

# Draft Merger Assessment Guidelines

## Comments by RBB Economics

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### 1 Summary

RBB Economics welcomes the opportunity to comment on the Draft Merger Assessment Guidelines (“the draft guidelines”) for the new mandatory merger control regime, released by the Australian Competition and Consumer Commission (ACCC) on 20 March 2025.

This short submission focuses on three economic aspects of those draft guidelines:

- First, the draft guidelines do not refer to the well-established “ability, incentive, effect” framework typically used to assess conglomerate effects concerns in Australia and overseas. It is unclear if this is intentional or not. If it is, it would represent a very significant change to the assessment of conglomerate mergers. To ensure that the appropriate level of rigour is applied to such assessments under the new regime, the ACCC should explicitly refer to this framework in its guidelines and continue applying it in its assessments of conglomerate mergers.
- Second, the draft guidelines do not provide sufficient guidance to merging parties and their advisors on the clarification of the SLC test and the meaning of the term “entrenching” market power, particularly with regard to conglomerate mergers. This lack of detail is surprising given that the legislation has changed the competition test that will be applied to mergers to explicitly capture those mergers that “entrench” market power.
- Third, the relegation of a substantive discussion of market definition, including the valuable role played by the hypothetical monopolist test (HMT), to an Appendix in the draft guidelines is a concerning

development. While market definition should form part of the broader competitive assessment and be consistent with the analysis of constraints in the competitive effects assessment, it remains an important first step that helps to inform that competitive assessment. It should not be an afterthought that is simply used to calculate market shares after a view on the main constraints has already been reached. To ensure that an appropriate level of rigour is applied when assessing available evidence on the competitive constraints faced by the merger parties, the guidelines should reaffirm the important role of market definition, and the HMT specifically, in merger assessments.

## 2 The appropriate analytical framework for assessing conglomerate effects

When discussing the assessment of non-horizontal mergers (including both vertical and conglomerate mergers), the current ACCC merger guidelines make it clear that the ACCC will adopt the well-established “ability, incentive and effect” framework when assessing whether a merger is capable of foreclosing rivals.<sup>1</sup> That is, it assesses whether:

- the merged firm would have sufficient market power in the relevant market – including, in the case of conglomerate mergers, whether the products are considered by customers to be especially important or a “must have” because of factors such as superior functionality – to be able to foreclose rivals (ability);
- whether it is profitable for the merged firm to engage in a foreclosure strategy (incentive); and
- whether the foreclosure of rivals will have a detrimental effect on competition (effect).

This approach is consistent with the merger assessment guidelines in other jurisdictions such as Europe and the UK and reflects the well-established application of this economic framework to the assessment of non-horizontal mergers.<sup>2</sup> This framework ensures appropriate rigour in the assessment of non-horizontal mergers.

The draft guidelines retain the reference to the “ability, incentive and effect” framework in the context of vertical mergers, but it is notably absent from the discussion of the assessment of conglomerate mergers.<sup>3</sup> This is a potentially very significant change to the framework for that assessment and it is unclear if this absence is intentional.

While the discussion of conglomerate effects does include reference to some factors that are relevant under the ability, incentive and effect framework, the draft guidelines only note that the ACCC “*may consider*” these factors.<sup>4</sup> On its face, this provides the ACCC with considerable discretion and suggests that the ACCC may seek to depart from the well-established ability, incentive and effect framework in its approach to assessing whether a conglomerate merger substantially lessens competition. This could potentially lead to assessments that lack appropriate rigour, as well as significantly lower the threshold for identifying concerns.

The revised guidelines should commit to adopting the ability, incentive and effect framework in the assessment of conglomerate mergers, and avoid departing significantly from the merger assessment guidelines in other jurisdictions.

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<sup>1</sup> ACCC Merger Guidelines, November 2008, paragraphs 5.18 to 5.43.

