

David Jones
Director
Mergers & Asset Sales Branch
Australian Competition & Consumer Commission
david.jones@acc.gov.au

Dear Mr Jones

Promina/Suncorp merger

The FSU represents 55,000 members employed in the finance sector across Australia.

Our knowledge of the industry and the experience of our membership provides the FSU with a unique perspective of the needs of consumers and other stakeholders in insurance, banking and wealth management markets.

We submit to the ACCC that if the merger between Suncorp and Promina proceeds it would create the country's biggest motor and third-party insurer and second-biggest home insurer behind Insurance Australia Group and would see the general insurance market dominated by five players: QBE, IAG, Allianz, Wesfarmers and Suncorp.

Further, it would represent the biggest financial services deal since Commonwealth Bank of Australia's takeover of Colonial Ltd for \$9.6 billion in 2000 (during which the FSU represented some 22,000 members).¹

The FSU believes that the ACCC should oppose the Promina/Suncorp merger on the grounds of the market concentration that will occur in certain insurance markets; the substantial lessening of competition in general insurance as all existing brands under the Promina and Suncorp umbrellas come under control of one entity; the consumer impact of job losses; and the increased pressure for further mergers that allowing this merger to proceed would create in the finance sector.

It is the view of FSU that the only basis for the ACCC allowing the merger to proceed would be as a result of significant divestiture of insurance brands, operations and products; and/or through the process of the ACCC satisfying itself of market concentration thresholds and competition in the industry by receiving enforceable undertakings from the merger partners.

However, in regard to enforceable undertakings, the FSU submits that the ACCC, needs to be given, or should exercise, authority to build extra safeguards into undertakings to ensure that they are fully complied with both in letter and spirit.

Further, FSU notes the discretion of the Federal Treasurer to approve or block mergers under the Financial Sector (Shareholdings) Act 1998, however, sees a failing in this legislation as being the lack of guidelines or processes regarding types of issues that should be considered in making this decision. The FSU contests that such matters should include the impact on the public interest and, in particular, on jobs and services.

¹ Brett Clegg and Stewart Oldfield, "Suncorp in \$7bn bid for Promina", *Australian Financial Review*, 12 October 2006 and More mergers unlikely", *The Advertiser*, 6 November 2006

Current Market Conditions

The market implications of the proposed merger are likely to be most significant in the insurance markets, consequently this submission only briefly touches on the banking and wealth management markets.

The insurance industry is enjoying healthy levels of profitability with net profit after tax for the year ended 30 June 2006 of \$5.5 billion (June 2005 - \$5.1 billion).²

Return on net assets was 22.3 per cent for the year, up from 21.5 % for the June 2005 year. Direct insurers accounted for \$5.0 billion (91%) of the industry profit.³

A survey of the general insurance industry by KPMG said the 2005-06 financial year showed operating profit in the sector improved 3.1 per cent to \$3.56 billion last year.⁴

According to JPMorgan, car insurance premiums rose 2 per cent last year, home insurance rates gained 3 per cent, while compulsory third party in NSW and Queensland fell by 6 per cent.⁵

Prior to the announcement of the merger, analysts predicted:

- A slow down in growth and a more intense era of competition, particular in personal lines of insurance;
- In the past two years, competition from offshore players has impacted on premiums, particularly in commercial insurance;
- Customers were expected to benefit from the new era of increasing competition;
- Increased merger and acquisition activity; and
- More aggressive marketing, alternative products and greater focus on differentiation through customer service.⁶

Essentially, the insurance industry is performing well for all stakeholders with the current mix of competitors in the marketplace. Competition is serving the community well in both restricting premium increases and providing access to products and services, shareholders are enjoying outstanding returns and companies are enjoying healthy profits.

² APRA June Statistics, include full citation for statistics, found at <http://www.apra.gov.au/Statistics/General-Insurers-Statistics.cfm> [last accessed 17 November 2006]

³ APRA June Statistics, include full citation for statistics, found at <http://www.apra.gov.au/Statistics/General-Insurers-Statistics.cfm> [last accessed 17 November 2006]

⁴ Sam Holmes, "Insurance 'rivalry' intense", *The Courier Mail*, 6 September 2006

⁵ Eric Johnston, "Survival: Suncorp is lucky it's with AAMI", *Australian Financial Review*, 14 October 2006

⁶ Sam Holmes, "Insurance 'rivalry' intense", *The Courier Mail*, 6 September 2006, Brett Clegg and Stewart Oldfield, George Lekakis, "Heat on insurers to merge", *Herald-Sun*, 6 September 2006, "Suncorp in \$7bn bid for Promina", *Australian Financial Review*, 12 October 2006, Eric Johnston, "Survival: Suncorp is lucky it's with AAMI", *Australian Financial Review*, 14 October 2006.

