THE NEW MERGER GUIDELINES AND SECTION 50 OF THE *TRADE PRACTICES ACT*

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> For the strong or lucky, freedom of trade just means freedom to expand; it means the survival of the fittest and the eventual destruction of the weak. To the others, however, it means the opposite: a duty of the community to restore, as far as possible, conditions of freedom of competition. This means restraint by legislative intervention and, at least to some extent, a denial of the very idea of freedom of trade. For inevitably, legislation which seeks to establish legal rules preventing the consequences of uninhibited competition, by which the strong may destroy the weak, must establish a legal apparatus, often of great complexity. This is the dilemma of all antitrust legislation.[1]

In the United States the accumulated learning on the merger guidelines runs to many thousands of pages as antitrust law, once described as a charter of economic liberty and now weighted with rules and guidelines, struggles to regulate the undesirable side effects of competitive forces.

In Australia the regulation of trade practices is reaching greater levels of complexity, with the laws regulating economic behaviour being readjusted regularly.

There are few areas of regulation that are capable of generating as much multi-

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1 W Friedman, *Law in Changing Society*, Penguin Books Ltd (1972) p 293.

disciplinary debate as the regulation of takeovers and mergers.

With the regularity of and, some would probably say strong correlation with, changes in fashion, the regulatory focus has changed in 20 years in Australia from proscribing mergers which substantially lessen competition, to those which create or enhance dominance and back again.

The mantra of competition is chanted with varying degrees of commitment by all sides of mainstream politics, while the social and economic goals that competition is to achieve are less clearly articulated, being enmeshed in the richer fabric of policy.[2]

Some might suggest that the new Merger Guidelines and changes to the legislation represent a continuation by government of a policy of abdication of merger policy to the Trade Practices Commission ("the TPC") and the courts. With the exception of clear cases of significant market power, the determination of whether a merger substantially reduces competition ultimately depends on a process which involves a subjective evaluation of conflicting economic evidence and an equally subjective authorisation process in giving weight to arguments of a public benefit. For example, in determining what constitutes a public benefit, the likely outcome depends to a significant extent on whether the analytical framework is driven by the Chicago economic school, which permits all mergers which may enhance efficiency, or a liberal multi-dimensional approach, which requires direct evidence of the existence of any matter which can be claimed as a public benefit.

While the debate continues about the relative benefits and costs of regulating competitive behaviour or market structures, most recognise the importance of Australia's unique economic and geographic position, with small, fragmented populations, small markets and substantial distances between markets.

The level of competition in Australia has received much comment. The Organisation for Economic Cooperation and Development has argued that Australia's market structures are not conducive to competition. Domestically, the Economic Planning and Advisory Council has provided data that evidences high levels of concentration in many Australian industries and increasing concentration in the manufacturing industry. Of course, this structural data must be viewed against the dynamics of behaviour in the relevant markets, including the threat of takeovers and entry of imports.

This is what the new merger law and the TPC's new Guidelines attempt to do.

This paper reviews the new Merger Guidelines and the recent amendments to s 50 of the *Trade Practices Act* 1974 (Cth) ("the Act"). This is not possible without appreciating a little of the legislative history, the position in some overseas jurisdictions and some of the arguments for and against a return to the pre-1974 competition test.

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2 See for example the amendment to *Trade Practices Act* 1974 (Cth) ("the Act") s 90 requiring the TPC to take into account exports and other matters affecting international competitiveness.

I. LEGISLATIVE HISTORY[3]

While early Australian trade practices legislation[4] contained provisions relevant to mergers, it did not explicitly or directly deal with the subject of merger regulation. The merger provisions operated almost indirectly. As one commentator noted:

> ... as a result of a merger a business may come to occupy a dominant position in the trade in goods or in the supply of services of a particular description. If the merged business then takes advantage of this acquired monopoly power contrary to the Act s 36(2) with s 37, it will attract the provisions of the Act. But this will be so only because of the consequences made possible by the merger, not because of the mere act of merger. A merger, simply because it is a merger, does not come within the *Trade Practices Act*.[5]

Direct regulation of mergers accompanied the commencement of the Act in 1974. As enacted, s 50 prohibited acquisitions which lead to a substantial lessening of competition in a market. This competition-oriented test operated from 1974 until 1977.

An extensive review of the Act was undertaken in 1976 by the Trade Practices Review Committee ("the Swanson Committee"). The Swanson Committee recommendations[6] included that the merger provisions should not apply to small acquisitions (of businesses with less than $3 million annual turnover). Following that report, the Government enacted legislation in 1977 to alter the competition test to the dominance test. Mergers and acquisitions became prohibited if the effect or likely effect of the merger or acquisition would be that a corporation would achieve a position of dominance or control in the marketplace. The amended prohibition was effective as of 1 July 1977, and remained operative until early 1993. Thus, while the monetary threshold was not adopted, the Government believed that the higher threshold of dominance would permit small acquisitions and, importantly, recognise the special needs of Australia's economy.

The amendment represented a fundamental change in the theoretical basis underpinning the regulation of mergers, from the regulation of behaviour to an attempt to prevent structures that would permit or enhance the likelihood of anti-competitive conduct.[7]

The stated rationale underlying the policy change was the belief that mergers would lead to economies of scale and that economies of scale were only possible in a closed economy like Australia if increased concentration was permitted. Potential for and actual undesirable anti-competitive effects would be regulated by sections of the Act designed to prevent the abuse of market power.[8]

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3 A summary of the various committees that have considered s 50 is set out in Appendix A to this paper.

4 *Trade Practices Act* 1965 (Cth) as amended in 1966 and 1967.

5 PH Lane, *The Trade Practices Act: Its Constitutional Operation*, Law Book Company (1966) p 36.

6 See Appendix A.

7 The change in approach is examined in more detail in Part II of this paper.

8 Australia, House of Representatives 1977, Debates, vol HR 105, p 1478.

In 1984, after the election of the Hawke Labor Government, a Green Paper[9] recommended a return to the substantial lessening of competition test. This recommendation was not acted upon. The rejection of the Green Paper recommendation echoed the reasoning for the change from the competition test to the dominance test in the first place:

> The Government is firmly committed to the encouragement of efficient Australian industry and to increasing our competitiveness on world markets. It has been decided that the existing dominance test in s 50 should remain essentially unchanged.[10].

The dominance test was considered in 1978 in *TPC v Ansett Transport Industries*.[11] In that case, Northrop J, of the then newly created Federal Court of Australia, decided that the concept of dominance was something less than control. The implication was that the higher standard, that of control, became effectively redundant in the test for prohibited mergers; effectively, the only mergers prohibited were those resulting in a position of dominance in the marketplace.

In 1986 the TPC released its first Merger Provisions Guidelines.[12] These guidelines set out at length the approach that the TPC would generally adopt in its consideration of proposed mergers.

In the late 1980s, probably as a result of the increase in the number and size of mergers in Australia during the then boom period[13] and the resulting economic problems arising from the 1987 stock market crash and the subsequent recession, agitation for reform of the merger provisions of the Act began to gather momentum. In May 1989, a Report of the House of Representatives Committee on Legal and Constitutional Affairs ("the Griffith Committee") recommended that the dominance test be retained,[14] there being insufficient justification to change the law in a way which would result in undue interference in merger activity. However, dissenting opinions were recorded by two committee members, who felt that a substantial lessening of competition test should be reintroduced.[15]

In 1991, the Senate Standing Committee on Legal and Constitutional Affairs ("the Cooney Committee") considered the merger provisions of the Act. Despite what at best may be described as limited analytical evidence as to desirability of a change to the test, differences of opinion and a split of the Committee, it was recommended by majority that the test in s 50 be altered from the dominance test to the competition test.[16] The Committee found it difficult to reconcile the existence of a dominance test in an Act directed at preventing anti-competitive conduct and

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9 *The Trade Practices Act - Proposals for Change*, AGPS (1984) at [450].

10 Australia, House of Representatives 1986, Debates, vol HR 147, p 1627.

11 (1978) 32 FLR 305.

12 Trade Practices Commission, *Merger Guidelines*, 1986.

13 SG Corones, *Competition Law and Policy in Australia*, Law Book Company (1990) p 137.

14 House of Representatives Standing Committee on Legal and Constitutional Affairs, *Mergers, Takeovers and Monopolies: Profiting from Competition?*, 1989 at recommendation 4.

15 *Ibid* at 111-22.

16 Senate Standing Committee on Legal and Constitutional Affairs, *Mergers, Monopolies and Acquisitions: Adequacy of Existing Legislative Controls*, 1992 at [3.131]. See Appendix A.

believed that, if the Act incorporated appropriate statutory guidelines, any uncertainty resulting from changing the test would be reduced. Two dissenting views, representing three members of the Cooney Committee, were reported.[17] The minority did not accept that the dominance test had had a detrimental economic effect and favoured continual certainty of the dominance test.

In 1992 the matter came before Parliament and, following lengthy debate, the Government adopted the recommendations of the Cooney Committee. As a result, s 50 of the Act was amended so as to prohibit acquisitions and mergers which resulted in a substantial lessening of competition in a market for goods and services. This new test was introduced by *Trade Practices Legislation Amendment Act* 1992 (Cth) ("the amending Act"). Sections 50(1) and 50(2) provide:

> Prohibition of acquisitions that would result in a substantial lessening of competition
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> 50(1) A corporation must not 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 the effect, or be likely to have the effect, of substantially lessening competition in a market.
>
> (2) A person must not directly or indirectly:
>
> (a) acquire shares in the capital of a corporation; or
> (b) acquire any assets of a corporation;
>
> if the acquisitions would have the effect, or be likely to have the effect, of substantially lessening competition in a market.

Subject to the transitional provisions set out in s 21 of the amending Act, the amended prohibitions apply to all mergers occurring after 21 January 1993.

