COMMONWEALTH OF AUSTRALIA

COMPETITION AND CONSUMER ACT 2010

IN THE AUSTRALIAN COMPETITION TRIBUNAL

ACT 1 of 2017

RE: Application by Tabcorp Holdings Limited under section 95AU of the *Competition and Consumer Act 2010* for an authorisation under subsection 95AT(1) to acquire shares in the capital of a body corporate or to acquire assets of another person

Applicant: Tabcorp Holdings Limited

ACCC'S REPORT

Contents

1. Executive summary

1.1. Tabcorp Holdings Limited (**Tabcorp**) proposes to acquire all of the shares in Tatts Group (**Tatts**) (the **proposed acquisition**).

1.2. The proposed acquisition will combine two gambling companies with significant operations in wagering, racing media, gaming services, lotteries and Keno, creating one of the world's largest gambling businesses. While there are industry participants that are supportive of the proposal, many have raised significant concerns.

1.3. Tabcorp and Tatts are both very significant providers of totalisator[1] and other wagering operations. Tabcorp also owns the racing media business, Sky Racing (**Sky**). Sky is the dominant broadcaster of racing vision through its holding of exclusive and fully bundled rights (digital, free to air, and subscription television) for the majority of Australian racing vision content.

1.4. Tabcorp and Tatts are also significant suppliers of a range of gaming related services to venues, such as pubs, clubs and hotels with electronic gaming machines (**EGMs**, also known as 'pokies').

1.5. In addition, Tatts is the largest operator of public lotteries in Australia and Tabcorp distributes the Keno product in several states.

1.6. The proposed acquisition raises many complex issues. It will remove the direct competition between Tabcorp and Tatts in several markets and gives rise to vertical integration concerns. The interactions between the industry participants are complicated, particularly the commercial relationships between the wagering providers, Sky and the principal racing authorities (**PRAs**) and racing clubs.

1.7. Tabcorp applied on 13 March 2017 to the Australian Competition Tribunal (**Tribunal**) for authorisation for the proposed acquisition under section 95AT of the *Competition and Consumer Act 2010 (Cth)* (the **Act**). This report has been prepared by the Australian Competition and Consumer Commission (**ACCC**) at the request of the Tribunal to assist the Tribunal's consideration of the application.

1.8. During the period leading up to Tabcorp's application, the ACCC was conducting a public informal merger review of the proposed acquisition, to determine whether the ACCC considered the proposed acquisition was likely to substantially lessen competition and therefore raise concerns under section 50 of the Act. The ACCC published a Statement of Issues (**SoI**) on 9 March 2017, which expressed the ACCC's preliminary view that there were several issues that may raise competition concerns.

1.9. Shortly after publication of the SoI and prior to the ACCC completing its merger review, Tabcorp applied to the Tribunal for merger authorisation. The legal test the Tribunal applies is different to the test in section 50. Under section 95AZH, the Tribunal must not grant authorisation unless it is satisfied in all the circumstances that the proposed acquisition would result, or be likely to result, in such a benefit to the public that the acquisition should be allowed to occur. There are public detriments that are likely to result from the proposed acquisition, and the Tribunal's task is to weigh those against the benefits that are likely to result from the proposed acquisition.

[1] In totalisator or pari-mutuel wagering, an operator establishes 'pools' for individual racing events. All bets accepted by the operator on the relevant event are consolidated into the pool created for that event, and the operator deducts from the pool a predetermined fixed commission percentage (take-out rate) which is regulated through state and territory government legislation. The remainder of the pool (referred to as the 'dividend pool') is divided by the number of units bet on the successful outcome and is available for distribution to the winning customers.

Wagering detriments

1.10. Tabcorp and Tatts both compete in the provision of wagering services to consumers (or 'punters').

1.11. Tabcorp and Tatts have a national presence supplying wagering products online and over the telephone. Corporate bookmakers (for example Sportsbet, CrownBet, William Hill, Ladbrokes and Bet365) compete with Tabcorp and Tatts in online/telephone (but only in the supply of fixed odds and tote-derivative[2] products).

1.12. Tabcorp and Tatts also both have stand-alone retail wagering agencies and wagering facilities located in pubs, clubs and hotels (together referred to as **retail wagering outlets**). Tabcorp has the exclusive licence to operate a totalisator and retail wagering outlet network in New South Wales (**NSW**), Victoria and the Australian Capital Territory (**ACT**) (the **Tabcorp jurisdictions**). Tatts has the exclusive licence to operate a totalisator and the retail wagering outlet network in Queensland, South Australia, Tasmania and the Northern Territory (the **Tatts jurisdictions**).

1.13. While the retail wagering outlets of Tabcorp and Tatts do not compete directly as they hold exclusive licences in different states/territories, combining Tabcorp and Tatts (the **merged entity**) appears likely to result in public detriments by:

- Lessening competition in wagering (particularly online/telephone wagering) due to the removal of direct competition between Tabcorp and Tatts
- Reducing the number of credible bidders from two to one for the exclusive retail licences
- Reducing the number of potential suppliers of pooling services from two to one
- Lessening competition in wagering due to the merged entity being able to use Sky to stop corporate bookmakers establishing arrangements with retail venues in Tatts jurisdictions.

1.14. Tabcorp and Tatts are both very significant wagering providers, with a combined share of national wagering revenue of approximately [**Confidential to Tabcorp and Tatts**] [redacted].[3] Tabcorp and Tatts are also both significant providers of online/telephone wagering, where they compete with each other and corporate bookmakers.

1.15. The proposed acquisition removes the direct competition between Tabcorp and Tatts. While the corporate bookmakers have grown their share of wagering turnover and revenue in recent years, Tabcorp and Tatts appear to have actually increased their average prices (the take-out-rate) for some types of services (e.g. totalisator services). Indeed, in recent years, Tabcorp has significantly grown its level of wagering revenue (its level of wagering revenue increased by approximately [**Confidential to Tabcorp and Tatts**] [redacted] during FY15).[4] Furthermore, the corporate bookmakers face barriers to expansion, in large part due to Sky's dominance in obtaining racing media rights (discussed further below). In addition, this report identifies other regulatory changes that appear likely to favour the merged entity over corporate bookmakers in coming years.

1.16. In competitive bidding processes for exclusive licences, Tabcorp and Tatts are likely to be each other's closest competitors and the two most credible bidders. There is

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[2] Tote derivative products are a wagering product whereby the payout odds replicate those available on the totalisators. Customers are able to bet on derivative products such as 'top tote', where they receive the best odds available across the three totalisators. Corporate bookmakers, in some cases, also offer a bonus on top of the standard dividend.

[3] Derived from Statement of Douglas Freeman, Executive General Manager - Commercial Development of Tabcorp, dated 8 March 2017 (**Freeman**) at [279], Figure 44.

[4] Freeman at Figure 44.

significant uncertainty that other bidders would be in a position to credibly bid. The merged entity's control of key inputs such as racing vision is likely to be a factor in deterring rival bidders. The proposed acquisition may impact future government licensing processes including the potential privatisation of the Western Australian TAB (**WA TAB**) and the next Victorian licence rights renewal in 2024.

1.17. Tabcorp and Tatts are also potential competitors in the provision of pooling services to the only other domestic totalisator operator: Racing and Wagering Western Australia (**RWWA**), the operator of the WA TAB. Tabcorp has made commitments to RWWA via a Commitment to Long Term Pooling Deed (**Deed**) to address concerns that Tabcorp may cease to offer such services. The Deed does not necessarily provide certainty about the commencement and terms of any future pooling agreements between RWWA, or any future acquirer of the WA TAB if privatised, and Tabcorp. It may be in the merged entity's interest to circumvent the long-term behavioural commitment, for example if a corporate bookmaker sought to acquire the licence in Western Australia, which could lead to there being no effective option for pooling.

1.18. The proposed acquisition may also impact on the ability of corporate bookmakers to compete with the merged entity by providing innovative products to licenced venues. Post-acquisition, the retail wagering operator will be vertically integrated with Sky, the dominant racing broadcaster, in Tatts jurisdictions. Sky is an essential input for licenced venues that host wagering facilities. This will provide the merged entity with an incentive to refuse supply of Sky on reasonable commercial terms to venues in Tatts jurisdictions which seek to enter into arrangements with competing wagering operators.

1.19. Recent arrangements, such as CrownBet's digital advertising offer to clubs in NSW, have prompted a swift competitive response by Tabcorp to introduce improved offerings in the form of digital wagering commissions to licensed venues. However, licensed venues are concerned that the merged entity may withhold supply, or raise the price, of Sky to deter entry into an arrangement with a rival wagering provider. The proposed acquisition extends this issue from the Tabcorp jurisdictions to all jurisdictions except Western Australia. This will make it more difficult for corporate bookmakers to provide innovative offerings to venues and customers in competition with the merged entity.

Racing media detriments

Sky's competitive advantages in acquiring media rights

1.20. The competition issues relating to Tabcorp's racing media interests have been a significant issue for some industry participants. As the dominant racing broadcaster, Sky enjoys competitive advantages in acquiring racing media rights. The amount of funding received by a racing club is highly dependent on the amount bet on each race, which in turn is highly dependent on the coverage the race receives in licensed venues. Essentially, media rights holders (PRAs and individual racing clubs) are dependent on the broadcast of their races in retail wagering outlets.

1.21. Tabcorp can threaten to not televise, or to de-emphasise particular races on Sky, if Sky is not granted exclusive rights across all distribution channels by a PRA. For example, Tabcorp can refuse to televise races on the Sky 1 primary wagering channel or not show introductory race content prior to the race which piques the interest of punters.

1.22. This competition issue exists, to some extent, regardless of the proposed acquisition. However, it is relevant when considering the level of competitive constraint from the corporate bookmakers in the wagering market. Furthermore, the proposed acquisition may heighten and entrench these barriers (as discussed below).

The difficulty corporate bookmakers have in obtaining media rights limits their future competitiveness

1.23. Sky's dominant position creates barriers to entry/expansion for corporate bookmakers, due to the difficulties they face in obtaining digital media rights. Although corporate bookmakers have grown and have competed with the merger parties in the supply of online wagering in recent years, their ability to challenge Tabcorp and Tatts in the future will become increasingly reliant on them gaining access to digital media rights (or their customers having a way of easily viewing a race, on free-to-air TV for example).

The proposed acquisition may lessen competition with Sky

1.24. The proposed acquisition may reduce competition with Tabcorp/Sky in the acquisition of racing vision content, particularly in the Tatts jurisdictions. Following the proposed acquisition, the merged entity will have the primary wagering relationship (typically a formal or economic joint venture with the PRAs) in the Tatts jurisdictions. The PRAs in these jurisdictions will become reliant on Tabcorp for much of their funding. Tabcorp may use that dependence to further limit the ability and incentive of PRAs to sell their media rights on an unbundled basis to competitors (including corporate bookmakers). The merged entity could also threaten to refuse to let retail outlets show a free-to-air racing channel that is competing with Sky for media rights in Tatts jurisdictions.

1.25. Without the acquisition, Tatts has the potential to act as a counter-weight to Tabcorp. It could be an alternative bidder for media rights, or a partner to an alternative bidder. Currently, Tabcorp advertises its own online wagering products on Sky, including when Sky is broadcast in Tatts' retail outlets. Tabcorp's brand has a higher brand awareness than the Tatts' brand UBET in Queensland (where UBET is the exclusive retail wagering operator) and Tatts has experienced difficulties differentiating its retail brand from Tabcorp's online brand.[5] As online wagering becomes increasingly important and punters more often place their bets via smart phones, this will have an increasing negative impact on Tatts.

1.26. Tatts is therefore likely to have an incentive to try to limit Sky's dominant position in racing media. Tatts' ability to do so is much stronger than other industry participants, as it can offer a guarantee that non-Sky broadcasts will be shown in retail outlets in Tatts jurisdictions.

1.27. If the proposed acquisition further increases Tabcorp's ability to "lock up" racing media rights, and limits competitive alternatives, there are several impacts:

- PRAs will obtain less for the media rights due to there being less competition for those rights, and their races may not be broadcast as widely
- The barriers to entry/expansion into wagering explained above (that arise due to the difficulty corporate bookmakers have in obtaining media rights) will be heightened further
- There may be detriments to both consumers and the racing industry by racing vision being less accessible to the wider public through free-to-air television broadcasting or streaming online.

[5] Statement of Andrew Catterall, Chief Executive Officer of Racing.com, dated 17 April 2017 (**Catterall**) at [29(e)].

Gaming

1.28. Tabcorp and Tatts overlap in the supply of a range of gaming related services to licensed venues with EGMs, such as pubs, clubs and hotels in Queensland, NSW and Victoria. Tabcorp and Tatts supply pokies venues monitoring services, gaming systems and related services, and repair and maintenance services (field services).

1.29. In Queensland, Tabcorp (Odyssey) and Tatts (Maxgaming) are the only active providers of monitoring and field services. Tabcorp has offered to divest its Odyssey business as a condition of authorisation and has entered into a sale agreement with Australian National Hotels Pty Ltd (Federal Group).

