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Our Ref: 206203/JDB:dvv

15 February 2008

Mr Avi Hubert
A/Executive Manager
Competitive Market & Fair Trade Division
Independent Consumer & Competition Commission
1st Floor, Garden City Building
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National Capital District

Office of the Commissioner
Received 18 102 2008

Received by Finance & Admin
Date 15/02/08
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facsimile on 15 02 08

Dear Sir

RE: MOTOR VEHICLES INSURANCE TRUST LIMITED - PACIFIC MMI LIMITED

We refer to your letters of 10 December, 2007 and 29 January, 2008 and to our responses on behalf of our client of 15 and 23 January, 2008.

In relation to your letter of 23 January, 2008, which refers to certain issues raised in your earlier correspondence, we address below each of those matters, following your numbering:

1. MVIL claims commercial confidentiality in relation to the price and the terms upon which that amount is payable for the balance 50% shareholding under the Share Sale Agreement ("Agreement"). Our client draws to the attention of the Commission the provisions of Clause 10 of the Agreement. Our client notes that the Commission is to consider which other aspects of the Agreement are likely to be commercially confidential based upon relevance and public interest. Please also refer to our comments under paragraph 2(j) below;
2. Further to our letter of 15 January, 2008 the following additional submissions are made concerning the provisions of Section 69(5) of the Act:
 - (a) Pursuant to the Insurance Act, the Insurance Commissioner may issue a licence to carry on general insurance business. It is therefore possible for additional or new companies to enter the market provided that the requisite capital adequacy and other statutory requirements are met to the satisfaction of the Office of Insurance Commissioner. In the circumstances, MVIL would propose that there is no restriction on import competition in the market. Nevertheless, market size and return

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on investment/capital are limiting factors in the potential for other competitors to enter the PNG insurance market;

- (b) The comments above are equally relevant here. As mentioned previously, there are at present eleven insurers of general insurance business in the market. Historically, it can be established that there have been fewer insurers enter the market than insurers which have exited the market. Cases in point include the likes of FAI, HIH, General Accident, GRE Pacific, and Zurich Insurance which itself was acquired by QBE Insurance. Again, this does not preclude the possibility of new insurers entering the market.

As part of PMMI's strategic business plan, consideration would be given to entering other markets within the Pacific region in order to achieve growth in the business model.

- (c) Again, the comments above are relevant. There are eleven insurers within the market. MVIL is not necessarily included as one of those eleven on the basis that it undertakes compulsory third party insurance business only. MVIL is a single line/class insurer that does not compete in the general insurance market.

The market is highly competitive due predominantly to price, the impact of insurance brokers and the nature of product being offered to the insurance buyer. These factors however do not necessarily prevent the admission of new competitors to the market. Although there have not been any new entrants in recent years, the number of participants in associated industries, such as insurance brokers (two new indigenous brokers have set up in the last 4 years), have demonstrated that there is sufficient scope and demand within the industry in general;

- (d) MVIL and PMMI would opine that there is little or no countervailing power within the market. There is however some possibility for insurance companies to exercise some limited countervailing power by providing cover and products at much reduced premiums. In the main however, this would not appear to be commonplace and despite brokers lobbying for lower rates, insurers themselves determine price and product as a direct result of market forces. There is also the avenue that the insurance buyer may place their insurance offshore (under the exemption process) and thereby exercise some countervailing power. That practise is not unusual in this market;

- (e) The current business model which has been adopted by PMMI encourages the status quo on pricing to remain. Where a policyholder has a good claims record they are rewarded. Actuarial science is used in the determination of the rates and premiums applied to rating the risk exposures for each class of insurance. Again, pricing is driven by market forces and as has been demonstrated, the insurance industry is highly competitive. Accordingly, pricing is unlikely to alter due to the shareholders changing. If any factor is relevant it would be the influence of brokers on securing cheaper prices and better products for consumers, and the impact that natural disasters have upon the availability of insurance and reinsurance. PNG is affected by world movements in price of insurance and reinsurance, however the local industry performs a balancing act to soften the peaks and troughs for the local insurance buyer. The acquisition of the balance 50% shareholding by MVIL would not alter the PMMI's business model;