Market concentration

The ASX Announcement of the proposed Suncorp and Promina merger indicates that the combined entity would continue to compete across three major business lines:

- Insurance;
- Wealth management; and
- Banking.⁷

Commentators have suggested that if the merger proceeded, Australia's top four insurance competitors would have 83 per cent of the general insurance market.⁸ The following table published in *The Weekend Australian* on 14-15 October 2006 contains similar figures regarding the level of market concentration that would exist if the merger proceeds. If these figures are accurate then it raises concerns given the general ACCC thresholds market share of the four largest firms in any particular marketplace and on this basis alone FSU contends that the merger should not occur unless significant divestiture occurs.

Table 1 Estimated National Market Share for Insurance – Personal Lines

	Motor (%)	Home (%)	CTP (%)
<i>IAG</i>	39	37	27
<i>Promina</i>	25	14	11
<i>SunCorp</i>	15	16	22
<i>QBE</i>	5	8	8
<i>Allianz</i>	8	7	22
<i>Others</i>	9	19	10
<i>Merged SunCorp & Promina</i>	40	30	33
Prior to SunCorp & Promina merger			
<i>Top 2</i>	64	51	50
<i>Top 4</i>	86	74	82
After SunCorp & Promina merger			
<i>Top 2</i>	79	67	60
<i>Top 4</i>	91	81	90

Source: Tim Boreham and Tim Blue, "M&A the only way ahead in insurance", *The Weekend Australian*, 14-15 October 2006

⁷ ASX Announcement of Suncorp and Promina Merger, 23 October 2006, found at www.suncorp.com.au [last accessed 17 November 2006], p12

⁸ Rhys Haynes and Sam Holmes, "Watchdog may reject Promina takeover", *Canberra Times*, 24 October 2006

Brand independence

Perfect markets require that customers have perfect information – the reality, of course, is different.

FSU submits that consumer knowledge about insurance brands is limited. For example, FSU suspects that many consumers would be unaware that AAMI, Vero, Just Cars, Shannons and APIA brands are all owned by Promina Group. Further, that while Suncorp operates under their own brand in Queensland, RACT Insurance in Tasmania and GIO throughout the rest of Australia, it also owns a 50% stake in joint ventures with motor clubs in Queensland and South Australia.⁹ Similarly, Promina owns a 50% stake in RAC in Western Australia.

Another element of concern is the extent to which substitutes are available in the market, or are likely to be available in the market i.e. genuine choice between products and/or services. That is, consumers may already be under the illusion that the available choice in the general insurance market is greater than it is in reality.

FSU is concerned that should all of the existing Suncorp and Promina brands be combined into the one entity that this may lead to a substantial lessening of competition in the general insurance market. Specifically, the FSU is concerned that the merged entity could continue to separately market the brands creating the illusion of competition, while internally agreeing on prices, products and markets.

Further, cross-selling of products may lead consumers to think they are being offered substitutes from independent sellers as opposed to separately branded products from the same seller.

Job losses

The primary concern for the FSU is, unashamedly, the potential loss of jobs. While FSU appreciates that the ACCC does not specifically consider job losses, FSU believes, they are a significant consequence of any merger and should not be overlooked. Our past experience indicates that if the merger proceeds, it is reasonable to anticipate a significant number of jobs lost.

Commenting on potential job losses, Suncorp's CEO John Mulcahy said significant synergies would be realised by bringing the two companies together. Though merger implementation costs would total A\$395 million, savings of at least A\$225 million a year were expected to be achieved and would be accretive to cash earnings per share in its second year, at which stage a total profit before tax of A\$2.19 billion was forecast.¹⁰

⁹ Suncorp Concise Report 2006, found at www.suncorp.com.au [last accessed 16 November 2006], p20

¹⁰ Consolidation under way in Australia, Life Insurance International, 8 November 2006

Further, in his AGM address, Mr John Short (Chairman, Suncorp) stated “the combined general insurance operation will have a scale that provides the opportunity to realize very significant efficiencies in every aspect of its business operations...”¹¹

Suncorp distributes general insurance products primarily through the network of 173 branches. In addition, the financial planning workforce is located in the branches on behalf of Wealth Management.¹²

While an increased ‘footprint’ of branches is likely, past experience suggests that rationalisation of those locations with duplicated branches across the merged entity is inevitable.

