
# Review of the Australian Competition and Consumer Commission 1995-96 Annual Report

Report from the House of Representatives Standing Committee on Financial Institutions and Public Administration

June 1997

The Parliament of the Commonwealth of Australia

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# FOREWORD

This examination of the Australian Competition and Consumer Commission's 1995-1996 annual report is the first of a series of reviews which the Committee will conduct each year.

Through this process the Committee intends to provide an accountability mechanism whereby the role and function of the Australian Competition and Consumer Commission (ACCC) can be monitored. It will also provide an opportunity for the oversight of issues and developments in the trade practices and prices surveillance areas, and in the regulation of market place competition.

This report focuses primarily on the ACCC's administration of the Trade Practices Act in the mergers area, in particular, the ACCC's use of administrative undertakings. The issues raised in this context also have relevance to the ACCC's administration of the Trade Practices Act and competition policy more generally.

I thank members of the Committee for their valuable assistance in the conduct of the review and in the preparation of this report. The Committee extends its appreciation to the ACCC for its support and assistance.

David Hawker MP
Chairman

# MEMBERS OF THE COMMITTEE

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# TERMS OF REFERENCE

The Standing Committee on Financial Institutions and Public Administration is empowered to inquire into and report on any matters referred to it by either the House or a Minister including any pre-legislation proposal, bill, motion, petition, vote or expenditure, other financial matter, report or paper.

Annual reports of government departments and authorities tabled in the House shall stand referred to the relevant committee for any inquiry the committee may wish to make. Reports shall stand referred to committees in accordance with a schedule tabled by the Speaker to record the areas of responsibility of each committee.

# RECOMMENDATIONS

1 That the ACCC investigate mechanisms whereby the process of accepting s.87B undertakings in merger cases can be made more transparent and that the ACCC report on this investigation to this Committee at a public hearing when the Committee reviews the ACCC's 1996-97 annual report.

2 That the Treasurer initiate a study of the extent to which the benefits of competition are flowing to rural and regional Australia.

3 That the ACCC give a higher priority to monitoring and evaluation of the impact of its merger decisions on market competition and that the ACCC report on its findings on a regular basis.

4 That the Treasurer consult with business and industry, the community and the ACCC to ascertain an appropriate means by which the general impact on competition and benefits to the community, of the ACCC's merger decisions, could be reviewed over the medium to long term.

# CHAPTER 1

# INTRODUCTION

1.1 The House of Representatives Standing Committee on Financial Institutions and Public Administration has, for some time, conducted reviews of major financial institutions. Previous reviews have demonstrated the benefits of regular annual reviews of the roles and responsibilities of such agencies. The Committee considers that continued parliamentary oversight of developments and issues with regard to financial institutions and other agencies that make up Australia's financial and economic regulatory framework will make an important contribution to public debate and policy making. The opportunity afforded by this review to discuss issues of current concern with the Australian Competition and Consumer Commission (ACCC) is also important from a public accountability perspective.

1.2 It is timely that the review canvass issues raised in the ACCC's first annual report. This is occurring at a time when wide ranging micro-economic reforms are being implemented across all sectors of the Australian community. It is therefore especially pertinent that the roles and functions of the national regulatory agency with major responsibility for implementing aspects of these reforms be reviewed. The ACCC review complements the Committee's other work on competition policy.

1.3 The authority for the Committee to inquire into matters arising from the ACCC's annual report derives from standing order 28B(b) whereby the ACCC's annual report stands referred for any inquiry the Committee may wish to undertake. At a meeting on 27 February 1997, the Committee resolved to examine the ACCC's 1995-96 annual report.

1.4 While this examination is a public process, it is not intended to be as comprehensive as an inquiry into a specific reference. The review is not advertised and written submissions are sought only from those organisations directly involved in the review process. The Committee regards this process as a means of monitoring a wide range of issues. If a particular matter gives cause for serious concern, the Committee has the option of following it up next year, or seeking a specific reference to conduct a more detailed inquiry.

1.5 The Committee resolved to examine the ACCC's annual report following concerns raised with a number of members about the processes and procedures used by the ACCC in relation to mergers and section 87B undertakings[1]. This was considered particularly relevant since, during the first year of its operation, the ACCC had been at the forefront of major, and at times, controversial decisions affecting Australian business and industry. The Committee was also aware of a body of business and industry concern over merger matters. The Committee wished to explore these issues with the ACCC on the public record.

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1 Trade Practices Act 1974, AGPS, Canberra, July 1996, p. 181.

1.6 This report, therefore, focuses primarily on the ACCC's administration in the mergers area, although the issues raised in this context also have relevance to the ACCC's administration of the Trade Practices Act and competition policy more generally.

1.7 The concluding chapter of this report briefly summarises a number of other issues arising from the consideration of the ACCC's annual report which were canvassed at the public hearing.

# CHAPTER 2

# ESTABLISHMENT OF THE AUSTRALIAN COMPETITION AND CONSUMER COMMISSION

## Background

2.1 The Australian Competition and Consumer Commission is one of the key national bodies at the forefront of micro-economic reforms designed to strengthen Australia's economic growth and performance. Together with the establishment of agencies such as the Productivity Commission and the National Competition Council, the ACCC functions to support measures designed to enhance market competition, improve economic growth and return benefits to the community. It has a major role as a competition regulator.

2.2 As stated in the 1995-96 annual report, the ACCC:

> ... seeks to improve competition and efficiency in markets, foster adherence to fair trading practices in well informed markets, promote competitive pricing wherever possible and restrain price rises in markets where competition is less than effective. [1]

2.3 The ACCC began operation on 6 November 1995 as a consequence of reforms set out in the Competition Policy Reform Act 1995. The structural and legislative framework for these competition reforms comprised:

- the establishment of the ACCC, formed by the merger of the Trade Practices Commission and the Prices Surveillance Authority;
- the establishment of the National Competition Council, to advise and report on national competition policy and its implementation;
- prohibition of anti-competitive conduct was extended to cover all businesses in Australia, including bodies such as unincorporated businesses and State and Territory government business enterprises;
- a timetable for review and reform of Commonwealth/State/Territory legislation that restricts competition; and
- third party access to the services of essential facilities of national significance, such as electricity grids or natural gas pipelines, was facilitated through the introduction of a legislative regime.[2]

2.4 A significant feature of this reform package was that the provisions of the Trade Practices Act were to be extended to areas which had otherwise been quarantined, such as government business enterprises, professional organisations and small business sectors. This reflected the intent of the reforms which was to achieve fair competition in all markets

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1 Australian Competition and Consumer Commission, Annual Report 1995-1996, AGPS, Canberra, 1996, p. xv.

