Government consultation on merger reform

Submission by

Professor Yane Svetiev (University of Sydney Law School, Chair in Market Regulation and Private Law) and

Joshua Sinn (University of Sydney Law School)

1. The consultation paper highlights concerns about the adequacy of Australia's mechanisms for controlling merger activity in protecting and promoting market competition.

The consultation paper notes that an ideal merger law should allow those mergers to proceed that enhance competition, while amending or preventing mergers that are harmful to the competitive process. Further, the paper points out that current merger settings may not be effective in achieving this objective, highlighting growing evidence of deteriorating competition across many sectors in the economy, based on measures of concentration and mark-ups. For example, ten of the 20 largest industry classes in Australia had a four-firm industry concentration ratio (CR4) of above one-third in 2023,[1] with the average CR4 increasing by over 2 percentage points between 2001-2 to 2018-9.[2] Average firm mark-ups have increased from close to 0% in the early 1990s to over 50% for most of the 2010s.[3]

The paper canvasses several shortcomings of the current merger control regime, which we group into two categories:

(i) In the application of the 'forward looking test', there is uncertainty as to how some markets (in particular, dynamic, as opposed to stable, markets) would evolve in the hypothetical futures with and without the merger.[4] As a corollary, there is uncertainty as to the most appropriate remedy that should be implemented to protect and promote competition. The ACCC

[1] Authors' analysis of industry reports from IbisWorld.
[2] Andrew Leigh, 'A More Dynamic Economy' (Speech, FH Gruen Lecture, Australian National University, 25 August 2022).
[3] Jan de Loeker and Jan Eeckhout, 'Global Market Power' (Working Paper No 24768, National Bureau of Economic Research, June 2018).
[4] The courts recognise these difficulties, but remain cautious in making conjectures about the future evolution of the market. As the Court noted in *ACCC v Pacific International Pty Ltd* [2020] FCAFC 77 at [218], 'In the usual case, prediction about the nature and extent of competition in the future with and without the acquisition will be rooted firmly in past and present market conditions, which are susceptible of proof in the ordinary way. Most markets have a history from which an assessment … can be undertaken and reliable predictions about the future can be made.' In nascent and/or highly dynamic markets, there may be no past or present market conditions, or these conditions may not form a sound basis upon which predictions about the future can be made.

and courts face challenges in designing and effectively implementing solutions that are not only appropriate ex-ante, based on present information about market dynamics, but also future-proof, in the sense of being appropriate in the face of ex-ante unpredictable market dynamics.[5]

(ii) There are administrative challenges that may hamper the ACCC's merger investigation process, further preventing the Commission from implementing a preferred remedy. This includes the failure of firms to notify the ACCC of their intention to merge and the consummation of a merger before the completion of the ACCC's investigations. Again these problems are particularly acute in markets which tend to evolve rapidly because of dynamic technological change, as opposed to more stable commodity markets.

2. The consultation paper canvases options for changing the merger control process that may address some of the administrative challenges identified, but would not address the more fundamental challenges of regulatory and remedial uncertainty.

The consultation paper outlines various options for changes to the merger control process. They include a change from voluntary to mandatory notification and mandatory suspension of mergers that are being reviewed. These proposed changes may go some of the way to countering shortcoming (ii) by addressing the concern that the ACCC does not have sufficient opportunity to review relevant mergers. However, we consider that this concern is less pressing – even if the ACCC has the opportunity (and the resources) to review all relevant mergers, such changes would increase workload but without providing a coherent assessment and remedial framework for mergers, which may also be accepted by the courts.

