Law Council
OF AUSTRALIA

Via email: creepingacquistions@treasury.gov.au

The General Manager
Competition and Consumer Policy Division
The Treasury
Langton Crescent
Parkes ACT 2600

Dear Sir or Madam,

Creeping Acquisitions – The Way Forward

I have pleasure in enclosing a submission in response to Treasury's discussion paper "Creeping Acquisitions – The Way Forward".

The submission has been prepared by the Trade Practices Committee of the Business Law Section of the Law Council of Australia. The submission has been endorsed by the Business Law Section. The submission has not been reviewed by the Directors of the Law Council of Australia Limited. Please note that the submission was prepared by the Committee prior to receiving information from The Treasury that the new Minister for Competition Policy and Consumer Affairs, Dr Craig Emerson, had extended the period for consultation until 10 July 2009. The Committee will be happy to address any further issues which come to light as a result of this extension.

If you have any questions regarding the submission, in the first instance please contact the Committee Chair, Mr Dave Poddar, on [02] 9296 2281.

Yours faithfully,

Bill Grant
Secretary-General

12 June 2009

Enc.

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Trade Practices Committee
Business Law Section
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Submission to the Commonwealth Treasury in Response to Creeping Acquisitions Discussion Paper

1 Introduction

1.1 The Trade Practices Committee of the Business Law Section of the Law Council of Australia ("**Committee**"), provides this submission to the Commonwealth Government ("**Government**") in response to the second Creeping Acquisitions Discussion Paper, published on 6 May 2009 ("**Discussion Paper**"). The Committee is grateful for the opportunity to participate in the Treasury's consultation process.

1.2 This submission outlines the Committee's views in relation to the Discussion Paper, and addresses concerns that the Committee has in relation to both of the options for reform which have been outlined in the Discussion Paper. Where relevant, the Committee has introduced a series of 'case studies', hypothetical examples which illustrate potential effects of the proposed reforms, and the problematic nature of the reforms.

1.3 Following an examination of issues that each of the options raises, and expressly noting that the Committee's strong belief is that it does not consider that any amendment to the existing merger provisions is necessary to account for creeping acquisitions, this submission proposes two alternative solutions for the Government to consider in the event that it remains resolved to introducing legislative amendments in respect of so called creeping acquisitions.

2 Executive Summary

2.1 The Committee reiterates the views articulated in its response to the Government's first discussion paper of 1 September 2008 (First Discussion Paper)[1] that no convincing case or arguments have been put forward to show that it is necessary to amend section 50 of the *Trade Practices Act 1974 (Cth)* ("**TPA**"), which currently requires a "*substantial lessening of competition*" to be proven, in the manner of either option contemplated by the Discussion Paper.

2.2 In particular, the Committee's view is that section 50 is not deficient in the face of creeping acquisitions and does not require fundamental amendment to account for small-scale acquisitions by corporations with "*substantial market power*". The Committee considers that the current "*substantial lessening of competition*" test in section 50 of the TPA is a highly flexible one which already gives the Australian Competition and Consumer Commission ("**ACCC**") (and

[1] Law Council of Australia Trade Practices Committee, *Submission on Commonwealth Government Discussion Paper - Creeping Acquisitions*, 15 October 2008.

the courts) the ability to take into account a wide range of factors that are relevant to the likely effect of a particular transaction on competition in a market. This view is reinforced by recent ACCC decisions and investigations which indicate that the ACCC is willing to apply the relevant provisions of the TPA to acquisitions of small assets and undeveloped retail sites, further indicating that Government's concerns are not reflected in the ACCC's current practices. In any event, the ACCC currently has a number of avenues open to it to challenge the type of transaction that the Discussion Paper suggests cannot adequately be dealt with when administering the relevant merger provisions. To choose to introduce radical legislative amendments when the ACCC has not been unsuccessful in seeking to prohibit a 'creeping acquisition' is premature and unwarranted, particularly given that overseas regulators in comparable jurisdictions have successfully opposed acquisitions of small grocery stores by larger competitors.

2.3 Neither of the two options raised in the Discussion Paper are "*consistent with the underlying policy principles of the TPA*". Both options would fundamentally alter the existing approach, which treats each acquisition on its merits based upon the impact of **that** acquisition on the level of competition in a particular market, and which does not result in the outright prohibition of acquisitions on the basis of a corporation's power in a market.

2.4 In contrast, the creeping acquisitions proposal may result in inconsistent application across all industries and corporations and amount to a *de facto* market share cap, to the ultimate detriment of competition and, therefore, consumers.

2.5 An option which prohibits acquisitions of *any* assets (outside of the ordinary course of business[2]), by *any* corporation which possesses substantial market power, is too broad and sweeping a reform and, importantly, does not address the original concern of a "creeping acquisition" strategy.

2.6 Additionally, as noted in the previous submission, the Committee is concerned that the proposals outlined in the Discussion Paper would result in Australia's merger control legislation being significantly out of step with international best practice and with merger control regimes in other leading jurisdictions, including the United States and European Union. It would also lead to an additional merger test to that contained in section 50 with a resultant increase in potentially burdensome and uncertain regulation. Caution will be required with such legislation given the fact that, with its relatively small population, Australia tends to have concentrated industries as a result of suppliers seeking necessary economies of scale. Without such economies of scale, suppliers would likely have higher cost structures which would make them less competitive, with the consequent potential for higher prices of goods and/or services. In the Committee's view, it is highly undesirable for Australia to consider diverging so significantly from international best practice in merger control by implementing unique provisions to account for concerns regarding creeping acquisitions.

[2] See section 4(4)(b) of the TPA.

2.7 The law should encourage firms to invest, innovate and enhance the quality and efficiency of their products and services. To do so will, in many cases, require the 'acquisition of assets' of one kind or another. Such growth, which can be called "organic growth", is not adequately addressed or catered for in the Discussion Paper.

2.8 The Committee is concerned that the merger provisions of the TPA are proposed to be changed in such a fundamental way, in spite of a clear absence of compelling evidence indicating that the existing legislation is in any way deficient. The ACCC's submissions in relation to this issue to date are not, in the Committee's view, persuasive[3]. We believe that the reform proposals will do substantially more harm than good, both legally and economically. In particular, the proposed changes will effectively create inefficient and anti-competitive market share caps, to the detriment of businesses (whether large or small), consumers and the Australian economy.

2.9 The Committee remains firmly of the view that no amendment to the existing merger provisions is necessary to account for creeping acquisitions. However, should the Government continue to insist on introducing unnecessary reform, the Committee offers two alternative reform models which may be regarded as more appropriate in overcoming the yet untested assertions contained in the Discussion Paper. We only do so noting our strong disagreement with the assertion that any legislative change is necessary.