2 ibid., p. 8.

throughout Australia, with uniform rules and rights for all consumers and businesses applying throughout the whole economy.

## Functions and powers

2.5 The ACCC is a statutory authority responsible for ensuring compliance with Parts IV, IVA, V & VA of the Trade Practices Act and the provisions of the Competition Code as enacted by the states and territories, and for administering the Prices Surveillance Act. The principal responsibility of the ACCC is the enforcement of the Trade Practices Act.[3]

The main compliance functions of the ACCC are:

- investigating complaints and market behaviour for breaches of both restrictive trade practices and consumer protection provisions;
- assessing the detriment to business and consumers of anti-competitive conduct;
- taking appropriate administrative or court action; and
- dealing with applications by business for exemption, through the authorisation and notification processes, from certain of the restrictive trade practices provisions of the Trade Practices Act.[4]

2.6 The annual report emphasises the priority given by the ACCC to educative and administrative resolution of matters without recourse to costly and time consuming litigation where possible. It also notes that an integral part of the ACCC's enforcement function is its efforts to improve general understanding of the law and the rights and obligations which flow from it.[5]

## New Environment/ New Work

2.7 The annual report emphasises that the ACCC now has a wider role than previously - with responsibilities in new sectors, such as telecommunications, electricity, gas, water, the professions, and local government.

2.8 The annual report refers to an increase in enforcement activities, and that the ACCC's role has become much more demanding with the increased range of sectors within which it must operate. These raise complex competition and public benefit issues, including the effectiveness and efficiency of competition in the delivery of goods and services. Changes in information technology have also created more complex products, different marketing and distribution techniques, which present new challenges.

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3 ibid., p.10. In order to improve compliance with the law, the ACCC also devote resources to education and information programs designed to improve community awareness of the requirements of the Trade Practices Act. See annual report, p. 295.

4 ibid., p. 295.

5 ibid., pp. 2,10,11.

2.9 In response to this wider brief, the ACCC reports that it has recognised the need to sharpen its focus on core business, which it sees as enforcement and administration of the law.[6]

2.10 While the ACCC sees that its primary focus is that of law enforcer, it is actively involved in pro-competitive micro-economic reform processes.[7] Its approach is described as pre-emptive with an emphasis on informing new sectors about their rights and obligations.[8] Underlying all of the ACCC's work are the related themes of competition and public benefit.[9] The ACCC sees that it has a long term role in promoting and preserving competition, and safeguarding consumers.[10]

## Promoting competition, and safeguarding consumers

2.11 The annual report highlights the social justice principles underlying the Trade Practices Act and the Prices Surveillance Act. It emphasises that positive outcomes and benefits for consumers are the ultimate goals of the law and of the ACCC's role in implementing it. The Chairman of the ACCC, Professor Allan Fels has stated that underlying the formal functions of the ACCC:

> ...is an ulterior objective: to enhance the material welfare of Australians by promoting, wherever practical, a more competitive and efficient economy.

indeed he views the ACCC as:

> ...the public guardian against anti-competitive or unfair business activities. [11]

2.12 Consumer bodies, such as the Australian Consumers Association have recognised the ACCC's strong consumer stance:

> They've been extraordinarily efficient ... One of the important features of the ACCC is that it's willing not to fire shots over the bow. It is prepared to start proceedings and tell industry, 'You'll lift your game and you'll do it fast.' The ACCC gets results. [12]

2.13 The ACCC's pro-consumer stance has, in some business quarters, been perceived as anti-business; a criticism no doubt aggravated by court action taken by the ACCC which has

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6 Evidence p. 4.
7 ACCC, op. cit., p. 6.
8 ibid., p. 11.
9 Evidence p. 4.
10 Allan Fels, *The Australian Competition and Consumer Commission and the New Regime*, Australian Journal of Public Administration, Vol 55 No 2, June 1996, p. 74.
11 ibid., p. 74.
12 Louise Sullivan, Executive Director, Australian Consumers Association, quoted in Natasha Bita, *Office Spies*, The Australian, Nov 12 1996.

resulted in large penalties being imposed on companies breaching the Trade Practices Act, and some controversial merger decisions.[13]

2.14 A body of criticism surrounding the ACCC's activities has come from 'the big end of town' industry and business interests who believe that the ACCC has too much power and influence, especially in the areas of mergers and acquisitions. A related criticism is that the ACCC applies the law too severely, and should take a more lenient approach.[14]

2.15 Chapter 3 of this report examines aspects of the ACCC's administration of the Trade Practices Act with respect to mergers, and explores some of the issues that have recently been the subject of public debate and concern.

13 See: David Forman and Lucinda Schmidt, *The most powerful official in the land*, Business Review Weekly, June 10 1996; Malcolm Maiden, *Equaliser*, Sydney Morning Herald, October 5 1996; and Bruce Jacques, *Too much bark, not enough bite*, The Bulletin, November 21 1995.

14 See: Australian Petroleum Agents & Distributors Association, *Undertakings Accepted Under s.87B of the Trade Practices Act: Making the Australian Competition and Consumer Commission Accountable*, October 1996; Forman and Schmidt, op. cit.; 7.30 Report, *ACCC rejection of Wattyl merger draws criticism from the business community*, September 10 1996; Maiden, op. cit.; Harry Wallace, *Painted into a corner*, The Age, March 20 1996; Mark Westfield, *Banks will find interesting precedents in Davids-QIW merger*, The Australian, March 30 1996; and Mark Westfield, *Banking, telecom upheavals put spotlight on Fels' power*, The Australian, February 6 1997.

