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Foreword

The financial sector in the Netherlands is and remains an important area of attention for the Netherlands Competition Authority (NMa). A spear point is the annual publication of the *Financial Sector Monitor* (FSM). We are pleased to present you with the third edition. The previous two editions mainly presented market-wide scans which focused on identifying risks. *The Financial Sector Monitor 2005* gives greater emphasis to market outcomes.

A number of developments in the past year have shown that the increased attention paid by NMa to the financial sector has borne fruit. In the wake of the Interpay case, there is evidence of nascent competition on the market for PIN payments. The minimum discount of one eurocent on PIN tariffs for retailers, agreed by banks and retailers, may reinforce this dynamism. In addition banks and retailers intend to work together in developing a more efficient system of payments. Most probably new competition issues will arise as a result. NMa will therefore continue to monitor developments in the area of payment services actively.

Another result of the intensified contacts with the sector is the growing awareness in the banking and insurance sector of the standards set by the Competition Act. This is apparent, for instance, from the increasing need for informal opinions, for instance on the setting up of Currence (the owner of the payment services products, PIN and Chipknip, and the successor of Interpay) and the Payment Services Covenant 2005 [*Convenant Betalingsverkeer 2005*]. This increased awareness is also apparent from the intensified consultation with the sector on matters relating to competition law. This concerns, for instance, the model compliance programme drawn up by the Dutch Association of Insurers in consultation with NMa, which has been implemented by most insurers. Following our invitation to attend the FSM symposium 'Electronic Payments Services: Competing in a Changing Market?' (*'Elektronisch betalingsverkeer: concurreren in een veranderende markt?'*) the Dutch Bankers's Association [Nederlandse Vereniging van Banken (NVB)] is considering introducing a similar programme.

The European dimension is playing an increasingly important role in current developments. The European Commission and the Member States have started paying more attention to the financial sector. The European Commission last year started conducting sector enquiries into retail banking and business insurance. The number of active members of the 'Financial Services Working Group', a European working group which analyses economic problems in relation to competition in the various European Member States has increased considerably under the chairmanship of NMa.

NMa's mission is to 'make markets work'. Monitoring markets, such as the financial sector, and publishing the insights obtained, makes a considerable contribution to this as it promotes an autonomous enforcement effect. The emergence of competitive financial markets demands a permanent effort. NMa will therefore continue to monitor the financial sector intensively in the coming years.

The Board of the Netherlands Competition Authority,

P. Kalbfleisch

R.J.P. Jansen

G.J.L. Zijl

1 The Financial Sector Monitor in 2005

1.1 Introduction

In earlier publications of FSM, it was concluded that there is a high risk of restrictions on competition in the financial sector. The sector is highly concentrated, there are considerable cross holdings and there is information asymmetry between buyers and sellers. The products offered in this sector are often complex and usually have a long-term character. As a result, the relationships between buyers and sellers are close. In addition, the financial sector is characterised by a wide variety of activities, types of institutions and product-market-customer combinations. Finally the sector is special due to its considerable importance to the Dutch economy and the intensive prudential and behavioural supervision to which it is subjected.¹

These factors emphasise the necessity for monitoring competition in the financial sector on a structural basis. FSM does so by carrying out economic research on a structural basis into competition on the various submarkets of the financial sector. This research analyses the risks of limited competition in the sector, for instance on the basis of structural characteristics, or analyses the competition process and market outcomes. Where possible, FSM shares the insights and analyses resulting from this research with the sector, for instance by publishing the annual *Financial Sector Monitor*. Structural monitoring has three complimentary effects, which contribute to a considerable degree to NMa's mission, namely 'making markets work'. Firstly, structural monitoring of the financial sector and the publication of insights and analyses resulting from this increases awareness of the standards contained in the Competition Act and the importance of compliance with the Act. This results in an autonomous enforcement effect. Secondly, structural monitoring contributes to efficiently prioritizing oversight, ensuring that investigations into infringements of the Competition Act are conducted effectively, and provides support in assessing mergers and acquisitions. Finally, the insights acquired provide starting points for policy recommendations, for instance where anti-competitive structures fall outside the scope of the Competition Act.

In this chapter, firstly an overview is provided of the activities of FSM in 2005. After this, the success factors for market research, which FSM has identified in the first three years of its existence, are discussed briefly.

Finally, it should be noted from the outset that the term 'markets' is used frequently in this Monitor. This does not mean, however, that these markets coincide with the definition of relevant markets under competition law.

1.2 Activities of FSM in 2005

Various phases in monitoring research

The characteristics of the financial markets were analysed in early editions of the *Financial Sector Monitor*. An analysis was also made of the extent to which competition is at risk on certain submarkets. In most cases, various indicators were researched which, considered in

relation to each other, provide an estimate of the risk from the perspective of competition. This is an initial phase in monitoring research. Typical examples of such research in the *Financial Sector Monitor 2004* are the chapters on competition between insurance brokers, competition on the share market and the international comparison of the markets for PIN services. An example of this in the *Financial Sector Monitor 2005* is the research into the market for healthcare insurance in chapter 5.

A second phase of monitoring research builds on the earlier risk estimates and provides greater depth. This *Financial Sector Monitor 2005* contains research into several areas which fall within the second phase. This is the research into the areas of interbank charges (chapter 6), the market for coinsurance (chapter 7), and the market for investment funds (chapter 8).

A third phase in the monitoring research involves establishing the extent to which economic risks in relation to competition which arise can be translated into actual market outcomes. This third edition of the *Financial Sector Monitor* focuses for the first time more specifically on the outcomes of the competition process. The chapters which fall into this category are chapter 2 on competition between insurance brokers, chapter 3 on the effects of the recent transfer of PIN contracts to banks, and chapter 4 on entries and exits in the banking sector. In some of the research, use is made of econometric methods and techniques, because these make it possible to draw conclusions which are substantiated better. In the coming years, quantitative analyses will play an ever more important role in research by FSM.

In addition, there are further reasons for focusing on the outcomes of the competition process. Firstly, the financial sector is undergoing rapid change. Changes initiated by the sector, such as the setting up of Currence and the transfer of PIN contracts, or changes as a result of government policy, such as the introduction of the Financial Services Act [*Wet financiële dienstverlening (Wfd)*] and the introduction of a new healthcare system, are aimed at making the market more efficient, increasing competition or addressing market failure. In particular, where changes affect competition it is important to establish what effect they have. The research reported in chapter 2 on competition between insurance brokers serves as an example of this. On the basis of this base measurement, it will be possible for further research to clarify what the effect of the Financial Services Act is on competition in this sector.

Secondly, changes on the market are sometimes the result of regulation by NMa. It is important to measure what the effect of such changes is. In the wake of the Interpay case, for instance, the dynamism of the market for PIN payment services appears to have increased. The discount of one eurocent on the PIN tariffs charged to retailers, agreed by the banks and retailers, may reinforce this dynamism. The research reported in chapter 3, analyses the PIN payment tariffs charged to retailers. Price trends on this market will have to be monitored closely to determine what the effects of the agreed minimum discount are. A further consequence of regulation by NMa is the process whereby the sector appears to be growing more aware of the standards set by the Competition Act. This process is apparent, for instance, from the compliance programme initiated by the insurance sector itself. The programme has been implemented by almost all insurers and is being followed in the banking sector. Important research which will start next year is the monitoring of how effective the

compliance programme in the insurance sector has been. This will be done in cooperation with the Dutch Association of Insurers.

Contacts with other regulators

The contacts with other regulators have been intensified. At the operational and management levels, agreements have been reached with the Dutch Central Bank [*Nederlandsche Bank (DNB)*] with regard to regular consultation and consultation on an informal basis about matters which affect each other's regulatory duties. The contacts with the Netherlands Authority for the Financial Markets [*Autoriteit Financiële Markten (AFM)*] have been strengthened. FSM regularly seeks contact on an informal basis to share insights and analyses. Regular consultation takes place with the Ministry of Finance with regard to findings about the sector. In a number of areas of research, FSM cooperates with the Netherlands Bureau for Economic Policy Analysis [*Centraal Planbureau (CPB)*] and the Dutch consumers' association, *Consumentenbond*, and discussions were held with various branch associations.

Increasing international attention

An important international development was the commencement of sector research into the financial sector by the European Commission. The Commission has initiated sector enquiries into retail banking and business insurance, and has been partly inspired by the active approach of competition authorities, such as NMa. This research has a strong monitoring character and will be completed in the course of 2006. The increased international interest of competition authorities in the financial sector is also apparent from the increase in the size of the 'Retail Banking and Payment Systems Working Group', which is chaired by NMa. This is a working group of the European Competition Authorities in which, in addition to the competition authorities of the United Kingdom, Ireland and Sweden, those of Germany, France and Denmark now also actively participate.

1.3 Success factors

Various lessons have been learned from the three years of active research. These lessons are set out in this section in terms of four success factors. The extent to which the success factors are important, differs per area of research. The order in which they are presented is therefore not intended to reflect their order of importance.

Consistency

An initial, important conclusion after three years of active research is that consistency is a success factor. In this regard, consistency is understood to mean building further on insights obtained and on earlier analyses. Where research leads to the conclusion that there is a high degree of risk to economic competition in a certain market segment, it is important to examine whether and in what way this risk manifests itself. Empirical research into the outcomes of the competition process is necessary for this. This makes it possible to obtain a complete overview of the competition, based on data analyses.

Scientific basis

The research which FSM conducts must have a scientific basis. This is a second important success factor. It means that conclusions are substantiated by evidence and economic analyses based on reliable data and that hypotheses are presented as such. By opting for this point of departure, FSM has acquired a reputation for sound and reliable research.

Active approach

Not all structures and practices which possibly have the effect of restricting competition fall within the scope of the Competition Act. Where, for instance, structural characteristics are the cause of restrictions on competition, the Competition Act does not always provide guidelines for intervention by NMa. Often other institutions are better equipped to deal with structural shortcomings or market failure. It is therefore important that FSM's findings are communicated actively. This ensures that FSM's research makes the maximum contribution to improving the operation of market forces. An active approach is therefore the third success factor.

Accessibility

Finally FSM is read by a broad audience. Irrespective of the reader's level of knowledge, the reader must be able to understand the results of FSM's analyses. This ensures that the research is widely known and has the maximum effect. FSM's findings of must therefore be communicated in an accessible way.

1.4 Structure

The structure of the *Financial Sector Monitor 2005* is as follows. The first three chapters focus on market outcomes. Chapter 2 contains an empirical analysis of competition between insurance brokers. This chapter builds on research into competition between insurance brokers in the *Financial Sector Monitor 2004*. The effect of the distribution channel used for the purchase of a lump-sum policy (purchased through an insurance broker or directly from an insurer) is central to the analysis. The study is closely related to current developments, as appears from the overview of current market trends in section 1.5. The effect on market outcomes of the transfer to the banks of PIN contracts by Interpay is the topic of chapter 3. An analysis is given of the prices which retailers paid for PIN transactions before and the price which they have paid since this transfer. We also refer you to the summaries of market trends under the headings 'Increased competition on the market for PIN payments' and 'Breakthrough in negotiations between banks, retailers and the hospitality industry' in section 1.5. Chapter 4 gives an overview of entries and exits in the banking sector. This chapter must be viewed in the light of the continuous attention which FSM pays to entries and exits in the financial sector.

The remaining chapters focus on the structure of the market and have a more descriptive character. Where possible, we draw conclusions about the risk to economic competition. Chapter 5 reflects the developments on the healthcare insurance market and outlines several possible future scenarios. The various scenarios have a variety of possible consequences for the way in which NMa assesses concentrations on this market. In chapter 6, multilateral

payments in two-sided markets are studied, a topic which is receiving international attention from competition authorities. The recent developments are presented on the basis of an overview of the economics literature and an international overview of competition-related cases. This chapter is an extension of the study of the PIN markets in the *Financial Sector Monitor 2004*. Chapter 7 describes competition on the market for coinsurance and builds on the scan of the non-life insurance market in the *Financial Sector Monitor 2003*. The European Commission shares the attention FSM has given to the coinsurance market, as is apparent from the sector research which the Commission initiated in 2005. Chapter 8 outlines the market for investment funds. This chapter is linked to an earlier studies of the sharemarket in the *Financial Sector Monitor 2004*. The Annexes provide an overview of decisions in relation to mergers and acquisitions.

1.5 Market developments in 2005

This section discusses several developments which are important from the perspective of competition and relate to the financial sector in the Netherlands during the first nine months of 2005. It is not a complete overview. However, it does give an impression of the topics relating to competition which are of importance at present in the sector. The headings have been taken from various newspapers and press releases, while the explanatory texts were compiled by FSM.

‘Betalen via nieuwe media?’

[Payments using new media]

(Press Release, Ministry of Economic Affairs, 9 March 2005)

ING, ABN AMRO, Postbank and Rabobank will introduce a common standard for Internet payments, which will be called iDeal. Customers will be able to pay electronically using iDeal through the website of their own bank, a variant of Internet banking. Fortis, SNS Reaal and Friesland Bank have joined this initiative. Web retailers are positive about the single standard and expected growth in turnover in so-called home shopping. The consumers' association, *Consumentenbond*, thinks that the possibility of fraud will be reduced because the customer authorises the bank rather than the supplier. However, according to *Consumentenbond*, this system has the disadvantage that it is not possible to reverse payments if the retailer does not deliver.²

‘Interpolis in handen van Achmea’

[Interpolis acquired by Achmea]

(*NRC Handelsblad*, 28 April 2005)

The activities of Interpolis (Rabobank) and Achmea will be merged. As a result, Achmea will become the largest provider of non-life-insurance and the second largest player in the area of life and health insurance.³ In exchange for the sale of Interpolis, Rabobank will obtain a share of 37% in Eureko, the parent company of Achmea, which owns various insurers, for instance in the Benelux. This will enable Rabobank to continue playing a part in determining the strategy of Interpolis and will increase its influence on the insurance market. NMa concludes that competition on the markets on which the parties are active (banking services, insurance, pension administration, health, safety and welfare services, and reintegration services) will

not be obstructed as a result of the merger of the activities of Interpolis and Achmea, and granted its approval for the merger.⁴

‘Commissie keurt overname van Banca Antonveneta door ABN AMRO goed’

[Commission approves acquisition of Banca Antonveneta by ABN AMRO]

(Press Release Economic Commission, 28 April 2005)

The European Commission has approved the proposed public takeover bid for Antonveneta by ABN AMRO. According to the European Commissioner, Neelie Kroes the proposed transaction is a positive sign of a shift towards a more integrated internal market for financial services.⁵ Cross-border mergers may increase competition and consumer choice, according to the Commission.⁶ ABN AMRO aims to create a second home market in Europe through the acquisition of the North-Italian bank, Antonveneta.⁷ ABN AMRO was embroiled in a takeover battle with the Italian bank, Banca Popolare Italiana (BPI), which also wished to acquire Antonveneta. On 16 September 2005, the Board of Directors of BPI approved the sale of BPI's interest in Antonveneta to ABN AMRO. All the regulators, including the central bank, have now given their approval for the sale.⁸

‘Meer concurrentie op markt pinbetalingen’

[Increased competition on the market for PIN payments]

(*Het Financieele Dagblad*, 18 May 2005)

There is a new player on the market for payment services: Currence.⁹ With the setting up of Currence by Interpay, the regulations have been separated from the processing of payments. Currence is now the owner of the brands of collective payment products in the Netherlands, including PIN and Chipknip.¹⁰ As the owner of these brands, Currence first of all sets criteria for the parties which use these brands. Financial institutions can only offer these payment products on the market if they have received a licence to do so from Currence.¹¹ Secondly, Currence certifies third parties who wish to carry out some functions in the area of payment services, such as processing, supplying terminals and supplying cards.

‘Banksector bespreekt gedragscode met NMa’

[Banking sector discusses code of conduct with NMa]

(*Het Financieele Dagblad*, 28 May 2005)

The Dutch Bankers's Association (NVB) has announced that it intends to consult NMa about drawing up an internal code of conduct for competition cases. A so-called compliance programme was introduced at the end of 2004 in the insurance sector (see the overview below). The code of conduct in the banking sector, according to NVB, will cover payment services, the settlement of securities transactions and the interbank market.

Compliance programme for insurers

On 17 November 2004, the Dutch Association of Insurers published a model compliance programme. The programme was drawn up in cooperation with NMa. During the General Meeting of Members of the Association on 15 December 2004, the compliance programme was incorporated into the Code of Conduct for Insurers. According to the Dutch Association of Insurers, 99% (measured on the basis of premium income) of the insurance companies have already signed the code of conduct and, by doing so, the compliance programme.

Signatories are not compelled to adopt the model compliance programme without amendment.

The model compliance programme contains the following main points:

Target group

- *The compliance programme focuses on the Executive Board or Management Board and managers and employees who maintain contact at a policy and/or commercial level with competitors and/or insurance brokers (the target group).*
- *The employees who belong to the target group are required to have a basic knowledge of the application of the Competition Act to the commercial activities of the undertaking. They will receive substantive information periodically about the Competition Act.*
- *An infringement of the Competition Act may have consequences for the employee under labour law.*

Position of the Compliance Officer (CO)

- *The CO has a proactive role within the organisation in preventing, investigating and terminating any practices and statements which are contrary to the Competition Act.*
- *The CO is appointed by the Management Board and is only accountable to the Management Board.*
- *The CO is entitled to inspect documents, to organise audits and to provide the Management Board with unsolicited advice.*

Notifications/consultations

- *Notification of the CO is obligatory if in retrospect practices and/or statements appear to be contrary to the Competition Act.*
- *If employees doubt whether a certain practice/statement is contrary to the Competition Act, the CO must be consulted.*
- *If the CO suspects an infringement or concludes that an infringement has been committed, he must notify the Management Board of this.*

'Doorbraak onderhandelingen banken, winkeliers en horeca'

Breakthrough in negotiations between banks, retailers and the hospitality industry

(Press Release by the Dutch Bankers' Association, 8 June 2005)

The banks, acceptors of PIN transactions and Interpay have reached agreement on the covenant to be drawn up. In the discussion about more efficient point-of-sale payments, the tariffs paid to Interpay became the centre of attention. On 29 April 2004, NMa concluded in its decision to impose a sanction that these tariffs had been too high in the period from 1998 up to and including 2001. The Letter of Intent which was signed indicates that the covenant is intended to settle the dispute about high tariffs for electronic payments and to promote efficiency in the area of point-of-sale payments. The covenant includes, for instance, agreements on a reduction in PIN tariffs. As compensation for this, the complaints and claims in relation to excessive PIN tariffs will be withdrawn.¹² On 17 November 2005, NMa indicated in an informal opinion that the discount scheme proposed in the Covenant did not restrict competition.

‘Kroes start met groot onderzoek kartels in de EU’

[Kroes starts extensive research into cartels in the EU]

(Het Financieele Dagblad, 14 June 2005)

The European Commission has started broad sectoral research into the degree of competition in, for instance, the retail banking and insurance sectors in the European Union. The research into the banking sector will focus on debit and credit card charges, which can differ by percentages which run into double figures between Member States, and on tariffs for transactions with other countries. In the insurance market, research will be done into the business insurance (for buildings and other assets), the reinsurance segments, and intermediaries.

‘Minder provisiejagen’

[Chasing after commission]

(Het Financieele Dagblad, 11 July 2005)

The Minister of Finance has proposed two policy measures to ensure that the market for distribution through brokers works better.¹³ Firstly, the ratio between upfront fees and recurring commission must be adjusted. This results in more even settlement of commission throughout the life of a product, which will limit the incentive for 'chasing after commission' in the short term. Secondly, a statutory obligation to provide transparency with regard to remuneration will be introduced. This will take effect as of September 2009 and will be included in the subsidiary legislation and regulations governed by the Financial Supervision Act [*Wet financieel toezicht (Wft)*]. This will give consumers more insight into the costs of advice with the aim of promoting competition between insurance brokers.

‘Luxemburg lonkt’

[Seduction by Luxembourg]

(Het Financieele Dagblad, 16 July 2005)

Due to its attractive tax regime, Luxembourg is gaining popularity as a domicile of investment funds. Amongst others, ABN AMRO, Robeco and Fortis have decided to relocate their funds from Euronext to Luxembourg. The departure of investment funds from the Netherlands is continuing despite numerous initiatives to improve the climate for business in the Netherlands, such as the proposal by the Winter Commission to abolish the obligatory listing of investment funds.¹⁴ One of the relaxations of fiscal rules announced by the Ministry of Finance is the abolition of capital tax as of 1 January 2006.¹⁵

‘Euronext kan bod op LSE uitbrengen’

[Euronext may bid for LSE]

(Het Financieele Dagblad, 2 November 2005)

The British competition authority, which assesses mergers (the Competition Commission), has carried out an investigation into a possible takeover of the London Stock Exchange (LSE) by Euronext. This investigation has concluded that Euronext must reduce its interest in LCH.Clearnet from the present 41.5% to less than 15% if it wishes to make a bid for LSE.¹⁶ LCH.Clearnet is responsible for settling share transactions for Euronext and LSE.¹⁷ The Australian Macquarie Bank and the Swedish listed stock exchange company OMX are

apparently also interested in acquiring LSE. In addition, Deutsche Börse, which earlier left the field under pressure from its shareholders, is also holding out the possibility of making a bid.

2 Competition between insurance brokers

2.1 Introduction

Life insurance policies play a considerable role in the financial planning of households. Through the advice they give consumers, insurance brokers are an important link between insurers and consumers, when consumers choose such insurance policies. In the *Financial Sector Monitor 2004*, NMa reported on its research into the market for insurance brokerage.¹ This research involved a broad market scan based on desk research and interviews with market parties. The analysis concluded that the incentives which insurers give insurance brokers possibly affect the advice that consumers are given by insurance brokers. These incentives, such as bonuses, forms of financing, production obligations and commission, in combination with the consumers' tendency not to search and switch, may result in a lack of competition and suboptimal advice. The preliminary conclusion was therefore that there was a risk that competition was restricted, in the sense of inefficient market outcomes were.

Following the research conducted in 2004, attention was also paid in 2005 to the market for advice given by insurance brokers. FSM has substantiated its preliminary analysis done in 2004 on the basis of empirical research. In cooperation with the Netherlands Bureau for Economic Policy Analysis (CPB), econometric research was conducted into the choices made by consumers. In particular, research was done into the effects of using an insurance broker on the purchase of lump-sum policies. The outcomes of this research were recently published in a joint report by NMa and CPB.² In addition, a consultation document was published by NMa.³ On the basis of the responses to the consultation document and CPB's research, NMa developed an analysis of the sector which is set out in this chapter.

Section 2.2 summarises the responses to the consultation document. In section 2.3, the survey carried out for the quantitative research is described and the results of the econometric analysis conducted in cooperation with CPB are discussed. Section 2.4 contains several conclusions.

2.2 Responses to the consultation document

The aim of the consultation document was to share with market parties the preliminary outcomes of the research by FSM into the structure of the distribution channel through insurance brokers and the way it works. The document contained 11 consultation questions. In total, 32 responses were received, of which 18 from insurance brokers, four from franchise or procurement organisations of insurance brokers, four from branch organisations, three from insurance companies, two from regulators and one from a consumer organisation. The answers to a number of questions are discussed in this section.⁴

The responses generally tend to confirm that NMa's outline of the market is correct and provided a sound analysis of the current market situation. A remark which was frequently made is that the sector is undergoing considerable change.⁵ This is the result of the

introduction of the Financial Services Act and the accompanying changes in regulation, as well as changes in the economic climate.

With regard to a number of consultation questions, the answers presented a uniform picture. All the responses received in answer to the question of how consolidation in the sector will develop indicated it was expected to increase. The number of small insurance brokers, in particular, will decrease, according to the respondents. In response to the question of how the importance of procurement organisations (undertakings which bundle the joint production of small insurance brokers through joint procurement) and the underwriting cooperatives (cooperative associations which enable insurance brokers to purchase insurance from insurers with which they have not entered into agency agreements) will develop, 84% of the responses indicated that this will grow. Only 8% indicated that they expected no further growth. Of the parties which responded, 69% indicated that they expected the importance of sales through multiple distribution channels to increase. In answer to the question with regard to the scale at which financing occurs within the insurance broker distribution channel, 67% stated that they did not have enough information on this. According to 17% of respondents, financing occurs on a considerable scale by offering current account facilities subject of favourable conditions.

However, market parties express conflicting opinions on the expected development of the number of insurance brokers in which insurers have a majority shareholding (captives). The majority (31%) did not have an opinion on this, while 23% thought that the number of captors will increase and an equally large percentage was of the opinion that it will decrease. On the consequences of majority shareholdings held by insurers in insurance brokers, roughly half (46%) of the respondents stated that this will result in preferential treatment by the parent company, while 31% was of the opinion that this will not have an effect. Of the respondents, 8% claimed that a majority shareholding will improve the quality of advice. In answer to the question as to whether consumers have sufficient insight into the remuneration of insurance brokers, 46% stated that in their view consumers are not interested in the remuneration of insurance brokers, while 31% thought that consumers have too little insight into this. In response to the question of how obstacles to searching and switching behaviour could be removed, 38% stated that this can be done by providing more transparency with regard to costs and the role of the adviser, while 31% argued that the consumer was not interested in financial products, which is the reason that searching and switching behaviour is absent. It was stated in 15% of the responses that comparative sites on the Internet could play an important role in this.

2.3 Survey

Together with CPB, FSM carried out research into the effect of the use of insurance brokers on the choice of products by consumers when purchasing lump-sum policies and the factors which determine whether consumers make use of insurance brokers. Lump-sum policies are financial products for which advice is important, although they are relatively standardised. For a lump-sum policy, a consumer pays a single or periodic premium; at the end of the insurance term, the customer is paid an amount.

There are two types of lump-sum policies. In the case of the one type of policy, the payment at the end of the insurance term is guaranteed (a guaranteed lump-sum policy). In this case, the consumer is assured of the final amount to be received and incurs no risk that this final amount will be higher or lower than expected. In the case of the other policy, the premium is invested in a unit-linked portfolio (unit-linked lump-sum policy). The payout depends on the performance of this portfolio and the level of this is therefore uncertain. The consumer therefore incurs the risk that the final amount will be higher or lower than the expected payout.

A panel from Centerdata was used for this survey. This panel consisted of 2000 people and was representative of the population of the Netherlands.⁶ In earlier research, Centerdata collected data on the purchase of lump-sum policies by the member of its panel. This related to the number of policies purchased, the type of policy, the date of purchase and the insurer from whom the product was purchased. Our survey therefore focuses on the way in which the product was purchased (through an insurance broker or directly from an insurer) and the sources of information used in making the purchase.

In addition to many personal characteristics (sex, income, age and education), it is known how risk averse the members of the panel are and how much they think they know about financial products. Risk aversion was measured by putting the following proposition to consumers: 'I consider it more important to invest safely and to obtain a guaranteed return than to take risks in the hope of obtaining the highest return'.⁷ The extent to which respondents thought that they had financial expertise was measured by asking consumers the question: 'How knowledgeable do you consider yourself to be in the area of finance?'⁸

On the basis of the choices made by respondents and their personal characteristics, an analysis was done of the relationship between consumer choice and the use of a particular distribution channel (insurance broker or direct) and the factors which influence the selection of distribution channel.

The questionnaire was completed by 368 respondents from 361 different households. In total, they purchased 562 policies. Of these, it was not possible to determine the type of product purchased for 23 of the policies. Of 23 more policies it was not possible to determine the distribution channel through which products were purchased. Of the remaining 518 policies, 287 were unit-linked lump-sum policies, of which 149 were purchased through an insurance broker and 138 directly from an insurer, and 231 were guaranteed lump-sum policies, of which 115 were purchased through an insurance broker and 116 directly from an insurer.

Firstly, on the basis of the results of the survey, the searching behaviour of consumers, their knowledge of the remuneration of insurance brokers and the effect of this knowledge on their searching behaviour was determined.

Figure 2.1 indicates for each source of information the percentage of respondents which used this source of information. The percentages have been broken down on the basis of respondents who purchased a lump-sum policy through the direct channel and respondents who did so through an insurance broker. The sum of the percentages exceeds 100% because

respondents may have used more than one information source. Of the respondents who purchased a lump-sum policy through an insurance broker, 75% used information from a single insurance broker. It is therefore important that this insurance broker provides the consumer with sound information. Of the respondents who purchase through the direct channel, 36% use information obtained from a single bank. Other relatively important sources of information are the newspaper, financial magazines, the brochures of insurers, and friends and family. Slightly more than 20% of consumers who purchase a lump-sum policy through the direct channel seek advice from an insurance broker.