3 Options Raised by Discussion Paper

3.1 The Discussion Paper sets out two alternative approaches ("**Options**"), both focused on corporations with substantial market power making smaller-scale acquisitions:

(a) **Option 1** - "*A corporation that has a substantial degree of power in a market must not directly or indirectly:*

(i) acquire shares in the capital of a body corporate; or

(ii) acquire any assets of a person;

if the acquisition would have the effect, or be likely to have the effect, of enhancing that corporation's substantial market power in that market"; OR

(b) **Option 2** - provide the Minister with a unilateral power (either on application by the ACCC or to be exercised at the Minister's discretion) to "declare" a corporation or product/service sector for a period of time, in a situation where the Minister has concerns about actual or potential harm from creeping acquisitions or acquisitions by corporations with substantial market power in the relevant market. The competition test applicable to any acquisitions by declared corporations, or acquisitions

[3] If the ACCC were to provide an additional submission which outlined areas of concern through practical examples, the Committee would appreciate the opportunity to test these examples.

by corporations in declared product/service sectors would be the same as for Option 1 (that is, an 'enhancement of substantial market power' test).

The Discussion Paper also posits that, as part of a declaration under Option 2, the Minister may set appropriate thresholds for the mandatory notification of acquisitions to the ACCC, by declared corporations or by corporations in declared product/service sectors.

4 Risks Associated with Substantive Legislative Amendments to Existing Australian Merger Control

4.1 Before considering the Options proposed in the Discussion Paper, the Committee wishes to make a few general observations about the proposed introduction of the creeping acquisitions reform, which is of importance even if a compelling case had been demonstrated for its introduction (which the Committee considers has not, in fact, been demonstrated).

The ACCC's informal clearance process

4.2 Merger control under section 50 of the TPA is a settled and well administered area of law. Over the past 5 years, the ACCC has developed a relatively efficient process for assessing mergers under section 50 of the TPA, and its new 2008 Merger Guidelines assist that process. Most businesses and advisers have gained confidence in the transparency, consistency and predictability of the existing merger review process, which has, in turn, promoted economic efficiency and enhanced the performance and growth of the Australian economy as a whole by facilitating investment through acquisitions.

Threats to the existing merger process

4.3 Introducing significant changes to the existing general merger review law, therefore, poses a substantial risk, especially in the current fragile economic climate. Irrespective of whether clear and effective creeping acquisition legislation were able to be drafted (notwithstanding that the Committee is of the view that neither Option is sufficiently clear nor effective in its current form), the imposition of material changes to the existing regime raises significant risk of unintended consequences which are both difficult to predict and mitigate. The Committee believes that the proposed changes would greatly undermine the current business confidence in Australian merger control.

Creation of uncertainty

4.4 In particular, any legislative change necessarily increases the regulatory burden on businesses (large or small) and individuals affected by that change, which may in turn have an unintended dampening effect on further investment in certain industries. Creeping acquisitions reform will introduce a considerable degree of uncertainty into an area that currently benefits from reasonable levels of certainty, predictability and transparency in Australia.

Parties intending to merge will be faced with additional regulatory burdens and cost, at least until such time as the practical ramifications of the amendments become clear, which may take many years. In addition to such potentially negative impacts that merging parties may experience, any proposed reform is likely to result in an increase in the administrative and cost burden on the ACCC itself, as mergers which raise few or no competition concerns, or which relate to particular industry sectors, may be notified in order to provide a degree of regulatory comfort to merging parties. This may further prevent the ACCC from allocating its resources in the most efficient manner for carrying out its statutory duties, which may ultimately harm Australian consumers and the economy.

4.5 The Committee believes that the additional regulatory burden and costs imposed on businesses and the ACCC as a result of the proposed reforms outweigh any potential public benefits that the creeping acquisitions proposals may be argued to create. The Committee is not persuaded by ACCC suggestions that the proposed reform is not a radical departure from current merger control, or that, over a period of time, there will not be a departure in the way the current merger test is administered.

Limited role of the courts in section 50 cases

4.6 It is likely that the development of adequate precedent and experience in the application and administration of any new creeping acquisitions test would occur over a considerable period of time, particularly in view of the fact that Australia is a relatively illiquid economy, and given that there is no international jurisprudence in this regard from which to obtain guidance. Further, the Committee notes that whilst clarity of interpretation of the new test may be achieved through the courts, the experience with section 50 has shown how few merger cases are litigated in full on their merits. This is often ascribed to the delays faced by merger parties in litigating a section 50 case, knowing that with appeals, most cases may take 2-3 years to complete. It may, therefore, take many years before a creeping acquisition amendment is similarly tested, particularly given the small scale transactions involved. Until then, merger parties and the ACCC will be required to apply a new law which has no local or foreign antecedents and no particular economic learning behind it.

4.7 Given the difficulty in testing the new provisions, the appropriate regulatory approach should be to proceed with caution in introducing such radical and unwarranted legislative amendments. This is particularly the case with regard to the creeping acquisitions reform proposals, as their introduction will create a groundswell of dissatisfaction, with no mechanism for correction. Clearly this is, from legal, economic and commercial perspectives, highly problematic.

4.8 No economy in the world has adopted a test that prohibits acquisitions which would result in an *"enhancing of that corporation's substantial market power"* or a *"lessening of competition"*. The lack of certainty and understanding as to the full scope of the new provisions will likely inhibit investment and have a negative impact on competition (of which acquisitions play a vital part) across all sectors of the economy.

The Government is not faced with an epidemic of creeping acquisitions

4.9 The number of so-called problematic acquisitions which have "slipped under section 50" has not been identified by the reform proponents, however, it is anticipated that the number over the last 5 years is small. Yet the solutions posed by Government seek heavy handed application "across the board".

4.10 In the Committee's view, utilising concerns, which arose in a limited range of unidentified transactions, to add to the regulatory burden for all businesses across all industry sectors amounts to poor policy. This is particularly so in the current economic climate. Moreover, the introduction of legislative amendments which result in uncertainty as to their application, will likely dampen economic activity until such time as the impact of the changes is understood.

5 Principal Issues that Arise from the Discussion Paper

Introduction

5.1 The Committee considers that one of the principal shortcomings associated with the introduction of creeping acquisitions reform is that no case has been put forward as to why the reform is considered necessary by Government. As noted in the Committee's submission in response to the First Discussion Paper, little argument in favour of introducing changes to the merger control regime to account for creeping acquisitions has been made, let alone satisfactory argument having been made. The Committee reiterates the points made in its first submission, in particular those set out in section 2 of that submission.

5.2 As noted in the Committee's submission in response to the First Discussion Paper, the ACCC has not identified any particular so called "creeping acquisition" with which it had concerns by reason of adverse impacts on competition but which it could not examine or oppose under the existing provisions of section 50 of the TPA. Further, as identified in the Business Council of Australia's submission to the First Discussion Paper, the ACCC conducted an inquiry into the grocery sector and, in July 2008, found that no problem of creeping acquisitions currently exists in that sector[4]. The ACCC's investigations found that:

> *"The ACCC has not been able to identify any supermarket acquisitions in the last five years where the result would have been different had the ACCC been able to take into account other acquisitions in the same market. This suggests that the cumulative effect of a series of acquisitions of independent supermarkets ... has not been a significant contributor to any competition problems in the supermarket sector in recent years."*[5]

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4 ACCC, Report of the ACCC Inquiry into the Competitiveness of Retail Prices for Standard Groceries, July 2008 (Grocery Inquiry Report)

5 Grocery Inquiry Report, p. 427

5.3 The grocery sector is a highly concentrated sector. However, the ACCC's statement reflects, in the Committee's view, the reality that the current merger control regime adequately addresses any competition concerns with so called creeping acquisitions within that sector, and reflects that there is no need for reform.