- (f) As mentioned, the entry of new insurers into the market is possible. That said, no new insurers have entered the market for some considerable time. PMMI itself is perhaps the only insurer which has received any significant level of offshore capitalisation in recent years.
- (g) The comments above are again relevant. Regulation of the industry by the Office of Insurance Commissioner does not preclude the entry of new insurers. What is becoming more prevalent is product innovation by the existing insurers. In fact, PMMI would argue that it has been more innovative with product and branding than any other PNG based insurer. Furthermore, PMMI is the only composite insurer in the industry holding both life and general insurance licences and selling all classes of these products. Given the level of competitiveness, product innovation is inevitable, if only to retain one's market share;
- (h) As stated in earlier responses to the Commission, both MVIL and PMMI refute any suggestion that the acquisition would result in the removal of a competitor from the market. MVIL intends to maintain its interest in PMMI as a "passive" investor. MVIL accepts that control over PMMI will be increased but at the same time maintains that MVIL is not a specialist general insurer and management of PMMI is deliberately and effectively placed in the hands of independent experts;
- (i) MVIL is of the opinion that there would be limited (if any) vertical integration. Whereas, MVIL is an insurer, it is limited to provide compulsory third party insurance only. Similarly, MVIL does not provide any reinsurance cover in respect of general insurance and under its Act is prohibited to only underwrite one class of insurance namely, compulsory third party insurance. The Commission will note the obligations contained in the Agreement in respect of reinsurance with Allianz Reinsurance Asia Pacific Limited. MVIL submits that the obligation is advantageous in that it provides some level of comfort for consumers and is prudentially sound. As mentioned, this reinsurance protocol does not preclude PMMI from sourcing reinsurance from other providers. In fact, PMMI introduced more competition to the marine insurance market in PNG in 2006 by the introduction of reinsurance arrangements with Zurich Australia Insurance Limited who underwrite part of PMMI's marine reinsurance programme in conjunction with Allianz Re Asia Pacific;
- (j) The only other factors which should be brought to the attention of the Commission are:
- (i) PMMI estimates that it presently holds approximately overall market share. The actual figures are not available as they are provided by the Office of Insurance Commissioner who has not collated and published the up-to-date industry figures beyond 2005. By way of example of the nature and corresponding percentages of the business written by PMMI, we **enclose** a pie chart prepared by PMMI. Confidentiality is sought in relation to the details disclosed as it is highly sensitive and confidential; release of same would damage PMMI's operations, and future profits. Furthermore, the details disclosed are not relevant to this application and are of no public benefit;



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- (ii) the Commission is also requested to consider the effect of the pre-emptive rights contained in the Constitution of PMMI. Subject to the approval of the Commission and other conditions precedent contained in the Agreement, MVIL has exercised its pre-emptive rights in relation to the 50% shareholding of Allianz. If approval by the Commission is not granted, the only other alternative which would be available would be that the shares are then transferred to a third party. Presumably, this could either be an investor outside of the insurance industry, an existing on-shore insurer or an off-shore insurer. In any event, the approval of the Commission would again be required; and
 - (iii) we also refer the Commission to its Final Report and Issues Paper regarding a review of the general industry in PNG.
3. As discussed at our meeting with the Commission on Monday 4 February, 2008 it is not the intention of MVIL to tie or parallel market comprehensive motor vehicle insurance cover with compulsory third party motor vehicle insurance.

Pursuant to the provisions of the Motor Vehicles (Third Party Insurance) Act Chapter 295 and the Insurance Act, MVIL is a licensed insurer to carry on general insurance business but is limited to compulsory third party insurance. By its enacting legislation MVIL is itself the monopoly provider of compulsory third party motor vehicle insurance. Accordingly, the general insurance business for which MVIL is licensed is restricted to compulsory third party motor vehicle insurance. Furthermore, as a regulated industry under the Independent Consumer and Competition Commission Act, the Commission, subject to obtaining necessary orders, is empowered to take over MVIL's operations in the event of the contravention of MVIL's license.

On this basis, any amalgamation of compulsory third party motor vehicle insurance and general insurance for which PMMI is licensed, would amount to a breach of MVIL's insurance licence under the Insurance Act which, in turn, would be a breach of the provisions of the Motor Vehicles (Third Party) Insurance Act.

4. MVIL submits that the proposed acquisition would not unduly benefit PMMI's reinsurance needs or requirements with Pacific Re Limited ("Pac Re").

As discussed, both MVIL and PMMI have existing and specific reinsurance treaties or policies in place. The level of reinsurance placed with Pac Re is determined by Pac Re's determination of not only price but also risk and therefore it's capacity to accept reinsurance liabilities.

PMMI is not a shareholder in Pac Re. Although PMMI places a small percentage of reinsurance with Pac Re, it is not committed to place reinsurance with Pac Re but quite to the contrary actively seeks to provide reinsurance alternatives offshore. As a matter of prudence, PMMI places the majority of its reinsurance requirements with Allianz Reinsurance Asia Pacific Limited whilst supporting Pac Re when circumstances, including price, require.

MVIL does not intend to exercise any undue influence on PMMI to place reinsurance with Pac Re over and above PMMI's determination of what would amount to sound business practice.



We acknowledge the content of your letter of 6 February, 2008 concerning the assessment period.

We look forward to receipt of the Commission's determination.

Yours faithfully,

PACIFIC LEGAL GROUP



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Encl...