Who should adjudicate mergers?

Philip Williams, Frontier Economics competition and dispute support lead, discusses the Australian Competition and Consumer Commission's proposed new merger process.

Introduction

At a speech to the Competition and Consumer Workshop 2021 of the Law Council of Australia on 27 August 2021, the Chair of the ACCC, Rod Sims, proposed a single new formal process for assessing the effects of mergers on competition. The proposed new merger process would have the following elements:

1. there would be a single process - authorisation would not be available
2. notification would be mandatory – above certain thresholds
3. the ACCC would replace the courts as the principal decision-maker
4. the ACCC would be obliged to provide detailed reasons for its decisions and
5. there would be a right of appeal to the Tribunal.

The current test for mergers under the *Competition and Consumer Act* is that the acquisition should not proceed if it is likely to have the effect of substantially lessening competition. This requires the decision maker to compare the future of the relevant market with and without the proposed acquisition and to decide whether the future state of competition with the proposed acquisition is so much worse than the future state of competition without the proposed acquisition that the proposed acquisition should not proceed. This law requires judges to undertake a detailed economic analysis of conduct that is likely to occur well into the future and to make difficult judgements as to appropriate public policy.

In my opinion, the ACCC's proposal for reform of the process by which mergers are assessed is worth serious consideration. From the beginnings of what is now known as the *Competition and Consumer Act*, distinguished commentators have expressed doubts as to whether courts are the appropriate institutions to undertake these tasks; and, although the courts have adopted changes in procedure that have improved their ability to deal with complex economic analysis, judges would be much better able to undertake this analysis if they were aided by an economist.

In 1974, Bob Baxt and Maureen Brunt wrote a detailed assessment of the bill that became our current *Competition and Consumer Act*.[1] The paper expressed concerns about the work that the courts would be required to do under the Bill. After the Bill become law, Maureen Brunt elaborated on these misgivings in a paper published in 1976.[2]

[1] R Baxt and M Brunt, "The Murphy Trade practices Bill: Admirable Objectives, Inadequate Means", (1974) 2 Australian Business Law Review.

[2] Maureen Brunt, "Lawyers and Competition Policy (1976)" reprinted pp 84 to 125 of Maureen Brunt, Economic Essays on Australian and New Zealand Competition Law, Kluwer (2003).

The theme of these concerns was that, although the courts are the appropriate enforcers of reasonably-clear legal rules, the courts were not suited to undertake economic regulation. She refers to her earlier paper with Bob Baxt and states:

> The crux of the argument is this. If the law can be stated with reasonable precision, with prospective liability established by per se rules or strong presumptions, such that the commission of an offence is knowable and avoidable, then the appropriate enforcement mechanism is a court and the appropriate remedy not only injunction but also punishment.[3]

She goes on to say: "The use of *per se* tests, rebuttable presumptions and short-cut rules of reason takes much economic analysis and public interest evaluation outside the court – which is as it should be."[4]

> Essentially, then, the contention here is that extended rule of reason analysis of any kind is out of place in a court of law: evidence must be cut back from "the jungle of 'all relevant factors'" to what is relevant to an articulated test; and while argument (one hopes) makes use of economic concepts it will tend to be in the nature of short chains of reasoning stemming from the evidence. As E. S. Mason once wrote: "An attempt to push enquiry into effects very far is clearly an invitation to non-enforcement". However inviting the wide generality of the language of the statute might be, however challenging the problems posed by broad-based issues of monopolization and merger, the tendency of the courts will be to cut back the issues – interpret the statute – in a way that gives rise to legally operational standards.' [5]

The reference in this quote to Edward Mason is revealing. Mason was Maureen Brunt's teacher when she undertook her Ph D at Harvard University. Mason was the founder of the structure-conduct-performance paradigm; and he wrote a series of papers in the 1940s and 1950s exploring whether US courts were fit for the task of analysing competition issues.[6]

After Professor Brunt had undertaken her early work on Australian industrial organisation, this issue became her key academic and professional interest. As she stated in the Introduction to the volume of her collected works:

> Over the last 30 years the question I have pursued at the centre of my academic and professional life has come this: How might the rule of law be used to achieve an effectively competitive economy as the economist would understand the phrase?[7]

In my opinion, the proposed new merger process would help address five problems that exist under the current system.