# CHAPTER 3

# MERGERS

## Background

3.1 As part of its role in preventing or limiting anti-competitive conduct, the ACCC examines and evaluates mergers.

3.2 Section 50 of the Trade Practices Act prohibits mergers and acquisitions that are likely to substantially lessen competition in a substantial market for goods and services in Australia, in a state or in a territory.[1] The rationale for government intervention in the area of mergers is noted in the Attorney General's second reading speech at the time of amendments to section 50 of the Trade Practices Act:

> Merger regulation is an important element of any law aiming to preserve levels of competition. Mergers can lessen competition, potentially providing increased scope for price rises or collusive behaviour and lessening dynamic factors such as the rate of innovation. These possible detriments provide the rationale for government intervention in the area of mergers.[2]

3.3 The Trade Practices Act sets out nine non-exclusive factors which must be taken into account in judging whether a proposed merger will result in a substantial lessening of competition:

- the actual and potential level of import competition in the market;
- the height of barriers to entry to the market;
- the level of concentration in the market;
- the degree of countervailing power in the market;
- the likelihood that the acquisition would result in the acquirer being able to significantly and substantially increase prices or profit margins;
- the extent to which substitutes are available in the market or are likely to be available in the market;
- the dynamic charactertistics of the market, including growth, innovation and product differentiation;
- the likelihood that the acquisition would result in the removal from the market of a vigorous and effective competitor; and
- the nature and extent of vertical integration in the market.[3]

3.4 The Trade Practices Act does not give a relative weighting to these factors, and they are generally considered relevant to a competition analysis in a merger case.

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1 ACCC, Summaries of the Trade Practices Act and the Prices Surveillance Act, AGPS, Canberra, November 1995, p. 28.

2 Quoted in ACCC's Merger Guidelines, ACCC, July 1996, p. 24.

3 ACCC, November 1995, op. cit., pp. 28-29.

3.5 The ACCC's revised Merger Guidelines translate these factors into a five step approach for evaluating mergers in terms of the substantial lessening of competition test:

- market definition;
- concentration thresholds;
- import competition;
- barriers to entry; and
- other structural and behavioural market features. [4]

3.6 If the ACCC considers that a merger is likely to be anti-competitive it can seek to block the merger by seeking an injunction in the Federal Court of Australia, where it must prove to the Court that the merger is likely to substantially lessen competition. The decision of the Court may be appealed to the full Federal Court.[5]

3.7 Mergers, which may be anti-competitive, can be authorised by the ACCC (see section 3.29 below). Authorisation determinations can be reviewed through the Australian Competition Tribunal. Some merger negotiations are resolved through the process of administrative undertakings (see section 3.41 below).

3.8 According to the ACCC the following procedure, with respect to merger considerations, normally occurs:

- most parties notify the ACCC in advance (in confidence) of mergers;
- the ACCC normally reserves its decision until the merger is publicly announced;
- mergers considered by the ACCC are typically border line;
- if the ACCC has no objections the merger may proceed; and
- if the ACCC has concerns, there is a further period during which parties put their views to the Commission.

If the ACCC considers the merger is anti-competitive the following options exist:

- the parties discontinue;
- the parties provide undertakings (see section 3.41 below) to overcome the anti-competitive concerns;
- the parties disagree with the ACCC's views and proceed with the merger. The ACCC then normally seeks an injunction and must prove to the Court's satisfaction that the merger would substantially lessen competition; and
- the parties may seek authorisation.[6]

3.9 In 1995-96 the ACCC considered 149 new merger proposals. According to the annual report most did not require detailed competition assessment. Eight were not proceeded with or were amended. Two determinations granting authorisations for mergers were issued during the year (Du Pont/Ticor and Davids/QIW). In two cases the ACCC undertook court action to block mergers (Wattyl/Taubmans and Howard Smith/Adelaide Steamship,Waratah Towage).

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4 ACCC, July 1996, op. cit., p. 29.

5 Allan Fels, *Competition and the Financial System: the ACCC View,* Companies and Securities Bulletin, No 161, October 1996, p. 7.

6 ibid., pp. 6-7.

Three merger negotiations were resolved by the parties giving undertakings (Mobil/Amgas, Port of Portland, Port of Geelong).[7]

3.10 The ACCC emphasised that it opposes only a small number of mergers a year, but that those generate a high level of interest:

> Whenever the Commission ticks something, nothing is said, but on the occasions when we oppose something, everything is said.[8]

The ACCC observed that this was also the case in the past, under the Trade Practices Commission:

> Mergers are always controversial; there is always criticism, no matter who is around. [9]

3.11 The ACCC has published guidelines about its administration of the merger provisions. Professor Fels has stated that the guidelines:

> ... reflect standard international practice which in turn reflects criteria developed by the world's leading industrial organisation economists and antitrust regulators over the years.[10]

## Issues and industry/business response

3.12 The Industry Commission has expressed a number of concerns about the way in which the ACCC deals with mergers and its administration of the substantial lessening of competition test.[11] The Business Council of Australia also believe that the ACCC blocks too many merger proposals. Its position is that Australian companies need to build a big enough critical mass to compete on the international market.[12]

3.13 There has been concern expressed from organisations such as the Industry Commission, the Business Council of Australia, the National Australia Bank, the Australian Chamber of Commerce and Industry, the Australian Food Council and the Australian Owned Companies Association that the ACCC has not given enough weight to economic globalisation in its merger considerations.[13]

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7 ACCC, Annual Report 1995-1996, AGPS, Canberra, 1996, pp. 42-43.
8 Evidence, p. 13.
9 Evidence, p. 30.
10 Fels, October 1996, op. cit., p. 7.
11 Industry Commission, Merger Regulation: *A review of the draft merger guidelines administered by the Australian Competition and Consumer Commission*, Information Paper, Canberra, June 1996.
12 7.30 Report, *ACCC rejection of Wattyl merger draws criticism from the business community,* September 10 1996.
13 See: Industry Commission, op.cit.; David Forman and Lucinda Schmidt, *The most powerful official in the land*, Business Review Weekly, June 10 1996; 7.30 Report, op. cit; Malcolm Maiden, *Equaliser*, Sydney Morning Herald, October 5 1996; and Harry Wallace, *Painted into a corner*, The Age, March 20 1996.