Our key submission is that the reform options presented in the consultation paper do not provide a coherent assessment and remedial framework that would adequately address shortcoming (i) above. The consultation paper perhaps unhelpfully frames this challenge around the question of whether Australia's merger regime is 'skewed towards clearance' and whether it would be 'more appropriate for the framework to skew towards blocking mergers where there is sufficient uncertainty about competition impacts'.[6] Adopting this framing, the consultation then presents options to address this perceived skew, such as the adoption of a 'satisfaction test' under a clearance model. These solutions are effectively outcome-

[5] The limits of hierarchical regulatory enforcement have been recognised in the literature. See generally, John Braithwaite, 'The Regulatory State?' in Sarah A. Binder, R.A.W. Rhodes and Bert A. Rockman (eds), *the Oxford Handbook of Political Institutions* (Oxford University Press, 2008), 231.
[6] See Question 6 of Australian Treasury, *Merger Reform* (Consultation Paper, November 2023).

determinative, leading to mergers being more likely to be blocked rather than cleared under conditions of uncertainty. Such proposals are often justified through the argument that the error of clearing an anti-competitive merger is less 'costly' than the error of blocking a pro-competitive or benign merger.[7]

We do not consider that this coherently responds to the problem of uncertainty. There is no ex-ante "correct" answer in cases involving uncertainty, only procedures for discovering an answer over time. As such, the error-cost framework does not provide much insight when applied to the kinds of mergers with which the consultation paper has the strongest concerns.

3. Experimentalist competition law provides an alternative enforcement template that coherently addresses regulatory and remedial uncertainty, and is already implemented in a partial form.

As discussed above, an effective framework for merger control should provide a coherent response to uncertainty about the effects of an impugned transaction on evolving market competition, as well as the challenges in designing and implementing effective and timely remedial solutions that do not become 'outdated' as market conditions evolve.[8]

An experimentalist architecture for competition law offers one dynamic regulatory response to these conditions. This model of competition enforcement adopts participative problem-solving and recursive remedial adaptation, as opposed to one-shot determinations as to whether a merger should be blocked or not, or subject to remedies that are defined based only on the information available to the authority and the parties ex-ante at the time of decision.

Experimentalist competition law enforcement is appealing because:

(i) It has been used effectively overseas (particularly in the European Union).[9]
(ii) Certain CCA instruments (in particular s 87B enforceable undertakings and authorisations subject to negotiated conditions) and the ACCC's informal merger review process reflect, a least in part, an experimentalist approach to merger control.[10]

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[7] See e.g., Frank Easterbook, 'The Limits of Antitrust' (1984), 63 *Texas Law Review* 1, 2-3.
[8] See Patrice Bougette, Oliver Budzinski and Frédéric Marty, 'In Light of Dynamic Competition: Should We Make Merger Remedies More Flexible?' (Ilmenau Economics Discussion Papers Vol 28 No 181, Ilmenau University of Technology, September 2023).
[9] Yane Svetiev, *Experimentalist Competition Law and the Regulation of Markets* (Hart 2020); Yane Svetiev "Antitrust Governance: The New Wave of Antitrust" (2007) 38 *Loy. Univ. Chicago Law Journal* 593.
[10] Joshua Sinn, "Managing Nascent Digital Competition: An Assessment of Australian Merger Law Under Conditions of Radical Uncertainty" (2021) 44 *University of New South Wales Law Journal* 919; see

Experimentalist merger enforcement differentiates two types of cases. In the first type, the agency (or court) faces limited or no strategic uncertainty. This is because the impugned conduct is covered by clear precedent or rule, or otherwise the negative effects on consumer welfare (or some other relevant parameter) can be clearly demonstrated through market modelling (typically in a stable industry with an extensive market history). Such modelling based on existing data leads to a decision as to whether the merger should be allowed to proceed in a familiar fashion.

In the second type of case, the decision-maker faces strategic uncertainty combined with an inability to impose its own preferred solution on the market. The experimentalist framework entails that the decision-maker acknowledge uncertainty and establish protocols for testing and modification. This is implemented through the following functional steps:

(i) Identify the goals pursued by the specific intervention. In this case, the goal would be to protect and promote competition in the market (for the benefit of consumers or according to some other parameter).

(ii) The ACCC would set out its concerns of competitive harm arising from the proposed merger. While there is unlikely to be consensus from market stakeholders about the existence, size or likelihood of harm, the legal standard would require sufficient feedback from a broad base of market participants who have concerns about the harmful effects of the proposed merger.

(iii) Instead of making a one-shot decision as to whether the merger should be allowed to proceed, the ACCC negotiates with the merger parties:
   a. Potential remedial proposals that could address concerns, and
   b. Protocols for testing hypothesised harms, and monitoring the size of such harms over time.