5.4 Accordingly, there appear to be highly persuasive arguments in favour of maintaining the current "*substantial lessening of competition*" test for *all* mergers, as it provides sufficient flexibility for the ACCC to prohibit problematic or anti-competitive mergers. The current test allows for rigorous analysis of, and investigation into, the dynamics of competition in a relevant market, with particular focus on the underlying structure of that market, rather than merely focusing on market shares held by existing participants. The ACCC's current 2008 Merger Guidelines[6] outline the range of factors that will be taken into account when conducting a merger review. The breadth of these factors indicates the flexibility provided by the existing *substantial lessening of competition* test under section 50 of the TPA, and that the ACCC has significant flexibility in applying this test to acquisitions of smaller targets, of the type that the creeping acquisitions reform is attempting to target.

5.5 International and domestic evidence supports the view that the existing test is legally sufficient. For example, in the UK, as well as in Australia, acquisitions of individual supermarkets or development sites have been reviewed by the competition authorities on the basis of a *substantial lessening of competition* test, rather than separate creeping acquisitions provisions, and, in at least three cases, prohibited[7] or opposed.

5.6 Accordingly, the Committee submits that the ability of comparable competition regimes to review and, where necessary, prohibit small scale acquisitions on the basis of a *substantial lessening of competition* test, is evidence of the fact that the existing *substantial lessening of competition* test under section 50 of the TPA is in fact sufficient for addressing potential creeping acquisitions, where there may be a genuine threat to competition. In the absence of cases that have been lost by the ACCC in this area, or otherwise publicly explained, it is difficult to demonstrate that the existing law, in its current form, is ineffective.

5.7 In addition to the principal shortcomings discussed above, both of the Options proposed in the Discussion Paper raise a number of specific legal and practical concerns, which are outlined below.

Option 1 - Enhancing Substantial Market Power

5.8 Option 1 would introduce a new element to the existing merger test under section 50 of the TPA by prohibiting acquisitions by corporations with a "*substantial degree of market power in a market*" if the acquisition would have,

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6 ACCC Merger Guidelines 2008, 21 November 2008, available online at: http://www.accc.gov.au/content/index.phtml/itemId/809866.

7 Acquisition of a Co-op store in Slough by Tesco, Competition Commission Enquiry Homepage: http://www.competition-commission.org.uk/inquiries/ref2007/tesco/index.htm. In Australia, see ACCC decision in *Woolworths/Karabah* and the ACCC's Statements of Issues in *Woolworths/Wallaroo* (2008).

or be likely to have, the effect of "*enhancing*" that corporation's substantial market power.

5.9 This option will not resolve any perceived concern which lies at the heart of the proposed creeping acquisition amendments ie that a number of smaller acquisitions which occurred over time, and which did not individually substantially lessen competition, may potentially substantially lessen competition when viewed in aggregate. Rather, this Option will effectively create two merger tests for a substantial number of corporations. A number of industry sectors within Australia are fairly concentrated due to our comparatively small population and substantial geographic distances, requiring companies to seek economies of scale. By introducing a secondary test based on "*enhancing*" a corporation's substantial market power in a market, any participant with a market share of approximately (and, in certain cases, less than) 20%[8] may face a dual merger assessment:

- first, section 50 of the TPA would be applied, to determine whether the acquisition would, or would be likely to, result in a substantial lessening of competition in a market; and

- second, the proposed new creeping acquisitions test set out in Option 1 would be applied to determine whether the corporation would, or would be likely to, enhance its substantial market power through the acquisition.

5.10 The two merger tests may result in inconsistency with the underlying policy of the TPA where a merger or acquisition which would not breach the test under section 50, may be found to breach the second test if it increases its market share by a small (almost insignificant) amount. In the Committee's submission in response to the First Discussion Paper, the Committee (when discussing the aggregation model) used the following example:

> *"... the question of whether an acquisition, by a company that already has, say, 45% of the relevant market, of a company that has 3% share of that market, will be likely to result in a substantial lessening of competition will depend, to a significant extent, on whether there will continue to be other vigorous and effective competitors in that market post-acquisition, rather than on the mere aggregation of the market shares of the merging firms.*
>
> *Moreover, the same analysis also applies regardless of the manner in which the merged firm has acquired its final market share – that is, there should be no material difference, for example, between the case of a firm whose market share has increased from 35% to 45% as a result of organic growth (and which then wishes to move to 48% via an acquisition), and the case of a firm whose market share has increased*

[8] In line with existing case law, it may be possible for a firm to have a substantial degree of market power in a market even where its market share is quite low, as noted in the Committee's first submission, p.15. See *ACCC v Australian Safeway Stores Pty Limited* (2001) 119 FCR 1, *ACCC v Australian Safeway Stores Pty Limited* (2003) FCAFC 149 and *ACCC v Australian Safeway Stores Pty Limited (No 4)* (2006) FCA 21.

from 35% to 45% as a result of three small acquisitions (and which wishes to move to 48% via another acquisition).

In each case, the impact that the 45% to 48% acquisition is likely to have on competition will still depend on whether other vigorous and effective competitors will remain in the market, rather than on the manner in which the previous increases in market share have been achieved."

5.11 In this example, the acquisition by the corporation with a 45% market share, of a company with a 3% market share, would presumably "enhance" the corporation's substantial market share. While the resulting merger may not substantially lessen competition due to the presence of vigorous and effective competitors, it would most likely breach the "substantial market power" test. This is further illustrated in section 5.12(a) below.

5.12 Option 1 gives rise to a number of legal and practical concerns, set out below:

(a) ***Meaning of "enhancing" is unclear***

The concept of "*enhancing*" the market power of a corporation is not defined in the Discussion Paper or in the TPA. Indeed, the Committee notes that the term "*enhance*" appears in only two provisions of the TPA: section 2 (the object of the TPA is "*to enhance the welfare of Australians*") and section 152CP(2)(e) (requiring a party to "*extend or enhance*" the capability with which a declared telecommunications facility is supplied). Due to the sparse use of the concept throughout the TPA, the meaning of "*enhancing*" substantial market power is unclear.

Views may differ in regard to whether "*enhance*" implies a materiality criterion. The courts are likely to resort to a literal meaning as contained in a dictionary if there is a need to define the term. The Macquarie Dictionary definition of "enhance" is "*to raise to a higher degree; intensify or to magnify*".

Therefore, a key failing of the use of the term "*enhancing*" is that it is not clear whether there is a qualitative or materiality element to it, such that it would require more than a simple acquisition of *any* assets to 'enhance' a corporation's substantial market power. The concept of 'enhancement' may be interpreted as being qualitative to a degree, requiring an acquisition to heighten, intensify or exaggerate a corporation's substantial market power, which would suggest something more than a simple increase in market share or asset base.

However, there is a considerable risk that "*enhancing*" may be interpreted to mean a simple increase, which treats the level, degree or effect of that enhancement as immaterial. Such an interpretation would promote serious concerns as to the ability for corporations to compete actively and effectively in a market, as the possibility of making any asset acquisitions would appear to be prohibited.

