AUSTRALIAN INVESTMENT COUNCIL

24 October 2024

Committee Secretary
Senate Standing Committees on Economics
PO Box 6100, Parliament House
Canberra ACT 2600

Dear Committee Secretary

An inquiry into the provisions of the Treasury Laws Amendment (Mergers and Acquisitions Reform) Bill 2024.

The Australian Investment Council (the Council) welcomes the opportunity to provide this submission to the Senate Economics Committee inquiry on the Treasury Laws Amendment (Mergers and Acquisitions Reform) Bill 2024 (Merger Reform Bill).

The Council is the peak body for private capital investment in Australia and has over 220 members, including the leading domestic and international private capital firms operating in Australia. Private capital spans private equity, venture capital, private credit, family offices, superannuation, and sovereign wealth funds. These are members of Australia's investment community that collectively invest in more than 850 businesses economy-wide, mostly small and medium-sized, are responsible for more than 600,000 full-time jobs and contribute three per cent to Australia's GDP (on a gross value-added basis).

The Council recognises the overarching policy objective of Australia's merger control regime is to promote competition that enhances the welfare of Australians, consistent with the objectives of the Competition and Consumer Act 2010.

Mergers have proven to be a pathway to a greater competition in a market, particularly where it leads to smaller, challenger businesses building the scale to credibly compete against larger incumbents. Certainty and speed are critical to investing, particularly when there is a competitive process to acquire a business. Importantly, domestic and international investors do not need to deploy capital in Australia. To incentivise Australian capital to stay onshore, and to attract foreign capital into the Australian economy, the Council constructively suggests that this set of merger reforms – particularly the proposed notification thresholds - must strike a sensible balance between policy intent and growing productivity through investment.

If you have any questions about specific points made in this submission, please do not hesitate to contact me or our policy team via email at [redacted]

Yours sincerely

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SUBMISSION

This submission sets out a range of concerns held by our members on the form and impact of the proposed Bill, with a focus on the notification thresholds and the special sector designation including:

1. The strong likelihood of over-capture of the proposed threshold settings;
2. Uncertainty as to how the 'cumulative effect' is to be applied in practice; and
3. Concern about the application of the proposed special sector designation to capture the vast majority of unlisted (private) transactions, regardless of their impact on competition.

Below, the Council has outlined the impact of these issues on private capital investment, which is largely deployed or made in small and medium-sized businesses (SMEs) including start-ups and growth companies. These businesses are important to improving Australia's productivity and innovation and, with the right support for growth, can provide significant competition, challenging existing market dynamics and delivering significant benefits to consumers.

1. Proposed thresholds are likely to capture the majority of mergers in the unlisted (private) capital market

The Council welcomes the decision to remove market share thresholds from the reforms.

With respect to the monetary thresholds, the Council maintains its position that these are proposed to be set at a very low level and do not strike an appropriate balance between safeguarding against acquisitions that substantially lessen competition and placing additional administrative burden (on both the ACCC and acquirers).

We understand the policy intent is to capture "acquisitions of businesses or assets by medium to very large businesses". However, the current proposed threshold settings are likely to capture a much wider range of businesses. For example, assuming a target group's Australian turnover is $50 million, notification would be required whenever the acquirer group has at least $150 million in Australian turnover. A $150 million turnover business is vastly different to the ANZ Group – Suncorp Bank example cited as an example of policy intent in the ACCC's *Government Response to Consultation.* In that example, acquirer and target turnovers were $17 billion and $13 billion respectively.

In relation to the very large acquirer threshold, the intention is to capture transactions by very large businesses, with Treasury estimating some 900 businesses falling into the category of very large business (with revenue of greater than $500 million). The Council's view is that the low transaction value for this test of only $10 million for target turnover would again capture a much larger volume of transactions, the vast majority of which are not likely to raise any competition issues.