Figure 2.1 Information sources used by consumers

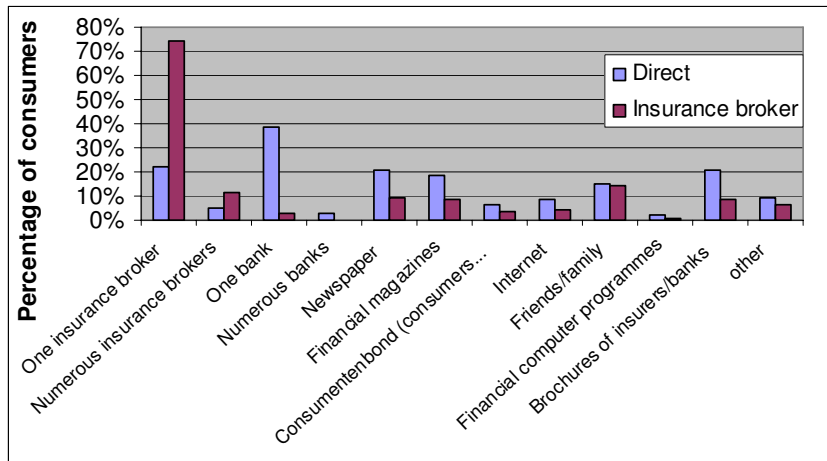
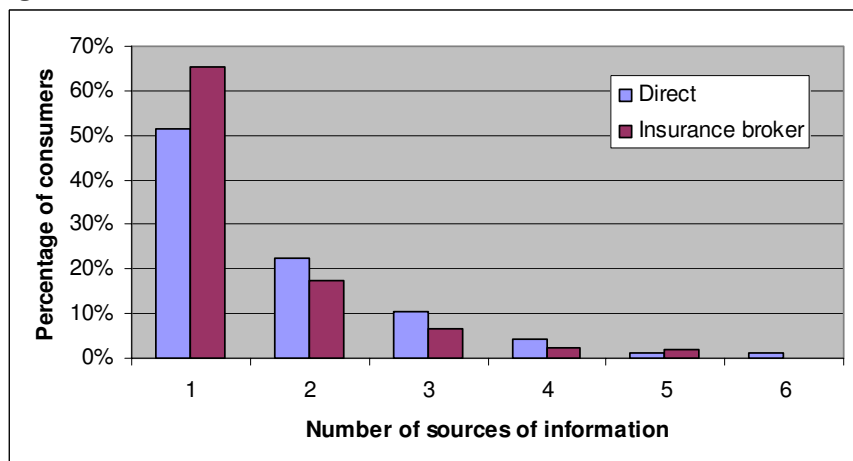


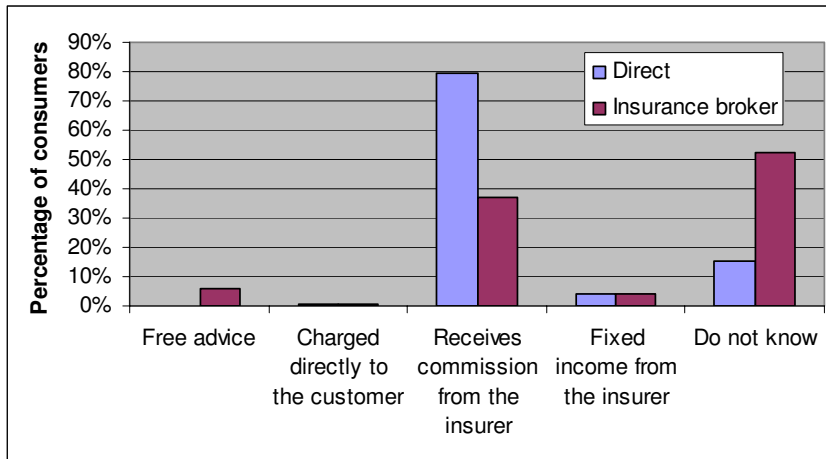
Figure 2.2 provides an overview per distribution channel of the number of sources of information which consumers use. It emerged from the answers given by the panel that 28% of consumers who purchase a product through an insurance broker used two or more sources of information. Of the consumers who have purchased a lump-sum policy through a direct channel, 40% use two or more sources of information. In both cases, 'family or friends' were the sources of information cited most frequently after 'one insurance broker' or 'one bank'.

Figure 2.2 Number of information sources consulted



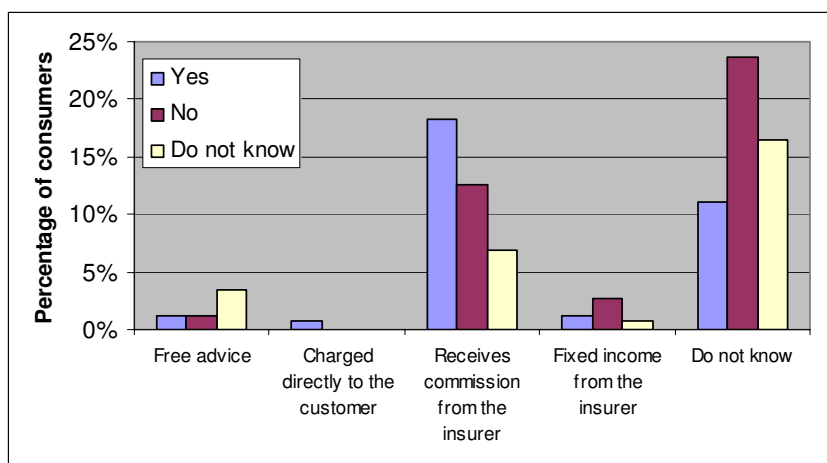
It appears from figure 2.3 that 80% of the respondents who purchase a lump-sum policy through the direct channel, know how an insurance broker is remunerated. Of the respondents who purchase a lump-sum policy through an insurance broker, more than 50% know how insurance brokers are remunerated. This seems to indicate that consumers who know how insurance brokers are remunerated, purchase a lump-sum policy more often directly from an insurer than consumers who do not know.

Figure 2.3 Knowledge of remuneration of insurance brokers



Finally, figure 2.4 shows the percentage of insurance brokers that discussed numerous offers with a respondent, with a breakdown on the basis of knowledge of the way in which the insurance broker is remunerated. Where respondents do not know how an insurance broker is remunerated, the probability that only one offer was discussed is greater than the probability that numerous offers were discussed. Where respondents do know how insurance brokers are remunerated, the exact opposite applies. Where respondents know how an insurance broker is remunerated, the probability that only one offer is discussed is smaller than the probability that numerous offers are discussed. This suggests that consumers who know how an insurance broker is remunerated receive more extensive advice.

Figure 2.4 Number of providers discussed versus knowledge of the method of remuneration



2.4 Analysis of consumer choice

On the basis of the panel data, an econometric analysis was done of the choices made by consumers with regard to the sales channel, type of product and insurer.⁹ In the case of respondents who indicated that they had purchased more than one lump-sum policy, only the first lump-sum policy purchased was taken into account in the analysis.¹⁰ An attempt has been made in this section to abstract from methodological issues and, where possible, technical comments have been made in the footnotes.

Choice of distribution channel

The choice of distribution channel was analysed first: which factors determine the distribution channel through which consumers purchase a lump-sum policy?

The results of the estimates are given in table 2.1. The estimate model is a so-called logitmodel. This model provides an estimate of the probability that a respondent will opt for a particular distribution channel. The following explanatory variables were used: knowledge of the way in which the insurance broker is remunerated; the degree of financial expertise which the respondent thinks he or she has; the age of the respondent at the moment that the lump-sum policy was purchased; the natural logarithm of the respondent's income; the level of education; and the respondent's sex.¹¹

Table 2.1 Results of the estimates of the choice of distribution channel (n = 270)

Knowledge of the way in which the insurance broker is remunerated	-1.977*
Declared financial expertise	-0.346
Age	-0.050*
Income (log)	0.323
Level of education	-0.658*
Sex	0.273
Constant	1.157

* = This parameter is significant at the 5% level.

Three variables appear to be important for the choice of distribution channel. The first is awareness of commission. The results of the survey showed that where consumers are aware of the way in which insurance brokers are remunerated, they are less inclined to purchase a lump-sum policy through an insurance broker. This effect is considerable. A consumer (male, 40 years, EUR 24,000 gross annual income, a low level of education) who knows how the insurance broker is remunerated, is 30% more likely to purchase a lump-sum policy directly from an insurer than a consumer who is not aware of the way in which the insurance broker is remunerated, but for the rest has the same characteristics. Age appears to be a second factor which affects the choice of distribution channel. The older the consumer, the lower the probability that an insurance product will be purchased through an insurance broker. A consumer (no knowledge of the method of remuneration, and for the rest the same specifications as above) aged 40 is roughly 5% less likely to purchase a product directly from an insurer than a consumer aged 30. Finally, the level of education is important. The better educated the consumer is, the lower the probability that a lump-sum policy will be purchased through an insurance broker. A consumer (again the previous specifications apply) who is highly educated, is 5% more likely to purchase a lump-sum policy directly from an insurer than a consumer who has a low level of education.

Choice of product type

Second, the factors which influence the type of product selected (a lump-sum policy versus a risk-bearing unit-linked lump-sum policy) were identified for each distribution channel. If insurance brokers advise their customers well, a relationship would be expected between the choice made by the consumers and their risk preference.

The estimated results are provided in table 2.2. Estimates are given on the basis of two models: one for respondents who purchased a lump-sum policy through an insurance broker and one for respondents who purchased a lump-sum policy directly from an insurer. In both cases, a logitmodel was estimated. The variable to be explained is the probability that a guaranteed lump-sum policy will be selected. The explanatory variables are: the degree of risk aversion, the natural logarithm of the respondent's annual income, a year dummy for the period 1995 to 2001, the respondent's age at the moment of purchase of the lump-sum policy and the product of demonstrated expertise and risk aversion.¹² The distribution channel through which a product is purchased does not appear to affect the type of product selected: the significant explanatory variables differ per distribution channel.¹³ In the case of consumers who purchased a lump-sum policy directly from an insurer, risk aversion is important. The higher the level of a consumer's risk aversion, the sooner he or she will be inclined to opt for a lump-sum policy with a guaranteed payout. This is an indication that the risk aversion which consumers themselves declared corresponds to the risk preference which they manifest in their behaviour.

Table 2.2 Estimated results of the preference for a guaranteed lump-sum policy per distribution channel

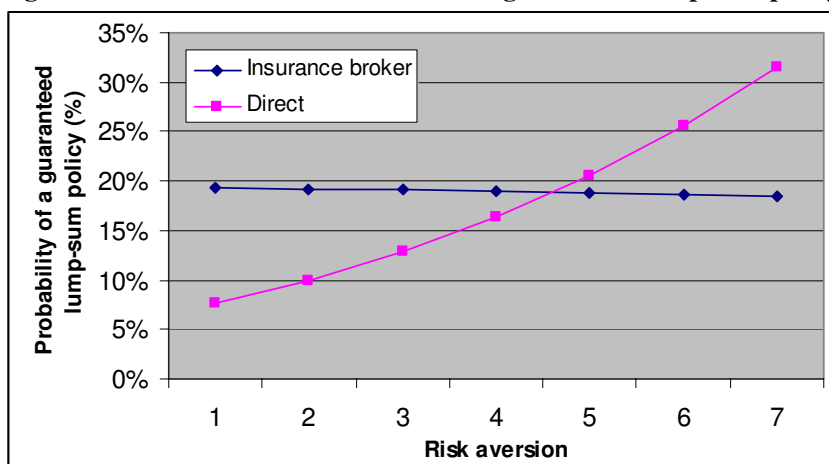
	Through an insurance broker (n = 146)	Direct (n = 121)
Risk aversion	-0.010	-0.285*
Income (log)	-0.483	0.279
Year dummy 1995-2001	-1.430*	-1.469*
Age	0.014	0.001
Risk aversion * demonstrated expertise	-0.256	-0.002
Constant	4.327	1.470

* = This parameter is significant at the 5% level.

Risk aversion does not seem to influence the probability of selecting a unit-linked lump-sum policy or a guaranteed lump-sum policy in the case of consumers who purchase a lump-sum policy through an insurance broker. This is represented graphically in figure 2.5. The predicted probability that a certain type of consumer will purchase a lump-sum policy with a guaranteed payout is represented on the vertical axis and the risk aversion of consumers on the horizontal axis (1 means a low and 7 a high level of risk aversion). In the case of a consumer (aged 40, annual income EUR 24,000, in the period 1995 to 2001, and little financial expertise) who purchases a lump-sum policy from an insurance broker, this probability is approximately 20%, depending on the respondent's risk aversion. Consumers who do not wish to take a risk, therefore do not purchase risk-free lump-sum policies more often than consumers who do wish to accept risk when they make use of an insurance broker. In the case of consumers who purchase a lump-sum policy through the direct channel, the probability increases from less than 10% to more than 30%. More risk-averse consumers therefore purchase guaranteed lump-sum policies more often when they do not make use of an insurance broker.

In addition, consumer choice behaviour appears to change over time. In the period that the outlook on the stock exchange appeared good, consumers opted more often for a lump-sum policy with an uncertain payout which depended on the development of the stock market as is to be expected.

Figure 2.5 Risk aversion and selection of a guaranteed lump-sum policy



Choice of insurer

Finally, in the case of lump-sum policies with a guaranteed payout, an assessment was made of how good the consumer's choice is. A ranking of insurers can be made on the basis of the payout of a lump-sum policy with a guaranteed endowment. It is possible to deduce from this how good the product chosen by the consumer was (measured on the basis of the payout).¹⁴ In particular, the effect of using an insurance broker on the choice made was ascertained. Where insurance brokers make a thorough search for their customers, the choice made by consumers, who make use of an insurance broker, is expected to be at least as good as that of consumers who themselves search and purchase a lump-sum policy directly from an insurer.

The estimated results are given in table 2.3.¹⁵ In the case of respondents who purchased a lump-sum policy with a guaranteed payout, it was analysed how good their choice of product was and what factors are important in their choice. For each combination of the year in which the insurance was purchased, age, sex, the type of product and the level of the deposit or monthly premium, a table was compiled with the guaranteed payouts which insurers offer, ranked according to the level of payout.¹⁶ This was done on the basis of data obtained from the consumer association, Consumentenbond, and Moneyview. The result was a table for each respondent on the basis of which it was possible to determine which alternatives there were for the product which was actually purchased. Where there was no table for a particular respondent, the nearest table was chosen.¹⁷ Within the set of possible choices, the deviation from the average guaranteed final payout was a measure of the quality of the choice.

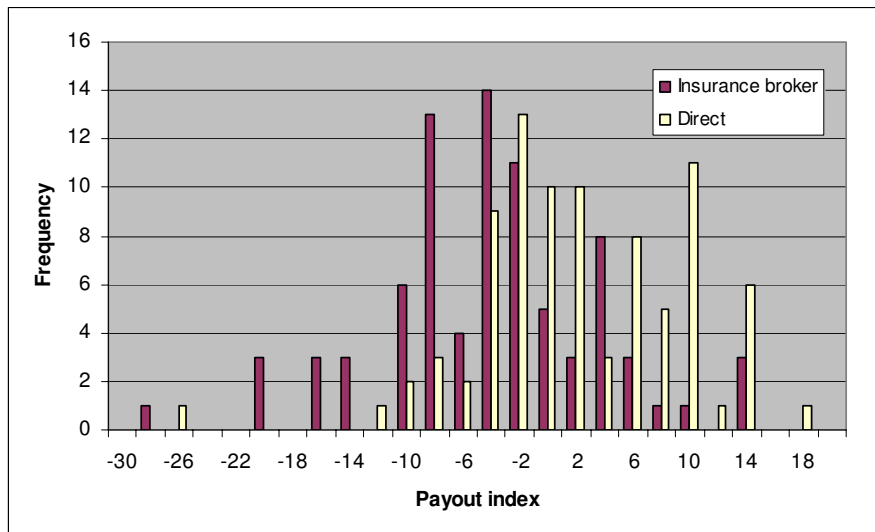
Table 2.3 Estimated results in relation to the choice of insurer

Adviser used	-5.34566*
Number of sources used	0.07899
Level of expertise	-0.78242
The level of education	0.02788
Constant	2.14637*

* = This parameter is significant at the 5% level.

Our analysis showed that consumers who purchase a lump-sum through an insurance broker on average opt for a lump-sum with a lower yield than consumers who purchase a lump-sum directly from an insurer. Figure 2.6 represents as a histogram the actual choices of respondents. The horizontal axis is the relative deviation from the average guaranteed final payout (the payout index). The vertical axis is the number of times that this value occurred. The graph clearly shows that the average yield for consumers who purchase a lump-sum policy through an insurance broker is below the level of the total sample, while consumers who purchase a lump-sum policy directly from an insurer realise an above-average yield. The econometric analysis shows that these differences are significant.

Figure 2.6 Payout index



2.5 Conclusions

The responses to the consultation document show that most market parties concur with NMA's description of the market. Not everyone, however, agreed with the analysis made on the basis of this description. Opinions were also divided on the expected developments. The responses did not lead to new insights.

It appears from the survey amongst the members of the Centerpanel that consumers do not search extensively for the best lump-sum policy. Only 20% of people, for instance, use two or more sources of information to determine their choice of product. The most important second source of information consists of friends and family. In addition, consumers who purchase a lump-sum policy through an insurance broker searched less intensively than consumers who purchase a policy directly from an insurer. This is evidence of the importance of objective advice by insurance brokers.

On the basis of the quantitative research described above, it can be concluded that consumers who made use of an insurance broker when purchasing a lump-sum policy in the period from

1980-2003, on average did not make better choices than consumers who purchased a lump-sum policy directly from an insurer. In the case of consumers who purchased a lump-sum policy through an insurance broker, the risk preference did not affect the type of product purchased. For consumers who purchased a lump-sum policy directly from an insurer, however, risk preference did affect the type of product purchased. In addition, consumers who take out a lump-sum policy through an insurance broker on average opt for products with a significantly lower payout than consumers who purchase a lump-sum policy directly from an insurer. If consumers purchase the product recommended by an insurance broker, this means that on average the advice of the insurance broker when purchasing a lump-sum policy in the period from 1980 to 2003 was suboptimal.¹⁸

In addition, it appears from the analysis that respondents who are aware of the way in which insurance brokers are remunerated, on average purchase a lump-sum policy more often directly from an insurer. This means that transparent information on the remuneration of insurance brokers influences consumer behaviour and is therefore expected to also have an effect on the behaviour of insurance brokers.

The market imperfections described above led the Ministry of Finance to prepare policy measures against commission-driven sales.¹⁹ The aim of these measures is to improve the position of consumers and the information which they have at their disposal in the near future. Firstly, the ratio of the upfront fee and the recurring commission will be gradually adjusted to a ratio of 50/50 by the end of 2009.²⁰ This reduces, for instance, the immediate incentive resulting from a high upfront commission. Secondly, transparency with regard to the level of remuneration will be introduced (on 1 October 2009).²¹ This gives consumers an incentive to examine critically the advice that they purchase and the price that they pay for this, and increases their ability to compare the cost of advice.

In another important development, which will improve the position of consumers, is the coming into force of the Financial Services Act at the end of 2006. The aim of this Act is to provide consumers with better protection by increasing the duty of care of financial service providers and includes, for instance, requirements with regard to expertise, requirements with regard to the provision of information, and requirements with regard to the drawing up and retention of customer profiles. In addition, within the framework of the Decree in Relation to Financial Services [*Besluit financiële dienstverlening (Bfd)*], the financial leaflet was revised with the aim of giving consumers insight into the risk, cost structure and yield of a product in a straightforward way. This decision still has to be debated in the Lower House of the Dutch Parliament and adopted by the Minister of Finance and is expected to come into force on 1 January 2006.

The sector also appears to realise that changes necessary. In addition to the policy measures mentioned above, initiatives have been taken to increase the transparency for consumers through self-regulation. FSM intends to monitor the development of this market closely.

3 Effects of the transfer of PIN contracts

3.1 Introduction

In response to the advice of the Working Group on Tariff Structures and Infrastructure in Relation to Payment Services (hereinafter the "Wellink Commission"), in 2002 the Dutch Central Bank recommended 'that all contracts for PIN transactions should be assigned to the banks in the future'.¹ The aim of this recommendation was to promote competition in the area of electronic payment services. The banks which are shareholders of Interpay then decided that not Interpay, but the individual banks, should enter into and administer contracts with retailers.² In March 2004, the transfer of PIN contracts from Interpay to the banks began.

The contracts relate to the acceptance and processing of PIN payments. The processing of PIN transactions consists, for instance, of the transmission of payment data from the point-of-sale terminal to the bank of the cardholder (switching) and the authorisation of the PIN payments. The authorisation is always done by the banks themselves. Since the transfer of the contracts, the other services, of which Interpay is the only provider, have to be purchased from Interpay.

A transitional period of 60 days applied to contracts with a single retailer, the so-called single contracts, in which Interpay's conditions continued to apply. However, the retailer had the opportunity prior to the transfer to enter into negotiations with its bank on new conditions or to enter into a new contract with a different bank. Initially, Interpay did not stipulate a final transfer date for the transfer of so-called master agreements whereby numerous retailers belonging to a chain or franchise organisation made use of the same contractual conditions. Since the retailers affiliated to a concern or chain usually make use of different banks, the negotiation process on new master agreements often required considerable time. At the beginning of 2005, not all the contracts had been transferred. The contracts which were still in operation with Interpay were cancelled as of 1 January 2005, subject to a period of notice of six months. On 1 September 2005, the last contracts with Interpay were terminated.³ ING/Postbank, ABN AMRO and Rabobank together had acquired 90% of all the new contracts with retailers by mid-2005.⁴

In the past year, FSM carried out research into the effects of this transfer. The central question was what effect this change in the structure of payment services had had on the prices which retailers pay for PIN transactions. This research consisted of two parts. Firstly, the research bureau ECORYS-NEI, in cooperation with NIPO, surveyed a sample of retailers about the transfer of PIN contracts, the negotiation process between banks and retailers and Interpay's role in this. The research results were presented on 10 February 2005 during a symposium organised by NMa with the title 'Electronic Payments Services: Competing in a Changing Market?' (*'Elektronisch betalingsverkeer: concurreren in een veranderende markt?'*).⁵ Secondly, to supplement this research FSM submitted questions in writing to a number of banks about the tariffs which retailers pay for PIN transactions. The results of both research initiatives will be discussed in this chapter.

3.2 Outcomes of the research by NIPO/ECORYS-NEI

In September 2004, NIPO held a telephone survey amongst retailers. In total, 1094 retailers cooperated in this survey, of which 753 were PIN users. The respondents originated from various branches of industry (automobile retailers/repairs, food retailers, non-food retailers, hospitality industry). Although the group was broader than just the retail trade, all the respondents will be referred to below as retailers. Since the distribution over the various branches of industry and companies of various sizes does not correspond entirely in the sample to the distribution in the total population, a correction was made for this difference. Where a group is represented more strongly in the population than in the sample, the answers obtained from this group weigh more heavily in the results.

In September 2004, according to the survey carried out by NIPO/ECORYS-NEI, 78% of contracts had been transferred from Interpay to the banks. Approximately 10% of retailers did not yet have a new contract and the situation of 12% of retailers was unknown. If the number of PIN transactions is considered, however, last year a smaller number were transferred. This is due to the fact that many master contracts, which represent considerable volumes, had not yet been transferred by September 2004. On the basis of our own estimate based on data provided by Interpay, 54% of contracts, measured in terms of volume, had been transferred by 1 December 2004.⁶ The transfer of master contracts gathered momentum at the end of 2004 and, according to Interpay, by the end of August this year the last of the contracts had been terminated.

Provision of information and acquisition by banks

It emerged from the NIPO/ECORYS-NEI that the provision of information by Interpay generally seems to have been good. Most retailers (83%) were aware that PIN contracts had been transferred from Interpay to the banks. Of the retailers, 82% knew that Interpay still processes the transactions. It is clear to the majority of undertakings (65%) that they can negotiate with banks about the conditions applicable to PIN contracts.

Banks appear not to have seized upon the transfer of PIN contracts as an opportunity to acquire new customers. Only 4% of retailers were approached by a bank other than their regular banker about entering into a new PIN contract. Most clients of banks were not approached by their own banker. Although every retailer had to enter into a new contract, in only 34% of cases did the clients' own banker contact them. On the basis of a telephone survey by FSM, it appears that many small companies were transferred automatically and that no consultation took place with their regular banker about new conditions. It does not appear from the information obtained that any one bank sought contact with its clients more than any other bank.

Searching and switching behaviour of retailers

It appears from the research by NIPO/ECORYS-NEI that only 12% of retailers entered into negotiations on the contractual conditions. The two most important reasons for not negotiating, as appears from table 3.1, are: 'satisfied with the regular banker/I do all my

business with a single bank' (25%) and 'did not get around to it/disinterested' (27%). In other words, most of the retailers did not actively look for the lowest price.

Table 3.1: Reasons for retailers not to obtain information about the contractual conditions from banks

Reasons	Number of transactions				
	<1,000	1,001-5,000	5,001-10,000	>10,000	Total
I am satisfied with my bank/I do all my business with a single bank	18%	28%	27%	23%	25%
Priority, did not get around to it/disinterested	23%	23%	27%	31%	27%
It went well, so I did not change anything	13%	11%	9%	7%	11%
I did not know it was possible	10%	9%	10%	14%	10%
We have few PIN transactions, so did not take the trouble	16%	11%	3%	1%	8%
A different bank is not really any better	7%	6%	6%	10%	6%
Red tape, not worth the trouble	10%	6%	1%	2%	6%
I received an offer and just accepted it	4%	2%	5%	4%	3%
My present bank is cheap (the cheapest), favourable conditions	1%	2%	4%	1%	2%
We are tied to a bank	2%	2%	0%	0%	1%
Other/no response	10%	10%	14%	22%	13%

Large retailers negotiated with banks about the conditions more often than small undertakings. Of the 40 large undertakings (with more than 800,000 PIN transactions per year), 76% entered into negotiations on the contractual conditions. In half of all cases, negotiations were only held with their regular banker. The majority of retailers questioned (75%) opted to remain with their regular banker, whether or not after negotiations. Only 3% of retailers switched to a different bank, while 10% indicated that they had not entered into a new contract. In the remaining 12% of cases, the situation is unknown.

It therefore emerges from the NIPO/ECORYS-NEI survey that a few retailers entered into a new PIN contract with a bank other than their regular banker after the transfer. Various possible reasons can be given for this. In 9% of cases, in which the retailer negotiated a new PIN contract with the bank, the purchase of other services was required as a condition for a PIN contract. In particular, retailers who negotiated with numerous banks, namely 68% of cases, were confronted far more often with the condition that they purchase other services. Opening a current account and depositing cash, in particular, were referred to as additional conditions for entering into a PIN contract. The fact that the overall relationship is considered important and that retailers did not wish to switch for a single product would also have played a role (see also Table 3.1). In addition, the differences in tariffs between the bankers were considered by the retailers to be small. Nevertheless, it emerged from the survey that negotiating did result in savings. The average difference between the first and the final offer in the negotiations on payment tariffs was 7.4%.

In future, some retailers will possibly switch providers. Approximately 13% of retailers are considering switching within two years, of whom 24% are considering doing so within six months. The hope of obtaining a lower tariff is given as the most important reason.

3.3 Outcomes of FSM's research into tariffs

In July 2005, FSM requested the six largest banks for information on the tariffs which retailers pay for PIN transactions and the contractual conditions applied. Prior to the transfer, it was possible to enter into two types of contract with Interpay: a Beatel contract with a fixed tariff and a Datanet/Digi ISDN Access contract with a tariff which depended on the number of PIN transactions realised. In the present situation, the various banks use different types of contract. In the case of single contracts, a fixed tariff per transaction may be charged, but a scale based on *ex post* realised PIN volumes may also be applied. In addition, some banks offer PIN transactions for a fixed amount per month, irrespective of the number of transactions, or a 'zero rate' is used, whereby no tariffs are charged up to a certain number of transactions. In the case of master contracts, on the other hand, all the banks use the same type of contract: a fixed tariff negotiated beforehand. In contrast to the former situation with Interpay, some banks also charge a subscription fee in addition to the transaction-based tariff.⁷

In table 3.2, a comparison is given of the previous tariffs charged by Interpay and the weighted average tariffs of the banks measured in mid-year, taking into account the number of transactions per bank. Some caution is required when comparing the average tariffs of the banks. Firstly, only limited data is available on the PIN volumes realised. The estimate of the number of PIN transactions on an annual basis, which is necessary for certain types of contracts to set the tariff, will not always be reliable. In addition, on the reference date in mid-July, not all the contracts had yet been transferred to the banks. Secondly, the banks may charge subscription fees. As far as possible, these had been taken into account when calculating the tariff. In the case of a maximum of 22% of the total number of contracts transferred, possible subscription charges could not be taken into account. The overview of tariffs paid in 2005 for PIN transactions must therefore be regarded as an initial indication of the development of prices on the market for PIN payments. FSM will repeat this survey next year.

Table 3.2 Average PIN tariffs for retailers (in eurocents, excl. VAT)

Number of PIN transactions per year	Interpay (2003)		Banks (2005)
	Tariff excluding the national discount	Tariff including the national discount ¹	
1-100,000	7.5	6.38	6.56
100,000-500,000	7.0	5.95	6.48
500,000-1,000,000	6.6	5.61	5.97
1000,000-5,000,000	6.3	5.36	4.92
>5,000,000	5.91	5.03	4.73

(1) In 2003 1,157 billion PIN transactions were realised, on the basis of which the National Discount amounted to 15%. This discount was settled in arrears and applied to the entire market.

It emerges from this overview that the large retailers (more than one million transactions a year) paid lower tariffs on average after the transfer than before the transfer. For smaller retailers (up to one million transactions a year), the picture is less clear. PIN transactions seem to have become more expensive for this group. On the basis of the data provided, it is not possible to make a distinction between the systems used (Beatel, Datanet/Digi Access). There was a difference between the tariffs of these two systems.⁸

Table 3.3 gives the ratio between the cheapest and the most expensive average tariff charged by a bank. The differences in the case of single contracts appear to be greater than those in relation to master contracts. The above-mentioned inaccuracies possibly play a role in this and caution must therefore be exercised when interpreting the results. In any event, the conclusion can be drawn that differences in the tariffs exist between the banks in relation to both types of contracts and in all volume ranges.

Table 3.3 Ratio between the average tariff of the most expensive and the cheapest bank

Number of PIN transactions per year	Single contracts	Master contracts
1-100,000	1.85	1.49
100,000-500,000	1.21	1.05
500,000-1,000,000	1.37	1.09
1000,000-5,000,000	1.11	1.03
>5,000,000	1.04	1.05

3.4 Conclusions

The transfer of PIN contracts from Interpay to the banks was completed on 1 September 2005. The majority of retailers, as appears from the research conducted by NIPO/ECORYS-NEI, were informed of the changes. However, according to this research, banks undertook relatively few steps to attract new customers through acquisition. Small retailers, in particular, also did not make use of the possibility of negotiating tariffs or switching to a different bank. The overall relationship with their regular banker is the main reason for the limited switching

behaviour. According to the research, the switching behaviour is expected to increase in the coming years.

In mid-2005, FSM analysed the average PIN tariffs charged on the basis of a questionnaire sent to the banks. The conclusion is that the larger retailers with more than one million transactions pay lower tariffs on average than they did before the transfer, while smaller retailers pay more. On the average tariffs are trending downwards. In addition, it emerged from the research that there are differences between banks with regard to the average tariffs charged and that the number of types of contract after the transfer increased.

Both of these studies present a picture of a market in which for the time being there is limited, but burgeoning, competition. It is not yet certain that this development will persevere to reach a situation in which there is active competition. NMa therefore also intends to pay the necessary attention to this market in 2006. Within this framework, FSM's monitoring activities will be continued in the coming year.