1.30. In NSW, the proposed acquisition combines the exclusive supplier of monitoring services (Tatts' Maxgaming) with the largest supplier of gaming systems and related services (Tabcorp's eBET and TGS). This may give rise to public detriments, as the merged entity may have an incentive to use its position as the monitoring services operator to obtain a competitive advantage in the supply of gaming systems and related services, and potentially foreclose its competitors by misusing commercially sensitive information collected in the course of supplying monitoring services and/or restricting the operation or functionality of third-party gaming systems and related services.

Other public detriments

1.31. The proposed acquisition appears likely to result in other public detriments. Following the proposed acquisition, the merged entity will have a significantly more extensive customer information database compared to the current database of either Tatts and Tabcorp. The merged entity would therefore have an increased ability to engage in customer profiling, targeted digital marketing and cross selling of a range of gambling products on this database, which will inevitably include vulnerable problem gamblers.

Claimed public benefits

1.32. Tabcorp claims that the proposed acquisition will result in approximately [**Confidential to Tabcorp**] [redacted] in direct quantifiable public benefits by the third year following its completion.[6] These are comprised of cost savings and revenue increases amounting to [**Confidential to Tabcorp**] [redacted] respectively.[7]

1.33. Tabcorp claims these improvements will generate further indirect public benefits as:

- 55 per cent of the combined direct benefits will be passed through to racing and sporting bodies; Federal and State governments; and pubs, clubs and agencies;[8]
- Those specific amounts passed through to racing industries will help to address a "free rider problem" associated with the funding of race meets
- [**Confidential to Tabcorp**] [redacted] of the cost savings and [**Confidential to Tabcorp**] [redacted] of the revenue increases will flow through to other parts of the economy, generating increases in gross national income (**GNI**) of between \$174.5 million and \$179.5 million p.a.[9] This is estimated using a computable general equilibrium (**CGE**) model.

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[6] Statement of Damien Johnston, Chief Financial Officer of Tabcorp, dated 6 March 2017 (**Johnston**) at Table 1.

[7] Johnston at [22], Table 1; Form S at [302], page 96.

[8] Annexure A to the Form S at [303], page 97.

[9] Report of Dr Ric Simes, Senior Advisor at Deloitte Access Economics, dated 9 March 2017 (**Simes**) at [145], Table 2, and Attachment B, Table 1.

1.34. Tabcorp also claims the proposed acquisition is likely to result in another public benefit by removing a commercial barrier to creating larger totalisator pools.

1.35. Whilst the proposed acquisition may result in some of the public benefits claimed, the magnitude and likelihood of the benefits are uncertain; and Tabcorp's estimates may be overstated.

1.36. Regarding the claimed direct benefits:

- It is likely some cost savings will be achieved by removing duplication. However, the size of the claimed savings is likely to be overstated because, for example, they include economic transfers and exclude integration costs. Economic transfers, for example the merged entity's ability to negotiate improved terms from suppliers, are not a public benefit. They are a redistribution of resources that do not result in increased production of goods and services, but simply a transfer of money from one entity to another.
- It is unlikely Tabcorp's claimed revenue increases represent a reasonable measure of public benefits. This is because gross revenue of itself is not an appropriate measure of economic welfare or surplus. Much of the claimed revenue increases are unlikely to be merger specific (they could be achieved by Tatts without the proposed acquisition) and the costs of achieving these revenue increases have not been netted off against the estimated revenue increases.
- Importantly, [**Confidential to Tabcorp**] [redacted] of the claimed revenue increases are better characterised as either a transfer or a detriment to wagering customers. Tabcorp's evidence shows that these revenues are expected to come from it improving Tatts' existing fixed odds betting system in a way that will enable it to keep a greater amount of money wagered by punters, while at the same time possibly leading to reduced wagering on fixed odds betting. In other words, the revenue increases are expected to come from Tabcorp giving less to (and taking more from) Tatts' fixed odds consumers.

1.37. Regarding the other claimed benefits:

- The pass-through of direct benefits to other parties should not be double-counted as additional benefits. However, the Tribunal may wish to consider what, if any, weight should be accorded to benefits which are passed through depending on how widely they are shared.
- The proposed acquisition is unlikely to result in national pooling. While the ACCC accepts that larger pools create more liquidity, and in turn greater stability in a pool, the proposed acquisition does not alter the prospects of a national pool being created. This is demonstrated by the fact that Tabcorp has not been able to merge the Victoria and NSW pools, despite common ownership of the pools since 2004.
- If there is a "free rider problem", the proposed acquisition does not address its underlying cause. A long-term solution would involve changing the way wagering operators contribute to the race industry (for example, by increasing race field fees), which is a separate matter to the proposed acquisition.

1.38. Finally, the CGE GNI modelling is likely to be of little utility in assessing the magnitude of public benefits flowing from the proposed acquisition. This is because this type of modelling does not measure changes to economic surplus or welfare; lacks transparency; is reliant on the untested assumptions provided by Tabcorp; and ignores the substantial off-setting impact of cost increases and competitive detriments associated with the proposed acquisition.

Weighing benefits and detriments

1.39. The weighing up of public benefits and detriments likely to result from the proposed acquisition is likely to be difficult. The proposed acquisition is in a complicated and highly regulated industry, and there are many different aspects to the detriments and benefits arguments. The commercial relationships between key industry participants give rise to complex interactions and inter-dependencies. It is no surprise that for such a significant transaction there are contrary views held by industry participants on many issues. In all this, it is important not to forget the largely unheard voice of end consumers.

1.40. At the time of writing this report, the ACCC has not reached concluded views on all of the issues the Tribunal will need to consider. Tabcorp lodged 32 lay witness statements and 4 expert reports, and over 20,000 pages of material (excluding spreadsheets). A further 298 pages of intervener affidavits, with 2988 pages of exhibits, was lodged on or around 13 April 2017. In addition, Tabcorp have altered some substantive elements of the overall proposal since lodgement.[10]

1.41. Although the ACCC had been considering whether the proposed acquisition raised competition concerns prior to the merger authorisation application, it had not considered any of the above material and had not turned its mind to the net public benefits test to be applied by the Tribunal.

1.42. In these circumstances, the ACCC has taken the approach of identifying core issues relating to Tabcorp's application where industry participants and/or the ACCC have contrary views.

1.43. The public detriments appear significant. The proposed acquisition may cement Tabcorp's very strong position in wagering due to:

- Removing Tatts as a wagering competitor
- Limited competition in future licence tenders
- Its ability to limit others from obtaining pooling arrangements
- The difficulty corporate bookmakers have in expanding further to compete with Tabcorp, particularly due to Tabcorp's control of Sky.

1.44. The acquisition may also limit competition against Sky, making it more difficult for the media rights owners to obtain a competitive price for their media rights and maximise coverage of their races.

1.45. There are additional detriments in gaming and in relation to control of customer information.

1.46. On the public benefits side, Tabcorp claims the proposed acquisition will result in cost savings and revenue increases. In relation to cost savings, it is likely some of these will occur, although Tabcorp's estimates may be overstated. However, there are significant doubts as to whether the revenue increases claimed are likely to result in public benefits. As an illustrative example, Tabcorp has claimed as a benefit the ability to improve Tatts' existing fixed odds betting system so it will earn better yields.

[10] This includes:

- Entering into a sale agreement for Odyssey with Federal Group on 14 April 2017 (and providing a copy of the Agreement to the ACCC only on 19 April 2017).
- Finalising a Commitment to a Long Term Pooling Deed to RWWA on 15 March 2017 (and providing a copy to the ACCC only on 20 April 2017, see **Highly Confidential Annexure A** to this report)
- [**HIGHLY Confidential to Tabcorp**] [redacted]

While this might be a benefit to Tabcorp's shareholders and possibly a benefit to aspects of the racing industry, it comes with intrinsic consumer detriment whereby consumers will pay more and receive less.

1.47. Tabcorp has claimed that both the cost savings and revenue increases will be passed through to the racing industry, retail venues, sporting bodies and the Federal and state governments. These should not be double-counted as separate benefits, however the Tribunal may wish to consider what weight should be accorded to benefits, which are passed through depending on how widely they are shared.

2. The proposed transaction

2.1. On 18 October 2016, Tabcorp and Tatts reached an agreement to combine the two companies. Tabcorp proposes to acquire the issued share capital of Tatts by means of a scheme of arrangement.

3. The legal test for authorisation

3.1. The test for granting authorisation is set out in section 95AZH of the Act. The Tribunal must not grant authorisation unless it is satisfied in all the circumstances that the proposed acquisition would result, or be likely to result, in such a benefit to the public that the acquisition should be allowed to occur. The Tribunal has determined that the test requires it to identify and assess the public benefits and detriments likely to result from the proposed acquisition, and weigh the two (**net public benefits test**).[11]

3.2. Tabcorp, as the applicant for authorisation, bears the burden of satisfying the Tribunal that, in all the circumstances, the proposed acquisition would be likely to result in such a benefit to the public that it should be allowed to occur.

3.3. In applying the net public benefits test, the Tribunal has considered it useful to compare the likely future 'with' the proposed conduct and, separately, the likely future 'without' the proposed conduct.[12] This comparison allows an assessment of the benefits and detriments likely to result from the proposed conduct, in this case the proposed acquisition.

3.4. 'Public detriment' is neither referred to in section 95AZH nor defined in the Act. However, in the context of non-merger authorisation decisions under section 90 of the Act, it has been given a broad interpretation by the Tribunal. Public detriments have been held to encompass any impairment to the community generally, including any harm or damage to the aims pursued by society.[13] In many cases, the detriment likely to result from the proposed conduct will be constituted by a lessening of competition.

3.5. The term 'benefit to the public' is also not defined in the Act.[14] In *Re AGL*, the Tribunal considered the expression 'benefit to the public' in the context of section 95AZH(1) of the Act. The Tribunal had regard to previous decisions in non-merger authorisation matters where the expression "the benefit to the public" was considered for the

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[11] *Application for Authorisation of Acquisition of Macquarie Generation by AGL Energy Limited* [2014] ACompT 1 (***Re AGL***) at [157]-[160] and *Application by Sea Swift Pty Limited* [2016] ACompT 9 at [41] (***Re Sea Swift***). See also, for example, *Re 7-Eleven Stores Pty Ltd, Australian Association of Convenience Stores Incorporated and Queensland Newsagents Federation* (1994) ATPR 41-357 (***Re 7-Eleven***) at 42,654; *Re Australian Pathology Practices Incorporated* (2004) 180 FLR 44 at [91]-[93]; *Re Qantas Airways Limited* (2005) ATPR 42-065 (***Re Qantas***) at [144]-[149]. The threshold test in section 95AZH(1) of the Act is identical to the threshold test in section 90(8) in relation to authorisations of conduct that would otherwise breach certain provisions of Part IV of the Act.

[12] See *Re AGL* at [169]; *Application by Medicines Australia Inc* (2007) ATPR 42-164 (***Medicines Australia***) at [117].

[13] See, for example, *Re 7-Eleven* at 42,683; *Re Qantas* at [150].

[14] Section 95AZH(2) of the Act requires that the Tribunal regard as benefits to the public: (a) an increase in the real value of exports; (b) a significant substitution of domestic products for imported goods; and (c) without limiting the matters that may be taken into account, all other relevant matters that relate to the international competitiveness of any Australian industry.

relevant authorisation tests in section 90 of the Act. In particular, the Tribunal noted that:

a) 'Benefit to the public' encompasses anything of value to the community generally or any contribution to the aims pursued by society including as one of its principle elements (in the context of trade practices legislation) the achievement of the economic goals of efficiency and progress[15]

b) Provided there is a causal relationship between the benefit or benefits to the public asserted and the conduct to be authorised, the range of matters that may be considered is not limited[16]

c) For benefits to be taken into account they must have substance and durability[17]

d) In assessing claimed public benefits:[18]

   i) Any estimates as to their quantification should be robust and commercially realistic

   ii) The assumptions underlying their assessment must be spelled out in such a way that they can be tested and verified

   iii) One-off benefits should be distinguished from those of a more lasting nature

e) The options for achieving claimed benefits should be explored and appropriate weighting be given to future benefits not achievable in any other less anti-competitive way.

3.6. Claims that are purely speculative in nature should not be given any weight.[19] For a benefit or detriment to be taken into account, the Tribunal must be satisfied that there is a real chance, and not a mere possibility, of the benefit or detriment eventuating.[20]

3.7. In *Re Sea Swift*, the Tribunal stated that:

A public benefit arises from a proposed acquisition if the benefit would not exist without the acquisition or if the acquisition removes or mitigates a public detriment that would otherwise exist. If a claimed public benefit exists, in part, in a future without the proposal, the weight accorded to the benefit may be reduced appropriately.[21]

3.8. In examining benefits to the public relied on by an applicant for authorisation, rather than assessing whether the benefit claimed is a public or private benefit, the enquiry should be directed towards the extent to which the benefit has an impact on members of the community. Does it fall into the category of "anything of value to the community generally"? If it does, what weight should be given to that benefit, having regard to the nature, characterisation and identity of the beneficiaries of it?[22] The Tribunal has held that the appropriate standard to apply in assessing public benefits is a "form" of the total welfare standard in which less weight is given to public benefits to the extent they are not shared among members of the community generally.[23] Consequently, if a

[15] *Re AGL* at [161], citing *Queensland Co-operative Milling Association Ltd; re Defiance Holdings Ltd* (1976) 8 ALR 481 at 510.