3.14 Sir Ron Brierley has claimed recently that the ACCC's approach to mergers is causing inefficiencies in Australian companies; that overseas companies are growing bigger and better organised, and that Australian companies are missing out.[14]

3.15 In a recent comment on this type of criticism, Professor Fels has argued that:

- the Trade Practices Act itself does not prevent firms achieving the economies of scale necessary to be internationally competitive;
- the ACCC has not opposed any mergers in the past five years where imports are significant; and
- even where there are no imports, the ACCC opposes relatively few mergers.[15]

3.16 During the review, Professor Fels reiterated these remarks and advised that the ACCC's revised Merger Guidelines attempt to recognise the impact of globalisation. The ACCC's revised Merger Guidelines recognise the increased exposure of business to global markets. They adopt an indicative position of not opposing mergers where a sustained and competitive level of imports exceeds 10 percent of the market.[16]

## Concentration thresholds

3.17 The Industry Commission argued that the ACCC looks at too many mergers, resulting in excessive administrative costs and discouragement of efficient mergers. The Industry Commission argued that the ACCC should raise its concentration threshold, which is used to screen out mergers which are unlikely to substantially lessen competition, to reduce the number of mergers which are considered by the ACCC.[17]

3.18 There is some debate about what constitutes an appropriate concentration threshold figure, with for example, the USA, Canada, New Zealand and Europe each adopting different threshold levels for a variety of reasons.[18]

3.19 Staff of the ACCC's Mergers and Asset Sales Branch, in a recent Competition and Consumer Law Journal article, argue that in the Australian context the current figure is appropriate; and that there is a risk that the ACCC would be failing in its statutory

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14 Philip Rennie, *Companies ripe for takeover*, Business Review Weekly, October 14 1996.

15 Fels, October 1996, op. cit., p. 10.

16 Evidence pp. 12-13, and p. 30.

17 The Industry Commission suggested replacing the current thresholds of a 75% four firm concentration ratio or a merged firm share of 40%, with a 75% three firm concentration ratio or a merged firm share of 50%. Currently, if the top four firms have less than 75% market share the ACCC does not investigate further except that if one firm has 40% or more of the market following a merger the ACCC would consider it for investigation. In other words below certain market shares the ACCC does not consider mergers.

18 See discussion in: Warwick Anderson, Tim Grimwade, Jill Walker, and Luke Woodward, *Merger Misconceptions: the Industry Commission's Paper on the ACCC's Draft Merger Guidelines*, Competition and Consumer Law Journal, Vol 4 No 2, December 1996, pp. 132-139.

responsibilities if the thresholds were set so high as to miss mergers which might breach the Trade Practices Act.[19]

3.20 Anderson et al cite examples of where increased thresholds would have presented such a risk had they been in place:

> It is possible that another merger with a market structure similar to that in the WA banking market could arise, but unlike the Westpac/Challenge case it would be likely to substantially lessen competition; raising the thresholds as suggested ...may preclude the ACCC from performing its statutory duty. Indeed a merger between any four major trading banks would not be examined under the proposed thresholds. Other examples of mergers and joint ventures which would not have been examined under the proposed thresholds are BA/Qantas, Dulux/Berger/British paints and Ampol/Solo petrol.[20]

3.21 The ACCC is concerned that the proposed Industry Commission thresholds are too generous:

> We would not have looked at mergers between the big four banks on that basis. We would not have looked at mergers between the five oil companies; that is, we would not have looked at Ampol/Caltex. We certainly would not be looking at a little thing like the Bank of Melbourne and Westpac - any of that sort of thing. So we are concerned as to whether their threshold is not a bit high, a bit generous. After all, all we are talking about is having a look at mergers, and we think it is generally a fairly low cost process for looking at mergers.
>
> ...Supposing...the big four banks got together. Under their guidelines, we would not have looked at it...That guideline makes us worried. I can understand the Industry Commission saying, 'We feel perfectly relaxed about the big four banks getting together or all the oil companies merging.' I can see that, but I cannot quite see the argument as to why a regulator should not spend a few minutes having a look at those mergers.[21]

3.22 Notwithstanding these reservations, the ACCC has undertaken to monitor the potential effects of replacing the current thresholds with those proposed by the Industry Commission in relation to mergers during 1996-97:

> We have decided that for the next year or so we will test the Industry Commission test. We will test ours, and then we will report publicly on how they work.[22]

3.23 At the time of the review the ACCC advised that it was too early to report on the results of this process.

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19 ibid.
20 ibid., p. 139.
21 Evidence pp. 13-14.
22 Evidence p. 13.

## Market definition

3.24 The Trade Practices Act requires that the assessment of substantial lessening of competition be related to a market. A market involves four dimensions - product, geographic, functional, and time.[23] Market definition is important for the evaluation of proposed mergers because it sets the context in which the analysis of competitive effects takes place.

3.25 The Industry Commission endorsed ACCC's general approach but suggested that a broader approach to market definition would be preferable.[24] Professor Bob Baxt, previous chairman of the Trade Practices Commission, has commented that the ACCC's definitions of markets are nearly always too narrow.[25] The initial opposition to the Ampol/Caltex merger, and the blocking of the Wattyl/Taubman's merger are often cited as examples of the ACCC's overly restrictive definitions of markets.[26]

3.26 The Industry Commission and some business/industry representatives and commentators have also claimed that the ACCC is inconsistent in its approach to market definition. The Davids/QIW case and the Westpac/Challenge banking merger are cited as examples of where two different conceptions of geographic market definition have been applied.[27]

3.27 The ACCC argues that, judging that banks, for example, operate in a state or regional market and that groceries operate in a national market does not reflect inconsistency in market definition, but rather reflects the realities of different industries. Anderson et al [28] claim that the inconsistency argument is incorrect, and also point out that in the Davids/QIW authorisation, market definition was not a key factor, nor has it been critical in many of the ACCC's prominent merger decisions (eg CSR/Mackay, Caltex/Ampol, Wattyl/Taubmans). [29]

3.28 The ACCC points out that in the Westpac/Challenge banking merger, the ACCC recognised that the market conditions in which that decision was made would not hold true for all time, and that future judgements about market definition would need to reflect industry and market changes:

> ...We said that that was the view we take - at this time...The reason we said that was that we were aware of the rapid structural change going on in the financial

23 ACCC, July 1996, op. cit., p. 31.
24 Industry Commission, op. cit.
25 Forman and Schmidt, op. cit.
26 See: Maiden, op. cit.; and Rennie, op. cit.
27 See: Industry Commission, op.cit.; Forman and Schmidt, op. cit.; Maiden, op. cit.; and Mark Westfield, *Banks will find interesting precedents in Davids-QIW merger*, The Australian, March 30 1996.
28 Anderson et al, op. cit., pp. 130-132.
29 More recently Davids Ltd's executive chairman has accused the ACCC of 'moving the goal posts' to allow Woolworths Ltd into the wholesaling market. He claims that the ACCC had previously ruled that wholesaling and retailing were the one market for the purposes of making a decision on the Davids' acquisition of QIW, and now was defining the markets as separate. See: Finola Burke, *David attacks ACCC 'logic'*, Financial Review, March 12 1997.

> services sector. We wanted to leave open the possibility that we might have to revisit some of these issues.[30]

## The authorisation process

3.29 The ACCC has power under the Trade Practices Act to grant immunity from legal action for market conduct that might otherwise breach the restrictive trade provisions of the Trade Practices Act.[31] The authorisation process provides the ACCC with the power to authorise proposed mergers and certain anti-competitive conduct. In general, the ACCC is empowered to grant authorisation only where it believes that the conduct or merger in question delivers public benefits.[32]

3.30 The Australian law differs from that in the USA which simply prohibits anti-competitive mergers. In Australia, in recognition of the fact that it is a small economy, mergers which are anti-competitive are allowed, if there is sufficient public benefit.[33]

3.31 The ACCC applies the following test when considering an application for authorisation:

- for mergers and acquisitions the applicant must satisfy the ACCC that the conduct results in a benefit to the public such that it should be allowed to occur.[34]

3.32 The concept of public benefit is not defined in the Trade Practices Act, and is based on assessments made in previous cases. The ACCC's revised Merger Guidelines cite a number of examples of public benefits that have been recognised to date:

- fostering business efficiency
- industry rationalisation
- employment growth
- industry cost savings resulting in lower consumer prices
- competition in industry
- equitable market dealings
- growth in export markets
- import replacements
- economic development eg exploration, research
- assisting small business
- industrial harmony
- improvement in quality and safety of goods and services
- improved consumer information [35]

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30 Evidence p. 15.
31 ACCC, November 1995, op. cit., p. 30.
32 There is also a process called 'notification' for exempting, on public benefit grounds, exclusive dealing conduct.
33 See: Fels, October 1996, op. cit., p. 10.
34 ACCC, November 1995, op. cit., p. 31.

3.33 In merger authorisations the ACCC is required to consider as public benefits - in addition to other potential public benefits - significant increases in the real value of exports and significant substitution of domestic products for imported goods; and is also to take into account all relevant matters that relate to the international competitiveness of Australian industry.[36]

3.34 The annual report notes that authorisation is a very public process.[37]

Under the Trade Practices Act the ACCC is required to:

- make public the receipt of applications for authorisation; and to accept and consider any submissions made by the applicant or any other interested party;
- prepare a draft determination prior to making its determination to accept or reject an application for authorisation; and to invite the applicant and any other interested parties to participate in a pre-decision conference. ( NB excluding mergers); and
- keep a register of applications for authorisations. This register is to include all documents furnished to the ACCC, draft determinations, records of conferences, and copies of determinations and the statements of reasons for determinations. Confidentiality may be granted for commercially sensitive material.[38]

Interested parties may apply to the Australian Competition Tribunal for a review of an ACCC decision.[39]

## Public benefit

3.35 There has been lively criticism from industry/business sectors and the Industry Commission that the authorisation process lacks transparency and is not working effectively. Some of this criticism is directed at how the ACCC applies and assesses the public benefit test. Critics have also argued that the ACCC's approach is unbalanced, favouring consumers over producers, giving insufficient weight to production efficiencies.[40]

3.36 Professor Fels has said that the ACCC gives weight to the private benefits a proposed merger would deliver to the companies involved, but that the public benefit test is essentially

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35 ACCC, Guide to Authorisations and Notifications, ACCC, November 1995, p. 20.
36 ibid., p. 21.
37 ACCC, Annual Report, op. cit., p. 37.
38 ACCC, Summaries of the Trade Practices Act and the Prices Surveillance Act, AGPS, Canberra, November 1995, p. 31.
39 ibid., p. 31.
40 See: Industry Commission, op. cit.; Forman and Schmidt, op. cit.; R Officer and P Williams, *The Public Benefit Test in an Authorisation Decision*, in M Richardson and P Williams (eds), The Law and the Market, Federation Press, 1995; and Sandra Navalli, *Australia's Merger Policy and the Caltex/Ampol Merger Case*, Agenda, Vol 3 No 3, 1996.

an economic efficiency test. He says that typically in merger authorisation cases competition and benefit issues are considered simultaneously and are usually linked.[41]

3.37 Anderson et al comment that recent ACCC decisions and the revised Merger Guidelines place greater emphasis on production efficiencies, even where these are unlikely to be passed through in lower prices. They also claim that the ACCC's Merger Guidelines should not attempt to define public benefit:

> ...it would be inappropriate for the ACCC to draft a prescriptive code, where the parliament has deliberately avoided doing so.[42]

3.38 They argue for a wide, rather than narrow interpretation, of what may constitute public benefit. They go on to cite the Du Pont/Ticor and Wattyl/Taubman's cases where the ACCC accepted that there were significant environmental benefits associated with the proposed acquisitions.[43]

3.39 There is significant debate in the literature and the field as to what standard should be applied in evaluating public benefit. Anderson et al point to the recent debates in the USA as an example of the complexity the issue.[44]

3.40 It should be noted that the application of the public benefit test only arises in authorisation cases,[45] that is, where exemption is sought for conduct which would be contrary to the competition provisions of the Trade Practices Act:

> ..it needs to be understood that these tests [ie the ACCC's five step process for assessing substantial lessening of competition] only apply in relation to the competition issue, not in relation to questions which arise if a firm or firms seek authorisation.
>
> ...much of the popular discussion about the possible benefits of bank mergers relates to authorisation considerations. The benefits in terms of branch rationalisation are probably most relevant to claims that bank mergers would lead to substantial public benefits (of course this is not to deny that certain sorts of cost savings can also stimulate competition as ACCC guidelines and other cases over the years have recognised). But the Commsission's much publicised pronouncements and decisions thus far on bank mergers have turned on Section 50 issues. The Commission has not considered any authorisation issues. This is sometimes a source of misunderstanding. [46]

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41 See: Allan Fels, *The Australian Competition and Consumer Commission and the New Regime*, Australian Journal of Public Administration, Vol 55 No 2, June 1996; and Fels, October 1996, op. cit.