(b) ***Determining whether a "substantial degree of market power" exists***

Furthermore, prior to consideration of an acquisition in question, determining whether an acquirer has a "substantial degree of market power" is not a straightforward task and may prove to be far more difficult than is acknowledged in the Discussion Paper.

Unlike in a section 46 case, in a section 50 context, there is no **conduct** by the acquirer which is subject to review or which could be tested for the suggestion that it demonstrates the existence of substantial market power by such standards as are used in section 46 cases. The existence of market power will have to be identified and proven by other means. It is difficult to expect that this can be done without some fairly arbitrary market share tests being introduced.

It is noted, for example, that the ACCC has published no current guidelines on how the concept of "substantial market power" is to be determined under section 46. Application of the case law criteria to prove the possession of a substantial degree of market power is difficult enough, even where there is a specific conduct which is under challenge, because it is said to involve an *exercise* of substantial market power.

It is unclear to the Committee whether it is intended that the factors in sub-section 46(2) to (3D), which assist to determine the extent of power held by a corporation under section 46, will also apply to the new provision. This would require clarification in any further draft legislation.

Under the suggested new model, the ACCC and the parties will be required to devise new criteria to measure whether the firm in question possesses that elusive concept of "*substantial market power*", in the absence of any specific conduct. The acquirer may have in fact behaved perfectly legitimately for years but its degree of market power, which is not market share, will need to be devised and applied in a merger clearance context which is required to take no longer than 4-6 weeks.

Substantial market power is a difficult concept and is not well suited to application in this type of review. We note that almost every section 46 case on that question has gone through multiple appeals on the issue, with Judges of the Federal Court and High Courts commonly in disagreement on the question of presence or absence of that degree of market power.

It will likely require the interpretation of the courts to provide sufficiently clear guidance to advisers and businesses. The gap between the introduction of creeping acquisitions reforms and the development of adequate judicial guidance is likely to be material, thereby increasing uncertainty for businesses during that period.

(c) ***Equating market power with anti-competitive impact is a flawed approach and will result in a potential market share cap***

Of particular concern is that the theoretical approach which underpins Option 1, appears to equate market power with anti-competitive impact and consumer detriment. However, the mere existence or accrual of market power is not, in and of itself, indicative that anti-competitive behaviour will result and is not sufficient to warrant regulatory intervention. Importantly, the misuse of market power regime under section 46 of the TPA does not *prohibit* the possession of market power, merely taking advantage of that power.

If "*enhancing*" is interpreted in a restrictive and narrow manner, such that it effectively is seen to mean that *any* acquisition by a corporation with a substantial degree of market power would enhance its market power in that market, the result would be a *de facto* market share cap for corporations that were held to have a "*substantial degree of market power*" in a market. As noted in paragraph 5.9 above, this may prohibit acquisitions by firms with relatively small market shares.

A *de facto* market share cap would constitute a retrograde step, as affected corporations would be unable to make acquisitions and, in circumstances where potential buyers are scarce (for example in the current financial climate), acquisitions may effectively cease within certain sectors. This could create a potential moribund corporate sector.

Any additional test which would effectively operate as a prohibition on *any* further acquisitions by certain corporations within certain markets would be unique, and would risk undermining the principles of section 50 of the TPA, which require a qualitative analysis of competition in a market to be conducted, and which do not seek to prohibit acquisitions outright. Moreover, acquisitions that 'enhance' the market power of one corporation may also enhance the welfare of Australians (consistent with the objects of the TPA, as set out in section 2) by way of increased savings arising from economies of scale, increased efficiency and innovation, and a greater ability to compete domestically and globally.

Additionally, the test envisaged by Option 1 raises the same issues identified in relation to the previous substantial market power option in the First Discussion Paper, which proposed the prohibition of any acquisition by a corporation with substantial market power where it resulted in any "*lessening of competition*". By introducing a prohibition on acquisitions which 'enhance' a corporation's substantial market power (depending on how "*enhancing*" is interpreted), there may be an absolute prohibition on acquisitions by corporations with substantial market power within the relevant markets.

(d) ***Effect on vertical or unrelated mergers***

The Discussion Paper does not provide any guidance as to how the proposed creeping acquisitions test would be applied in relation to vertical acquisitions which do not directly increase a corporation's market share position in a *particular* market. Additionally, the Discussion Paper does not address the question of whether an acquisition of assets or interests which raises no vertical or horizontal competition issues, as a result of there being no competitive overlap, and which takes place at a level in the supply chain outside a corporation's current sphere of operations, would face prohibition under Option 1.

In most jurisdictions with well established and entrenched competition laws, vertical mergers are recognised as generally not raising competition issues and generally being efficiency enhancing.

The ACCC currently provides for the examination of the vertical effects of mergers (see 2008 Merger Guidelines). However, the introduction of a creeping acquisitions test may in practice prevent a corporation with a substantial degree of market power in one market from making upstream or downstream acquisitions, as any such acquisition may potentially 'enhance' its substantial market power, even if the acquisition is of a complementary, and not of a competitively overlapping, asset.

This is a significant departure from the existing test under section 50 of the TPA and may have the effect of prohibiting non-horizontal growth in certain markets. Moreover, the possibility of stifling such vertical acquisitions arguably contravenes the primary purpose of the creeping acquisitions reform, which is to prevent horizontal acquisitions that individually may not raise competition issues, but collectively may potentially give rise to concerns. For example, consider Case Study 1 and 2 below:

<u>Case study 1 (vertical acquisitions)</u>

An energy retailer (gas and electricity) with substantial market shares in each of Melbourne, Sydney and Adelaide residential and commercial markets seeks to acquire part interest in a large-scale coal burning power station in Victoria. The rationale for the acquisition is to create a natural hedge against extreme movements in the electricity pool price by combining generation and retail under the same ownership structure. This type of combination is commonplace in other jurisdictions and has been recognised as welfare-enhancing.

The test embodied in Option 1 would likely preclude this acquisition from proceeding because the energy retailer would likely be found to have substantial market power, and the acquisition would probably be construed as enhancing that market power by giving the energy retailer an advantage over its rivals in accessing hedge cover.

It is noted that, under the current TPA, the Federal Court made a positive determination that such a transaction would not in fact lead to a substantial lessening of competition (AGL v ACCC (No 3) [2003] FCA 1525, Melbourne.

Case study 2 (complementary acquisitions)

A market leading Australian freight forwarder with substantial rail freight interests seeks to acquire one of the two major Australian stevedoring firms. The two firms have relatively minor overlaps in rail freight and services ancillary to stevedoring. The rationale for the acquisition is to improve logistics chain coordination from dockside to customer premises by placing the entire chain under unified ownership. The economic literature recognises the superior efficiency of unified ownership over contractual coordination among unrelated parties.

The test embodied in Option 1 would likely preclude this acquisition from proceeding because the freight forwarder would likely be found to have substantial market power, and the improved supply chain efficiency would probably be construed as enhancing that market power by improving its relative cost structure.