4 Entry and exit of banks

4.1 Introduction

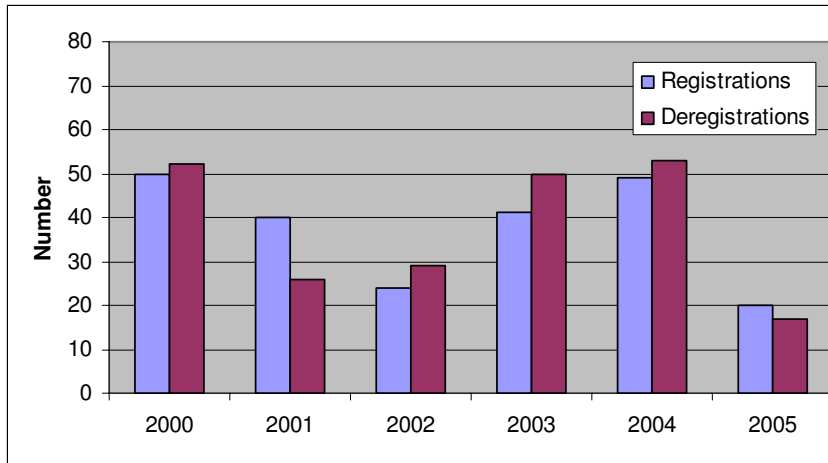
In the *Financial Sector Monitor 2003*, it was argued plausibly on the basis of a large number of indicators and various studies that the banking and insurance sectors are characterised by an increased risk of suboptimal conditions with regard to the operation of market forces.¹ In addition to structural characteristics, the demographic developments in the industry, for instance, were considered, which give an indication of the dynamism of the market.²

An important element in these analyses is the entry and exit of companies. This chapter presents a picture of the entries and exits in the banking sector during the past five years on the basis of the register kept in accordance with the Credit System (Supervision) Act [*Wet toezicht kredietwezen (Wtk)*] (hereinafter "the Register"). The Register is a record of all institutions which have been issued with a licence or a notification of the Dutch Central Bank, on the basis of which they can carry out activities on the Dutch market. All banks active in the Netherlands are credit institutions and are subject to the Credit System (Supervision) Act.

4.2 Registrations and deregistration under the Credit System (Supervision) Act

Figure 4.1 contains an overview of changes in to the Register in the period from January 2000 up to and including May 2005. On the basis of this overview, the conclusion can be drawn that relatively many entries and exits occurred in this period. The number of changes in the Register fluctuates roughly between 20 and 50 a year, whereby the number of entries and exits balances out fairly well in each year. However, this graph does not distinguish between the type of licence or institution.³ If the underlying data are broken down according to the type of institution and activity, a very different picture emerges.

Figure 4.1 Changes in the Register kept in accordance with the Credit System (Supervision) Act, January 2000-May 2005



Source: Register kept in accordance with the Credit System (Supervision) Act, (May 2005).

4.2.1 Breakdown according to the type of institution

Registrations according to the type of institution

In table 4.1 the registrations in the Register in the period from 2000 to 2005 are broken down according to the various types of entrants.⁴

Table 4.1 Registrations in the Register according to type of institution, January 2000-May 2005

	2000	2001	2002	2003	2004	2005	Total
Dutch commercial banks	11	5	2	6	4	1	29
Foreign commercial banks (EU) with a branch office in the Netherlands	2	2	2	2	3	0	11
Foreign commercial banks (EU) without a branch office in the Netherlands	37	33	20	33	42	19	184

Source: Register kept in accordance with the Credit System (Supervision) Act (May 2005).

It appears from this table that in the period from January 2000 up to and including May 2005, a total of 29 commercial banks with a legal entity in the Netherlands successfully applied for a licence, including Akbank International N.V., BinckBank N.V. and Yapi Kredi Bank Nederland N.V. In addition, 195 non-Dutch EU banks were given the opportunity of operating on the Dutch market through notification of the Dutch Central Bank.

Of the notified commercial EU banks, 11 opened a branch office in the Netherlands. A further analysis shows that of the remaining 184 commercial EU banks, only three were registered with the Chamber of Commerce and had an *.nl website.⁵ The vast majority (83%, see table 4.2) is neither registered with the Chamber of Commerce nor has an *.nl website.

Table 4.2 Characteristics of commercial EU banks without a branch office in the Netherlands

Not registered with the Chamber of Commerce, no *.nl website	83%
Registered with the Chamber of Commerce, no *.nl website	15%
Registered with the Chamber of Commerce and en *.nl website	2%

Source: Register kept in accordance with the Credit System (Supervision) Act (May 2005), Chamber of Commerce (2000-July 2005) and FSM's own analysis.

A notable feature of this is that in this period not a single bank from outside the EU was issued with a licence to set up a branch office in the Netherlands. Banks from outside the EU did set up a subsidiary in the Netherlands. A possible explanation for this is that banks from outside the EU opted to set up a subsidiary somewhere in Europe (for instance, in the Netherlands). By applying for a licence for the subsidiary, in principle they gain access to the

entire EU. Another possible explanation is that most large banks from outside the EU were already present in the Netherlands in 2000.

Deregistrations according to the type of institution

In table 4.3 deregistrations from the Register in the period from 2000 to 2005 are broken down according to various types of deregistrations. Credit institutions affiliated to a central credit institution (116) and commercial EU banks without a branch office in the Netherlands (56) made the greatest contribution to the total of 225 changes to the Register.

Table 4.3 Deregistrations from the Register according to the type of institution, January 2000-May 2005

	2000	2001	2002	2003	2004	2005	Total
Dutch commercial banks	19	12	4	5	2	0	42
Foreign commercial banks (EU) with a branch office in the Netherlands	0	2	0	0	1	0	3
Foreign commercial banks (EU) without a branch office in the Netherlands	8	3	11	23	6	5	56
Credit institutions affiliated to a central Dutch credit institution	24	7	12	19	43	11	116
Dutch savings banks	1	0	0	0	0	0	1
Foreign commercial banks (non-EU) with an office in the Netherlands	0	0	0	2	1	1	4
Securities credit institutions	0	2	0	1	0	0	3

Source: Register kept in accordance with the Credit System (Supervision) Act (May 2005).

In the period from January 2000 up to and including May 2005, the decrease in the number of credit institutions affiliated to a central credit institution was caused entirely by the restructuring of Rabobank's branch network.⁶ The peak of this restructuring occurred in 2004, resulting in 43 changes to the Register. In 2002, the restructuring of Fortis was responsible for the largest share of changes in the category of Dutch commercial banks and in 2001 the restructuring of SNS Bank accounted for more than half of the changes in this category. In general, three quarters of the changes to the register in the category of Dutch commercial banks in the period can be explained in this way.

In addition, a large number of notifications amongst commercial EU banks without a branch office in the Netherlands were withdrawn in the period from 2000 to 2005. The question which emerges here is the extent to which these parties were actually active on the market. Table 4.4 shows that only 5% (three out of 56) of the undertakings whose notification lapsed in the period from January 2000 up to and including May 2005 had been registered with the Chamber of Commerce in the past and had had a *.nl website. Of these undertakings, it is known from data obtained from the Chamber of Commerce that they were, in fact, discontinued as banking institutions in the Netherlands.

Table 4.4 Characteristics of deregistered commercial EU banks without a branch office in the Netherlands

Not registered with the Chamber of Commerce, no *.nl website	82%
Registered with the Chamber of Commerce, no *.nl website	13%
Registered with the Chamber of Commerce and with an *.nl-site	5%

Source: Register kept in accordance with the Credit System (Supervision) Act (May 2005), Chamber of Commerce (2000-July 2005) and FSM 's own analysis.

4.2.2 Registrations and Deregistrations of Dutch commercial banks according to their background

Registrations according to background

As was stated in the previous section, deregistration from the Register arose from restructuring of the branch networks of various banks. The background of the registrations in the category of Dutch commercial banks, is given in table 4.5. Restructuring was also the reason for issuing a licence or notification in 69% of cases. In addition, the granting of a licence and notification arose mainly from the commencement of new activities (21%) and in a limited number of cases arose directly from a merger or acquisition (7%). This corresponds to the issuing of an average of one to two licences a year in relation to the commencement of new activities or undertakings.⁷ A rising or falling trend cannot be determined on the basis of this.

Table 4.5 Reasons for registration by Dutch commercial banks, January 2000-May 2005

	2000	2001	2002	2003	2004	2005	Total	
Merger or acquisition	0	0	0	2	0	0	2	7%
Unknown	0	0	0	0	1	0	1	3%
Restructuring	10	3	2	2	3	0	20	69%
Start of the new activity	1	2	0	2	0	1	6	21%

Source: Register kept in accordance with the Credit System (Supervision) Act (May 2005), *Het Financieele Dagblad* (2000-July 2005), Chamber of Commerce (2000-July 2005) and FSM 's own analysis.

Deregistrations according to background

The restructuring of offices also plays an important role (65%) in the number of exits amongst Dutch commercial banks. In addition, the share of withdrawals as a result of mergers and acquisitions within the Netherlands is relatively large (14%) compared to the number of cross-border mergers and acquisitions (2%). In a limited number of cases (10%), exits occurred as the result of liquidation. As a result, the licence or notification lapsed. Finally, in a limited number of cases (7%), the activity ceased. Due to the small numbers, a trend in the exiting of banks during the period 2000 to 2005 could not be observed.

Table 4.6 Reason for deregistration by Dutch commercial banks, January 2000-May 2005

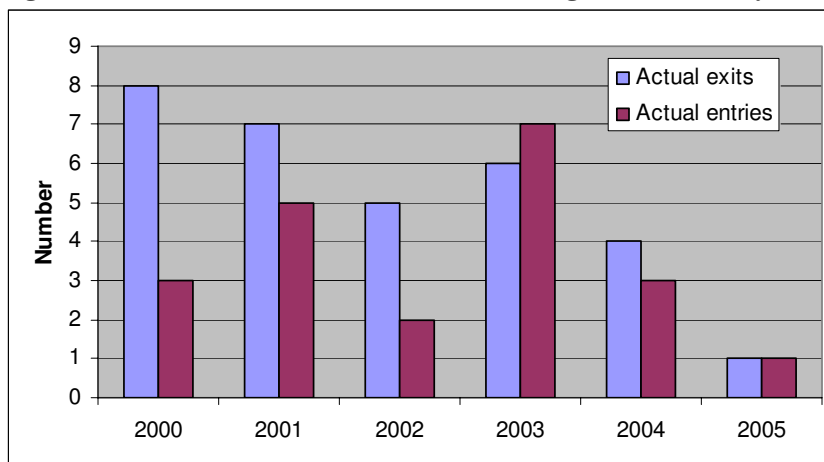
	2000	2001	2002	2003	2004	2005	Total	
Merger or acquisition outside the Netherlands	1	0	0	0	0	0	1	2%
Merger or acquisition in the Netherlands	4	1	0	0	1	0	1	14%
Liquidation	0	0	2	2	0	0	20	10%
Unknown	0	0	0	1	0	0	6	2%
Restructuring	14	10	1	1	1	0	20	65%
Cessation of activities in the Netherlands	0	1	1	1	0	0	6	7%

Source: Register kept in accordance with the Credit System (Supervision) Act (May 2005), *Het Financieele Dagblad* (2000-July 2005), Chamber of Commerce (2000-July 2005) and FSM 's own analysis.

4.3 Entries and exits

An undertaking active in the Netherlands is understood below to be a company with a licence or a notification, in combination with either a branch office or both a registration with the Chamber of Commerce and a *.nl website. Actual entry occurs when a company becomes active. A company actually exits if it ceases to be active. Figure 4.2 shows the actual entries and exits defined in this way. In the period from January 2000 up to and including May 2005, an average of 3.9 market parties entered the Dutch market per year and 5.7 parties exited. Up until 2003, the number of exits was higher than the number of entries. From 2003 onwards, the number of entries and exits was more or less in balance, but was at a lower level than previously.

Figure 4.2 Entries and exits in the Dutch banking sector, January 2000-May 2005



Source: Register kept in accordance with the Credit System (Supervision) Act (May 2005), *Het Financieele Dagblad* (2000-July 2005), Chamber of Commerce (2000-July 2005) and FSM 's own analysis.

4.4 Conclusions

In this chapter, entries and exits are analysed on the basis of the Register. A large number of changes to the Register are the result of the restructuring of existing banks. In addition, a large number of EU banks request notification in order to enter the Dutch market without actually becoming active. They do not open a branch in the Netherlands, do not register with the Chamber of Commerce, as and do not set up an *.nl website (they therefore do not appear actively to acquire customers in the Netherlands via the Internet).

The analysis shows that the actual entries and exits to the Dutch banking market (entries or exits by a bank active in the Netherlands), are lower than expected on the basis of the number of changes to the Register. The number of actual entrants remains limited to an average of approximately 4 undertakings a year. The number of actual exiters is therefore higher than the number of entrants. In addition, the number of entrants and exiters has decreased since 2003. The competitive pressure on banks active in the Netherlands as a result of entries is therefore limited.

5 The geographical dimension of the health insurance market

5.1 Introduction

The new Health Insurance Act [*Zorgverzekeringswet (Zvw)*] will come into force on 1 January 2006.¹ The Health Insurance Act is meant to result in greater efficiency, less central management and good accessibility to healthcare. Consumers will be given greater freedom to choose their health insurance. Health insurers will have to compete for the patronage of customers and will therefore have to negotiate favourable price-performance levels in competition with each other for the insured.²

An important condition for the success of the Health Insurance Act is the development of competition between the health insurers (private insurers and health insurance funds) which is still often regionally oriented. The legislator has stated that in the short-term advantages may arise from a situation characterised by strong regional health insurers with a high market share, because they are in a good position to realise procurement advantages. However, if competition at the national level does not emerge, there is a danger in the long term 'that, in a situation where an insurer is strong in a certain region, it will be less attractive for other insurers to compete in this region (...), which will be disastrous in the long-term as it will remove the incentive to compete and, by doing so, the incentive to procure healthcare at competitive prices.'³ To promote the development of competition at the national level, health insurers of significant size are obliged to offer a basic policy throughout the Netherlands. The question which has to be asked in this regard is whether this obligation will actually result in national competition on the health insurance market (and within what period).⁴

A restrictive factor with regard to the emergence of national competition is the possibility that the regional ties of health insurers to their original areas of work will be continued and strengthened. Mergers and acquisitions may play a role in these ties and will therefore frustrate competition at the national level, which the legislator wished to achieve. In a general sense, the likelihood of infringements of the prohibition on cartels contained in section 6 of the Competition Act is greater on regional markets in which only a few insurers of a particular size are active compared to the national markets with numerous players. Acquiring insight into the future health insurance market is therefore of considerable importance for competition regulation by NMa.⁵

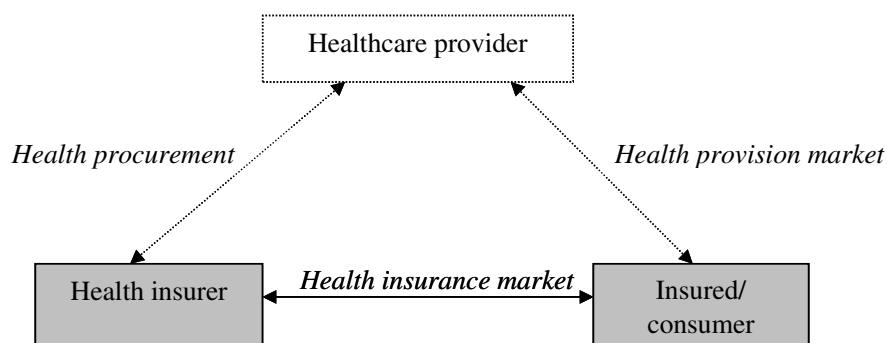
Depending on the development towards regional or (more) National competition, three scenarios for the geographical dimension of the market are conceivable, namely (a) a regional scenario, based on the traditional core areas of work; (b) a national scenario; (c) a hybrid form, in which supply is determined in some areas by national or supraregional players, while regional players set the tone in other areas. The aim of this chapter is to obtain insight into the development of competition on the new health insurance market and to examine which of the three scenarios above seems to be the most plausible.

The structure of this chapter is as follows. First the way in which the health insurance market operates will be discussed (section 5.2). Following this, the way in which this market can be described geographically (section 5.3) and the factors which affect whether regional submarkets are maintained or not (section 5.4) will be discussed. The chapter closes with a number of preliminary conclusions with regard to determining the scenario (section 5.5).

5.2 The healthcare market

figure 5.1 provides a schematic overview of the way in which the healthcare market operates. Three markets are distinguished. The *health provision market* reflects the relationship between consumers (patients) and healthcare providers (amongst others, hospitals, general practitioners, physiotherapists and pharmacists). The *health procurement market* describes the relationship between healthcare providers and health insurers. Although at present patients often make use of a healthcare provider without the intervention of a health insurer, payments take place (in most cases) through the health insurer. The *health insurance market*, the relationship between the insurer and the consumer, is the subject of this chapter.

Figure 5.1 Operation of the healthcare market



Source: 'Consultation Document Insurance Market Monitor', Medical Charges Board (CTG)/Office of Health Regulation(ZAio) and the Healthcare Supervisory Board (CTZ), July 2005.

Health Insurance Act

With the coming into force of the Health Insurance Act, a single obligatory basic healthcare insurance policy was introduced for all residents of the Netherlands.⁶ The cover provided by this insurance largely corresponds to the present health insurance fund package and is determined by the government. In addition, it is possible to take out supplementary insurance for treatments which do not fall within the basic health insurance policy. Health insurers are obliged to accept everyone who applies for the basic health insurance policy. In addition, health insurers must operate nationally, unless they have fewer than 850,000 insured. If the insurer has fewer than 850,000 insured, the health insurer is allowed to limit its area of

operation to at least one entire province.⁷ An insurer may differentiate between policies per province, even if it operates nationally.

The possibility of premium differentiation and risk selection within the basic healthcare insurance policy is almost entirely excluded.⁸ The premium for the basic health insurance policy is set at a nominal amount and is therefore not income related.⁹ It emerged from the premiums announced by insurers in mid-November 2005 that the nominal premium for 2006 will amount to approximately EUR 1,050.¹⁰ Insurers may offer policyholders basic packages with a variable excess. This excess may be offered in steps of EUR 100 up to a maximum of EUR 500. This is lower than the present maximum excess. In contrast to the basic health insurance policy, health insurers may offer different premiums and apply risk selection to the supplementary insurance policies. The consequences of risk selection are mitigated by the existence of a settlement system. This system, with criteria known beforehand which are the same for everyone, is meant to ensure that insurers do not experience financial disadvantages arising from imbalances in the distribution of insurance risks as a result of the obligation to underwrite policies.¹¹

Insurance-in-kind and restitution policies

Insurers may offer various types of insurance policies. On the one hand, there is the 'insurance-in-kind policy'. In this case, the insured is entitled to the healthcare for which he is insured. This has to be obtained from healthcare providers with whom the health insurer has entered into a contract. If healthcare is obtained from a healthcare provider with whom the insurer has not procured healthcare in advance, the insured are entitled to 'restitution in line with the market'.¹² On the other hand, there is the 'restitution policy'. In this case, the insured is entitled to restitution of the cost of healthcare received. The insured therefore has greater freedom of choice. In the case of restitution policies, healthcare may also be contracted, although this is less usual than in the case of insurance-in-kind policies. Insurers may also offer a hybrid form comprising both insurance-in-kind and restitution policies.¹³ The insurance-in-kind policy and the restitution policy correspond in general to insurance by a health insurance fund and private insurance under the old system.

Group contracts

The possibilities for entering into group contracts with health insurers will change under the Health Insurance Act. In contrast to the old system, in addition to group contracts with employers, health insurers may also enter into group contracts with other legal entities, whereby they may grant a discount on the premium. The discount on the group contracts is subject to a maximum of 10% of the nominal premium of the respective policy.

Possibilities for switching

A straightforward basic package with obligatory acceptance is meant to ensure that consumers can compare different policies easily. Since consumers do not have to cancel their supplementary insurance with their former insurer if they insure their basic insurance elsewhere, the threshold to switching is low (in theory).¹⁴ Switching may be attractive, for instance, due to price differences.

Insured

The dataset analysed for this chapter contains 15 million insured.¹⁵ Approximately 10 million of these are insured with a health insurance fund and 5 million are insured privately. Of the

privately insured policyholders, approximately 3 million are insured through a group contract. The remaining 2 million privately insured policyholders have individual insurance policies.

Health insurers

Traditionally health insurance funds (*ziekenfondsen*) were tied to their so-called core areas of operation. Up until 1992, health insurance funds even had a statutory monopoly in their area of operation. Since 1992, health insurance funds may operate nationally and consumers are free to switch from one health insurance fund to another. Some insured have already switched. At the regional level, however, there are notable differences. In some regions, relatively few consumers have switched and the health insurance fund has a market share of more than 75%. In other regions, the market share of the former monopoly health insurance fund is lower.¹⁶ The market shares per region for private health insurers are generally below 50%, with the exception of a few (in such cases, the market share is less than 60%). As a logical consequence of the high market shares of the largest insurer in the region, the values of the indicators of the level of concentration are high.

At the beginning of 2005, there were 59 (brands of) health insurers in the Netherlands. These included 22 health insurance funds, 33 private healthcare insurers and 4 public health insurers. Of these 59 health insurers, 11 health insurers do not belong to a group, while the others do.¹⁷ The largest (group of) health insurers are currently Achmea, VGZ, CZ, Menzis, and Agis, all of which arose (partially) from former monopoly health insurance funds. An overview of groups of the most important health insurers, including their brands and labels) is provided in Annex 2.

Healthcare providers

Healthcare providers (hospitals, general practitioners, physiotherapists and pharmacists) are important negotiating partners of health insurers. One of the main opportunities which an insurer has to improve its operating result is to optimise its procurement of healthcare. A good procurement position amongst healthcare providers may generate significant advantages for a health insurer in the battle for customers. Another way in which insurers can operate more efficiently is through vertical integration. This allows insurers, for instance, to employ healthcare providers or to participate (financially) in the businesses of the healthcare providers.¹⁸

5.3 Relevant geographical dimension

As was stated in section 5.1, it is conceivable that the health insurance market will develop in line with a regional, national or intermediate scenario under the Health Insurance Act. In estimating this development, it is necessary to determine whether and, if so, how the supply structures of the various possible geographical health insurance markets differ from each other.

At the national level, the largest health insurers each have a market share in the area of health insurance funds of 10% to 20%. Even if policies insured with health insurance funds and by means of private insurance are combined, this picture does not change. The sums of the

market shares of the three and four largest health insurers (C3 and C4) are 50% and 61% respectively. The Herfindahl-Hirschmann Index (HHI) amounts to approximately 1,200, which is lower than the value of 2,000, which the European Commission uses as an indication that a notified merger must be given additional attention.¹⁹ This is an indication that there is no *a priori* reason to suspect a lack of competition in the event that competition occurs at the national level.

However, the picture changes if one considers the regional level. In this chapter, attention will be given both to provinces, due to the statutory possibility for health insurers to offer separate policies per province, and to the present areas of operation of the former monopoly health insurance funds.²⁰ Due to the close relationship between the so-called healthcare agency regions and the areas of operation of health insurance funds, the areas of operation of the health insurance funds are approximated by taking the regions as the basis for the analysis.²¹

The market shares of the largest health insurers vary per province from approximately 25% to approximately 65%. If consideration is only given to the activities of health insurance funds, there are provinces in which the largest health insurer has a market share of up to approximately 85%. C3 varies from 52% to 90%, while C4 varies from 60% to 90%. The HHI is therefore much higher than in the case of the national market, ranging from 1,256 to 4,355, whereby HHI values, particularly in the northern and southern provinces of the Netherlands, are considerably higher than in the provinces of Noord-Holland and Zuid-Holland.

A striking feature is that at the level of the area of operation of the former monopoly health insurance funds, the market structure differs strongly in a considerable number of cases from the provincial level.²² In provinces consisting of numerous health agency regions, different health insurers have the highest market share in the various health agency regions. The degree of concentration in the health agency regions also differs from that observed at the level of the respective province. In certain health agency regions, relatively high concentration indices were observed. At the level of health agency regions, C3 varies from 61% to 91%, while this increases to a range of 71% to 94% in the case of C4. The HHI per health agency region varies from 1,754 to 4,355.

If there are indeed separate geographical markets, the values of the concentration indicators found for the various regions and provinces indicate possible problems in relation to competition. Many regional HHI levels, for instance, exceed the value of 2,000 points.²³ These regions are located mainly in the north, east and south of the Netherlands. For example, HHI levels of 4,355, 3,768 and 3,731 were observed in the regions (and provinces) of Groningen, Friesland and Drenthe respectively. Annex 3 provides a more extensive description of the concentration indicators for the various parts of the Netherlands.

On the basis of the preceding analysis, it appears that the supply structure of the health insurance market at the national level differs strongly from the structure at the provincial level. If a province consists of numerous health agency regions, it appears that the structure within these health agency regions differs strongly from the provincial structure. The present supply structure, at both the national and provincial levels, is therefore not indicative of homogenous competitive relationships. In addition, the values found for the concentration

indicators indicate possible shortcomings in the competitive relationships. The possibility that the provinces or the health agency regions constitute separate geographical markets must therefore be examined seriously.

5.4 Dynamic factors

Two types of dynamic factors will be discussed below: on the one hand, factors which may strengthen the existence of separate geographical markets and, on the other hand, factors which may stand in the way of the continued existence of geographical submarkets. Since the introduction of the Health Insurance Act still has to take place, it is not easy to estimate the direction and strength of these dynamic factors.

The factors of the first type are strongly related to the operation of the healthcare market and the way in which the health insurance market, the healthcare procurement market and the healthcare provision market (figure 5.1) interact. A regional mechanism can be derived from this which, depending on the extent to which the mechanism works, makes entry difficult and, as a result, has the effect of extending the existence of separate regional markets.

The factors of the second type relate to the increased freedom of choice for the insurer and the insured and show under what conditions the effect of the regional mechanism is counteracted. In such cases, the development towards a market which operates more at the national level is more plausible, because there is then more room for entry by non-regional insurers, for instance by means of an aggressive pricing policy or regional-specific marketing activities. It is then plausible that the high market share of the regional health insurer will (sooner) come under pressure.

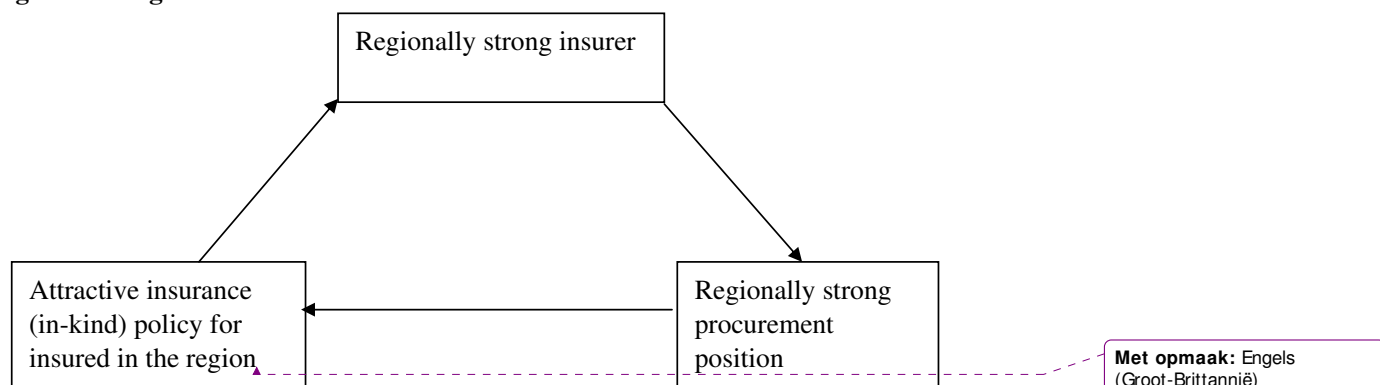
5.4.1 Regional mechanism

It is possible to conclude from figure 5.1 that the healthcare procurement, healthcare provision and health insurance markets will interact. For this chapter, the relationship between the healthcare procurement market and the health insurance market is important. On the basis of certain assumptions, this relationship may result in a mechanism that makes the regional scenario more plausible. These assumptions will be discussed below.

Since a large number of health procurement markets are regional in size, the position of the health insurer, in particular on regional procurement markets, is important.²⁴ Their relationship can be illustrated on the basis of figure 5.2. This figure reveals a mechanism which could result in the continuation or strengthening of the present strong positions of health insurers at the regional level in the future. After all, if a regionally strong insurer is in a position to negotiate substantial procurement advantages and to pass these on (partially) to its policyholders, this insurer will become more attractive to policyholders in this region. Although these advantages in themselves may be viewed positively, the position of the strong regional insurer will be strengthened further. Since insurers with few policyholders and new entrants will not be in a position (or will be in less of a position) to negotiate these advantages, this mechanism will result in continuation of the position of the strong insurer on both the healthcare insurance market and the healthcare procurement market.²⁵ This position allows the insurer actually to pass on only part of the procurement advantages realised to its

policyholders, while at the same time the entry of other insurers is obstructed. As was stated in the introduction, the incentive to procure healthcare at competitive prices may be reduced due to the lack of competitive pressure.

Figure 5.2 Regional mechanism



The plausibility of the regional mechanism outlined in figure 5.2

The plausibility of the regional mechanism outlined in figure 5.2 depends on three assumptions and, in addition, on the lack of a number of counteracting factors (see also section 5.4.2). For instance, the mechanism assumes firstly that procurement advantages can in fact be realised on the various procurement markets, which results in attractive insurance (in-kind) policies for policyholders in the region.²⁶ Secondly, the mechanism assumes a positive relationship between the number of policyholders of an insurer and the procurement power which this insurer can develop. Thirdly, it is assumed that procurement advantages which have been realised have an effect on the policy conditions applicable to policyholders in the respective region.

Realisable procurement advantages

The first assumption relates to the realisation of procurement advantages.²⁷ Although insurers are required to purchase a broad range of healthcare services, the emphasis in this chapter is on the purchase of hospital care. Due to the considerable amount attributable to hospital expenses as part of the total healthcare budget (excluding exceptional medical care under the Exceptional Medical Expenses Act)—approximately 50% to 60%—the procurement of hospital care is one of the most important factors to which a health insurer can realise procurement advantages. The price advantages can be realised on a limited part of the hospital budget which became freely negotiable at the beginning of 2005 (the so-called 'B segment'). At present, this part amounts to 10% of the total number of treatments and approximately 8% of the total hospital budget. The aim is to increase this part over a number of years, but it is not yet clear when this extension will take place.

It appears from the 'Orientation Monitor of Hospital Care' (*Oriënterende Monitor Ziekenhuiszorg*) published by the Medical Charges Board (CTG)/Office of Health Regulation (ZAio) that the discount which a strong regional insurer is able to negotiate with a hospital (in

the region) is (for the time being) on average approximately 1% to 6% higher than the discount obtained by other insurers.²⁸ On the basis of the above data, the price advantages that can be realised at this moment are therefore of limited size. No price advantages can be negotiated on most other types of healthcare procurement, although advantages of other types may be generated. These include, for instance, waiting lists mediation, extended opening hours in the evenings, or other service elements which may be attractive to policyholders.