The amending legislation also included other amendments, most notably an increase in penalties for anti-competitive behaviour (including breaches of s 50) from $250,000 up to $10 million for corporations. This increase was designed to remedy what was described as a "woefully inadequate" figure, and "reflects the seriousness with which infringements of the competition provision are regarded, and the potential benefits that corporations could gain by such infringements".[18]

The TPC in November 1992 released for comment Draft Merger Guidelines in relation to the 1993 merger test.[19] The Guidelines provide detailed indications of the TPC's assessment of mergers. In October 1993 the TPC also released a joint discussion paper with the New Zealand Chamber of Commerce[20] on the approach that the relevant Australian and New Zealand authorities would take to companies seeking to merge to prevent financial collapse ("the failing company defence").

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17 *Ibid* at 135-43.

18 Senator Michael Tate, "Trade Practices Amendments come into Force", Media Release, 13 January 1993.

19 TPC, *Merger Guidelines - A Guide to the Commission's Administration of the Merger Provisions (ss 50/50A) of the Trade Practices Act*, Draft for comment, 1992.

20 The New Zealand counterpart to the TPC.

II. ANALYSIS OF ARGUMENTS FOR THE AMENDMENT OF SECTION 50

A. Consistency

One of the primary arguments advanced in support of the new s 50 test is that it is consistent with the overall tenor of other provisions of Part IV of the Act. The Attorney-General in the Explanatory Memorandum to the Bill to introduce the 1992 amendments said:

> As the *Trade Practices Act* is about competition, a test which concentrates on competition and whether there is a lessening of that competition is more consistent with the policy underlying the legislation.[21]

This argument is cited repeatedly in support of the change. For example, in the Senate debates on the proposed amendments, Senator Spindler said:

> The philosophy underlying Part IV of the *Trade Practices Act* 1974 is the protection and enhancement of competition ... the existence of s 50, which specifies the dominance test in the area of merger regulation, is difficult to reconcile with the essential thrust of the Act...[22]

Statements to the same effect can be found in the second reading speech on the Bill delivered by the then Attorney-General, Michael Duffy.[23]

Professor Allan Fels, the current chairman of the TPC, has also supported this argument. Commenting at the time when the dominance test prevailed, Professor Fels said:

> There is an inconsistency between the merger provisions and the remainder of the Act. The Commission is puzzled as to why Government, having accepted the principle that any anti-competitive behaviour that substantially lessens competition should be prohibited unless authorised by the Act has not carried over this principle into the field of merger policy. It would seem to the Commission in principle that any merger which substantially lessens competition should also be prohibited unless authorised. [24]

Is the argument that the new competition test is more in line with the philosophy of the Act as a whole well founded? Two comments can be made.

The consistency argument assumes that the previous market dominance test focussed on "changes to the structure of the market that would be affected by the acquisition",[25] and not on competition per se.

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21 *Explanatory Memorandum*, Trade Practices Legislation Amendment Bill 1992 at [11]. Also note that the stated objectives of the Act are to prevent anti-competitive conduct, thereby encouraging competition and efficiency in business and resulting in a greater choice for consumers in price, quality and service and to safeguard the position of consumers in their dealing with producers and sellers. See Draft Merger Guidelines (1992).

22 Australia, Senate 1992, Debates, Weekly Hansard 55, p 1981.

23 Australia, House of Representative 1992, Debates, Weekly Hansard 15, p 2405.

24 A Fels, "The Future of Competition Policy", presented at the National Press Club, 10 October 1991; A Fels, "The Future of Competition and Prices Policy", presented at Monash University Law School Foundation, 7 May 1992.

25 *Explanatory Memorandum*, Trade Practices Legislation Amendment Bill 1992 at [11].

Whilst the dominance test does not directly deal with competition, it is overly simplistic to say that the test focuses exclusively on market structure. Implied in the structural approach of the dominance test is a focus on competition in the marketplace. Indeed, the Explanatory Memorandum to the Bill to introduce the 1992 amendments acknowledges that the dominance test "also takes some account of the likely effect on the competitive process of such an acquisition".[26] In addition, both the 1986 Merger Guidelines and the case law on the dominance test illustrate the extent to which competition is embedded in the notion of dominance.

For example, in post-1977 merger cases, there are statements to the effect that market dominance is measured in terms of "market power".[27] Market power in turn was defined in terms of competition - "a firm possesses market power when it can behave persistently in a manner different from the behaviour that a competitive market would enforce on a firm facing otherwise similar cost and demand conditions".[28] The question as to whether a firm had attained a position of dominance in the market by virtue of a merger was answered with reference to how the firm would behave if the market was "competitive". Implicit in this reasoning is the idea that, by definition, dominance reduces competition.

Similarly, in *TPC v Australian Meat Holdings Pty Ltd*,[29] Wilcox J described dominance in the following way:

> ...dominance, unlike control is not primarily concerned with the formal relationship between entities but rather with their conduct towards each other within a particular market environment. If the size and strength of a particular entity is such that, in practice, other entities are unable or unwilling actively to compete with it in a particular market, that entity is dominant in that market.[30]

Again, dominance is being defined in terms of the effect that a particular merger would have on competition in the marketplace.

The analysis of dominance by examining limits on conduct was further developed by Australian courts with reference to overseas decisions. For example, in *TPC v Ansett Transport Industries (Operations) Pty Ltd*,[31] much reliance was placed on the reasoning of the European Court of Justice in *United Brands Co v Commission of European Communities*[32] ("the *United Brands* case"). In that case, dominance was explained as "a position of economic strength enjoyed by an undertaking which enables it to prevent effective competition being maintained on the relevant market...".[33]

Further, in *TPC v Ansett Transport Industries (Operations) Pty Ltd*,[34] Northrop J listed factors relevant to the assessment of whether a firm is in a

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26 *Ibid*.

27 *Trade Practices Commission v Arnott's Ltd* (1990) 12 ATPR ¶41-061.

28 *Queensland Wire Industries Pty Ltd v BHP* (1989) 167 CLR 177 at 200.

29 (1988) 83 ALR 299.

30 *Ibid* at 337.

31 Note 11 *supra*.

32 [1978] 1 CMLR 429.

33 *Ibid* at 486; note 13 *supra*, p 105.

34 Note 11 supra at 325.

dominant position in the marketplace. These included market share and market concentration, capacity to determine prices, barriers to entry, product differentiation in the relevant industry, and the character of corporate relationships. To varying extents these considerations of dominance mirror the relevant factors for determining competition in s 50(3). Thus, as Heydon[35] points out, "while 'domination' is conceptually distinct from a substantial lessening of competition, Justice Northrop's analysis has continuing relevance".

The consistency argument does not assist in a debate on whether it is appropriate to have a conduct-based merger test rather than a test that concentrates on market structure. Is the regulation of mergers by reference to possible conduct to be preferred to regulating structures which give rise to anti-competitive conduct? And from a policy point of view, what are the adverse consequences of pursuing the same objective by these alternative paths?

Sections 45, 47 and 49 of the Act contain tests based upon substantial lessening of competition. Those sections deal with agreements affecting competition, exclusive dealing and price discrimination respectively. Each relates to some mode of behaviour or conduct. In each case it is possible to consider whether that conduct is compatible with competitive behaviour and competition in the market place; the conduct has a direct effect on competition and it is manifestly sensible to ask whether the conduct in question lessens competition.

The mere act of merging, however, is never in itself anti-competitive. In fact, the threat of takeover is recognised as an essential dynamic characteristic of markets, acting as a break to a trend for reducing consumer welfare in concentrated markets. It is the conduct that flows from the merger that might be anti-competitive. All one can say is that a particular merger may give rise to anti-competitive behaviour. Unlike ss 45, 47 and 49, the merger provisions prohibit an act which only has an indirect effect on competition. Hence, the Merger Guidelines, if the safe harbour of low concentration is not available, focus on postulated dynamic factors.

One cannot measure the degree of competition in a market simply by counting the number of firms operating in that market. Undoubtedly there are markets in which just two firms operate that are more competitive than markets with 20 or more firms. The degree of competition depends on a wide range of factors. It is impossible to say that, in a market with three competitors, a merger of two of those firms will, by definition, lead to a substantial lessening of competition. It is not impossible that such a merger could in fact increase competitive behaviour. It is much more difficult to tell whether a particular merger will substantially lessen competition than it is to consider the direct effect on competition of behaviour such as exclusive dealing. In the latter case one looks at conduct which has occurred and in the former one is forced to surmise about future conduct.

In general, the task of anticipating competitive behaviour following a merger is extraordinarily difficult. On the other hand, if a merger gives rise to a dominant

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35 JD Heydon, *Trade Practices Law*, Vol 2, Law Book Co (1989) at [9.410].

firm, then competition is almost certainly going to suffer. And while determining whether a firm will become dominant is not a simple process, it can be done with a greater degree of certainty that making judgments on the future dynamics of markets to determine whether a merger would substantially lessen competition.

In the absence of a merger giving rise to dominance, the task of gauging competitive effect loses some of its analytical objectivity and the process of the analysis to be undertaken includes the subjective evaluation of many factors affecting future conduct. This suggests, in the absence of any weighing process, an ability ultimately of the courts to shape Australia's economic landscape.

One matter which was given strong weight by the Cooney Committee can be used to demonstrate much of the analysis set out above. The Committee pointed to the apparent recent spate of mergers which were thought to have passed the dominance test but which, in the opinion of some, ought to have been prevented. The supposed anti-competitive consequences of the following mergers were discussed: Coles/Myer, News Ltd/Herald and Weekly Times, Ansett/East-West, ICI/Berger-British Paints and Tubemakers/McPhersons. In relation to each of these mergers, the TPC indicated in its submission to the Cooney Committee that it was unable to attack the mergers under a dominance test but would have been able to do so using a substantially lessening competition test.