[16] *Re AGL* at [162], citing *Medicines Australia* at [107].

[17] *Re AGL* at [163], citing *Re Qantas* at [205] and *Re Rural Traders Cooperative (WA) Ltd* (1979) 37 FLR 244 at [262]-[263].

[18] *Re AGL* at [163], citing *Re Qantas* at [206].

[19] *Re AGL* at [164], citing *Re Qantas* at [156]. See also *Re Howard Smith Industries Pty Ltd* (1977) 28 FLR 385 (***Re Howard Smith***), at 17,335; *Medicines Australia* at [109]; *Re VFF Chicken Meat Growers' Boycott Authorisation* (2006) ATPR 42-120 at [83].

[20] *Re Qantas* at [156].

[21] *Re Sea Swift* at [42].

[22] *Re Qantas* at [188].

[23] *Re Qantas* at [185]-[189], *Re Howard Smith* at [391]-[392].

merger benefits only a small number of shareholders of the applicant corporations through higher profits and dividends, this will be given less weight by the Tribunal, because the benefits are not being spread widely among members of the community generally.[24]

4. Public detriments

The public detriments section of this report has been separated into the following four topics:

- Wagering
- Racing Media
- Gaming
- Other public detriments

The first three topics focus on public detriments where a lessening of competition may arise. The fourth topic focuses on other public detriments.

Wagering

Overview of wagering

4.1. In Australia, wagering has traditionally been based on thoroughbred, harness and greyhound racing. These continue to account for the majority of wagering industry turnover.

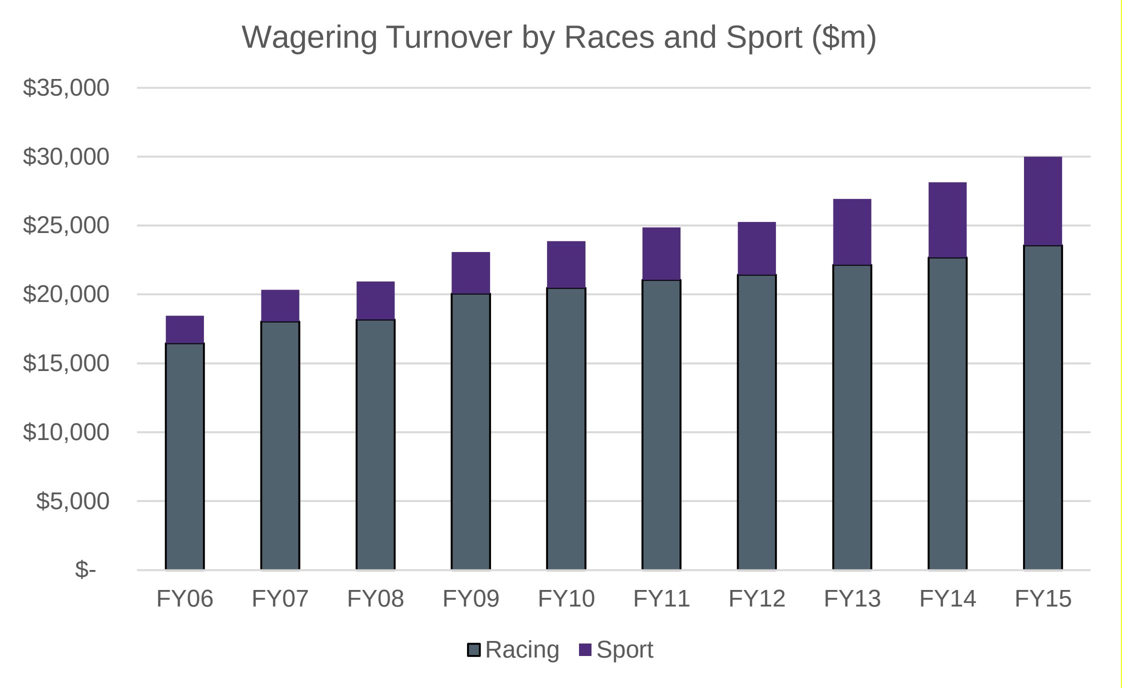
4.2. More recently, wagering on other sports events (such as the AFL and NRL), as well as wagering on overseas events, has grown in relative significance. Minor forms of wagering also exist, such as wagering on the outcomes of elections, reality television shows or novelty events.

4.3. Figure 1 below shows the absolute value of turnover in Australia from FY06 to FY15 for racing and sport wagering.[25] In wagering, turnover refers to the amount bet by punters (as opposed to the amount kept by wagering service providers). Figure 1 shows that while racing wagering has been growing and continues to represent the largest proportion of wagering turnover, sports wagering has been increasing at a faster rate. In FY15, wagering on races was still over 3.5 times higher than wagering on sport.

[24] *Re Howard Smith* [391]-[392]; *Re Qantas* [185].

[25] Source Freeman at [270].

Figure 1 - Absolute value of turnover in Australia from FY06 to FY15 for racing and sport wagering



4.4. Racing wagering occurs through various channels: retail wagering outlets (such as TABs and pubs/clubs); digital (online via desktop, tablet or mobile apps); over the phone; and on-course at race meetings. While Tabcorp and Tatts provide racing wagering opportunities to punters through all of these channels, corporate bookmakers (for example Sportsbet, CrownBet, William Hill, Ladbrokes and Bet365) are only able to provide wagering services through digital and phone channels.

4.5. In general terms, racing wagering products take the form of pari-mutuel wagering (exclusively provided by the totalisator operators) and fixed odds wagering (provided by both totalisator operators and corporate bookmakers).

- **Pari-mutuel wagering** involves the ‘pooling’ of all bets by a totalisator operator – the customers odds may change up until the close of betting on the event and the final odds are not known until the completion of the relevant event. A totalisator’s revenue on any given event is ‘risk free’ and is a function of the size of the pool and the take-out rate.
- **Fixed odds wagering** involves a bookmaker acting as the counterparty to the customer’s bet – the customer is informed of the odds they will receive at the time their bet is placed. Bookmaker revenue on fixed odds betting on any given event involves risk as the revenue on an event is dependent on the outcome of that event.

4.6. Tabcorp has the exclusive licence to supply totalisator and retail wagering services in the Tabcorp jurisdictions. Tatts has the exclusive licence to supply totalisator and retail wagering services in the Tatts jurisdictions. RWWA, a WA government owned corporation, is the exclusive supplier of retail and totalisator services in WA. Wagering products in Australia are supplied by the totalisator operators licensed by each of the state and territory governments, as well as bookmakers and Betfair, the only existing betting exchange.

4.7. A comparison of the various distribution channels and product types that Tabcorp, Tatts and corporate bookmakers are able to provide is set out in Table 1 below. This shows that while Tabcorp and Tatts are able to compete to provide all racing wagering product types across all distribution channels, corporate bookmakers are more limited in the ways they can provide racing wagering opportunities.

Table 1 - Comparison of distribution channels and product types

		Tabcorp	Tatts	Corporate Bookmakers
Distribution Channel	Retail	✓	✓	
	On-course	✓	✓	
	Phone	✓	✓	✓
	Online	✓	✓	✓
Wagering Type	Pari-mutuel	✓	✓	
	Fixed odds	✓	✓	✓

4.8. Tabcorp and Tatts are the largest providers of wagering products in Australia. Across all wagering types and channels, they had a combined share of total revenue of approximately [**Confidential to Tabcorp and Tatts**] [redacted] in FY15. Revenue has a distinct meaning in wagering markets, and equals the amount bet by punters that wagering service providers "take-out" or don't pay back to punters through winnings. In other words, it is the amount of turnover kept by wagering service providers. Wagering revenue by service provider over the period FY06 to FY15 is set out in Figure 2 below.

Figure 2 - Wagering revenue by service provider over period FY06 to FY15 [Confidential to Tabcorp and Tatts][26]

[redacted]

[26] Source: Freeman at [279].

4.9. Figure 2 allows a number of important observations:

- [**Confidential to Tabcorp and Tatts**] [redacted].
- Tatts as an individual entity appears to have the second greatest level of wagering revenue based on estimates provided by Tabcorp. While corporate bookmakers as a whole now represent the second largest earner of overall revenue, this is divided amongst a number of individual corporate bookmakers.
- The combined revenue share of the merged entity will, based on Tabcorp's estimates, represent approximately [**Confidential to Tabcorp and Tatts**] [redacted] of wagering revenue earned across distribution channels and wagering product types.

4.10. It is clear from Figure 2 that corporate bookmakers are, in combination, growing their share of wagering revenue. This has grown from approximately [**Confidential to Tabcorp and Tatts**] [redacted] in FY06 to around [**Confidential to Tabcorp and Tatts**] [redacted] in FY15.

4.11. This appears to have occurred for a combination of reasons, including:

- Significant growth in overall wagering turnover, largely driven by growth in online wagering as the portability and adoption of smartphones and tablets has increased the ease and frequency of wagering
- Some wagering customers having an increased preference for fixed odds and tote-derivative wagering, which are offered by corporate bookmakers[27]
- Growth in wagering customers attracted by sports wagering.

Market definition for wagering

4.12. It is clear that there are a number of areas of competition relevant to an assessment of competitive detriment in this matter, including that:

- Tabcorp and Tatts compete to acquire the right to be the exclusive provider of totalisator and retail wagering services within each state
- Tabcorp and Tatts compete to provide pari-mutuel wagering products to punters – at least to some extent via online channels
- Tabcorp, Tatts and corporate bookmakers compete to provide fixed odds wagering services via online and phone distribution channels.

4.13. A preliminary issue is whether all of these areas of competition occur within a single national wagering market; or whether each represents a separate market for the purposes of analysing the competition effects of the proposed acquisition.

4.14. Tabcorp submits that there is a national market in Australia for the supply to consumers of wagering on horse races and other sporting events, comprising pari-mutuel, fixed odds and tote derivative odds betting as well as wagering through a betting exchange.[28]

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[27] A fixed odds product that derives its pricing by reference to the prices available in totalisator pools and may involve a stretch or bonus above the derived pari-mutuel odds.

[28] Form S at [5.2]–[5.3], page 50; Report of Dr Christopher Pleatsikas, Vice President of Charles River Associates, dated 8 March 2017 (**Pleatsikas**) at [96]-[100].

4.15. While a single broad market may be appropriate it may have the effect of glossing over the extent of competitive constraints provided by different wagering products and distribution channels on each other.

4.16. Tabcorp, Tatts and corporate bookmakers appear to compete to provide fixed odds wagering services through online and phone distribution channels. However, there are reasons to believe corporate bookmakers do not fully constrain Tabcorp and Tatts in the provision of fixed odds services. For example, Tabcorp has indicated it expects to be able to increase its prices for these products if the proposed acquisition proceeds.[29]

4.17. Further, it is not clear to what extent totalisator and fixed odds products constrain each other. Evidence provided by Tabcorp shows that [**Confidential to Tabcorp**] [redacted].[30] However, the evidence also shows that the effective price charged by Tabcorp and Tatts for their totalisator products has [**HIGHLY Confidential - derived confidential information**] [redacted] during this period – including over the last five years.[31] This suggests that fixed odds products provided by corporate bookmakers are not acting as a constraint on the pricing of Tabcorp and Tatts' totalisator products.

4.18. In addition, the extent to which wagering services provided in retail venues are constrained by those provided through online channels is unclear. Evidence provided by Tabcorp demonstrates that online wagering [**Confidential to Tabcorp**] [redacted]

4.19. In his expert report filed by the ACCC, Mr James Mellsop of NERA Economic Consulting concludes that:

… it is difficult to identify a clear market boundary. At a minimum, the products are differentiated. This is implied by the:

*a) [**Highly Confidential - derived confidential information**] [redacted]; and*

b) Apparent value in acquiring an exclusive tote wagering licence.[33]

4.20. Whatever market definition(s) the Tribunal considers appropriate for the 'downstream' supply of wagering products to consumers, it is also relevant to consider separate 'upstream' markets for the acquisition of key inputs which may be necessary to supply totalisator and retail wagering operations,[34] or enable competing wagering operators to compete effectively, including:

- Bidding for totalisator licences and retail exclusivity rights with state and territory governments
- Access to pooling arrangements
- Access to racing vision.

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[29] Report of James Mellsop, Managing Director of NERA Economic Consulting, dated 27 April 2017 (**Mellsop**) at [269(a)].

[30] Freeman at [268] shows the proportion of overall wagering turnover on fixed odds products has grown from [**Confidential to Tabcorp**] [redacted]; while the proportion of overall wagering turnover on pari-mutuel products has fallen from [**Confidential to Tabcorp**] [redacted] over the same period.

[31] Mellsop, Figures 4 and 5.

