new entrants in this market for the past three years. It maintained that 3 198 Self Administered Funds, 11 808 Audit Exempt Funds, 330 new funds were registered in December 2001 while 122 administrators were registered up to April 2003.

49. Although the barriers to entry appear to be relatively high for insurers and administrators, the above figures indicate that entry has been taking place notwithstanding.

Public interest considerations

50. Except for employment, this transaction does not raise any other public interest concerns. The parties stated clearly in their papers filed with us that no retrenchment is envisaged as a result of this transaction.

51. The administration arrangement is in effect an outsourcing by IEB to Liberty of the administration of the business. Liberty therefore undertakes to employ the IEB's employees on similar (but not less favourable) terms and conditions as that of IEB[13].

52. The parties further submitted that should there be any necessity (as a result of the consolidation) to retrench, on a worst-case scenario, the employment of not more than 7 of the 255 employees may be affected by the transaction. However, the merged entity would opt for alternative employment before retrenching.

Conclusion

53.Although the merger would result in the merged entity being one of the larger players in the retirement fund market when compared with its competitors, with 18 % of the market, this is not a market share which would give rise to concerns. In addition, the market is characterised by a high level of competition and regular entry.

54. We accordingly conclude that this merger is unlikely to substantially lessen or prevent competition in the relevant market, and accordingly approve the transaction without conditions.

_______________ 18 August 2003

N. Manoim **DATE**

Concurring: F. Fourie, P. Maponya

For the merging parties:	Mr. G Driver & Mr. D Rudman, Werksmans Attorneys. E. Barnard, Jowell, Glyn and Marais.
For the Commission:	Ms. M Sebothoma assisted by Ms. L Blignaut, Competition Commission

[13] The employees will be transferred to the merged entity as envisaged by section 197 of the Labour Relations Act 66 of 1995, as amended.