Tech Council of Australia

Merger reforms consultation

Tech Council of Australia Submission

January 2024

techcouncil.com.au

1. Introduction

Thank you for the opportunity to make a submission regarding potential changes to Australia's merger rules and processes. The Tech Council of Australia (TCA) recognises the importance of strong competition laws as a foundation for economic growth and driver of innovation across all industries. In particular, we recognise the importance of merger laws and their role in clearing pro-competitive mergers with minimal delay or disruption to the transaction, while preventing anti-competitive mergers and acquisitions. Competitive markets result in enhanced choices, reduced costs and improved quality for consumers.

The TCA is Australia's peak industry body for the tech sector. The tech sector is a key pillar of the Australian economy and is Australia's seventh largest employing sector. The TCA represents a diverse cross-section of Australia's tech sector, including startups, scale-ups, venture capital funds and global tech companies.

Australia currently benefits from a well-developed, effective merger regime. While there are opportunities for improvement, the TCA is concerned that some of the proposed changes to Australia's merger control regime outlined in Treasury's Consultation Paper carry long-term risks for the growth of Australia's tech sector. Importantly, the TCA considers that the proposals outlined in the Consultation Paper should not proceed as a package, and each proposal needs to be considered on its own merit.

This submission considers the issues raised in the Consultation Paper and focuses on three key themes:

- The importance of mergers and acquisitions to the tech sector in Australia, and in particular to tech startups, driving competition and innovation
- Creating a better tech investment environment in Australia through merger review processes, and
- The consequences of proposals to change the merger test.

We also make several recommendations, which are set out at the end of the submission.

2. Mergers and acquisitions are a key feature of the tech sector in Australia

An effective merger control regime is critically important for the whole economy and to ensure incentives exist for innovative products and services delivered at the lowest cost to consumers. Mergers and acquisitions are a particularly important part of the tech sector landscape, especially in Australia, and provide incentives for innovation. A merger regime that blocks, prevents or substantially delays pro-competitive or neutral mergers and acquisitions will reduce competition in the long term, where it disincentivises innovation and entry into new markets.

Startups in Australia have four long-term options available to them:

- Remain privately held
- List on a stock exchange by way of IPO
- Be acquired by way of merger or acquisition, or
- Exit/leave markets entirely.

Competition in the tech sector thrives where startups can attract investment to foster their growth. Investors choose to invest in startups on the basis that those investments will eventually result in returns materialising. In order for investors to materialise returns, companies typically need to proceed to an IPO, or be acquired / sold. There are a range of hurdles to companies realising returns by way of an IPO, and as a consequence, mergers and acquisitions are an important way for investors to materialise returns on tech investments.

The venture ecosystem is young in Australia relative to the U.S. and Europe. Australia has not developed the depth in funding markets between venture funds and growth equity/ secondary funds that you see in those other regions.[1] As such, the vast majority of exits and instances of realised returns have been through strategic acquirers as opposed to financial investors. In order for venture funds to continue to raise funds to invest in startups, they need to show realised returns.

The option to sell a company is also important to founders and their motivations for creating a startup. Strategic acquirers offer founders the chance to see some of their equity value realised, or help them in the distribution of their product. This optionality is invaluable to them. The ability to divest companies is also a key strategy for large, established firms that are changing business strategy, and this can have significant pro-competitive effects.

The ability to be acquired, and realise returns, is critically important to investors and founders of tech startups in Australia. A major venture capital firm in Australia reports that of its portfolio companies, 14% have exited. Of these exits:

- Less than 10% have proceeded to an IPO
- More than 70% have been acquired by another company
    - Of those acquired, 20% were acquired by local strategic sponsors, and 80% were acquired by international strategic sponsors, of which almost 90% kept the product IP and 10% was to acquire the customers of the target.
- More than 20% of exits have been the result of a company exiting entirely from markets, with no merger or acquisition.

Creating barriers for companies seeking exit opportunities is likely to have a material adverse effect on the venture capital and investment landscape. It may make it harder for venture funds and investors to materialise returns, decreasing the attractiveness of these funds and thereby decreasing innovation funding over the long run. A decrease in innovation funding would impact incentives for innovation, and may result in less competition in the long term by reducing incentives for startups to innovate and enter new markets.

Mergers and acquisitions also deliver economies of scale and scope to startups, for example by expanding the combined firm's product range and capability, and enhancing economic efficiency. Nascent startups, particularly in the tech sector, introduce innovative products and services to the market, but may not benefit consumers and enhance economy-wide productivity if they are not matched with the complementary products and services, funding, operational capacity, distribution and marketing capabilities that more established firms can bring.