Relationship between market position and realisable procurement advantages

The second assumption—a strong position on the procurement market resulting in advantages obtained through negotiation—appears in any event to correspond to the way in which the negotiations were, in fact, conducted.²⁹

A number of hospitals have made it known that they would grant the largest price discounts on the basis of volume. In other words, the largest insurer pays the lowest price, while a 'risk surcharge' applies to other insurers on the basis of their size.³⁰ Hospitals have indicated that they have not negotiated about quality or service or have hardly done so at all.

It occurs regularly, however, that insurers procure healthcare jointly in the regions in which their market position is small. Procurement cooperatives, however, are only permitted by NMa under certain conditions, so that the cooperatives can only lead to economies of scale at the negotiating table to a limited extent.³¹ Hospitals regard procurement cooperatives as a positive development as they have to spend less time and money on negotiations. Numerous insurers, however, have noted that procurement cooperatives may improve their procurement position, but that there is still an appreciable difference between the price realised by the regionally strong insurer and the procurement cooperatives.

Regional differentiation

The third assumption relates to the passing on of certain negotiated advantages to policyholders. The mechanism works strongest if advantages realised on the regional procurement markets are also passed on to policyholders in the same region. If such procurement advantages are shared amongst all the insurer's policyholders, in other words also amongst policyholders in regions in which (large) procurement advantages are not realised, the mechanism outlined in figure 5.2 will be diluted slightly. The large health insurers are obliged under the Health Insurance Act to offer a policy to any applicant in the Netherlands,³² but forms of differentiation at the regional level are possible. As was stated earlier, for instance, insurers may offer policies per province.

It should be noted, however, that it is possible for insurers to try to interest policyholders, who reside in their core areas of operation, in health insurance (in-kind) through marketing activities. The obligation to offer applicants from outside the core area of operation insurance subject to the same conditions can be circumvented in this way by drawing applicants' attention to the fact that the payment for treatment in non-contracted institutions, in other words on the basis of restitution, is subject to a maximum. This is also a possibility for areas within provinces covered by the same provincial policy. The Healthcare Supervisory Board

(CTZ) and the Medical Charges Board (CTZ)/Office of Health Regulation (ZAio) also make reference to this possibility.³³

The operation of the mechanism therefore depends on the extent to which insurers offer policies on a provincial basis (regional differentiation), and the extent to which health insurers are able to pass on the procurement advantages obtained (in part) to policyholders in their core areas of operation by offering these policies or by other means, because these procurement advantages can be realised, in particular in this area.³⁴

5.4.2 Counteracting factors

The regionalisation mechanism is affected by several factors which exercise a force in the opposite direction. The (procurement) market shares of the regional players come under pressure firstly if policyholders switch in large numbers to different insurers. Secondly, since the mechanism occurs mainly in relation to health insurance-in-kind. If (a sufficient number of) policyholders opt for restitution policies the mechanism becomes less plausible. Thirdly, the same applies to the development of (supraregional) groups. Fourthly, the regional mechanism becomes less plausible if the most important regional healthcare providers also give access to negotiations to players with small positions in the region or new entrants.

First these factors are considered in more detail below. After this, section 5.4.3 will discuss the plausibility of these factors in more detail using the empirical material currently available.

Switching behaviour of policyholders

The switching by many policyholders from their present, often regional, insurer to a different (non-regional) insurer, would be an important indicator of the existence of supraregional geographical markets. After all, in the light of the assumption that many policyholders still have insurance with a former monopoly health insurance fund, switching provides an opportunity for entering the market. The most important factor which determines the plausibility of switching behaviour is the relative price sensitivity of the insured, in other words the extent to which the insured is primarily influenced by the price of the policy, and to a lesser extent by quality and service. If the insured is only influenced to a limited degree by price differences between insurers, the probability that he or she will not switch is great.³⁵

It must be borne in mind, however, that the possibility cannot be excluded *a priori* that the existing regional health insurer will make the most favourable offer with regard to price due to its strong position on the healthcare procurement market, as a result of which costs and other advantages can be obtained relative to a competitor.³⁶ If consumers are indeed price sensitive, this would ensure that policyholders remain with the strong regional player. Policyholders from the region who are not yet insured with this strong regional insurer will be more willing to switch due to the lower price. In such situations, the regional mechanism will be reinforced.

A potentially restricting factor with regard to the switching behaviour of policyholders is the link between the basic and supplementary insurance. In contrast to the present system, it is possible to take out the basic and/or supplementary insurance with different insurers. If policyholders have a preference for insuring their basic and a supplementary insurance with

the same insurer or if insurers discourage separating these types of insurance,³⁷ the possibility of separation provided by the Health Insurance Act will not result in a clear increase in switching behaviour compared to the present system.

Preferences of policyholders

The regionalisation mechanism depends on the extent to which policyholders opt for insurance-in-kind policies. If numerous policyholders opt for restitution policies, the mechanism may be counteracted, because in relation to these policies close contacts with regional healthcare providers appear to be less important. Restitution policies, in comparison to insurance-in-kind policies, offer the policyholder greater freedom of choice to choose a healthcare provider. Convenience for the policyholder and possibly also the price may favour insurance-in-kind policies.³⁸ The choice in favour of a particular type of insurance therefore depends on the extent to which a policyholder weighs up the greater convenience of an insurance-in-kind policy against the more expensive options offered by a restitution policy.

A complicating factor is the possibility which the Health Insurance Act offers policyholders with an insurance-in-client policy to opt for a non-contracted healthcare provider at a 'restitution rate in line with the market'. If this rate is so high that the policyholders do not have to pay any more or hardly any more if they use non-contracted healthcare, there will be few incentives for policyholders to opt for restitution policies and insurance-in-kind policies will also offer the advantages of a restitution policy.

Development of (supraregional) groups

The other demand factor which may stimulate switching behaviour is the development of groups. Non-employer groups may be an interesting new sales market for insurers. Statistically, large (employer) groups, relatively speaking, are very willing to switch to a different insurer and they are not exclusively regionally oriented.³⁹ On the one hand, the number of groups may increase under the Health Insurance Act due to the creation of non-employer groups. On the other hand, the discount for a group under the Health Insurance Act is subject to a maximum of 10% of the nominal premium.

Groups may be interesting ways of entering markets for health insurers outside their traditional core areas of operation. If an increase in groups is observed under the Health Insurance Act and if these mainly acquire a supraregional character, they will provide an important stimulus to the creation of a national market.

Negotiating policy of healthcare providers

The behaviour of healthcare providers is also of considerable importance with regard to the plausibility of a scenario whereby the mechanism will result in narrow, regional markets. In principle, it is more difficult for a healthcare insurer to enter markets with a relatively high degree of concentration of certain healthcare providers (such as various regional markets for hospital care) than markets with a relatively large supply of healthcare. The problem of entry is expected to be less great, however, if healthcare providers are willing to negotiate with non-regional health insurers. Another possibility is that the health provider does not differentiate in the negotiations between regional and non-regional health insurers, and regional players cannot realise decisive advantages.

In negotiating discounts in the B segment of hospital care, the number of hospitals in the region also appears to be important. The greater the number of hospitals in a certain area, the greater the probability that one of the hospitals in the region will be willing to enter into serious negotiations with a smaller insurer or a new entrant, with the possible motive of being less dependent as a hospital on the large regional insurer. In the western coastal region of the Netherlands, the Randstad, there is a considerably greater supply of hospitals than in the rest of the Netherlands, so that it appears to be slightly easier to enter a certain region there than in the more sparsely populated areas in the north, east and south of the Netherlands.

The factor which may counteract the mechanism resulting in narrow geographical markets is the possible emergence of supraregional healthcare providers. Regional healthcare providers may unite into chains which operate at the national (or supraregional) level. Negotiations with health insurers will be possible no longer at the regional level, but at the national level. As a result, having a regionally strong position will become less important and, as a result, the mechanism resulting in narrow, regional markets will become less probable.

5.4.3 Empirical research

The relevant factors, which contribute to estimating the plausibility of a certain scenario, were distinguished above. Information on a number of factors was found which informs the question of which scenario is probable. These are available empirical studies, the decision taken by NMa in case 5052/CZ-OZ, and information obtained from interviews with health insurers. It is too early at this moment to draw conclusions with regard to the number of other factors and it will only be possible to obtain further information after the Health Insurance Act has been introduced.

Switching behaviour of policyholders

At the end of 2005, health insurers will make a so-called 'suitable offer' to every policyholder, to avoid the possibility that people will become uninsured as a result of the change to the system. This means that every policyholder will receive an offer from his or her health insurance fund, private health insurer or public health insurance plan before 16 December 2005 of health insurance with the health insurer stipulated in the offer. Unless the policyholder states that he or she rejects this offer, the policyholder will be 'automatically' insured in accordance with that offer as of 1 January 2006.⁴⁰ Since the policies, in principle, have a period of validity of one year, it is quite possible that more clarity will arise only after the beginning of 2007 with regard to the willingness of policyholders to switch under the new system.

Several recent studies discussed the switching behaviour of consumers under the former healthcare system. It appears from the research by Vektis that an estimated 3.4% of people insured by health insurance funds switched to a different health insurer in the period from 1 January 2005 up to and including 28th February 2005.⁴¹ Amongst people who were privately insured, approximately 10% switched health insurers in the same period. Approximately two thirds of the latter mobility was caused by (changes in) group contracts. Slightly more than 3% of individual policyholders switched, which is comparable to people insured with health insurance funds.

A similar picture emerges from research done by iBMG.⁴² In this case, it was calculated that 4.2% of people insured with health insurance funds switched health insurance funds in 2005. The percentage of privately insured people who switched is 8.7%, but is mainly determined by the switching behaviour of groups to which these privately insured persons belong. It should be noted that the mobility of people insured by health insurance funds has increased relative to the preceding years.⁴³

It also emerges from the research that the level of the premium is a very important reason to switch.⁴⁴ It also appears that the main reason to switch health insurers is the financial advantage which a different insurer offers, as a result of which privately insured people more frequently switch health insurers than people insured with health insurance funds.⁴⁵ In this regard, it should be noted that price is the most important deciding factor once the decision to switch has been taken. Price differences themselves only appear to be a limited incentive to switch. This is confirmed by a study carried out by the Netherlands Bureau for Economic Policy Research (CPB) into switching costs, in which CPB reaches the conclusion that these are high in the case of healthcare insurance.⁴⁶

On the basis of the results of the above-mentioned research, it is not possible to express a clear expectation with regard to the number of policyholders who will switch after the introduction of the Health Insurers Act. The interviews held within the framework of the research for this chapter give the impression that a considerable increase in switching is not taken into account in the first year after the introduction of the Health Insurance Act, partly due to the suitable offer which policyholders will receive at the end of 2005 from their present insurer. With regard to the development of the geographical scenarios, switching is of considerable importance. Not only the extent of switching is a relevant factor, but also any differences between regions may provide indications as to which scenario is the most plausible.

Preferences of policyholders

On the basis of interviews with health insurers, there is an expectation that insurance-in-kind policies will be the most important type of insurance after the introduction of the Health Insurance Act. There are numerous reasons for this. Firstly, two thirds of residents of the Netherlands are insured with a health insurance fund and on the basis of the suitable offer the majority of residents of the Netherlands will be offered an insurance-in-kind policy as of 1 January 2006. This is in line with the legislator's aim. It is the explicit aim to achieve 'efficient procurement', which is more plausible in the case of insurance-in-kind policies. In addition, it emerged from the interviews that an insurance-in-kind policy will probably be cheaper than a restitution policy due to the lower administrative costs and due to the procurement advantages achieved by purchasing healthcare beforehand. In addition, health insurers referred to the elements which consumers value, such as good waiting-list mediation, and mediation with general practitioners and dentists, which can be insured under an insurance-in-kind policy. The greater freedom of choice of a restitution policy is not expected to outweigh the above arguments. Insurers will also offer hybrid forms of insurance-in-kind and restitution insurance. It is still unclear to what extent these hybrid forms will develop.⁴⁷

Several insurers have indicated that they only wish to serve their present policyholders in the core operating areas on the basis of their insurance-in-kind policy. Of course, policyholders within their area of operation may take out a restitution policy. A number of insurers have stated that they intend to provide policyholders with an incentive, through penalties and discounts, to make as little use as possible of the 'restitution rate in line with the market' in the case of the insurance-in-kind policy or to make use of healthcare provided by non-preferred providers. For the time being, insurers do not appear to be marketing any explicit 'provincial policies' with the introduction of the Health Insurance Act, although one of the insurers noted that this certainly cannot be excluded in the future. The extent to which insurance-in-kind policies, restitution policies or hybrid forms will play a major role is important in determining the extent to which competition at the national or regional levels is likely.

Development of (supra)regional groups

Almost all the health insurers questioned acknowledge that groups may act as a means of gaining access to a non-core area of operation. They also expect dynamism in relation to group contracts due to the increased possibilities under the Health Insurance Act for the setting up of groups. This provision of the Act has therefore resulted in a number of initiatives with regard to new types of insurance groups. For instance, the website www.independ.nl and a firm of civil law notaries in Twente are in the process of organising groups to negotiate a discount from insurers on the introduction of the Health Insurance Act. A special role may be reserved for patient associations.⁴⁸ Due to the large number of members they have, they are an interesting target group for health insurers, while the higher level of claims is compensated by the settlement fund. The Dutch Society of the Disabled (*General Netherlands Algemene Nederlandse Vereniging Gehandicapten Organisatie*) (with 17,000 members) has already entered into a group contract with Agis Zorgverzekeringen⁴⁹ and Delta Lloyd Groep has created a separate policy for patients with diabetes.⁵⁰ Various initiatives have also been taken whereby sport clubs, associations, trade unions and the like will possibly form groups. A number of these groups appear to be of limited size for the time being and, in addition, focus strongly on a specific healthcare region. Insurers have indicated that for them it is difficult to estimate what the effect will be of, on the one hand, the expected reduction in the employer groups and, on the other hand, the emergence of non-employer groups. A number of insurers are of the opinion that groups will generally be regionally focused, as a result of which the position of existing regional insurers will be strengthened and entry by non-regional insurers will therefore be more difficult. The development of (supra)regional groups is therefore potentially of considerable importance to the geographical dimension of the market.

Negotiating policy of healthcare providers

From the interviews held, it appears that hospitals are only negotiating with a small number of insurers because negotiations are costly and time-consuming. The Medical Charges Board (CTG)/Office of Health Regulation (ZAio) notes that hospitals first negotiate with the insurer with the highest market share in the region before negotiating with smaller health insurers.⁵¹ Negotiations with non-regional insurers under the old system were generally conducted by telephone, which often amounted to the insurer's accepting standard contracts. The hospitals have indicated that they do not expect they will be able to circumvent the large regional insurer(s) under the new system. In their case, certainty with regard to capacity utilisation is an important reason to enter into contracts with these insurers.

5.5 Conclusions

The aim of this chapter is to obtain insight into the development of competition on the new health insurance market. In this regard, three conceivable scenarios were introduced, namely a national scenario, a regional scenario and an intermediate variant. The development towards regional markets is supported by the existence of a mechanism identified within the framework of this research. The existence of this mechanism depends on a number of assumptions and, in addition, may be counteracted by the emergence of a number of other factors. These assumptions and other factors were analysed in more detail.

Partly due to the lack of clarity about how the health insurance market will develop, the empirical material at present does not allow firm conclusions to be drawn. However, it appears to be too early to assume *a priori* the existence of a health insurance market which operates nationally or regionally.

If the development of the healthcare market ultimately results in a scenario in which several separate geographical areas continue to exist in the Netherlands, in addition to larger areas in which supraregional competitive relationships have developed, these separate areas will probably be situated in the relatively sparsely populated areas in the north, south and east of the Netherlands. At present, both health insurers and healthcare providers have a high degree of concentration in these regions, which may indicate a lack of competition. Mergers and acquisitions within these areas may therefore give rise to competition concerns. This is a reason for NMa to continue monitoring closely the development of competition precisely in these areas.

6 Interbank charges: economic theory and international overview of cases

6.1 Introduction

To analyse competition on the market for PIN payments, the *Financial Sector Monitor 2004* reported on an international comparison of PIN payment systems (debit cards).¹ It emerged from the comparison that several market structures are possible.² While the Netherlands only had a single PIN payment system, numerous systems exist alongside each other in Germany and the United Kingdom. In some of these market structures, a multilateral interchange fee is used. The multilateral interchange fee is a jointly agreed fee which banks charge each other for carrying out services in relation to a transaction and, in general, is paid by the retailer's bank (the acquiring bank) to the cardholder's bank (the issuing bank).³

Partly due to the collective nature of multilateral interchange fees, these are studied closely by competition authorities throughout the world.⁴ In a growing number of competition-related cases the central question addressed was what the effect of such collectively determined tariffs is on the cost of electronic payments by consumers and retailers. As of yet there is little empirical research which can answer this question.

There is however a growing body of economics literature relating to electronic payment systems. In this literature, the multilateral interchange fee is placed within the framework of two-sided markets. A characteristic of payment systems (for instance PIN payment system in the Netherlands) is that a payment only occurs when a retailer accepts the payment and the consumer wishes to pay by means of the payment system. If many retailers accept payments by means of a certain payment system, it is attractive to consumers to pay by this means. If many consumers wish to pay by means of the payment system, it is attractive for the retailer to accept payments by this means. Due to this mutual interdependence of demand on the consumer side and demand on the retailers' side, the market is referred to as a two-sided market. In a two-sided market, the price charged to retailers affects the behaviour of consumers and *vice versa*. The multilateral interchange fee shifts revenues and costs between issuers and acquirers. In the interactions of prices, costs and competition, the multilateral interchange fee is therefore an instrument which may be used to influence the tariffs which consumers and retailers pay.

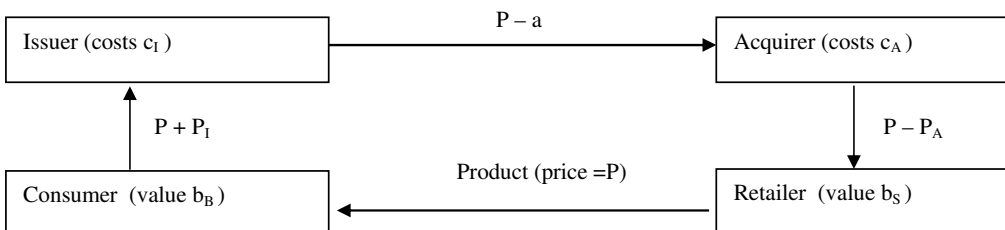
To obtain a better insight into the role of these charges, FSM therefore carried out a study this year into two-sided markets and multilateral interchange fees. This chapter first reports on the economics literature on two-sided markets (section 6.2) and discusses the extent to which the central question referred to above can be answered within this framework (section 6.3). This is followed by an overview of the various competition cases which are taking place in the Netherlands and in other countries in relation to the multilateral interchange fee (section 6.4). The chapter closes with several concluding comments (paragraph 6.5).

6.2 Economic theory

Before discussing the economics literature, it is important first to state what a two-sided market is. The literature is not unambiguous on this issue.⁵ The most important characteristic of a two-sided market is that there are two different types of end users, which both derive a benefit from a transaction. The transaction takes place on a platform and only occurs if both user groups participate.⁶ In addition, there is also an indirect externality: the more users there are on the one side, the more benefit there is on the other side.⁷ The platform has to charge both sides of the market a tariff in such a way that both user groups can (continue) to participate optimally and the platform makes a profit overall. This means that not only the total price which is charged to the two user groups is important, but also the way in which this total price is divided between these two groups. Examples of two-sided markets which are often referred to in the literature, in addition to debit card and credit card systems, are computer operating systems and shopping centres.⁸

The first analysis of the economic reasoning behind the interchange fee, which acknowledged the two-sided nature of the market, was by Baxter.⁹ Since the model used by him was relatively simple and is the starting point for the literature, the the essence of this model is set out below. Baxter's model is based on several assumptions, which were abandoned in later work by other authors. In particular, he assumes that retailers do not use the payment system to attract customers. Retailers therefore do not compete in this model with each other by offering the possibility of debit card payments. Furthermore, he assumes that both acquirers (banks which sell debit card services to retailers) and issuers (banks which sell debit card services to consumers) compete fiercely with each other for retailers and consumers respectively. Finally, Baxter assumes that consumers and retailers are homogenous. The essential features of the model are set out in figure 6.1.¹⁰

Figure 6.1 Simplified model of the interbank charge



The consumer purchases a product for price P from a retailer and is willing to pay a maximum of b_B (B stands for 'buyer') if the payment is made by means of a debit card transaction rather than in cash. The retailer is willing to pay a maximum of b_S (S stands for 'seller') if the payment for the product is made by means of a debit card transaction rather than in cash. The acquirers and issuers incur costs for offering the services. The (constant) marginal costs which issuers and acquirers incur to make electronic payments possible are represented by c_I (I stands for 'issuer') and c_A (A stands for 'acquirer'). It is important to note that these costs are relative to cash payments as is the value which consumers and retailers attach to debit card payments.¹¹ These costs are offset by revenues. The issuer and the acquirer charge consumers

and retailers P_I and P_A respectively for their services. Finally, the issuer and the acquirer settle the interbank charge with each other.

From an economic point of view, it is efficient if a payment originates when the value which the consumer and retailer jointly attach to payment by means of a debit card transaction rather than payment in cash, equal to b_B plus b_S , is greater than the total marginal cost to the issuer and acquirer for carrying out the debit card payment, equal to c_I plus c_A . Baxter notes that where issuers compete with each other for consumers, and acquirers compete for retailers, an efficient price level will not always arise without interbank payments. See the text box below.

Textbox

Under conditions of perfect competition, the issuer, will charge c_I (the issuer's marginal costs) and the acquirer will charge c_A (the acquirer's marginal costs).¹² A transaction therefore only occurs when b_B is greater than or equal to c_I and b_S is greater than or equal to c_A .¹³ Assume that the consumer's value b_B is less than c_I and the retailer's value b_S is greater than c_A , while the sum of both values $b_B + b_S$ is greater than $c_I + c_A$. Without the interchange fee ($a = 0$), in this specific situation no transaction would occur because the consumer would not wish to pay by means of a debit card transaction. The transaction would therefore be made in cash. However, it would be more efficient if the payment were to be made by means of a PIN transaction. Through a settlement (the interchange fee a) between the issuers and acquirers, the efficiency can be restored. If the acquirer pays the issuer an interchange fee of $a = b_S - c$, the acquirer's cost per transaction is b_S and the issuer's cost is $c_I + c_A - b_S$. The retailer will therefore have to pay b_S , while the consumer will be charged $c_I + c_A - b_S$. With this interchange fee, the consumer will pay by means of a debit card transaction if b_B is greater than $c_I + c_A - b_S$, or where $b_B + b_S$ is greater than $c_I + c_A$.¹⁴ In this case, debit card payments will indeed take place if this is economically efficient.

An aspect which is not given attention in Baxter's article is the precise dependence of the total number of debit card transactions on the tariffs which both sides of the market pay. A number of studies of more recent date explicitly model this dependence and at the same time abandon some of Baxter's assumption.

Schmalensee extends Baxter's model by allowing for imperfect competition between issuers and between acquirers.¹⁵ In addition, he takes into account the heterogeneity of retailers. Finally, he models the explicit dependence of total demand for debit card transactions as a function of the price charged to retailers and the price charged to consumers.¹⁶ He concludes that under some conditions, the interbank charge which is optimal for a private owner of a payment system is also the social optimum.¹⁷ More generally, he concludes that this level may lie either above or below the social optimum and that there may be either too many or too few card transactions.¹⁸

Rochet and Tirole explicitly model consumers' and retailers' demand in terms of the underlying advantages of using a payment system.¹⁹ This enables them to take into account the effects of competition between retailers in determining the effects on prosperity of various tariffs. They assume that issuers have market power, while acquirers are in perfect competition with each other. Rochet and Tirole concluded that if charging consumers for the

cost of debit card payments ('surcharges') is not permitted, the interbank charge determined by an electronic payments system is either equal to or higher than the social optimum.²⁰ The latter will result in too many debit card payments. Due to the lower tariffs charged to consumers, they will want to make PIN payment more often. Since retailers, despite the higher costs, will still accept debit card payments due to the competition between them for the patronage of consumers, too many transactions would occur. If surcharges are permitted, the level of the multilateral interchange fee will not affect the number of payments.

Wright uses a similar model to that of Rochet and Tirole.²¹ He ascertains the extent to which a multilateral interchange fee determined by an undertaking which maximises its profits generates optimal prosperity and what the role of surcharges is. Wright considers two scenarios in this regard. In the one scenario, retailers are in perfect competition with each other.²² The profits and total prosperity in this case are independent of the multilateral interchange fee and are independent of whether surcharges are allowed or not. In the other scenario, retailers are monopolists. In this case, the retailers cream off the surplus from the consumers. The multilateral interchange fee in this case results in too little use of cards.²³

Bolt and Tieman consider a so-called 'corner solution' of Rochet and Tirole's model.²⁴ For this purpose, they assume that the demand curves for retailers and consumers are characterised by constant price sensitivity (price elasticity). In this corner solution, the most price sensitive side of the market pays the least and the least price sensitive side pays the most. This appears to correspond to the actual situation on the Dutch market, where the retailer pays a certain tariff and the consumer pays nothing per transaction. Bolt and Tieman also determine what interbank charge the government would set, assuming total prosperity (consumer plus manufacturer prosperity). Their conclusion is that this level would not allow banks to recover their costs.

6.3 Analysis

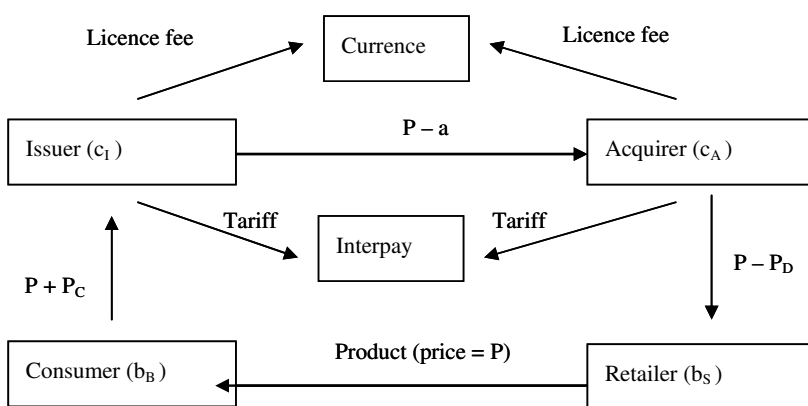
In the economics literature, an analysis is made of the way in which consumer and producer prosperity changes as a result of a multilateral interchange fee.²⁵ The following conclusions can be drawn. Firstly, in a two-sided market not only the total price, but also the price structure—the distribution of the total price between the one and the other side of the market—determines (in part) the number of transactions realised. The multilateral interchange fee may be an instrument to change this price structure. Secondly, a multilateral interchange fee may have the effect of increasing prosperity compared to a situation without the multilateral interchange fee if it is set at a very specific level. A multilateral interchange fee which is set incorrectly, however, may have the effect of reducing prosperity compared to a situation without a multilateral interchange fee. Thirdly, the specific level of the multilateral interchange fee which has the effect of increasing prosperity depends in a complex way on many factors.²⁶ Finally, there is no guarantee that a collectively determined multilateral interchange fee will be set at the right level from a welfare perspective.

Evans and Schmalensee draw similar conclusions.²⁷ The first conclusion is that the optimal multilateral interchange fee from a welfare perspective is not always equal to the multilateral

interchange fee based simply on the cost factors of issuers and acquirers: ‘(...) the socially optimal interchange fee is not in general equal to any interchange fee based on cost considerations alone’. This means that from a welfare perspective an optimal multilateral interchange fee determined collectively cannot simply be based on the costs of issuers or acquirers, according to Evans and Schmalensee. The second important conclusion is: ‘One cannot presume on the basis of theory alone that the interchange fee set collectively by an association is greater than, less than, or equal to the socially optimal interchange fee.’ This means that a collectively determined multilateral interchange fee does not automatically result in welfare gains.

If we consider the existing situation in the Netherlands, the simplified model used in the literature to analyse the effects of a multilateral interchange fee does not straightforwardly apply (see figure 8.1). In the Netherlands, acquirers and issuers pay tariffs to Interpay (which administers the PIN payment network) and Currence (which administers the intellectual property rights and network standards).²⁸ In addition, retailers pay an amount per transaction and consumers a fixed annual contribution for their card.²⁹ It is therefore unclear to what extent the conclusions drawn from the model also apply to the situation in the Netherlands.

Figure 6.2 Schematic representation of the Dutch multilateral interchange fee and PIN payment system



Another issue, of an empirical nature, is the extent to which two-sidedness plays a role in the setting of tariffs for the use of electronic payment systems. There may be differences, for instance, between markets which are at the start of their development and fully developed markets. The strength of the two-sided effects on the present market for PIN transactions is an empirical question which has not yet been answered.

Finally, the model used to analyse the effect on welfare of a multilateral interchange fee is a static model. In reality, competition is a dynamic process in which innovation and efficiency play an important role. The multilateral interchange fee possibly plays a role in this process, for instance because it may affect the incentives to invest.³⁰ Within this framework, the

economics literature as yet provides few guidelines for an analysis of the effects of the multilateral interchange fee.

6.4 Overview of competition cases

An overview of the most important competition-related cases in relation to the multilateral interchange fee is given below. The description is based on the actual state of affairs in September 2005. This section concludes with a summary of the most important arguments discussed in these competition cases. A schematic overview of the competition cases which relate directly to a multilateral interchange fee is given in table 6.1.³¹

Table 6.1 Competition cases in which the multilateral interchange fee was central

Country	Institution	Case	Year	Description of the case
United States	Private case	NaBanco v. Visa	1986	Collective setting of the multilateral interchange fee by Visa
United States	Private case	Reyn's Pasta Bella v. Visa and Kendall v. Visa and MasterCard	2003 – today	Collective setting of the multilateral interchange fees by Visa and MasterCard
European Union	European Commission	EuroCommerce v. Visa and MasterCard	2002 (Visa) 2003 – today (MasterCard)	Cross-border multilateral interchange fees; lack of transparency and relationship to cost.
United Kingdom		Visa and MasterCard	2004 – today (Visa) 2003 – today (MasterCard)	Collective setting of the multilateral interchange fees by Visa and MasterCard and insufficient relationship between the level of the multilateral interchange fees and cost.
United Kingdom	Office of Fair Trading	LINK ATM Network	2001	Application for exemption for the collective setting of multilateral interchange fees by LINK ATM Network
Spain	Tribunal de Defensa de la Competencia	Servired, Euro 6000 and 4B Services	2005	Dismissal of the application for exemption for the collective setting of multilateral interchange fees followed by an assessment of the multilateral interchange fee.
Netherlands	NMa	SOGA and Telegiro32	2003	Application for exemption for the collective setting of

				multilateral interchange fees by SOGA and Telegiro
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In addition to competition cases in which the multilateral interchange fee was central, a number of international cases have taken place, which are indirectly related to the multilateral interchange fee. These are listed in **table 6.2**.