<sup>2</sup> See, for example, European Commission Guidelines on the assessment of non-horizontal mergers under the Council Regulation on the control of concentrations between undertakings, 2008, paragraphs 94 to 118; and CMA Merger Assessment Guidelines, 18 March 2021, paragraphs 7.30 to 7.37.

<sup>3</sup> ACCC Draft Merger Assessment Guidelines, paragraph 4.7.

<sup>4</sup> ACCC Draft Merger Assessment Guidelines, paragraphs 4.27 to 4.31.

### 3 The application of the new SLC test to conglomerate mergers

One of the changes brought about by the Treasury Laws Amendment (Mergers and Acquisition Reform) Bill 2024 was to explicitly set out in the legislation that an acquisition can give rise to an SLC by “*creating, strengthening or entrenching a substantial degree of power in the market*”.<sup>5</sup>

One would expect that a change to the wording of the competition test that applies to mergers would be accompanied by a detailed discussion in the draft guidelines. However, that is not the case. The draft guidelines make a general statement that “[t]he more market power one party already has, the more likely it is that a merger will entrench that market power and be a ‘substantial’ lessening of competition”.<sup>6</sup> In terms of the specific circumstances in which this might arise, the draft guidelines only refer to “entrench” in the context of two types of merger concerns.

- First, in the context of “*mergers that eliminate potential competition*” the guidelines state that “*an acquirer may view the target as a potential competitor, and the acquirer may acquire the target as a strategy to capture and control the competitive threat before the target develops into a true rival (this is sometimes referred to as a ‘killer acquisition’). When an acquirer undertakes multiple acquisitions of nascent rivals as part of a concerted strategy over time, the effect may be to strengthen or entrench the acquirer’s market power, making subsequent entry more difficult*” [emphasis added].<sup>7</sup>
- Second, in the context of “*serial acquisitions*” the guidelines state that these “*can enable firms to attain a position of substantial power in a market and erode competition. They can also be used by firms that already have a position of market power to extend or entrench that power*” [emphasis added].<sup>8</sup>

This suggests that the application of the new (interpretation of the) SLC test might limit “entrenchment” concerns to mergers involving potential competitors and those involving so-called serial acquisition.

There is no reference in the draft guidelines to how the term “entrench” market power would apply in the context of a conglomerate merger. On its face, this could suggest that the ACCC does not consider the “entrenching” of substantial market power to be a concern within the context of conglomerate mergers, and that the new SLC test does not warrant a change to the guidance on the ACCC’s assessment of conglomerate mergers. If that is the case, it should be made clear in the assessment guidelines.

RBB Economics previously made a submission in response to the release by Treasury of the exposure draft of the Treasury Laws Amendment Bill 2024 warning about the risks of introducing concerns around “entrenching” market power in the context of conglomerate mergers.<sup>9</sup> That submission included a discussion of the phrase “*entrenching a substantial degree of power in the market*” and noted the following.

- While the terms “creating” and “strengthening” market power can be traced back to the old dominance test and may have been included in the proposed amendment to remind decision-makers that the SLC test is clearly capable of capturing mergers that create a clear dominant position, the term “entrenching” is less clear.<sup>10</sup>
- Recent references to “*entrench*” in the ACCC’s Seventh Interim Report in the Digital Platform Services Inquiry; the European Commission’s (“EC’s”) prohibition of the proposed acquisition of Flugo Group

<sup>5</sup> Competition and Consumer Act 2010 (Cth), s 51ABZH(4); Explanatory Memorandum to Treasury Laws Amendment (Mergers and Acquisitions Reform) Bill 2024, paragraph 4.23 and 4.25.

<sup>6</sup> ACCC Draft Merger Assessment Guidelines, paragraph 1.8.

<sup>7</sup> ACCC Draft Merger Assessment Guidelines, paragraph 5.7.

<sup>8</sup> ACCC Draft Merger Assessment Guidelines, paragraph 5.38.

