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Merger Reform in Australia: Possible Approaches

By Rhonda L. Smith & Deborah Healey

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Like many other jurisdictions, Australia is reviewing its approach to assessing mergers, particularly in the context of the digital environment.

Merger notification is not compulsory in Australia. The most common review process is a voluntary informal clearance procedure not contained in the Competition and Consumer Act 2010 (CCA), where the Australian Competition and Consumer Commission ("ACCC") gives an informal view to the parties under a standard procedure. Court cases are relatively unusual. If parties receiving a negative view continue with the merger, the ACCC may seek an injunction in court. Merger parties may also seek an authorization, a formal administrative exemption, from the ACCC under which likely lessening of competition is balanced against resultant public benefit.

The Chair of the ACCC, Rod Sims, has regularly argued for reform and in the ACCC 2019-2020 Annual Report,[2] for example, following losses in the *Vodafone*[3] and *Pacific National*[4] merger cases, Sims emphasized the importance of ensuring the Australian economy did not become too concentrated. He also noted the likely impact of anticompetitive mergers on innovation, productivity and inequality. [5]

A review by the Treasury was to have occurred in 2020 but was delayed until 2021 due to the pandemic. In a joint statement with the Competition and Markets Authority ("CMA") and the Bundeskartellamt, the ACCC more recently referred to "the need for rigorous and effective merger enforcement."[6] It went on to state:

> *Competition agencies are increasingly reviewing mergers in dynamic and fast-paced markets. These mergers can involve hundreds of products or services in related markets, as well as products and services in earlier research and development stages. In addition, the last decade has seen the rise of acquisitive tech giants with activities across multiple current or future markets*.[7]

The Joint Statement offers no specific remedies other than a preference for structural rather than behavioral undertakings as a means of addressing problematic mergers. The ACCC has indicated that it will provide its recommendations for change in the middle of this year. However, in July 2019 in its Final Report of the Digital Platforms Inquiry,[8] the ACCC did put forward proposals for change in relation to mergers, recommending additional factors for consideration, such as the removal of

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[2] ACCC, *2019-2020 Annual Report* (n 76) 5.

[3] *Vodafone Hutchinson Australia Pty Ltd v. ACCC* [2020] FCA 117.
[4] *ACCC v. Pacific National Pty Limited* [2020] FCAFC 77 (May 6, 2020) (*Pacific National Appeal*).
[5] ACCC, Rod Sims, "Competition Issues in Infrastructure and changes since COVID-19," (Speeches, 15 October 2020) https://www.accc.gov.au/speech/competition-issues-in-infrastructure-and-changes-since-covid-19 accessed March 7, 2021.

[6] CMA, ACCC, Bundeskartellamt, Joint Statement on merger control enforcement, 20 April 2021, paragraph 1. https://www.accc.gov.au/system/files/Joint%20statement%20-%20merger%20control%20enforcement.pdf.
[7] Joint statement, paragraph 10.
[8] Australian Competition and Consumer Commission, Digital Platforms Inquiry Final Report, July 26, 2019 https://www.accc.gov.au/publications/digital-platforms-inquiry-final-report.

a potential competitor, and the nature and significance of the assets being acquired, including data and technology. The ACCC also recommended that large digital platforms should agree to a notification protocol in advance of proposed acquisitions. These amendments have not been made to date

The problem is not merely the complexity of the markets involved: "The combination of the uncertainty inherent in the forward-looking nature of merger control and changes in the nature and complexity of the mergers under review presents challenges to preventing further concentration from anticompetitive mergers over the longer term."[9]

The real issue is how to provide admissible evidence to establish the *likely future effect* of a merger, especially in markets that are dynamic and where the acquisition is of a small business that *might* develop into a competitive threat to the would-be acquirer in future, independently or in other ownership. Much attention has focused on the counterfactual, that is, what will happen absent the merger, but the factual is subject to the same uncertainty about the future. In a general context, but particularly in a digital environment, the present may be a very poor guide to the future.

What change is needed? Section 50 of the Competition and Consumer Act ("CCA") prohibits a merger that has the effect or likely effect of substantially lessening competition ("SLC").

