Factsheet

WHAT YOU NEED TO KNOW ABOUT:

the ACCC's approach to merger reviews, including local markets

April 2014

The ACCC reviews mergers and acquisitions to determine whether they are likely to substantially lessen competition, with the aim of ensuring that markets work well for consumers. This may include acquisitions of single outlets in industries such as supermarkets, petrol, liquor and childcare. This factsheet explains which factors the ACCC takes into account in its merger review process.

Competition can be reduced when one firm buys another firm or its assets, potentially resulting in increased prices and/or reduced product quality, service, choice or innovation for consumers.

The role of the Australian Competition and Consumer Commission (ACCC) is to assess whether a proposed acquisition is likely to substantially lessen competition in the relevant market as a whole.

The ACCC cannot oppose an acquisition that reduces competition unless the effect is *substantial*. It also cannot oppose an acquisition due to community preferences, national interest considerations or other reasons that aren't competition related.

Why does the ACCC review mergers and acquisitions?

The level of competition in a market performs an important function in the economy. The prices we pay and the level of service we receive as consumers are affected by the level of competitive tension between firms in a market. Greater competition means that firms are also more likely to innovate and invest in new products.

When one firm buys another firm or its assets, the acquisition may create efficiency benefits but will also have an impact on competition. In many cases the impact on competition will be minimal, but some acquisitions can reduce competition significantly by reducing the number of competitors and changing the way the remaining competitors behave. This can negatively affect consumers through higher prices, lower quality or service or less choice or innovation.

The ACCC's role is to review acquisitions to determine whether they are likely to adversely affect competition. If the ACCC thinks an acquisition is likely to substantially lessen competition and the parties still intend to proceed, the ACCC can apply to the Court to stop the acquisition. If the acquisition has already occurred, the ACCC can apply for penalties or an order that the acquired business be divested. The ACCC must prove to the Court that the acquisition is likely to substantially lessen competition.

What is the test and how does the ACCC decide?

Section 50 of the *Competition and Consumer Act 2010* (Act) prohibits an acquisition of shares or assets (including a merger between two companies) which is likely to have the effect of *substantially lessening competition* in any market. The main indicator of a substantial lessening of competition is whether the acquisition will enable firms in the market to *raise prices or reduce product quality (including service and choice) or innovation* following the acquisition. In competitive markets, firms are constrained from raising prices (or reducing quality or innovation) by the threat of customers moving to another supplier. If an acquisition reduces this threat (because customers have fewer alternatives to turn to), then it may become profitable for the merged firm to raise prices or reduce quality or innovation.

However, just because an acquisition will reduce the number of firms in the market does not necessarily mean that it will *substantially* reduce competition. The ACCC must also look at other factors such as whether the remaining firms in the market are likely to provide enough competition, or whether the threat of new firms entering the market is sufficient to stop the acquirer from increasing prices. Even a market with only two or three firms may be competitive if those firms face the threat of new firms entering and taking away their customers.

The Act requires the ACCC to focus on the impact of the acquisition in question. Even if the acquiring firm has previously made similar (but separate) acquisitions, the ACCC can only consider the impact of the current acquisition, not the combined effect of that and other acquisitions by the same firm.

The markets that the ACCC considers in its review may be national, state-based, regional or local. The Q&A on the next page discusses the ACCC's approach to acquisitions that affect local markets.

What factors are not relevant to the ACCC's decision?

Impact of the acquisition on specific competitors

The Act requires the ACCC to decide how a proposed acquisition is likely to affect the competitive process as a whole in the relevant market. Sometimes an acquisition will create a more efficient competitor meaning that other firms in the market will have to compete harder in order to survive and their profits may be reduced. Generally this will be a pro-competitive outcome and the acquisition will not be opposed by the ACCC, as it means lower prices, improved quality and/or increased innovation, all of which benefit consumers.

Fixing existing competition problems

Sometimes the relevant market will be uncompetitive before the proposed acquisition occurs, for example because there are one or two large firms that dominate the market. In that situation, the ACCC must decide whether the proposed acquisition itself will substantially worsen the state of competition in that market, or prevent a significant pro-competitive development from occurring. The ACCC cannot use the merger review process to fix existing competition problems in a market.