Table 6.2 Competition cases which are indirectly related to the multilateral interchange fee

Country	Institution	Case	Year	Description of the case
United States	Department of Justice	Visa and MasterCard	2001	Complaint: Visa and MasterCard's exclusivity rules
United States	Wal-Mart chain	Wal-Mart v. Visa	2005-today	Complaint: HAC (Honor all Cards) Visa and MasterCard's rules
European Union	European Commission	not applicable	2001	Confirmation of HAC and non-discriminatory rules
Australia	Reserve Bank of Australia	not applicable	2003	Abolition of 'no-charge' rules MasterCard, Visa, American Express and Diner Club credit cards
Australia	Reserve Bank of Australia	not applicable	2003-today	Regulation of interbank charges for credit cards and design of a tariff structure for interbank charges for debit cards and cash dispensers

National Bancard Corp v. Visa (private case, United States)

In 1986 National Bancard Corp (NaBanco), a non-banking issuer of credit cards, claimed that collectively determining the multilateral interchange fee should be considered to be excessive price-fixing.³³ NaBanco's claim was rejected by the court for the following reasons:³⁴

- According to the court, the interbank charge was necessary to compensate for the cost of the risk of fraud and the insurance of the means of payment.
- The level of the interbank charge was checked by an independent firm of accountants.
- The court did not consider the bilateral setting of interbank charges to be a better alternative. Due to the large number of members (more than 10,000), affiliated to Visa, the transaction costs of bilateral negotiations would be high. The failure of bilateral negotiations would result in certain retailers not being able to accept some means of payment.
- The effect on competition, according to the court, was small because the possibility that PIN payments could be substituted by other means of payment, in the court's opinion, limited Visa's opportunity to charge anti-competitive prices. In addition, the court determined that the interbank charge was not obligatory because individual banks could adopt alternative schemes. It was therefore possible for the banks to enter into bilateral agreements and circumvent Visa's system involving the multilateral interchange fee.
- Finally the court concluded that multilateral interchange fees must be regarded as transfer payments which restore the balance between costs and revenues. They would be no incentive to set multilateral interchange fees at a strategically supracompetitive level,

since the decision-making body, the Board of Management of Visa, consisted both of issuing and acquiring banks. The multilateral interchange fee would therefore guarantee a balance between the issuing banks and the acquiring banks.

Retailers v. Visa and MasterCard (private case, United States)

Two private cases have been heard by the Federal Court in San Francisco. In both cases, retailers claimed that collective setting of the multilateral interchange fee by banks affiliated to Visa and MasterCard is a form of illegal price-fixing.³⁵ The court has to determine, amongst other things, whether the judgment in the case mentioned above (*Nabanco v. Visa*) is applicable to these cases. In the one case (*Reyn's Pasta Bella v. Visa*) a motion for dismissal of the case was rejected. In the other case (*Kendall v. Visa and MasterCard*) the claim was rejected. According to the court, there is insufficient evidence that Visa and MasterCard charged an excessive MSC (Merchant Service Charge).³⁶ Kendall has appealed against this judgment.³⁷

EuroCommerce v. Visa en MasterCard (European Commission)

Following a complaint from EuroCommerce, the European organisation of retail traders, the European Commission started an investigation into the cross-border multilateral interchange fees charged by Visa (1999) and MasterCard (2003).³⁸ In its decision in the Visa case (2002), the Commission concluded that the multilateral interchange fee restricted competition in the sense of Article 81 of the EC Treaty.³⁹ The Commission determined that the multilateral interchange fee harmed competition both between issuing banks and between acquiring banks. The Commission referred to the fact that Visa could set the multilateral interchange fee at any desired level without taking into account an objective benchmark, which increase the costs incurred by retailers. In addition, the lack of transparency with regard to the multilateral interchange fee weakened the negotiating position of retailers.

The European Commission granted an exemption subject to the following conditions. Firstly, Visa was to introduce amended multilateral interchange fees before September 2002. Secondly, Visa was obliged to carry out a cost study into the three above-mentioned cost components for payment cards, credit cards and 'deferred' debit cards.⁴⁰ Thirdly, it was not permissible to set the multilateral interchange fees at a level which was higher than the tariff calculated in the cost study. Finally, Visa was required to notify the European Commission within one month if the interregional multilateral interchange fees were changed.

As a result of the ruling, Visa has reduced the level of the multilateral interchange fees on credit cards and deferred debit cards to 0.7% of the average transaction amount until 2007. In addition, a fixed charge per transaction, rather than a percentage, was introduced for debit cards in 2003.⁴¹ Secondly, the level of the multilateral interchange fees will be based on the actual cost of the services provided to retailers. These are the costs of executing the transaction, the interest-free period for cardholders and the provision of a payment guarantee. Visa will have the cost orientation of the multilateral interchange fees audited by an independent firm of accountants. Thirdly, Visa will allow affiliated banks to publish information on various cost components of the multilateral interchange fees. Fourthly, Visa has introduced a separate tariff for transactions paid by e-mail or telephone. The cost of a payment guarantee and the execution of transactions made by e-mail or telephone are

different, as a result of which a separate tariff is desirable. The case against MasterCard has not yet been completed.

Visa and MasterCard (Office of Fair Trading (OFT), United Kingdom)

In 2000 the British competition authority, OFT, started an investigation into the multilateral interchange fees on MasterCard and Visa's credit cards.

In the case against MasterCard, OFT concluded that the collective setting of a multilateral interchange fee in the period from 1 March 2000 to 18 November 2004 resulted in a restriction on competition and did not qualify for an exemption in this period. OFT, however, did not impose a fine.⁴² According to OFT, the multilateral interchange fee sets the minimum level for the tariff that retailers pay to acquirers. In addition, it is important that the multilateral interchange fee, according to OFT, was used as a payment for external costs and was not directly related to maintaining MasterCard as a viable payment platform, such as the costs for providing an interest-free period. OFT acknowledged that the multilateral interchange fee could also be to the advantage of consumers.⁴³ In the case of bilateral contracts, acquiring banks could refuse the means of payment used by certain issuing banks. A multilateral interchange fee contributes to ensuring that retailers accept the means of payment of all issuing banks, which makes the means of payment more valuable to consumers. In the absence of a multilateral interchange fee, each user of MasterCard's network would have to negotiate with all other users on the additional costs incurred.

In the investigation into Visa, OFT published its statement of objections.⁴⁴ In this OFT indicated that it was of the opinion that the collective fixing of the interbank charge by Visa and its members restricted competition. According to OFT, the way in which the multilateral interchange fee was set results in tariffs which are too high for retailers and, ultimately, for consumers.

LINK ATM Network (OFT, United Kingdom)

In April 2000 LINK ATM, the largest network of cash dispensers in the United Kingdom, requested OFT to give its opinion on the multilateral interchange fee. The multilateral interchange fee provides compensation for the cost of distributing money and providing services.⁴⁵ In this case, the multilateral interchange fee is paid in the United Kingdom by the issuing bank and the acquiring bank. In fact, this is not a two-sided market. As a result, the economic analysis of the multilateral interchange fee differs from the analysis of the multilateral interchange fee in relation to a transaction involving a retailer.

OFT concluded in 2000 that in theory a multilateral interchange fee could result in three possible restrictions on competition.⁴⁶ Firstly, it may restrict the opportunities which members affiliated to LINK ATM have to determine their own pricing policy. Secondly, a multilateral interchange fee may reduce the incentive to compete for the customers of other banks. Finally, a multilateral interchange fee could restrict competition between different payment systems.

OFT granted an exemption in October 2001 for a period of five years. According to OFT, the multilateral interchange fee, as used by LINK ATM, met the criteria for exemption for the

following reasons.⁴⁷ Bilateral negotiations on interbank charges would not constitute an alternative for the multilateral interchange fee. These may result in higher tariffs due to the additional transaction costs and possible free-rider behaviour of individual banks. In addition, the ATM cash dispensers were accessible to all cardholders, irrespective of the bank at which they had an account. This would mean that small banks have access to large ATM networks without having to incur high costs. Furthermore, spreading the costs make it easier to extend the network. Competition would result in the above advantages being passed on to cardholders. Finally, according to OFT, it was important that LINK ATM set the level of the multilateral interchange fee at the level of its members' average costs. These costs are measured by an independent company and are adjusted on a regular basis.

Servired, Euro 6000 and 4B Services (Tribunal de Defensa de la Competencia (TDC), Spain)

On 11 April 2005, the Spanish competition authority TDC rejected an application for exemption for the period from 2002 to 2005 submitted by three organisations which facilitate network services and other cooperative activities between banks.⁴⁸ Following this, the multilateral interchange fees were terminated as of 15 July 2005. The court gave the following assessment of TDC's decision. The level of the multilateral interchange fees, according to the court, was not related in any way to the costs. There was a lack of 'objectivity, transparency and economic logic'.⁴⁹ The following aspects of the method of calculation of the multilateral interchange fee were not accepted by the court:

- setting the same multilateral interchange fee for both payment cards, and credit cards and deferred debit cards;
- the arbitrary way in which the maximum multilateral interchange fee was determined;⁵⁰
- the multilateral interchange fee was determined per sector on the basis of annual turnover data, whereby there was a lack of objectivity in classifying the sectors;
- the discretionary power to give preferential treatment to various retail sectors when calculating the multilateral interchange fee compared to other retail sectors.

In its decision, the court stated that the exemption was only possible under certain conditions.⁵¹ Firstly, the interbank charges for transactions with payment cards should be different to those for transactions with credit cards or deferred debit cards, in accordance with the difference in costs of these transactions. Secondly, according to the court, in determining the interbank charge of transactions with payment cards and credit cards, only the cost of authorisation and executing the transaction may be taken into account. Costs which are not directly related to services which acquiring banks provide to retailers and the cost of administering the system should not be taken into account. These costs must be determined as a fixed amount per transaction. In addition, the multilateral interchange fee for credit cards must be based on the cost of the risk of fraud in relation to transactions. These costs should be determined periodically on the basis of actual figures.

Visa U.S.A. and MasterCard (Department of Justice, United States)

The Department of Justice (DoJ) concluded in 2001 that exclusivity rules must be considered anti-competitive.⁵² These rules stipulate that the banks, affiliated to Visa and MasterCard, were not permitted also to issue American Express and Discover payment cards. The court

concluded, following a decision by DoJ, that Visa and MasterCard both had market power in the relevant markets of credit cards and the network for credit card services (the infrastructure which facilitates payments). The exclusivity rules, according to the court, restricted the output of payment cards and network services and constituted a restriction on price competition. The court concurred with the analysis of DoJ. On these grounds, Visa U.S.A. and MasterCard were obliged to abolish these rules.

Wal-Mart *et al.* v. Visa and MasterCard (United States)

A group of retailers submitted a complaint about the non-discrimination rule applied by Visa and MasterCard (the so-called "Honor-All-Cards rule").⁵³ The rule stipulates that retailers which accept Visa and MasterCard must also accept other payment cards such as Visa Check and Mastermoney. These cards (Visa Check and Mastermoney) incurred much higher multilateral interchange fees than Visa and MasterCard credit cards and payment cards. In 2003, the parties reached an out-of-court settlement of more than USD 3 billion. Also, the non-discrimination rule was abolished and the multilateral interchange fee on all payment cards was reduced. In the out-of-court settlement proposal, as of 1 January 2007, official standards will also apply with regard to visual 'identifiers' on Visa and MasterCard payment cards so that these payment cards can be distinguished clearly by consumers and retailers from credit cards.⁵⁴ As of 1 January 2005, 80% of payment cards complied with these requirements.

Honor-All-Cards rules and the no-surcharge rule (European Commission)

In August 2001, the European Commission approved Visa's Honor-All-Cards rule (all cards of a certain supplier must be accepted) and the non-discrimination rule (no surcharge may be charged or discount given for payments with a certain means of payment).⁵⁵ In theory, these rules could restrict the retailers' commercial freedom. On the basis of two studies, from the Netherlands and Sweden, the Commission concluded, however, that the abolition of these rules would have little or no effect.⁵⁶ According to these studies, many retailers do not use the possibility of surcharging and the abolition of this rule would not affect the affiliation of retailers to the payment system.⁵⁷

Regulation of the tariff structure of interbank charges (Australia)

In Australia, some of the interbank fees are regulated by the central bank.⁵⁸ The multilateral interchange fee in the case of most payment cards is also paid by the issuing bank to the acquiring bank, in contrast to the practice in other countries.⁵⁹ Only a few payment cards use the system of a multilateral interchange fee. In the case of other payment cards, the interbank charges are determined bilaterally.

In the case of credit cards, a multilateral interchange fee had been determined before 1 July 2003.⁶⁰ Since 1 July 2003 the multilateral interchange fee is also regulated by the Central Bank of Australia.⁶¹ One of the requirements is that the average multilateral interchange fee must be lower than a tariff determined on the basis of the costs of the issuing banks. The new method of calculation of the multilateral interchange fee was determined on 31 October 2003. The multilateral interchange fee for credit cards subsequently fell from approximately 0.95% to 0.55% per transaction.⁶²

After regulating the multilateral interchange fee for credit cards, the central bank has also given consideration to the interbank fees for payment cards (Visa and EFTPOS⁶³) and cash dispensers. In the case of EFTPOS payment cards, the new interbank charge will be determined bilaterally. This is approximately AUD 0.20 per transaction. Visa payment cards are characterised by a multilateral interchange fee, which (in the specific case of Australia) is paid by the issuing bank to the acquiring bank.⁶⁴ On 14 October 2004, the central bank decided to regulate the interbank tariffs of payment cards. At present, in consultation with the sector, a standard is being formulated.⁶⁵

The interbank charge for guest use of cash dispensers is determined at present on a bilateral basis. Noticably, the differences between bilateral contracts are minimal. The average tariff is AUD 1 per transaction. Following discussions with regard to the interbank charges for payment cards, the central bank conducted research into the necessity of regulating these tariffs. For the time being, the central bank has decided not to regulate these tariffs, partly on the advice of the sector.⁶⁶

6.5 Analysis

Competition cases in relation to the multilateral interchange fee have been and still are an issue in various countries, including the United States, United Kingdom, the European Union (in relation to cross-border payment services) and in some separate European Member States. In most of the countries, the multilateral interchange fee is paid by the acquiring bank to the issuing bank. Only in Australia, where the multilateral interchange fee is partially regulated, is the interbank charge paid by the issuing bank to the acquiring bank in relation to certain means of payment (Visa and EFTPOS).

In these cases, the following aspects were regarded as practical advantages of the multilateral interchange fee:

- Determining a multilateral interchange fee incurs lower transaction costs than a situation where banks enter into bilateral agreements.
- The multilateral interchange fee is thought to create a level playing field for possible new entrants and small parties whose negotiating position would be limited by the use of bilateral interbank charges.
- If banks were to apply bilateral tariffs, there would be an incentive to set the tariffs as high as possible, without taking into account the negative external effects of a tariff which is too high on the payment system as a whole. Determining the multilateral interchange fee collectively might limit this effect.

In addition, a number of countries appear to impose the following conditions on the multilateral interchange fee:

- The multilateral interchange fee must be determined objectively.
- The method of calculating the multilateral interchange fee must be transparent to the participating banks, retailers and consumers.
- The level of the multilateral interchange fee must be related to the costs incurred. Cost components referred to in various cases include: the cost of executing the transaction and

authorisation of the transaction, the cost incurred by the risk of fraud in relation to the use of the means of payment, the cost of the interest-free period and the cost of issuing a payment guarantee. In different cases, however, varying (combinations of) cost components are considered important.

6.6 Conclusions

In this chapter, a description was given of the economics literature relating to two-sided markets and competition cases relating to the multilateral interchange fee. On the basis of this description, four conclusions can be drawn.

Firstly, it appears from the literature that a multilateral interchange fee cannot be based simply on the one-sided costs of issuers or acquirers. If this is selected, the resulting level is not necessarily optimal from a welfare perspective. In this regard, a theoretical economic analysis does not imply some of the demands made at present in competition-related cases.

Secondly, to give an unambiguous answer to the question as to how setting a multilateral interchange fee for the PIN payment product effects consumer prosperity, it would be necessary to carry out an analysis tailored to the Dutch situation. The competition process would have to play a role in this analysis. The existing theoretical economics literature is a point of departure for this.

Thirdly, the empirical question as to the extent to which two-sidedness is decisive in determining the tariffs which users of electronic payment systems pay is relevant. Empirical research relating to the multilateral interchange fee is limited as yet to overviews of the level and development of the multilateral interchange fee in the various countries or in relation to payment systems.

Finally, various countries reach different conclusions with regard to the anti-competitive effects of the multilateral interchange fee and the criteria which a multilateral interchange fee must meet if it is to be approved under competition law. The increasingly international dimension of payment services emphasises the importance of establishing a general framework for analysing the effects of the multilateral interchange fee.

7 Competition on the coinsurance market

7.1 Introduction

Coinsurance occurs where numerous insurers jointly underwrite a risk. Every participant underwrites part of this risk. Coinsurance is a form of primary risk spreading when underwriting insurance.¹ This is important in relation to risks of considerable size (large amounts have to be paid out in claims), major risks (the probability of claims is high), complicated or one-off risks for which there are no claims statistics (the claims are difficult to predict) and possible long-term effects (the claim only occurs after many years). In such cases, the insurer is not willing or able to underwrite such risks alone. The customer may also wish to have a risk underwritten through coinsurance. There may be various reasons for this such as price and sometimes also the desire for certainty. After all, the risk that the insurer's obligations will not be met is greater in the case of a single insurer than in the case of a group.

Coinsurance agreements only relate to business non-life insurance. It relates to transport and fire insurance and a number of other types of insurance, such as technical insurance and accident and liability insurance. The last category is referred to below as miscellaneous risks insurance. Within the transport branch, this involves mainly marine and inland shipping all-risks insurance, and goods-in-transport and transport insurance.²

On the market for coinsurance, far-reaching cooperation occurs between insurers.³ This is permissible under certain conditions in accordance with the Block Exemption for the insurance sector.⁴ There are also intensive contacts between insurers and insurance intermediaries active on the insurance exchange, referred to as insurance brokers. In addition, the market has a high degree of concentration and the number of providers on the coinsurance market has decreased in recent years. Finally, the market has a strong tendering character: the same risks are often offered each year by the same insurance brokers to the same insurance. These factors were the reason to examine the Dutch coinsurance market from the perspective of economic competition. For this research, interviews were held with insurance brokers, insurers, an association of buyers, the branch association Nederlandse Assurantiebeurs (VNAB) and academics. In addition, use was made of relevant literature and the annual reports of VNAB.

The structure of this chapter is as follows. Firstly a description is given of the coinsurance market. After this, the Block Exemption is discussed. This is followed by an estimate of the risk to economic competition of limited competition on this market.

7.2 Description of the market

The coinsurance market can be divided into two different segments. For the major and very large risks of large international undertakings, such as Akzo Nobel and Shell, there are few alternatives to coinsurance. Within the market, these multinationals also rely on insurance

brokers and insurers which can underwrite or can provide cover for risks throughout the world, and which have an international network. In addition, these multinationals make considerable demands with regard to the rating of insurers. The fact that an insurer meets the regulator's solvency requirements is not sufficient. This means that for these customers, only five to ten insurers remain who are active worldwide, insure all types and sizes of risk and cover specialist risks, as well as having a sufficiently high rating.

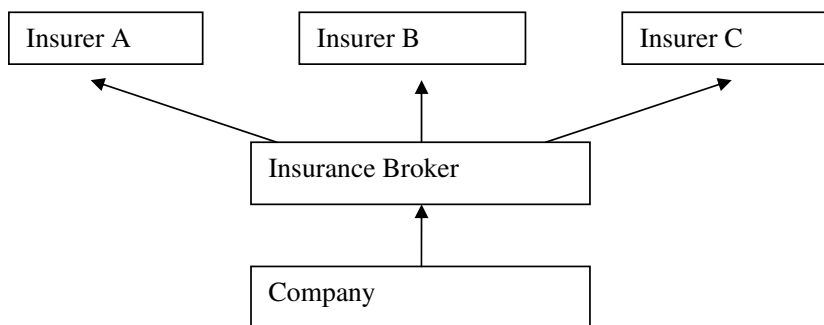
Secondly there is the segment in which medium-sized undertakings operate. These risks are generally not so great that they cannot be underwritten by a single insurer. For these medium-sized undertakings, having a risk underwritten by a single insurer is therefore an alternative to the coinsurance market. Insurance brokers active in this segment state that they examine possibilities for their customers both on the provincial market (where a single insurer underwrites the insurance) and on the coinsurance market. In general, however, the interviewees stated that the provincial market is more expensive than the coinsurance market.

The analysis below applies largely to both market segments. Where this is not the case, this is stated.

7.2.1 Market parties

Coinsurance always takes place with the intermediation of a broker. The broker looks for insurers who are willing to underwrite part of a risk. In the case of a coinsurance agreement, each insurer underwrites the risk in proportion to its share of the insured sum. The insurance agreement can be entered into directly by a broker with the various insurers, but may also be underwritten by an authorised agent or underwriter, who accepts risks on behalf of a pool of insurers. This structure is represented schematically in figure 7.1.

Figure 7.1 Schematic structure of coinsurance



Insurance exchange

The insurance exchange is the meeting place of brokers, authorised agents and insurers who wish to underwrite insurance through coinsurance. In the Netherlands, there were traditionally two insurance exchanges, in Amsterdam and Rotterdam. The need for a daily insurance exchange has decreased sharply in recent years. One explanation for this is that less face-to-face contact is necessary due to new electronic means of communication. VNAB is currently introducing an electronic exchange system (E-ABS).⁵ In addition, the number of brokers and insurers active on the exchange has fallen. The Amsterdam insurance exchange was closed in

2004. The Rotterdam insurance exchange has only opened two afternoons a week for the signing of contracts since January 2004. Coinsurance contracts are also entered into without going through the exchange. Insurance brokers of any size which are not active on the exchange can offer a risk to numerous insurers. However, there is no public information available on this. All the transactions which go through the insurance exchange are registered by VNAB.

The parties involved in coinsurance agreements are discussed below, namely insurance brokers, insurers, authorised agents, policyholders and the branch association.

Insurance brokers

Insurance brokers mediate between the policyholder (a company) and insurers. Policyholders are not permitted to negotiate directly on the insurance exchange without an insurance broker. To be active on the insurance exchange, an insurance broker must be a member of the brokers section of VNAB.⁶ The tasks of the insurance broker on the insurance exchange are more extensive than those of an insurance broker who mediate on the provincial market between the policyholder and the insurer.⁷ In addition to analysing the customer's wishes and negotiating with insurers, the tasks of the insurance broker on the insurance exchange also include:

- drawing up a risk analysis of the object of the insured, which is presented to the insurers;
- drafting the insurance cover and possibly drawing up a draft of the policy text which will be presented to the insurers (the so-called 'cover note');
- drawing up the coinsurance agreement;
- collecting the premium. In the fire and transport branches, the insurance brokers and not the insurers incur the risk that it will not be possible to collect the premium.

Insurers

Insurers must be members of the insurers section of VNAB if they wish to trade on the insurance exchange. When entering into an insurance agreement, there is always one lead insurer, which is the first to sign and takes on the largest part of the risk.⁸ The lead insurer is often the insurer with most knowledge of a certain type of insurance. According to most of the interviewees, other insurers (followers), the co-signatories, generally take their decision on the basis of the fact that the lead insurer is willing to underwrite part of the risk. However, others noted that when premiums are under pressure, more insurers do research themselves into the risks of the object to be insured. The lead insurer also takes the lead in settling claims. The policies include a so-called 'to follow clause', which stipulates that when a claim is paid out, the lead insurer must be followed and the followers must make a proportional contribution to the payment of the claim. Even if the lead insurer makes a payment out of fairness to the policyholder, the followers must contribute to this.⁹

Authorised agents

Authorised agents, also referred to as underwriters, receive a power of attorney from an insurer to accept risks up to a certain maximum amount.¹⁰ An authorised agent increases its own capacity to sign for risks for the account and risk of the principal(s) by obtaining numerous powers of attorney and then entering into an agreement with all the principals. This is a so-called pool agreement. To trade on the insurance exchange, an authorised agent must

be a member of the insurers section of VNAB. Previously, authorised agents had a very strong position on the insurance exchange. The number of authorised agents active on the insurance exchange has decreased in recent years due to acquisitions by insurers. According to the annual reports of VNAB, the number of authorised agents active on the insurance exchange fell from 18 in 1995 to 10 in 2003.

Policyholders

The policyholders on the stock exchange are large companies, starting in the highest segment of the small and medium-sized enterprise sector. The risk managers of the largest (145) internationally operating Dutch companies are united within the Netherlands Risk and Insurance Management Society [*Nederlandse Associatie van Risk en Insurance Managers (NARIM)*].

Branch association

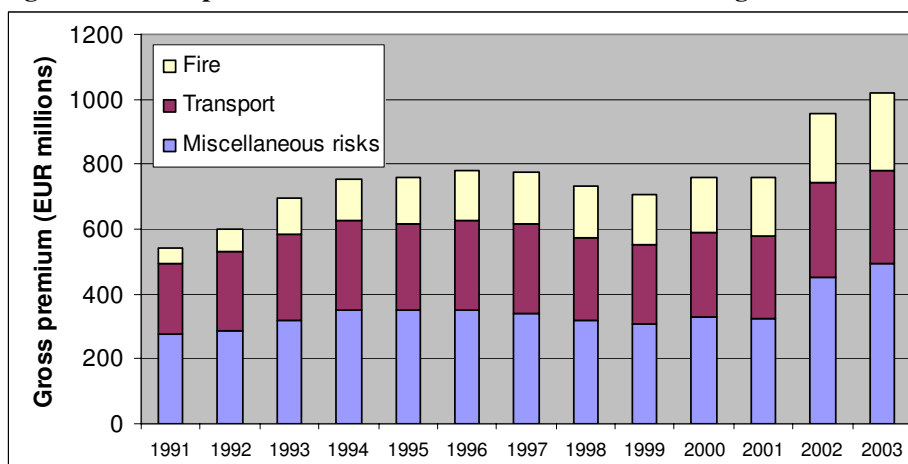
As was stated, VNAB is the association of insurers, authorised agents and insurance brokers active on the insurance exchange. Membership is obligatory in order to enter into agreements on the insurance exchange. VNAB is responsible for the administrative processing of transactions through the so-called *Beurs Clearing Systeem (BCS)* [Insurance Exchange Clearing System]. In addition, the association is involved in developing standard insurance exchange policies in cooperation with the Dutch Association of Insurers (for further information see section 8.3).

7.2.2 Size and development of the market

In its annual report, VNAB publishes the premium income realised on the insurance exchange by insurers and insurance brokers affiliated to VNAB. This premium income is an underestimate of the total premium income from coinsurance, because coinsurance agreements are also entered into without going through the insurance exchange. In addition, some of the contracts entered into on the insurance exchange are not included in VNAB's figures because large internationally active insurers pay part of the premiums directly through foreign parents or subsidiaries.

In 2003, insurance brokers who were members of VNAB recorded more than EUR 1.1 billion and insurers who were members EUR 1 billion in gross premium income from trade on the insurance exchange.¹¹ The difference is the commission which the insurance brokers receive from the insurers. The premium recorded on the insurance exchange is approximately 5% of the total gross premium income recorded for non-life insurers active in the Netherlands.¹² Figure 7.2 gives the development of the recorded premium in the period 1991-2003. Fire insurance at 47% of the recorded premium income is the largest category on the insurance exchange, followed by transport (32%) and miscellaneous risks insurance (21%). Of the total for fire insurance, 16% is underwritten through the insurance exchange. Transport, measured on the basis of gross premium income, accounts for 12%.

Figure 7.2 Gross premium of insurers on the insurance exchange



Source: Annual reports VNAB 1990-2003.

The gross premium income for fire insurance underwritten on the insurance exchange shows an increase from 2002 onwards after a slight dip at the end of the 90s. As a result of poor results, associated with an increase in claims on fire policies underwritten on the insurance exchange and a fall in results from investments, the insurers has introduced large premium increases in recent years.¹³ The interviewees stated that the premium for fire insurance had once again started falling. The miscellaneous risks category has increased sharply since the beginning of the 90s, mainly due to an increase in demand for liability insurance. The shift from delictual liability to risk liability in various areas, the increase in the size of liability claims (for instance environmental claims resulting from accidents with tankers) and a greater awareness of the ability to make claims by parties suffering losses are the reason for this. The recorded gross premium for transport insurance remained fairly constant during the period 1991-2003.

7.2.3 Insurance broker's commission

According to the interviewees, most of the contracts provide for commission paid to the insurance broker by the insurers. The respondents stated that an insurance broker, in principle, receives the same commission rate from all insurers. These rates are lower than the rates on the provincial markets.

However, there are also insurance brokers who work for large customers on a fee basis, whereby all the services for the customer are specified and invoiced. In these cases, the commission is returned to the customer. For a long time, a shift has been observed towards working on a fee basis. The interviewees also stated that this method of remuneration is used increasingly.¹⁴

7.3 The framework of competition law

In 2003 the European Commission approved a Regulation on the basis of which, subject to conditions, certain joint-venture agreements between insurance undertakings were permitted.¹⁵ This replaced the Regulation of 1992.¹⁶ The exempted agreements include, for

instance, the setting up of groups for co(re)insurance, also referred to as coinsurance groups, and the adoption of non-binding standard policy conditions. According to the European Commission, this Regulation ensures that there is a balance between providing the insurance sector with legal certainty and the need to exempt only those agreements which clearly result in efficiency advantages and benefit consumers.

7.3.1 Coinsurance groups

For the insurance of large and exceptional risks, which individual insurance undertakings would have difficulty underwriting in full, insurance groups may be established in which a number of insurers participate.¹⁷

Insurance groups, in principle, fall within the scope of the Regulation if the group's market share on the relevant market does not exceed 20%.¹⁸ This ensures that buyers can continue to benefit from competition between coinsurance groups. In addition, the Regulation imposes additional conditions on coinsurance groups. For instance, the agreement may not result in a division of markets and customers amongst undertakings or to the joint setting of commercial premiums.