A number of points can be made in reply. First, the new test does not readily provide an ex-ante test for permitting or refusing a possible merger. It is all very well to consider a merger with the benefit of hindsight and point out that the merger substantially lessened competition. It does not follow, however, that at the time of the merger the application of a substantially lessening competition test would have successfully prevented the merger. If, as suggested above, the anti-competitive consequences of a merger are difficult to predict, so long as the onus of proof in s 50 rests with the TPC, it is conceivable that the TPC would have been unable to act effectively even with the supposed advantage of a substantial lessening of competition test. Secondly, there is still continuing debate as to whether the mergers in question did in fact cause a reduction in competition. If we cannot ascertain the competitive consequences some time after a merger, what chance do we have of doing so at the time of the proposed or actual merger? Finally, as will be expanded upon later, it is unlikely that in the real world of determining, before the event, whether a particular course of conduct will infringe the merger provisions, that the debate between structure and conduct will take on much relevance. Because of the amount of guess work inherent in determining whether a proposed acquisition would or would be likely to lead to a substantial lessening of competition, practitioners will be forced to look at those factors which are known. In most cases the starting point and, in the absence of strong countervailing factors, such as freedom of entry or market dynamics, the primary determinant will be the level of market concentration. This is an analysis of market structure.

B. Certainty

The fear that a change in merger tests will introduce an unacceptable degree of uncertainty and the appeal to judicial and legislative certainty are cited against changing the merger test. The dominance test had been in operation in Australia since 1977. A body of case law, judicial precedent and, most importantly, business practice, had developed around the dominance test. As Professor Pengilley argues in his criticism of the Cooney Committee's recommendations, "the law may take a decade in which to develop into some semblance of normality".[36]

However, if the criteria used to assess a substantial lessening of competition are similar to those used to assess the dominance test, the change in analysis may not be as pronounced as first appears.

Secondly, there is a significant body of case law on the interpretation of "substantial lessening of competition". Many foreign jurisdictions, such as the United States, Canada, and Japan, have merger tests that focus on the level of competition in a market place. Over time, Australian courts have been more willing to look to these jurisdictions when considering trade practices law.[37]

There are also Australian precedents available from 1974-77, when the substantial lessening of competition test was operative. Indeed, Professor Fels suggests that with the reintroduction of the competition test we are in a unique position to benefit from hindsight:

> In those early years of the *Trade Practices Act* when policy makers were on a learning curve the test may have held up some mergers which would otherwise have occurred but 17 years later with far more experience these difficulties are not likely to reoccur.[38]

Sections 45, 47 and 49 of the Act rely on a substantial lessening of competition test. Judicial pronouncements on these sections, though not authoritative, will certainly prove to be persuasive guides in the interpretation of s 50.

C. International Aspects

Economic matters are today of a more international than national character. Firms involved in mergers are often global corporations, and the impact of the merger is felt not only within the Australian marketplace. The suggestion is made that Australian merger control regulations should roughly conform to their international counterparts to create a form of global benchmarking of Australian regulation. The United States has regulated mergers by reference to whether the merger may substantially lessen competition or tend to create a monopoly. It is therefore useful to pause, before examining the new statutory guidelines that must be examined in a merger, and look briefly at the manner in which mergers are regulated in other jurisdictions.

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36 W Pengilley, "Merger Policy - Why Did the Cooney Committee Answer the Trade Practices Commission's Prayers?" (1992) 22 *Western Australian Law Review* 300 at 312.

37 For example, the use of the *United Brands* case, note 32 *supra* by Northrop J in the *Ansett Transport Industries* case, note 11 *supra*.

38 A Fels (1991), note 24 *supra*.

(i) United States

The primary merger control provision in the United States is found in § 7 of the *Clayton Act* which relevantly provides:

> That no person engaged in commerce or in any activity affecting commerce shall acquire, directly or indirectly, the whole or any part of the stock or other share capital...of another person engaged also in commerce or in any activity affecting commerce, where in any line of commerce in any section of the country, the effect of such acquisition may be substantially to lessen competition, or to tend to create a monopoly.

The *Sherman Act* (§ 1 and § 2 being the anti-restraint and anti-monopoly provisions respectively) has also been used to control mergers, but the 1980 amendments to § 7 of the *Clayton Act* to cover "persons" rather than "corporations" and those "engaged in commerce or in any activity affecting commerce" has meant that the *Sherman Act* is now largely superfluous in US merger litigation.[39]

American antitrust law relating to mergers is highly sohisticated in both its legal and economic analysis. The underlying issue in American merger analysis is whether the merger will permit the exercise (or increased exercise) of market power.[40]

The 1992 United States Merger Guidelines[41] state that for a seller, market power "is the ability profitability to maintain prices above competitive levels for a significant period of time". Market power for a seller or a group of sellers (monopsonists) is the ability "to depress the price paid to a product to a level that is below the competitive price and thereby depress output".[42] The focus upon the existence or non-existence of market power means that the American approach to merger analysis is closer to the now discarded dominance test under the *Trade Practices Act*, notwithstanding that the overall injunction contained in § 7 of the *Clayton Act* focuses upon mergers which substantially lessen competition, in line with the amended s 50 of the *Trade Practices Act*.

Although the question of the exercise or non-exercise of market power is a behavioural one, the primary analytical tool adopted by American courts and regulators focuses upon market concentration, a fundamentally structural issue. Professor Areeda and Professor Hovenkamp explain the link between market structure and the anti-competitive behavioural effects of a merger:

> A horizontal merger eliminates competition between the merging parties and increases market concentration...elevated concentration threatens competition in

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39 See also *Federal Trade Commission Act* §5.

40 1992 Merger Guidelines, s 0.1; J Whalley "Merger Analysis in the '90s: The Guidelines and Beyond - A Former Enforcer's Perspective" (1992) *Antitrust Law Journal* 171.

41 The 1992 United States Merger Guidelines, jointly issued by the Department of Trade and the Federal Trade Commission (the "1992 Merger Guidelines") deal with horizontal mergers only, although certain principles emerging from the 1992 Merger Guidelines will be applied to vertical and conglomerate mergers which are still dealt with under the 1984 Guidelines. For a summary of the principles related to vertical and conglomerate mergers, see PE Areeda and H Hovenkamp, *Antitrust Law* (Supp, 1993) chs 10-11.

42 1992 Merger Guidelines, s 0.1.

> two ways: the post-merger firm might itself so dominate the market as to control price - as where a merger unites all or most of the firms in the market. Today such monopoly-creating mergers are quite rare. The usual merger simply reduces the number of significant firms in the market and thereby helps then co-ordinate their prices, either expressly or tacitly, at supra-competitive levels.[43]

(ii) European Community

Until recently, the basic European Community merger control regulations were provided for in European Economic Community Treaty Articles 85 and 86. Article 85 prohibits agreements between companies if the effect of the agreement would be to prevent, restrict or distort competition within the EC Common Market. Article 86 prohibits the abuse of a dominant market position. However, as of 21 September 1990, regulation 4069/89 of the European Council has operated. This regulation has radically overhauled EC merger regulation. It focuses entirely on market concentrations, and provides that any market concentration that "strengthens a dominant position as a result of which effective competition would be significantly impeded" is incompatible with the goals of the common market.

(iii) Other Jurisdictions

Briefly, in other jurisdictions, the German test for the prohibition of anti-competitive mergers is based on market domination;[44] the United Kingdom has an interesting "public interest" criteria for merger controls;[45] the French antitrust laws prohibit mergers which are likely to inhibit competition;[46] and finally both Japanese law[47] and Canadian law[48] adopt tests very similar to the current Australian test, with a focus on whether the merger is likely to substantially lessen competition in the market.

(iv) Conclusion

On balance, then, it would seem that the majority of major Western economies outside the EC rely on a competition test. In this light, the change to s 50 brings Australia more in line with the general tenor of antitrust law in the United States, Canada and France. However, the Australian and European Community tests are potentially at odds, given the European Community's relatively new swing towards a dominance test. This is a matter that may become increasingly significant as Australia's economy becomes more open.

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43 PE Areeda and H Hovenkamp, note 41 *supra*, p 934.

44 *German Act Against Restraints of Competition* (*Gesetz Gegen Wettbewerbschrankungen*), s 24(1).

45 *Fair Trading Act* 1973, s 84(1).

46 Act No 77-806 of July 19, 1977.

47 *Japanese Anti Monopoly Act*, s 10.

48 *Canadian Competition Act*, s 92.

D. Economics

Those arguing both for and against the recent amendments often seek justification for their arguments in economics. The Cooney Committee, in recommending the change to the substantial lessening of competition test, appears to have been guided by empirical evidence (albeit scant) as to the very limited productive efficiencies achieved by mergers and that such efficiencies have not improved Australia's international competitiveness.[49] One of the primary reasons for the 1977 amendments to s 50 of the Act was the potential for an improvement in the international competitiveness of Australian industry with the introduction of a market dominance test. It was argued that in order to obtain the economies of scale necessary to compete internationally, it is necessary to have large firms and it is inevitable that, in a relatively small country, this will mean high domestic industry concentration.

Much reliance was placed by the Cooney Committee on the work of American economist Professor Porter, which was used to advance the position that "the dominance test has weakened Australian industry's capacity to compete internationally by reducing the need for it to compete domestically...".[50] Professor Porter reached his conclusions after studying a number of countries, including some small countries. Unfortunately, Australia was not one of those countries.

The main thrust of Professor Porter's theory is as follows:

> Few roles of government are more important to the upgrading of an economy than ensuring vigorous domestic rivalry...creating a dominant domestic competitor rarely results in international competitive advantage. Firms that do not have to compete at home rarely succeed abroad... The national champion theory, or the idea that domestic firms will be more efficient if they merge into one or two more large national competitors, fails the test of logic and history.[51]

On the other hand, several noted lawyers, economists and academics made submissions to the Cooney Committee that the dominance test was stated far more sensibly from an economic perspective.[52] In a similar vein, Professor Pengilley has stated that "there is little doubt that a lower test will mean fewer Australian companies will achieve economies of scale which, to date, have been regarded as an important factor in competing in the world market".[53]

In the Review of Research Studies submitted to the Cooney Committee by the TPC, it was suggested that the findings of recent research studies on the effects of mergers had tended to be somewhat negative.

