Chapter 3

The premise of the bill

3.1 This chapter focuses on the claim made by the drafter of the legislation that the need for action on creeping acquisitions reflects the Australian Competition and Consumer Commission's (ACCC) highly permissive approach to merger applications.

The high rate of merger approval

3.2 The principal argument put by the proponent of the bill to amend section 50(1) is that the current rate of merger approvals by the Australian Competition and Consumer Commission (ACCC) is too high. Associate Professor Frank Zumbo argues that the ACCC approves 97 per cent of all merger and acquisition applications and that as a result, 'Australia has some of the most highly concentrated markets in the world'.[1]

3.3 In evidence to the committee, Associate Professor Zumbo explained how the figure of 97 per cent was calculated:

> In the year 2008-09 there were 412 mergers considered. The number not opposed outright was 397; opposed outright, 10. When I get to around the 97 per cent figure I look at the number totally opposed outright. On that number, 10 out of 412, you get 97.57 per cent. There is a further category—and I add this for the sake of clarification—that says 'applications resolved during review through undertakings'. That represents a further five cases. That is a case where the ACCC has raised concern and the parties have given undertakings to the ACCC that satisfy the ACCC. That is a further five. Even if you add that further five as having been stopped by the substantial lessening of competition test, then that is a further one per cent. That takes you down to roughly 96.57 per cent. So, the 97 per cent number is looking at the opposed outright, but I do accept that there is some flexibility and I am happy to throw in those extra five or that extra per cent and you are still around 97 per cent.[2]

Criticism of this analysis

3.4 Both Treasury and the ACCC have queried Associate Professor Zumbo's analysis. The following section canvasses their respective arguments.

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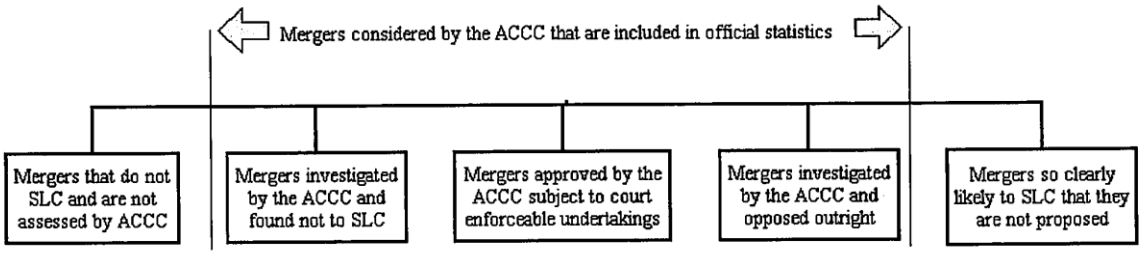
1 Associate Professor Frank Zumbo, *Submission 14*.

2 Associate Professor Frank Zumbo, *Proof Committee Hansard*, 9 April 2010, p. 19.

Treasury's analysis

3.5 In its submission, Treasury noted that the percentage of mergers opposed and not opposed is not a good measure of the effectiveness or application of the merger test because some merger matters are not included in the official statistics.



3.6 Treasury's submission included the above diagram by way of illustration. The boxes on the far left and far right of the spectrum represent those merger categories that are excluded from the official statistics.

3.7 The far left box represents those mergers that do not substantially lessen competition and are not assessed by the ACCC. A large proportion of the merger matters that are considered but not opposed by the ACCC are referred to it by the Foreign Investment Review Board (FIRB) or the Australian Prudential Regulatory Authority (APRA) or by the merger parties as a matter of courtesy. These do not raise competition concerns.

3.8 The far right box represents those mergers so likely to substantially lessen competition that they are not proposed. These mergers are prevented by section 50(1) 'even though they are not recorded as having been proposed by the ACCC'.[3]

3.9 The three middle boxes are those mergers that are considered by the ACCC and are either found not to substantially lessen competition, are approved subject to enforceable court undertakings or are opposed outright.[4]

3.10 Associate Professor Zumbo did note that the mergers included in the official statistics and those so 'likely to substantially lessen competition that they are not proposed' are more likely to arise in concentrated markets. He told the committee that in a highly fragmented market, the parties are unlikely to go to the ACCC unless they want 'a letter of comfort'.[5]

3.11 Nonetheless, the key point to make is that if those mergers in highly fragmented markets represented in the far left box were included in Professor Zumbo's calculations, the merger approval figure would be significantly less than 97 per cent.