While the Consultation Paper acknowledges that a merger regime that clears anti-competitive mergers can risk harm to consumers, it is equally important to acknowledge

[1] Shots-on-Goal-vF.pdf (techcouncil.com.au), page 19

that merger regimes that block pro-competitive or neutral mergers, or that discourage parties from contemplating mergers, also have a significant impact on consumers. Blocking pro-competitive mergers and increasing regulatory risk would likely result in more companies failing, removing innovative products and services from markets, fewer incentives for new startups, and reduced investment in Australia compared to other countries. Ultimately, this would reduce competition from which consumers benefit and have broader consequences across the Australian economy.

It is also possible that the introduction of reforms to merger laws may cement the strength, size and competitive position of businesses who have been able to pursue more acquisitions in the past that they would otherwise be able to under a stricter regime. This could restrict the growth for emerging firms to compete with these incumbents.

Preserving the ability of startups to exit or grow by way of merger or acquisition is critically important to ensuring the long-term competitiveness of Australian tech markets, and to ensure the Australian economy can attract investment in its tech sector and keep pace with the dynamic acceleration of innovation in foreign jurisdictions. Any changes to Australia's merger regime should reflect this.

3. Australia currently has an effective merger regime

Australia currently benefits from a well-developed, effective merger regime, with the ACCC as an effective investigator and enforcer of Australia's competition laws. We consider that the current judicial enforcement regime works well.

The very few cases that are litigated likely reflect the most borderline substantial lessening of competition (SLC) cases (from either an evidentiary or legal perspective), where mergers and acquisitions that clearly raise competition concerns tending to either be dropped by the parties during the informal merger review process, or modified by remedies in such a way that they are ultimately cleared by the ACCC with conditions. The ACCC's recent higher profile losses in courts and tribunals are not necessarily a sign of ineffective merger laws, and proposals for reform must be viewed in this context.

Many of the issues that are articulated with the current merger regime are already being dealt with by the ACCC effectively, for example:

- **Mergers not being notified to the ACCC –** Woolworths' acquisition of Petstock in 2023 was delayed by an ACCC enforcement investigation into Petstock's past acquisitions of pet supply retailers. Ultimately, Petstock had to separately sell 41 retail stores,[2] reducing the purchase price by an estimated $150 million.[3] The delay and the reduction in the purchase price of the Petstock business is likely to be a significant deterrent to other companies not notifying mergers to the ACCC, in addition to the significant threat of enforcement action by the ACCC. Additionally, may mergers and acquisitions have mandatory notification requirements under foreign investment laws.
- **Mergers completing before the ACCC has concluded its review –** there is no evidence that this is a significant issue, and the ACCC has shown its highly capable

[2] Woolworths Group Limited - PETstock Pty Ltd | ACCC
[3] M&A: ACCC approves Woolworths acquisition of Petstock (afr.com)

of acting where these circumstances arise. In 2021, the ACCC was successful in obtaining an interlocutory injunction to restrain Virtus Health from completing its acquisition of Adora Fertility before the ACCC had concluded its review. The parties ultimately abandoned the transaction, and the ACCC Chair at the time stated that 'this was an important decision and sent a powerful message… [that] the ACCC will not hesitate to take appropriate action in the Federal Court to prevent completion of a transaction'.[4] This is a significant deterrent to other companies seeking to complete a transaction prior to completion of the ACCC merger review.

In relation to tech, while many of the proposed reforms are likely to have a disproportionate impact on tech compared to other industries, there is little evidence to justify why the tech sector would be targeted. The ACCC has publicly reviewed relatively few tech mergers (despite many being notified to the ACCC through the pre-assessment process) and has not recently opposed any tech mergers.

The TCA considers that to the extent that there are shortcomings with Australia's merger laws at present, the ACCC has not sufficiently tested or demonstrated these shortcomings and this is an essential prerequisite to pursuing significant reforms. To the extent that there are notification concerns, these concerns can be resolved without the significant breadth of reforms that has been proposed.

4. Getting the merger review process right can encourage investment and drive competition in the tech sector

While the TCA considers that the current merger regime is well-developed and effective, we agree that there are opportunities to improve Australia's merger regime. Targeted reform to key areas should focus on the effective administration of Australia's competition laws relative to our global peers, and promoting pro-competitive mergers while disincentivising anti-competitive mergers.

