

## CREEPING ACQUISITIONS – THE WAY FORWARD

1. On 1 September 2008 the Government released a creeping acquisitions discussion paper that sought views from interested parties regarding options for the implementation of a creeping acquisitions law. The paper was released in response to concerns raised by the Australian Competition and Consumer Commission (ACCC)<sup>1</sup> that section 50 of the *Trade Practices Act 1974* (TPA) may not be able to deal with creeping acquisitions that, according to the ACCC, have the potential to cause competition concerns in certain concentrated industries.<sup>2</sup>

2. As canvassed in the first discussion paper, the Government considered that creeping acquisitions concerns related to a potential loophole in section 50<sup>3</sup>, which currently prohibits acquisitions that would, or would be likely to, substantially lessen competition in a market. This loophole was understood to relate to a series of small acquisitions that individually would not substantially lessen competition in a market, but collectively may have that effect over time. Many submissions found that the loophole in itself may not be a problem in all situations, but that it could cause considerable competitive harm and consumer detriment in certain circumstances.

3. A number of submissions considered that the key concern with creeping acquisitions arises when corporations with substantial market power make one or more small-scale acquisitions, such that even a small enhancement of that market power may have an impact on consumers that warrants concern.<sup>4</sup> As a result, this paper focuses specifically on activities of corporations with substantial market power.

4. Substantial market power is a concept that is currently used in section 46, but has previously not been used in mergers and acquisitions provisions of the TPA. Substantial market power has been interpreted to mean:

- *“The ability of a firm to raise prices above the 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.”*<sup>5</sup>

5. Subsection 46(3D) states that more than one corporation may have a substantial degree of power in a market. The concept of market power is well established in

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1 For example: Senate Economics Legislation Committee Estimates (2006) Hansard, 1 June, p.63

2 For example: Assessing shopper docket petrol discounts and acquisitions in the petrol and grocery sectors (2004) ACCC p.27

3 Unless otherwise indicated, all references to sections relate to provisions of the *Trade Practices Act 1974*.

4 For example, ACCC submission p3.

5 *Queensland Wire Industries Pty Ltd v Broken Hill Pty Co Ltd* (1989) 167 CLR 177 at 188.

competition law, and is far more effective than a focus on market share, as it allows a court to take into account all the relevant characteristics of a market.

- For example, the Federal Court<sup>6</sup> has previously imposed penalties for misuse of substantial market power where a corporation had only around 16-20 per cent of the share in the relevant market.

6. Current mergers and acquisitions legislation does not prevent acquisitions that increase existing positions of substantial market power but do not substantially lessen competition: there is an inherent limitation to the existing section 50 that enables corporations with substantial market power to further enhance that power through small-scale acquisitions.

7. Some submissions noted that the TPA is generally regarded to place greater scrutiny on corporations with existing substantial market power in a market.<sup>7</sup> Therefore, there is an argument that a new creeping acquisitions provision that specifically targets smaller-scale acquisitions by firms with substantial market power may be regarded as being consistent with the underlying policy principles of the TPA. A range of submissions supported this approach to a creeping acquisitions law, particularly those from the independent grocery sector and the ACCC.

8. On the other hand, many submissions raised concerns that a provision targeting small-scale acquisitions may represent a level of intervention that could be out of proportion with the size of the competitive harm and consumer detriment associated with the conduct. However, where there is evidence of a limitation in the TPA that may be exploited to the detriment of consumers, there is a role for government to resolve this limitation. Through amendments to the TPA, or other policy options, governments can attempt to create the conditions for markets to function more effectively and ultimately help enhance the welfare of Australians.

9. In the first discussion paper, the Government canvassed two possible solutions to address creeping acquisitions concerns: the 'aggregation model' and the 'substantial market power model' (SMP model). The Government notes that there were divergent views as to the effectiveness and appropriateness of these models as practical responses to creeping acquisitions concerns. In particular, in addition to the 'proportionality' issue mentioned above, the aggregation model was deemed impractical by many and there were concerns the SMP model had the potential to undermine the existing prohibition in section 50 by introducing the term 'any lessening of competition' as opposed to 'substantial lessening of competition'.

10. Therefore, the Government welcomes alternative approaches to the issue. These may include both regulatory and non-regulatory options.

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<sup>6</sup> *Australian Competition and Consumer Commission v Australian Safeway Stores Pty Limited* (No 4) [2006] FCA 21 (31 January 2006)

<sup>7</sup> For example, ACCC submission p10.

11. One option being carefully considered by the Government is an amended version of the SMP model introduced in the first discussion paper. This model would prohibit mergers and acquisitions that enhance a corporation's existing substantial market power.