[32] Report of Patrick Smith, Partner at RBB Economics, dated 9 March 2017 (**Smith**) at [75], Figure 5.

[33] Mellsop at [241].

[34] Mellsop at [43].

4.21. A reduction in the ability of wagering operators to acquire these key inputs may have competitive impacts in the wagering market or markets for the supply of wagering products to consumers.

4.22. The remainder of this section of the report considers the extent to which:

- Corporate bookmakers would be likely to constrain the merged entity if the proposed acquisition proceeds
- The proposed acquisition will lead to a reduction in wagering competition in the supply of wagering services between Tabcorp and Tatts
- The proposed acquisition lowers the competition in bidding processes for wagering licences.

Competitive constraint of corporate bookmakers in the future

4.23. Tabcorp considers corporate bookmakers pose "vigorous competition" to its wagering operations within the national wagering market.[35] It submits that, post-acquisition, the merger parties will continue to be constrained by "continued vigorous and aggressive competition from corporate bookmakers".[36] In support of these contentions, Tabcorp states that [**HIGHLY Confidential to Tabcorp**] [redacted][37] The evidence is clear that corporate bookmakers have grown significantly in recent years (see Figure 2 above at paragraph 4.8 above), and that the digital/online channel they do compete in has become increasingly important. Tabcorp states there has been rapid growth in digital wagering over the past five years, with digital wagering increasing from 30 per cent to 51 per cent of industry turnover.[38] This is illustrated by Figure 3 below, which sets out industry turnover by channel in absolute terms since FY06. It is to be noted that this data combines both racing and sports wagering. As sports wagering predominantly occurs via digital (rather than retail) channels, this means that this figure is likely to overstate the relative growth in digital racing wagers.

Figure 3 - Industry turnover by channel [**Confidential to Tabcorp**][39]

[redacted]

[35] Form S at [10.2], page 84.

[36] Form S at [10.1], page 83.

[37] Statement of David Attenborough, Managing Director and Chief Executive Officer of Tabcorp, dated 8 March 2017 (**Attenborough**) at [149]. Freeman [248].

[38] Form S at [4.59], page 29.

[39] Freeman at [255], Figure 34.

4.24. Evidence also shows the importance of digital wagering to Tabcorp, with it taking the view that [**HIGHLY Confidential to Tabcorp**] [redacted],[40] and implementing a strategy [**HIGHLY Confidential to Tabcorp**] [redacted][41] This lends support to the contention that digital wagering is key to future competition between wagering operators, although retail outlets will continue to be significant.

4.25. Despite this, there are a number of reasons to be concerned that corporate bookmakers may not be able to effectively constrain the merger parties – either now, or in a future with the proposed acquisition.

4.26. First, while the proportion of wagering made through digital channels has grown strongly in recent years, Mr Mellsop states that retail turnover has [**Confidential to Tabcorp**] [redacted] in nominal terms between 2006 and 2015. This is clear from Figure 3 above, and leads to the conclusion that digital channels have likely grown wagering as a whole, "rather than cannibalise retail to a material degree".[42] Similarly, despite the relative growth of corporate bookmakers, Tabcorp's absolute level of revenue has also grown significantly over recent years (see Figure 2 above).

4.27. Second, and as indicated above, it appears both Tabcorp and Tatts charge [**HIGHLY Confidential - derived confidential information**] [redacted] for their wagering services than those provided by corporate bookmakers. In this regard, the effective price of wagering is equal to the proportion of money wagered by punters that service providers "take-out" for themselves. That is, if $100 were bet on a race, and punters were returned $85 after the completion of the race, the wagering service provider would have a "take-out" of $15 at a rate of 15 per cent of turnover. In wagering, turnover is the amount bet or wagered by punters; while revenue is the amount "taken-out" by the service provider. Mr Mellsop considers that:

The economics literature defines the price of wagering by the "take-out rate", i.e. the fraction of wagering turnover that is withheld by the provider. For example, Suits (1979, p.156) states that "the take-out rate constitutes the true price of playing the game".[43]

4.28. Mr Mellsop's report demonstrates that between FY12 and FY16, Tabcorp and Tatts have [**Confidential to Tabcorp and Tatts**] [redacted].[44] Mr Mellsop further states in his evidence that:

[**Confidential to Tabcorp**] [redacted][45]

4.29. Third, the evidence of Mr Johnston, the Chief Financial Officer of Tabcorp, indicates it expects to [**Confidential to Tabcorp**] [redacted] wagering services following the proposed acquisition. In this regard, he states:

[**Confidential to Tabcorp**] [redacted]

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[40] Attenborough, Tab 5 of Highly Confidential Exhibit DA-2 [TBP.003.001.0941].

[41] TBP.004.003.6960 [Tabcorp section 155 document].

[42] Mellsop at [54]. See also Smith at [75]-[76].

[43] Mellsop at [31].

[44] Mellsop, Figure 3.

[45] Mellsop at [50].

[redacted][46]

4.30. [**Confidential to Tabcorp**] [[redacted] This point is further addressed in section 5 on public benefits.

4.31. Tabcorp submits that corporate bookmakers "enjoy several important competitive advantages" over the merger parties' traditional wagering businesses. These advantages include lighter regulation and lower taxation for those licensed in the Northern Territory, as well as lower contributions to the racing industry and lower overheads.[47]

4.32. In contrast, corporate bookmakers Ladbrokes and CrownBet both consider that there are a number of factors which are likely to limit their continued expansion in the national wagering market and hinder their ability to effectively constrain the merged entity in future.

4.33. In particular, Mr Nicholas Tyshing, Chief Operating Officer of CrownBet, states that Tatts and Tabcorp, by virtue of their status as totalisator and retail operators, have a number of competitive advantages over corporate bookmakers including: [48]

- The ability to leverage a retail network to drive wagering, including by valuable multi-channel customers (i.e. punters operating across both retail and online channels)[49]
- A large national customer database which can be utilised to cross-subsidise, cross-leverage or cross promote wagering operations with other gaming operations[50]
- Access to customer groups that are unlikely to be reachable by corporate bookmakers, including punters who have a strong preference for placing a pari-mutuel bet and/or for using retail products.[51]

4.34. Mr Mellsop comments "it is probably fair to conclude that each set of operators (totes and corporate bookmakers) have advantages and disadvantages compared to the other set. [**Confidential to Tabcorp**] [redacted] have been growing their turnover over the last five years, or to put this another way, neither type of firm is being competed out of the market, which we might expect to occur if the competitive advantages were all one way." [52]

4.35. The ACCC highlights the following issues which may also limit the extent of competitive constraint provided by corporate bookmakers or any prospective new entrants to the merged entity in future.

[46] Johnston at [79]-[80].

[47] Form S at [10.4], page 84; Pleatsikas at [153]; Freeman at [283]-[284].

[48] Statement of Nicholas Tyshing, Chief Operating Officer of CrownBet, dated 13 April 2017 (**Tyshing**) at [376].

[49] Tyshing at [374].

[50] Tyshing at [376].

[51] Second Affidavit of Giles Thompson, Acting Chief Executive Officer of Racing Victoria, dated 13 April 2017 (**Second Affidavit of Thompson**) at [44]; see further Affidavit of Simon Barrile, General Counsel of Racing Victoria, dated 13 April 2017 (**Barrile**).

[52] Mellsop at [72] (footnote omitted).

Future regulatory environment

4.36. There are a number of impending or proposed regulatory changes which may impact on the wagering industry in the foreseeable future. These changes appear to favour retail wagering operators and may limit the effectiveness of competition offered by the corporate bookmakers. Mr Patrick Brown, General Counsel and Corporate Affairs Manager of Ladbrokes Digital Australia, provides comments on the impact of these changes at [38] and [39] of his statement.[53]

In-play betting

4.37. In-play betting is a form of betting which involves placing a bet once the event has begun. It is the world's fastest growing gambling segment. [54] It is currently prohibited online; however punters may place an in-play bet in a retail wagering venue or via telephone.[55] Proposed changes to the *Interactive Gambling Act 2001* (Cth) (**IG Act**) are currently before Parliament. The *Interactive Gambling Amendment Bill 2016* (Cth) (**IG Bill**) proposes to insert a 'place-based betting service' exemption, which will allow only retail betting venues (TABs, pubs and clubs), and not corporate bookmakers, to offer online in-play betting on sports.

4.38. In light of these changes, Tabcorp considers that [**Confidential to Tabcorp**] [redacted][56] and [**Confidential to Tabcorp**] [redacted].[57]

Point of consumption tax

4.39. The South Australian Government has also announced a 15 per cent place of consumption tax model to commence on July 2017.[58] This will apply on top of existing product fees (race field fees) and licence fees and taxes payable to the state government that issued the licence.

4.40. The Federal Treasurer has also recently announced that the Commonwealth Government is considering introducing a national point of consumption tax, similar to that of South Australia. This tax will not apply to retail wagering operators in that state or territory (i.e. Tabcorp, Tatts Group/UBet and WA TAB).[59] CrownBet contends that the imposition of a national point of consumption tax scheme would have little, if any, impact on the merger parties (as existing taxes paid in those jurisdictions will be offset by the new tax) but will have a significant impact on corporate bookmakers.[60]

Potential restrictions on wagering advertising

4.41. Tabcorp refers to the [**HIGHLY Confidential to Tabcorp**] [redacted]

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[53] Statement of Patrick Brown, General Counsel and Corporate Affairs Manager of Ladbrokes Digital Australia, dated 27 April 2017 (**Brown**).

[54] Statement of Robert Cooke, Managing Director and Chief Executive Officer of Tatts, dated 20 March 2017 (**Cooke**) at [153(e)].

[55] Cooke at [38].

[56] Attenborough, Tab 1 of Highly Confidential Exhibit DA-2, Documents presented to the Tabcorp Board Strategy Meeting on 14 September 2016, page 24 [TBP.001.001.8697].

[57] Attenborough, Tab 1 of Highly Confidential Exhibit DA-2, Documents presented to the Tabcorp Board Strategy Meeting on 14 September 2016, page 40 [TBP.001.001.8697].

[58] Attenborough, Tab 1 of Highly Confidential Exhibit DA-2, Documents presented to the Tabcorp Board Strategy Meeting on 14 September 2016; [**HIGHLY Confidential to Tabcorp**] [redacted], page 2 [TBP.001.001.8697].

[59] Brown at [38(b)].

[60] Tyshing at [349]

[redacted][61]

4.42. Public support for more active regulation of wagering advertising could lead to increased restrictions on the ability of corporate bookmakers to advertise. This may limit the growth of corporate bookmakers in the future. In contrast, the merged entity will have direct advertising access to racing wagering customers through its ownership of Sky. Sky is distributed into retail wagering outlets nationally and to residential pay television customers via Foxtel.

Access to advertising

4.43. Mr Tyshing, on behalf of CrownBet, states that the expansion of corporate bookmakers is hindered by Sky's refusal to allow them to advertise on Sky Racing1, as it makes it more difficult for them to reach potential customers.

4.44. Without the ability to readily reach wagering customers through Sky, corporate bookmakers are required to spend a considerable amount on advertising to achieve similar customer impressions. Mr Tyshing states that due to Sky's control over media racing content, corporate bookmakers are heavily reliant on advertising in conjunction with sport which is an indirect and costly way to reach racing customers.[62]

Access to racing vision

4.45. Racing media is closely related to the wagering industry and is a major factor in facilitating participation in racing and wagering off-course. A large part of attracting wagering customers depends on the provision of accurate and timely access to racing coverage.[63] Given the impact of vision on wagering activity, racing vision appears to be a key functional input which may impact on the ability of corporate bookmakers to compete with the merged entity. For example, Mr Tyshing states:

I regard the integration of racing media content into our digital wagering products as a critical element of our ability to compete effectively in the future…In my view, full access to digital racing wagering media would be a true 'game changer' in terms of its impact on our ability to compete and offer new, innovative and highly valuable wagering services and experiences to Australian punters.[64]

4.46. Given the shift towards digital, access to digital media rights is of increasing importance and may be a key factor in determining the constraint that the corporate bookmakers actually impose on the merged entity.[65] Tabcorp/Sky's dominance of racing media rights, and how this raises barriers to entry/expansion by the corporate bookmakers is discussed in further detail in paragraphs 4.126 to 4.138 below.[66]

Impact of Tabcorp's ownership of Sky on the ability of corporate bookmakers to negotiate alternative proposals with licensed venues in Tatts jurisdictions

4.47. Corporate bookmakers are also trying to improve their wagering performance through offering innovative products to clubs and pubs. As detailed below at paragraphs 4.53 to 4.58, corporate bookmakers have experienced challenges entering into such partnerships, such challenges are likely to worsen should the proposed acquisition

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[61] Attenborough, Tab 1 of Highly Confidential Exhibit DA-2, Documents presented to the Tabcorp Board Strategy Meeting on 14 September 2016, page 35 [TBP.001.001.8697].

[62] Tyshing at [376].

[63] Form S, [4.53], page 28; Freeman at [203].

[64] See Tyshing at [419]-[421].

[65] Statement of Robert Hines, Principal at Hines Pty Ltd, dated 25 April 2017 (**Hines**) at [86].