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49 R Steinwall, "Recent Amendments to the Trade Practices Act" (1993) 30 *Law Society Journal* 62 at 63.

50 H Jordan, "Mergers, Monopolies and Acquisitions: Adequacy of Existing Legislative Controls" (1992) 20 *Australian Business Law Review* 270 at 272; see also A Fels (1991), note 24 *supra* at 6. See also Cooney Committee Report at [3.25].

51 ME Porter, *The Competitive Advantage of Nations*, Macmillan (1990).

52 *Ibid*. See Cooney Committee Report at [3.25] and [3.40] for a list of those who made submissions to this effect.

53 W Pengilley, note 36 *supra* at 320-1.

The Cooney Committee itself, however, concluded that "the economic evidence that mergers actually yield productive efficiencies remains equivocal."[54]

It is instructive that the Commonwealth Treasury, Australia's primary source of economic and policy advice, did not adopt the economic reasoning of Professor Porter. In fact, the submissions made by the Treasury, the Confederation of Australian Industry and the Business Council of Australia to the Cooney Committee all warned that conditions peculiar to Australia meant that Professor Porter's theory could not be automatically applied to this country.

E. Conclusion

Undeniably, the reintroduction of a competition test in preference to a dominance test in s 50 of the Act will have significant repercussions for the development of Australian industry. The change represents a conscious decision by the legislature to lower the threshold of the test in the operation of s 50. But will the change be as far reaching or fundamental as some commentators would suggest? Under the new competition test, established market dominance criteria will be relevant considerations in assessing whether there is a reduction in competition. From an analytical viewpoint, the two tests are not as different as they may first appear. This no doubt may give legal practitioners and the courts some comfort, notwithstanding that the degree of uncertainty that may be introduced from a practical sense will be significant. The lowering of the threshold, when coupled with significantly increased monetary penalties means that it is significantly more difficult for firms to proceed on best available advice if there is any degree of uncertainty. Such uncertainty could be exploited by competitors or competing bidders. Moreover, faced with increasing standards of care and a more litigious society, directors will seek levels of comfort from advisers which will not be readily available. Thus, one would predict increased approaches for authorisation or informal authorisation from the TPC.

III. PRACTICAL CONSIDERATIONS

One of the major changes effected by the 1992 amendments was the introduction of a list of factors to be considered when assessing whether a proposed acquisition infringes the competition test.[55] It would seem that the legislature has introduced

54 Cooney Committee Report at [3.25].

55 Section 50(3) of the Act provides:

Without limiting the matters which may be taken into account for the purposes of subsections (1) and (2) in determining whether the acquisitions would have the effect, or be likely to have the effect, of substantially lessening competition in a market, the following must be taken into account:

(a) the actual and potential level of import competition in the market;

(b) the height of barriers to entry to the market;

(c) the level of concentration in the market;

(d) the degree of countervailing power in the market;

these factors in an attempt to negate the elements of uncertainty that will result from the jettisoning of over a decade of definitive case law on the application of the dominance test.[56]

Prior to commenting on the factors listed in s 50(3), I deal with two difficulties that may result from the application of s 50(3).[57] First, what does the word "must" imply? Secondly, how is the assessment process to take place?

A. What Does the Word "Must" Imply?

Regard to the listed matters is phrased as an imperative; according to s 50(3), the factors listed "must be taken into account". What does this mean? These factors are all very detailed and complex, and each involve careful and considered study. As one of the authors of the *Australian Trade Practices Reporter* has suggested, given the use of the imperative, "the Federal Court will be likely to require an applicant to adduce evidence as to each of the nine factors in any case in which relief is sought under s 50".[58] The converse should also generally be true - if an applicant challenging a TPC ruling against a proposed acquisition adduces evidence as to the listed merger factors, the TPC will have to be able to show that it considered each of these factors.[59] Practically, however, it would be difficult for the TPC to consider these items for each and every merger. Indeed, the TPC has made it plain, as is evidenced in the Draft Merger Guidelines (which are dealt with in more detail below), that it will not explicitly consider every factor in all but the most exceptional cases.[60]

In discussing how the criteria of s 50(3) are to be considered, the TPC states in the Draft Merger Guidelines at [3.34] that "the Commission has had regard to these statutory criteria in drafting these guidelines". The Guidelines continue, "the way in which the Commission incorporates these factors in its evaluation process is

(e) the likelihood that the acquisition would result in the acquirer being able to significantly and sustainably increase prices or profit margins;

(f) the extent to which substitutes are available in the market or are likely to be available in the market;

(g) the dynamic characteristics of the market, including growth, innovation and product differentiation;

(h) the likelihood that the acquisition would result in the removal from the market of a vigorous and effective competitor;

(i) the nature and extent of vertical integration in the market.

See "The Chemical Industry under pressure ..." *The Australian*, 17 March 1994, p 25.

56 See for example the comments of Al Tonking in CCH, *Australian Trade Practices Reporter* at [8-005].

57 See R Baxt, "Restrictive Trade Practices" (1993) 21(1) *Australian Business Law Review* 79.

58 CCH, *Australian Trade Practices Reporter* at [8-142].

59 See ss 5(1)(h), 5(3), 6(1)(h) and 6(3) of the *Administrative Decisions (Judicial Review) Act* 1977 (Cth) ("the *ADJR Act*"); *Australian Broadcasting Tribunal v Bond* (1990) 170 CLR 321; *Minister for Immigration, Local Government and Ethnic Affairs v Pashmforoosh* (1989) 18 ALD 77; *Detsongjarus v Minister for Immigration, Local Government and Ethnic Affairs* (1990) 21 ALD 139; and *FCT v McCabe* (1990) 21 ALD 740.

60 In *Powell v Evreniates* (1989) 87 ACR 117, Hill J stated that there is no obligation under s 13 of the *ADJR Act* for a decision maker to set out in their written reasons all material matters on which a finding was made. An inference will not be drawn that a relevant fact, not set out in the written reasons, was not considered. If, however, no evidence is brought by the decision maker that they did consider that relevant fact, there may be an adverse inference drawn.

designed to minimise the costs of compliance and enforcement". The TPC seems to be suggesting here that it has taken all of the factors listed in s 50(3) into account in designing its merger evaluation process.

From the TPC's point of view, this type of reasoning makes much practical sense. As the Draft Merger Guidelines suggest, "the process is designed to give clear signals to the business community...as to the Commission's likely attitude to potential mergers; and to minimise the costs of compliance, data collection and analysis for both the parties to the merger and the Commission".[61]

No matter how desirable from a policy viewpoint, this approach is inconsistent with s 50(3). Section 50(3) commands the TPC to take the listed criteria into account when determining whether an acquisition would have the effect, or would be likely to have the effect, of lessening competition. This clearly refers to the acquisition referred to in ss 50(1) and s 50(2), namely the particular merger under consideration. Will a court interpret the imperative contained in s 50(3) to mean "must be considered when formulating the assessment process by which a determination as to lessening of competition will be made"?[62]

That is, will our courts adopt the approach the United States Court of Appeals in *United States v Baker Hughes Inc*[63] to rebut a presumption of substantial lessening of competition raised by market statistics. Alternatively, one could suggest that "the Draft Merger Guidelines can be seen more as a statement of the TPC's approach to determining which mergers it will examine for s 50 contravention than as an analysis of the lessening competition test".[64] But for this to be true, when a merger is finally examined by the TPC, the examination process would still have to be completed on at least a checklist of merger factors. In addition, the TPC may in the circumstances of a proposed merger be required to take into account in its consideration of the application of ss 50(1) and 50(2) other matters. Failure to do so may enable an applicant to argue that the TPC had improperly exercised its powers in that regard.[65] On the other hand, if the Draft Merger Guidelines are intended as a guide to the evaluation process, they are inadequate, as they arguably do not comply with the imperative command in s 50.

Whatever the explanation, the inclusion of the word "must" in s 50(3) is, from a practical point of view, an administrative dilemma, which the TPC has indicated in its Draft Merger Guidelines that it will deal with in a very selective manner.[66] When it comes to actually considering the merits of a merger, the use of the word

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61 At [4.20].

62 Cf *In re Findlay* [1984] 3 WLR 1159.

63 908 F 2d 981 (DC Cir 1990).

64 CCH, *Australian Trade Practices Reporter* at [8-410].

65 See s 5(1)(e) of the *ADJR Act*, coupled with s 5(2), and generally *Minister for Immigration and Ethnic Affairs v Peko-Wallsend Ltd* (1985) 162 CLR 24.

66 Note that it is a ground for review under s 5(1)(e), coupled with s 5(2)(f), of the *ADJR Act*, if a discretionary power is exercised in accordance with a rule or policy without regard to the merits of a particular case: see *Green v Daniels* (1977) 51 ALJR 463, where it was held that a government policy, referring unemployment benefits to persons under the age of 16 years who were fresh out of school, was ultra vires the relevant Act as the policy omitted relevant criteria, dictating inadequate consideration of the merits of each individual case.

"must" in s 50 may result in an incredibly laborious examination by the TPC. If the TPC neglects to carry out an examination of all factors, there exists the possibility that a shareholder of a target or person who suffers as a result of a merger which has been allowed (for example, because of the availability of the safe harbour of low concentrate ratios), could challenge the decision in court. Such a person could, with a reasonable chance of success, argue that the decision of the TPC, although based on the guidelines, failed to conform with the requirements of s 50(3), in that the TPC did not individually consider each factor.

Needless to say, as a practical matter, a contested public takeover would have stalled in this process. Thus, the s 50(3) criteria could become an effective defensive weapon in the arsenal of a target.

