Australian Competition and Consumer Commission

Merger Assessment Guidelines

Email: MergerReformInfo@accc.gov.au

12 April 2025

Submission to the ACCC's Draft Merger Assessment Guidelines

Dear Sir/Ma'am,

Thank you for the opportunity to submit to the ACCC's Draft Merger Assessment Guidelines. Please find our submission enclosed. In it, we comment on three areas related to the guideline: merger-induced kill zones, mergers involving multi-sided platforms, and merger policy and innovations.

The Digital Lab at Monash Business School is a multidisciplinary, inter-faculty research hub that collaborates with government and industry partners to advance cutting-edge research on competition and regulation, with a particular focus on the digital sector.

We are happy to address any follow-up questions you might have. Please note that the views expressed in this submission are solely ours and should not be attributed to Monash University.[1]

Kind regards,

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[1] I would like to thank Stephen King and Chris Teh for their insightful comments and valuable discussions on an earlier draft of this submission.

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Summary

This submission offers comments and suggestions in three important areas of merger control: acquisition-induced kill zones, mergers involving multi-sided platforms, and the relationship between merger policy and innovation. We explain why the draft guideline would benefit from including or expanding its discussion in these areas, drawing on relevant insights from the recent economics literature.

1. Merger-induced kill zones

To protect profits from potential competition, a dominant firm may acquire or merge with a company in an adjacent market. Such acquisitions eliminate not only the immediate competitive threat posed by the target firm but also deter future entrants into that adjacent market. For instance, an independent instant messaging app that amasses a large user base could expand its offering over time to become a social network (e.g., WhatsApp in India, or WeChat in China), posing a significant threat to an existing dominant social network. While the draft guidelines highlight how mergers can prevent potential competition in this kind, they overlook how these acquisitions can also create *kill zones*—deterring future entry into the adjacent market and further insulating the dominant firm from future threats coming from the adjacent market.[2]

Entrenchment: Entrenching a firm's market power can substantially lessen, or be likely to substantially lessen, competition. Firms with market power may use mergers or acquisitions to entrench their dominance—either by neutralising immediate threats to their core business or by preemptively addressing future threats that could arise from adjacent markets.

In the case of adjacent markets, these threats can take two forms: a medium-run threat posed by an existing firm already operating in the adjacent market, or a long-run threat from a potential entrant into the adjacent market. We call the former medium-run because it is not a current entrant, but a potential threat that may arise in the future from the adjacent market. A dominant firm can eliminate a medium-run threat by acquiring the existing adjacent-market firm outright. That is, even in the absence of immediate rivalry, acquiring a firm in an adjacent market can help entrench the dominant firm's power in the core market.

Once a firm in an adjacent market is acquired by a dominant player, it may be perceived by potential entrants as a far more formidable competitor than it would be if operating independently. This perception stems not only from the parent company's scale, financial strength, and market access, but also from the merged firm's strategic incentive to aggressively deter new entrants—particularly to prevent future competition that could threaten its core market. As a result, the expected profitability of entering the adjacent market declines, discouraging entry and weakening the long-run competitive pressure that might otherwise spill over into the dominant firm's core market.

In this way, the acquisition not only removes a medium-run competitive threat from the adjacent market but also suppresses the emergence of long-run threats—effectively entrenching the dominant firm's position both directly and indirectly.

Additional theories of conglomerate mergers: The scenario described above illustrates another theory of harm for conglomerate mergers—those that do not involve direct substitutes or complements. Unlike traditional theories that focus on bundling or leveraging market power,[3] this

[2] See more details about acquisition-induced kill zones in Teh, Christopher, Dyuti Banerjee, and Chengsi Wang. *Acquisition-induced kill zone*. 2024. https://www.dropbox.com/scl/fi/k2uuzhk2z7buyrh4e0mfa/acquisition-induced-kill-zone_MS.pdf?rlkey=a9ufg1w385s5fjmv9dbiq9g00&dl=0

[3] Unlike the predictions of leverage theories, the theory of harm we propose does not rely on the foreclosure of a more efficient entrant in the adjacent market. In fact, the acquired firm may offer a higher-quality product than a potential

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framework emphasizes two key elements:
(i) A strong player in the adjacent market could become a direct or indirect competitor to the dominant firm under discussion in the future (e.g., generative AI could substitute search engines, or instant messaging apps could compete for advertising revenue with a social network);
(ii) The acquisition enhances the perceived strength of the acquired firm in the adjacent market, thereby deterring entry into the adjacent market.

Serial acquisitions: This theory also fits naturally into discussions of serial acquisitions, where a dominant firm acquires multiple small companies over a short time period. With numerous adjacent markets surrounding a core market, acquiring one firm from each adjacent market can be an effective strategy to systematically eliminate potential competition and deter future entry across all adjacent markets.