We consider that there are improvements that could be made to the merger review process with respect to:

- Increasing certainty about which mergers or acquisitions are likely to require review by the ACCC, and
- Improved timeliness and certainty about timing of merger reviews.

We do not have strong views about whether a voluntary or mandatory suspensory regime should be introduced, however, we also make some observations about the benefits and potential risks of both.

Mandatory or voluntary notification of mergers to the ACCC

The informal merger regime does not clearly specify which mergers and acquisitions should be notified to the ACCC. As a result, it is left to companies themselves to form a view of when a transaction requires ACCC notification. At present, the Merger Guidelines state that merger parties are encouraged to notify the ACCC where 'the products of the merger parties are either substitutes or complements [or] the merged firm will have a post-merger market

[4] Virtus abandons proposed acquisition of Adora | ACCC

share of greater than 20 per cent in relevant market/s'.[5] However, the Consultation Paper contemplates that mergers may be problematic where they do not meet either of these criteria (for example, in the case of creeping acquisitions), and this guidance is not always reflected in the transactions the ACCC currently reviews. Regardless of whether Australia's merger regime is voluntary or mandatory, clearer guidance should be given so that companies can be clear about when transactions should be notified.

Mandatory notification risks some companies (ie, those that would meet a revenue threshold) having every acquisition they make reviewable by the ACCC. If a mandatory notification scheme were pursued, there should be a quick, confidential mechanism for ensuring that non-problematic merger reviews are quickly and effectively dispensed with. The notification should not impose a cost burden on parties to non-problematic mergers.

In setting thresholds, we note that the concept of market definition is regularly a contentious issue between the ACCC and merging companies, and that thresholds that rely on market definition may not provide helpful guidance. If government decides that a mandatory notification regime is required, we consider that it is important that:

- There is a pathway for mergers to be quickly and confidentially cleared by the ACCC where the transaction meets notification thresholds but is unlikely to raise competition concerns. This must be confidential to ensure the initial notification and review is timely, maintains confidentiality in competitive bid scenarios and encourages merger parties to be honest and open with the information they provide.
- A mandatory notification threshold should only capture mergers and acquisitions that impact Australia.
- There should be a staged approach to the provision of information for mergers that are reviewed, where initial information is provided for preliminary views, and further information can be provided if and when required.
- Consideration should be given to the adequacy of the ACCC's resourcing, noting that a mandatory regime is likely to capture more mergers than are currently caught by the informal merger regime.
- Merger parties should also be deemed to have clearance from the ACCC if they have not received notification or further concerns from the ACCC within a defined timeframe.

We also consider that any call-in power should be accompanied by clear guidance about which transactions the ACCC is likely to call-in when they do not meet mandatory thresholds.

If notification remains voluntary, the Merger Guidelines should be amended to provide clearer guidance about which acquisitions should be notified to the ACCC.

A suspensory merger regime

As the merger regime currently stands, there is a low risk of companies threatening to complete before the ACCC has finished its review. The consequences for completion before the ACCC has finalised its review, as demonstrated by the Virtus/Adora transaction noted

[5] Merger guidelines - Final.PDF (accc.gov.au)

above, include additional delay, and significant costs and legal risk to the transaction completing.

Whether or not a mandatory and suspensory model is adopted, there should be clear timeframes for how long each stage of merger review will take. One key benefit of merger authorisations is more certainty about the length of review, where the statutory period for review is 90 days but can be extended by consent. A defined review period that can be extended by consent should extend to other merger reviews.

One of the key issues with the current merger regime are the significant delays associated with merger reviews. Delays in regulatory approval for mergers has enormous commercial implications, with delays or the expectation of long regulatory delays capable of killing deals. This would be exacerbated if a suspensory model is adopted, which would almost certainly be fatal to many merger deals.

If a mandatory and suspensory notification regime is adopted, we note:

- Consultation on the specifics of the reform is needed before such a regime is implemented. This includes consultation on the nature of the notification thresholds, the process for notification, confidentiality, and timeframes.
- An efficient and confidential mechanism is needed for non-issue transactions. Parties should be able to provide a short form 'notification' to the ACCC and the ACCC should be able to conduct a confidential review with the result of confirming that the acquisition can proceed without a public filing.

Review of ACCC decisions

The Consultation Paper contemplates various options for review of merger review decisions. If an administrative-decision making model is adopted, we consider that it is critical that there be full merits review of merger decisions, by either the Australian Competition Tribunal or Federal Court.

We consider that there is value in the Australian Competition Tribunal reviewing merger decisions, as it has the expertise and the ability to hear and decide on merger cases in an efficient manner.