B. How is the Assessment Process to Take Place?

Assuming that the conclusion reached above is correct - that is, that the TPC should properly consider all criteria listed in s 50(3) - it remains to consider how those criteria are to be weighted.[67] Section 50(3) provides little assistance in this respect. For example, consider a merger that satisfies all factors, except for the fact that there are extremely high barriers to entry (s 50(3)(b)). What would be the effect of this?

One response would be to say that the fact that the TPC is compelled to consider all merger factors in s 50(3) implies that each merger factor is critically important, and that if even one factor cannot be satisfied, the merger should be disallowed. This is clearly not the intention of the legislation.

The more reasonable approach would be that in considering the merger factors of s 50(3) a global approach should be taken. That is, all s 50(3) factors must be considered and the effect of all these factors, together with any other factors which, in the circumstances of the proposed acquisition, are relevant with respect to a lessening of competition should determine whether the merger is permitted.

C. Section 50(3) Factors

Turning now to an examination of the factors to which the legislature has determined regard must be had in assessing whether a merger will have the proscribed effect or likely effect, it is relevant to note at the outset that despite the criticisms of the uncertainty that will be said to result from the adoption of the new test, the s 50(3) factors do not differ greatly from those matters to which the courts have traditionally had regard in assessing whether or not a firm is in a position to dominate a market.[68]

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67 See the observations of Mason J in *Minister for Aboriginal Affairs v Peko-Wallsend Ltd* (1985) 162 CLR 24 at 41 that it is generally for the decision maker and not the court to determine the appropriate weight to be given to the matters which are required to be taken into account in exercising a statutory power.

68 See *TPC v Ansett Industries (Operations) Pty Ltd* (1978) 32 FLR 305 at 325 discussed above. See also the discussion below in relation to the practical operation of the new section.

(i) *Section 50(3)(a) - The Actual and Potential Level of Import Competition in the Market*

This factor has not previously been considered to any extent in the cases, although it is becoming more and more apparent that import competition is an important factor in the Australian context and in an economic environment which has been marked in recent years by substantial reduction in tariff protection.

As Hay and Walker[69] point out, despite Australia's geographic isolation, the economies of scale achieved by overseas firms compared to domestic firms are often such as to provide them with a cost advantage. The Explanatory Memorandum to the *Trade Practice Legislation Amendment Act* 1992 recognises this factor, stating that:

> With increasing internationalisation of the Australian economy, import competition is an increasingly important element in assessing the competitive impact of mergers. Reductions in tariffs and other forms of industry assistance have exposed many sectors of the economy to increasing levels of international competition. Such competition can help maintain competitive markets in Australia, even with a very small number of domestic firms.[70]

In the Draft Merger Guidelines, the TPC states that the underlying rationale in considering import competition is that if such competition is an effective check on the exercise of domestic market power, then it is unlikely that the TPC will intervene in a merger. The current chairman of the TPC, Professor Fels, has been quoted as saying that, as an economist, he takes a broader view of market and that if there is import competition the TPC is unlikely to object to the merger.[71] But contrast this with CSR's defence in its merger proposal in relation to the refined sugar industry.[72] CSR argued that its pricing policy was designed to keep potential imports at bay, however CSR alleges that the resultant low levels of refined sugar imports was then used against the merger proposal. Contrast this with the Court of Appeal's approach in the *Baker Hughes* case. The Court stressed the importance of possible future entry if a merger may lead to supra competitive pricing and took into account entrants from overseas. In the CSR proposal the definition of the market was insufficiently broad to cater for the potential limits of the market at different supply prices.

Some of the factors to which the TPC will have regard in considering the role of imports include whether existing import supply routes could accommodate a significant expansion of supply without the need to invest in sunk costs of distribution, advertising and promotion; whether changes to tariff levels and other forms of protection are likely to occur over the next two to three years; and information that overseas corporations have concrete plans to enter the Australian market.

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69 G Hay and J Walker, "Merger Policy and the TPC's Draft Merger Guidelines" (1993) 1 *Competition and Consumer Law Journal* 33 at 37.

70 *Explanatory Memorandum* at [16].

71 "TPC - Help or Hindrance?" *The Australian*, 17 March 1994, p 25.

72 See discussion below.

(ii) Section 50(3)(b) - The Height of Barriers to Entry to the Market

Barriers to entry have long been recognised as a factor of fundamental importance to an assessment of the existence of market power. The Draft Merger Guidelines state:[73]

> Barriers to entry can be any feature of a market that places an efficient prospective entrant at a significant disadvantage compared with incumbent firms. They may consist of legal or regulatory barriers, access to scarce resources or cost advantages enjoyed by incumbent firms, economies of scale, product differentiation and brand loyalty. In particular, the amount of sunk investment which is required from a new entrant, in...production capacity, accessing shelf space, advertising and promotion costs, will be important deterrents to potential entrants. Also important will be the expected impact of their entry on the market price, which will be affected by the minimum efficient scale at which they can enter, price elasticity of demand and the likely price and output responses of incumbent firms.

The TPC also noted that a concentrated market is often an indication that there are significant barriers to entry, and will look to parties to demonstrate that effective entry is likely to occur despite the high level of concentration in the market.

(iii) Section 50(3)(c) - The Level of Concentration in the Market

This corresponds to the first of Justice Northrop's factors in the *Ansett* case.[74] The more concentrated a market, the greater is the likely anti-competitive effect of a merger.

The Explanatory Memorandum to the 1992 amendment bill states:

> Almost all mergers result in some increased concentration in the hands of a participant in the relevant market, but that in itself is not sufficient to establish substantial lessening of competition. A merger which results in a large increase of concentration in the relevant market may reduce competition in the market by increasing the market power of the merged firm or increasing the scope for tacit collusion or co-ordination among the remaining competitors.[75]

The Explanatory Memorandum does note that it is possible that a merger which increases market concentration may have the effect of enhancing post-merger competition. For example, two merging firms may be better placed to compete effectively with the remaining firms and competition may be heightened in a more concentrated market.[76] As discussed below, the Draft Merger Guidelines reflect the TPC's view that the level of market concentration is a threshold test - if the merged firm will have a market share below certain ratios, then the TPC is unlikely to be concerned about the merger. If oligopolistic structures are added to other features suggesting a market structure not conducive to competition, such as a relatively homogenous product, existence of excess capacity, low profitability and the like, a merger is likely to breach s 50. Of course, it begs the question - what is

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73 At [4.58].

74 Note 11 *supra*; see discussion below in relation to the practical operation of the new test.

75 *Explanatory Memorandum* at [21].

76 *Explanatory Memorandum* at [22].

a structurally competitive market - prima facie one with a large number of firms none of which is dominant.

The rationale behind the pivotal position to be accorded to the issue of market concentration is that "the most useful prediction provided by economic theory is that higher levels of concentration are likely to result in higher prices and losses in allocative efficiency - any merger which increases concentration may reduce competition and raise prices".[77] Thus, it appears that the shift to a competition test requires as the first step an examination market structure, because market structure is determinant of economic behaviour.

Many examples abound of clearance and authorisation decisions under the 1974 Act, but prior to the 1977 amendments that examined the structural characteristics of markets which would result, post-merger, in a substantially less competitive markets.[78]

(iv) Section 50(3)(d) - The Degree of Countervailing Power in the Market

This factor was described in the Explanatory Memorandum in the following terms:

> The notion of countervailing power refers to the extent to which market power held by the merged firm could be offset by market power held by customers or suppliers. The degree of countervailing power held by buyers or suppliers may have an impact on the level of competition in the market, insofar as this may limit the capacity of the acquirer to take advantage of any increase in market power following the merger.[79]

The TPC has indicated that the degree to which a merged firm will face any countervailing power is likely to be particularly significant when the firm is dependent upon a small number of buyers who are subject to competitive restraints in their own output market.[80]

(v) Section 50(3)(e) - The Likelihood that the Acquisition Would Result in the Acquirer Being Able to Significantly and Sustainably Increase Prices or Profit Margins

This factor corresponds to the second factor listed by Northrop J in the *Ansett* case,[81] namely whether the acquisition creates a firm able to behave independently of others, particularly in determining prices without being consistently inhibited in its determination by other firms.

Tonking[82] notes that this factor lies at the heart of the substantial lessening of competition. The inclusion of this factor recalls the views expressed by Mason CJ

77 G Hay and J Walker, note 69 *supra* at 43.
78 Land Newspaper Ltd acquisition of assets of Country Life: see CCH, *Australian Trade Practices Reporter*, Vol 1, pp 5337-5343.
79 *Explanatory Memorandum* cl 23.
80 Draft Merger Guidelines at [4.62].
81 Note 11 *supra*; see discussion below.
82 CCH, *Australian Trade Practices Reporter* at [8-435].

and Wilson J in *Queensland Wire Industries Pty Ltd v BHP*,[83] namely that market power is the ability of a firm to raise prices above supply cost without rivals taking away customers in due time, supply cost being the minimum cost an efficient firm would incur in producing the product.[84]

It would appear that the major problem with the inclusion of this factor is its practical application. The factor arguably calls for a speculative prediction of future conduct (namely, whether the acquirer will be able to increase prices) which may be influenced by a multitude of factors which are impossible to measure or in most cases infer, except for a case in which the merger eliminates virtually all competition (or at least places the corporation in a dominant position). In such a case the ability to increase prices sustainably may be easier to infer. This is also the case in the United States. In *FTC v Proctor & Gamble*[85] the Court noted that the core question in determining whether a merger may substantially lessen competition requires a prediction of the merger's impact on present and future competition.[86] Tonking[87] makes the point that the limited regard that the courts will have to opinion evidence and survey evidence will make the application of this factor even more difficult.