2. Mergers involving multisided platforms

We agree with the ACCC's approach to market definition for multisided platforms, which treats each side as a distinct market while acknowledging the interdependencies and feedback effects between them. We also support the view that market definition remains a valuable tool for assessing the competitive effects of mergers, but it should not be the sole determining factor. It is crucial to focus more directly on the competitive constraints that a particular conduct imposes or removes, and the resulting impact on competition.

Bundling platform goods: Recent economic theory has extended the analysis of bundling to include platform goods that exhibit cross-group network effects. Consider a monopoly firm in market A (firm 1) that also supplies a platform good in market B. In market B, firm 1 competes with firm 2, which offers a higher-quality platform good. Market B is multi-sided—if a firm sells its good in this market, it earns not only revenue from consumers but also additional profit from the other side of the platform, such as advertisers.[4]

A key assumption underpinning the profitability of bundling in this context is the *non-negative price restriction* (NNPR), which prevents firms from setting negative prices to consumers. This assumption is grounded in the concern that negative prices would create opportunities for arbitrage. When firm 1 sells its products in markets A and B separately, the NNPR prevents firms from discounting prices to offset the additional profit earned from the other side of the platform (e.g., advertisers). However, by bundling its products from both markets and offering a single price, firm 1 can effectively discount its product in market A, thereby gaining a competitive advantage. This bundling strategy becomes profitable if the additional profit from the other side is sufficiently large relative to the quality gap between the competing products in market B.

This bundling strategy clearly leads to efficiency losses, as consumers are steered toward purchasing the inferior good in market B. Nevertheless, in the short run, bundling can benefit consumers, as the bundle price more than offsets the quality gap in market B and is significantly lower than the combined price of the goods when sold separately.[5]

Economic literature on platform mergers: Most mergers involving platforms are vertical or conglomerate in nature. Mergers between substitutive platforms are less common and tend to occur primarily in the media sector (e.g., newspapers, radio). The economic theory on platform

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entrant. The concern, instead, lies in the loss of opportunity—whether for the target firm or for future entrants—to challenge the dominant firm's core business from adjacent markets.

[4] Given our advocacy for the multi-market definition, we could say Market B consists of two sub-markets, consumer-faced B1 and advertiser-faced B2.

[5] More detailed theory of harm and the discussion of the case of bundling complementary goods can be found in Choi, Jay Pil, and Doh-Shin Jeon. "A leverage theory of tying in two-sided markets with nonnegative price constraints." *American Economic Journal: Microeconomics* 13, no. 1 (2021): 283-337.

mergers remains limited, largely due to tractability constraints. Existing models often rely on strong assumptions—such as duopoly platforms merging into a monopoly, full market coverage both before and after the merger, platform symmetry, and Cournot competition—which can restrict their relevance to real-world scenarios.[6]

Given the nature of actual merger cases and the current state of the literature, we focus on mergers between platforms that are exclusively financed by advertising. This category includes many media platforms, as well as search engines and social networks. Since consumers do not pay for platform services in such settings, the only price effects of mergers arise on the advertising side. A common assumption in this literature is that while advertisers are interested in capturing consumers' attention, consumers care only about the media content and view advertisements as a nuisance. Another typical assumption is that advertisers multihome across all platforms.

Viewers' homing decisions play a crucial role in shaping merger outcomes. When most viewers singlehome on only one platform, platforms must compete aggressively for their attention, leading to lower ad volumes and higher ad prices, as viewers tend to dislike advertisements. A merger in this setting reduces competition for viewers, resulting in higher ad volumes and lower ad prices. The substantial lessening of competition is a loss of quality (due to increased nuisance) on the consumer side even though prices reduce in the related advertising market. In contrast, when most viewers multihome, there is little competition for viewers even before the merger. In this case, the merger has the standard effect of increasing ad prices and reducing ad volumes. Consistent with this prediction, most empirical studies of media platform mergers report a rise in ad prices following such mergers.

3. Merger policy and innovations

Arguments related to investments and innovation have become increasingly central in merger investigations and cases. Innovation is a particularly critical issue in merger cases involving certain sectors such as pharmaceutical and information technology, while investments can play a key role in shaping arguments in a broader range of sectors such as supermarkets. The economics literature on the relationship between competition, investment, and innovation is vast.[7] In this context, we focus on scenarios where large firms acquire small start-ups and on the design of dynamic merger policies that explicitly consider the long-term impact of acquisitions on innovation incentives. The draft assessment guidelines only briefly touches upon innovation within the discussion of dynamic and potential competition. We believe that the merger assessment guidelines should be expanded to more thoroughly address innovation concerns in the design of merger control.[8]

Pre-acquisition innovations: The well-known research on killer acquisitions (and the related reverse killer acquisition scenario mentioned in Section 5.6. in the draft guideline) focuses on post-acquisition innovation, specifically whether R&D incentives weaken once the negotiation between the acquirer and target has concluded. This is a crucial issue and has been extensively discussed by Massimo Motta and Martin Peitz in their review article.[9] We instead would like to focus on a complementary concern: innovation activities that occur prior to merger negotiations. These include investment and innovation-direction decisions made by small startups before