(iv) The ACCC and parties monitor the implementation of the remedy, including through input from market participants, and by requiring regular reporting of the effects of the remedy.

(v) The remedy is then adjusted in light of experience with its implementation. The ACCC (and parties) may need to modify the remedy if monitoring and review highlights that it is ineffective or unnecessary.

The ACCC has already used undertakings as an efficient and flexible tool to negotiate remedies to address merger concerns.[11] The experimentalist approach uses of undertakings is as a dynamic tool for testing theories of harm and remedies under

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also Matthew Jennejohn, "Innovation and the Institutional Design of Merger Control" (2015) 41 *Journal of Corporate Law* 167.

[11] ACCC, Making Markets Work – Directions and Priorities, 1999, at 7.

conditions of uncertainty.[12] In this case, remedies would be provisional, in that they can be adjusted over time in light of observed effects.

Functionally, s 87B undertakings could be formulated as an experimentalist remedy by, for example:

(i) Setting out a provisional remedy (for instance, allowing the merger parties to share assets which are unlikely to have any meaningful risk of irreversibly altering market dynamics).

(ii) Establishing a protocol for testing theories of harm and/or the efficacy of remedies. For example, in the case of a global merger involving a digital platform, the ACCC could test the efficacy of a particular remedy by provisionally implementing it locally (e.g., by having the remedy geographically ringfenced to Australia), and comparing the outcome of this local 'test' to outcomes in other markets. Market stakeholders, as well as merger parties and the ACCC would provide feedback on the efficacy of the provisional remedy. In this way, the s 87B undertakings act as a learning tool.

(iii) Including a 'review clause' to the undertaking, which allows the ACCC or merger parties to negotiate an adjustment to remedies if, for instance, the remedy is found to be ineffective or unnecessary, or market conditions change in ways that could not be predicted ex-ante.[13] The review clause would provide conditions which can trigger alternative pre-agreed remedies (for example, the merger parties could be required to make certain divestitures if prices are observed to rise above a pre-agreed threshold or in the case of the exit of certain key players from the market).

It seems that no significant statutory amendment would be required to give effect to an experimentalist enforceable undertaking in the merger context. Section 87B allows for dynamic adjustment of remedies, given that undertakings may be withdrawn or varied with the consent of the ACCC.[14] However, ACCC practice or guidance may be required to establish more robust mechanisms for monitoring effects and collecting stakeholder input about remedial efficacy.

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[12] Yane Svetiev, "Settling or Learning? Commitment Decisions as a Competition Enforcement Paradigm", (2014) 33 *Yearbook of European Law* 466; Svetiev, *Experimentalist Competition Law* (Ch. 2 specifically in the context of digital platforms).

[13] For more recent reflections on dynamic considerations in analysis and remedies consistent with the experimentalist intuition see Patrice Bougette, Oliver Budzinski and Frédéric Marty, 'In Light of Dynamic Competition: Should We Make Merger Remedies More Flexible?' (Ilmenau Economics Discussion Papers Vol 28 No 181, Ilmenau University of Technology, September 2023); Nicolas Petit et al, "Situating Dynamic Competition: An Evolution Beyond Chicago" (2024) *Dynamic Competition Initiative (DCI) Working Paper*.

[14] *Competition and Consumer Act 2010* (Cth) s 87B(2).

4. Experimentalist remedies for mergers could be structured in a similar way to remedies already used for conditional authorisations.

The ACCC's practice in providing conditional authorisations for specific conduct is an example of incorporating an experimentalist logic, based on provisional permission for conduct subject to mechanisms for monitoring effects as the basis for adjusting the original decision (which could also apply to a remedy). The ACCC's decision to authorise resale price maintenance in the case of Tooltechnic[15] is an instructive example for a remedial structure that could be applied in the merger context to cope with uncertainty.

This was the first resale price maintenance authorisation application since the Act was amended to allow the ACCC to authorise such conduct. There was heightened uncertainty about the extent of public benefits that would arise from the transaction. The public benefits that the applicant claimed would arise from the proposed conduct included increased supply of retail services, increased intra-brand non-price competition (e.g., competition on service quality) and greater innovation in products and retail services.[16] There was also uncertainty about what conditions should be imposed for the authorisation to ensure that public benefits continue to outweigh public detriments and be appropriately distributed.