(vi) Section 50(3)(f) - The Extent to Which Substitutes are Available in the Market or are Likely to be Available in the Market

The reason for the inclusion of s 50(3)(f) as a factor is unclear because the existence of substitutes has to be taken into account in the first instance in determining the definition of "market".[88]

The Explanatory Memorandum states:[89]

> The availability of substitute products in a market where a merger takes place allows consumers to purchase alternative products if the merged firm seeks to raise its price. Similarly the scope for substitution in production may limit the scope for the merged firm to raise prices. For example, in response to any attempt to increase prices, manufacturers of other products which use similar production processes may be able to switch at low cost to producing the merged firm's product. In such circumstances it is less likely that the merger would substantially lessen competition. Similarly, if new substitutes are likely to be available if the merged firm raises its price, the merged firm is likely to be constrained in its behaviour, and competition is less likely to be lessened.

In considering the possibility of cross-elasticity of supply, the TPC has stated that it will need to be convinced that potential sources of supply could and would be likely to rapidly switch their production and distribution facilities to supply a closely substitutable product to the customers of the merged firm, without the need for any significant investment of sunk costs in production, distribution or

83 (1989) 167 CLR 177.
84 *Ibid* at 188.
85 386 US 568 (1967).
86 *Ibid* at 577.
87 Note 82 *supra*.
88 See the definition of "market" in s 4E.
89 At [27].

promotions.[90] By way of example, the TPC has pointed out that although a cannery could physically switch from the production of dog food to the production of canned peaches, the firm would need to make a significant investment in promoting the product for it to gain market acceptance.

(vii) Section 50(3)(g) - The Dynamic Characteristics of the Market, Including Growth, Innovation and Product Differentiation

The relevance of this factor is that in a market that is growing as a result of expanding demand or when new technology is providing new and improved products, the ability to exercise market power may be less than in a mature market where demand and supply are in equilibrium and products remain unchanged. Barriers to entry in a growing market may also be lower and will erode any increase in concentration that might result from a merger. In this way, consideration of the characteristics of the market should, in the author's view, be regarded as an inherent part of most of the other merger factors.

(viii) Section 50(3)(h) - The Likelihood that the Acquisition Would Result in the Removal from the Market of a Vigorous and Effective Competitor

Generally, it is thought that this factor should be the easiest to apply, as it will be clear from the nature of the acquisition whether the acquired shares or assets are those of a competitor and whether the competitor will remain in the market. The TPC's Draft Merger Guidelines indicate that the rationale behind this factor is that the removal of even a small competitor may substantially lessen competition by removing the source of aggressive competition:

> In some markets, the "maverick" behaviour of particular firms serves to undermine attempts to co-ordinate the exercise of market power. These firms tended to lever benefits to consumers beyond their own immediate supply by forcing other market participants to deliver better and cheaper products. The Commission would be particularly concerned if such firms were the target of mergers.[91]

(ix) Section 50(i) - The Nature and Extent of Vertical Integration in the Market

It is said that the significance of increased concentration in the product market may be accentuated if members of the industry are vertically integrated, for this means that the merger will increase the extent to which sources of supply or outlets are foreclosed. The Explanatory Memorandum[92] notes that vertical mergers can lessen competition where, prior to the merger, one of the firms had substantial market power at one level which can be exploited in the relevant upstream or downstream market as a result of the merger, for example, by denying downstream competitors access to essential inputs. The Draft Merger Guidelines state that vertical integration is not a necessary concomitant of a substantial degree of market power and that the TPC recognises that vertical mergers are often undertaken in

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90 Draft Merger Guidelines at [2.17].

91 Draft Merger Guidelines at [4.64].

92 At [31].

order to reduce transaction costs and increase efficiency. In certain circumstances, they may also enhance competition.[93]

(x) Other Factors

The list of factors in s 50(3) is not exhaustive. The Draft Merger Guidelines[94] also refer to the possibility that a merger may create a more vigorous competitor in the marketplace. Issues relating to the post-market conduct of firms are relevant matters to be taken into account, for example, whether the market has been characterised by price fixing, coordinated oligopolistic pricing or vigorous price discounting. Also, there may be room to consider the failing firm argument - that is, that a merger should be allowed if it results in one of the firms being able to continue in business, where, in the absence of a merger, it would close. It appears however that the TPC is more likely to have regard to a failing firm argument via the public benefit issues arising under the authorisation procedure than as part of the other factors to be considered when determining whether a proposed merger or acquisition will result in a substantial lessening of competition.[95]

D. TPC Guidelines

Briefly, the Draft Merger Guidelines state[96] that the TPC will adopt a five stage evaluation process in determining whether, in its view, a particular acquisition will be likely to contravene s 50. The five stages are:

(a) Define the market.

(b) Establish whether the proposed merger fits within certain concentration thresholds designed to filter out mergers which are not likely to result in a substantial lessening of competition. If the proposed merger will result in either of the following concentrations, then the TPC will want to examine the proposed merger further:

  (i) if the merger results in the four largest firms having a market share of 75 per cent or more and the merged firm having a market share over 15 per cent; or

  (ii) if the merger results in the four largest firms having a market share of less than 75 per cent and the merged firm having a market share of 40 per cent or more.

(c) Review import competition.

(d) Examine barriers to entry.

(e) Examine other structural and behavioural market features.

As discussed above, the use of this five stage process by the TPC is arguably not in accordance with the provisions of s 50(3) which require the TPC to take into

93 Draft Merger Guidelines at [4.71].

94 At [4.65]-[4.66].

95 See "Acquisitions and the Failing Company Argument", a joint discussion paper by the Australian Trade Practices Commission and the New Zealand Commerce Commission, October 1993. See also L Pasternak, "Should the normal rules governing mergers apply to failing companies?" (1990) 6 *Company Director* 44.

96 At [2.24].

account each of the matters listed in that subsection, however the process does provide valuable assistance to the business community and the trade practices practitioner determining the TPC's likely attitude to a proposed merger.

E. A Recent Authorisation Application - *CSR, Mackay Sugar, Man Australia*[97]

CSR and Man Australia were producers and competitors in the market for the supply of refined sugar. Mackay Sugar, whilst not a competitor in that market, was in the process of constructing a refinery and, but for the conduct the subject of the authorisation application, would have entered into the refined sugar market.

The proposal for which the applicants sought authorisation involved a joint venture between CSR, Mackay Sugar and Man Australia pursuant to which the applicants would jointly produce and sell refined sugar, both domestically and overseas.

It was conceded by the applicants that the proposed joint venture would result in a reduction in the domestic supply of refined sugar as a part of the agreement was the closure by CSR of its Brisbane refinery.

The applicants argued, however, that any reduction in competition in the domestic market for refined sugar would be offset by an increase in exports that would result from the joint venture. CSR claimed that the joint venture, with the use of the technology brought to the joint venture by the parties, would make exporting refined sugar viable where it had not been in the past.[98] It was claimed that this increase in the export potential for refined sugar would not be at the expense of existing raw sugar export.

Other purported benefits used by the applicants to support their application included:

- industry efficiency - there would be a reduction in the excess capacity that existed in the market; and
- industry rationalisation - it was argued that, absent the joint venture, CSR would be required to keep its inefficient refinery open in order to serve existing markets. The joint venture, it was claimed, would allow for that refinery to be closed leading to a saving of approximately $4 million in fixed costs.

It is important to note that several independent parties provided submissions to the TPC supporting the applications. These included the Queensland Department of Primary Industries and the Commonwealth Department of Industry, Technology and Regional Development. Both government departments relied upon the perceived export enhancement benefits of the proposal to support their views. A

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97 Determination in respect of Application for Authorisation lodged under s 88(9) and s 88(1) of the *Trade Practices Act* by CSR Limited, Mackay Sugar Co-operative Association Limited, ED & F Man Australia Pty Limited, No A30156, A30157.

98 *Ibid* at [6.4].

similar view was also expressed by the Australian Bureau of Agricultural and Resource Economics ("ABARE").[99]

Submissions were also received from parties opposing the application. These were primarily from users, from Australian Refined Sugar (a competitor) and the Prices Surveillance Authority. Each of these parties feared the anti-competitive effects that they asserted would result from the joint venture.

(i) Decision of the TPC

Notwithstanding the independent economic evidence produced in support of the application, the TPC refused to grant an authorisation for the proposed joint venture.

(a) Market Definition

Notwithstanding contentions to the contrary by the applicants, the TPC concluded that the relevant product market was refined sugar. The TPC rejected submissions by the applicants that certain sugar substitutes such as aspartame and artificial sweeteners were substitutable for, and therefore in the same market as, refined sugar. Both sides were in agreement that the relevant geographical markets were, first, the crescent consisting of the eastern and southern States of Australia and, secondly, Western Australia.

(b) Market Structure

If the joint venture were allowed to proceed there would have been only three producers in the market. As it was, there were at the time of the application only three producers in the relevant market. However, absent the proposed joint venture, it was anticipated that Mackay Sugar would enter the market in its own right.

It was argued by the applicants that the low number of market participants was reflective of the high fixed cost and economies of scale that characterised the industry. It was also argued that the ever-present threat of import competition provided an upper limit beyond which prices could not rise. Rejecting this submission, the TPC found that, whilst imports could impose an effective cap beyond which prices would not rise, the cost disadvantages faced by importers (such as freight) meant that imports were ineffective as a competitive restraint.

(c) Relevant Factors

The TPC concluded that the refined sugar market was characterised by significant barriers to entry including high fixed costs and significant economies of scale. The Commission rejected evidence to the effect that because Mackay Sugar was planning to enter into the market and because existing market participants were planning on expansion, that the barriers to entry in the market were low.

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99 ABARE calculated that the joint venture would result in net efficiency gains of at lease $12 million per year and a net increase in export benefits of approximately $30 million.

The applicants contended that buyer concentration in both the industrial and retail markets was high and this provided effective discipline on the prices charged by sugar refiners. The TPC, whilst not disputing the applicants' claim, considered that there was little scope for buyers to exercise downward pressure on domestic prices for refined sugar because of the fact that imports were not a viable threat.

The TPC regarded the level of vertical integration which existed in the market as a relevant factor. It was of the view that this would disadvantage potential market entrants who were not vertically integrated. The TPC was also of the view that because the market was "mature", it was unlikely that there would be sufficient market dynamics to counter the anticompetitive effects of the joint venture.

