fair trading coalition

Mr Scott Rogers
Competition and Consumer Policy Division
The Treasury
Langton Crescent
PARKES ACT 2600

By email: scott.rogers@treasury.gov.au

Dear Mr Rogers

Thank you for the opportunity to comment on the discussion paper on creeping acquisitions. The Fair Trading Coalition welcomes the debate on this important issue and acknowledges that the release of this discussion paper is part of an election commitment by the Government to consider the need for legislative reform in the area of creeping acquisitions.

The FTC is an informal coalition of small business organisations committed to reform of the Trade Practices Act. The Members of the Fair Trading Coalition believe that a vibrant small business sector is important if Australia is to sustain a competitive market.

The FTC has always been of the view that the Trade Practices Act should cover the issue of "creeping acquisitions". The FTC has long had real concerns about conduct where larger players in the economy gradually acquire smaller ones and incrementally increase aggregate market share. In fact the FTC raised the issue of the Trade Practices Act and creeping acquisitions in its submission to the Dawson Review of the Trade Practices Act in 2002. At that time, the FTC recommended to the Review that the Trade Practices Act be amended to state that where market concentration had passed a nominated threshold, the ACCC should take into consideration previous mergers and acquisitions by an acquirer and to aggregate the effect of previous mergers and assess the resultant state of competition in any relevant market.

members of the Fair Trading Coalition:

1 Apple & Pear Growers Association of SA Inc
2 Australian Automotive Aftermarket Association
3 Australian Automobile Dealers Association
4 Australian Hotels Association
5 Australian Motor Body Repairers Association
6 Australian Newsagents' Federation
7 Australian Petroleum Agents and Distributors Association
8 Australian Private Hospitals Association
9 Australian Service Station and Convenience Store Association
10 Chamber of Women in Business
11 Civil Contractors Federation
12 Council of Small Business Organisations of Australia
13 Drycleaning Institute of Australia
14 Growcom
15 The Horticulture Council
16 Independent Liquor Group NSW
17 Independent Liquor Stores Association
18 Liquor Stores Association of Victoria
19 Motor Trades Association of Australia
20 The Motor Trades Association of the Australian Capital Territory
21 The Motor Traders' Association of New South Wales
22 The Motor Trades Association of the Northern Territory
23 The Motor Trade Association of South Australia
24 The Motor Trade Association of Western Australia
25 National Institute of Accountants
26 The Pharmacy Guild of Australia
27 Service Station Association Limited
28 Victorian Automobile Chamber of Commerce
29 Western Australian Dental Implant Society AOS (WA) Inc

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As you are aware, mergers and acquisitions are presently addressed in section 50 of the Trade Practices Act. Mergers and acquisitions which result in a substantial lessening of competition are prohibited under the Act; though it is possible to seek Authorisation for such mergers/acquisitions. The 'test' for such an Authorisation being granted is that the public benefit outweighs the public detriment. Under changes introduced to the Trade Practices Act in 2007, applications for Authorisation are heard by the Australian Competition Tribunal.

Small business has for years been voicing concerns about s50 of the Act; particularly in the circumstance where a larger party acquires, over a period of time, a number of businesses, where each transaction does not itself result in a substantial lessening of competition in the market (and so does not 'trigger' section 50 concerns), but where over time the cumulative effect of all of those transactions is a significant increase in market share of the larger party. Concerns have been voiced about creeping acquisitions in a number of markets, including, the retail grocery market, the retail petroleum market, the retail liquor market and taxi credit operators.

The FTC recognises that the issue of creeping acquisitions is a complex one. For many small business owners, their business and the goodwill established in that business is effectively the owner's 'superannuation' and measures which restrict their ability to sell their business will therefore impact on their 'superannuation'. Any 'blanket' restriction on them selling that business is likely to be opposed by small business groups. Yet, the issue of 'creeping acquisitions' and how to address the concerns associated with it, is a policy matter which the FTC believes needs to be resolved.

The discussion paper released by the Government includes only two options for consideration. The 'aggregation model' (Option 1) would involve a corporation being prohibited from making an acquisition if, when combined with acquisitions made by the corporation within a specified period, the acquisition would be likely to substantially lessen competition in a market.

To some extent now, depending on the market circumstances of particular acquisitions, previous acquisitions can be considered in a merger. However previous acquisitions are only likely to be considered where it can be shown that the acquirer has a long term policy to embark on anti-competitive acquisitions. In general, it is thought that most acquisitions are opportunistic, rather than strategic. Unless an anti-competitive strategy can be shown, in the FTC's view it will be difficult to see how being able to aggregate acquisitions will ever determine that a current acquisition is anti-competitive. It is also difficult to see how, in most circumstances, the acquisition of one small retailer will result in a substantial lessening of competition in a market.

The Fair Trading Coalition's preference would be for this Option not to be adopted by the Government. This Option is seen as one of least change and thus unlikely to address concerns about creeping acquisitions.

Under Option 2 a new prohibition would be added to section 50. The new section would state that a corporation would be prohibited from making an acquisition if it already has a substantial

degree of power in a market, and the acquisition would result in any lessening (as opposed to a substantial lessening) of competition in that market.