<sup>9</sup> See RBB Economics, Proposed changes to the SLC test, Economic considerations, 16 August 2024 [Available at: <https://treasury.gov.au/sites/default/files/2024-10/c2024-554547-rbb-economics.pdf>] (The RBB Submission).

<sup>10</sup> The RBB Submission, pages 2 and 4.



Holdings AB ('eTraveli') by Booking Holdings ('Booking'); and the revised US Merger Guidelines suggest the phrase may be targeted at conglomerate mergers.<sup>11</sup> These suggest that “entrenchment” concerns, including the ecosystem theory of harm, may arise when a firm possesses substantial market power in market A (e.g., meat pies) and seeks to acquire a firm that supplies complementary goods or services in market B (e.g. tomato sauce). The conventional concern would be that the merged entity may seek to leverage its substantial market power in meat pies to foreclose rival suppliers of tomato sauce, leading to an SLC in the market for tomato sauce.<sup>12</sup> However, with entrenchment concerns (such as the ecosystem theory of harm), the concern could be that, as a result of acquiring the supplier of tomato sauce, the barriers to entry or expansion in the supply of meat pies will increase, “entrenching” the merged entity’s market power in the supply of meat pies.<sup>13</sup>

In our view, whether these “entrenchment” theories of harm could already have been captured by the existing analytical framework used by the ACCC to assess conglomerate effects was an important question that should have been answered before changing the definition of the SLC test.<sup>14</sup> But the legislation has now changed, and the question is how this new legislation will be applied by the ACCC. The absence of any discussion around the application of the new term in the context of conglomerate effects potentially reflects ACCC agreement with Treasury’s position set out in the Explanatory Memorandum, that the change “*should be seen as an elucidation of the ways in which a substantial lessening of competition can arise rather than a change to the meaning of a substantial lessening of competition*”.<sup>15</sup> The suggestion is that this is simply a clarification and will not have a material effect on the assessment of mergers under the new regime, with the change only seeking to clarify that serial acquisitions and mergers involving potential competitors can “entrench” a substantial degree of market power.

If this is the case, the revised guidelines should make that clear. If, on the other hand, the change in the test might alter the way that conglomerate mergers are assessed by the ACCC, these changes should be set out in the revised guidelines.<sup>16</sup>

## 4 The role of market definition

One of the most striking proposed changes to the merger guidelines is the relegation of the substantive discussion of market definition, including discussion of one of the most important tools introduced to competition analyses over the past 50 years – the Hypothetical Monopolist Test (HMT) – to an Appendix in the draft guidelines.

We agree that market definition is not an end in itself, and that the outcome of the competitive assessment of a merger would not turn on the definition of the market alone. Indeed, a merger may be found not to substantially lessen competition irrespective of which of several plausible markets is adopted. Similarly, and as noted in the draft guidelines, when there are several plausible markets, a merger may lead to a substantial lessening of competition irrespective of which market is ultimately adopted.<sup>17</sup> The implication is that it will not always be necessary to reach a view on the most appropriate boundaries of the market when undertaking a competitive assessment of a merger.

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<sup>11</sup> Conglomerate mergers are mergers that combine firms that supply complementary goods or services to partially overlapping customer bases. Conglomerate mergers tend to be benign or pro-competitive other than where they harm consumers through anti-competitive foreclosure.

<sup>12</sup> Indeed, this is the concern that the ACCC refers to in paragraph 4.27 of its Draft Merger Assessment Guidelines.

<sup>13</sup> The RBB Submission, pages 7 and 8.

<sup>14</sup> The RBB Submission, page 8.

<sup>15</sup> ACCC Draft Merger Assessment Guidelines, paragraph 1.27.

<sup>16</sup> Irrespective of the ACCC’s position on the impact of the change to the wording of the SLC test on the assessment of conglomerate mergers, the revised guidelines should adopt the well-established ability, incentive and effect framework in the assessment of conglomerate mergers (as discussed in Section 2 above).

