Global mergers

Australia's competition laws are the world's best

— reports the 16 May 1998 issue of **The Economist** in relation to a survey comparing competition law around the world taken for the IMD, A Swiss business school, World Competitiveness Yearbook.

The last 18 months have seen a dramatic increase in the number of global mergers — not all having a direct impact on Australia — a trend that shows no sign of slowing. There has also been an increase in the number of Australian companies looking at offshore mergers and acquisitions.

Some factors driving many are the need to cut costs, increase productivity, and enhance efficiencies of scale in efforts to remain competitive in the global marketplace.

This increased activity is resulting in a number of interesting challenges for industry, the Commission and other overseas competition regulators. An interesting point is that the majority of global transactions the Commission scrutinises relate to consumer goods.

It's now settled law that the Commission has the power to deal with mergers that are primarily overseas mergers. The precedent was set by the 1992 Federal Court case dealing with the US-based Gillette Company's proposal to acquire the world-wide Wilkinson Sword wet shaving operations. The Commission was concerned that it would result in Gillette dominating the Australian market.

Gillette notified the Commission that it had completed the acquisition of Wilkinson Sword's Australian assets through a series of offshore transactions involving New Zealand companies. The transactions had been carried out in such a way that they appeared to fall outside the extra-territorial scope of the Trade Practices Act. The court found that they did not.

Gillette appealed all the way to the High Court, eventually admitting defeat and giving the court undertakings that it would license the Australian operations to an independent and unrelated company.

Commission approach to mergers

The Commission looks at merger proposals on a case-by-case basis using a five-stage assessment process: market definition, market concentration, potential or real import competition, barriers to entry, and other factors such as countervailing power. Essentially the Commission follows a framework of legislation.

Its revised **Merger guidelines** — published this month and available from all offices for $10 — outline its approach. The guidelines indicate the factors it considers when conducting investigations.

Critical mass

A frequently asked question is whether the merger provisions of the Trade Practices Act prevent Australian firms reaching the critical mass required (the size necessary) for them to be able to take part in global markets.

The Commission believes that mergers (and other collaborative agreements) do not necessarily enhance a firm's ability to compete internationally. It can be argued that internationally competitive businesses are more likely to develop where there is effective domestic competition, rather than national dominance.

Possible solutions to competition concerns

Merger proposals don't have to be abandoned if they do not comply with the merger conditions in a given country. The Commission utilises many methods to allow them to continue in Australia.

Authorisation can be granted, if the public benefits offset competition concerns. For example, export generation, import replacement and contributions to the international competitiveness of the Australian economy.

In some mergers the anti-competitive effects of an acquisition can be counter-balanced by divesting certain brands, trademarks or assets to an independent third party.

If a country objects (or is likely to object) to a global proposal, the proposal can be structured so that assets in that country are excluded from the proposed acquisition. The bulk of the merger can then proceed.

Merging companies can give the Commission s. 87B undertakings in order to allow an anti-competitive merger to proceed. In this context the merging parties agree to meet certain conditions designed to neutralise or balance the anti-competitive effects of the proposal.

In cases where import competition is constrained by tariff restrictions or standards it is possible that changes to the regulation may overcome the constraint. The entry of viable imports into the market would be an effective restraint on the potential misuse of market power, and could reduce the potential anti-competitive effects of a merger.

Case examples

- Adelaide Brighton Limited (ABL) conducted informal negotiations with the Commission in relation to a number of transactions it wanted to enter into which would affect the cement and lime markets. There were potential competition concerns under s. 50 and ABL lodged two authorisation applications. Authorisation enabled the Commission to balance the benefits to the public that would result against the detriments. The issues that concerned the Commission were addressed by s. 87B under-takings offered by the parties. Authorisation was granted for both applications.

- Guinness Plc and Grand Metropolitan Plc world-wide merger in late 1997 — production, marketing and sales of spirits and beers around the world, publishing and hotels — had regulators around the world consulting about the global effects and concerned about market conditions in their respective jurisdictions. In Australia the Commission felt the merged firm would control a number of category leaders but that concentration level increases would be confined to the vodka and gin categories, and would be minimal in the largest category, scotch. It allowed the merger to go ahead without conditions.

- Divestiture was the answer to allowing the PepsiCo acquisition of United Brands (Smith's Snackfoods) to proceed. The process resulted in the creation of Snack Brands Australia to take over the divested facilities and brands. The new company was bought by Dollar Sweets Holdings (the owner of Players Biscuits and AV Jennings Homes).

- Section 87B undertakings to neutralise the Commission's concern about the anti-competitive effects enabled the Ampol and Caltex merger to proceed. The undertakings provided for the sale of surplus imports, storage and retail sites to independent distributors and retailers, with guaranteed supply of petrol at a competitive price during a transition phase.

- Rationalisation was behind Email Limited's acquisition of Southcorp Limited's whitegoods business — and demonstrated how the Trade Practices Act is not an obstacle to mergers in sectors exposed to international competition. Both companies are major Australian manufacturers of whitegoods products and felt rationalisation was necessary to achieve international competitiveness.

- British American Tobacco's proposed world-wide merger with Rothmans International was one that was not allowed to proceed in Australia because it would have substantially lessened competition in the Australian cigarettes market by giving the merged company a stranglehold control of market share and nearly all major Australian cigarette brands. The parties are still in discussions with the ACCC.

  The parties submitted that proposed tax changes would lead to increased import competition but Commission inquiries indicated otherwise: there would be barriers to establishing retail distribution links independently of incumbent suppliers; existing trading arrangements between manufacturers and retailers would restrict opportunities for new entrants to gain brand visibility, recognition and loyalty; and advertising restrictions would limit the ability to build brand images.

- The Coca Cola Company's proposed acquisition of Cadbury Schweppes' beverage brands in more than 120 countries illustrates how a global merger can be structured to leave some key markets outside its scope. The proposal did not apply to the US, France or South Africa. The Commission blocked it in Australia on the grounds that there would be a substantial lessening of competition in the markets for the production and wholesale supply of carbonated soft drinks. The ACCC is currently considering a revised proposal covering certain brands and assets of Cadbury Scheweppes.

Uniform competition laws and cooperation

Companies participating in global mergers are often forced to address competition concerns in several jurisdictions simultaneously. The resulting increased transaction costs may deter the merger, but all countries have the right to examine a proposal to ensure it will not be detrimental to its own markets.

A medium needs to be found, and the increasing cooperation between regulators is a move in the right direction, particularly if companies waive confidentiality requirements and allow information to be shared.

A uniform notification procedure would help — a basic set of questions could be adopted which would provide the information required by all relevant competition agencies.

This would probably be in addition to existing national laws but it would have two benefits. First, it may lead to the harmonisation of merger laws; and second, it would bring the transaction costs down.

Merger publications

The Commission's newly revised **Merger guidelines** and updated **Mergers: a statistical summary** will be published shortly. The guide will be available for $10 and the statistical summary will be free.