FSU is concerned that the combined effect of the change in management structure and philosophy and the cuts in employment levels that will be the result of the proposed merger will have detrimental effects on the service that customers will receive from the network of merged branches and agencies.

Across the two entities, several thousand staff are employed in the two head offices, administrative divisions including back office claims processing and in call centres.

FSU is concerned that the duplication of functions in the merged entity is likely to result in significant job losses in the administrative and shared services areas of one or both of the entities.

FSU is also concerned that any job creation opportunities will be lost offshore to low cost centres as has been witnessed in a number of the major banks in recent months. Suncorp already sources software development projects from India and there is speculation that further parts of their IT operations may be off-shored.

Forecasts indicate that the merger would not deliver positive earnings until 2010 i.e. some three years after the two companies come together¹³. In this environment, FSU’s experience suggests that those employees who remain in employment immediately following the merger can expect a long period of uncertainty.

FSU is concerned about the occupational health and safety of staff in the lead up to the merger and during the merger implementation process.

To date, Suncorp and Promina have both declined to publicly say if the merged entity would offload business lines. Neither have they advised whether the proposed merger is likely to result in closure of any of the existing branches or agencies. Nor have they provided detail on the future of the various call centres or administration centres. For this reason, it is very difficult for FSU to accurately assess the impact of the proposed merger on job security.

¹¹ ‘Suncorp Chairman’s Address’, Suncorp Annual General Meeting, Wednesday October 2006, located at <http://www.suncorp.com.au/suncorp/shareholder/agm.html> [last accessed on 15 November 2006], page 4

¹² [Suncorp Concise Report](#) found at www.suncorp.com.au [last accessed on 16 November 2006], p16

¹³ “Anger grows as Suncorp shares plunge”, [The Australian Financial Review](#), Wednesday 25 October 2006, p60

Impact on regional and rural communities

It is not yet known whether the proposed merger will result in the closure of any of the existing Suncorp or Promina branches or agencies.

In the absence of this information, the FSU has identified 20 regional communities where both operators, Suncorp (i.e. Suncorp or GIO branches) and Promina (i.e. AAMI or APIA branches) currently serve customers. There are 12 sites in Queensland, 7 sites in NSW, 2 sites in Victoria and 1 site in Tasmania¹⁴.

These figures do not include co-existing Suncorp & GIO retail branches or AAMI & APIA retail branches in the same town, which would add a further 29 instances.

The FSU is concerned that not only would branch closures cause considerable job losses, they may also substantially reduce service levels in many regional and rural markets.

Impact of further industry rationalisation

Suncorp's strategy of combining general insurance and banking in one financial conglomerate has attracted a lot of scepticism over the decade since the group was created through a three-way merger driven by the Queensland government.¹⁵

The FSU is concerned that a substantial broadening of banking, insurance and wealth management products will require staff to acquire and maintain a vast range of specialist product knowledge.¹⁶ If not supported by adequate staffing levels, training, reward and recognition, this has the potential to seriously impact on the quality of advice provided to customers.

While FSU appreciates that the ACCC will not engage in speculation in rapidly evolving markets, looking forward two to three years it would be difficult not to imagine further industry rationalisation.

The FSU is concerned that the proposed merger may place undue pressure on other banks and insurers to look for acquisition opportunities.

¹⁴ 12 QLD = Bundaberg, Cairns, Coolangatta, Hervey Bay, Innisfail, Ipswich, Mackay, Maroochydore, Rockhampton, Southport, Toowoomba, Townsville), 7 NSW = Albury, Charlestown, Coffs Harbour, Dubbo, Lismore, Port Macquarie, Tamworth, Wagga Wagga, 2 VIC = Bendigo, Frankston and 1 TAS = Hobart.