Insurance groups or other types of joint ventures, which do not fall directly within the scope of the Regulation, may also benefit under the exemption from the prohibition on cartels if they satisfy the conditions of Article 81(3) of the EC Treaty and/or Article 6(3) of the Dutch Competition Act. These conditions are (1) that the agreement contributes to improving production or distribution, while allowing consumers a fair share of the resulting benefit; (2) that the agreements are indispensable; and (3) that there is sufficient remaining competition.

7.3.2 Standard insurance exchange policies

On the insurance exchange, standard insurance exchange policies are used which are drawn up by VNAB in cooperation with the Dutch Association of Insurers. The standard insurance exchange policies which, for instance, give a description of the occurrences which are covered (for example, fire, water and storm damage) and contain clauses in relation to the period of notice and claims settlement (for example, the appointment of experts), make it possible to take out insurance quickly and efficiently because the insurance broker would otherwise have to negotiate every clause with all the insurers involved. This would increase the transaction costs considerably. There are various types of standard insurance exchange policies for various types of insurance.¹⁹

The standard insurance exchange policies have been deposited on the website of the VNAB. This means that if the policy text drawn up deviates from the deposited text, due to a typing error, the latter applies. Deviating provisions may be included. In practice, according to the interviewees, the parties frequently deviate from the standard clauses. In addition to the standard insurance exchange policies, insurance brokers also draw up their own policies.

Use of the standard insurance exchange policies and the Regulation

As was stated above, undertakings active in the insurance sector—whether or not within the context of VNAB—may adopt non-binding standard policy conditions in accordance with the Regulation.²⁰ These standard policy conditions may define, for instance, the risks which are

covered. If no insured amounts and premiums are stated in the standard policy conditions *and* if all the other conditions for exemption are met, the standard insurance exchange policy will fall within the scope of the Regulation.²¹ The Regulation emphasises that standard insurance exchange policies which contain provisions which stipulate the (maximum) amount to cover (or the inverse thereof, namely the part to be paid by the policyholder, the 'excess'), are not exempt from the prohibition on cartels.²²

7.4 Analysis of risks to economic competition

This section examines the risks to economic competition on the coinsurance market on the basis of a number of structural indicators (such as the degree of concentration, entries and exits and barriers to entry).

Degree of concentration

In 2003 there were 60 insurance brokers active on the insurance exchange in the Netherlands. However, the market shares are distributed unevenly. Interviewees stated that the two largest insurance brokers, Aon and Marsh, together have a market share in the Netherlands of 50% to 60%.

In 2003, 37 insurers were active on the Dutch insurance exchange, of which 10 were registered as authorised agents. As was stated above, there is only a small group of insurers which cater for all types of insurance and have the necessary capacity to accept the risks of large international undertakings. These are, in particular, the German and American insurers: Allianz (German), AIG (American), Zurich (Swiss), HDI (German), ACE (American), Gerlich (German), Chubb (American) and XL (American). Relatively few Dutch insurers are active on the insurance exchange. Their joint market share is estimated to be less than 25%. In addition to these players, niche players are also active on the insurance exchange, which do not offer all products, but focus on certain types of insurance, such as directors' liability insurance and professional liability insurance.

Entries and exits

The number of insurers and authorised agents active on the insurance exchange has fallen from 52 in 1990 to 37 in 2003 (see table 7.1). Since the entries and exits balance each other out, the decrease can be explained mainly by mergers, whereby authorised agents, in particular, were acquired by insurers. The average number of insurers that underwrite a policy fell from 3.8 in 1990 to 2.8 in 2003. In the insurance brokers section, on balance there were more entrants in the period 1990-2003. The number of insurance brokers increased from 54 to 60 (see table 7.2). Several mergers have also taken place amongst insurance brokers in recent years.

Table 7.1 Entries and exits of insurers and authorised agents

	2003	2002	2001	2000	1995	1990
Number of insurers	37	41	40	42	49	52
Of which, authorised agents	10	12	11	13	18	not known

Entries	1	2	0	0	0	not known
Exits	3	1	0	1	2	not known
Mergers	2	0	2	3	0	not known

Table 7.2 Entries and exits of insurance brokers

	2003	2002	2001	2000	1995	1990
Number of insurance brokers	60	62	62	61	68	54
Entries	5	3	1	1	6	not known
Exits	4	2	0	2	4	not known
Mergers	2	1	0	3	0	not known

Requirements for admission to the insurance exchange

Every insurance broker may, in principle, become an insurance broker on the insurance exchange. In practice, however, there are thresholds, on the one hand, because the insurance broker must be familiar with the way in which the insurance exchange works and, on the other, because it is necessary to connect to the administrative processing and clearing and settlement system, the *Beurs Clearing Systeem (BCS)*. Membership of VNAB is necessary for this. VNAB has set the following requirements for the admission of new members which are available to everyone and a published in VNAB's Standing Rules.

Insurance brokers must be registered in the register of the Social and Economic Council (SER) and must have an Insurance A diploma. In addition, they must have professional liability insurance and must be a member of Nederlandse Vereniging van Assurantie Adviseurs en Financiële Dienstverleners (NVA) [Netherlands Association of Insurance Advisors and Financial Service Providers] or Vereniging van Onafhankelijke Financiële en Assurantieadviseurs (NBVA) [Association of Independent Financial and Insurance Advisors]. The following production requirements also apply if one wishes to use BCS: at least 100 insurance broker transactions must be made annually and a gross premium of at least EUR 50,000 must be offered to insurers.

According to various interviewees, the requirements for admission to the insurance exchange are not strict and the admission procedures do not take long. Both insurers and insurance brokers could easily enter or exit the insurance exchange. The production requirement for insurance brokers with regard to the minimum number of entries in the BCS does not appear to be high compared to the average production of insurance brokers already active on the insurance exchange (on average 4900 entries and a recorded average gross premium of EUR 8.2 million per annum). In addition, VNAB stated that new members are dealt with leniently with regard to the production requirement. In practice, entries and exits occur. Nationale-Nederlanden withdrew from the insurance exchange at the beginning of the 90s due

to the poor results, but has once again entered. AXA, which ceased its activities on the exchange five years ago, has announced that it will rejoin.²³

Switching costs

Coinsurance agreements are generally entered into for a short period (one year). As a result, policyholders can switch fairly easily. The interviewees stated that in the case of every agreement, the insurance broker (and customer) actually reconsiders which insurers could make the best offer. Due to the decrease in the number of insurers and specialisation amongst insurers on the basis of the type of risk, the number of insurers from which companies on the insurance exchange can choose is limited.

Intensive contacts

In comparison to the provincial market, in the case of coinsurance the contacts between insurers are more intensive, whether or not with the intermediation of an insurance broker. The various insurers obtain information through the insurance broker about the customer and in processing claims the insurers which jointly underwrite a policy will have to cooperate. In the past, a so-called industrial tariff applied, whereby a bureau appointed for this purpose set the premium for certain types of risks. 'Best terms or conditions' were also used. In this case, an insurer stipulates that if an insurer which underwrites a risk receives a higher premium than was agreed earlier with the other underwriters of the risk, this premium will apply with retrospect to all the insurers. A clause such as this may have the effect of driving up prices. VNAB has stated that these clauses are no longer used.

7.5 Conclusions

For medium-sized companies, the provincial non-life market is an alternative to coinsurance. Considerably more insurers are active on the total (provincial) non-life market than are active on the coinsurance exchange. This means that a high degree of concentration on the coinsurance exchange does not necessarily indicate that competition is restricted. Entries and exits on the insurance exchange are possible and do, in fact, occur. The insurance exchange in the Netherlands shows that entries and exits occurred in the period 1990-2003 both amongst insurers and amongst insurance brokers. On the provider side (insurers), this sometimes involved parties which had been active earlier on the market. Due to the short duration of contracts, it is easy, in principle, to switch, but due to the small group of insurers policyholders do not have much choice. This description of the market structure points in the direction of a limited risk to economic competition.

On the market for coinsurance, however, far-reaching cooperation takes place between insurers. The contacts between insurers and insurance brokers are also intensive and coinsurance has the character of a tender market. These factors, both separately and in relationship to each other, do give rise to risks to economic competition. Continuing competition regulation is desirable from this point of view. Finally, VNAB makes various demands on parties who wish to be active on the insurance exchange. From the perspective of competition, it is important that these requirements meet the criteria of objectivity,

transparency and independence, as set out in the Guidelines for Cooperation between Undertakings [*Richtsnoeren samenwerking bedrijven*].

8 The market for investment funds

8.1 Introduction

A scan of the share market was published in the *Financial Sector Monitor 2004*. As was announced, FSM carried out further research in 2005 into the market for investment funds.¹ This chapter reports on this research.

According to the Dutch Central Bank, the total capital of Dutch investment funds amounted to EUR 99.7 billion in 2004.² Both private investors and institutional investors invest in investment funds. The total invested capital in the Netherlands at the end of 2003 is estimated to have comprised investments by private individuals amounting to EUR 41 billion, indirect investments through insurers by private individuals amounting to EUR 37 billion (for instance through pension insurance, annuities, lump-sum policies and mortgages with a unit-linked component) and investments by pension funds amounting to EUR 22 billion.³ The total capital from investments by private individuals is therefore estimated to be EUR 79 billion.⁴ Investment funds are therefore of considerable importance to the financial planning of Dutch households.

The aim of this research is to establish whether there are risks to economic competition on the market for investment funds.⁵ The present chapter reports on this research which took place mainly on the basis of desk research and interviews with regulators and people active in the sector. Information was also requested from market parties.

Firstly, a description is given of the market (section 8.2). Various structural characteristics are considered to provide an indication of the risk to economic competition on this market. The most important developments on the market are also discussed. The chapter closes with a conclusion based on this description (paragraph 8.3). It should be noted in advance that reference is made in this chapter to investment funds and investment institutions in terms of the Investment Institutions Supervision Act [*Wet toezicht beleggingsinstellingen (Wtb)*].⁶

8.2 Description of the market

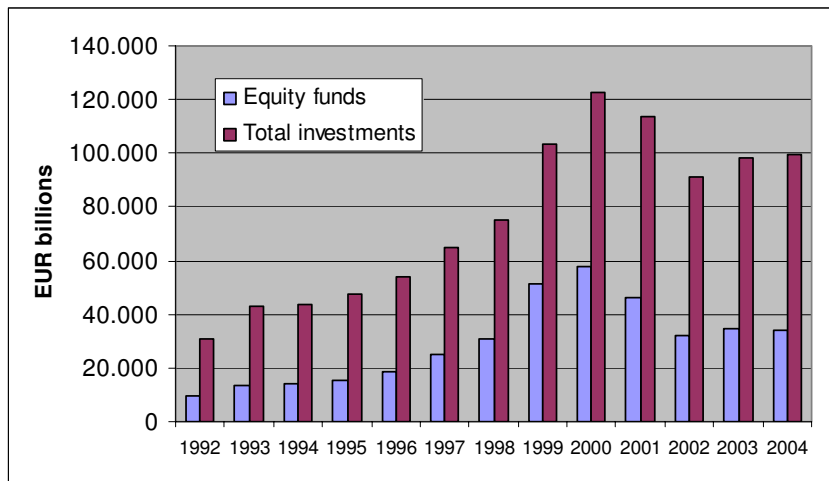
An investment fund consists of group investments, with the aim of enabling the participants in the fund to share the revenues from these investments. Investment funds provide for a need to invest capital and come in all shapes and sizes. In practice, a distinction is made between equity funds (with funds often focusing on specific regions or economic sectors), bond funds, real estate funds, money market funds and mixed funds. Alternative ways of investing money include direct investments in shares, bonds, real estate or savings deposits.

After this, market developments, concentration on the market, entry to the market, distribution, market innovation, consumer behaviour, and the regulations and supervision will be discussed.

Development of the market

Figure 8.1 gives an overview of the invested capital for the period 1992-2004.⁷ In mid-2005, the total invested capital of investment institutions based in the Netherlands amounted to EUR 103.5 billion according to the Dutch Central Bank (compared to EUR 99.7 billion at the end of 2004), of which 35% was invested in equity funds.

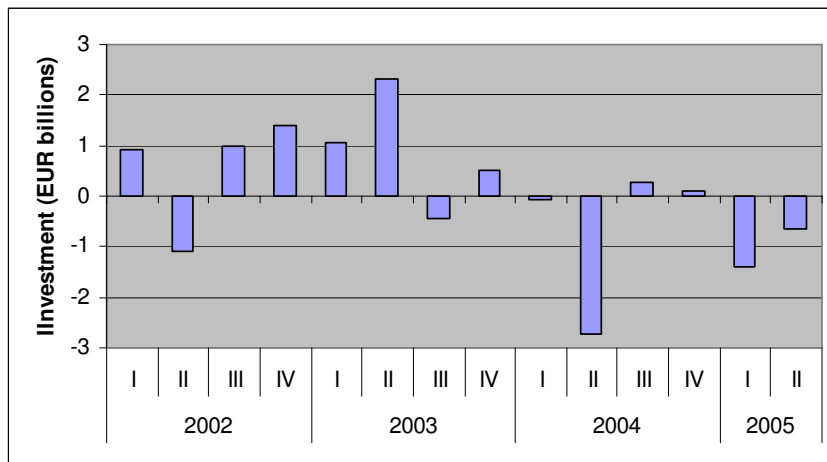
Figure 8.1 Invested capital in the Netherlands



Source: DNB statistics, Balance-sheet totals of investment institutions according to the type of fund

The fall in the level of total invested capital after 2000 was caused, on the one hand, by a decrease in the net investments and, on the other hand, by a fall in share prices. Figure 8.2 shows the development of net investment in detail from 2002 onwards. This investment fluctuates considerably. From the third quarter of 2003, a low level of investment (or even withdrawals) can be observed. The withdrawals in the second quarter of 2004 were caused to a significant degree by the relocation of various Dutch equity funds to Luxembourg.⁸ According to the Dutch Central Bank, an amount of EUR 1.4 billion was also withdrawn from investment funds based in the Netherlands in the first quarter of 2005. This fall occurred in all important categories of investment funds and occurred mainly amongst the larger funds. The net outflow can be attributed to the fact that institutional investors focus strongly on foreign bonds, while small investors mainly save via the Internet.⁹

Figure 8.1 Net investment in investment funds



Source: Press Release DNB, 24 May 2005.

Concentration

In total, at the end of 2004, there were 695 investment funds with registered offices in the Netherlands which had been issued with a licence by the Dutch Central Bank.¹⁰ This is 10 fewer than at the end of 2003. The previous years (1997-2003) showed an increasing number of investment funds each year.

In the 70s and at the beginning of the 80s, Robeco controlled the largest share of the Dutch market. In 1973, Robeco had a market share of 79% (see table 8.1). The HHI was well above 6,000.¹¹ After this, new parties entered the market and Robeco's market share shrank to approximately 36% in the year 2000. The arrival of in-house investment funds set up by various banks played an important role in this.¹² As a result, the HHI fell to a level below 2,000.

Table 8.1 Market shares of investment funds according to providers, 1973-2000

	1973	1982	1992	2000
Robeco Groep	79%	71%	45%	36%
ABN AMRO	13%	12%	24%	17%
ING Groep	0%	0%	6%	12%
Other providers	8%	17%	25%	35%
Total	100%	100%	100%	100%
Lower limit HHI	6,410	5,185	2,637	1,729

Source: B. Slot. *Iedereen een kapitalist: de ontwikkeling van het beleggingsfonds in Nederland gedurende de 20ste eeuw*, doctoral thesis, 2004. These figures exclude the investment funds of Dutch institutions in Luxembourg. The lower limits for the HHI values were calculated on the basis of these figures.

Nevertheless, even after 2000 Robeco was the largest provider of Dutch investment funds with a market share of 29% at year-end 2004, closely followed by ABN AMRO with a market share of 24.5% (see Table 8.2).

The HHI fluctuates from 2002 onwards around the level of 1,750. The Dutch market for investments therefore has a moderate level of concentration.¹³ The shifts in the market shares of providers of investment funds were relatively low in the period 2002-2004. Only Delta Lloyd and Fortis swapped fourth and fifth places. The top three did not change, resulting in a maximum shift in market shares of 2.7%. In the period from mid-2002 up to and including year-end 2004 market shares were fairly stable.

Table 8.2 Market shares of the large five investment funds, June 2002-December 2004 (as %)

	2002		2003		2004	
	June	December	June	December	June	December
Robeco	32.6	31.9	30.9	29.9	30.6	27.9
ABN AMRO	23.6	24.4	24.4	25.9	25.7	24.5
ING Groep	11.5	11.3	11.2	10.7	10.8	13.3
Fortis	6.6	6.5	6.3	7.6	6.2	8.6
Delta Lloyd	5.2	5.5	6	6.1	6.6	6.6
Lower limit HHI	1,823	1,813	1,751	1,774	1,795	1,673

Source: Morningstar (2003, 2004). The lower limits for the HHI values were calculated on the basis of these figures.

Entry

One of the few foreign undertakings which has managed to acquire a position in the Netherlands is Fidelity. Fidelity is one of the largest providers of investment funds worldwide. In the Netherlands, has built up its position over a period of 10 years. By year-end 2004, with a capital of EUR 1 billion, Fidelity had a market share of approximately 1% of the investment fund market in the Netherlands.¹⁴ Successful entry by foreign providers therefore does not seem to occur often.¹⁵ A number of factors play a role in this.

The first is brand recognition and track record. Consumers invest mainly in the funds of providers which they know and are often hesitant to invest in the financial products of foreign providers. This emerges, for instance, from research by the European Commission.¹⁶ It appears from research by KPMG that Dutch consumers are very cautious.¹⁷ In addition, results realised in the past are an important selection criteria for consumers.¹⁸ This makes it difficult to set up new funds which do not have a track record. For existing foreign funds the latter, of course, does not apply.

Secondly, it is important for successful entry to gain access to the distribution channel for investment funds. According to informal estimates, the banks serve approximately 80% of the market. The remaining distribution, approximately 20%, apparently occurs through insurance brokers, financial planners, mortgage providers, direct insurers and the Internet.¹⁹ Research from 2004 shows that 60% of respondents purchased shares in an investment fund through a bank. Approximately 20% had invested in an investment fund through an insurance broker.²⁰ A very large part of the shares in investment funds are therefore sold through the banks themselves.

A factor which possibly had an effect on the entry of foreign funds in the past was the fictive-yield scheme which applied up until 2001 to foreign funds. Under this scheme, the Tax Department assumed that a foreign fund had a certain annual rate of return.²¹ Shareholders were required to add this to their income. In the case of Dutch funds, shareholders of the fund were only taxed on the dividends distributed.²² This inequality was abolished as of 1 January 2001. Since then, in the case of both foreign and Dutch funds, private investors pay capital gains tax.²³

There is, however, an important factor which facilitates entry. In 2004, Postbank and Rabobank (although to a limited extent) started offering the investment funds of third parties (both Dutch and foreign parties). ABN AMRO had already started doing so in the summer of 2002. In June 2004, 47% of the inflow into investment funds through ABN AMRO went to the funds of other providers, such as Robeco and Fidelity. Two years later, this was only 8%.²⁴ In addition there are two investment fund 'supermarkets' which sell the funds of a large number of providers, namely SNS Fundcoach (approximately 30 providers of investment funds, more than 300 funds, part of SNS Bank) and Fundix (approximately 50 investment fund providers, more than 700 funds, part of ING Bank). They also offer the investment funds of foreign providers. An important driving force behind this, according to the interviewees, is the fact that consumers are becoming more assertive and demand the funds of other providers.

Finally, only to a limited extent do regulations appear to be an obstacle to entry onto the Dutch market by foreign providers. At the end of December 2003, Robeco had transferred a number of its investment funds to Luxembourg. Recently ABN AMRO also relocated 24 funds to Luxembourg.²⁵ The funds will be combined with similar existing funds in Luxembourg and will be actively marketed on the Dutch market. This involves a total invested capital of approximately EUR 4 billion.²⁶

Distribution channel

A distinction is made between active and passive distribution of investment funds. Active distribution is understood to be the inclusion of investment funds in one's own assortment, whereby the funds of third parties are also recommended to one's own customers. A distribution agreement is usually the basis for this form of distribution, in which the distributor is paid for its services by the respective provider. This is not the case with regard to passive distribution. Examples of passive distribution are *SNS Effectenlijn* (SNS Securities Line) or an *ING Bank Effectendepot* (ING Bank Securities Account), through which one may purchase the shares of listed stocks, or Fundix as an online provider.

If a provider/distributor actively offers the investment funds of a different provider, it receives a distribution fee for this. This may be a percentage of the management fee, whether or not with a threshold based on the invested capital, sometimes a scale based on the level of the investment, or a percentage of the invested capital. In general, the distribution fee is paid from the management fee which the respective provider receives from its customers. In addition to the management fee, in the case of most funds customers pay transaction costs on the purchase and sale of shares in the fund. It appears from research by Standard & Poor's that the costs which the providers of investment funds charge, as a percentage of the managed capital, may vary considerably, namely from 1.01% to 1.48%.²⁷

In 2004 ABN AMRO and Robeco decided to increase the management fees for investment funds. Increases of up to 30% were made and arose, according to those involved, from the increase in marketing and distribution costs due to the fact that banks offered the investment funds of competitors more often (for which the banks charge each other commission).²⁸ In addition, stricter rules imposed by regulators, accompanied by cost increases for banks, were also referred to as a cause. Possibly customers who invest are relatively insensitive to the level of the management fee, so that investment institutions are able to pass on any increases in costs through the management fee.

Where a large number of distributors only include the investment funds of other providers if they also include their investment funds (reciprocity), this may possibly have the effect of excluding smaller providers of investment funds and providers without their own distribution channel. It appears, however, from a survey by FSM amongst the 15 largest providers of investment funds in the Netherlands that reciprocity does not occur on a large scale.

It is the case, however, that active distribution occurs, in particular by smaller providers and to lesser extent by large providers. The investment funds of the top three providers are actively distributed by the other 13 providers questioned. On the other hand, the three largest providers—Robeco, ABN AMRO and ING—with a combined market share of 66% (year-end 2004) almost exclusively offer the investment funds of the top five providers.²⁹ An important part of the Dutch distribution network is therefore possibly inaccessible to smaller, less well-known and/or foreign providers of investment funds. Listed funds, however, can be purchased, for instance through Euronext, or shares in funds can be obtained through some other form of passive distribution. Given the considerable importance of sales through active distribution, effective competition with well-known providers without access to the distribution network of the large providers is difficult.

Product innovation

The so-called index funds are examples of relatively new products on the market. The development in the value of these funds is linked to an index, such as AEX. These funds are very popular in the United States, but demand seems to be limited in the Netherlands despite the lower management fees of such funds compared to actively managed investment funds.

Click funds are new products which are more successful. These are investment funds where the result is determined when the price level of the fund has reached a certain level. Recently funds which guarantee a minimum yield have gained in popularity. These products are, in fact, combinations of existing products and are responses to market developments accompanied by a change in the preferences of consumers.

In the financial sector, competitors may replicate innovative products without much difficulty. This possibly has the effect of slowing down innovation in this sector. In addition, in the case of investment funds it is important, in particular, to find distribution channels for innovative products and to convince them to promote these products actively. There have been reports that the market has therefore started focusing less on product innovation and more on aggressive fund management.³⁰

Consumer behaviour

Of all Dutch households, 23% invest directly in investment institutions.³¹ It appears from the research that management fees are a factor which explains the realised returns on investment funds.³² It appears from other research that these costs have a negative correlation to the expected future return.³³ Furthermore costs are a relatively certain factor, while the return on an investment fund is uncertain. In addition, funds with low management fees are easier for consumers to select than funds with a high return. This indicates that management fees ought to be a decisive factor for consumers in selecting an investment fund.

Consumers select investment funds, for instance, on the basis of recent prices.³⁴ In addition, private investors also consider costs as a criterion when deciding to purchase, whereby purchase costs play a greater role than management fees.³⁵ Consumers also appeared to attach considerable importance to reliability. For instance, 35% of investors indicated in the survey by the consumer association, Consumentenbond, that they have to have confidence in the fund manager before they invest their money in an investment fund.³⁶

Regulations and supervision

The supervision of investment institutions is governed by the Investment Institutions Supervision Act [*Wet toezicht beleggingsinstellingen (Wtb)*].³⁷ The Netherlands Authority for the Financial Markets [*Autoriteit Financiële Markten (AFM)*] is the institution which licences investment institutions, as referred to in the Act, and is responsible for behavioural supervision. The Dutch Central Bank is responsible for prudential supervision (financial guarantees). The investment institutions can now operate on the entire internal market of the European Union on the basis of a 'European passport'. However, this European passport only applies to institutions which invest in securities.

In April 2004 AFM published its report *Zicht op beleggingsinstellingen* [Overview of Investment Institutions].³⁸ It appears from the interview that there are shortcomings with regard to transparency and the care with which investment institutions operate. For instance, AFM has observed that the system of increases and reductions, and the settlement of these costs is not always properly stated in the prospectus. As a result, investors are given an incorrect and incomplete overview of these costs (and therefore also of the total costs) and possibly incur a loss.

Following this report, the Modernisation of Investment Institutions Commission [*Commissie Modernisering Beleggingsinstellingen*] was set up. This Commission presented a series of recommendations on 22 December 2004 including, for instance, the recommendation to limit the number of moments at which it is possible to trade with investment institutions to one moment each day, so that settlements with all investors can take place as close as possible to the net asset value (in other words, without the above-mentioned increases and reductions).³⁹ The Commission also advocated improvements in the governance of investment institutions by setting up a sufficiently independent supervisory board for each manager. This supervisory board would ensure that the interests of investors are promoted sufficiently by the manager. In addition to reforming the trading system and setting up a supervisory board for each manager, the Commission also advocated requiring investment institutions to account for all costs

associated with investment in the funds and strengthening the administrative organisation and internal controls.

On 1 September 2005, the amended Investment Institutions Supervision Act and the new Investment Institutions (Supervision) Decree [*Besluit toezicht beleggingsinstellingen*] came into force. Some of the recommendations made by the Commission were included. The most important amendments related to an improved scheme for protecting the capital invested by investors and an administrative simplification of the licensing procedure for investment institutions. A number of European directives were also implemented. The Investment Institutions Supervision Act will in time be integrated and harmonised with the Financial Supervision Act [*Wet op het financieel toezicht (Wft)*]. The other recommendations still have to be examined and/or require an amendment to legislation which will take place with its inclusion in the Behavioural Supervision part of the Financial Supervision Act.⁴⁰

The relocation of investment funds to Luxembourg has elicited a discussion in the Netherlands about the role which regulations play here. Following relocation by Robeco, ABN AMRO relocated a total of 24 Dutch investment funds to Luxembourg. The Secretary of State for Finance subsequently announced that the fiscal regime would be amended so that the tax burden on investment funds in the Netherlands would decrease and the obligatory stock exchange listing would be abolished.⁴¹ In future, investment funds will be able to opt for the same fiscal treatment as they receive in Luxembourg, the so-called 'deluxe variant' (without capital tax, corporation tax, and without an obligation to distribute a dividend and to withhold dividend tax).⁴²

8.3 Conclusions

The concentration of the market for investment funds is moderate and the market shares of the providers of investment funds are reasonably stable. The importance of active distribution, in particular by the large Dutch banks, is increasing and the concentration of this distribution channel is probably higher than that of the market for investment funds.⁴³ Developing distribution activities is more difficult and more expensive than 'producing' an investment fund. In addition, the market is characterised by a lack of transparency with regard to the level of the various cost components of investment funds and the searching and switching behaviour of consumers, based on purchase costs, historical performance (track record) and reliability. As a result, competition on management costs probably occurs only to a limited extent. These are factors which increase the risk to economic competition on the market.

Barriers to entry with regard to setting up funds, however, seem to be low and have, in any event, decreased, while the importance of Internet as a distribution channel has increased. The size of the market and the net investment depend on the development of share prices on the stock exchange and are volatile. In addition, developments have been initiated following the report presented by the Winter Commission with the aim of increasing transparency with regard to costs for consumers. Information brokers, such as morning Star and S&P, are increasingly making it possible to access and compare data on investment funds. These

factors point in the direction of a reduction in the risk to economic competition. All in all, the conclusion is therefore that the risk to economic competition on this market appears to be low.

Annex 1 Decision-making practice in relation to merger cases

The overview below lists Dutch and European cases in the area of merger control in the financial sector. This overview of decisions relates to merger cases in the period from 1 July 2004 to 1 September 2005. A large number of these cases were settled by NMa or the European Commission in a short-form decision with minimal justification. This is permitted if a number of conditions are met. For the conditions applicable in the Netherlands to short-form decisions, see 'Best Practices in relation to Competition Cases' [*Spelregels bij Concentratiezaken*], 15 July 2005, recital 54 *et seq.* Where a merger case was settled in a short-form decision, this is indicated by (SF).

A small number of merger cases in the banking sector in this period occurred at both the national and European levels. In the securities sector, no notifications were given of mergers, neither at the national nor at the European level. Most merger cases involved the insurance sector. At the national level this involved mainly health insurance.

All the cases below were approved either by NMa or the European Commission because the parties involved were not active on the same (relevant) markets or because there were no objections based on the market position of the parties.

Banking

Dutch cases

1. *Decision of the Director-General of NMa of 21 March 2005 in case 4759: ING Bank - NMB Heller*

As a result of a merger, the present joint control, which ING Bank and General Electric Capital Corporation exercise over certain Dutch working capital financing activities of NMB-Heller, will be changed into exclusive control by ING Bank.

European cases

2. *Decision of the European Commission of 15 September 2004 in case COMP/M. 3547: Banco Santander - Abbey National*

Banco Santander will take over Abbey National Bank in the United Kingdom. Banco Santander is the market leader on the Spanish financial services market and is not yet active on the UK market.

3. *Decision of the European Commission of 19 November 2004 in case COMP/M. 3574: Rabobank - BGZ*

Rabobank and the State Treasury of the Republic of Poland, a banking institution controlled by the Polish government, will jointly take over the Polish commercial bank BGZ. Rabobank is active in the Netherlands on the entire market for financial services and is not yet active in Poland. BGZ specialises in financing the agricultural and food sectors. The State Treasury is specialised in financing the agricultural sector and food sector. The State Treasury of the Republic of Poland owns six other Polish banks. (SF)

4. *Decision of the European Commission of 7 January 2005 in case COMP/M.3659:
Dresdner Bank - Cetelem*

Dresdner Bank is active on the entire German financial services market, both on the business and retail markets. Cetelem S.A., which is active in the area of consumer credit in France, will acquire control of Cetelem Bank GmbH, established in Germany, together with Dresdner Bank. As in the case of Dresdner Bank, Cetelem Bank GmbH is active on the consumer credit market. (SF)

5. *Decision of the European Commission of 19 January 2005 in case COMP/M. 3556:
Fortis - BCP*

Fortis Insurance International N.V., part of Fortis International N.V., will acquire 51% of the insurance activities of BCP (established in Portugal). Fortis is not yet active on the insurance market in Portugal.