42 Anderson et al, op. cit., p. 146.

43 ibid., p. 146.

44 ibid., p. 147.

45 It also applies in notification cases. See footnote 32 above.

46 Fels, October 1996, op. cit., p. 7.

## Section 87B Undertakings

3.41 The annual report notes that:

> As part of its overall enforcement strategy the Commission has in the past sought undertakings from businesses that they will cease particular conduct or undertake specific action to redress action that may have breached the Act.[47]

Section 87B of the Trade Practices Act provides for the legal enforcement of undertakings by the Court.[48]

3.42 Such undertakings may be withdrawn or varied, but only with the consent of the ACCC. There is no provision in the Trade Practices Act for a right of appeal (with respect to the ACCC's determinations for withdrawal or variation of an s.87B undertaking) to the Tribunal or the Court, although there are some possible avenues for judicial review.[49]

3.43 The annual report also notes that:

> ...the available benefits are not specifically prescribed or limited by the law - in each case it is a matter for negotiation leading to undertakings appropriate to the circumstances.[50]

Examples cited of undertakings include: financial compensation, corrective advertising, a commitment to internal programs to improve management and staff understanding of the law's requirements. Most undertakings are not in the mergers area. In 1995-96 the ACCC accepted 34, s.87B undertakings; 3 of which were for mergers.

3.44 The ACCC has accepted undertakings from parties to an acquisition to resolve matters where the proposed acquisition is, in the ACCC's view, likely to contravene the Act.[51]

> In these circumcstances, the offer of such an undertaking designed to address the competition concerns is a matter for strategic decision by the parties to the acquisition, and presumably will be considered along with other options open to the parties, for example challenging the Commission in Court, seeking authorisation, revising the proposal without undertakings, or even abandoning the proposal.[52]

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47 ACCC, Annual Report , op. cit., p. 296.
48 ACCC, Summaries of the Trade Practices Act and the Prices Surveillance Act, AGPS, Canberra, November 1995, p. 66.
49 See: A Tonking and L Castle, *Mergers: The Use and Utility of Undertakings*, Trade Practices Law Journal, Vol 1, March 1993.
50 ACCC, Annual Report, op. cit., p 10.
51 ACCC, July 1996, op. cit., p. 70.
52 ibid., p. 70.

## Issues and industry/business comment

3.45 The extent of the ACCC's discretionary power in the area of undertakings has drawn criticism from the Industry Commission and industry/business interests.[53]

3.46 The concerns are that the Trade Practices Act provides the ACCC with unfettered power to make and impose enforceable undertakings, and that this power is widely used to restructure industries, and without any requirement that details of these undertakings be made available on the public record as authorisations are. The Caltex/Ampol merger is cited as an example of where the ACCC has shaped industries into its preferred models; in that case to reshape the petrol retailing market.[54]

3.47 The ACCC explains that when faced with this proposed merger, that was likely to breach the Trade Practices Act, ie it was considered anti-competitive; the ACCC had three options - to block the merger, to allow it to proceed, or to accept undertakings to amend the proposal to avoid any breach of the Trade Practices Act:

> We could have just dug in and said, 'This merger is not on, we're opposing it,' or we could have sat back and let it happen, and it would have been anti-competitive...we told Ampol/Caltex, 'We are of the view that this is an anti-competitive merger and should not be allowed under section 50.'...They then contacted us and said, 'Is there anything we can do to overcome your concerns?' We said, 'We don't know, but we are happy to explain our concerns. 'So we then had a long talk with them and went through a whole list of our concerrns, which were published and had been in a press release, but we explained them more fully. They said, 'All right, we will go away and see if we can come up with something that will address those concerns.'...
>
> We believe that was the best outcome because the arrangements, looked at from the point of view of the public, preserve competition, have done some things of benefit in the longer term to rural areas and have, at the same time, allowed the benefits of the merger to occur. We reckon that was better than the alternatives, and it was done fairly quickly under the undertakings process.[55]

3.48 In its paper on s.87B undertakings the Australian Petroleum Agents & Distributors Association (APADA) notes that there are no statutory guidelines in relation to the exercise of the ACCC's discretion in accepting undertakings and that the Trade Practices Act provides no mechanism or procedure for reviewing or otherwise making the ACCC accountable for its actions surrounding the acceptance of s.87B undertakings. Moreover third parties are not required to be consulted, nor can third parties seek a review of undertakings.[56]

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53 See: Industry Commission, op. cit.; Navalli, op. cit.; Australian Petroleum Agents & Distributors Association, op. cit.; and Forman and Schmidt, op. cit.

54 See: Navalli, op. cit.; Australian Petroleum Agents & Distributors Association, op. cit.; and Forman and Schmidt, op. cit.

55 Evidence p. 24.

56 Australian Petroleum Agents & Distributors Association, op. cit.

3.49 APADA asserts that this has potentially serious ramifications in relation to the administration of and enforcement of the Trade Practices Act; in particular Part IV:

> ...there is the danger that such undertakings will become de facto authorisations not subject to the same safeguards as the Act provides in relation to authorisations...

and

> ...there is no guarantee that the s 87B undertaking will be in the public benefit or that it will not adversely impact on third parties.[57]

APADA argues that undertakings should be reviewable by the Australian Competition Tribunal, as is the case for authorisations.

