Chapter 2

The section 50 provisions

2.1 This chapter examines the bill's provisions in relation to its amendments to section 50 of the *Trade Practices Act 1974* (TPA). Currently, section 50(1) of the TPA states that:

> A corporation must not directly or indirectly:
>
> a) acquire shares in the capital of a body corporate; or
>
> b) acquire any asset of a person;
>
> if the acquisition would have the effect, or be likely to have the effect, of substantially lessening competition in a market.

2.2 Section 50(6) of the Act clarifies the meaning of 'a market':

> In this section:
>
> market means a substantial market for goods and services in:
>
> (a) Australia; or
>
> (b) a State; or
>
> (c) a Territory; or
>
> (d) a region of Australia.

2.3 Section 50 is the key provision relating to mergers and acquisitions. Creeping acquisitions are a series of small-scale acquisitions that, individually, do not substantially lessen competition in a market, but collectively may do so over time.[1] Each of these small acquisitions is not in breach of section 50, and the series of acquisitions are therefore permissible by law.

2.4 There are currently no provisions in the TPA to prevent or limit 'creeping acquisitions'. This has been an area of recurring concern for this committee. It recommended in a 2004 inquiry that 'provisions should be introduced into the Act to ensure that the Australian Competition and Consumer Commission (ACCC) has powers to prevent creeping acquisitions which substantially lessen competition in a market'.[2]

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1 The Hon. Dr Craig Emerson, Second Reading Speech, *House of Representatives Hansard*, 27 May 2010, p. 1.

2 Senate Economics References Committee, *The effectiveness of the Trade Practices Act in protecting small business*, March 2004, p. xviii and p. 64. Government (Coalition) Senators did not support this recommendation. p. 89.

The bill's provisions on section 50

2.5 The bill deletes the word 'substantial' from section 50(6). The Minister for Competition Policy and Consumer Affairs, the Hon. Dr Craig Emerson MP, explained that this would remove the risk that a court could adopt the view that acquisitions in geographically confined markets may not be considered substantial and therefore not fall within the scope of section 50.[3] It is important to note, however, that this amendment does not oblige the ACCC to examine the competitive impact of an acquisition on small markets. It is simply a clarification that it can, and that it is a relevant factor where there are issues.[4]

2.6 The bill also amends section 50 to replace references to 'a market' with references to 'any market'. The amendment will clarify the ability of the ACCC or a court to consider multiple markets when assessing mergers. In other words, a business cannot challenge a decision to block a proposed acquisition on the grounds that the substantial lessening of competition would be in a market other than the primary market in which the acquisition would occur.[5] The ACCC will be able to examine the effects of a proposed merger in both upstream and downstream markets.

2.7 The Minister explained that together, these amendments will clarify the operation of section 50 as it is currently interpreted by the ACCC, as set out in its November 2008 publication, *Merger Guidelines*.[6]

Acquisition of greenfield sites

2.8 In addition, the government proposes to ensure that the ACCC can examine the acquisition of greenfield sites and not just existing businesses. There have been some queries as to whether the ACCC has the power to review acquisitions of greenfield sites. In particular, the government's intent is to ensure that the ACCC can review acquisitions by the major supermarket chains of interests in new sites to investigate whether such acquisitions could substantially lessen competition.[7]

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3 The Hon. Dr Craig Emerson, Second Reading Speech, *House of Representatives Hansard*, 27 May 2010, p. 2.

4 See Mr Dave Poddar, Law Council of Australia, *Proof Committee Hansard*, 9 June 2010, p. 13.

5 The Hon. Dr Craig Emerson, Second Reading Speech, *House of Representatives Hansard*, 27 May 2010, p. 2.

6 The Hon. Dr Craig Emerson, Second Reading Speech, *House of Representatives Hansard*, 27 May 2010, p. 1.

7 The Hon. Craig Emerson, 'Government to secure powers to deal with creeping acquisitions', *Media Release*, 22 January 2010.