<sup>17</sup> ACCC Draft Merger Assessment Guidelines, paragraph 1.20.

However, this does not diminish the importance of market definition, and in particular the HMT, as the appropriate analytical tool to identify the main, or effective, competitive constraints acting on the merger parties. It is a valuable first step that brings important rigour to the competitive assessment of mergers.

There are suggestions in the draft guidelines that the ACCC may seek to depart from the framework of the HMT when assessing the competitive constraints acting on the merger parties, and that “*formal market definition*” employing the HMT can only “*sometimes be helpful*” in so far as it allows for the preparation of market shares and measures of concentration.

- “*Depending on the facts of the merger under review, the identification of the relevant market or markets may be relatively straightforward. The ACCC may simply define the market as comprising the most important constraints on the merger parties that have been identified in our competition assessment. In other cases, the ACCC may undertake a market definition exercise to identify the area or areas of competition, including potential competition, between firms, and to assess the degree of substitutability between different products and geographic areas*”.<sup>18</sup>
- “*The ACCC’s experience is that in many mergers, the evidence and information gathered as part of the competition assessment, which includes an assessment of the constraints on the merger parties, captures the competitive dynamics more fully than formal market definition*”.<sup>19</sup>
- “*In some cases, the ACCC may take a simple approach to defining the market – for example, by describing the market as comprising the most important constraints on the merger parties that have been identified in the ACCC’s competition assessment*”.<sup>20</sup>
- “*formal market definition, in the sense described below, can sometimes be helpful in developing certain types of evidence that may be relevant to the competition assessment. For example, the ACCC may define the market as a basis to calculate market shares or for developing other measures of concentration, which may be helpful in some cases (especially where products are undifferentiated)*”.<sup>21</sup>

Consideration of the competitive constraints acting on the merger parties is central to the assessment of mergers. The HMT provides the appropriate framework through which to assess available evidence on these constraints. Certain evidence related to constraints may be considered as part of the competitive assessment, such as an analysis of bidding data (or data on customer switching more generally), as well as the competitors or constraints that are referenced in the merger parties’ internal documents. This evidence may be particularly relevant in assessing closeness of competition between the merger parties, or identifying the *closest* competitors. However, there is a very real risk that if such evidence is considered in isolation of the HMT framework and its principles that important and *effective* competitive constraints are missed. For instance, proper regard may not be had for the response of actual or potential competitors to an attempt by the merged entity to increase prices, or the possibility that internal documents reflect only narrow views on competitors or constraints. To ensure that the appropriate level of rigour is applied in the competitive assessment it is important that the identification of the main competitive constraints on the merger parties is consistent with the HMT framework and its principles.

Suggesting, as is done in the draft guidelines, that market definition can be bypassed and the HMT ignored is misguided. While market definition should form part of a broader competitive assessment and be consistent with the analysis of constraints in the competitive effects assessment, it should be a first step that helps to inform that competitive assessment. It should not be an afterthought that is simply used to calculate market shares after a view on the main constraints has already been reached.

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<sup>18</sup> ACCC Draft Merger Assessment Guidelines, paragraph 1.19.

<sup>19</sup> ACCC Draft Merger Assessment Guidelines, Appendix 1, paragraph 2.

<sup>20</sup> ACCC Draft Merger Assessment Guidelines, Appendix 1, paragraph 3.

<sup>21</sup> ACCC Draft Merger Assessment Guidelines, Appendix 1, paragraph 4.

In our view, the form or style of the guidelines (and where market definition and its role are discussed) is less important than the substance of what is said. However, the relegation of the substantive discussion of market definition to an Appendix, together with the above-mentioned issue, suggests a diminished role for market definition, limited to the calculation of market shares and measures of concentration.

The guidelines should reaffirm the fundamental role of market definition, and the HMT, in identifying the main, or effective, competitive constraints acting on the merger parties.