¹⁵ Stephen Wisenthal, "Suncorp under pressure", Australian Financial Review, 1 September 2006

¹⁶ Alex Tilbury, The Courier Mail, 4 November 2006

A number of articles that appeared just before and after the announcement of this proposed merger paint a picture of the increased predatory environment that this merger bid has created. The FSU has concerns about the outcome this chain of events or the 'domino effect' of the proposed merger on other industry competitors.

Westpac, St George and QBE are mentioned as among those companies interested in expanding regional footprints in banking and/or insurance. While CBA and ANZ ruled out interest in the current merger, this by no means rules them out from future mergers/acquisitions.¹⁷

IAG CEO, Mr Mike Hawker indicated that IAG could possibly make another one or two acquisition announcements in 2007.¹⁸

FSU experience suggests that rationalisation decisions are oriented towards short term profit outcomes that have detrimental impacts on the interests of consumers, employees, communities and the industry.

The FSU strongly supports that the ACCC needs to look at the totality of the proposed outcome and all the proposed flow-on effects.

Undertakings

Past performance is often the best predictor of future performance. Based on our experience with mergers involving large finance sector organisations, FSU believes that the undertakings provided by merging organisations were often complied with in a perfunctory and minimalist fashion rather than observed in good faith.

In some cases, complex processes appear to be built into undertakings transactions, sometimes obscuring the outcome and often providing companies leeway to avoid or dilute the impact of the undertakings.

FSU supports the ACCC being given authority to build extra safeguards into undertakings.¹⁹ For instance, clauses that ensure the wording of the undertaking will be interpreted with regard to the objectives of the parties, as set out in the undertakings document as well as any ancillary documentation.

FSU also supports the suggestion of appointing an independent auditor with appropriate industry expertise whose job it will be to monitor, day by day, that companies are living up to the legally enforceable promises they make.

¹⁷ Brett Clegg and Stewart Oldfield, "Suncorp in \$7bn bid for Promina", [Australian Financial Review](#), 12 October 2006, Katherine Jimenez, "Westpac eyes the sun but mum on Suncorp", [The Australian](#), 3 November 2006

¹⁸ "IAG to lodge submission to ACCC over Suncorp-Promina merger", [AAP Financial News Wire](#), 15 November 2006

¹⁹ Graeme Samuels (Chairman, ACCC), "Regulator seeks best outcome for all", [Australian Financial Review](#), 30 October 2006

Review of M & A activity

The FSU is concerned that while there are mechanisms to identify competitive and prudential problems, there is no mechanism to evaluate the impact of mergers on people, communities and society.

Under the Financial Sector (Shareholdings) Act 1998 the Treasurer has discretion to approve or block a proposed merger, however there are currently no guidelines or process regarding types of issues that should be considered or the appropriate forums for consultation with effective parties.

FSU holds the view that issues such as jobs, services and regional impacts should be formally and publicly considered as part of any merger proposal review.

Conclusion

In summary, the FSU is opposed to the merger on the basis that:

- it will create market concentration levels in certain insurance markets that will result in a substantial lessening of competition;
- it will compromise the ability of competitors to exercise countervailing power in general insurance should all existing brands under the Promina and Suncorp umbrellas come under control of one entity;
- job losses will have a detrimental impact on services and communities; and
- pressure will be increased for further mergers in the finance sector.

It is the view of FSU that the only basis for the ACCC allowing the merger to proceed would be as a result of significant divestiture of insurance brands, operations and products; and/or through the process of the ACCC satisfying itself of market concentration thresholds and competition in the industry by receiving enforceable undertakings from the merger partners.

FSU experience in the previous mergers of large financial institutions has highlighted not only reductions in competition and service but the absence of any benefits beyond those to shareholders and senior executives holding stock. It is also clear that mergers of essential service providers such as banks and insurance companies impact on a wide range of issues beyond narrow definitions of competition.

We encourage the ACCC to adopt a broad definition for the public interest test. Further, we encourage the ACCC to ensure that any undertakings are clear with transparent and quantifiable monitoring arrangements. Finally, we encourage the ACCC to take account of the 'domino effect' of this merger on further industry rationalisation.

If you have any questions in relation to this submission please contact James Bennett on (03) 9261 5321.

Yours sincerely

A handwritten signature in black ink, appearing to be 'Paul Schroder', is written on a light-colored rectangular background. A thin red vertical line is visible to the right of the signature.

Paul Schroder
National Secretary

23 November 2006