Senate Economics Committee's inquiries

2.9 This committee has examined the issue of creeping acquisitions in the context of section 50 on two previous occasions during this parliamentary term. In August 2008, the committee reported on the provisions of the Trade Practices (Creeping Acquisitions) Amendment Bill 2007.[8] The bill was introduced into the parliament by Family First Senator Steve Fielding in September 2007. In May 2010, the committee reported on the provisions of the Trade Practices Amendment (Material Lessening of Competition—Richmond Amendment) Bill 2009. This bill was introduced into the parliament by independent Senator Nick Xenophon on 26 November 2009.[9]

2.10 Senator Fielding's bill advocated a timeframe within which the courts and the ACCC would be directed to determine whether an acquisition had the effect of substantially lessening competition. It proposed that an acquisition could be prohibited if it and any one or more other acquisitions by the company in the previous six years together have the effect, or are likely to have the effect, of substantially lessening competition.

2.11 The committee report on Senator Fielding's bill recommended that the Senate defer its consideration until the Government's legislation on creeping acquisitions is presented.[10]

2.12 Senator Xenophon's bill proposed that a corporation that already has a substantial share of a market would be prohibited from acquiring shares or an asset which would have the effect of lessening competition in a market. The bill also proposed a lower threshold for the section 50(1) prohibition, replacing a 'substantial' lessening of competition with a 'material' lessening of competition.

2.13 The Committee's report rejected the 'Richmond Amendment'. It argued that setting a percentage market share threshold would be both arbitrary and contentious. If the threshold is set too low, it may prevent relatively small firms with a sizeable share of a local market from merging to increase efficiency and competitiveness.[11]

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8 Standing Committee on Economics, *Trade Practices (Creeping Acquisitions) Amendment Bill 2007*, August 2008.

9 Senate Economics Legislation Committee, *Trade Practices Amendment (Material Lessening of Competition—Richmond Amendment) Bill 2009*.

10 Standing Committee on Economics, *Trade Practices (Creeping Acquisitions) Amendment Bill 2007*, August 2008, p. 9.

11 Senate Economics Legislation Committee, *Trade Practices Amendment (Material Lessening of Competition—Richmond Amendment) Bill 2009*, p. 26.

The government's inquiry process

2.14 The Australian Labor Party pledged prior to the 2007 federal election that in office, it would enact laws to deal with creeping acquisitions by amending section 50 of the TPA.

2.15 In July 2008, the ACCC released its report into the competitiveness of retail prices for standard groceries. Although it noted that creeping acquisitions do not appear to be a significant current concern in the supermarket retail sector, the ACCC supported the introduction of a general creeping acquisition law. It noted that given 'particular structural features' of the retail supermarket industry, 'creeping acquisitions are a potential area of concern'.[12]

2.16 The Second Reading Speech to this bill notes that following the ACCC's report, the government subsequently undertook 'extensive public consultations in 2008 and 2009 to seek the community's view on possible reform options'.[13] These consultations were initiated through two government discussion papers. The first, released in September 2008, noted two possible approaches to addressing concerns about creeping acquisitions:

- to prohibit a corporation from making an acquisition if, when combined with acquisitions made by the corporation within a specified period, the acquisition would be likely to substantially lessen competition in a market; or
- to add a new prohibition to section 50 whereby a corporation must not make an acquisition if it already has a substantial degree of power in a market, and the acquisition would result in any lessening (as opposed to substantial lessening) of competition in the market.[14]

2.17 The committee notes the strong similarities between these proposals and Senators Fielding and Xenophon's private members bills (see above).

2.18 The government released a second discussion paper in May 2009. This paper invited comment on two further options to implement a creeping acquisitions law:

- to prohibit mergers and acquisitions that enhance a corporation's existing substantial market power where a direct or indirect acquisition of shares or assets 'would have the effect, or be likely to have the effect, of enhancing that corporation's substantial power in that market' (thereby avoiding the phrase 'substantial lessening of competition'); or

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12 ACCC, 'Report of the ACCC inquiry into the competitiveness of retail prices for standard groceries', July 2008, p. xxi.

13 The Hon. Dr Craig Emerson, Second Reading Speech, *House of Representatives Hansard*, 27 May 2010, p. 1.

14 Treasury, First Discussion Paper—Creeping Acquisitions, http://www.treasury.gov.au/documents/1409/PDF/Discussion%20Paper%20-20Creeping%20Acquisitions.pdf (accessed 9 June 2010).