However, the current 'limited merits review' model that applies in merger authorisations should not be replicated. One key consequence of limited merits review for the tech sector is that limitations on the introduction of new evidence could lead to the tribunal making a decision on the basis of outdated information, as the tech sector is characterised by rapid change and dynamism. Limiting the information that a court or tribunal can assess in reviewing a ACCC decision is likely to impact how international and tech investors view Australian as an investment destination, especially in the context of other potential reform proposals such as the reversal of the onus of proof.

5. Reforms to the merger test are likely to have significant consequences for the tech sector

As a starting point, we note that the current merger factors are neutral, and should remain that way. They form the framework for the analysis of mergers and acquisitions, and do not (and should not) have the effect of changing the test itself to have a higher or lower bar for what constitutes an SLC. We consider that the current SLC test has proven to be remarkably effective and flexible in its application to a broad range of industries, and is consistent with international merger laws.

We have strong concerns that some of the proposed changes to the merger test would have the effect of dramatically lowering the bar for what is considered to be an SLC. These changes would give the ACCC the ability to prohibit mergers that are not anti-competitive, with significant consequences.

Reversal of the onus of proof

The proposal outlined in the Consultation Paper to reverse the onus of proof is concerning for a range of reasons.

Firstly, changing the onus of proof would move Australia away from international jurisdictions where mergers are permitted unless they are likely to have the effect of SLC. This vastly increases the regulatory risk associated with transactions in Australia, and as a consequence is likely to make Australia a far less attractive place to invest. Australian tech companies compete in global markets. This will leave Australia as a less attractive place to invest in or start a tech business. In the long-term, this proposal will likely stifle legitimate economic activity rather than increasing productivity or growth in Australia's economy.

The future of tech companies is also particularly difficult to predict, with significant uncertainty about which companies will succeed and which will fail. If the onus of proof is reversed, it is much more likely that transactions with any uncertainty about the future will be rejected as they cannot show that the transaction will *not* SLC. For example, while BeReal was initially touted as a social media competitor to Meta's Facebook and Instagram, and initially met with significant success, within 5 months from its peak, its use had dropped by over 61%.[6]

Additionally, the reversal of the onus of proof is likely to have significant evidentiary implications for parties seeking to show that their transaction will not SLC. The ACCC has compulsory information gathering powers which it uses in the course of its reviews to gather information from both merger parties and a range of third parties. The ACCC uses this material to build its case that the acquisition will result in an SLC, where that is relevant. Reversing the onus of proof will require merger parties to provide evidence to the ACCC that the acquisition will not SLC, but merger parties do not have the same ability to procure evidence from third parties (either other industry participants, or third parties who may hold key data relevant to the assessment of the acquisition). We note that obtaining or attempting to procure this sort of information from other industry participants may also raise concerns about collusion.

For these reasons, the proposal to reverse the onus of proof should not proceed. Our strong concerns regarding reversing the onus of proof are further exacerbated when considered in combination with other proposals in the consultation paper, particularly the proposals to limit merger parties' ability to have full merits review of the ACCC's decision, and to expand the SLC test itself with additional factors.

[6] The death of BeReal | Dazed (dazeddigital.com)

Consideration of substantial market power

The proposal to include a structural element to the merger test by considering whether either a target or acquirer has substantial market power should also not proceed. Any company that has substantial market power in any market could be prevented from making any further acquisitions through the inclusion of this element, and this would shift the test away from considering the change that the acquisition has on competition within a market.

Tech companies, including those that operate globally, form an important part of Australia's tech ecosystem and are often uniquely placed to invest in startups and scale those startups' products and services so that they are available to customers. Startups developing potentially innovative solutions that carry significant future uncertainty and have high costs (for example, significant compute costs), may be less attractive to other investors than they are to tech companies who can use their existing assets and infrastructure to reduce the costs of startups and make them viable.

Creeping acquisitions

We have significant concerns about the way that a prohibition on creeping acquisitions would apply to tech companies. Traditionally, creeping acquisitions have been considered in the context of undifferentiated assets – the slow acquisition of a number of similar physical businesses (for example, grocery stores in a local area). In cases where tech companies have grown by acquisition, each acquisition is often differentiated, with targets providing different products and services to each other.

The introduction of a prohibition on creeping acquisitions that would apply to tech companies would have the effect of limiting acquisitions by any company making multiple acquisitions. It would also likely have the effect of widening the gap between large tech companies who have benefitted from being able to more easily make acquisitions in the past, and future competitors who will not be able to grow scale through acquisitions in the future.