3.50 Anderson et al have responded to these types of criticisms. They point out that undertakings are not imposed by the ACCC, that they must be offered by the parties; and that this is often seen by those parties as an attractive alternative compared with the alternatives of court action or seeking authorisation. They note that as undertakings are only enforceable in the Court, that it is the Court which retains absolute discretion as to whether to grant orders to enforce the undertakings.[58]

3.51 With respect to public accountability for undertakings, although not required by the Trade Practices Act, the ACCC keeps a register of the details of undertakings, and according to the ACCC, it often consults extensively when considering an s.87B proposal; for example, the proposed undertaking in AWB/Graincorp and the actual undertaking in Davids/CBL and Ampol/Caltex.[59]

3.52 There is, however, no provision in the Trade Practices Act, nor in the ACCC's own procedures, for public notice to be given of s.87B considerations, as in authorisation matters, nor for formal conference procedures that apply in relation to authorisations for matters other than mergers.[60] In regard to s.87B cases, the ACCC commented that it makes a judgement as to whether a significant third party issue exists; that it consults where it believes there is a third party issue; and that third parties often approach the ACCC directly. The ACCC also commented that in some cases, such as the Ampol/Caltex undertaking, a number of third parties approached the ACCC with their concerns and that the ACCC is well informed about the oil industry's concerns because the ACCC is in almost daily contact with its representatives.[61]

3.53 The ACCC advises that s.87B undertakings do not function as de facto authorisations because authorisations exempt certain conduct, whereas undertakings do not.[62] Undertakings

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57 ibid., p. 2.

58 Anderson, et al, op. cit., pp. 148-149.

59 Submission Vol. 1, p. S 4; and Anderson, et al, op. cit., p. 150.

60 The provision of the Trade Practices Act which requires the ACCC to invite interested persons to notify the ACCC whether they wish the ACCC to hold a conference in relation to a draft determination of an authorisation application, does not apply to an application for authorisation of a merger. See: ACCC, Summaries of the Trade Practices Act and the Prices Surveillance Act, AGPS, Canberra, November 1995, p. 31.

61 Evidence p. 23.

62 Submission Vol. 1, p. S 4.

allow for conduct that would breach the law to be amended so that such a breach would not occur. The authorisation process allows such breaches to be made exempt if the public benefit outweighs any anti-competitive effect. What authorisation does is to give legal cover to what would otherwise be a breach of the Trade Practices Act. On the other hand, an undertaking does not give an exemption, nor does it prevent a third party from taking legal action under the Trade Practices Act alleging that the conduct infringes the Act.[63]

3.54 The issues canvassed with respect to s.87B undertakings and mergers in this review generally arise from concerns regarding the transparency of the ACCC's procedures, decision making processes and judgements. Whilst not required to by law, the ACCC reports that it often does consult with third parties during its consideration of undertakings; that a public register of s.87B undertakings is kept; and that the outcomes are published. The ACCC has advised that it is willing to consider more transparency for s.87B undertakings, but point to the need for confidentiality in the negotiation process, although the outcomes are made public.

63 See: ACCC, Summaries of the Trade Practices Act and the Prices Surveillance Act, AGPS, Canberra, November 1995.

# CHAPTER 4

# CONCLUSION

## Mergers

4.1 This report focuses primarily on the ACCC's administration in the mergers area, and represents a brief overview of some preliminary exploration of matters which the Committee was concerned to examine at this point in time. The review has drawn together, for brief consideration, some questions and concerns which had arisen in the public domain and which the Committee saw fit to address with the ACCC directly.

4.2 During the course of the review a number of important matters were clarified, in particular those associated with the ACCC's administration of mergers. It would appear that some level of confusion or misunderstanding about merger processes may exist in the public arena. It may also be the case that the concerns of business and industry groups, who have been the most vocal in their criticism of the ACCC's merger decisions, are in part a reflection of resistance to perceived government intervention. As the annual report observes:

> ...the implementation of competition policy involves major ongoing challenges, many of which reflect the paradox that government intervention is sometimes needed in order to achieve a free, competitive and efficient market - especially when, in the early phases of deregulation, incumbent firms possess considerable market power.[1]

4.3 The issues canvassed with respect to s.87B undertakings and mergers in this review generally arise from public accountability concerns regarding the transparency of the ACCC's procedures. The Committee views undertakings as a useful tool in administering relevant aspects of the Trade Practices Act and for ensuring that mergers are not anti-competitive. It does, however, have some concerns about the extent to which the undertakings process is transparent - although the Committee appreciates the need for confidentiality in some parts of this process. The Committee favours a more transparent approach than is currently the case with mergers and s.87B undertakings, and is pleased to note that the ACCC is willing to consider more transparency for s.87B undertakings.[2] The question of whether the administration of undertakings should be prescribed in more detail by the Trade Practices Act has not been covered in this review. Nor has the review examined the implications or effects of the ACCC's administration of undertakings in the mergers area in detail.

4.4 It would be appropriate for these matters to be considered in more detail in the context of the Committee's review of the ACCC's annual report for 1996-97 later this year.

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1 ACCC, Annual Report 1995-1996, AGPS, Canberra, 1996, p. 6.

2 Submission Vol. 1, p. S 5.

4.5 **Recommendation 1**

> **That the ACCC investigate mechanisms whereby the process of accepting s.87B undertakings in merger cases can be made more transparent and that the ACCC report on this investigation to this Committee at a public hearing when the Committee reviews the ACCC's 1996-97 annual report.**

## Competition and consumer benefits

4.6 A number of issues related to broader competition policy matters arose during the review. Two related themes emerged and are briefly summarised below.