- to give the Minister the power to unilaterally 'declare' a corporation where s/he has concerns about potential and/or actual competitive harm from creeping acquisitions.[15]

2.19 On 22 January 2010, the Minister for Competition Policy and Consumer Affairs, the Hon. Dr Craig Emerson MP, announced that the government will move to ensure that the ACCC has the power to reject acquisitions that would substantially lessen competition in any local regional or national market. As chapter 1 noted, the bill was introduced into the parliament on 27 May 2010.

Views on the 'creeping acquisitions' provisions

2.20 This section canvasses the comment the committee received on the creeping acquisitions provisions in the bill. The majority of this comment related to the amendment to section 50(6) and the implications of removing the word 'substantial' for the ACCC's analysis of mergers and acquisitions.

A minor clarification

2.21 Several submitters to both this inquiry and the committee's inquiry into the Richmond Amendment in April this year expressed the view that the section 50 amendments are merely a clarification of existing understanding and practice.

2.22 The ACCC have stated they already consider the competitive effects of an acquisition on a local market when assessing section 50(1) cases. Mr Tim Grimwade told the committee:

> We act on the basis, and have acted on the basis, that we have jurisdiction to deal with local markets. In fact, it is an incredibly important part of merger review, because there are so many retail acquisitions of import that occur in local markets, and we have blocked transactions where mergers occur in local markets on the basis of local markets. There has been some legal doubt expressed to us whether a substantial market encompasses a local market. The government's announcement to ensure that it is clear that a local market can be a substantial market does shore up our ability to deal with mergers in local markets.[16]

2.23 The Law Council argued that of all the options raised over the past few years to reform section 50, this bill's proposals are 'least objectionable' because they largely clarify existing merger law and practice.[17] Mr Dave Poddar, the Chair of the Law Council's Trade Practices Committee, elaborated:

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15 Treasury, Second Discussion Paper—Creeping Acquisitions, http://www.treasury.gov.au/documents/1530/PDF/Discussion_paper_Creeping_Acquisitions.pdf (accessed 9 June 2010).

16 Trade Practices Amendment (Material Lessening of Competition—Richmond Amendment) Bill 2009; Mr Tim Grimwade, *Committee Hansard*, 9 April 2010, p. 32.

17 Law Council of Australia, *Submission 1*, p. 2.

> …our committee notes that the proposed amendments are largely pragmatic responses to the government's desire to implement legislative change to account specifically for the possibility of harmful creeping acquisitions not caught by the current legislation. As such, and taking into account the governmental commitment to amending section 50 of the TPA, our committee believes the proposed amendments are the least objectionable because they largely clarify the existing merger law and practice without making substantial and unnecessary amendments to the operation of section 50 of the act, retain the economic rationality of the current merger test and are consistent with the existing architecture of the substantial lessening of competition test in section 50 and other provisions in part IV of the TPA.[18]

2.24 The Law Council argued that in its opinion, that ACCC already considers the effects on a local market when considering the provisions of section 50(1). In evidence during the committee's hearing into the Richmond Amendment in April this year, the Law Council noted that:

> The ACCC, when looking at the Woolworths acquisition of those FAL stores in Perth, undoubtedly looked at each individual local area as a separate market and considered the acquisition in each separate local market. I was advising the ACCC.[19]

2.25 Mr Milton Cockburn, Executive Director of the Shopping Centre Council of Australia was asked his opinion of the government's proposed change to section 50. He responded:

> …my understanding of Minister Emerson's media statement in January was that it was a clarification. I think, if you look at a lot of the mergers and acquisitions that have been examined by the ACCC, they have got down to the nitty-gritty of local markets. I think someone has referred to the Woolworths acquisition of FAL and its acquisition of some of the old Franklin sites, the recent Caltex-Mobil examination and the Westfield acquisition of the AMP Shopping Centre Trust. In all of these cases, my understanding is that the ACCC looked at the impact upon local markets. My understanding is that a legal opinion was floating around that said, by examining the impact on the local markets, the ACCC was possibly in contravention of the Trade Practices Act simply because the word 'local' is not mentioned; it refers to…national or state regional markets but not local markets.[20]

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18 Mr Dave Poddar, *Proof Committee Hansard,* 9 June 2010, p. 9.

19 Trade Practices Amendment (Material Lessening of Competition—Richmond Amendment) Bill 2009; Dr Phillip Williams, *Committee Hansard*, 9 April 2010, p. 17.