It is noted that under the current TPA, the overlaps in the Toll-Patrick merger were successfully dealt with through divestiture commitments. Conditional on those commitments, the ACCC ultimately did not oppose it. However, the undertakings may not adequately deal with the enhancement of that market power.

Similarly, the Discussion Paper does not consider the issue of acquisitions of new plant and equipment or intellectual property assets by corporations with a substantial degree of market power. Section 46(5) of the TPA states that "*a corporation shall not be taken to contravene [the prohibition against misuse of market power] by reason only that it acquires plant or equipment*". There is no equivalent exception set out in the Discussion Paper. Without an equivalent exception, the acquisition of a new factory, or new machinery to use within its factory, which will increase efficiency for a manufacturer with substantial market power in a particular market, may arguably 'enhance' that corporation's market power, and thereby be prohibited under Option 1.

Case study 3

One of the main capital city airports in Australia wishes to acquire a parcel of adjacent land for the purpose of expanding its on-airport air freight handling facility, which is currently operating at an inefficiently small scale due to space limitations. To some extent this on-airport facility competes with other off-airport freight handling facilities which are able to compete in part because of their less-stringent space constraints, despite the additional transport cost. Permitting the on-airport facility to operate at efficient scale would be welfare enhancing.

The test embodied in Option 1 would likely preclude this acquisition because the airport would be found to have substantial market power in several markets, apart from airside services. The acquisition would improve the competitive position of the on-airport freight facility at the expense of the off-airport facilities and could, therefore, be construed as enhancing the airport's market power.

Thus the Option 1 test would likely prevent the airport from making a logical and desirable investment in improving the efficiency of air-freight handling services.

This example highlights how the proposed creeping acquisitions reform has moved away from examining competition in a market and taking account of efficiencies as a means of facilitating increased competition, to focus merely on the acquisition of additional assets or shares. As such, the proposed new test is flawed.

(e) ***Impact on innovation and investment***

In paragraph 20 of the Discussion Paper, the Government states that "*intervention in this area…should not stop the legitimate and organic growth of businesses*". There is, however, no consideration given in regard to what is meant by "*organic growth*" and no definition has been proposed. This raises practical difficulties, as "*organic growth*" is not something that necessarily has a clear meaning.

For example, should the acquisition of a greenfield site from a land owner by a retailer for new store development be considered to be organic or inorganic growth? In addition, where a corporation with 30% market share in the fertiliser industry acquires a large site to build a new plant and acquires a licence to use patents to adopt an innovative new production technology, which lowers its costs and which will likely render most of its competitors uncompetitive on cost. As the cost of this investment is approximately $500 million, and the corporation has not previously made an investment of this kind, it is hard to say that it is made "in the ordinary course of business" under section 4(4)(b). There is no exception for the acquisition of such assets in section 50. The acquisition will most definitely enhance or materially increase the firm's market power. Should the acquisition be prohibited?

Such uncertainty would be likely to inhibit innovation and investment and, again, appears to be inconsistent with the initial comments about the new provision being intended to deal with a series of small acquisitions of competitors over time.

For example, consider Case Study 4 and 5 below:

<u>Case study 4 (innovation-related acquisition)</u>

The market leading provider of subscription television services in Australia wishes to acquire shares in a small technology company that *designs and manufactures smart cards that are used in digital set-top boxes. The motivation for the acquisition is that the smart cards necessarily embody proprietary information concerning customer access and system information functions of the broadcaster. Ownership is seen as necessary to protect that IP. In fact it is a necessary precondition to the roll-out of a range of new services to customers, which embody substantial IP.*

The test embodied in Option 1 would likely preclude this acquisition because the ACCC in the past has held that subscription television service providers have substantial market power, and the acquisition could be construed as enhancing that power by giving the firm a competitive advantage over rivals through its new product offering.

Thus the Option 1 test could discourage, impede or prevent product innovations that would otherwise have benefitted consumers.

Case study 5 (innovation-related acquisition)

One of the four major Australian banks wishes to acquire a small data security/encryption firm that has a 'best of breed' data encryption method that can be used on credit cards and debit cards. The reason for the acquisition is that it would permit the bank to offer more secure transaction services to its customers and reduce costs associated with fraudulent transactions. Ownership of the technology is seen as necessary for security reasons, as the bank would need to work closely with the encryption firm and share the bank's own proprietary information to fully develop the application.

The test embodied in Option 1 would likely preclude this acquisition because the bank would be found to have substantial market power in a cluster of banking-related markets. The acquisition could be construed as enhancing that power by giving the bank a competitive edge through the ability to offer consumers a more secure transaction service and reducing the bank's costs.

Thus the Option 1 test could act to impede or prevent the introduction of superior data security measures by the bank.

Additionally, the Committee notes that continued inorganic growth (ie through acquisitions) is specifically something which the Discussion Paper appears not to support, which is quite contrary to most accepted economic view points. Efficient and successful economies typically require acquisitions in order to function properly. Acquisitions allow inefficient firms to exit the market and for effective and vigorous competition to take place, thereby benefitting consumers and the broader economy. It would be extremely disappointing if a reform were implemented which had the effect of inhibiting mergers *per se*. In particular, pro-competitive mergers could be limited, become less timely from a commercial perspective, or be blocked in certain circumstances, to the detriment of all consumers. For example, see Case Study 6 below:

Case study 6 (efficiency-enhancing investment acquisition)

The two largest supermarket chains in Australia each seek to acquire (different) providers of EFTPOS technology in order to improve their service delivery at the checkout counter - faster and more accurate scanning, more reliable fraud detection and credit authorisation, etc. One dimension of the competition between these supermarket chains is the technology 'arms race'.

The test embodied in Option 1 appears to be squarely aimed at preventing firms such as supermarkets from acquiring smaller rivals, but the way it is framed, it would almost certainly also prevent supermarkets from acquiring complementary service providers who may play an integral role in the process of competition between the largest and most vigorous rivals.

One may say that it is not necessary to acquire a technology firm in order to benefit from the technology. However, in many cases, an ownership stake in such a technology firm may be the only viable means of utilising the technology because of the need to share and protect IP, the need to protect data encryption methodologies from wider dissemination, or the need to ensure that complementary investments between the two firms are made in a timely and effective manner.

(f) ***No international equivalent***

The Committee noted in its previous submission on this topic that the introduction of a creeping acquisitions law would put Australia out of step with international best practice and comparable regimes in the United States and European Union. In particular, the creeping acquisitions regime would in practice be substantially different from the closest equivalent merger framework, being that of the European Union.

The European Community Merger Regulation[9] requires that "*concentrations which would significantly impede effective competition in the common market, or substantial part of it, in particular as a result of the creation or strengthening of a dominant position, shall be declared incompatible with the common market*"[10].

It is clear that the creation or strengthening of a dominant position is a determinant of whether an acquisition may "*significantly impede effective competition*". It is not the sole, or even the key determinant,

[9] European Community Merger Regulation, Council Regulation No. 139/2004, available online at: http://ec.europa.eu/competition/mergers/legislation/legislation.html.

[10] ECMR, Article 3.

however. Importantly, the creation or strengthening of a dominant position is not a reason to prohibit an acquisition ***per se***.