Removal of a potential competitor

As noted above, it is extremely difficult to predict the future growth and market impact of tech companies. For example, the Consultation Paper outlines Facebook's acquisition of Instagram as an example of a gap in current laws which could be addressed by changes to the merger test to consider the removal of a potential competitor.

However, the potential for Instagram to become a competitor to Facebook was considered by other competition authorities internationally, none of which rejected the transaction. The UK Office of Fair Trading (OFT) noted that an industry participant told the OFT that 'it does not consider that Instagram provides significant marketing opportunities. The commercial opportunities are limited because consumers take and upload photos, but do not spend a significant amount of time in the app'.[7] The OFT ultimately concluded that it 'does not believe that it is or may be the case that the merger may be expected to result in a

[7] Office of Fair Trading (UK) - decision re anticipated acquisition by Facebook Inc of Instagram Inc, page 4

substantial lessening of competition', after considering whether Instagram would be a potential competitor to Facebook in the future.[8]

The Facebook/Instagram example demonstrates the difficulty in predicting which transactions are likely to raise concerns in the future. The issue is not whether the competition laws adequately allow for consideration of whether a company is likely to be a future competitor, but the difficulty in picking which companies are likely to succeed or grow in the long-term, which is often impossible for both investors and competition regulators alike. Changing merger laws in this way is likely to result in the blocking of many more mergers on highly speculative grounds, and is likely to result in the ACCC attempting to 'pick winners' by focusing on speculative assessments of future performance.

Consideration of data and technology

We consider that it is not necessary to include an additional merger factor that relates to 'the nature and significance of assets, including data and technology, being acquired'. Section 50 of the CCA already provides that other factors may be taken into account and the ACCC could through its Merger Guidelines clarify those factors it considers are necessary for its assessment.

6. Reforms should be considered in the context of other regulatory processes

We consider that it is essential that the consideration of potential merger reforms also take account of other regulatory processes, such as the likelihood of digital platforms regulation, FIRB processes and potential reforms.

Digital platforms regulation

Merger reforms are not the only potential competition reforms impacting Australia's tech sector.

The Government has indicated its in-principle support to the ACCC's recommendations for new competition measures for designated digital platforms. The ACCC's recommendations were made on the basis that economy-wide competition laws (such as merger laws) are unlikely to adequately protect and promote competition in digital platform markets.[9] The Government should consider the potential cumulative impacts, duplication and risks that could arise across its competition reform agenda before making decisions on individual reform proposals.

FIRB processes and potential reform

Many transactions that require merger approval also require Foreign Investment Review Board (FIRB) approval. For many companies, FIRB approval is too slow, uncertain and costly. If merger laws are reformed so that they capture more mergers, we consider that FIRB processes and potential reforms should also be considered to ensure that:

---

[8] Office of Fair Trading (UK) - decision re anticipated acquisition by Facebook Inc of Instagram Inc, page 10
[9] Digital platform services inquiry - September 2022 interim report.pdf (accc.gov.au)

- There is minimal duplication between both regulatory processes, in particular, if a mandatory notification merger clearance regime is introduced, FIRB should not require separate ACCC input for its assessment (as it currently does)
- The timeframes for both reviews are clear, and run concurrently, and
- Any filing fees introduced for merger reviews take account of FIRB filing fees so as not to disproportionately drive up the expense of acquisitions in Australia.

7. Recommendations

The TCA makes the following recommendations:

1. **Recommendation 1:** Merger laws should make Australia an attractive place to invest, and encourage the founding and growth of tech start-ups, by removing regulatory uncertainty and focusing on transactions that are likely to have a proven anti-competitive effect, rather than highly speculative theories of harm.
2. **Recommendation 2:** The merger test should remain a substantial lessening of competition. Any changes to the test should not have the effect of lowering the bar for substantiality of the effect on competition, nor should they add to or augment the test with new considerations that are not part of the well-understood and developed SLC standard that applies consistently across the competition provisions of the CCA.
3. **Recommendation 3:** Australia's merger regime should have clear timeframes for review to provide parties with improved certainty and reduce costly delays.
4. **Recommendation 4:** Australia's merger regime should have clear guidance about which transactions should be notified, in either a voluntary or mandatory regime.
5. **Recommendation 5:** Any change to an administrative decision-making regime must include full merits review.
6. **Recommendation 6:** Reforms to Australia's merger laws should be considered in the context of other regulatory processes.

We appreciate the opportunity to contribute feedback to these proposed reforms and look forward to an ongoing consultation on them.