The conditional authorisation by the ACCC involved an experimentalist response to uncertainty. The ACCC implemented a time-limited (thus, provisional) solution for a period of four years 'to allow Tooltechnic sufficient time to demonstrate that the conduct has delivered public benefits',[17] in other words allowing the ACCC and Tooltechnic, as well as market participants, to learn about the nature and extent of benefits and detriments of the proposed conduct.

It was recognised that this would place the ACCC 'in a good position to assess whether the conduct should be re-authorised'.[18] To facilitate learning, the conditions attached to the authorisation established protocols for monitoring the nature of benefits and harms, and the efficacy of the provisional solution (authorising Tooltechnic to implement its proposed arrangements for four years). Tooltechnic was required to report certain information to the ACCC, including the minimum retail prices set, the average wholesale prices charged, and changes in the conduct of re-sellers.[19]

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[15] Australian Competition and Consumer Commission, *Determination: Application for Authorisation Lodged by Tooltechnic Systems (Aust) Pty Ltd in Respect of Resale Price Maintenance* (Report, 5 December 2014).
[16] Ibid [104].
[17] Ibid [152].
[18] Ibid [154].
[19] Ibid [157].

The ACCC subsequently used the information provided by Tooltechnic per the conditions of authorisation when it reviewed Tooltechnics' resale price maintenance notification in 2018, before the original authorisation was about to lapse. The ACCC was satisfied that, based on the monitoring information, the expected public benefits would continue to outweigh expected public detriments, and allowed the notification to stand.[20]

We submit that the experimentalist architecture of the Tooltechnic authorisation remedy could be translated to the mergers context with modifications. In the mergers context, an experimentalist remedy could also include a provisional merger outcome, with a pre-negotiated follow-up remedy which is implemented if monitoring the market effects of the provisional outcome reveals that certain conditions are met. For example, under conditions of uncertainty:

- A merger could be allowed to proceed with the pre-negotiated condition that if certain pricing, customer or supplier behaviour is observed (e.g., price increases, specific forms of reductions in quality or innovation), then the merger parties would be required to make pre-agreed divestitures. Such a remedy would require the ACCC and merger parties to monitor and report certain data (e.g., prices or customer behaviour or complaints) to be able to determine if the conditions have been triggered.
- Alternatively, a merger could be provisionally opposed, with a pre-negotiated condition that if certain market dynamics are observed (e.g., significant forms of entry or failures in innovation projects), the merger would be allowed to proceed.

To ensure that the parties minimise any potential for anti-competitive harm from the merger, the remedy could also include a pre-negotiated penalty default (e.g., requiring the acquirer to divest the target if it fails to meet agreed monitoring and reporting conditions).

5. Concluding remarks

We have argued in this submission that while the concerns about limitations of existing merger control in Australia have been correctly identified, the options set out in the consultation paper are, at the very least, insufficient to address them. While they ensure that the ACCC has an opportunity to review and make its own assessment of mergers, they they do not assist in providing a coherent framework for analysing mergers and designing and implementing appropriate remedies under

[20] Australian Competition and Consumer Commission, *Statement of Reasons in Respect of a Notification Lodged by Tooltechnic Systems (Australia) Pty Ltd for Resale Price Maintenance Conduct on Festool and Fein Power Tools* (Report, 25 July 2018).

conditions of strategic uncertainty. Such a framework is necessary if the ACCC is to be faced with a greater number of merger reviews and if dynamic market conditions necessitate the ACCC to make (more difficult and contentious) decisions under uncertainty, to do so in a speedy and efficient manner and in a way that those decisions would be approved by the courts.

We have argued that experimentalist merger law provides a promising route. This regulatory architecture responds to uncertainty by facilitating flexible real-time problem-solving, without forcing an ex-ante decision as to whether the merger should be allowed to proceed, but by providing a framework that seeks to ensure the public interest benefits of the merger are maximised consistently with the parties' commercial objectives.