6. *Decision of the European Commission of 14 February 2005 in case COMP/M.3677:
Danske Bank - National Europe Holding - Northern Bank Insurance Services*

Danske Bank from Denmark will acquire both National Europe Holding and Northern Bank Insurance Services. Both undertakings are from Ireland. Danske Bank and National Europe Holding are active in the area of financial services. The Northern Bank Insurance Services is active in the area of investment management and life insurance. (SF)

7. *Decision of the European Commission of 15 April 2005 in case COMP/M. 3706:
ÖVAG - Investkredit*

ÖVAG will acquire Investkredit by means of a public offer. Both undertakings are active in the financial services market in Austria. (SF)

8. *Decision of the European Commission of 27 April 2005 in case COMP/M.3780: ABN
AMRO - Antonveneta*

ABN AMRO will acquire Antonveneta by means of a public offer. As in the case of Antonveneta, ABN AMRO is active in the area of financial services. Antonveneta is active mainly in Italy, where ABN AMRO is only active to a limited degree. (SF)

9. *Decision of the European Commission of 27 April 2005 in case COMP/M.3768:
BBVA - BNL*

BBVA will acquire BNL by means of a public offer. Both BBVA and BNL are active in the area of financial services. BBVA is mainly active on the Spanish and Latin American markets, while BNL is active on the Italian market.

10. *Decision of the European Commission of 2 June 2005 in case COMP/M.3740:
Barclays Bank - Föreningssparbanken - JV*

On 2 June 2005, the Commission decided that it would not raise objections to the merger of Barclays Bank from the United Kingdom and Föreningssparbanken from Sweden in the area of credit cards. A joint venture will be set up to issue credit cards.

*11. Decision of the European Commission of 14 June 2005 in case COMP/M. 3781:
Crédit Agricole - Caisse d'Épargne*

Caisses D'Épargne and Crédit Agricole will set up a joint-venture to secure banking instruments and management funds for institutional investors. Both undertakings operate on the entire financial services market.

*12. Decision of the European Commission of 4 August 2005 in case COMP/M.3799:
Dexia - Kommunal Kredit - JV*

Dexia, established in France, and Kommunal Kredit, established in Austria, will jointly acquire control of Kommunal Kredit in the Czech Republic and Dexia in Austria. Kommunal Kredit in the Czech Republic was owned solely by Kommunal Kredit in Austria prior to the merger. Dexia Austria was owned solely by Dexia France prior to the merger. All the undertakings are active on the financial services market with a focus on public finance. (SF)

Insurance

Dutch cases

1. Decision of the Director-General of NMa of 5 November 2004 in case 4243: Achmea - AXA

This relates to the acquisition of the entire private health insurance portfolio of AXA by Achmea.

*2. Decision of the Director-General of NMa of 29 November 2004 in case 4283:
Zwitserleven - Goudse Levensverzekeringen*

Zwitserleven will acquire control over the group pension insurance portfolio of Goudse Levensverzekeringen N.V. Both undertakings provide life insurance. (SF)

3. Decision of the Director-General of NMa of 16 December 2004 in case 4351: Fortis - Fundum

Fortis ASR Verzekeringsgroep N.V. will acquire Fundum. Both parties provide income insurance.

4. Decision of the Director-General of NMa of 24 January 2005 in case 4667: Achmea - OZF - OZB

Achmea will acquire control of OZF and OZB. OZF offers both private health insurance and supplementary insurance for people insured by health insurance funds. OZB is active in the area of providing insurance through a health insurance fund. Achmea also provides health insurance, for private individuals and persons insured by health insurance funds. OZF will add less than 1.5% to Achmea's market share. OZB is hardly active at all in Achmea core operating area.

5. Decision of the Board of Directors of NMa of 7 July 2005 in case 5052: CZ - OZ

Stichting CZ groep Zorgverzekeringen Beheer intends to acquire O.W.M. aanvullingsfonds OZ zorgverzekeringen. Since the new Health Insurance Act will come into force in January 2006 and the distinction between private insurance and insurance by a health insurance fund will cease, the present position of the parties on the health insurance market is considered in

assessing the consequences of the merger. It appears from NMa's investigation that there is evidence that merges, which result in strong regional market positions, may be an obstacle to the emergence of competition at the national level. The Board of Directors of NMa therefore decided that a licence was required for this merger.

6. *Decision of the Board of Directors of NMa of 26 July 2005 in case 5112: SNS REAAL - NHL*

SNS REAAL Groep N.V. acquires Nieuw Hollands Lloyd Verzekeringsgroep N.V. (SF)

7. *Decision of the Board of Directors of NMa of 22 August 2005 in case 5074: Achmea - Rabobank*

The activities of Interpolis and the insurer Achmea were merged into a joint-venture of Achmea and Rabobank. In addition, Rabobank will acquire control of Eureko, a subsidiary of Vereniging Achmea (Achmea Association), which owns 100% of the share capital of Achmea Holding. NMa has no reason to assume that competition on the market for banking services (savings, credit and mortgages), insurance (non-life and life), pension administration services and health, safety and welfare and reintegration services will be obstructed by this merger.

European cases

8. *Decision of the European Commission of 20 August 2004 in case COMP/M. 3528: SWISS RE- LAHC*

SWISS RE will acquire LAHC. SWISS RE is active on the market for long-term insurance and on the reinsurance market. LAHC is only active on the long-term insurance market. (SF)

9. *Decision of the European Commission of 1 September 2004 in case COMP/M. 3501: SEB Trygg Liv - Codan Pension*

SEB Trygg will acquire shares in Codan Pension. SEBB is a provider of life and pension insurance in Sweden, Estonia and Lithuania. Codan Pension is also active on this market, mainly in Denmark. (SF)

10. *Decision of the European Commission of 15 October 2004 in case COMP/M. 3565: Talanx - Neue Leben*

Talanx will acquire Neue Leben. Talanx operates on the market for non-life and life insurance, and investment management. Neue Leben only sells insurance. (SF)

11. *Decision of the European Commission of 30 November 2004 in case COMP/M. 3610: Friends Provident - Lombard - IDH*

Friends Provident will acquire Lombard and IDH. Friends Provident specialises in life insurance and pensions. Lombard is only active in the area of life insurance. IDH focuses on marketing. (SF)

12. *Decision of the European Commission of 22 December 2004 in case COMP/M. 3620: CODAN ET AL - NAI JV*

Codan and Converium will set up a joint-venture which will operate in the area of aviation insurance. Codan is a general insurance company and Converium is an insurance company active in the area of reinsurance. (SF)

*13. Decision of the European Commission of 3 May 2005 in case COMP/M. 3772: AVIVA
- RAC*

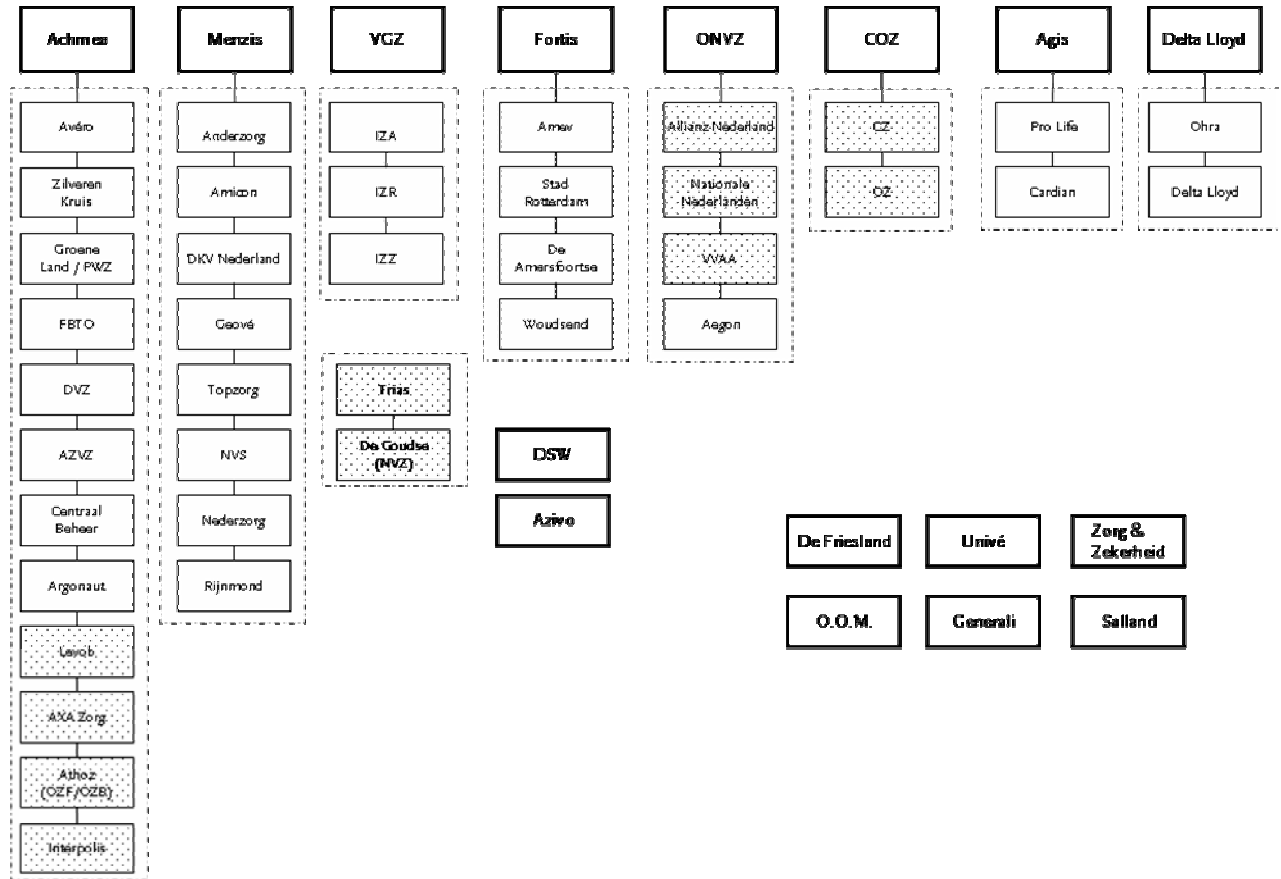
The UK company Aviva, active on the global market for life insurance and non-life-insurance, will acquire control of RAC, the British automobile association. They will also offer non-life-insurance. In the area of non-life insurance, the joint market share of the parties is less than 15%.

*14. Decision of the European Commission of 5 September 2005 in case COMP/M. 3887:
Clerical Medical - MLP- Life Insurance*

Clerical Medical is a subsidiary of the HBOS Group from the United Kingdom. Clerical Medical will acquire MLP- Life Insurance. HBOS is an international bank which is partly active in the area of life-insurance. MLP-Life Insurance is it only active in the area of life-insurance. (SF)

Annex 2 Labels and operating companies in the healthcare sector

Recent mergers are shaded.



Annex 3 Healthcare agency regions

The conclusion that a regional definition of the market may predominate in certain regions makes it important to determine which regions this involves. As can be derived from the body of this report, this involves regions with a concentrated structure on the health insurance market and, above all, with relatively concentrated healthcare provision. To assess the concentration of healthcare provision, data was obtained from the National Institute of Public Health and the Environment [Rijksinstituut voor Volksgezondheid en Milieu].

1. Noord-Nederland

The boundaries of the northern healthcare agency regions coincide with the provincial boundaries. The concentration indices obtained are high. In the north of the Netherlands healthcare provision is also relatively concentrated.

Table 1 Concentration indices per healthcare agency region in the northern provinces of the Netherlands

Healthcare agency region	Largest player	Indicator		
		C3	C4	HHI
Groningen	Menzis	84%	89%	4,355
Friesland	De Friesland	80%	86%	3,768
Drenthe	Achmea	80%	88%	3,731

Source: Vektis and FSM's own calculations.

2. Overijssel and Gelderland

The provinces of Overijssel and Gelderland comprise numerous healthcare agency regions. The regions of Zwolle and Midden-IJssel mainly comprise the Overijssel municipalities, but also (some of) the Gelderland municipalities. Most policyholders in the Nijmegen region reside in municipalities in Gelderland, but a number of municipalities in the province of Brabant are also included in this region.

The levels of concentration in the various Overijssel regions are high. As in the northern provinces, healthcare provision in Overijssel is relatively concentrated. The values for the concentration indices for the Gelderland regions is generally at a lower level than those in the province of Overijssel although they are not below 2,000 points in any single instance. Healthcare provision in Gelderland, in comparison with the areas in the province of Overijssel, is also less concentrated.

Table 2 Concentration indices voor healthcare agency region in Overijssel and Gelderland

Healthcare agency region	Largest player	Indicator		
		C3	C4	HHI
Zwolle	Achmea	78%	85%	3,635
Twente	Menzis	83%	87%	4,433
Midden-IJssel	Salland	73%	82%	2,407
Apeldoorn-Zutphen and surrounding	Agis	68%	76%	2,253

areas				
Arnhem	Menzis	70%	79%	2,735
Nijmegen	VGZ	77%	84%	2,227

Source: Vektis and FSM's own calculations.

3. Flevoland and Utrecht

The boundaries of the healthcare agency regions of Flevoland and Utrecht largely coincide with the provincial boundaries. Flevoland is exceptional to the extent that a distinction is sometimes made between the municipality of Almere and the rest of Flevoland. In Almere, Agis fulfils the healthcare agency function and in the rest of Flevoland Achmea does so. The healthcare agency region of Utrecht also includes the Gelderland municipality of Nijkerk, in addition to the municipalities in the province of Utrecht. The values of the concentration indices found are at a level comparable to the values found in Gelderland. Healthcare provision in Flevoland is relatively concentrated, while this is less so in Utrecht.

Table 3 Concentration indices for healthcare agency regions in Flevoland and Utrecht

Healthcare agency region	Largest player	Indicator		
		C3	C4	HHI
Flevoland	Achmea	75%	80%	2,445
Utrecht	Agis	66%	74%	2,124

Source: Vektis and FSM's own calculations.

4. Noord-Holland

The province of Noord-Holland has six healthcare agency regions. Relatively high values for the concentration indicators were found in the various regions, but there is also a region with an HHI value below 2,000. With regard to the provision of hospital care, there appears to be a clear difference between the region of Noord-Holland-Noord (relatively concentrated), on the one hand, and the rest of the province of Noord-Holland (relatively less concentrated), on the other hand.

Table 4 Concentration indices for healthcare agency regions in the province of Noord-Holland

Healthcare agency region	Largest player	Indicator		
		C3	C4	HHI
't Gooi	Agis	70%	77%	2,521
Noord-Holland-Noord	Univé	79%	83%	4,020
Kennemerland	Achmea	74%	79%	3,473
Zaanstreek-Waterland	Achmea	74%	80%	3,604
Amsterdam	Agis	81%	86%	4,203
Amstelland and Meerlanden	Z&Z	63%	71%	1,953

Source: Vektis and FSM's own calculations.

5. Zuid-Holland

The province of Zuid-Holland has no less than eight healthcare agency regions, of which several are relatively small with regard to their geographical size and the number of insured. The province has several regions with relatively high values for the concentration indices, but there are no regions with an HHI value above 4,000, as in the case of the province of Noord-

Holland and several other regions. In the province of Zuid-Holland, healthcare provision, relatively speaking is not exceptionally concentrated, with the exception of regions such as Zuid-Hollandse Eilanden and to a lesser extent Waardenland and Midden-Holland.

Table 5 Concentration indices for healthcare agency regions in the province of Zuid-Holland

Healthcare agency region	Largest player	Indicator		
		C3	C4	HHI
Zuid-Holland-Noord	Z&Z	74%	80%	2,756
Haaglanden	DL-OHRA	70%	79%	2,083
Delft Westland Oostland	DSW	61%	72%	1,754
Nieuwe Waterweg-Noord	DSW	78%	82%	3,328
Rotterdam	Achmea	77%	81%	3,641
Midden-Holland	VGZ	68%	75%	2,507
Zuid-Hollandse eilanden	OZ	72%	81%	2,489
Waardenland	VGZ	72%	79%	2,958

Source: Vektis and FSM's own calculations.

6. Zuid-Nederland

The healthcare agency in the Zeeland region coincides with the province of Zeeland. The province of Noord-Brabant has four healthcare agency regions, while Limburg has two. In all three provinces, regions are found with high values for the concentration indices. A further striking feature is the fact that in a connected area in the southeast of the Netherlands, with the exception of the region of West-Brabant, but including the healthcare agency region of Nijmegen, CZ and VGZ are still the largest players. The provision of care is relatively concentrated in the provinces of Zeeland and Limburg (in particular, in the regions of Noord-Limburg and Midden-Limburg), and in the region of West-Brabant. In the other areas of the province of Noord-Brabant, healthcare provision is less concentrated compared to the other southern regions.

Table 6 Concentration indices for healthcare agency regions in the south of the Netherlands

Healthcare agency region	Largest player	Indicator		
		C3	C4	HHI
Zeeland	CZ	80%	88%	2,931
West-Brabant	OZ	80%	86%	2,630
Midden-Brabant	VGZ	86%	90%	3,506
Noord-Oost Brabant	VGZ	86%	89%	3,457
Zuid-Oost Brabant	CZ	89%	92%	3,648
Noord- en Midden Limburg	VGZ	90%	92%	3,793
Zuid-Limburg	CZ	91%	94%	4,058

Source: Vektis and FSM's own calculations.

Notes

Chapter 1

¹ NMa, *Financial Sector Monitor 2003*, December 2003; NMa, *Financial Sector Monitor 2004*, December 2004.

² 'iDeal webwinkelen', *Het Financieele Dagblad*, 21 June 2005.

³ 'Rabobank verkoopt Interpolis aan Achmea', *Het Financieele Dagblad*, 28 April 2005.

⁴ 'NMa: Groen licht voor joint venture Achmea en Rabobank', *NMa*, 22 August 2005.

⁵ 'Fusies: Commissie keurt overname van BNL door BBVA en overname van Banca Antonveneta door ABN AMRO goed', *European Commission*, 28 April 2005.

⁶ *Ibidem*.

⁷ 'ABN AMRO wil Antonveneta overnemen', *De Volkskrant*, 9 March 2005.

⁸ 'Rivaal ABN overstag in Italiaanse bankenstrijd', *Het Financieele Dagblad*, 16 September 2005; 'ABN hanteerd in Italië prijswapen', *Het Financieele Dagblad*, 1 November 2005.

⁹ Before 17 May 2005, Currence used the working name Brands & Licences Betalingsverkeer Nederland.

¹⁰ The brands PIN and Chipknip were previously the property of Interpay.

¹¹ The providers of payment products will be active on the end-user market and will therefore fulfil the role of issuing and/or acquiring banks.

¹² 'Doorbraak in onderhandelingen tussen banken, winkeliers en horeca', *NVB*, 8 June 2005.

¹³ 'Uitkomsten adviesmatch', letter from the Ministry of Finance to the Lower House of the Dutch Parliament with reference FM 2005-01734; ECORYS-NEI, *Marktwerking op de markt voor hypothecaire kredietverlening*, Report commissioned by the Ministry of Finance, May 2004.

¹⁴ 'Fondsensector ziet tij keren', *Het Financieele Dagblad*, 15 June 2005.

¹⁵ 'Kapitaalbelasting verdwijnt', *Ministry of Finance*, 24 March 2005.

¹⁶ Competition Commission, *Deutsche Börse AG, Euronext NV and London Stock Exchange Plc: A Report on the Proposed Acquisition of London Stock Exchange Plc by Deutsche Börse AG or Euronext NV*, November 2005.

¹⁷ 'Euronext moet bittere pil slikken', *Het Financieele Dagblad*, 2 November 2005.

Chapter 2

¹ See NMa, *Financial Sector Monitor 2004*, December 2004, pp. 19-30. This research started following a market-wide scan of the insurance sector in 2003, see NMa, *Financial Sector Monitor 2003*, December 2003, pp. 40-41. The concept of a 'market' is not used here in the way it is used in competition law. This is therefore not a definition of the relevant market in accordance with competition law.

² NMa and CPB, *Competition in the Market for Life Insurance*, 22 September 2005.

³ NMa, *Consultatiedocument Het intermediaire distributiekanaal*, November 2004. The consultation on this document closed on 1 February 2005 and in April 2005 an anonymised overview of the responses from the sector was published on NMa's website.

⁴ For this purpose, the answers to the open questions were categorised by NMa. Given the large number of active insurance brokers in proportion to the number of responses to the consultation document, this possibly does not reflect the views of the sector as a whole.

⁵ However, not all respondents agree with this analysis by NMa.

⁶ For more information, see <http://www.uvt.nl/centerdata/nl/>.

⁷ Respondents can indicate the extent to which they agree with this statement on a scale from 1 to 7, where 1 means 'disagree entirely' and 7 'agree entirely'.

⁸ Respondents can choose (1) no expertise, (2) some expertise, (3) knowledgeable, and (4) very knowledgeable.

⁹ The results in this chapter can be found in more detail in the research report published by NMa and CPB, *Competition in the Market for Life Insurance*, 22 September 2005.

¹⁰ When all the lump-sum policies are taken into account, the results remain qualitatively the same. The same applies when not the first but the second lump-sum policy is considered for all respondents with more than one policy. This indicates that the results are robust.

¹¹ The natural logarithm of income was chosen because we expected the effects of additional income to be lower as income increases. If age or the natural logarithm of income squared is used, these coefficients appeared to be statistically insignificant. There are two levels of education, high and low. High means that the level of education of the respondent is a university of professional education or a traditional research-based university.

¹² The year dummy is added to take into account the progression of average preferences over time. On the basis of specification tests, a single dummy was selected for the period 1995-2001. The demonstrated expertise is relevant because someone who actually understands financial products will choose a product which suits his or her risk aversion. The term is included as a crossed term because no direct effect of the demonstrated expertise is expected. Demonstrated expertise is high when a number of questions are answered correctly.

¹³ This may indicate a distortion due to selection effects. Such effects occur '(...) if the probability of a particular observation to be included in the sample depends upon the phenomenon we are explaining.' (Marno Verbeek, *A Guide to Modern Econometrics*, Wiley & Sons, 2004.) Selection effects may occur, for instance, when consumers who purchase a unit-linked lump-sum policy, due to non-observed characteristics, do so with greater probability through an insurance broker than people who purchased a guaranteed lump-sum policy. To establish whether selection effects occurred, a switching regression choice model was estimated. The result shows that there are no selection effects.

¹⁴ The payout depends on factors such as age, life to maturity and sex. The ranking of payouts for a specific combination of factors is referred to as a table. The ranking is done for a number of standard values. This results in numerous tables. One particular table is associated with a particular consumer (for instance, a woman, 40 years old, who purchases a lump-sum policy with a life to maturity of 10 years). Her choice will be found in this table. The place in the table gives an indication of how good the consumer's choice was. A measure of this is the yield relative to the average yield. When the correct table is not available, the 'nearest' table is chosen. The results are robust for various definitions of 'closest'.

¹⁵ Due to heteroscedasticity in the errors, a model was estimated using 'feasible generalized least squares'. The adjusted R^2 of the model is 0.1122 and the number of observations is 167.

¹⁶ Since the product analyses have the same invested capital, this is equivalent to ranking on the basis of realised return.

¹⁷ This is operationalised as taking first the nearest year, then sex, then age and then premium. To check the robustness of the analysis, various orderings were used. The results are robust under these changes. Two alternative models were also estimated. In one model, the payout

indices were estimated parametrically on the basis of the available policies. In the other model, only the first policy was used for each respondent and respondents whose purchase date differed by two years from the nearest table were not included. In both cases, the results remain unchanged. The ascertained effect of the use of an insurance broker becomes even stronger.

¹⁸ The research shows what the causes are of suboptimal advice by insurance brokers. The research neither proves, nor falsifies the hypothesis that advice is commission-driven. To determine whether commission is the driving force behind advice given by insurance brokers, further research would be necessary, possibly on the basis of 'mystery shopping' or an econometric study, where the level of commission which insurance brokers receive per product is also known. Under the Financial Services Act such a study could be carried out by the Netherlands Authority for the Financial Markets.

¹⁹ See also the research by Ecorys-NEI, *Marktwerking op de markt voor hypothecairehypothecaire kredietverlening*, 26 May 2004. It appears from this research that the markets for mortgages and mortgage advice have characteristics which could result in suboptimal price competition as a result of switching costs, a lack of transparency about the price and quality of products and possibly commission-driven sales. See also Proceedings of the Lower House of the Dutch Parliament, Session 2003–2004, 29 629, No. 1.

²⁰ The upfront fee is set at a maximum of 50% of the commission income. There is a gradual shift in the ratio between the upfront fee and recurring commission to 80/20 as of 1-1-2007, 70/30 as of 1-1-2008, 60/40 as of 1-1-2009 and 50/50 as of 31-12-2009. There is no maximum for the total commission.

²¹ The exact details of this were not known at the time of writing.

Chapter 3

¹ De Nederlandsche Bank, *Aanbevelingen van de Nederlandsche Bank inzake tariefstructuren en infrastructuur in het Nederlandse betalingsverkeer*, 28 March 2002.

² 'Keuzemogelijkheid voor het afsluiten van overeenkomst PIN en/of Chipknip', Interpay, 22 December 2003.

³ 'Interpay stopt verwerking pintransacties', *Novum*, 1 September 2005.

⁴ NMa, *Effecten van overdracht pincontracten, eindrapport*, February 2005.

⁵ The concept of a 'market' is not used here in the way it is used in competition law. This is therefore not a definition of the relevant market in accordance with competition law.

⁶ Of a total of 1.2 billion PIN transactions in 2004, on 1 December 2004 an estimated 550 million transactions had not yet been transferred to the banks.

⁷ The average tariffs presented are tariffs per transaction. In this regard, it is possible to take into account various components and different types of contracts (such as free-rate contracts and contracts with subscription fees).

⁸ The Interpay Beatel tariff in 2003 was 8.6 eurocents per transaction excluding the national discount and 7.31 eurocents per transaction including the National discount.

Chapter 4

¹ NMa, *Financial Sector Monitor 2003*, December 2003, p. 14.

² NMa, *Financial Sector Monitor 2003*, December 2003, p. 13. The concept of a ‘market’ is not used here in the way it is used in competition law. This is therefore not a definition of the relevant market in accordance with competition law.

³ All banking institutions which have obtained access to the Dutch banking market by means of a licence or notification are included in this, as well as all withdrawals of licences and notifications.

⁴ The Register pursuant to the Credit System (Supervision) Act distinguishes between commercial banks, central credit institutions, credit institutions affiliated to a central credit institution, securities credit institutions, savings banks, mortgage banks and electronic money institutions. These institutions may be based either in the Netherlands (a Dutch legal entity), or in the EU, or outside the EU. Finally, the institution may have a branch office (section 1(i) of the Credit System (Supervision) Act. Electronic money institutions are not taken into account in this document. In the categories of mortgage banks and central credit institutions, no changes occurred in the Register in the period from January 2000 to May 2005.

⁵ Undertakings active in the Netherlands have to be registered with the Trade Register kept by the Chamber of Commerce. See section 3(1) of the Trade Register Act [*Handelsregisterwet*].

⁶ Rabobank is the only credit institution in the Netherlands with such a structure.

⁷ This relates partly to new undertakings and partly to existing undertakings which have obtained permission to enter the market.

Chapter 5

¹ See the website created by the Ministry of Public Health, Welfare and Sport:

www.denieuwezorgverzekering.nl.

² Explanatory Memorandum to the Health Insurance Act, Lower House of the Dutch Parliament, Session 2003-2004, 29 763, No. 3, p. 2.

³ Explanatory Memorandum to the Health Insurance Act, p. 26.

⁴ H.A. Keuzekamp, ‘Marktwerking in de zorg’, *ESB*, 30 June 2005, Vol. 90, No. 4464, pp. 21-23. See also de Explanatory Memorandum to the Health Insurance Act, p. 26 and the decision of NMa of 7 July 2005 in case 5052/CZ – OZ, recitals 56 up to and including 60.

⁵ The concept of a ‘market’ is not used here in the way it is used in competition law. This is therefore not a definition of the relevant market in accordance with competition law.

⁶ See section 2 of the Health Insurance Act. In the present situation, only employees, recipients of benefits and entrepreneurs with an income below the health insurance fund ceiling have to be insured in accordance with the former Health Insurance Act [*Ziekenfondswet*].

⁷ See section 29 of the Health Insurance Act.

⁸ The Health Insurance Act prohibits health insurers from charging different premiums for the same healthcare package on the grounds of age, sex, health risk or any other factors relating to (potential) policyholders. Everyone pays the same insurer the same nominal premium for a certain standard agreement. Risk selection, the selection of insured on the basis of possible risk factors, is not permitted under the Health Insurance Act. Insurers may not refuse applicants, for instance on the grounds of age, sex or the risk of illness.

⁹ In addition to the nominal premium, every person who is obliged to take out insurance has to pay an income-related contribution. This contribution, which is levied by the Tax Department, amounts on average to half of the total premium.

¹⁰ In (partial) compensation for this premium, the income-related health supplement is paid to a considerable part of the population.

¹¹ Risk settlement means that insurers with relatively many risks will be financially compensated. Resettlement reduces the incentive for insurers to apply risk selection, in other words to turn away less attractive insured. Where the benefits to the insurer of risk selection are small, the insurer will focus mainly on contracting efficient healthcare.

¹² See the Explanatory Memorandum to the Health Insurance Act, p. 31: “[the insurer] does not have to reimburse higher costs than a rate which, within reason, is consistent with usual market conditions in the Netherlands. ”

¹³ See section 11 Health Insurance Act.

¹⁴ Under the present system, it is difficult for many insured to switch insurers if they wished to retain their supplementary insurance, due to the possibility that the insurer, when underwriting the supplementary policy, will apply selection criteria. Since 80% to 90% of people insured with health insurance funds have supplementary insurance, this is a substantial barrier to switching.

¹⁵ This is a dataset obtained from Vektis. With regard to those who are privately insured, Vektis did not provide 100% of all insured, but approximately 90%. The difference relative to the total number of insured may also be attributed to residents of the Netherlands who are not insured, or to the loss of a number of insured for processing reasons in a statistical sense.

¹⁶ See for the development in the period 1994-1999 the 'Healthcare Atlas' (*zorgatlas*) produced by RIVM; see www.rivm.nl.

¹⁷ Vektis, *Zorgthermometer*, April 2005. A group may also comprise one provider of private health insurance. Groups may also market various brands.