[6] A more detailed discussion of the literature on platform mergers can be found in Correia-da-Silva, Joao, Bruno Jullien, Yassine Lefouili, and Joana Pinho. "Horizontal mergers between multisided platforms: Insights from Cournot competition." *Journal of Economics & Management Strategy* 28, no. 1 (2019): 109-124.
[7] A general review of the studies on the impact of mergers on innovations can be found in Lefouili, Yassine, and Leonardo Madio. "Mergers and Investments: Where Do We Stand?" (2025). https://publications.ut-capitole.fr/id/eprint/50415/1/wp_tse_1617.pdf
[8] The discussion is based on Teh, Christopher, and Chengsi Wang. "Startup acquisitions and innovation" (2025).
[9] Motta, Massimo, and Martin Peitz. "Big tech mergers." *Information Economics and Policy* 54 (2021): 100868.

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commercializing their products or receiving acquisition offers from larger firms—an increasingly important driver of technological progress.

It is worth noticing that acquisition is the primary exit strategy for most startups. The prospect of being acquired at a good price provides strong incentives for startups to invest in costly R&D. In particular, when a startup innovates in a way that poses a competitive threat, the incumbent is willing to offer a high acquisition price to preempt future competition. This dynamic further encourages innovation by startups.

Explicitly acknowledging these positive effects of *entry-for-buyout* incentives in the merger assessment guidelines would offer greater certainty and reassurance to startups, supporting their willingness to undertake high-risk, high-reward R&D activities.

Dynamic merger policy: In principle, the merger control should adopt a forward-looking perspective that accounts for startups' investment incentives and the direction of innovation. In contrast, court decisions on merger cases often reflect a static approach—evaluating whether the merger should be approved based solely on its immediate competitive effects, i.e., whether the merger would substantially or is likely to substantially lessen competition compared to the counterfactual of rejection.

Merger control has the potential to be more dynamic by considering how policy shapes startups' innovation choices. For example, a startup may face a strategic decision between innovating in search engine technology or in generative AI. In the absence of acquisition opportunities—perhaps due to the presence of a dominant incumbent in search or a presumption that any acquisition would harm consumers and be blocked—the startup may choose to innovate in generative AI, where independent growth seems more viable. However, this comparison overlooks the broader goal of promoting dynamic competition. It is possible that consumers would be better off if the startup innovated in search and was later acquired by the incumbent, rather than pursuing generative AI and remaining independent. A more nuanced or flexible approach to merger control could influence the startup's direction by increasing the perceived feasibility and rewards of entry into more socially valuable, but highly concentrated, sectors. In this way, the design of merger policy can play a proactive role in steering innovation toward areas where it delivers greater long-term benefits.

The key to developing a dynamic merger policy lies in striking the right balance: incentivizing start-ups to pursue socially desirable innovation paths before a merger, while minimizing the loss of competition after the merger. In this way, dynamic merger policy can play a crucial role not only in protecting competition but also in shaping the broader innovation landscape.[10]

We understand that the ACCC is bound by competition law and cannot approve mergers that are likely to substantially lessen competition, even if there are compelling long-term benefits from innovation. However, we offer the following suggestions that may help develop a more forward-looking, dynamic approach to merger control while remaining compliant with the law:

- The ACCC could consider lowering the threshold for merger clearance in technology-related industries by adjusting the evidentiary requirements during the screening process—rather than approving mergers that are found to be anticompetitive. For example, the ACCC might accept a lower standard of evidence when assessing claims of innovation-related efficiencies. If the available evidence ultimately shows that the proposed merger is likely to substantially lessen competition, the ACCC should, in line with the law, move to block it. However, by r

[10] A more lenient merger policy does not mean approving an anti-competitive merger with probability one. It only means that all merger under review will be cleared by a higher probability (e.g., requiring less evidence to show efficiency gains from the merger) such that small firms, which are potentially acquisition target, expect viable exit for innovation and have enough incentive to choose the socially desired innovation direction. See more details on dynamic merger policy in Gilbert, Richard J., and Michael L. Katz. "Dynamic merger policy and pre-merger product choice by an entrant." *International Journal of Industrial Organization* 81 (2022): 102812.

educing the evidentiary burden at the screening stage, the process of obtaining clearance b ecomes more accessible, which could in turn create stronger incentives for firms to pursue i nnovation and entry.

- The ACCC could consider explicitly incorporating innovation benefits into the application of the net public benefit test. This would provide a possible pathway for approving a merger that might otherwise be blocked under the substantial-lessening-of-competition standard. Specifically, the ACCC could argue that permitting a particular merger would generate broader dynamic benefits—such as enhancing incentives for other firms to enter and innovate in response. This is a policy tool that can be flagged to the Competition Tribunal and market participants.

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