[3] Ibid at p 106.

[4] Ibid at p 107.

[5] Ibid at pp 108-109.

[6] The papers are reprinted in E S Mason, *Economic Concentration and the Monopoly Problem*, Harvard University Press (1957).

[7] Maureen Brunt, Economic Essays on Australian and New Zealand Competition Law, Kluwer (2003), p 4.

First problem: lack of transparency

Although the courts are the ultimate decision makers under the current merger law, we have an informal process whereby parties apply to the ACCC for informal guidance as to whether the proposed acquisition is likely to infringe the Act. In cases that have a high probability of ending in court, applicants, third parties and the ACCC itself have strong incentives to hide information from each other: they have an incentive to hide information so as to maximise their chances of succeeding if the matter ends up in court. This can be inefficient and fundamentally unfair.

This would be changed under the proposed procedure. Applicants will have a strong incentive to disclose information because rights of appeal will be limited to the material that has been disclosed to the ACCC. As the Chair stated in his speech, "Importantly, the Tribunal would only be able to have regard to the material which was before the ACCC when it made its decision, unless subsequent events have occurred."

In my opinion, similar obligations and incentives should be imposed on the ACCC. The Tribunal should only be able to have regard to material from the ACCC which the ACCC had disclosed to the applicants sufficiently prior to the ACCC's decision so that the parties had adequate time to respond to the material prior to the ACCC's making its decision. This material should include the workings of any calculations undertaken by the Commission and any evidence from third parties.

Second problem: no detailed decisions

The second problem also relates to the current informal advisory process. The problem is that the ACCC provides no detailed reasons for the advice it gives. This has been raised as an issue for some years; and the ACCC has responded to the criticism by producing Public Competition Assessments (PCAs) for matters that the ACCC has considered at some length.

The PCAs are usually between five and 30 pages long. They give the parties (and the public) some idea of the processes of reasoning behind the advice of the ACCC. However, they reveal little about how the ACCC evaluated the evidence before it. As they always state: "As assessments are brief and do not refer to confidential information provided by the parties or other market participants, assessments do not necessarily set out all of the issues and information considered by the ACCC, nor all of the analysis and reasons of the ACCC."

The proposed procedure will require the ACCC to publish detailed reasons for its decision to clear, or decline to clear, proposed acquisitions. In my opinion, this will do much to inform applicants of the reasons for the decisions of the ACCC; and it will inform other parties of the processes of reasoning of the ACCC.

Third problem: court processes bias economic evidence

I share the opinions of Professors Mason and Brunt that courts can deal well with short chains of reasoning; but they are not well equipped to undertake extended rule of reason analysis. For this reason, the US courts have developed short-cut operational tests for liability. These short-cut operational tests take economic regulation closer to the rule of law. Expert economists giving evidence in the United States are, of course, bound to follow these operational tests. This has the effect of reducing matters of tricky economic judgement to simple rules.

Expert economists (whether from Australia, the United States or elsewhere) giving evidence in Australian courts sometimes feel obliged to adopt these short-cut operational tests as though they were part of the general practice of professional economists when, in fact, they are simple rules constraining economists when they give evidence before courts in the United States.

A vivid example of economists using these short-cut operational rules occurred in the litigation in New Zealand and Australia involved with international air cargo.[8] A key issue in both these cases were the principles by which the geographic boundaries to markets should be defined. Experts from the United States gave evidence in both jurisdictions to the effect that the geographic boundaries to an air cargo market begin and end at the point where the cargo is loaded on the aircraft. This evidence was not based on any established economic theory. Rather, it was based on the text of the US Horizontal Merger Guidelines. The economists from the United States had so absorbed the short-cut operational tests in their Merger Guidelines that they had come to regard them as part of the literature of economics. The first-instance, High Court of New Zealand had no difficulty in rejecting this view. The Australian courts had a more-difficult time of it. However, the High Court of Australia also rejected this view.[9]

In my opinion, the proposed procedure will help overcome this problem. Because the decision makers (both initially and on appeal) will involve professional economists, economic experts will not feel obliged to follow operational short-cuts that have been developed to make an issue justiciable. They will be able to deal with issues based on standard economic theory.