¹⁸ The Dutch Central Bank regulates such activities to ensure that they are consistent with the framework for non-life insurance activities.

¹⁹ This value is equal to the sum of the individual market shares of all undertakings on the market squared. See the 'Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings', *OJEC C 31* of 5 February 2004, recitals 19 and 20. In these guidelines it is considered improbable that the Commission will conclude that there are competition concerns if the HHI after the merger is (i) less than 1,000, (ii) between 1,000 and 2,000 and the change in the HHI is less than 250, and (iii) greater than 2000 and the change is less than 150. In the United States, a threshold of 1,800 points is assumed.

²⁰ See the Explanatory Memorandum to the Health Insurance Act, p. 27.

²¹ The term 'healthcare agency region' (*zorgkantoorregio*) refers to the implementation of the Exceptional Medical Expenses Act (*AWBZ*). Since 1998, the implementation of this act has been the responsibility of the healthcare agencies. These agencies were set up jointly by the health insurers. Healthcare agencies, which are closely affiliated to the largest health insurer in the region, work independently and attempt to match the demand for and supply of healthcare in a specific region as far as possible. Although the healthcare agency region and the area of operation correspond fairly closely, not all healthcare agency regions correspond exactly with the former core areas of operation of health insurance funds.

²² In a number of cases, the healthcare agency regions and provinces coincide exactly. In a number of other cases, provinces consist of (parts of) numerous healthcare agency regions. For further information see Annex 3.

²³ See the ‘Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings’, *OJEC* C 31 of 5 February 2004.

²⁴ With regard to the relevant geographical market(s) for the procurement of healthcare, NMa has concluded that it is necessary to consider how great the distance is that consumers/patients are willing or are expected to travel for a visit to the respective healthcare provider. This distance depends, for instance, on the type of healthcare and the average frequency of visits. In the case of hospital care, see the decisions of the Director-General of NMa of 8 June 2005 in case 3897/Ziekenhuis Hilversum – Ziekenhuis Gooi-Noord, of 8 June 2005 in case 5047/Erasmus MC – Havenziekenhuis and of 11 April 2001 in case 537/Landelijke Huisartsen Vereniging.

²⁵ In this regard, it should be noted that the entry of a regional insurer into a different region is possibly easier if this insurer has a strong position in an adjacent area. For such an insurer, after all, it is easier to have policyholders purchase healthcare across the regional borders than for an insurer, most of whose insured live in areas which are at a greater distance.

²⁶ The mechanism works, in particular, in relation to insurance-in-kind policies because in the case of this type of policy, in particular, healthcare is purchased in advance. If restitution policies become the predominant type of policy, the emergence of this mechanism is less plausible because it is less usual in the case of this type of insurance to procure healthcare.

²⁷ In addition to procurement advantages, which insurers can obtain in the case of (insurance in-kind) policies, they can also obtain advantages by steering the insured towards preferred providers they can also obtain advantages. It is plausible that steering insured will play a greater role in relation to insurance-in-kind policies than in relation to restitution policies.

²⁸ CTG/ZAio, *Oriënterende Monitor Ziekenhuiszorg*, 12 September 2005, p. 56.

²⁹ CTG/ZAio, *Oriënterende Monitor Ziekenhuiszorg*, 12 September 2005, p. 56.

³⁰ See the decision of NMa of 7 July 2005 in case 5052/CZ – OZ, recitals 108 and 115.

³¹ See for instance *Richt snoeren voor de zorgsector*, recitals 152-163 and the case 652/VGZ-OZ-CZ (combined with case 145).

³² See section 29(1) of the Health Insurance Act.

³³ See CTG/ZAio en CTZ, *Consultatiedocument Monitor Verzekeringmarkt*, July 2005, p. 19.

³⁴ In this way, NMa attached conditions to the acquisition of OZ by CZ. The stipulated conditions ensure that a position of power does not arise which is such that it limits the opportunity which other healthcare insurers have to offer a competitive policy to persons insured in the provinces of Zeeland and Noord-Brabant. See the decision of NMa of 28 October 2005 in case 5052/CZ-OZ.

³⁵ Of course, the insured can base their choices on the relative price/quality ratio rather than on price. It emerged from the research for this chapter and from publications that it is difficult for the insured to obtain insight into the quality of healthcare provision. As a result, it is unlikely that they will attribute much weight to this factor. They may take into account the quality of service of their healthcare insurer. Since this factor is not decisive in determining whether the development will be regional or national, it is not discussed further here.

³⁶ In addition, both insurers and healthcare providers state that insurance-in-kind policies incur lower administrative costs.

³⁷ After all, premium differentiation is permitted with regard to the supplementary insurance.

³⁸ It appears from the premiums announced by insurers in mid-November 2005 that the insurance-in-kind policy is cheaper than a restitution policy purchased from the same insurer.

³⁹ Vektis, *Onderzoek naar verzekerdennobiliteit en oorzaken daarvan door Vektis*, June 2005.

⁴⁰ See the Amendment Memorandum in relation to the Health Insurance (Implementation and Amendment) Act, section 2.5.1.

⁴¹ Vektis, *Onderzoek naar verzekerdennobiliteit en oorzaken daarvan door Vektis*, June 2005.

At present, those insured by health insurance funds may switch health insurance funds once a year between 1 January and 28 February of the respective calendar year.

⁴² iBMG, *Monitor verzekerdennobiliteit*, April 2005.

⁴³ A similar picture emerges from the research by NIVEL in which in 2005 3.7% of those insured with health insurance funds in the representative panel switched health insurance funds. In 2001 this was 3.1%. See NIVEL, *Wisselen van ziekenfonds per 1-1-2003*, 2003, and NIVEL, *Nog steeds veranderen maar weinig mensen van ziekenfonds*, 2005.

⁴⁴ The present relative price differences between health insurance funds and between private insurers amounted to more than 60%. Source: NMa's overview based on www.independ.nl on the basis of (comparable) insurance premiums on 1 January 2005.

⁴⁵ TNS NIPO, *Switchen in de zorg, ervaringen van Nederlanders met het overstappen van zorgaanbieder en –verzekeraars*, 14 October 2004. Research commissioned by NMa.

⁴⁶ CPB, *Switch on the Competition; Causes, Consequences and Policy Implications of Consumer Switching Costs*, CPB Document No 97, September 2005, p. 104.

⁴⁷ On the basis of the policies presented by insurers in mid-November 2005, most insurers do not seem to offer hybrid forms.

⁴⁸ 'Verzekeraars omhelzen patiëntenvereniging', *Zorgvisie*, 4 October 2005.

⁴⁹ 'Agis biedt polis voor chronisch zieken', *Trouw*, 30 December 2004.

⁵⁰ 'Speciale polis voor diabetici', *De Telegraaf*, 29 September 2005.

⁵¹ See the decision in case 5052/CZ – OZ, *op. cit.*, recitals 115 and 116.

Chapter 6

¹ NMa, *Financial Sector Monitor 2004*, December 2004.

² The concept of a 'market' is not used here in the way it is used in competition law. This is therefore not a definition of the relevant market in accordance with competition law.

³ The payment, however, may also occur in the opposite direction. In Australia, for instance this is the case in relation to some means of payment.

⁴ This is often due to complaints by customers who purchase acquiring services.

⁵ J. Rochet and J. Tirole, 'Two-Sided Markets: an Overview', *IDEI Working Paper 275*, March 2004. An attempt is made in this article to give a formal definition of two-sidedness. This is based on two conditions: (1) whenever one of the two sides does not participate, a transaction is not possible, and (2) not only the total price charged to the two user groups determines profit, but also the way in which this is divided between the two sides.

⁶ A condition for two-sidedness is that bargaining is not possible between the two user groups. In this case, the indirect externalities are internalised through negotiations.

⁷ A subtle point in this regard is the difference between user and membership externalities. In the one case, the number of transactions is important and, in the other case, the number of members.

⁸ M. Armstrong, 'Competition in Two-Sided Markets', *Mimeo*, University College London, 2004; J. Rochet en J. Tirole, 'Platform Competition in Two-Sided Markets', *Journal of European Economic Association*, 1, 2003, 990-1029.

⁹ W.F. Baxter, 'Bank Interchange of Transactional Paper: Legal and Economic Perspectives', *Journal of Law & Economics*, 26, 1983, pp. 541-588.

¹⁰ In the original article, the costs and advantages depend on the number of transactions. However, this is not essential to an understanding of the role of interbank charges.

¹¹ Where cash payments are more expensive than electronic payments, the 'costs' of issuers and acquirers are therefore negative. Electronic payment systems often incur lower costs than cash payments.

¹² We assume that these costs are positive. This need not be the case in reality.

¹³ This assumes therefore that the buyer and seller do not negotiate with each other on price. No 'bargaining' is possible. In this case, inefficiency can be sold through 'side payments' between the consumer and the retailer.

¹⁴ Various settlements are possible to restore efficiency. For instance, a payment by the acquirer to the issuer amounting to $c_I - b_B$ is an alternative means of restoring efficiency. In this case, the consumer pays b_B and the retailer pays $c_I + c_A - b_B$.

¹⁵ R. Schmalensee, 'Payment Systems and Interchange Fees', *The Journal of Industrial Economics*, 50, 2002, pp. 103-122.

¹⁶ He does so by arguing that the number of PIN transactions is the product of consumer demand and demand from retailers.

¹⁷ This is based on a total welfare measure, in other words consumer plus producer welfare. This is important in relation to applications under competition law. One of the conditions of section 6(3) of the Competition Act is that the benefits must be passed on to a sufficient degree to consumers. In practice, this means that consumer welfare has priority in an analysis in accordance with competition law.

¹⁸ An additional conclusion is that, in the case of symmetry (in other words, all banks carry out acquiring and issuing activities to the same extent), the optimal interbank charge is nil.

¹⁹ J. Rochet and J. Tirole, 'Cooperation among Competitors: Some Economics of Payment Card Associations', *RAND Journal of Economics* 33 No. 4, 2002, pp. 549-570.

²⁰ They extend the Schmalensee model by explicitly modelling the behaviour of consumers and by modelling competition between retailers for the patronage of consumers on the basis of a Hotelling model.

²¹ J. Wright, 'Optimal Card Payment Systems', *European Economic Review*, 47, 2003, pp. 587-612; J. Wright, 'One-sided logic in two-sided markets', *Review of Network Economics*, 2004, Vol. 3, No. 1 (March), pp. 44-64.

²² Wright examines pure price competition (Bertrand competition) between retailers.

²³ Where surcharges are not permitted, two types of retailers emerge: those who accept PIN transactions and those who do not accept PIN transactions. The analysis assumes that cash is cheaper for retailers than PIN payments.

²⁴ W. Bolt and A. Tieman, 'Skewed Pricing in Two-Sided Markets: An IO Approach', *Mimeo*, De Nederlandsche Bank, 2004.

²⁵ The relevant question, however, in relation to competition law is how the introduction of a multilateral interbank charge affects consumer welfare. This means that the conclusions from the economics literature cannot be applied directly to issues relating to competition law. This

point is not taken into account in the present analysis, but would have to be considered in an actual case.

²⁶ These factors include, for instance, the degree of cross subsidisation, the level of start-up fees, the number of active platforms, the costs of cash payments, the cost of PIN payments, the price elasticities of consumers and retailers, the relationship between the issuing and acquiring activities of banks and the relationship between total demand and prices on both sides of the market.

²⁷ D. S. Evans and R. Schmalensee, 'The Economics of Interchange Fees and Their Regulation: An Overview', *MIT Sloan Working Paper* No. 4548-05, 2005.

²⁸ Up until March 2004, Interpay was the only acquirer in the Netherlands. From that moment onwards, banks also started offering acquiring services, with the ultimate aim of transferring all Interpay's PIN contracts to the banks. This process has now been completed. In order to carry out issuing and acquiring activities in the Netherlands, banks must have a licence from Currence. Currence is the owner of the payment products, PIN and Chipknip, and was set up on 1 January 2005 under the name of Brands & Licences Betalingsverkeer Nederland B.V. by ABN AMRO, Rabobank, ING, Fortis, SNS, BNG, Friesland Bank and Van Lanschot Bankiers. Since 1 May 2005, the company has been called Currence. Acquirers and issuers pay a licence fee to Currence, while Interpay charges acquirers and issuers a fee for switching and clearing. See also, NMa, *Financial Sector Monitor 2004*, December 2004, pp. 92-93.

²⁹ In addition, there are other revenues which arise from this, such as the low interest on current accounts, high interest on current account credit, value days and cross subsidies. These revenues are not taken into account in this analysis. These revenues should be taken into account in a more detailed study.

³⁰ This assumes that issuers and acquirers have market power.

³¹ This overview is based on public documents (up to 1 October 2005).

³² For the description of NMa cases, you are referred to the *Financial Sector Monitor 2003*, pp. 32 to 36.

³³ D. Balto, 'The Problem of Interchange Fees: Costs without Benefits', *European Competition Law Review*, issue 4, 2000; National Bancard Corp. ("NaBanco") v. Visa U.S.A. (1986), Inc., 596 F. Supp. 1231 (S.D. Fla. 1984), aff'd, 779 F.2d 592 (11th Cir.), cert. denied, 479 U.S. 923.

³⁴ *Ibidem*.

³⁵ Balto, D.A. and R.W. March, *Recent Government Enforcement Actions on Interchange Fees*, Kaplan Miller & Ciresi L.L.P., 2005;

³⁶ Retailers pay the MSC charge (merchant service charge) to banks for offering various payment services (for instance a PIN terminal or credit card services).

³⁷ 'Plaintiffs' lawyers argue Kendall won't sink their interchange cases', *Digital Transactions*, September 2005.

³⁸ The cross-border multilateral interbank charge relates to Visa transactions between various Member States of the EEA (European Economic Area).

³⁹ The Commission of European Communities, *Commission Decision, Case No COMP/29.373 – Visa International – Multilateral Interchange Fee*, 2002.

⁴⁰ Deferred debit cards are PIN cards which offer the possibility of payment at a later moment or in instalments.

⁴¹ Visa argued that a rent-free period has the effect of increasing consumption because consumers can make additional purchases which they would not otherwise have made. The Commission thought that this was a plausible argument and agreed to the inclusion of this cost category.

⁴² Press Release, Office of Fair Trading, *Mastercard Agreement Anti-Competitive Rules Office of Fair Trading*, 6 September 2005. See also the companion paper CP/0090/00/S to this decision.

⁴³ *Ibidem*.

⁴⁴ Press Release Office of Fair Trading, *Office of Fair Trading Issues Statement of Objections on Visa Agreement*, 19 October 2005.

⁴⁵ The multilateral interbank charge is charged in the case of "shared transactions" where the bank of the cardholder and the owner of the cash dispenser are not the same. A distinction is made between fixed and variable costs. Examples of these are the costs of the cash dispenser and maintenance costs.

⁴⁶ Office of Fair Trading, *Decision of the Director General of Fair Trading LINK Interchange Network Limited*, 16 October 2001.

⁴⁷ *Ibidem*

⁴⁸ This relates to the organisations: Servired, Euro 6000 and 4B Services. Spanish Competition Tribunal (TDC), Judgment (Case A 318/02, SERVIRED Interchange Fees), 2005; TDC, Judgement on Individual Exemption (Case no. A314/2002 Sistema 4B), 2005; TDC, Proceedings in the Cases of Amendment or Revocation (Case No. A287/00 Euro 6000), 2005; "Spain's Interchange Shock for Banks", *European Card Review*, May/June 2005. The decision which was officially drawn up by the organisation ServiRed also applies to the network organisations Euro 6000 and 4B Services.

⁴⁹ *Ibidem*

⁵⁰ The maximum multilateral interbank charge was set annually and ranges from 2.75% in 2002 to 2.0% in 2007 without the disclosure of a transparent method of calculation.

⁵¹ 'Spain's Interchange Shock for Banks', *European Card Review*, May/June 2005.

⁵² Balto, D.A. and R.W. March, *Recent Government Enforcement Actions on Interchange Fees*, Kaplan Miller & Ciresi L.L.P., 2005; see www.justice.gov.

⁵³ Balto, D. and Marth, R.W., *Recent Government Enforcement Actions on Interchange Fees*, Robins, Kaplan Miller & Ciresi L.L.P., 2005; "In re: Visa Check/Mastermoney Antitrust Litigation (a/k/a Wal Mart Stores, INC. et al v. Visa U.S.A. Inc. and MasterCard International Inc).", *Constantine Cannon*, 2005.

⁵⁴ Balto, D. and Marth, R.W., *Recent Government Enforcement Actions on Interchange Fees*, Robins, Kaplan Miller & Ciresi L.L.P, 2005.

⁵⁵ 'Commission Clears Certain Provision of the Visa International Payment Card System', *European Commission*, 10 August 2001.

⁵⁶ *Ibidem*

⁵⁷ IMA, *Study Regarding the Effects on the Abolition of the NDR in Sweden – Results and Conclusions*, February 2000; ITM Research, *The Abolition of the No-discrimination Rule*, March 2000.

⁵⁸ S.E. Weiner and J. Wright, 'Interchange Fees in Various Countries: Developments and Determinants, Payments System Research Department Federal Reserve Bank of Kansas City', *Working Paper 05-01*, September 2005, p. 2.

⁵⁹ Reserve Bank of Australia, *Debit and Credit Card Schemes in Australia: A Study of Interchange Fees and Access*, October 2000.

⁶⁰ *Ibidem*

⁶¹ The multilateral interbank charge may differ per transaction, for instance where it is a percentage of the amount of the purchase.

⁶² Reserve Bank of Australia, 'Payments System Board', *Annual Report*, 2004, pp. 8-9.

⁶³ Both cards (Visa and EFTPOS) are PIN-based debit cards (payment cards with a PIN code).

⁶⁴ Reserve Bank of Australia, 'Payments System Board', *Annual Report*, 2004, pp. 13-14.

⁶⁵ The parties involved were asked to provide input for the definition of the standard for EFTPOS and Visa debit payment systems.

⁶⁶ Reserve Bank of Australia, 'Payments System Board', *Annual Report*, 2004, p. 16.

Chapter 7

¹ Insurance underwritten by means of coinsurance can also be reinsured.

² See NIBE SVV, *Assurantie A: Algemeen* and *Annual Report VNAB 2003*

³ The concept of a 'market' is not used here in the way it is used in competition law. This is therefore not a definition of the relevant market in accordance with competition law.

⁴ Regulation 358/2003 on the application of Article 81(3) of the Treaty to certain categories of agreements, decisions and concerted practices in the insurance sector.

⁵ 'Wegvallen assurantiebeurzen is niet het einde van co-assurantiemarkt', *VVP*, 21 January 2004.

⁶ Articles 1, 2, 3 and 4 of the Standing Rules of VNAB.

⁷ See also J.G.C. Kamphuisen, *De Beursmakelaar*, Prior recommendations to Vereniging voor Verzekeringswetenschap [Association for Insurance Sciences], 1990 and J.G.C. Kamphuisen, *De opdracht aan de assurantiëtussenpersoon*, Prior recommendations to the Vereniging voor Verzekeringswetenschap [Association for Insurance Sciences], 1996.

⁸ 'De toegevoegde waarde van een beursbedrijf', *Het Verzekeringsblad*, September 2004.

⁹ Payments made out of fairness are non-obligatory payments which may be made to maintain the good relationship with the insured or the broker, but would not have to be made on the grounds of the cover, as described.

¹⁰ See also NMa, *Financial Sector Monitor 2004*, December 2004, Chapter 2.

¹¹ Gross premium income is the premium income prior to deduction of the premium paid to the reinsurer. The insurer, after all, can always insure the risk which it has underwritten with another company. The premium recorded was considered, which includes the commission paid by the insurer.

¹² VNAB, *Jaarverslag 2003*, 2003; Dutch Association of Insurers, *Verzekerd van Cijfers 2004*, 2004. The total relates to consumer and business insurance.

¹³ 'Resultaat brand bedrijven 10% negatief', *Het Verzekeringsblad*, 30 May 2002;

'Assurantiebeurs is begonnen aan wederopbouw', *Het Verzekeringsblad*, 2 May 2002.

¹⁴ See: *The People of the State of New York* by Eliot Spitzer, Attorney General of the State of New York – Marsh & McLennan Companies Inc and Marsh Inc, New York, October 14, 2004

¹⁵ Regulation 358/2003 on the application of Article 81(3) of the Treaty to certain categories of agreements, decisions and concerted practices in the insurance sector. In this regard, see also IP/03/291.

¹⁶ Regulation 3932/92.

¹⁷ Recitals 18 up to and including 23 and Article 7 of regulation 358/2003.

¹⁸ Article 7 of Regulation 358/2003.

¹⁹ The Netherlands Insurance Exchange All-Risks Policy for Construction 1995 [*Nederlandse Beurs-cascolpolis voor aanbouw 1995*]; Netherlands Insurance Exchange Policy for Agricultural Material 1991 [*Nederlandse Beurspolis voor Landmateriaal 1991*]; Netherlands Insurance Exchange Policy for Goods-in-Transit 1991 [*Nederlandse Beurs-goederenpolis 1991*]; Netherlands Insurance Exchange All-Risks Policy for Inland Shipping 1991 [*Nederlandse Beurs-cascolpolis voor de binnenvaart 1991*]; Netherlands Insurance Exchange Extended Risks Policy 1998 [*Nederlandse Beurspolis voor Uitgebreide Gevaren 1998*] (this does not only cover fire, but usually also a series of other causes of damage, such as lightning, storm, water damage and theft); Insurance Exchange Category Policy: Construction Insurance for Construction Projects [*Beurs Rubriekenpolis Constructieverzekering voor Bouwwerken*], *afgekort als Beurs-CAR-Polis*], abbreviated as 'Beurs-CAR-Polis'.

²⁰ Article 5 of Regulation 358/2003.

²¹ Article 5 and 6 of Regulation 358/2003.

²² Article 6(1)(b) of Regulation 358/2003.

²³ 'AXA waagt zich weer op de beurs', *Assurantiemagazine*, 9 September 2005.

Chapter 8

¹ NMa, *Financial Sector Monitor 2004*, December 2004, pp. 60-61.

² DNB Statistics, *Balansstaten van beleggingsinstellingen naar fondstype* [Balance-sheet totals of investment institutions according to the type of fund].

³ AFM, *Zicht op beleggingsinstellingen*, April 2004.

⁴ AFM, *Zicht op beleggingsinstellingen*, April 2004. Of this, EUR 41 billion is invested directly by private individuals, while an estimate of EUR 37 billion is invested indirectly by private individuals through insurers (for instance pension insurance, annuities, lump sums and mortgages with an investment component).

⁵ The term 'market' is not used here in the way it is used in competition law. The use of this term therefore does not imply that there is a relevant market for investment institutions in accordance with competition law. This was not researched.

⁶ Investment institutions are subdivided in the Investment Institutions Supervision Act into investment companies and investment funds. In accordance with section 1(8) of the Investment Institutions Supervision Act, an investment company is a legal entity which acquires or has acquired money or other goods to invest collectively with the purpose of enabling the participants to share in the return on the investments. An investment fund is capital not invested in a legal entity for which money or other goods are acquired or have been acquired for the purpose of a enabling be participants to share in the returns on the investments.

⁷ Figures provided by the Dutch Central Bank. These figures have not been corrected for inflation.

⁸ DNB, *Statistisch Bulletin september 2004*, September 2004.

⁹ 'Het actuele getal: -1,4 miljard euro', DNB, 24 May 2005.

¹⁰ DNB, *Statistisch Bulletin maart 2005*, March 2005.

¹¹ The HHI is defined as the sum of the squares of the market shares of the undertakings active on the market.

¹² B. Slot, *Iedereen een kapitalist, De ontwikkeling van het beleggingsfonds in Nederland gedurende de 20^{ste} eeuw*, Ph.D. thesis, Aksant, 2004.

¹³ See also 'Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings', *OJEC C 31* of 05/02/2004, recitals 19 and 20. In these guidelines it is considered improbable that the Commission will conclude that there are competition concerns if the HHI after the merger is (i) less than 1,000, (ii) between 1,000 and 2,000 and the change in the HHI is less than 250, and (iii) greater than 2000 and the change is less than 150. In the United States, a threshold of 1,800 points is assumed.

¹⁴ 'Buitenlands vermogensbeheer aan zet', *Het Financieele Dagblad*, 16 December 2004.

¹⁵ With regard to the sale of funds to institutional investors, it is probably easier for foreign parties to establish themselves.

¹⁶ The percentage of Dutch consumers which have financial products of foreign providers is small: this is 6% for bank accounts, 3% for credit cards, 2% for mortgages and 2% of shares. See Eurobarometer 58.1, *Report B*, of the Public Opinion Research Group, commissioned by the European Commission, February 2003.

¹⁷ KPMG, *Banking beyond Borders: Will European Consumers Buy It?*, 2004.

¹⁸ Harless, D.W., Peterson, S.P., 'Investor Behaviour and the Persistence of Poorly Performing Mutual Funds', *Journal of Economic Behaviour & Organisation*, Vol. 37, 1998, pp. 257-276.

¹⁹ At present, no sources are known which state what the exact market shares of the various distribution channels are.

²⁰ Millward Brown/Centrum, *Evaluatie Financiële bijsluiter: resultaten van onderzoek onder consumenten intermediairs en aanbieders*, report for AFM, June 2004.

²¹ This yield was adjusted annually. In 2000 this was approximately 6 procent.

²² Foreign funds are more advantageous where the dividend payment is greater than this notional yield.

²³ 'Buitenlandse fondsen scoren het best', *de Volkskrant*, 11 January 2003. The amendments were part of the tax reform 2001. See www.minfin.nl *Wet inkomstenbelasting 2001* [Income Tax Act 2001].

²⁴ 'ABN AMRO: meer marktaandeel bij particuliere belegger', *De Financiële Telegraaf*, 25 January 2005.

²⁵ 'Stop uittocht van beleggingsfondsen', *Het Financieele Dagblad*, 18 May 2005. An advantage of relocating to Luxembourg for investors is that funds which are listed in Luxembourg do not have a spread. Investment funds with a listing on Euronext Amsterdam use a spread around the net asset value (the market value of the shares in the fund). The spread means that the customer pays a surcharge when purchasing shares in the fund and the actual value of the fund is reduced on the sale of shares. Another difference with Luxembourg is that a fund in the Netherlands pays 0.55% capital tax on every new share issued, while this is only 0.05% in Luxembourg. Finally, investment funds can be traded throughout the day in the Netherlands, while in Luxembourg, as in the US, they can only be traded at one moment each day.

²⁶ 'Luxemburg lonkt', *Het Financieele Dagblad*, 16 July 2005.

²⁷ Standard & Poor's Fund Services Nederland, 2003. Based on the so-called Total Expense Ratio (TER). Trading costs are not included in this standard.

²⁸ 'Standard & Poor's hekelt kosten beleggingsfondsen', *Het Financieele Dagblad*, 27 November 2003; 'Fondsen zeer zwijgzaam over kosten', *Het Financieele Dagblad*, 27 November 2003; 'Veel onbegrip over scherpe tariefsverhoging door Robeco', *Het Financieele Dagblad*, 3 July 2004; 'Robeco verhoogt kosten 30 procent', *Volkscrant*, 6 July 2004; 'Fondsen vechten om distributiepunt', *Het Financieele Dagblad*, 7 July 2004; 'ABN verhoogt tarieven voor fondsbeheer', *Het Financieele Dagblad*, 29 September 2004; 'Wij gaan mee in de prijsverhoging', *Het Financieele Dagblad*, 29 September 2004.

²⁹ Leaving aside foreign funds.

³⁰ 'Agressie is de trend bij fondsverkoop', *Het Financieele Dagblad*, 1 June 2005.

³¹ DNB, *kwartaalbericht DNB June 2002*, June 2002.

³² B.G. Malkiel, 'Returns from Investing in Equity Mutual Funds from 1971 to 1991', *Journal of Finance*, 50(2), 1995, 549-572; S.P. Umamaheswar Rao, 'Economic Impact of Distribution Fees on Mutual Funds', *America Business Review*, Januari 2001, pp. 1-5; E.J. Elton, M.J. Gruber, S. Das en M. Hvlaka, 'Efficiency with Costly Information: A Reinterpretation of Evidence of Managed Portfolios', *Review of Financial Studies*, 6, 1993, pp. 1-22.

³³ B. Barber, T. Odean, L. Zheng, 'Out of Sight, Out of Mind: The Effects of Expenses on Mutual Fund Flows', working paper, December 2001.

³⁴ D.W. Harless, S.P. Peterson, 'Investor Behaviour and the Persistence of Poorly Performing Mutual Funds', *Journal of Economic Behaviour & Organization*, 37, 1998, pp. 257-276.

³⁵ R.T. Wilcox, 'Bargain Hunting or Star Gazing? How Consumers Choose Mutual Funds', *Marketing Science Institute*, 1998, working paper; Barber, B., Odean, T., Zheng, L., 'Out Of Sight, Out Of Mind: The Effects of Expenses on Mutual Fund Flows', working paper, December 2001.

³⁶ Consumentenbond, *Consument en Geldgids*, November 2001, pp. 7-9.

³⁷ Investment institutions may be subdivided into:

(1) Variable capital investment companies which are legal persons (more than 90% of the invested capital). Section 2:76A of the Netherlands Civil Code makes it obligatory for the company to be listed (this is unique in the EU) and is derived from the European company law directive. Open-ended investment companies can be subdivided into:

- Open-ended (approximately 90% of the total). In the case of open-ended investment institutions, units in the assets of the institution may be purchased by or repaid to participants directly or indirectly. Open-ended investment institutions are active as buyers and sellers of shares.
- Closed-end (approximately 10% of the total) do not purchase shares nor do they issue shares continuously). These are mainly real estate institutions. In the case of a closed-end investment institution, the share price of a participation depends on supply and demand. The market price of a closed-end institution is usually not equal to the net asset value of the fund. New shares are only issued if there is a share issue.

(2) Investment funds (in terms of the Investment Institutions Supervision Act) are not legal entities (approximately 5% to 10% on the basis of invested capital). A separate administrator must be appointed which is a legal entity. Only a small number of funds are investment funds.

³⁸ AFM, *Zicht op beleggingsinstellingen*, 27 April 2004.

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- ³⁹ Winter Commission, *Rapport commissie modernisering beleggingsinstellingen*, 2004.
- ⁴⁰ See Proceedings of the Lower House of the Dutch Parliament 2004-2005 No. 28998, p. 11.
- ⁴¹ 'Kapitaalsbelasting verdwijnt', Ministry of Finance, 24 March 2005.
- ⁴² 'Wijn verlaagt belasting voor fondsensector', *Het Financieele Dagblad*, 24 June 2005.
- ⁴³ This would have to be researched in more detail.