20 Trade Practices Amendment (Material Lessening of Competition—Richmond Amendment) Bill 2009; Mr Milton Cockburn, *Committee Hansard*, 9 April 2010, p. 34.

The need for more action

2.26 Other witnesses and commentators have argued that the amendments to section 50 are indeed minor and they needed to go further. For example, the Motor Trades Association of Australia (MTAA) expressed doubt as to whether the bill addresses its concerns about creeping acquisitions. It noted in its submission that throughout the inquiry process, the MTAA has supported a more significant change to the Act. Its preference is for a provision prohibiting a corporation from making an acquisition if it already has a substantial degree of power in a market and the acquisition would result in any lessening of competition in that market (see paragraph 2.16).[21]

2.27 *Choice* was quoted in the *Australian Financial Review* as saying that the bill simply reinforces the powers the ACCC already has. Mr David Howarth, *Choice*'s senior policy officer said that the bill therefore does not address the issue of creeping acquisitions.[22] In the same article, Minter Ellison partner Mr Richard Murphy was quoted as saying:

> It doesn't matter if it's a geographically large market or a geographically small market, at the end of the day it has to be recognisable as an economic concept as a separate market.[23]

2.28 Mr Ken Henrick, Chief Executive Officer of National Association of Retail Grocers of Australia (NARGA), told the committee that the effectiveness of the legislation will depend on the ACCC's response.[24] On this score, however, he argued that the ACCC had failed in the past:

> They have had laws like this. For example, the Baird committee recommended including the word 'regional' so that a smaller market could be looked at. They were trying to do in the context of 1999 what this bill is trying to do now. It has had no effect on the way the ACCC has operated.[25]

Micromarkets

2.29 The committee asked Treasury why it was necessary to remove the word 'substantial' from section 50(6). Treasury noted the comments of Justice French in the Federal Court case of *AGL v ACCC*.[26] Justice French observed that there were

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21 Motor Trades Association of Australia, *Submission 7*, p. 2.

22 Sam McKeith, 'TPA reform wins few supporters', *Australian Financial Review*, 28 May 2010, p. 3.

23 Sam McKeith, 'TPA reform wins few supporters', *Australian Financial Review*, 28 May 2010, p. 3.

24 Sam McKeith, 'TPA reform wins few supporters', *Australian Financial Review*, 28 May 2010, p. 3.

25 Mr Ken Henrick, *Proof Committee Hansard*, 9 June 2010, p. 19.

26 *Australian Gas Light Company v ACCC* [2003] FCA 1525

circumstances in which a substantial lessening of competition (section 50(1)) could arise in a particular market, but because it was not held to be substantial (section 50(6)) it might fall outside of the ACCC's ability to block that acquisition.[27]

2.30 However, the Law Council expressed concern that the proposed amendments will result in the ACCC undertaking greater analysis of 'very small submarkets which are not economically distinct' and should not form part of the ACCC's section 50 assessment.[28] Mr Poddar was asked his opinion on how to define the smallest market for which section 50 concerns might arise. He responded:

> It has to be something meaningful to the level of competition. We do not have something which creates thresholds of turnover, as some countries do. The commission has the ability to come in and look at markets which may involve very small amounts of commerce if the products which are in those markets are critical and relevant to products or sales of different products. It is not possible to give you a definitive answer as to how small that number could be. I am aware that the commission has looked into mergers which are in a numeric matter of $4 million, over the years that I have been a practitioner on the other side of the commission. I have been in transactions where the commission has looked into mergers involving $250,000. Hence some of our comments about the fact that we need to be very mindful about just how far regulators move down into commerce and what actually is a significant degree of commerce.[29]

2.31 The Business Council of Australia (BCA) has also expressed concern that the amendment to section 50(6) of the Act will have the effect of 'unnecessary examination of less than economically meaningful markets that are not substantial'. It argued that this would create unnecessary burdens and costs for business which would in turn dampen economic activity and investment. The BCA recommended that the bill should provide for a review of its effect after two years.[30]

Spillover effects

2.32 The Law Council also expressed concern at the effect of the bill's amendments on industry sectors other than supermarkets. Mr Poddar told the committee that the amendments will apply across all industry sectors, including to those sectors about which no concerns have been raised. He argued that while the intention of the bill is a general amendment, there is a need for the ACCC to minimise

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27 *Australian Gas Light Company v ACCC* [2003] FCA 1525, paragraph 353. Justice French noted that the case 'does not appear to throw up any dispute between the parties that, whichever of their propounded markets is in issue, it is a 'substantial market' for the purposes of section 50(6).