Practical implications

Our members advise that most private equity portfolio company turnover exceeds $200 million individually - or is likely to when aggregated with the target (i.e. $150 million of acquirer turnover plus $50 million of target turnover to provide a combined turnover of $200 million); the monetary

threshold test is therefore likely to be satisfied almost all of the time. This means that notification would be required for all exits via a sale process, and more often than not if portfolio companies are undertaking acquisitions. Similarly, $50 million is low as a turnover value: for example, one member advised that all but one portfolio company would have revenue exceeding $50 million and that transaction values are generally more than $200 million.

The very large acquirer turnover values are even lower at $10 million. These are set at such a level that they would likely catch all acquisitions made by businesses, regardless of the size or competitive impact of the acquisition, or transaction value. It is likely that this would cause, ultimately, needless burden on acquiring parties as well as the ACCC.

To provide context to these in relation to the numbers of transactions likely to be caught by the proposed thresholds: Merger Market data indicates that from 1 January 2020 to 14 October 2024 there were 6,858 transactions involving a target with a head company based in Australia (of these 5,861 were unlisted/private). This includes announced, completed and lapsed deals (as they all have the potential to be filed with the ACCC even if they lapse or have only been announced). This data omits transactions involving an Australian private or unlisted company which is a subsidiary of a group with head company incorporated outside of Australia, but such deals may also nonetheless be subject to ACCC notification as part of that deal.

For many businesses, every acquisition they undertake will be caught, irrespective of whether they could give rise to competition issues. Given the thresholds have been set at such a low level, it is important for business confidence for the ACCC to provide information about how it will have the administrative capacity to process notifications in line with the objectives of a "faster, clearer, streamlined process for review of acquisitions" as outlined in clause 1.3 of the Explanatory Memorandum.

To avoid over-capture, the Council has proposed:

- increasing the combined Australian turnover limb to $400 million (from $200 million);
- increasing the individual Australian turnover limb to $100 million (from $50 million); and
- increasing the definition of a 'very large acquirer' to $750 million in Australian turnover (from $500 million), with reference to the relatively large size of the Australian economy.

The Council notes the announcement that the thresholds will be reviewed 12 months after the reforms become effective. We would strongly recommend that this review includes public consultation on the impact on investment efficiency and confidence.

2. Serial acquisition thresholds

As presaged by the above, the current proposed thresholds for the three-year cumulative turnover, where combined Australian turnover is more than A$200 million and the cumulative Australian turnover from acquisitions in the same or substitutable goods or services over a three-year period, is at least A$50 million or A$10 million if a very large business is involved. This threshold is likely to be met in many cases for more than one acquisition merely by the existing size of either the acquirer or target before they are combined, meaning they are too low to be practicable.

It is the Council's view that there should be no requirement to aggregate turnover in addition to what is already in the acquirer's total turnover (including the turnover of those acquired businesses). If this is meant to be added to the target's turnover, this is not clear.
It is also unclear if it is only an accumulation of the Australian portion of the past transactions that applies and is to be aggregated. The current proposal is not clear on this element, or how this would apply in practice.

3. Special sector designation

In introducing the legislation into Parliament, the Government announced that it would exercise its power to direct the ACCC to review purchases of an interest or more than 20 per cent in an unlisted company if one of the parties to the transaction has turnover of more than $200 million.

Policymaking process

The Second Reading Speech indicates that the intention to apply special sector designation to private markets transactions was made on the ACCC's advice and is intended to give the regulator "the ability to analyse changes of control in private companies to ensure negative competition effects are avoided".

We understand there is further consultation to be conducted on the legislative instrument that will be drafted to give effect to this 'special sector designation'. However, we note that this matter has had no consultation to date and, consequently, stakeholders have yet to see the evidence base. We note this to the Committee as the approach to this announcement differs from that taken to the supermarket sector (which was subject to consultation) and is different to sectors to be considered for designation where no decision on designation has been made.

We are concerned by the absence of any process to date to engage in relation to this proposal which, without any apparent supporting evidence, sends a signal that there is a concern with all private markets transactions. Moreover, given the proposed serial acquisitions threshold, it is unclear why this additional designation is required.