In contrast, the introduction of a creeping acquisitions test of the type proposed in Option 1 would prohibit all transactions that 'enhance' a corporation's substantial market power and would effectively make the existence of market power the key or sole determinant of whether or not an acquisition may be permitted. As indicated, such an approach would be substantially different to the approach adopted in other leading jurisdictions, and would create considerable uncertainty for merging parties and their advisers.

The introduction of an additional regulatory hurdle for a significant number of corporations active in various sectors in Australia would not only add to the regulatory burden and cost for merging parties and the ACCC, as discussed above, but may also deter vigorous economic activity and acquisitions which may be necessary and/or beneficial in certain industry sectors. Such an outcome would not, in the Committee's view, promote the economic well-being of the country.

Option 2 - Ministerial direction of sensitive sectors

5.13 Option 2 would provide the Minister with a broad discretion to 'declare' a corporation or product/service sector of the economy for a period of time in a situation where the Minister has concerns about actual or potential harm from creeping acquisitions. The consequence of this would be that declared corporations, or corporations active in the declared product or service sector, would be required to notify all proposed acquisitions to the ACCC for assessment, regardless of size or impact.

5.14 This would unnecessarily increase the regulatory burden and cost for corporations who would not otherwise notify the ACCC and would also significantly increase the caseload of the ACCC in having to investigate these mergers.

5.15 The Committee notes that there has been little expansion in the Discussion Paper as to how either of these elements of Option 2 would work in practice. However, the lack of explanation and detail in relation to Option 2 is potentially more problematic, as the proposal would provide significant discretion to the Minister to make a declaration. Clarity as to how a declaration may be made (for example, whether there would be parameters within which the decision would have to be made, what defined factors would have to be considered prior to a declaration, what the period of declaration would be, whether all acquisitions would be required to be notified or whether a notification threshold would be introduced) is required to enable respondents to provide substantive comment on the Option.

5.16 Notwithstanding the absence of detail in the Discussion Paper, the Committee is, in principle, opposed to the introduction of a creeping acquisitions provision of the type set out in Option 2 for the reasons set out below:

(a) ***Same limitations as for Option 1***

Option 2 raises the same issues highlighted above in respect of Option 1 (such as the potential introduction of a practical market share cap, lack of certainty, negative impact on innovation and investment etc), as the substantive competition test to be applied would be identical.

(b) ***Contrary to principle of applying merger control consistently across all sectors***

In principle, legislation of general rather than specific application is preferable because it creates greater certainty, transparency and confidence. In particular, the declaration process would undermine the general application of section 50 of the TPA across all industries on an equal basis. The possibility of the Minister unilaterally declaring a corporation or product/service sector is contrary to the principle of general application and risks introducing considerable uncertainty both within declared corporations/sectors, and the wider economy.

Additionally, there is a considerable risk that the introduction of a Ministerial declaration process in relation to particular corporations and/or product or service sectors may result in distinct approaches to mergers within the declared corporations or sectors. In turn, this may result in serious inconsistency of merger control practice across different sectors of the economy, leading to further legal and practical uncertainty.

That said, while the adoption of disparate approaches to merger control in different industry sectors would increase commercial uncertainty and risk (which may in turn stifle investment), to the detriment of the Australian economy as a whole, it does appear that such an approach may, comparatively, be less harmful than a reform of general application.

(c) ***Lack of transparency***

Some degree of risk arises in relation to the grant of a blanket power to 'declare' corporations or industry sectors, especially where there is little or no transparency in the processes and procedures resulting in a declaration. As noted above, there is currently a lack of detail as to the circumstances in which a declaration may be made, or the factors that the Minister would be required to take into account before declaring a particular corporation or product/service sector. As a result, the administrative procedures and safeguards around the declaration process would be opaque, creating substantial uncertainty, especially within those sectors which may be at risk of being declared. In its response to the First Discussion Paper, the ACCC merely asserted that certain industry sectors have suffered from creeping acquisitions in the past, without providing evidence in support or further details[11]. For example, the reference to funeral services was an issue that was not otherwise known to competition law practitioners. Similarly, in the case of optical industries, barriers to entry have not previously been found to be high and it is not clear that any participant possesses, in practice, a "*substantial degree of market power*". If the Minister's decision was based on ACCC recommendation, it raises concerns as to the ability to test that recommendation through normal legal avenues.

Similarly, the Committee considers that the introduction of Option 2 may result in a perception (whether warranted or not) that:

- the Minister is seeking to exercise his or her discretion in an arbitrary manner, perhaps with a view from some industry sectors to introduce a degree of 'social engineering' in respect of mergers within specific sectors, or to provide regulatory support for new entrants within particular markets based on some form of perception of "workable" competition;
- those sectors which are declared are subject to extra scrutiny as a result of political pressure or even misinformed debate in relation to particular companies, rather than due to any failures of competition within those sectors; and
- significantly, the ACCC may take a 'no smoke without fire' view that, as the Minister has declared a particular sector, there must be a problem which militates in favour of blocking rather than approving acquisitions within that industry sector.

(d) ***Extent of impact on declared firm and appeals***

The Discussion Paper does not provide any details in relation to the impact that a declaration would have on an individual corporation. There is no discussion of whether a declaration could be made in relation to a single corporate entity, or a group of companies as a whole, within a single economic entity.

In particular, there is no consideration as to how a declaration (if made in relation to a whole corporate group rather than a specific part or standalone corporation within a group) would impact support functions, or business divisions which are unrelated to the specific product or service sector in which the declaration is seeking to control acquisitions.

Case study 7

[11] See *ACCC Submission to the Assistant Treasurer and Minister for Competition Policy and Consumer Affairs regarding creeping acquisitions*, October 2008.

A conglomerate comprised of various business divisions has interests in retail stores, travel services, mineral exploration and car manufacturing. The travel services division has a large share of the travel industry, approximately 45% to 50%, and there have been a number of acquisitions within that sector in the past five years. The Minister declares the entire corporation, thereby preventing, in effect, additional acquisitions by the corporation as a whole, even though the principal concern arises in relation to the influence by one of the division's of the corporation in the travel sector. The car manufacturing division wishes to purchase some additional sites on which to build more efficient factories. The existence of a declaration of the corporation gives rise to problems, however, as it is not clear whether the efficiency enhancing acquisition by the car division would be subject to regulatory scrutiny, and may even be prohibited given that those cars could potentially be used for the conglomerate's car hire business.

Additionally, there is no visibility as to whether a corporation subject to a declaration would be permitted to appeal decisions made in relation to the declaration. If appeals were allowed, the grounds and manner pursuant to which that appeal would be permissible have yet to be defined. In summary, the lack of certainty undermines the degree to which a full and sensible assessment of Option 2 is possible.

It appears that the application of a declaration to an ultimate holding company in Australia (or indeed overseas) would, in effect, be a blunt regulatory instrument and would have significant impact across the corporate group as a whole. It would also impose a considerable additional regulatory burden to parts of the business that operate in highly competitive markets. Further, by singling out some market players, application to a corporation or corporate group would effectively result in the choosing of "winners and losers" by the Minister. In that sense, application to industry sectors is preferable to application to individual corporations so that every market participant is treated equally and the regulatory impact does not discriminate against individual corporations or corporate groups.