A further factor, which in the author's view was considered to be the most important by the TPC, was the fact that the joint venture would prevent a further competitor from entering the market. In its determination the TPC said "that the motivation of CSR and Mackay and Man to form the joint venture was not the result of any decision to develop new export markets but rather to avoid the consequences of substantial domestic competition between them."[100]

(d) Public Benefits

The main public benefit advanced by the applicants was the expected export enhancement that would result from the joint venture[101]. Whilst not dismissing that exports would increase were the joint venture allowed to proceed, the TPC was of the view that the export benefits could be achieved without the CSR joint venture.

Other benefits relied upon by the applicants, but which failed to sway the TPC, included the fostering of business efficiency and industry rationalisation.

(e) Summary

In summary, the TPC was of the view that whilst significant export benefits were potentially available in the market, it was not necessary for the joint venture to occur for these benefits to be realised. Accordingly, the TPC was of the view that any potential benefits would not outweigh the likely anti-competitive effects of the proposed joint venture.

(ii) What Conclusions can We Draw from CSR?

The CSR authorisation application is significant in relation to the new competition test in s 50 in two ways.

- First, the approach parties and their advisers are likely to take in circumstances where the impact of a merger may involve some reduction of competition. While the applicants did not admit a substantial reduction in competition (a view not shared by the TPC) they nonetheless sought authorisation. No doubt because of a degree of residual and unacceptable

100 Note 97 *supra* at [9.130].

101 *Ibid* at [6.4].

uncertainty arising from the fact that the joint venture would involve some lessening of competition. The existence of significant new penalties; and

- Secondly, the application showed the TPC's approach to examining factors such as market structure, barriers to entry and import competition (particularly having regard to the necessity to have regard by s 90(9A) to significant export enhancement or import replacement effects flowing from the acquisition).

The application confirms that the TPC will implement its selective approach to the factors set out in s 50(3) and also that the approach of the TPC outlined in its Draft Merger Guidelines will be broadly adopted without the use of a checklist approach.

F. Observations on the Practical Operation of the New Test

(i) Is the Analytical Process Different Under the New Test?

In the view of this author, despite the debate and rhetoric concerning the suggestion that the movement from the dominance test to the substantial lessening of competition test represents a change in focus from analysis of structure to one of conduct, in practice there will be very little difference in the analysis to be undertaken in determining whether s 50 has been breached. Set out as Appendix B is a short summary comparing the 1986 Merger Guidelines with the 1992 version. The view that there is little practical difference between the tests can be illustrated by taking the *Ansett Transport Industries* case[102] and comparing the analysis undertaken by Northrop J with the 1992 Merger Guidelines.

In late 1977, Ansett Transport Industries (Operations) Pty Limited, a wholly owned subsidiary of Ansett Industries, entered into a agreement to acquire all of the issued shares in Avis Rent-a-Car Systems Pty Limited.

Avis was in the business of providing the service of hiring of motor cars, otherwise than under a hire purchase agreement and without the services of a driver. Such car rental businesses were conducted throughout Australia by more than 160 operators. Most of these operators conducted their businesses within limited geographical areas the small number conducting their activities on an Australia wide basis. Avis was the largest operator in Australia.

In the judgement of Northrop J, the element market participants and their market shares were as follows:

Avis	43-46 per cent	Letz	5 per cent
Hertz	17 per cent	Thrifty	1 per cent
Budget	16 per cent	Others	15-18 per cent

The TPC relied on two arguments to support their contention that the acquisition would infringe s 50. The TPC argued, first, that Avis was in a position to dominate the car rental market and that as a result of the acquisition, Ansett would

102 (1978) 32 FLR 305.

be in a position to dominate that market. The TPC's second argument was that even if Avis were not there in a position of market dominance, Ansett would be or be likely to be in such position as a result of the acquisition and of other factors resulting therefrom.

The analysis and reasoning of Northrop J can be summarised as follows.

The first step is to define the market. In this case the relevant product market was the service of providing cars for rental. The geographic market was Australia.

The second step involves an examination of the level of market concentration to determine whether this gives rise to a presumption of market dominance. On the basis of the market shares set out above, Northrop J stated that, in his view, the large market share of Avis created the presumption that market dominance did exist.

Thirdly, examine whether, despite any market concentration levels, there existed strong and effective competition in the market. Justice Northrop concluded that the market was characterised by strong and effective competition between its participants.

The fourth step in Justice Northrop's analysis was to examine the extent of barriers to entry. His Honour concluded that the barriers to entry in the car rental market were low.

The fifth step is to examine the extent of product differentiation. In this regard Northrop J concluded that there was little differentiation in respect of the car rental services provided by the market participants.

Finally, the character of corporate relationships and the extent of corporate integration was examined. Justice Northrop held that the assistance that Ansett would be likely to provide through its airlines operation to Avis car rentals would not be sufficient to place Ansett in a position to dominate the car rental business.

In the result, Northrop J held that Avis (and hence Ansett) would not be in a position to dominate the market. His Honour effectively held that the presumption created by the high market share of Avis was overcome by the other qualitative factors set out above.

The analysis undertaken by Northrop J bears a striking resemblance to the five stage evaluation process set out in the 1992 Draft Merger Guidelines. Perhaps the only significant difference is the prominence that import competition now takes in the evaluation of whether a merger will result in a substantial lessening of competition.

If the five stage evaluation process were applied to the facts of *Ansett Transport Industries*, the analysis would be as follows.

Market definition would probably be the same, that is, the market for car rentals.

On the figures set out above, the four largest firms would have been 81 per cent and 84 per cent of the market and Avis would have between 43 per cent and 46 per cent of the market. This would breach the market concentration thresholds set by the TPC and the TPC would undertake further market investigations before deciding whether or not the merger would be likely to result in a substantial lessening of competition.

The import competition factor would not be relevant in relation to the domestic car rentals market.

In all likelihood, the view of Northrop J that barriers to entry in the relevant mrket were low would be followed.

Other structural and behavioural market features, such as the extent of product differentiation and the extent of vertical integration, would be considered.

It is likely that, even on the analysis of Northrop J, the result in the *Ansett Transport Industries* case would be less clear under a substantial lessening of competition test. The crucial question that would need to be resolved is whether the qualitative factors set out above would be sufficient to outweigh the presumption of a substantial lessening of competition created by the high Avis market share.

The analysis set out above is provided merely to illustrate that the analysis to be undertaken under the substantial lessening of competition test and the dominance test are almost identical and that, in reality, all that the change in the test has achieved is a lowering of the threshold that must be reached for an acquisition to contravene s 50.

(ii) The Role of the Authorisation Procedure

It is, of course, not possible in reviewing the new Merger Guidelines and the amendments to s 50, and in assessing the impact of these changes on merger and takeovers in modern day Australia, to omit making some observations on the authorisation process.

The authorisation procedure contained in the Act permits the TPC to allow mergers that would otherwise contravene s 50 if it can be shown that the merger will result in sufficient public benefits so as to justify the merger being allowed.

At the same time as s 50 was amended, the authorisation provisions in the Act were also amended so as to provide that the TPC, in assessing whether a proposed merger will result in public benefits, must consider the effect of the merger on the level of exports, import substitution and international competitiveness.[103]

Just as the new s 50(3) is silent on the weight to be given to the various factors listed in that section, the authorisation procedure leaves it to the TPC to determine what constitutes a public benefit.[104] Specifically, s 90(9) does not envisage any weighing of resulting benefit to the public against resulting detriment.

Thus, the TPC has refused authorisation in cases where efficiency gains have been of a private nature, that is where benefits enure to shareholders or employment is provided to a relatively small number of persons. In part, this stems from the fact that "public" has been interpreted as meaning anything of value to the community generally[105] and the TPC's view that the goal of the Act is to give greater choice to consumers in price, quality and service.[106]

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103 Section 90(9A).

104 See for example *Re ACI Operation Pty Limited* (1991) ATPR ¶50-108.

105 *Re Queensland Co-operation Milling Association Limited* (1976) 25 FLR 169.

106 *Ibid.*

If it is the case that the primary goal of the Act is consumer choice, it is not always the case that anti-competitive conduct will, of itself, reduce consumer choice. In that sense the Australian government has made a policy value judgment - mergers which substantially lessen competition, irrespective of efficiency effects, are prohibited unless authorised. However (other than the direction in s 90(9A) with respect to export enhancement or import replacement), no such direction is given in the authorisation procedure and the TPC is free to take any economic, social or political consideration into account and is free to weight these considerations as it sees fit.

Business is placed in an invidious position. Firstly, if concentration ratios do not offer a safe harbour, as the CSR-Makay Authorisation process demonstrates, it is extremely difficult to determine *ex ante* whether or not a merger will breach s 50 because the Act gives no weight to the factors to be taken into account. This is where the merger guidelines provide invaluable practical assistance in providing an analytical framework - through the five stage process of weighing the various factors (although this may be wrong at law).

Secondly, the efficacy of seeking an informal ruling is, as was evidenced by the Santos/Sagasco litigation, fraught with risks.[107]

Thirdly, the TPC is unable under the Act to consider public benefits of its own volition; therefore the TPC will probably encourage applications for authorisation, as this will give the TPC a statutory mandate to consider public benefit factors.

It is therefore disappointing that the Government did not take the opportunity to set out clear guidelines on the authorisation process - for example that consistent with s 90(9A) any merger which increases the efficiency of the Australian economy ought to be authorised. This would remove elements of subjectivity and weighting which have in the past led to a great deal of uncertainty and a desire to avoid the formal authorisation route.

In this regard, it should be pointed out that we are still yet to see any draft legislation to implement the compulsory pre-merger notification procedure that was foreshadowed at the time of the amendments to s 50.[108]

IV. CONCLUSION

The reintroduction of the substantial lessening of competition test in Australian merger law has had, and will continue to have, a marked effect on corporate acquisitions in Australia. Just how marked and different an effect it will have remains to be seen.