[66] See also Hines at [86].

proceed, due to the integration of the dominant racing broadcaster and the retail wagering operator in all states and territories (except Western Australia).

4.48. Broadcasting of racing vision is a crucial input to the successful wagering operations of licensed venues.[67] As supplier of Sky, Tabcorp is in a strong position when dealing with licensed venues, because it is able to use its control of Sky to prevent these venues from considering competitive products offered by corporate bookmakers.

4.49. In order to obtain Tabcorp's retail wagering services, venues must enter into an agreement which [**HIGHLY Confidential to Tabcorp**] [redacted].[68] It is also a condition of the wagering agreement that every venue offering Tabcorp wagering services must subscribe to Sky.[69] Tabcorp has typically bundled services by offering rebates to clubs for the cost of Sky where those clubs also have a Tabcorp retail wagering service.[70] Many clubs rely on this rebate for their retail wagering facilities to be commercially viable.[71]

4.50. In Tatts jurisdictions, venues must obtain a 'full race telecasting service' to obtain Tatts' retail wagering services.[72] While Tatts does not refer to Sky in its agreements with licensed venues, in order to comply with this requirement, Tatts considers that venues must, at minimum, subscribe to Sky Racing1.[73]

4.51. In its agreements for the provision of Sky to licensed venues, [**HIGHLY Confidential to Tabcorp**] [redacted].[75] Evidence from some club representatives indicates that clubs have no real ability to negotiate with Tabcorp in relation to Sky, including on pricing.[76] In particular, Mr Christopher White, Group Operations Manager of Club Central, states "Tabcorp has a take it or leave it" approach.[77]

4.52. The ability of the merged entity to use Sky as a means to influence the behaviour of licensed venues and foreclose digital wagering opportunities in states where Sky is vertically integrated with Tabcorp's wagering operations has been demonstrated recently in NSW.[78]

4.53. Following the announcement of the digital wagering partnership between Registered Clubs Association of New South Wales (**ClubsNSW**), ClubsNSW and CrownBet (as set out in the statement of Mr Joshua Landis, Executive Manager - Public Affairs of ClubsNSW, dated 27 April 2017 and Mr Nicholas Keenan, Commercial Director of CrownBet, dated 13 April 2017), Tabcorp engaged in conduct, which according to Mr

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67 Statement of Joshua Landis, Executive Manager - Public Affairs of Clubs NSW, dated 27 April 2017 (**Landis**) at [21].

68 Statement of Christopher White, Group Operations Manager of Club Central, dated 27 April 2017 (**White**) at [22] and [23(a)]; Landis at [41], JDL-6; Statement of Michele Lavorato, Chief Executive Officer of Campbelltown Catholic Club, dated 27 April 2017 (**Lavorato**) at [9(d)-(e)], Highly Confidential Annexure ML-1.

69 Statement of Joshua Blanksby, Executive Director, Racing & Corporate Affairs, Melbourne Racing Club, dated 17 April 2017 at [17]-[18] and [20]; Statement of Michael Wilson, Chief Executive Officer of Ashfield Bowling Club, dated 27 April 2017 (**Wilson**) at [8], Highly Confidential Annexure MPW-2.

70 Landis at [22].

71 Landis at [38].

72 Freeman at [211].

73 Ibid.

74 Tony Costain, Queensland General Manager at Hotel Clubs & Services Pty Ltd, dated 27 April 2017 (**Costain**) at [20]; Lavorato at [37]; Landis at [53]; White at [14]; Wilson, Highly Confidential Annexure MPW-2 (see Clause 5.1(d)).

75 Wilson at [9(b)]; Highly Confidential Annexure MPW-2 (see Clause 10(a)).

76 Lavorato at [22]; White at [15]; Costain at [18].

77 White at [15].

78 Landis at [30].

Keenan, "sought to deter members of the ClubsNSW network from engaging CrownBet as their digital wagering advertising partner".[79]

4.54. This is supported by the evidence of Mr Landis, Executive Manager – Public Affairs of Clubs NSW, who also considers that Tabcorp has sought to "use its control of racing vision (through Sky channels) to deter clubs from entering into arrangements with competing digital wagering providers".[80]

4.55. Such conduct has included, on 24 February 2017, Tabcorp sending a letter to a club which had given notice of its intention to terminate its retail wagering service agreement with Tabcorp (**24 February letter**). The letter stated, among other things:

We note the statement in your letter that you are not seeking to affect other services provided by Tabcorp other than under the Agreement. We are currently considering our position in relation to the provision of other services (such as Sky vision) and will contact you separately about this.[81]

4.56. Mr Keenan's evidence and Mr Landis' evidence refer to a number of representations allegedly made by Tabcorp representatives regarding continued access to, or pricing of, Sky, should a venue take up the CrownBet offer (**Tabcorp Representations**).[82]

4.57. The 24 February letter and Tabcorp Representations created an impression that access to Sky would be terminated or prices substantially increased, if a venue chose to also obtain digital wagering services from another provider.[83] After this issue became the subject of media reports, Tabcorp confirmed in correspondence sent to ClubsNSW, dated 16 March 2017, that access to Sky would continue to be supplied to venues which enter into an agreement with CrownBet.[84] Despite this, this incident illustrates the potential for Tabcorp to leverage its control of Sky as a tool in negotiating with venues.

4.58. Tabcorp has also recently increased the cost of Sky to NSW clubs by a combined $2 million per annum, by cancelling its longstanding Sky rebates.[85] Mr Landis understands that Sky rebates have been relabelled as a "Partnership Exclusivity Rebate" which involves a $6,000 up front payment for clubs that agree to exclusively promote Tabcorp's retail digital wagering services.[86] Mr Landis understands that such terms will apply to all clubs, unless they "opt out" of the new contract. He considers that "[b]y simultaneously offering the $6,000 per year "Partnership Exclusivity Rebate" to clubs on an "opt out" basis, many clubs will be unintentionally agreeing to "bundle" their retail wagering facilities, digital wagering facilities and Sky Racing subscriptions, which will have the effect of foreclosing competitors to Tabcorp for the supply of digital wagering services to clubs."[87]

4.59. The ACCC recognises that these issues already exist in the industry, and do not arise as result of the proposed acquisition. It is therefore important to assess what difference the proposed acquisition will make.

4.60. Arguably, Tabcorp already has some incentive in all states and territories to prevent corporate bookmakers from initiating innovative proposals with venues by refusing

[79] Keenan at [27]; see further Landis at [29(b)].

[80] Landis at [29(b)].

[81] Keenan at [36]; Annexure NK-8.

[82] See Keenan at [48]-[67] and Landis at [42]-[52] for details of these representations.

[83] White statement [23(b)-(c)]; Lavorato statement [31]; Landis [41] and [45].

[84] Keenan at [43]; Annexure NK-11.

[85] Landis statement at [37]-[38]; Wilson at [13]-[14].

[86] Landis at [37].

[87] Landis at [38].

supply of Sky, raising the price of Sky, or providing Sky at a lower price subject to the outlet not having a partnership with a corporate bookmaker.

4.61. However, the ACCC considers that this incentive will become much stronger in the Tatts jurisdictions after the proposed acquisition. The proposed acquisition will result in the integration of the retail wagering operator and the dominant supplier of racing vision in all states and territories (except for Western Australia). Without the acquisition, if a venue enters into a partnership with a corporate bookmaker in a Tatts jurisdiction where Tabcorp is not the retail wagering operator, this poses no risk to Tabcorp's retail wagering operations. It is Tatts that has the most to lose if its licensed venues are forming partnerships with corporate bookmakers. Conversely, if the acquisition proceeds, the merged entity will have an incentive to make threats to, or to refuse to provide Sky to venues in former Tatts jurisdictions, or supply Sky on unfavourable terms, such as by increasing the price of Sky, if a venue decides to pursue a partnership with a corporate bookmaker.

4.62. Some Queensland venues have highlighted these concerns. Mr Timothy Wright, Board Member of the RSL & Services Clubs Association Queensland Inc and General Manager of Greenbank RSL Services Club Inc, has the following concerns regarding the proposed acquisition:

> *The first is the potential for the merged entity to price gouge in relation to the price of Sky Racing by significantly increasing the price of it. The second is that the merged entity may restrict vision.*[88]

4.63. Mr Wright is also concerned about the impact the proposed acquisition may have on the ability of clubs to enter into agreements with corporate bookmakers. He considers:

> *[C]lubs in Queensland would have a greater risk of having Sky Racing vision cut or the price of Sky Racing increased if they enter into an arrangement with another wagering provider. I believe that it will be very difficult for clubs to use other providers because the retail wagering facility and Sky Racing will be provided by the one company (Tabcorp).*[89]

4.64. These concerns echo those of Mr Landis who is concerned that the approach taken in NSW will be adopted by the merged entity in Tatts jurisdictions. He considers that the effect of this will be that:

> *…clubs have no real choice to use competitor digital wagering providers and, if they do use a competitor digital wagering provider, they run the risk of losing access to Sky Racing or the cost of their Sky Racing subscription increasing significantly to a level that it is not commercially viable.*[90]

4.65. If the acquisition limits the ability of corporate bookmakers to provide innovative offerings in competition with the merged entity in Tatts jurisdictions, this is likely to have several impacts:

- It damages the options of venues in Tatts jurisdictions, by restricting them from pursuing competing options for wagering partnerships/facilities
- It lessens competition in wagering, by limiting the ability of corporate bookmakers to expand (particularly their ability to expand in a way that more closely competes with the retail outlets of Tabcorp and Tatts)

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[88] Statement of Timothy Wright, Board Member of the RSL & Services Clubs Association Queensland Inc and General Manager of Greenbank RSL Services Club Inc, dated 27 April 2017 (**Wright**) at [17].

[89] Wright at [22].

[90] Landis at [54].

- It lessens innovation in wagering/retail offerings more generally, and reduces choice for consumers.

Removal of wagering competition between Tabcorp and Tatts

4.66. Tabcorp and Tatts appear to be strong competitors with each other. The proposed acquisition will remove that competition.

4.67. The ACCC accepts that Tabcorp and Tatts' share of racing wagering revenue and turnover has fallen as corporate bookmakers have grown. However, Tabcorp and Tatts are both still very significant players. As indicated above, Tabcorp and Tatts have a combined share of approximately [**HIGHLY Confidential to Tabcorp**] [redacted] of wagering revenue earned across all distribution channels and wagering product types.[91]

4.68. The ACCC recognises that the merger parties' retail wagering operations are exclusive in each state and territory and there is therefore little. if any. direct competition between these retail operations.[92] However, in all other respects, Tabcorp and Tatts compete strongly with each other in telephone and digital/online wagering, and are likely to be close competitors to each other. This is because they are able to compete across both fixed odds and pari-mutuel products, whereas corporate bookmakers are limited only to providing fixed odds and tote derivative products. Further, evidence shows that the take-out rates of (i.e. prices set by) [**Confidential to Tabcorp and Tatts**] [redacted].[93]

4.69. Mr Tyshing states that there is evidence to suggest that if the proposed merger does not proceed, Tatts and Tabcorp will compete with each other more strongly in the digital space than has occurred historically.[94] Mr Mellsop also considers that evidence submitted by Tabcorp overstates the competitive constraint from corporate bookmakers and understates the competitive tension between Tabcorp and Tatts.[95]

4.70. In addition, there are certain customer segments who have a strong preference for pari-mutuel betting, such as certain professional gamblers. The proposed acquisition removes that direct competition between Tabcorp and Tatts in a market segment where the corporate bookmakers are not a competitive constraint.

4.71. In summary, the ACCC considers that Tabcorp and Tatts compete closely and there are many factors that limit the ability of the corporate bookmakers to challenge the incumbent positions that Tabcorp and Tatts hold (in particular access to media rights which is discussed later in this report).

Removal of a close competitor in bidding processes for wagering licences

4.72. Tabcorp and Tatts hold the exclusive rights to supply totalisator and retail wagering services in each of the states and territories in Australia, with the exception of Western Australia (which remains state-owned).

4.73. As the only incumbent totalisator and retail wagering providers, Tabcorp and Tatts are likely to be each other's closest competitors, and potentially the only credible

[91] Freeman at [279].

[92] References here to "day-to-day" competition put aside issues such as bidding for licences which are discussed later in this report.

[93] Mellsop, Figure 3.

[94] Tyshing at [379] and [384].

[95] Mellsop at [244].

bidders, for these wagering licences. With the proposed acquisition, Tabcorp will have a virtual monopoly of retail wagering and totalisator operations in Australia.[96]

4.74. There are two potential bidding opportunities which could arise prior to 2035:

- The potential privatisation of the WA TAB[97]
- The Victorian retail and totalisator wagering licence in 2024.[98]

4.75. Evidence given by Tatts suggests that if the proposed acquisition did not proceed, Tatts would likely be interested in bidding for both the WA TAB and the Victorian licence.[99] Therefore the proposed acquisition removes Tatts as a competitor to Tabcorp for these licences.