Accordingly, while in many ways the Committee is sympathetic to this approach based on a more upfront reflection of political concerns with particular sectors of the economy, it is a process that could rapidly expand across industry sectors with limited checks and balances and regulatory impacts that outweigh the benefits; and

(e) ***Third party declaration procedures***

The Discussion Paper does not address the position of third parties in a litigation process under Option 2, particularly whether:

- third parties would be able to seek declarations from a court of a contravention of the new provisions where an acquisition proceeded without prior merger clearance; and

- third parties could bring actions against the merger parties for declaration of a contravention of the new provision by the declared corporation or sector participants.

As noted above, the lack of certainty undermines the degree to which a meaningful assessment of Option 2 is possible.

6 Proposed Options for the Creeping Acquisitions Reform

6.1 The Committee does not believe that the various permutations of creeping acquisition reforms are necessary and does not believe that a compelling case for their introduction has been made.

6.2 Nevertheless, if the Government is intent on making specific legislative changes in respect of creeping acquisitions, the Committee suggests that the following proposals be considered. The Committee's preference is for the Government to adopt Proposal A, being an aggregation model, to be applied to specific declared markets or industries. In the alternative, and if Proposal A is not acceptable to the Government, we put forward Proposal B as the basis for a creeping acquisition reform which mitigates the worst effects of the current Options by introducing a clear qualitative element to the test surrounding a corporation's "*substantial degree of market power*". In particular, Proposal B would require that an acquirer's substantial market power were "*materially increased*". This approach is the most consistent with the underlying nature of the creeping acquisitions reform, in that it is intended to prevent piecemeal aggregation.

Proposal A: Aggregation Model

6.3 Although the Committee, in its previous submission expressed a number of reservations on this issue, an aggregation model of the type raised in the Government's first discussion paper may be a preferable alternative **provided** the 'look back' or aggregation period is limited, possibly to a period not exceeding 2 years.

6.4 The primary advantage of an aggregation model is that, compared to the alternatives under consideration, it is the most appropriate method to achieve the policy objectives which underpin the creeping acquisitions reform debate; that is, to provide greater regulatory oversight of small acquisitions over time which, individually are unlikely to contravene the existing merger test in section 50 of the TPA, but which, when taken together, may have such an effect, i.e. of substantially lessening competition. An aggregation model permits previous acquisitions (precisely the types of acquisitions that the Government is concerned with) to be aggregated with the current acquisition, thereby helping to determine whether or not the current acquisition would, or would be likely to, lead to a substantial lessening of competition.

6.5 Consequently, the Committee reiterates the recommendation in its previous submission of 15 October. In this regard, section 50(3) of the TPA might be amended to require prior acquisitions by the corporation within a reasonable specified period (of up to two years) to be taken into account when assessing, in aggregate, whether or not an acquisition, combined with those prior acquisitions, would have the effect, or be likely to have the effect, of substantially lessening competition in an industry. A period of two years appears workable in most industries where competition is unlikely to have changed significantly within this period and it would, therefore, be easier to identify the counterfactual and apply a "future with and without" test.

6.6 Such an amendment would make clear that the relevant legal test to be applied in relation to the latest acquisition (the creeping acquisition) is the same as that under the existing section 50 of the TPA, and that all of the criteria which apply under section 50(3) will also continue to apply.

6.7 Because of the unusual nature of this test, and its cost and uncertainty of application, we believe it should be confined to notified or declared sectors only and should not have blanket application across all sectors of the economy. We accept that an aggregation model may still require the ACCC to clear a reasonable hurdle and demonstrate that the latest acquisition, when aggregated with past acquisitions over a reasonable period, would lessen competition substantially. The proposed test would also suffer from the issue of being a backward looking test in aggregating past acquisitions with a forward looking test of the current acquisition. Nonetheless, from a competition perspective it is a test much more "true" to tackling the stated harm of a series of "creeping" acquisitions. The combination of a declared corporation, or product/services sector, together with the aggregation test would limit the fundamental difficulties associated with having two merger tests, as addressed above, and would be much more workable than the enhancement test. A corporation would only have to consider the aggregation model if it was in a declared industry. While still not ideal, this would reduce the burden on a number of corporations outside the declared industries.

6.8 The proposed aggregation test should not be viewed as a panacea and there would still be a number of practical problems to be managed. However, the Committee considers that, in the event that the Government proceeds with amendments to the merger provisions of the TPA to take account of creeping acquisitions, the proposed aggregation model is the best solution.

6.9 Details in relation to the proposed aggregation model and industry declaration are set out in the Attachment.

Proposal B: "Material Increase"

6.10 The Options proposed in the Discussion Paper raise a number of legal and practical concerns. One of these concerns is that the meaning of 'enhancement' is unclear and may result in the prohibition of transactions which are not harmful and which are beyond the intended scope of the amendments. The term 'enhance' is not presently defined in the TPA and has not been the subject of any substantial consideration in commercial jurisprudence.

6.11 In order to provide a greater level of certainty, this submission proposes that the word "*enhancing*" be replaced with the words "*materially increasing*" in order to introduce a more practical and proportionate element to the test being proposed.

6.12 The words "*material increase*" can currently be found in Part IIIA of the TPA, where it is specified that a service cannot be declared unless access to the service would promote a "*material increase*" in competition. This submission considers the meaning of the words "*material increase*" and "*material*" as it appears in other provisions of Commonwealth legislation, and how this concept may be applied in the context of the Options proposed in the Discussion Paper. The Committee recognises that such a change may still be viewed as difficult by the ACCC, but it is, in the Committee's view, a much better test than "*enhancing*", which suffers from the substantial drawbacks described in this submission.

Meaning of "material increase"

Amendment to Part IIIA

6.13 The term "*material increase*" was introduced into criterion (a) of sections 44G(2)(a) and 44H(4)(a) of the TPA by items 16 and 23 of Schedule 1 of the *Trade Practices Amendment (National Access Regime) Act 2006* (Cth) ("**TPA Amendment Act**").

6.14 The Explanatory Memorandum for the TPA Amendment Act states that the inclusion of "*material increase*" in section 44G(2)(a) was intended to ensure that "*access declarations are only sought where increases in competition are not trivial*".[12] The Explanatory Memorandum further states that criterion (a), as previously drafted, did not adequately address the situation where declaration would result "*only in a marginal increase in competition*". The Explanatory Memorandum makes equivalent comments in relation to section 44H(4)(a).

6.15 The Explanatory Memorandum referenced the Government's response to the Productivity Commission's report, *Review of the National Access Regime* in which recommendation 7.1 was that criterion (a) be amended to require that access (or increased access) to the service would promote a substantial increase in competition. The Government's response was that the term "*substantial*" "*may exclude situations where a small supplier is prevented from gaining access to nationally significant infrastructure*".[13] On this basis, the Government instead chose the wording "*material increase*", in order to include circumstances in which increases in competition would be "*not trivial*".

NCC Recommendations

6.16 The National Competition Council ("**NCC**") has considered the meaning of "*material increase*" in the context of making recommendations as to whether infrastructure should be declared under Part IIIA of the TPA.