28 Law Council of Australia, *Submission 1*, p. 3.

29 Mr Dave Poddar, *Proof Committee Hansard*, 9 June 2010, p. 13.

30 Business Council of Australia, *Submission 5*, p. 2.

extra cost to industry by being mindful of how it administers across sectors where there have not been concerns.[31]

2.33 Mr Gerard van Rijswijk, Senior Policy Advisor at NARGA, dismissed these 'spillover' concerns as largely irrelevant. He told the committee that:

> …if other industries were not as concentrated, they would not be as affected. The problem is concentration. Section 50 deals with the competitive issues that result from overconcentration in relation to acquisitions and mergers. If the other industries do not have that problem then they will have nothing to worry about.[32]

Market size or market power?

2.34 In its evidence to the committee, the Law Council distinguished between the use of the word 'substantial' in section 50(1) and in section 50(6). In section 50(1), the word is used in the context of the effect of the acquisition on competition. In section 50(6), 'a substantial market' relates to the scale of the market in which the competition takes place. Mr Poddar expressed the Law Council's concerns at the bill's amendment to section 50(6) through a sporting analogy:

> Our concern that the football field, or the field in which the dynamics of competition are assessed, does not become tiny—that it does not in fact become the square in which the ball is bounced. The appropriate market is the football field so you can see all the dynamics of competition.[33]

2.35 It was put to Mr Poddar that the key issue is not the size of the field (market size) but the unequal number of players on the teams (market share). He responded:

> It is not the market share that it is important; it is the conditions of competition. It is the entry barriers, the ability for people to enter into that football field and compete vigorously. We think it is wrong to look and focus too narrowly on concentration figures because concentration figures do not show the real dynamics of competition. They do not show a vigorous new entrant who comes in and competes vigorously whether it is a tall ruckman or a fantastic rover. What you should be looking at is how that competition actually occurs on the football field, not the shares of those football fields because competition changes every day.[34]

2.36 Other submitters disagreed with this analysis and emphasised the importance of market share in the context of assessing mergers. NARGA, notably, told the committee that:

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31 Mr Dave Poddar, *Proof Committee Hansard*, 9 June 2010, p. 12.

32 Mr Gerard van Rijswijk, *Proof Committee Hansard*, 9 June 2010, p. 20.

33 Mr Dave Poddar, *Proof Committee Hansard*, 9 June 2010, p. 10.

34 Mr Dave Poddar, *Proof Committee Hansard*, 9 June 2010, p. 10.

> …the real nub of competition is having many competitors, each having a small share of the market, competing with each other and improving the market as a whole. That is competition, and nobody seems to think of that as the model of competition on which the Trade Practices Act should be based or should regulate. In fact, the act has no definition of competition. It just assumes everybody knows what it is.[35]

The Herfindahl-Hirschman Index

2.37 NARGA referred in its submission to the Herfindahl-Hirschman Index (HHI). The Index is a measure of the size of firms in relation to the industry and an indicator of the amount of competition among them. It is defined as the sum of the squares of the percentage market shares of each individual firm.[36]

2.38 The HHI can range from 0 to 10 000 moving from a very large amount of very small firms to a single monopolistic producer. Where there are only two firms of equal size, the HHI will be 5000. Where there are many firms of different size and the HHI is around 1000, for example, the degree of concentration is equivalent to ten firms of equal size.

2.39 NARGA noted that in other jurisdictions, notably the United States, the quantification of market share is an important part in the merger approval process. It observed that:

> In the USA a post merger market with a HHI of less than 1000 is defined as 'unconcentrated', between 1000 and 1800 as 'moderately concentrated' and above 1800 as 'highly concentrated'. A merger potentially raises 'significantly competitive concerns' if it produces an increase in the HHI of more than 100 points in a moderately concentrated market or more than 50 points in a highly concentrated market. A merger is presumed 'likely to create or enhance market power or facilitate its exercise' of it produces an increase in the HHI of more than 100 in a highly concentrated market.[37]