4.76. Tabcorp submits that, despite the removal of Tatts from any future bidding process, it would not lead to public detriment. This is based on the view that: (i) there are several parties beyond the merger parties that could be considered credible bidders, and (ii) state governments have the ability to optimise the outcomes of such competitive processes.[100] These factors are discussed below.

Existence of credible alternative bidders

4.77. Tabcorp claims that "[t]here are several parties beyond Tabcorp and Tatts, including large and well-credentialed overseas wagering operators, that would have strong interests in participating" in relation to the two bidding opportunities identified above.[101]

4.78. Industry participants including Mr Simon Barrile (General Counsel of Racing Victoria), as well as Mr Mellsop, consider that Tabcorp and Tatts have incumbency advantages that may act as a deterrent to other potential bidders.[102] If the merger proceeds, it is likely the merged entity will be the only credible bidder due to its:

- Retail wagering and totalisator experience and expertise in Australia
- Sunk investments in retail and totalisator wagering[103]
- Access to key inputs needed to supply the services including access to totalisator pools and racing vision.[104]

4.79. As outlined above, racing vision is a key input needed to operate a retail wagering network. As the dominant racing broadcaster, Tabcorp through its ownership of Sky has the ability to either withhold access to vision completely or set unreasonable commercial terms for the supply of Sky. This creates significant uncertainty for the ability of a potential competitive bidder to access vision, which may mean that otherwise credible bidders are unwilling to attempt to enter the market.

4.80. These factors are likely to significantly hinder the ability of competitors to credibly bid for retail wagering licences, and therefore impact on their decision whether to bid. The following evidence suggests that there are unlikely to be any other credible bidders for these wagering licences.

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[96] Hines at [50].

[97] Form S, [19.3], page 122; TBP.004.003.6960 [Tabcorp section 155 document].

[98] Form S, [19.3], page 122; TBP.004.019.7611; TBP.004.003.6960 [Tabcorp section 155 documents].

[99] Cooke at [180] and [202]; TAT.001.003.0016 [Tatts section 155 document].

[100] Form S at [19.4], page 122.

[101] Form S at [19.4], page 122.

[102] Barrile at [17]; Mellsop [171].

[103] Hines at [52]-[53].

[104] Hines at [52]-[53].

4.81. Ladbrokes considers it would be unlikely to bid for retail wagering licences in the future unless it could obtain access to vision of a significant number of races around the country at a commercially reasonable rate.[105] In particular, if Sky was to win the Victorian media rights in 2020, Ladbrokes would be significantly less likely to bid for the Victorian retail wagering licence in 2024.[106] Likewise, with respect to the WA TAB, Ladbrokes again would be unlikely to bid unless it could ensure access to pooling services and access to Western Australian racing content.[107] Relevantly, Ladbrokes withdrew from the competitive bidding process for the Victorian 2012 licence.[108]

4.82. [**HIGHLY Confidential to CrownBet**] [redacted].[109]

4.83. Betfair Australia considers it unlikely that it will bid for a retail wagering licence because firstly, as a low margin operator, it is unlikely to be able to cover the higher costs involved in running a retail network and secondly, because its betting exchange services a "niche" customer that would not transact via a retail network.[110]

4.84. Recent bidding processes, in Victoria and ACTTAB, and comments in relation to the privatisation process for the WA TAB, support that Tabcorp and Tatts are the only two credible bidders for retail and totalisator wagering licences:

- The 2012 bidding process for the Victorian retail and totalisator wagering licence highlights the importance of competition between Tabcorp and Tatts. Racing Victoria is of the view that Tatts and Tabcorp were the only participants in the 2012 process that possessed "the attributes, business capacity and interest to acquire and operate the Victorian retail network and pari-mutuel pool" and "only Tatts, [Tabcorp's] closest competitor, provided a fully compliant rival bid."[111]
- The bidding process for the sale of the ACTTAB in 2014 also suggests that Tabcorp and Tatts are the most credible bidders for wagering licences. The Auditor-General's report regarding the sale makes clear that while there were five interested parties at the expression of interest stage, the operational capacity of the other three parties failed to satisfy the requisite criteria.[112] In particular, the other parties did not have existing pari-mutuel pools and it considered they had low likelihood of entering into a pooling arrangement on reasonable terms. The ACT Government Sale Project Team therefore considered it was inevitable that only Tabcorp and Tatts, as the only two operators of totalisator pools in Australia, could proceed to the next stage.[113]
- Commentary from the Western Australian government in 2016 regarding the potential privatisation of the WA TAB also indicates there is a view that "there are only two purchasers in this".[114] This is contrary to Tabcorp's submission that

[105] Brown at [28(a)].

[106] Brown at [28(c)(ii)].

[107] Brown at [29(a)]-[29(b)].

[108] Barrile at [23].

[109] Tyshing at [454].

[110] Statement of Timothy Moore-Barton, Chief Executive Officer of Betfair, dated 13 April 2017 (**Moore-Barton**) at [82].

[111] Barrile at [29].

[112] Attenborough, Tab 19 of Exhibit DA-1, Auditor-General's report regarding the sale of the ACTTAB (Report No 7/2015) dated 26 June 2015 [TBP.011.001.2808], pages 67, 68, 72.

[113] Attenborough, Tab 19 of Exhibit DA-1, page 70.

[114] Media report titled "Western Australia rift over TAB sell-off" – Sydney Morning Herald, 18 May 2016, TBP.011.001.2111 – DA -1.16.

there are other credible bidders likely to participate in any competitive bidding process for the WATAB.

4.85. Racing Victoria is concerned that the proposed merger would remove the only other serious bidder to Tabcorp for the 2024 retail and totalisator wagering licence. Mr Andrew Twaits, Managing Principal of The Strategy Canvas, considers that Tabcorp and Tatts would be the only two likely bidders as in his view, it is "unlikely that any new entrant would be able to balance the operational and commercial requirements needed to generate sufficient returns to maintain the funding requirements of the racing industry or provide adequate service to the punting community in the time frames it would be subject to."[115] This view is consistent with the evidence of CrownBet, Ladbrokes and Betfair Australia (as outlined above).

Countervailing power of state governments

4.86. Tabcorp contends that state governments have the ability to optimise the outcomes of competitive retail wagering licensing and privatisation processes.[116]

4.87. Mr Flavio Menezes, Professor of Economics at the University of Queensland, outlines that a "strategic seller" has a number of options available to promote competition in the auction (licensing process) and increase their expected revenue.[117] He assesses both the Victorian and Western Australian governments to be strategic sellers.[118]

4.88. In Mr Menezes view, potential strategies available to strategic sellers include:

- Setting an optimal reserve price
- Selling an exclusive licence for a period that is sufficiently long to attract new entry
- Structuring the format of the auction to encourage entry.[119]

4.89. Other evidence filed with the Tribunal raises doubt as to the effectiveness of any actions governments could take to increase the value of licences when there are likely to be limited bidders.

4.90. Mr Twaits is of the view that setting a reserve price is an "impractical" strategy as it could effectively result in the licence reverting back to government ownership, if no bidding parties agree to meet the reserve price.[120]

4.91. Mr Mellsop also disagrees with certain aspects of Mr Menezes evidence, and concludes that:

I am also concerned that the proposed transaction would merge the likely two strongest bidders for the 2024 Victorian tote licence, and that this would:

a) Lower the expected selling price for the licence; and

b) Possibly result in less favourable (funding) arrangements for the Victorian racing industry, lower quality, and productive inefficiency.

Similar concerns exist in respect of the proposed privatisation of the Racing and Wagering Western Australia (RWWA), although I think the issues are less acute.[121]

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[115] Statement of Andrew Twaits, Managing Principal of The Strategy Canvas, dated 19 April 2017 (**Twaits**) at [63].

[116] Form S at [19.4], page 122.

[117] A seller that designs the auction rules, including the reserve price, to maximise their expected revenue from the auction or to achieve another specific objective such as economic efficiency – see Statement of Flavio Menezes, Professor of Economics at University of Queensland, dated 9 March 2017 (**Menezes**) at [73].

[118] Menezes at [175]-[181] and [228].

[119] Menezes at [73]-[77].

[120] Twaits at [68].

Impacts on the racing industry

4.92. The end result of any licensing/bidding process has flow on effects for the racing industry. In the majority of the states and territories in which they hold the totalisator licences, both Tabcorp and Tatts are required to make significant contributions to the racing industry in that jurisdiction.[122]

4.93. It was a key element of the 2012 Victorian licensing process that the funding to the Victorian racing industry was to be on "no less favourable" terms than those existing under the previous licence.[123] Both Tabcorp and Tatts' offers were predicated on benefits to both the State of Victoria and the Victorian racing industry, with the scale of the benefit believed to stem from the competitive tension within the process.[124]

4.94. The removal of Tatts from a future competitive bidding process for a wagering totalisator therefore could result in significant flow on effects for the racing industry. With only one credible bidder, there is no certainty that terms of the licence will be as favourable to the racing industry as those that could be generated in a competitive bidding process.

Impact on price and non-price terms

4.95. The lack of close competitors or credible alternative bidders to the merged entity will impact on both the price and non-price terms able to be achieved by governments for their wagering licences. Although state governments may have a certain degree of countervailing power, any such power is unlikely to offset the anti-competitive effects of the proposed acquisition.

4.96. While state governments may be able to engage in the strategies put forward by Mr Menezes to ensure an acceptable price, this does not account for the fact that competitive tension between two (or more) competing bidders may still result in a significantly greater price or improved offering. As an example, the recent sale of ACTTAB realised $105.5 million for the territory, with the Auditor-General noting that this "far exceeded expectations".[125] As outlined above, only Tabcorp and Tatts progressed to the "bid stage" for this asset.

Access to pooling services

4.97. Totalisator operators establish 'totalisator pools' for individual racing events and for each bet type. Operators consolidate all totalisator bets they accept into the pool created for that event and bet type.

4.98. Totalisator pools can be standalone, in which case only one totalisator operator manages the pool and only bets made with that operator are placed in the pool. Alternatively, a totalisator operator (the 'host') may offer a pooling service to one or more other totalisator operators (the 'guest'). This allows the guest to combine (co-mingle) their totalisator pool with the host's pool. Generally, the host has a larger totalisator pool.[126] The three totalisator pools in Australia are:

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[121] Mellsop at [17]-[18].

[122] Freeman statement at [229]-[230].

[123] Department of Treasury and Finance, Review of the wagering tax rate post 16 August 2012, http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Review-of-the-wagering-tax-rate-post-16-August-2012.

[124] [**HIGHLY Confidential to Tatts**] [redacted]; Department of Treasury and Finance, Review of the wagering tax rate post 16 August 2012.

[125] Auditor-General's report regarding the sale of the ACTTAB (Report No 7/2015) dated 26 June 2015: TBP.011.001.2808 - page 1.

[126] Freeman at [141] as cited in the Annexure A to the Form S at [136], page 171.

- The SuperTAB pool (operated by Tabcorp): A combination of the Victorian, ACT and WA totalisators pools. The SuperTAB pool also co-mingles with certain other international pools.
- NSWTAB (operated by Tabcorp): A combination of the NSW totalisator pool with certain other international pools.
- UBET (operated by Tatts): A combination of all totalisator pools in states and territories where Tatts holds the totalisator licence – Queensland, South Australia, Tasmania and Northern Territory.[127]

4.99. The benefit of pooling arrangements is that they increase the size and therefore stability and liquidity of totalisator pools.[128]

4.100. A totalisator operator in Australia, particularly in any of the smaller jurisdictions by reference to wagering turnover, is likely to need to acquire pooling services. An inability to enter into pooling arrangements at all, or on reasonable commercial terms, may materially affect both the competitiveness and viability of a totalisator operator. Further, where pooling services are not offered, or are offered on unreasonable terms, this could increase the barriers to entry into the wagering market by deterring or preventing other wagering operators from bidding for an exclusive totalisator licence.

4.101. Tabcorp currently provides pooling services to a third-party totalisator, RWWA, the operator of the WA TAB. Tabcorp also co-mingles with international totalisator operators. Tabcorp obtains a fee for providing pooling services.[129] Tatts currently does not provide pooling services to any third parties in Australia or internationally.[130]

4.102. Tabcorp and RWWA's current pooling agreement expires in 2024.[131] Access to competitive pooling services beyond 2024 is important to RWWA and, in the event of privatisation, any non-government operator of the WA TAB.[132] RWWA (or any future operator of the WA TAB) would not be able to operate a standalone pool for the WA TAB as it lacks sufficient liquidity. Opportunities to pool with international jurisdictions to increase liquidity may be limited by the extent to which international jurisdictions already pool into the SuperTAB and NSWTAB pools.

4.103. RWWA has expressed concerns in relation to the proposed acquisition about whether RWWA will continue to have access to pooling services (during the remaining term of the existing pooling agreement and after its expiry in 2024).[133] [**HIGHLY Confidential to Tabcorp**] [redacted].[134]

4.104. Mr Tyshing states that any corporate bookmaker contemplating a future bid for an exclusive totalisator licence would need to acquire pooling services.[135] Corporate bookmakers would require access to pooling services to operate a totalisator effectively and access large pools with high liquidity.[136] Mr Tyshing identifies concerns

[127] Freeman at [143] as cited in the Form S at [4.16], pages 20-21.