[12] Explanatory Memorandum to the Trade Practices Amendment (National Access Regime) Bill 2005 at p 21.
[13] http://www.treasurer.gov.au/DisplayDocs.aspx?pageID=&doc=publications/FinalReport_NationalAccessRegime.htm&min=phc.

6.17 In the NCC's final recommendation regarding an Application for declaration of a Service provided by the Tasmanian Railway Network, it noted that the introduction of the term "*material increase*" 'confirms' the approach of the NCC and the Tribunal to interpreting criterion (a), which "*has always been that the promotion of competition in the dependent market has to be non-trivial*".[14] The NCC further stated that:

> "*The additional words now contained in criterion (a), "a material increase", indicate that the level of competition promoted must be more than trivial, being at a level that could reasonably be expected to have a tangible impact on competition in the dependent market. (emphasis added)*"[15].

6.18 The NCC also noted that whether Part IIIA declaration would promote a "*material increase*" would need to be measured against the state of the current market:

> "*if a dependent market is already effectively competitive, access would be unlikely to promote a material increase in competition. Similarly access may not materially promote competition where high barriers to entry or other conditions, that are unrelated to the existence of the bottleneck facility, preclude additional competition in a dependent market*"[16].

6.19 In the NCC's final recommendations regarding Applications for declaration of services provided by the Goldsworthy, Hamersley and Robe Railways further emphasises that the words "*material increase*" indicate that "*the change in competition promoted by access must be more than trivial*" as opposed to "*marginal*". The Committee therefore believes that such a test would be preferable to a test based on the concept of 'enhancement'.

7 Conclusion

The Committee's strong submission is that there is no need for any further amendment to the TPA to address 'creeping acquisitions'. However, if the Government is minded to proceed with a creeping acquisitions test, the Committee favours its Proposal A, being the aggregation model to be applied to particular industry. This is more clearly directed at the perceived harm to be addressed. In the alternative, if the Government rejects the aggregation model (acknowledging that there are some difficulties with such a model, having regard to assessment of substantial market power and market delineation), the Committee submits that a test involving a "material increase" in a substantial market power is a preferable test, and puts forward Proposal B. In particular, introducing a test based on the concept of "material increase" is preferable to one reliant on "*material enhancement*", as such an alternative

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[14] NCC, *Application for declaration of a Service provided by the Tasmanian Railway Network*, Final Recommendation (14 August 2007) at [5.15] http://www.ncc.gov.au/pdf/DeRaTRFR-001.pdf.
[15] NCC, *Application for declaration of a Service provided by the Tasmanian Railway Network*, Final Recommendation (14 August 2007) at [5.16] http://www.ncc.gov.au/pdf/DeRaTRFR-001.pdf.
[16] NCC, *Application for declaration of a Service provided by the Tasmanian Railway Network*, Final Recommendation (14 August 2007) at [5.8] http://www.ncc.gov.au/pdf/DeRaTRFR-001.pdf.

would not address the shortcomings enunciated above with a test based on "*enhancement*".

Any questions regarding the submission should, in the first instance, be directed to the Committee Chair, Mr Dave Poddar, on [02] 9296 2281.

12 June 2009

Attachment: Proposed Aggregation and Industry Declaration Model

THE PROCESS TO DECLARE A SENSITIVE INDUSTRY

[1](1) If the ACCC determines, after due inquiry, that both of the following criteria are satisfied in respect of a substantial industry:

(a) one or more corporations may possess a substantial degree of market power in that industry; and

(b) there have been a number of acquisitions within the industry in the preceding 2 years, by those corporations referred to in subsection (1)(a), of assets or shares of a person in that industry (other than by an acquisition in the ordinary course of business);

the ACCC may recommend to the Minister that the relevant industry be designated as a sensitive industry for the purposes of section **[2]**[17].

(2) The Minister may accept or reject the ACCC's recommendation. If the Minister does not accept the recommendation within 90 days, the Minister is deemed to have rejected the recommendation.

(3) The Minister may only accept the ACCC's recommendation if the Minister is satisfied that designation of the industry as a sensitive industry would be in the public interest, having regard to:

(a) the objectives of promoting competition, innovation and efficiency in Australian markets;

(b) the objectives of not discouraging organic growth nor firms increasing their efficiency by means other than by acquiring assets or shares of a competitor, customer or supplier;

(c) the objectives of promoting the international competitiveness of Australian businesses;

(d) the costs of designation likely to be incurred by persons carrying on business in the substantial industry weighed against the likely benefits of designation for consumers; and

(e) any other matter which the Minister considers relevant.

(4) The Minister must publish his or her decision and reasons for his or her decision.

(5) A designation made by the Minister under subsection (2) expires after 2 years from the date of publication.

(6) If a designation made by the Minister under subsection (2) is in force, section **[2]** applies in respect of that industry.

[17] The Committee expressly notes the difficulties with market delineation and assessment of substantial market power that such a test creates.

(7) A recommendation by the ACCC under subsection (1) or a designation by the Minister under subsection (2) is not admissible as evidence of whether a corporation referred to in the designation has a substantial degree of market power in any proceedings.

THE SUBSTANTIVE PROHIBITION-ALTERNATIVE ONE- ENHANCE MARKET POWER

[2] (1). A corporation which possess a substantial degree of market power in a sensitive industry designated under section **[1]** must not, while the designation remains in force, directly or indirectly:

(a) acquire shares in the capital of a body corporate; or

(b) acquire any assets of a person,

if the acquisition would have, or be likely to have the effect, of **materially increasing /enhancing**, that corporation's degree of market power in that industry.

(2) Without limiting the matters that may be taken into account for the purpose of subsection (1) in determining whether the acquisition would have the effect, or be likely to have the effect, of materially strengthening/enhancing, the corporation's substantial degree of power in that industry, the matters set out in section 50(3) must be taken into account.

OR ALTERNATIVE 2- AGGREGATION AND SLC TEST

A corporation in a sensitive industry designated under section **[1]** must not, while the designation remains in force, directly or indirectly:

(a) acquire shares in the capital of a body corporate; or

(b) acquire any assets of a person,

if the acquisition (**New Acquisition**), when aggregated with the effect or likely effect of any other acquisition of shares or assets of a person made by that corporation in the period of 2 years prior to the New Acquisition, would have, or be likely to have the effect, of **substantially lessening competition** in that industry.

REVIEW OF DESIGNATIONS

[3] (1) A person whose interests are affected by a decision of the Minister under section **[1]** may apply in writing to the Tribunal for review of the Minister's decision.

(2) The person must apply for review within **[21]** days after the Minister publishes his or her decision.

(3) The review by the Tribunal will constitute a reconsideration of the matter.

(4) For the purpose of the review, the Tribunal has the same powers as the Minister.

(4) If an application for review of a designation decision is made, the designation remains in operation until the Tribunal makes its decision on the review.

(5) If the Minister made a decision to designate an industry, the Tribunal may affirm, set aside or vary the designation.

(6) If the Minister made a decision not to designate an industry, the Tribunal may affirm, set aside or vary the decision not to designate the industry.

(7) A designation by the Tribunal is taken to be a designation by the Minister for all purposes (except this section).