Consumers put at end of the queue

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Placing a greater weight on consumer welfare forces merging companies to be more imaginative and to think about their customers' interests.
Photo: *Fiona-Lee Quimby*

Trade practices legislation will allow consumers to be hurt by mergers so long as others, such as shareholders, benefit, says Joshua Gans.

HIGH on the list of contentious topics in the Dawson reforms to trade practices legislation before Parliament is a new set of rules governing mergers.

The rules will allow merging parties to bypass the Australian Competition and Consumer Commission and go directly to the Australian Competition Tribunal for approval.

Business has applauded this change because the tribunal has been more willing to place weight on profits as a benefit from mergers to weigh against any potential consumer harm flowing from less competition.

The ACCC has long argued that when a merger is driven by efficiency benefits, some of these benefits should "pass through" to consumers in order to be approved. In its recent decision over the Qantas-Air NZ alliance, the Australian Competition Tribunal reaffirmed its commitment to total welfare — the sum of consumer and producer net benefits — as the goal of merger policy.

Strictly speaking, adherence to a total welfare standard gives no credence to "pass through". You only have to assure yourself there is a benefit for someone.

The idea that shareholders deserve some weight in merger decisions has long been advocated by economists. But for others there is nervousness. A total welfare standard is saying: "The merger is going to harm a significant group of consumers, but that is OK because the additional profits going to producers will outweigh this." This is the same as saying: "I am going to steal your watch, but that is OK because I can demonstrate that I need it more than you do."

Parties can choose to merge and consumers must shrug their shoulders and be satisfied because others are benefiting.

That's the moral concern, but also think about the economics. The merger system has a fundamental bias: companies can propose a merger but consumers cannot propose a divestiture. Suppose a company became dominant in an industry. Why can't consumers argue that it should be broken up because the reduction in its profits would be outweighed by consumer benefit from greater competition? They can't. As the case of Telstra shows, it is even hard to argue this for publicly owned companies. Too many mergers will be approved under a total welfare standard.

The only way to proceed is to place a greater weight on consumer welfare and on "pass through" of benefits. Anti-competitive concerns about mergers can be mitigated , including partial divestitures, access pricing regimes or price undertakings that ensure benefits are passed through.

Placing a greater weight on consumer welfare would force merging companies to be more imaginative and think about their customers' interests. They have a greater incentive to propose mergers that in fact maximise total welfare. As is often the case with policy, to achieve one objective (maximising total welfare), policymakers need to legislate for another (in this case, weighing consumers more heavily). And if the ACCC represents the voice of consumers in the new system, then that is all to the better.

I wonder if the Qantas-Air NZ alliance did not occur because of a lack of imagination. The concern in NZ was that the number of seats flying across the Tasman would be lower if the alliance went ahead. Qantas and Air NZ claimed otherwise — they were just reallocating seats. One wonders why Qantas and Air NZ did not simply propose to maintain the number of seats. It

would be easy to monitor and also allay anti-competitive concerns. The system should encourage imaginative proposals along these lines. More mergers would be approved than in the current environment.

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