[128] See Annexure A to the Form S at [143] for a list of benefits Tabcorp identified in relation to accessing large totalisator pools.

[129] Freeman at [158] as cited in Annexure A to the Form S at [142], page 174.

[130] Freeman at [143(b)] and Cooke at [35] and [168] as cited in Annexure A to the Form S at [138].

[131] Statement of Richard Burt, Chief Executive Officer of RWWA, dated 7 March 2017 (**Burt**) at [36(a)].

[132] Burt at [36(a)].

[133] RWWA submission to the Tribunal at [2.1(a)].

[134] Freeman, Tab 3 of Highly Confidential Exhibit DF-3.36: Letter RWWA sent to Tabcorp on 27 January 2017 [TBP.001.018.6430].

[135] Tyshing at [281].

[136] Tyshing at [447].

about a corporate bookmaker's ability to secure pooling from the merged entity at [447-449].[137]

If they were not able to secure a suitable pooling arrangement from the merged entity prior to bidding, the bookmaker would most likely be unable to put forward a competitive bid. If they were successful in their bid but were subsequently unable to secure a suitable pooling arrangement from the merged entity, the additional risk that the bookmaker would bear would likely impede its ability to offer a competitive totalisator offering.[138]

4.105. Mr Brown states "LDA would be unlikely to bid for a Western Australian retail wagering licence unless it could ensure that it would be able to pool those totalisator operations with those in other States on commercially reasonable terms in order to establish the critical mass necessary to operate a totalisator successfully".[139]

4.106. The proposed acquisition removes Tatts as the only other operator of a totalisator pool in Australia. Consequently, as outlined below, the proposed acquisition removes Tatts as a potential:

- Competing provider of pooling services to third-party totalisator operators
- Competitive constraint on Tabcorp when Tabcorp is negotiating third party pooling arrangements with third party totalisator operators.

4.107. To provide pooling services, a totalisator operator must have the globally accepted protocol for inter-tote communications, Inter-Tote System Protocol (**ITSP**) technology.[140] The ACCC understands Tatts does not have ITSP technology as it does not currently provide pooling services but it may have a commercial incentive to obtain the technology in the future. [**HIGHLY Confidential to Tatts**] [redacted]

[redacted]][142]

4.108. [**HIGHLY Confidential to Tabcorp**] [redacted]:

[redacted] *143*

4.109. [**HIGHLY Confidential to Tatts**] [redacted]

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[137] Tyshing at [447]-[449].

[138] Tyshing at [448].

[139] Brown at [29(b)].

[140] See Annexure A to the Form S at [126], [140] and [145] for Tabcorp's views on other necessary approvals and barriers to combining totalisator pools.

[141] TAT.001.001.0280; TAT.001.003.1173. [Tatts section 155 documents].

[142] TAT.001.003.1173 [Tatts section 155 document].

[143] Freeman, Tab 36 of Highly Confidential Exhibit DF-3 [TBP.001.018.6430].

[redacted][144]

Tabcorp's commitments to RWWA

4.110. In response to RWWA's concerns about ongoing access to pooling services, Tabcorp and RWWA have entered into confidential arrangements in the Deed (Commitment to Long Term Pooling Deed) annexed to this report as **Highly Confidential Annexure A.**[145]

4.111. RWWA considers that the Deed substantially, but not fully, addresses RWWA's concerns.[146] In its submission to the Tribunal, RWWA stated in relation to the Deed:

> *RWWA continues to have concerns that the proposed merger may have effects on competition in relation to access to pooling services and, consequently, the viability of competition in the market for the acquisition of the WA state-based wagering licence, but it believes that its concerns have been addressed to the extent possible since RWWA lodged the Submissions [that is, submissions to the ACCC during its informal merger review process].*[147]

4.112. RWWA's outstanding concerns with the Deed appear to be primarily related to the way in which the Deed deals with uncertain future market conditions. For example, according to RWWA, the Deed does not guarantee that RWWA, or a future acquirer of the WA TAB, will be able to secure an agreement for pooling services once the existing arrangement expires in August 2024.[148]

4.113. The ACCC is concerned Tabcorp is seeking to address a substantial competition concern, the loss of competition in pooling services, through a long-term behavioural commitment in a deed. The commitments are [**HIGHLY Confidential to Tabcorp**] [redacted]

4.114. It is unknown what [**HIGHLY Confidential to Tabcorp**] [redacted] This creates some uncertainty about the commencement and terms of any future pooling agreements.

4.115. It may be in the merged entity's interest to circumvent the long-term behavioural commitment in the Deed. For example, if a corporate bookmaker sought to acquire

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[144] TAT.001.016.0361 [Tatts section 155 document].

[145] RWWA submission to the Tribunal at [2.3], page 2.

[146] RWWA submission to the Tribunal at [3.2], page 2.

[147] RWWA submission to the Tribunal at [3.5], page 3.

[148] See RWWA submission to the Tribunal at [3.2(a)-(d)], page 2, for a full list of outstanding issues, which RWWA considers have not been addressed by the Deed. See also Twaits at [73] and [74], who provides his views on the proposed commitments to RWWA.

the licence in Western Australia, the merged entity may be able to find ways to circumvent its commitments. This could lead to there being no effective option for pooling for any future operator of the WA TAB.

Racing media

Introduction to racing media

4.116. Tabcorp's racing media business, Sky, holds the vast majority of rights for racing media content throughout Australia.[149] Sky acquires these rights from individual racing clubs or from PRAs who hold the aggregated media rights on behalf of the racing clubs they represent.[150] Mostly these rights are exclusive and bundled (i.e. Sky holds digital, free-to-air and subscription television rights). Sky is currently vertically integrated with Tabcorp's wagering operations, including its exclusive totalisator/retail licences in the Tabcorp jurisdictions (Victoria, NSW and the ACT).

4.117. The proposed acquisition will result in the combination of Sky with Tatts' wagering operations, including Tatts' exclusive totalisator/retail operations in Tatts retail jurisdictions (Queensland, South Australia, Tasmania and the Northern Territory). Therefore, following the acquisition, the merged entity will be vertically integrated as the dominant broadcaster of racing content and the totalisator/retail wagering operator in all states and territories (except Western Australia).

4.118. While Sky currently holds exclusive rights to the majority of Australian racing content, there are several exceptions. Racing.com has acquired a non-exclusive right to digitally stream live coverage of Victorian thoroughbred racing and it sub-licences vision of those races to RWWA, Sportsbet, Ladbrokes, CrownBet, Betfair, Bet365 and William Hill.[151] William Hill has acquired the right to digitally stream NSW thoroughbred races.

4.119. There are a number of media rights that will be contestable in the foreseeable future, including:

- South Australia this year and again in seven years' time
- Queensland in 2020
- NSW in 2025
- Tasmania in 2026
- Perth Racing Club in 2022 or 2024
- the rest of WA at similar timing to Perth Racing
- various international jurisdictions, including New Zealand before 2020.[152]

4.120. When considering media issues, it is important to recognise that the amount of wagering turnover on a race is highly dependent on the coverage of the race.[153] Pre-race coverage (i.e. commentary on the field) piques the interest of punters. Live coverage of the actual race is also critical, as punters like to see what they have bet on. Having races televised in retail wagering outlets is very important, but coverage on free-to-air and pay-TV outside of retail wagering outlets also encourages more wagering. The ability to stream a race on a digital platform (such as online or via app)

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149 Catterall at [12].

150 Hines at [55]: "Individual race clubs own the rights to vision of their races. In nearly all cases clubs have assigned these rights to their PRA." As such, references to PRAs in this section of the report also incorporates individual racing clubs whose racing media rights are not held by the relevant PRA.

151 Catterall at [8(c)(ii)]; Hines at [77].

152 Catterall at [19].

153 Twaits at [78]; Freeman at [203].

also supports more wagering, as it enlivens the experience for online punters (particularly if at the time they are placing that bet they have no other way of viewing the race).

4.121. It is also important to recognise that the amount wagered on a race is critical to the PRAs, as wagering provides a significant portion of their revenue. Therefore it is in the interests of PRAs to maximise their coverage, whilst also obtaining maximum value for selling their media rights.

4.122. This section of the report is divided into the following topics:

- The relevant markets for considering racing media issues
- How there are high barriers for competitors to Sky, and how Sky's dominance in racing media also raises barriers to entry/expansion for corporate bookmakers, and therefore limits competition against Tabcorp in wagering
- How the proposed acquisition may lessen competition with Sky in bidding for racing media rights, cementing Sky's dominance.

Market definition for media issues

4.123. Tabcorp submits that racing media is an industry related to the wagering market, rather than a separate market relevant to the assessment of the proposed acquisition's effect on competition. Accordingly, Tabcorp does not support a market definition for the acquisition of media rights.[154] Expert reports provided by Tabcorp refer to a national market for television broadcasting to end consumers.[155]

4.124. While the ACCC supports the view that there is a significant degree of complementarity and interdependence between the wagering market and the racing media industry,[156] it disagrees that the market for the acquisition of media rights is not a relevant markets in its own right. The ACCC considers that there is a national market for the acquisition of racing media content and rights. There may be separate markets for each mode of delivery: (i) digital; (ii) free-to-air television; and (iii) domestic subscription television.

4.125. This view is supported by Mr Gregory Houston of HoustonKemp, who in his expert report also considers that the market or markets for the rights to show racing media content is a relevant market for the purposes of the proposed acquisition.[157] While he has articulated the market definition in slightly different terms, the ACCC does not consider this to have a substantive impact on the market in which the assessment is to be undertaken.

Barriers to competing with Sky and how Sky's dominance creates barriers to entry/expansion for corporate bookmakers

4.126. Competing acquirers and broadcasters of racing media rights face a number of significant barriers to entry/expansion. The difficulty of obtaining media rights in turn creates significant barriers to entry/expansion for the corporate bookmakers in wagering. As stated by Mr Houston:

"The ability to integrate racing media content with online wagering platforms is critical to driving online wagering activity, and so any firm that has access to such content is

[154] Form S at [18.1], page 112.

[155] Pleatsikas at [129]. Pleatsikas also identifies the state or substate markets for radio broadcasting to end users as relevant to the competitive effects of the proposed acquisition. The ACCC does not consider radio broadcasting to raise competition concerns regarding the proposed acquisition.

[156] Form S at [18.2], page 112.

[157] Report of Gregory Houston, Partner at HoustonKemp, dated 21 April 2017 (**Houston**) at [140].

at a significant competitive advantage. This competitive advantage is increased if fewer firms hold those rights, and greatest if they are held exclusively"[158]

4.127. Sky's ability to influence wagering turnover may deter PRAs from considering awarding their rights to a competitor. In order to successfully negotiate the acquisition of racing media rights from a racing body, it is critical for a new entrant to satisfy the rights holder that its racing content will continue to be distributed into the retail network (preferably on Sky Racing1).

4.128. As the dominant racing broadcaster, Sky exerts significant control over the programming of racing content and can determine when racing content is shown, whether it is shown on its primary wagering channel, demoted to its secondary wagering channel or otherwise "blacked out" and not shown at all.[159] This gives Sky competitive advantages when bidding for racing media rights, as the risk of such behaviour occurring may deter PRAs from licensing their rights to a competitor to Sky.[160] According to Mr Andrew Catterall, Chief Executive Officer of Racing.com, Sky has a proven ability to impact the wagering performance on a race event or entire season through:

- (In relation to residential subscription channels) - shifting live coverage of race meets to Sky Racing2 (which has an inferior audience to Sky Racing1 in home because it is an additional pay channel)
- (In relation to in venue channels) - moving the races from Sky Racing1 to Sky Racing2 (which has an inferior wagering performance and no audio in the retail outlets)
- Constraining lead in and lead out coverage around feature race events that are important for building wagering.[161]

4.129. Sky can also impact the wagering activity on races by influencing the broadcast schedule. Sky's position as broadcaster means that it has very significant influence in the scheduling of races. For example, scheduling a race (**Race A**) very shortly after a major race in another State typically negatively impacts the wagering performance of Race A as there is insufficient time for punters to "get interested" in the race. Sky can also schedule races at viewing times which attract a lower audience.

4.130. As noted by Mr Bullock, former CEO of TOTE Tasmania:

Changes on Sky can impact on your dividends overnight… even down to how much time they allot you. If they do not give you a couple of minutes running into your race your turnover can be down $10,000 or $20,000 and you are talking a minute.[162]

4.131. As a more extreme measure, Sky's control of racing programming also means that it has the ability to "black out" and refuse to screen particular racing content on either of its racing channels, which also has a substantial impact on wagering revenue.[163] For example, the 2014 black outs of Victorian Racing content, which "adversely impacted wagering turnover on Victorian Racing" and funding to the industry,[164] resulting in a negative impact on overall Victorian thoroughbred wagering turnover of approximately 5 per cent over this period.[165]

[158] Houston at [205].

[159] Moore-Barton at [68]; Catterall at [117]-[119].

[160] See further Houston at [282]; Hines at [81(e)].