National interest considerations

Sometimes members of the public are opposed to an overseas company buying an Australian company because they believe that the acquisition is against Australia's national interest. The Federal Treasurer, on advice from the Foreign Investment Review Board, decides whether acquisitions by foreign controlled companies are against the national interest. The ACCC cannot oppose an acquisition on national interest grounds. Therefore if an acquisition by an overseas firm does not raise competition concerns, the ACCC will not oppose it.

The 'character' of a local area and community preferences

In some cases residents are concerned that the purchase of a local business (often by a large chain) will negatively impact on their local area, for example by changing the character of the area or simply through the loss of a business that has been in the local community for a long time. The ACCC cannot oppose an acquisition for these reasons. Concerns of this type may raise planning issues, but these issues are the responsibility of local government, not the ACCC.

For more information

The ACCC's merger review process aims to ensure that markets work for Australian consumers, both now and in the future. For more information on how the ACCC reviews mergers and acquisitions, please see our Merger Guidelines and Informal Merger Review Process Guidelines at www.accc.gov.au/-/mergers/merger-reviews.

Q&A on acquisitions involving local markets

Why does the ACCC review some acquisitions in local retail markets?

In some cases, for example when assessing an acquisition by a major retail chain, the ACCC may focus its review on a local market, which could be as narrow as a few kilometres' radius if the evidence indicates that customers don't usually travel further than this to access the product or service. Examples of industries in which local retail markets are often relevant are supermarkets, liquor, petrol and childcare.

Is the test different for local markets?

No, when the ACCC looks at a local market its focus is still the impact of the acquisition on competition (for example, will removing a local competitor mean higher prices for consumers?).

Both acquisitions of existing businesses or their sites (either freehold or leasehold) and acquisitions for the purpose of developing new sites can raise competition issues in local markets.

Can the ACCC stop a large chain from entering a new market if it will negatively impact local retailers?

No. The objective of the Act is to protect competition, not competitors. When a chain enters a new area where it currently has no stores, it will generally introduce a new source of competition to that local market and therefore the acquisition in question will not raise competition concerns.

The ACCC recognises that the entry of a large chain which has scale and buying power may adversely affect the viability of independent retailers in that market and in some cases may even mean that a retailer goes out of business because it can no longer compete. However, the ACCC cannot oppose the chain's entry into that market on that basis.

A common concern is that the opening of a new supermarket will make it harder for butchers, bakers, greengrocers and other local retailers to compete. However, the ACCC cannot oppose an acquisition solely to protect local businesses.

What factors does the ACCC take into account?

In assessing whether an acquisition of an independent retailer or a development site by a chain is likely to substantially lessen competition, the ACCC will consider a range of issues, including:

- Where the chain proposes to acquire an existing retailer, does competition from that retailer provide benefits that are valued by many consumers and will be lost if the acquisition proceeds, such as discounts or promotions, high levels of service or a different product range? For example, the removal of an independent retailer which competes vigorously on price or quality is likely to raise significant competition concerns. On the other hand, if customers mainly shop there because of the location then it is less likely to substantially lessen competition because customers will still get the benefit of the convenient location once the independent store is replaced with a chain store.
- To what extent does the independent retailer's presence cause the other retailers in the local market to compete harder (whether on price, quality or some other aspect) and will this source of competition be lost if the acquisition occurs? Even if there are a number of firms in the local market, if the acquisition removes the chain's closest competitor (meaning the firm that competes most directly, not necessarily the one that's geographically closest) it may raise competition concerns. On the other hand, removal of a retailer that isn't a significant competitor is less likely to raise concerns.
- Where the chain proposes to acquire a development site, does the chain already have a significant presence in the local area? And what is likely to happen to the site if the chain doesn't acquire it? The ACCC is more likely to have concerns with an acquisition of a development site if the acquiring chain already has a significant presence in the area and the likely alternative to the acquisition is that a competing retailer would open on that site.
- Will there be opportunities for other retailers to enter the local market in future, or is the acquisition likely to remove those opportunities (e.g. are other suitable retail sites available)?

The large chains already have market power—shouldn't the ACCC stop them from expanding?

The ACCC must assess the impact that each individual acquisition will have on competition. An acquisition of a retail store may also have effects outside the local market, for example increasing the scale and buyer power of the acquiring chain (which could make it harder for other retailers to compete with the chain). However, an acquisition of a single store is unlikely to have a substantial effect on competition in those other markets. Australian law does not have market share caps or other rules that stop a chain from growing above a particular size. This is consistent with laws in many other countries, including the United States.

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