Impact on investment

The effect of this designation is that for many businesses, particularly those with turnover over $200 million, every acquisition they undertake will be caught, regardless of whether they could give rise to competition issues.

We understand from Treasury that the $200 million threshold is Australian turnover, however this has yet to be confirmed in public consultation materials. Regardless, our view is that the volume of transactions that will become notifiable as a result of this designation will be significantly higher than the 300 - 500 notifications per year anticipated by the ACCC.

The designation would require notification of a wide range of minority and non-controlling investments in very small companies that would not otherwise be notifiable and of which the ACCC has not previously required notification. Examples of this kind of acquisition are below:

- where a private equity fund, whose portfolio companies derive revenues of over $200m from Australian customers, takes out a minority stake (>20 per cent) in a startup based overseas that has no or very limited turnover from customers in Australia; and
- where a private equity fund, whose portfolio companies are active in the supply of workflow software that generate $210 million in revenue in Australia, seeks to diversify by funding a new supplier of a completely different type of enterprise software through the acquisition of a non-controlling 21 per cent equity position (with no board seats and only customary minority shareholder protections in its shareholders agreement with the diluted founders).

The Council notes that the proposed monetary and very large acquirer thresholds alone will include the vast majority of unlisted (private) acquisitions. On this basis, we query the benefit of casting an even wider net for private markets transactions compared with the cost which includes increased financial imposts, timing delays and uncertainty. These costs are disproportionately burdensome for smaller businesses. The special sector designation also puts private sellers at a significant disadvantage relative to public companies in competitive processes and will reduce the options available to private vendors of businesses, including private capital providers.

For these reasons, if the proposed cumulative turnover threshold is indeed implemented, we would strongly argue that, as for the 12-month review of the monetary thresholds, a similar review is conducted to assess the impacts of the policy setting.

The Council is also concerned about the treatment of platform acquisitions, almost all of which will exceed the cumulative provisions and will require notification to the ACCC. This would be a perverse outcome given there typically intentionally no overlap between platform acquisitions for PE funds given they seek diversification, rather than market concentration.

Exemption for goodwill protection on sale of business

Under s51(2)(e) of the CCA, in relation to the sale of a business, an agreement to restrict competition by the seller in respect of the business it is selling to the purchaser is exempt from the anticompetitive conduct prohibitions of Part IV of the CCA, including the cartel conduct prohibitions, if the restriction is solely for the purpose of the protection of the goodwill of the business acquired by the purchaser.

Under proposed s51ABZG(1) to (3) of the CCA, the Commission would have power to declare that the exemption does not apply if it considers that the provision is not necessary for the protection of the purchaser under the contract in respect of the goodwill of the business.
Non-competes in relation to a sale of a business are fundamental to the contractual bargain. If there were a risk that a seller could the next day open a rival business next door, the purchase price would be significantly diminished.

The proposed shift to allow the ACCC to determine the lawfulness of a sale of business restraint would be a dramatic departure from well-established practice, where a Court would make such a determination, and where companies are advised by their lawyers as to the appropriateness of the scope of the non-compete based on the case law. This is particularly so given the close relationship between the common law restraint of trade doctrine and s 51(2)(e) of the CCA. It

would be a perverse result where the same contractual provision was concurrently subject of judicial and ACCC scrutiny. It is unclear what the rationale is for conferring this power on the ACCC, but it is respectfully submitted that this proposal is inappropriate and will undermine the certainty that contracting parties have based on case law as to the lawfulness of a non-compete.

Surprise hostile takeovers

The Council welcomes the introduction of a confidential review process in respect of surprise hostile takeover bids involving the acquisition of shares in a target company. However, with respect to the proposal that the matter be listed on the public register 17 business days after notification, the Council is concerned that there is no provision to enable an extension to the confidentiality where it may be necessary to further consider the potential takeover. This may occur, for example, if while the ACCC was reviewing, the market changed significantly, and it became necessary for the potential buyer to allow markets to stabilise before proceeding. In this context, 17 business days may be too short. The Council considers that the legislation requires greater flexibility to allow for an extension to this period if it became necessary.