The substantial market power model would sit alongside the substantial lessening of competition test (SLC) already in section 50. That SLC test has been the basis of Australia's merger laws since 1993.

The FTC believes that adoption of Option 2 could be likely to result in many large players in any sector being very careful with each acquisition. It would also add another dimension to merger law and introduce a 'two-tier' approach in mergers.

Adoption of Option 2 is not though without some inherent problems because, as you will be aware from the lengthy debates on section 46 (misuse of market power), the concept of a substantial degree of market power is a difficult one; albeit that recent amendments to section 46 have sought to clarify the intent of the phrase in the legislation.

Nevertheless, the FTC believes that adoption of Option 2 would result in large companies thinking twice about mergers and if they do seek to acquire another business it is likely they will "need", because of the 'any lessening of competition' test, to have the acquisition reviewed by the Australian Competition Tribunal under the existing Authorisation process.

The FTC believes however that in relation to Option 2, the following matters also need to be considered:

Market power issues

- it is likely that even if the lessening of competition resulting from an acquisition is to be very minor, a merger will be prohibited. (Option 2 would preclude an acquisition where the acquirer has a substantial degree of power in a market and there was any lessening of competition);
- there will be a 'substantial degree of market power' test in section 46 and one also in the proposed new part of section 50 but with a lessening of competition test. (As mentioned above, this proposed new test will 'sit' in section 50 alongside the existing substantial lessening of competition test.) The issue here is, will the 'market power' threshold tests (section 46 and section 50) be the same? Or will the section 50 market power threshold be higher than the section 46 one as the discussion paper appears to imply?
- the discussion paper states that in assessing a substantial degree of market power, the factors listed in section 50(3) (which relate to the level of competition in the market, barriers to entry, availability of substitutes and so on) and the ability to raise prices above competitive levels would be taken into consideration. Again this sends the message that the threshold for substantial degree of market power test in the proposed new section would be very high and thus potentially few corporations will have 'market power' – which does not assist small business in dealing with creeping acquisitions; and
- companies with no market power in the Australian market, such as foreign companies, will have an advantage over domestic companies when making acquisitions but that is inherent in section 50 now.

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Authorisation issues

- it is likely that where an acquisition is objected to under the new test, the parties may seek an Authorisation (under the TPA). However, merger Authorisations are the responsibility of the Australian Competition Tribunal (ACT) and not the ACCC. If Option 2 is to be adopted by the Government it may be necessary to ask it to amend the Trade Practices Act to enable the ACCC to deal with Authorisations under the new section; and
- the possibility of forcing more companies to an Authorisation process will add to compliance costs for many; especially small businesses which are keen to sell. In many cases the lessening of competition will be minor, but the Authorisation process (and through it, ACT hearings) will still need to be addressed by the parties.

Other

- there is likely to be a concern that the threat of the new law will cause a flood of creeping acquisitions. It is suggested that any new law be effective from the date the Government decides on which policy measure to adopt; and
- it is presumed that the divestiture power in section 81 would apply to the amended section 50 (that is where a merger can be shown to have been illegal the Courts could apply a divestiture penalty).

Negatives for small business

- importantly, and probably our greatest concern, is that it needs to be understood that the proposed new test is likely to stop many small business operators being able to sell their asset or they will have to sell at a lower price; because of the inclusion of the 'any lessening of competition' test in the legislation; and
- the adoption of Option 2 (or Option 1 for that matter) will not stop larger parties gaining market share through 'green-field' developments.

Summary

The preference of the Fair Trading Coalition is for the adoption of Option 2 over Option 1. That said however, it must be noted that the FTC does have some concerns about Option 2 and they are as outlined above. The FTC proposes that those matters need to be further and carefully considered before the Government makes a final decision about the form of any legislation to be introduction to deal with creeping acquisitions.

The FTC strongly recommends that the Government consider an alternative option which is that where concentration in a market in Australia has passed the CR4[1] test, (or, in the alternative, an HHI[2] index level of over 2000) any corporation falling within that threshold must notify any further acquisitions in that market and any other market to the Commission. The Commission must review each such notification on the basis of whether or not the acquisition will or is likely to

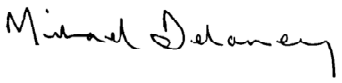
[1] CR4 is defined as the sum of the market shares of the four largest firms in the market being greater than 75 per cent. MTAA and the FTC have previously (for example to the 2002 Dawson Review of the Trade Practices Act) suggested that a CR4 test be adopted as a threshold in addressing concerns about creeping acquisitions.

[2] HHI is the Herfindahl-Hirshman Index which equals the sum of the squares of the market share for each firm in the market

result in an overall public detriment. If the Commission decides that there is an overall public detriment then the acquisition will not be allowed to proceed. In this model the threshold is somewhat more certain than in Option 2 and the Authorisation issues are factored into the ACCC process.

If you have any questions about the issues I have raised, please do not hesitate to contact me.

Yours sincerely



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10 October 2008