2.40 Mr van Rijswijk contrasted the approaches of the Australian and American regulators in their use of the HHI:

> The US regulators look at a market of 1,000 or higher post merger as being of concern. The ACCC, where our markets are much more concentrated already, do not bother looking at the market until it is over 2,000. That is a much higher level of concentration. In fact 2,000 in terms of the regulator in the USA is above their 1,800 threshold which they regard as highly concentrated. That is significant in the USA context because at that level of concentration antitrust laws kick in where they can actually require the market to be split up. We do not have those provisions in the act. The US regulators are quite active on the concentration issue. They see

35 Mr Gerard van Rijswijk, *Proof Committee Hansard*, 9 June 2010, p. 17.

36 National Association of Retail Grocers of Australia, *Submission 4*, p. 2.

37 National Association of Retail Grocers of Australia, *Submission 4*, p. 4.

> concentration as being the major problem in the lack of competition within the market.[38]

2.41 Treasury was asked why the HHI was not a greater determinant in the merger and acquisition approval process in Australia, as it is in the United States. Mr Andrew Deitz responded:

> One of the things I would point out is that the HHI is one of many indicators used by the commission when considering the state of competition in a particular market, as it is with the US. Market shares are always a factor that everyone does consider, but I would not place it any higher than it is—something which is a factor considered in a broader competition analysis. So the reference to the USA merger guidelines and the extent to which they talk about HHIs, yes, they do have a view about what the numbers mean; but it is a rebuttable presumption.[39]

2.42 Treasury also noted that the merger guidelines published in the United States this year diminished the importance of market shares as determinative in looking at whether a merger is likely to substantially lessen competition.[40] The committee notes the following observation in the guidelines:

> The purpose of these thresholds is not to provide a rigid screen to separate acceptable mergers from anticompetitive transactions, although high levels of concentration do raise concerns. Rather, they provide one way to identify those mergers for which it is particularly important to examine whether other competitive factors confirm, reinforce, or would counteract the potentially harmful effects of increased concentration. The higher the post-merger HHI and the increase in the HHI, the greater is the likelihood that the Agencies will request additional information to conduct their analysis.[41]

'Any market'—the section 50(1) amendment

2.43 The committee received some comment on the bill's amendment to section 50(1), changing 'a market' to 'any market'. The MTAA welcomed the amendment stating it should allow the ACCC to consider all markets in which the acquirer is active in relation to any merger matter.[42]

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38 Mr Gerard van Rijswijk, *Proof Committee Hansard*, 9 June 2010, p. 18.

39 Mr Andrew Deitz, *Proof Committee Hansard*, 9 June 2010, p. 5.

40 Mr Andrew Deitz, *Proof Committee Hansard*, 9 June 2010, p. 5. The proposed US Guidelines have been released for public comment: http://www.ftc.gov/os/2010/04/100420hmg.pdf (accessed 10 June 2010).

41 *Horizontal Merger Guidelines: For public comment*, Released 20 April 2010, p. 18; http://www.ftc.gov/os/2010/04/100420hmg.pdf (accessed 10 June 2010).

42 Motor Trades Association of Australia, *Submission 7*, p. 2.

2.44 While supporting the change, NARGA argued that the phrase 'any market' needs to be clarified. It noted that the grocery market is composed of a number of subsets from the full range of grocery products supplied through a large supermarket, to packaged groceries, fruit and vegetables, meat, delicatessen goods, milk and bread. Each of these markets could be differentially affected by an acquisition in a local market. NARGA urged for guidelines to explain how the ACCC will interpret the 'any market' definition.[43]

2.45 Master Grocers Australia and Liquor Retailers Australia supported NARGA's proposal. They argued in their submission that:

> The inclusion of the word "any" should enable the ACCC to embrace the impact on all markets that are likely to be affected by an acquisition rather than being limited to a single market. There is no doubt that in order to ensure that the amendments are effective, they need to be tested and MGA supports the views expressed by National Association of Retail Grocers Australia (NARGA) in its submission, in particular, the call for Guidelines which would provide a clear interpretation of the amended clauses.[44]

Committee view

2.46 The committee supports the government's proposed amendments to section 50 of the TPA. While the amendments may seem fairly minor points of clarification, it is important that the regulator, the courts and the public at large understand that the ACCC can consider a local market in their assessment of section 50.

43 NARGA, *Submission 4*, p. 5.

44 Master Grocers Australia, *Submission 6*, p. 2.