From the viewpoint of a legal practitioner involved in the mergers field, the new test is in the author's view unlikely to substantially alter the legal analytical process that will be undertaken in determining whether an acquisition will be likely

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107 *TPC v Santos Ltd & Ors* (1992) ATPR ¶41-194, (1992) ATPR ¶41-195, (1993) ATPR ¶41-221, (1993) ATPR ¶41-232, (1993) ATPR ¶41-277.

108 The Draft Merger Guidelines state at [26] that a draft exposure bill was expected in early 1993.

to contravene s 50. Market concentration thresholds will continue to be the primary determinant of whether at first glance there will be likely to be a s 50 problem. It will then be a matter of examining the factors set out in s 50(3) and the TPC Draft Merger Guidelines. The threshold has, however, been lowered. This leaves the adviser and the adviser's client at a difficult cross road - one now fraught with significantly harsher penalties. The adviser and his or her client must decide whether to pursue the views of the TPC via the so-called informal clearance procedures,[109] to apply to the TPC for authorisation[110] or to take its advice and face the possibility of TPC intervention. Even if the TPC issues a no action letter, there is still the risk that the Attorney-General may take independent action to prevent the merger.[111]

109 A danger clearly illustrated by the unsuccessful bid by Santos Ltd for Sagasco. See *ibid.*

110 A process that gains its own inevitable slow momentum, which requires great stamina and resolution to pursue to the ultimate appellate tribunal - often an unrealistic goal where time or costs is important or for most public listed companies (for example, the CSR authorisation).

111 *Attorney General of Commonwealth v Davids Holdings Pty Limited & Anor* (1993) ATPR ¶41-210, (1993) ATPR ¶41-211, (1993) ATPR ¶41-212, (1993) ATPR ¶41-213, (1993) ATPR ¶41-226, (1993) ATPR ¶41-247.

APPENDIX A

Findings and Recommendations of Committees which have reviewed s 50 of the *Trade Practices Act* 1974 (Cth)

(i) Swanson Committee

1. A law on anti-competitive mergers is necessary.
2. Merger law should include acquisition of interests in assets and mergers of companies effected by operation of law.
3. A statutory defence should be provided in the case of a failing target company, defined by reference to the imminent likelihood of it going out of business, and lack of alternative buyers on similar terms.
4. Merger provisions should not apply to small acquisitions (businesses with an average annual turnover for the two previous complete financial years of $3 million).
5. The threshold test should not be applied where the acquiring corporation engages in a pattern of buying small businesses in the same industry.
6. Clearance procedures should be retained for mergers.
7. The power of ministerial intervention in merger matters should be removed.

(ii) Green Paper

1. The appropriate test for mergers should be one based on the likely competitive effect of the merger in the market, rather than solely on market structure.
2. No proposal for the specific grounds for authorisation or specific matters should be taken into account when determining public benefit.
3. Pre-merger clearance procedure proposed.
4. Section 50 should apply to acquisitions by natural persons or bodies corporate other than corporations as defined in the Act.

(iii) Griffiths Committee

Majority

1. Committee not convinced of the need for a scheme of pre-merger notification.
2. Any proposal to return to the pre-1977 test of substantial lessening of competition would, of necessity, need to be linked to the retention of the existing requirement in relation to a substantial market in order to avoid undue interference in merger activity.
3. Not convinced of sufficient justification, at that stage, to recommend the adoption of a substantial lessening of competition test.
4. Recommended that the existing test be retained.

Expressions of concern - Duncan Kerr, MP and Mr Cleeland, MP:
Expression of particular concern as to the retention of dominance test

Dissenting Report by Mr Robert Tickner, MP and Mr Keith Wright, MP

1. Existing dominance test has tendency to allow the abuse of market power and a high degree of concentration to develop in many Australian markets.
1. Mergers should not be allowed if they substantially reduce competition and they should only be authorised if the public benefit of the merger demonstrably outweighs competition considerations.
3. The general thrust of the existing provision lies in favour of promoting economies of scale.
4. A pre-notification system should be introduced.
5. A ministerial discretion to institute a government inquiry should be created, to be used only in exceptional circumstances to ensure that the public interest concerns, including those of workers, consumers, shareholders and government industry policy, are effectively addressed.
6. A general public interest test to be applied by the TPC was not recommend at that stage, but that the position of such a test be kept under constant review.
7. The existing evidence on the economic benefits or costs of takeover is inconclusive.

(iv) Cooney Committee

Majority

1. Found empirical evidence on the effects of mergers is conflicting and not conclusive and that economic evidence that mergers actually result in productive efficiencies remains equivocal.
2. Existence of a dominance test in the area of merger regulation is difficult to reconcile with the essential thrust of the Act which is directed to preventing anticompetitive conduct.
3. Any uncertainty that changes to the test might bring could be reduced significantly by the incorporation into the Act of statutory guidelines, possibly along the lines of the Canadian model, to assist in applying the test.
4. Change needed to s 50 of the of the Act and the benefit to flow from it will clearly outweigh any detriment that may arise.
5. Substantially lessening competition test in line with tests adopted by countries having most in common with Australia.
6. Recommended that it be obligatory for a notice to be given to the TPC where mergers or acquisitions of a substantial nature are proposed. What is a matter of substantial nature should be defined in the Act.

The matters of which notice is to be given should be limited so that undue burden is not cast on those who must comply.

7. Notification proposals should be drawn up by Commonwealth Attorney General's Department and released for public comment.
8. Parties proposing to merge should have the option of either approaching the TPC for authorisation, with a right of appeal to the Trade Practices Tribunal, or of approaching the Tribunal directly.

Dissenting Report by Senator Rod Kemp

1. Economic evidence as to operation of s 50 has proved inconclusive.
2. Insufficient evidence to indicate that any demonstrable harm has resulted from the application of the dominance threshold.
3. Adoption of a new threshold would entail another decade of uncertainty while the ambit of the new threshold is determined by the courts.
4. Recommended that dominance test be retained.

(v) *Hilmer Committee*

1. Merger regulation is an important past of national competition policy.
2. Any more detailed review of the merger provision of the *Trade Practices Act* could best be undertaken with the benefit of more practical experience with the amended provisions.

The Reports

Swanson Committee: TB Swanson, JA Davidson, AM Kerr, AG Hartnell and HS Schreiber: *Report to The Minister for Business and Consumer Affairs*, Trade Practices Act Review Committee, August 1976

Green Paper: G Evans, B Cohen and R Willis: *The Trade Practice Act - Proposals for Change*, February 1984.

Griffiths Committee: AG Griffiths, PM Ruddock, AE Adermann, DE Charles, PR Cleeland, DJ Kerr, PJ McGauran, JC Moore, PK Reith, GGD Scholes, WL Smith, RE Tickner and KW Wright: Report of the House of Representatives Standing Committee on Legal and Constitutional Affairs, *Mergers, Takeovers and Monopolies: Profiting from Competition*, May 1989.

Cooney Committee: B Cooney, A Vanstone, P Giles, R Kemp, W O'Chee, C Schacht, S Spindler & P Walsh, Report of the Senate Standing Committee on Legal and Constitutional Affairs, *Mergers, Monopolies & Acquisition: Adequacy of Existing Legislative Controls*, December 1991.

Hilmer Committee: F G Hilmer, M Rayner & G Taperell, Report by the Independent Committee of Inquiry, *National Competition Policy*, August 1993.

APPENDIX B

1986 GUIDELINES

A. Define the Market

- determine the product market which depends to a large extent on the goods which are substitutable for the goods primarily concerned; and
- determine the geographic market, this will depend upon such matters as the nature of the product and the conditions of supply of the product.

B. Examine Whether the Acquirer will be in a Position to Dominate a Market

This involves an examination of both qualitative and quantitative considerations including the following:[112]

1. *The Degree of Market Concentration* - the TPC states (at page 3 of the 1986 Guidelines) that they would inquire into all mergers where the outcome will be that the acquirer will have a market share of 45 per cent or more and will be the largest competitor in the market, or will have a market share exceeding that of its nearest competitor by 15 per cent or more.
2. *Consistent Inhibition* - the crucial factor here is the extent to which a firm can operate independently.
3. *The Heights of Barriers to Entry* - here the relevant issues are the costs of entry and also whether any new entrant may reasonably be expected to secure a viable market.
4. *Product Differentiation* - the TPC states that if the products in the market are homogenous then market share will be important, however if the market is characterised by product differentiation, competitiveness may still exist with small producers being able to differentiate their products.
5. *Integration* - this is important to the extent that a firm with a higher level of integration will generally have a higher level of market power.

1992 GUIDELINES

A. Define the Market

This is the area of close competition or rivalry among firms[113]. It has both a product and geographic dimension. The product dimension will depend upon the substitutability of other goods which in turn is measured by the cross elasticity of both demand and supply.

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112 The Commission relies upon the factors set out by Northrop J in *Ansett*; see p 9 of the 1986 Guidelines.

113 The TPC relies on the decision of the High Court in *Queensland Wire*.

B. Examine Market Concentration Levels

If the post-merger market shares are in either of the following two categories the TPC will investigate further:

1. four largest firms have more than 75 per cent of the market and the merged firm has at least 15 per cent market shares; or
2. if, in any case, the merged firm has a market share of 40 per cent or more.

C. Examine Import Competition

If import competition is an effective check on the exercise of domestic market power, it is unlikely the TPC will intervene in a merger.

D. Barriers To Entry

Even if the market concentration thresholds are breached, if the market is not subject to significant barriers to new entry, incumbent firms are likely to be constrained by the threat of potential new entrants and as such are more likely to behave in a competitive manner.

E. Other Factors are Examined

- Countervailing market power.
- Chain of substitution with products in other markets.
- The likelihood that the merger will result in the removal of a vigorous and effective competitor.
- Past market conduct of firms.
- Growth prospects of the market.