4.7 With regard to the implementation of competition policy, there was some discussion about the apparent differential effects in the city and rural Australia. It is generally accepted that the benefits of competition, in particular, consumer benefits, are not being realised as strongly in rural areas as in the city. There is some concern amongst country consumers that there is a gap in the way that competition policies are being administered, with effective competition operating in the city, but not translating into the provision of the same benefits in rural areas. Petrol prices are an example of where this appears to be the case.[3]

4.8 The ACCC advised that there were a number of factors which effect the pricing of petrol in rural areas, resulting in higher prices than in city areas - transport costs, the costs of conducting business, and the fact that there is less competition in rural areas.[4]

4.9 The ACCC pointed out that the Trade Practices Act was applied in much the same way in the city as in rural areas; and that it was the underlying structure of the arrangements in the country that meant that the full benefits of competition had not been felt:

> The structure of markets in country areas is such that you tend to get less competition in them. We are not quite sure what to do there. If a market has a structure that is uncompetitive, what are the answers? Import competition is not really relevant in most of these cases. Busting up monopolies is fine for big monopolies in a town where we have those powers, but in smaller country areas you are not going to bust up businesses and get competition. Merger policy is not really relevant in country areas to any great extent. The players are just smaller and the structure is less competitive. There are fewer opportunities to compete with smaller markets. Although I think country people benefit from competition policy, you tend to get a more vigorous competitive market, because of structural reasons, in city areas. [5]

3 Evidence p. 7.
4 Evidence p. 7.
5 Evidence p. 7.

4.10 The ACCC did not believe that competition policy was not effective in rural Australia, but rather that:

> ...there is a general benefit but that it is bigger in the city than in rural areas. I do not see rural areas as a loser on balance from competition policy but as simply deriving a bit less of the benefit.[6]

Nor did the ACCC believe that the gap between city and country was any wider than in the past.[7] In the experience of Committee members this is not the case and the Committee is not satisfied with this explanation. The Committee will pursue the issue of competition and consumer benefits with respect to city/country petrol pricing, when it reviews the ACCC's annual report later this year.

4.11 One area where the ACCC saw that improvements in competition could be made, for petrol, was in the horizontal arrangements between oil companies. The ACCC advised that it was looking more closely at issues such as borrow and loan refinery exchange and joint terminal access arrangements between oil companies.[8]

4.12 The question of whether the benefits of competition were being passed on to consumers was also considered in the context of sugar and sugar product prices. For example, it could be expected that with greater competition in a particular market consumer prices would be reduced or price increases kept to a minimum. There is, however, some evidence that this has not been the case in the sugar industry. The ACCC advised that it was not aware of conclusive evidence that benefits were not being passed on to consumers, and advised that it would be exploring the issue further.[9]

4.13 **Recommendation 2**

> **That the Treasurer initiate a study of the extent to which the benefits of competition are flowing to rural and regional Australia**.

## Monitoring and evaluation of outcomes

4.14 The pursuit of competition is not an end itself, but is intended to contribute to the public good, to create more efficient markets, to improve the provision of goods and services, and bring about lower prices. With these objectives it is crucial that government, business and industry, and the general public can measure the extent to which these benefits are being realised, and whether the approaches being undertaken are working.

4.15 Evaluation of competition policy per se is not the task of the ACCC. However, to the extent that the ACCC implements aspects of competition policy, as embodied in the law, it can be expected to monitor and evaluate that work.

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6 Evidence p. 7.
7 Evidence p. 8.
8 Evidence pp. 9-10.
9 Evidence pp. 26-27.

4.16 Professor Fels has noted in a recent journal article that:

> The ACCC is aiming for a cumulative effect over many years. Although it has achieved some notable successes in its short existence, a real measure of the effectiveness of the Commission (and the new competitive regime) should not be attempted for quite a few years.[10]

4.17 Professor Fels commented during the public hearing that the ACCC has not generally devoted sufficient resources to the evaluation of outcomes:

> ...in organisations like ours there is always immense pressure on the organisation to deal with here and now problems. We keep saying to ourselves, ' Yes, it is important to evaluate outcomes ' and so on but, typically, we do not devote sufficient resources to evaluating outcomes.[11]

The ACCC has also suggested that lack of cooperation from the industry/business sector, and the long time frames required to see outcomes, are also factors.[12]

4.18 The ACCC does monitor some of its activities but with a focus on internal processes, rather than public outcomes.[13] It has commented that ideally it would see the evaluation processes focussing on the market place, but argues that this would be very expensive.[14]

4.19 As the ACCC has commented, there is room for a more substantial monitoring and evaluation regime with respect to the ACCC's administration and implementation of aspects of competition policy.[15] There is also a strong desire and expectation from business and the community generally that evidence of the benefits of competition will be forthcoming. Moreover, the systematic collection of information about the effects of ACCC decisions in the mergers area, and its administration of the Trade Practices Act is important feedback for the ACCC, the business/industry, the community and government.

4.20 The ACCC has suggested that with the establishment of the National Competition Council and the Productivity Commission more comprehensive monitoring and evaluation of outcomes from competition policy could be undertaken.[16] More detailed consideration of monitoring and evaluation issues is a matter for the ACCC, the National Competition Council and the Council of Australian Governments in their ongoing planning and development work.

4.21 While the Committee supports the role played by the ACCC, it believes there would be some benefit in a more systematic review of the general impact of the ACCC's decisions in the mergers area on competition and benefits to the community.

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10 Allan Fels, *The Australian Competition and Consumer Commission and the New Regime*, Australian Journal of Public Administration, Vol 55 No 2, June 1996, p. 78.
11 Evidence p. 21.
12 Evidence p. 21 and Submission Vol. 1, p. S 5.
13 Evidence p. 21.
14 Submission Vol. 1, p. S 5.
15 Evidence p. 21.
16 Submission Vol. 1, p. S 5.

4.22 **Recommendation 3**

> **That the ACCC give a higher priority to monitoring and evaluation of the impact of its merger decisions on market competition and that the ACCC report on its findings on a regular basis.**

4.23 **Recommendation 4**

> **That the Treasurer consult with business and industry, the community and the ACCC to ascertain an appropriate means by which the general impact on competition and benefits to the community, of the ACCC's merger decisions, could be reviewed over the medium to long term.**

David Hawker MP
Chairman
17 June 1997

# APPENDIX 1

# LIST OF SUBMISSIONS

1 Australian Competition and Consumer Commission

# APPENDIX 2

# LIST OF HEARINGS AND WITNESSES

## Melbourne, Monday 21 April 1997

Australian Competition and Consumer Commission

Professor Allan Fels
Chairperson

Ms Rhonda Smith
Commissioner

Mr Hank Spier
General Manager