Bulletin

DECEMBER 2016

Is that a fact?

THE PREFERENCE FOR FACTUAL INFERENCES FROM ORAL TESTIMONY IN SEA SWIFT'S ACQUISITION OF TOLL MARINE

A recent decision by The Australian Competition Tribunal brings into sharp focus a difference between economists and the courts in their approach to facts. The decision is Application by Sea Swift Pty Limited [2016] A Comp T 9. Frontier Economics examines this case and suggests how the Tribunal's approach to the facts contributed to the outcome.

Economists are trained to be sceptical of people's statements about their motivation or their intentions. They have a strong preference to characterise people's behaviour based on their past conduct. In contrast, lawyers have a strong tradition of relying on the oral testimony of individuals and testing that testimony by means of cross-examination.

The case

Sea Swift applied to the Australian Competition Tribunal for authorisation of its proposed acquisition of Toll Marine Logistics (TML). Prior to 2013, Sea Swift operated scheduled marine transport services in far-North Queensland and Toll Marine operated similar services in the Northern Territory. In January 2012, Sea Swift commenced an assault on the traditional business of Toll Marine. Toll Marine

→

retaliated by expanding into the traditional areas of Sea Swift. The result was that both parties were losing money. The parties decided to solve this problem through a merger and sought an informal clearance from the ACCC. The ACCC refused to grant an informal clearance; and Sea Swift applied to the Tribunal for authorisation on two grounds. The first ground was that the merger would not lessen competition. The second ground was that its undertakings to continue operation of services to remote communities, and to submit these services to a regime of price controls, would create benefits to the public. The Tribunal accepted both these propositions.

The ACCC's case

The ACCC opposed the acquisition on the ground that Sea Swift was willing to pay a 'substantial premium' over the value of tangible assets that it intended to acquire from TML. According to the ACCC, this substantial premium was a payment for the transfer of customers. The ACCC contended that the fact that Sea Swift was willing to pay a significant price for the "certainty" of acquiring the TML contracts showed that, in the future without the proposed acquisition, Sea Swift was uncertain whether it would win those contracts. The Tribunal stated:

> *In saying this, the ACCC relied on the evidence of Mr Readdy (an executive of CHAMP Ventures [the private equity firm that controlled Sea Swift] and non-executive director of Sea Swift) that Sea Swift considers the certainty of picking up TML's Largest Contracts to be a benefit of the Proposed Acquisition. The ACCC asserted that Sea Swift was prepared to pay a "substantial premium" despite TML's announcement that it would exit the market in the short term if the Proposed Acquisition was not authorised because it avoided the risk posed by competitive forces which would exist if the Proposed Acquisition did not proceed. (at para 210)*

The Tribunal acknowledged that this argument was fine in theory; but found it was inconsistent with the facts:

> *In theory, the payment of a consideration greater than the value of a company's tangible assets may indicate that the purchaser is paying for a market share that could result in a significant lessening of competition. However, in the Tribunal's consideration of Sea Swift's Application, theory must give way to fact. (at para 211)*

The key fact that the Tribunal found 'fatally undermined' the ACCC's theory of harm was that Sea Swift would win all of TML's large customers either by subcontract or as a result of winning a new contract whether or not the authorisation was granted (paras 248 and 249). In other words, competition wouldn't be lessened as a result of the merger. It formed this view after considering the evidence in chief and cross-examination of the executives of competitor

Is that a fact?

companies. The Tribunal rejected the evidence of those competitors which claimed they could win major contracts in competition with Sea Swift; and it accepted the oral evidence of those competitors which said they had no plans to compete for any contracts that might become available in the near future.

Weighing up

In its assessment of the likely effect of the proposed acquisition on competition, the Tribunal relied entirely on its assessment of the evidence in chief and cross-examination of industry participants. These prompted its factual findings that Sea Swift would gain all of TML's key customers with or without the proposed acquisition; and, because of these factual findings based on evidence in chief and cross-examination, the Tribunal decided that it did not need to deal with (i) the premium that Sea Swift was paying and (ii) Sea Swift's perception that it needed to pay this premium to avoid the risk of not winning TML's key customers.

The Tribunal stated:

> *These factual findings fatally undermine much of the ACCC's theory of harm. On this basis, the Tribunal does not consider that it is necessary to deal with the ACCC's submission that Sea Swift was willing to enter into the ARASSA on 17 March 2016 and pay a "substantial premium" to avoid the risk of failing to capture the revenue streams from TML's Largest Contracts. Suffice it to say that as there was no evidence given to the Tribunal of the present value of the vendor note or the shares in Sea Swift which Toll will receive as consideration under the Proposed Acquisition, the foundation for the ACCC's contention that there was a "substantial premium" was not made out. Further, Sea Swift's perception of risk without full knowledge of TML's intentions or the intentions of TML's Largest Customers, and the amount that it was willing to pay for TML's assets as a result, is irrelevant to the Tribunal's evaluation of the impact on competition with and without the Proposed Acquisition. (Para 249)*

At the close

In the end, the Tribunal found that it knew more about the competition faced by Sea Swift than did Sea Swift itself. The opinion of Sea Swift (and its private equity owners) in March 2015 was that it had to pay something for the certainty that it would be able to secure all of TML's major contracts. However, the Tribunal found, as a matter of fact, that Sea Swift was mistaken.

Is that a fact?

Although the Tribunal characterised its reasoning as facts fatally undermining theory, the truth is more subtle. The 'facts' found by the Tribunal were based on its assessment of the evidence in chief and cross-examination of business executives. On the basis of accepting some of this evidence and rejecting others, it decided on 'facts' which made the magnitude of the premium and the reasons paid for the premium to be irrelevant.

Early competition cases in Australia often reflected tension between the approaches of lawyers and those of economists. This tension largely disappeared over the years as lawyers and economists came to understand each other's reasoning. However, the decision of the Tribunal in Sea Swift shows that remnants of the tension remain.

CONTACT	**Philip Williams** philip.williams@frontier-economics.com.au
	Frontier Economics Pty Ltd
	FRONTIER ECONOMICS ASIA-PACIFIC BRISBANE | MELBOURNE | SINGAPORE | SYDNEY
	www.frontier-economics.com.au