Fourth problem: judges are limited in their ability to assess economic argument

Non-specialist judges encounter expert testimony from a range of professions: medical practitioners, chemists, physicists, economists, anthropologists and so on. Because of our common law heritage, an expert put up by one side is generally countered by an expert produced by the other. The court is then faced with the difficult problem of who to trust.

The courts have published guidelines for expert witnesses that require experts to assist the judge, rather than to act as advocates for the party which has hired them. The courts have been forced to adopt these strategies principally because they do not always have the expertise to recognise bad economics if it is put persuasively. Professor Brunt had no such problem when sitting as a member of the Competition Tribunal:

> It is a corollary that "partisan economist experts" - "hired guns" – are not necessarily counterproductive. This "partisan" characterization is long-standing, even conventional, and almost universally deplored. I note that Judge Richard Posner, for example, in a recent essay on "The Law and Economics of the Economic Expert Witness" adopts this stance. I myself used to think this way, adopting uncritically the conventional view: see the early essays in this volume, "Lawyers and Competition Policy" and "Economic Evidence". It was only after years of sitting both in the Tribunal and the New Zealand

[8] *Commerce Commission v Air New Zealand and others* (2011) CIV-2008-404-8352; and *ACCC v Air New Zealand* [2014] FCA 1157.

[9] *Air New Zealand Ltd v Australian Competition and Consumer Commission; PT Garuda Indonesia Ltd v Australian Competition and Consumer Commission* [2017] HCA 21 (14 June 2017)

> courts that I realised that this was the wrong perspective. Invariably I was assisted if more than one economist appeared and something of a debate ensued. Of course, economists, just like other people, can at time lack integrity. But there is no reason to deny ourselves the assistance that can be obtained from economists debating their interpretation of the facts and the issues.[10]

In my opinion, the proposed procedure will assist decision makers in dealing with bad economics put persuasively. Decision makers will not have to decide who they should trust; they will be able to assess arguments on their merits.

Fifth problem: artificial distinction between competition and the public interest

The ACCC's proposal is for a single process: it would eliminate the option of applying for authorisation.

One of the unusual features of Australian competition law is its system of dual adjudication. The courts decide whether or not conduct lessens competition; and it is left to the Commission and the Tribunal to decide whether conduct is likely to yield such benefits to the public that, even though it may lessen competition substantially, it should be allowed.

This distinction between substantial lessening of competition and public benefit has always troubled economists.[11] Consideration of whether conduct is likely to substantially lessen competition may involve consideration of its likely effect on the structure of a market, the conduct within the market and the performance of the market. As the Tribunal stated in Chime No. 2:

> What, then, do we draw from the various models for studying a market to determine its competitiveness and for assessing how the market may behave in the future? In the Tribunal's view a market is sufficiently competitive if the market experiences at least a reasonable degree of rivalry between firms each of which suffers some constraint in their use of market power from competitors (actual and potential) and from customers. The criteria for such competition are structural (a sufficient number of sellers, few inhibitions on entry and expansion), conduct-based (e.g. no collusion between firms, no exclusionary or predatory tactics) and performance-based (e.g. firms should be efficient, prices should reflect costs and be responsive to changing market forces).[12]

This would be a standard view in most antitrust jurisdictions. However, if proper consideration of effects of competition involves consideration of its effects on structure, conduct and performance, there seems to be little left for any other public interest considerations. In my opinion, denying parties access to authorisation would involve little or no cost. All relevant considerations can be allowed under a proper consideration of effects on competition.

[10] Maureen Brunt, "Author's Introduction", to Maureen Brunt, Economic Essays on Australian and New Zealand Competition Law, Kluwer (2003), p 44.

[11] See, for example, Maureen Brunt, "The Australian Antitrust Law after 20 Years – A Stocktake", reprinted in Maureen Brunt, Economic Essays on Australian and New Zealand Competition Law, Kluwer (2003) at 328-332.

[12] *Application by Chime Communications Pty Ltd (No 2)* [2009] ACompT 2 at paragraph 48.

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