Section 50(3) identifies factors that must be taken into account in assessing a SLC. These include but are not limited to:

> (a) the actual and potential level of import competition in the market;
>
> (b) the height of barriers to entry to the market;
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> (c) the level of concentration in the market;
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> (d) the degree of countervailing power in the market;
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> (e) the likelihood that the acquisition would result in the acquirer being able to significantly and sustainably increase prices or profit margins;
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> (f) the extent to which substitutes are available in the market, or are likely to be available in the market;
>
> (g) the dynamic characteristics of the market, including growth, innovation and product differentiation;
>
> (h) the likelihood that the acquisition would result in the removal from the market of a vigorous and effective competitor;
>
> (i) the nature and extent of vertical integration in the market.

In the Final Report of the Digital Platforms Inquiry the ACCC recommended including two further factors in s.50(3):

> "(j) the likelihood that the acquisition would result in the removal of a *potential* competitor from the market;
>
> (k) the nature and significance of assets, including data and technology, being acquired directly or through the body corporate."[10]

While the addition of these factors would make clear the need to take them into account, given their relevance it would be expected that this

[9] Joint Statement, paragraph 2.
[10] ACCC, Digital Platforms Inquiry Final Report, June 2019, Recommendation 1. https://www.accc.gov.au/system/files/Digital%20platforms%20inquiry%20-%20final%20report.pdf.

should already be the case, and decided cases indicate that potential competition is already an important consideration.

Currently, parties may alternatively seek an exemption from s.50 if the merger will result in a net public benefit (usually due to expected efficiency gains). This process, referred to as "authorization," involves the ACCC making an administrative decision. The first step is for the ACCC to determine whether the merger is likely to SLC. If it would not do so, a formal clearance is issued. If it is likely to SLC, the ACCC assesses the claimed public benefits and balances them against the SLC. Its decision may be reviewed by the Australian Competition Tribunal and the Tribunal's decision can only be appealed to the court on points of law.

Our suggestions aim to increase the effectiveness of the merger assessment process by adapting existing processes rather than replacing them. In its Digital Platforms Inquiry report, the ACCC recommended that "[l]arge digital platforms …[should] agree to a notification protocol, to provide advance notice to the ACCC of any proposed acquisitions potentially impacting competition in Australia."[11] However, in the US and the EU where there are mandatory reporting requirements for mergers, these have been largely ineffective in relation to the mergers of particular concern – acquisitions of small start-ups by major platform businesses. This is because the thresholds are expressed in terms of market shares and most often the market share of the target is very small. Even if the threshold was expressed in revenue terms it is unlikely to be effective. More appropriate might be the ratio of revenue to the offer price, but it is the future revenue rather than current revenue which is relevant. In Australia's case, despite the lack of mandatory reporting, the ACCC is informed, directly or indirectly, of most mergers. Possibly this is in part because it is a relatively small economy with an active business media. Given this, there seems to be little benefit from a mandatory reporting requirement which is hard to specify appropriately and which is targeted only at one type of business structure. One issue of concern is where parties inform the Commission only shortly prior to completion of a merger, not allowing sufficient time for the Commission's assessment.

In dynamic and emerging markets, market participants, not the ACCC, will have the best understanding of the impact of a proposed merger. Reports such as the US House Judiciary Committee report on competition in digital markets, the European Commission's "Competition policy for the digital era"[12] and the Stigler Committee on Digital Platforms Final Report,[13] have recommended reversing the onus of proof for acquisitions by digital platforms to reflect this. However, in Australia at least, the onus already effectively rests with the parties to any merger unless the ACCC institutes court proceedings.

The substantive change that we suggest is to give the ACCC the power to make administrative decisions in relation to all mergers, not just under the authorization process as is the case at present. The current informal assessment ("informal clearance")

[11] ACCC, Digital Platforms Inquiry, Recommendation 2.

[12] https://op.europa.eu/en/publication-detail/-/publication/21dc175c-7b76-11e9-9f05-01aa75ed71a1/language-en.

[13] Competition Policy for the Digital Era, Report for the EU by Jacques Crémer Yves-Alexandre de Montjoye Heike Schweitzer Digital 2019 https://www.chicagobooth.edu/research/stigler/news-and-media/committee-on-digital-platforms-final-report. The Furman Report (UK) did not recommend reversing the onus. However, Amelia Fletcher, a member of the committee, did subsequently consider that it might be useful (OECD, Digital competition policy: Are ecosystems different? – Note by Amelia Fletcher, Best Practice Roundtable, June 2020).

process would be retained as Phase 1. Mergers would be cleared to proceed at the end of Phase 1 if they are unlikely to SLC, as they currently are under informal clearance. Mergers identified as likely to SLC would move to a Phase 2 investigation. At the end of Phase 2, the ACCC would make an administrative decision on the merger. To clarify, to avoid running parallel processes, the first step in the authorization process, that is, establishing whether the merger is likely to SLC, would be undertaken as part of a Phase 1 inquiry. Given that the basis for seeking authorization is a recognition by the parties that the merger is likely to SLC, most of the merger authorization applications will move through to Phase 2 and likely be found to SLC, reflected in the Commission's administrative decision. At that point, the parties could choose to seek authorization, based on the associated public benefit from the merger.