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3 Treasury, *Submission 15*, p. 2.

4 Treasury, *Submission 15*, p. 3.

5 Associate Professor Frank Zumbo, *Proof Committee Hansard*, 9 April 2010, p. 19.

3.12 The ACCC was also critical of Associate Professor Zumbo's merger approval statistic of 97 per cent. Mr Tim Grimwade of the ACCC told the committee that the figure of 97 per cent cannot be a meaningful measure of the effectiveness of the test. He gave three main reasons why this is the case.

3.13 First, it does not take into account the nature of the matters that the ACCC reviews. Specifically, there are many merger clearance requests—'between 100 and 200 a year'—referred to the ACCC by the FIRB. The vast majority of these raise no concerns 'because they relate usually to a new entrant coming in and buying an asset or business in Australia'. Mr Grimwade noted that these instances:

> …clearly would inflate the denominator, if you are going to start using a 97 per cent statistic to measure the effectiveness of the test.[6]

3.14 Second, there are matters that do not require review and important sub-categories among those that do require a review. The ACCC explained that in this financial year it has sought to distinguish between pre-assessed mergers that do not require any review and those that do. In the 2009–2010 financial year, about 120 merger requests have been pre-assessed without any review, leaving 'about 118' that require review.[7] Of those requiring review:

- some are opposed outright;
- some are accepted that would otherwise have been blocked but for a remedy being proposed and accepted by the commission; and
- some are put for review but 'withdrawn before we give our final decision'. There were 'around 21' of this category last year and 'another 10 already' this financial year.[8]

These categories accord with the three middle boxes in Treasury's diagram (above).

3.2 Third, the ACCC emphasised that there is no legal obligation by parties to notify the Commission of a merger proposal. Instead, the ACCC structures and incentivises notifications 'to capture a really large number of mergers' in order to ensure that it can block any anticompetitive merger. Mr Grimwade explained:

> If we had a mandatory notification process—and we have given it some thought—it would have all sorts of adverse consequences. For instance, it would send a signal to those that do not meet the notification thresholds—because you have to have a threshold for notification—that perhaps their merger is okay when in fact it might not be.[9]

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6 Mr Tim Grimwade, *Proof Committee Hansard*, 9 April 2010, p. 27.

7 Mr Tim Grimwade, *Proof Committee Hansard*, 9 April 2010, p. 27.

8 Mr Tim Grimwade, *Proof Committee Hansard*, 9 April 2010, p. 27.

9 Mr Tim Grimwade, *Proof Committee Hansard*, 9 April 2010, p. 28.

3.3 The ACCC was asked its view as to how many mergers and acquisitions are prevented by the substantial lessening of competition test. Mr Grimwade gave the following response:

> …having regard to the matters that we review, leaving aside the matters we do not review that we pre-assess do not require review, and you include the matters we oppose, the matters we would have opposed but for accepting a remedy or the matters that were withdrawn, you end up this financial year looking at about 77 per cent, I think. I think it is a furphy to use a statistic like that to make such a big decision on changing a test of this function effectively for two decades that is consistent with international best practice and has largely generated very good outcomes for the Australian economy.[10]

International comparisons

3.15 Ms Julie Clarke of Deakin University has argued that the approval of roughly 95 per cent of merger proposals notified to the ACCC in any given year does not necessarily mean that the 'substantial lessening of competition test' is set too high. Indeed, she noted in her submission to the inquiry that this:

> …percentage is consistent with the percentage of notified mergers challenged in most other OECD jurisdictions. In the United States, for example, the percentage of notified mergers challenged is routinely lower than that challenged in Australia. This statistic simply reflects the fact that the vast majority of mergers do not raise competition concerns. It does not imply that the law itself is too lenient.[11]

3.16 Associate Professor Zumbo told the committee that comparisons of merger approvals between Australia and the United States must be seen in context. He explained:

> Our concern in Australia is that our markets are getting even more concentrated and quickly so. If you have a 97 per cent approval rating in the United States, which is a much bigger market, it takes a lot longer to get to the level of concentrations that you have in Australia if it is the same approval rating of 97 per cent. We need to look at each country on its own merits, as we have to look at each merger on its own merits.[12]

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10 Mr Tim Grimwade, *Proof Committee Hansard*, 9 April 2010, pp 31–32.

11 Ms Julie Clarke, *Submission 6*, p. 2.

12 Associate Professor Frank Zumbo, *Proof Committee Hansard*, 9 April 2010, p. 21.