12. This amended version of the SMP model might read:

(1) *A corporation that has a substantial degree of power in a market 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 enhancing that corporation's substantial market power in that market.*

13. In relation to the original SMP model, there was a concern that the use of the descriptor "any lessening of competition" may result in ambiguity and risk reinterpretation by the Courts of the "substantial lessening of competition" test in the existing prohibition in section 50. By amending the SMP model to deal directly with the "enhancement" of market power, this model seeks to complement, rather than undermine, the existing substantial lessening of competition test in section 50. The Government continues to be committed to the existing section 50, and considers that it is functioning well in the majority of mergers and acquisitions cases.

14. This amended model would enable the ACCC to address creeping acquisitions concerns in a timely manner, and could be effectively incorporated into the ACCC's existing informal clearance process.

15. Another approach could be to trigger the application of a creeping acquisitions law for a set period of time in certain restricted circumstances only, similar to the Price Surveillance provisions in Part VIIA of the TPA. Under this proposal, the Minister would have the power to unilaterally, 'declare' a corporation or a product/service sector, where the Minister has concerns about potential and/or actual competitive harm from creeping acquisitions, or acquisitions by corporations with substantial market power. Alternatively, this model could be designed so the Minister could only make a declaration after receiving an application from the ACCC. The ACCC would make an application where it has concerns regarding creeping acquisitions by a particular corporation, or in a product/service sector.

16. The test that would apply to acquisitions by declared corporations or acquisitions by corporations in declared product/service sectors would be the same as the test described in paragraph 12 above. That is:

(1) *A corporation that has a substantial degree of power in a market 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 enhancing that corporation's substantial market power in that market.*

This would operate in addition to the existing mergers and acquisitions test in section 50 of the TPA.

17. As part of the declaration, the Minister would clearly specify the relevant corporation or product/service sector. As an additional feature, the Minister could also be provided with the power to set appropriate thresholds for the mandatory notification of acquisitions to the ACCC, by declared corporations or by corporations in declared product/service sectors, as part of the declaration process. Thresholds would be carefully established to ensure the creeping acquisitions law was applied with minimal burden while still maximising transparency and accountability.

18. The Parliamentary Joint Select Committee on the Retailing Sector (Baird Committee) in its 1999 *Fair Market or Market Failure* report recommended<sup>8</sup> in response to creeping acquisitions concerns in the grocery sector that a code of conduct be established requiring the mandatory notification of supermarket acquisitions by publicly listed corporations. This recommendation was not implemented. However, there has been a voluntary code introduced by the Government, the *Produce and Grocery Industry Code of Conduct*, which requires signatories to notify the ACCC of acquisitions of a controlling interest in a grocery retailer. In the Grocery Inquiry report, the ACCC noted that, despite the requirements of this code, the ACCC is aware that there were still a small number of acquisitions over this period where it was not notified.<sup>9</sup>

19. While the mandatory notification of acquisitions by declared corporations or by corporations in declared product/service sectors may increase regulatory burdens on business and the ACCC, it may serve to resolve information asymmetries and increase transparency regarding the practical impact of creeping acquisitions, through the use of a public process by the ACCC.

20. Interventions by governments in markets can have unintended consequences and unexpected dynamic effects. In response to the SMP model in the first discussion paper, many submissions raised concerns about the impact such a model may have on legitimate and organic growth of businesses. The Government is acutely aware that any intervention in this area, while preventing harm and detriment, should not stop the legitimate and organic growth of businesses that is designed to increase production efficiencies to enhance the welfare of Australians. This is particularly important in the current economic environment. As such, the Government recognises that there is a fine balance to be struck here.

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8 Recommendation 4

9 At page 427.

21. To help achieve this balance, the Government seeks further views on:
- the potential unintended consequences of a creeping acquisitions law that targets enhancements to a corporation’s substantial market power. Recognising that such an amendment would use a different threshold and concept than the existing substantial lessening of competition test, the Government is also interested in the potential impact such an amendment might have on existing section 50, and on other prohibitions in Part IV (such as section 46).
  - the potential unintended consequences of a creeping acquisitions law that targets ‘declared’ corporations or product/service markets.
  - how any potential unintended consequences may be addressed or minimised, particularly in the design of the law.
  - the costs and benefits associated with the option of including a mandatory notification requirement, using thresholds unique to each particular declaration, determined by the Minister.

### Question 1

*What are your views on the two regulatory options mentioned above? What potential unintended consequences need to be considered? How might these unintended consequences be addressed?*

### Question 2

*Are there alternative regulatory or non-regulatory options that might be appropriate responses to creeping acquisitions concerns? How might these work in practice? What are the costs and benefits?*

### Submissions

The Government welcomes any submissions regarding the issues identified above, or any other matter related to the issue of creeping acquisitions.

Submissions will be made publicly available on the Treasury website. If a submission, or any part of it, is to be treated as confidential, please indicate this clearly on the submission.<sup>10</sup>

Submissions should be made by Friday 12 June to:

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<sup>10</sup> Any request made under the Freedom of Information Act 1982 for a submission marked ‘confidential’ to be made available will be determined in accordance with that Act.

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