A limited merits review of the ACCC's administrative decision could be sought from the Australian Competition Tribunal. Why the Tribunal and not the court? Much of the difficulty encountered by the ACCC in successfully prosecuting merger cases in court has been the interpretation of "likely" and the flow-on effects from that.[14] Essentially, the ACCC is required to prove that on the balance of probabilities merger would have, or be likely to have, the effect of substantially lessening competition in any market. This requires it to provide admissible evidence, that is, evidence acceptable under the Evidence Act, that the merger is likely to SLC in future if it proceeds. However, as noted above, as the merger has yet to occur, leaving aside any effect that the proposal may have had on the market, there is generally no real evidence, but simply informed opinions. In practical terms this often boils down to whether absent the merger an alternate buyer is likely to emerge. However, alternative buyers of the business would be irrational to spend time and money preparing to buy the business if a deal is already being accepted subject to it not breaching s.50 – they will often wait to see what happens.

Review by the Tribunal has two benefits compared to litigation in the court. The first is its composition which includes not only a judge but a business person and an economist. This would enable the Tribunal to better address what is likely to be increasingly complex economic models which provide the basis for the opinions of expert economists on the likelihood of SLC. Second, the Tribunal is not bound by the rules of evidence. This should mean that it is more amenable to establishing the likelihood of a SLC based on the structural conditions of the market (as well as strategic behavior where relevant to barriers to entry) and opinions derived from market circumstances such as the price being paid for the acquisition compared to its current revenue. It is suggested that, as is the case in the New Zealand High Court (which plays a similar role to the Tribunal), the ACCC should be regarded as an expert body and so its findings should be accepted unless the parties can provide information that establishes error.

Mergers are time sensitive. Once information about a proposed merger becomes public, rivals may engage in conduct designed to counter the expected benefits from the merger and/or other suitors may emerge. A delayed decision-making process for mergers has the potential to kill off a merger that may ultimately be found not likely to SLC. Given this, there would be concern if any change to the process for assessing mergers extended the time taken compared to the current arrangements. This is unlikely. The

[14] For an important and current discussion of the meaning of "likely" see *ACCC v. Pacific National*, paragraph 222 ff.

ACCC is subject to quite strict time lines. Between 2007 And 2017 the Tribunal determined authorization applications, a process that was subject to a maximum three-month period. The same period could apply its review of the ACCC's administrative decisions under the revised process. Given the limited ability to appeal the Tribunal's decision and given the time taken by courts to arrive at a concluded decision, the proposed change may well shorten the process even in cases where it proved necessary to extend the time available to the ACCC to reach a decision in its inquiries. Authorization decisions in relation to mergers would continue to be able to be reviewable by the Tribunal.

What role would the court play in relation to mergers if these changes were to be implemented? As at present, the ACCC would need to apply to the court if an injunction was required to prevent a merger completing prior to it completing its investigation or to enable the ACCC to investigate a completed merger that had not been notified. Parties would no longer be able to apply to the court for a declaration concerning a proposed merger. Should a merger proceed despite a decision by the ACCC that it would contravene s.50, this decision might be subject to mandatory review by the Tribunal, If the Tribunal upheld the ACCC's decision, application would be made to the court to issue orders in relation to penalties based on agreed facts, as is currently the case for settlements.

In a rapidly changing world, there is no crystal ball that enables a glimpse into the alternate futures with and without a proposed merger. The parties to the merger are best placed to anticipate the outcome of the merger but, of course, have an incentive to be selective about the information they provide. That the ACCC has existing power under s.155 of the CCA to require the production of documents, especially those brought into existence prior to the decision to pursue the merger, as well as to require oral evidence under oath, helps to address this issue. However, the processes available for arriving at a determination of whether the proposed merger is likely to SLC are critical and at present there is real concern that they are not capable of this, especially in dynamic markets.