[161] Catterall at [139].

[162] Joint Standing Committee – Environment, Resources and Development, Interim Report, Sale of the TOTE, April 2009 – Appendix 3; Attenborough, Tab 5 of Exhibit DA-1 [TBP.001.026.0161].

[163] Second Affidavit of Thompson at [88]; Catterall at [118], [124].

[164] Tyshing at [235]-[236].

[165] Twaits at [85].

4.132. Mr Catterall states that [**HIGHLY confidential to Racing.com**] [redacted]

[redacted][166]

4.133. When Sky engages in such conduct, it also loses a portion of wagering turnover from bets that would have been placed with Tabcorp, had vision of the blacked out races been available to punters. This reduction in wagering activity is damaging to the racing industry, competing wagering providers and Tabcorp itself. It appears that the main reason that Tabcorp has engaged in such conduct is to punish PRAs who may be looking to unbundle some of their rights and to deter PRAs from engaging in negotiations with other potential acquirers of media rights.

4.134. Tabcorp board documents indicate that it is Sky's strategy to [**Confidential to Tabcorp]** [redacted].[167]

4.135. Mr Catterall also outlines a number of additional barriers to entry and expansion faced by potential competing broadcasters.[168] In addition to the investment required to establish a competing broadcasting service, Mr Catterall notes that:

> *Sky has to date employed a strategy of acquiring exclusive bundled (domestic and international) rights across all racing codes – thoroughbred, greyhound and harness – with staggered start and end dates of its media rights agreements….Sky also imposes 'first and last' rights over future media bidding.*[169]

4.136. This strategy of seeking to acquire exclusive, bundled rights, refusing to sub-licence digital rights to other wagering services, and refusing to commit to accepting a sub-licence from an alternative bidder (i.e. a sub licence so that races can still be shown on Sky), limits other potential competitors from acquiring individual media rights (such as digital streaming rights).

4.137. The staggered expiry of these exclusive rights agreements also hinders a potential competitor from being able to acquire sufficient rights which could be aggregated to establish a viable racing channel in competition with Sky.

4.138. Tabcorp/Sky's ability to engage in much of this behaviour exists regardless of the proposed acquisition, but it is important to recognise that the barriers to bidding for media rights have a significant impact in the wagering market, for they limit the ability of the corporate bookmakers to expand/enter.

The proposed acquisition may lessen competition with Sky

4.139. Tabcorp considers that the proposed acquisition will result in the merged entity having an increased reliance on media rights to the benefit of racing media rights holders.[170] Tabcorp states that it has an incentive to reach agreement with media rights holders and to ensure vision is available in venues due to the strong complementarity between racing media and wagering. Tabcorp's incentive will be

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[166] Catterall at [49].

[167] Documents presented to the Tabcorp Board Strategy Meeting on 14 September 2016; [**HIGHLY Confidential to Tabcorp**] [redacted], page 136; Attenborough, Tab 1 of Highly Confidential Exhibit DA-2. [TBP.011.001.8697].

[168] See Catterall at [128]-[141].

[169] Catterall at [21].

[170] Form S at [18.32] and [18.33], page 117.

supplemented by the additional need to ensure vision is available in states where Tabcorp replaces Tatts as the relevant retail wagering operator. As a result, Tabcorp claims that this increased reliance "can only strengthen the commercial position of media rights owners in all relevant States".[171]

4.140. Several industry participants disagree with this assessment, and consider that the proposed acquisition will cement Sky's control of media rights, to the detriment of media rights holders; competition in wagering; and punters more generally due to lack of choice and access to racing vision.[172]

4.141. The competition issues that arise are complicated, and the ACCC has focussed on the impact the proposed acquisition is likely to have, rather than pre-existing competition issues. The key issues the ACCC has focussed on are:

- Whether Tatts is a potential competitor to Tabcorp in bidding for media rights, either on its own or in partnership with another industry participant
- Whether Tabcorp owning the Tatts retail wagering outlets in Tatts jurisdictions materially changes Tabcorp/Sky's position when negotiating for media rights
- The flow-on impacts if competition against Sky is lessened

Tatts as a rival bidder/counterweight to Sky in bidding for media rights

4.142. Tabcorp and some racing bodies contend that the proposed acquisition will not result in a reduction in competition in bidding for media rights.[173] Such a contention, in some cases, appears to be based on the fact that Tatts does not currently compete with Sky for the acquisition or broadcasting of media rights.[174]

4.143. However, without the proposed acquisition, some witnesses consider that Tatts is likely to have the incentive to emerge as either a potential rival bidder for media rights in future, or as a partner to other potential competing acquirers of media rights. Mr Houston considers that *"[a]fter Tabcorp, Tatts has the greatest need to show live races in retail wagering outlets…It follows that Tatts is a close potential competitor to Tabcorp in acquiring the right to show races in retail venues*."[175] This may be likely in jurisdictions where it has a retail footprint and commercial arrangements with the racing industry.[176]

4.144. Mr Catterall suggests that Tatts will be able to leverage its position as the retail wagering operator and primary wagering partner of the PRAs in Queensland, South Australia, the Northern Territory and Tasmania to credibly bid for media rights in these states.[177] Tatts' control of the retail network and ability to supplement its funding agreements with the PRAs in these states mean that it could emerge as a legitimate competitor to Sky.

4.145. While Tabcorp alleges that Tatts has not previously sought to compete against Sky to acquire rights to racing media content,[178] this may not be so in the future. As outlined by Mr Tyshing, absent the proposed acquisition, Tatts may be:

…more likely to bid for such rights in the future given that customers are increasingly migrating from retail to digital channels and it would not wish to be dependent on a

[171] Form S at [18.33], page 117.
[172] See further Catterall; Tyshing; Hines at [11(b)-(c)]; [78]-[89].
[173] Form S at [18.42]-[18.44]; V'landys at [31]; Gunston at [46]; Yovich at [59]; Dumesny at [82]; Watters at [36]; Corby at [57].
[174] V'landys at [31]; Dumesny at [82]; Watters at [36]; Corby at [57].
[175] Houston at [311].
[176] Tyshing at [411].
[177] Catterall at [36].
[178] Form S at [18.2], page 112.

key competitor for access to content and because it possess a retail network into which it could broadcast racing vision.[179]

4.146. Further, Mr Catterall explains that the reason Tatts has not sought to acquire media rights in the past is that Sky had already "tied up the exclusive media rights in Queensland, South Australia and the Northern Territory" before Tatts merged with UniTAB Limited in 2006 (becoming the retail wagering operator in these states), and "thus before it was large enough to have any chance of competing for media rights".[180]

4.147. Relevantly, Tatts has faced a number of difficulties related to its dealings with Sky, including Sky's promotion of Tabcorp's betting services. Mr Robert Cooke, Managing Director and Chief Executive Officer of Tatts, has recently spoken publicly about the difficulties Tatts has experienced differentiating its retail brand with Tabcorp's online brand. Tabcorp has a higher brand awareness in Queensland than Tatts' brand, UBET. Mr Catterall attributes these branding issues to the fact that Sky is the exclusive provider of vision available in Tatts' retail outlets. [181] Currently Tabcorp's online/telephone wagering services are advertised extensively via Sky in Tatts' retail wagering outlets.

4.148. In the past this may not have been of great concern to Tatts, as the majority of wagering was conducted in retail wagering outlets, so the advertising on Sky would have little impact. But as the rise in digital wagering has led to more and more customers wagering online via their smart-phones when in retail outlets or wagering from home while watching Sky on pay-TV, this will increasingly hurt Tatts' position. [182]

4.149. Tatts has also encountered difficulties with Sky regarding the fees charged for vision to its digital platforms.[183] When Sky and Tatts failed to reach agreement on such fees, Sky restricted its live feed from Tatts' UBET website and mobile app.[184]

4.150. The changing environment means that it will be increasingly in Tatts' interests to obtain racing media rights in the future. But even if Tatts does not bid for media rights, Mr Catterall considers that, without the proposed acquisition, the presence of Tatts as an entity of sufficient scale to support a competing broadcaster of racing content, imposes a competitive constraint on Tabcorp/Sky. [185]

4.151. Mr Catterall considers that partnering with Tatts for the distribution of vision through its retail network remains as a possible entry point for a competing broadcaster. He is of the view that, should the proposed acquisition not proceed, Tatts will have an incentive to work with Racing.com to:

- Introduce new and differentiated innovations that could be customised for Tatts' venues and ensure that the Tatts brand is exclusive at its venues
- Build the brand of UBET to a larger national audience to capture digital wagering account holders from outside of Tatts' states through advertising on competitor media services like Racing.com.[186]

4.152. The unique point that differentiates Tatts from a rival bidder for media rights is the ability to guarantee that the vision will be displayed effectively throughout its retail wagering network (which is approximately 1,400 retail wagering outlets, pubs and

[179] Tyshing at [413].

[180] Catterall at [35].

[181] Catterall at [29]; Annexure APC-4.

[182] See Catterall at [29] for a more detailed discussion of these difficulties; see also Tyshing at [413].

[183] Catterall at [33].

[184] Catterall at [33]; Annexure APC-5.

[185] Catterall at [32]; see also Second Affidavit of Thompson at [92]-[93].

[186] Catterall at [31].

clubs).[187] For example, it could ensure that a free-to-air racing channel rival to Sky will be displayed prominently in those outlets. In particular, it can guarantee to PRAs in Queensland, South Australia, Tasmania and Northern Territory that their races will be shown locally, which is an important factor in determining wagering turnover.

4.153. In this respect, Tatts acts as a counterweight to Tabcorp's ability to threaten to not show races on Sky if it does not receive exclusive bundled rights. At present, should Sky blackout or de-emphasise the content of a racing body in a Tatts jurisdiction, Tatts has an incentive to ensure the continued broadcast of the races (via non-Sky means) throughout its retail wagering outlet network to prevent any reduction in wagering activity.

Whether combining Tatts' totalisator/retail wagering operations with Sky lessens competition against Sky

4.154. Currently Tabcorp/Sky has exclusive retail licence and associated funding agreements in place in three of Australia's eight racing jurisdictions. Post-acquisition, the merged entity will hold this primary wagering relationship in seven of the eight Australian racing jurisdictions.

4.155. Mr Catterall, Mr Tyshing and Mr Hines are of the view that this increased economic and/or commercial integration with the merged entity will result in a reduced incentive for rights holders to unbundle rights or supply them (exclusively or non-exclusively) to Tabcorp/Sky's competitor.[188] This may occur as:

- PRAs in a formal joint venture with the merged entity will have a financial incentive to maximise wagering with the merged entity, as wagering revenue is ultimately shared with the PRAs. This is ultimately likely to result in the foreclosure of negotiations with competing broadcasters of media rights.[189]
- In particular, the suppliers of racing media rights in Queensland, South Australia, Northern Territory and Tasmania will have a direct commercial incentive to supply their rights to Sky as, post-acquisition, they will receive a proportion of turnover, profit or revenue on wagering conducted with the merged entity.[190]
- Sky/Tabcorp can "create a nexus between wagering activities and revenue from media rights".[191] As such, the merged entity can offer higher payments to PRAs for their media rights than they otherwise would as they can use mechanisms within the wagering joint venture to "claw back" a portion of the media rights payment.[192]

4.156. Racing.com considers that it will be able to compete on its merits against Sky to acquire media rights in Tatts jurisdictions. This is because its rival, Sky, will not be vertically integrated with the entity which holds the monopoly totalisator rights.[193] This may materially improve its chances of acquiring media rights in competition with Sky.[194] Mr Catterall is therefore of the view that this increased economic integration creates a '*dire'* predicament in terms of its long-term strategy to incrementally acquire the rights to thoroughbred racing vision in other jurisdictions in Australia, and to build up a credible alternative to Sky. [195]

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[187] Tyshing, Annexure NDT-61.

[188] See Catterall at [36]-[41]; Tyshing at [409]-[410].

[189] Tyshing at [409]; Houston at [292]-[293].

[190] Tyshing at [410].

[191] See Catterall at [38(b)].

[192] Catterall at [38].

[193] Catterall at [22]

[194] Catterall at [40]

[195] Catterall at [39].

4.157. Mr Hines considers that due to this increased integration between the PRAs and the merged entity, PRAs will be expected (and will see it as in their interests) to support the merged entity (as the totalisator/retail wagering operator in their state) in acquiring media rights and wagering. This is attributable to the importance of the relationship with the licensed wagering operator to each PRA. This in turn makes PRAs vulnerable if the relationship is damaged. Mr Hines provides the example that if the proposed acquisition proceeds, and Racing Queensland award their media rights to Racing.com (or even place Sky in a competitive bidding process), it would expose Racing Queensland to a number of potential disadvantages. Such disadvantages could include a risk of underinvestment by the merged entity into Queensland retail wagering outlets, which impacts on maintaining and growing revenue through the retail channel. The promise to upgrade technology or retail wagering outlets (or threat to delay upgrading) could be used by Tabcorp and Sky to influence media rights negotiations.[196]

4.158. As outlined above, Sky already enjoys competitive advantages when bidding for racing media rights, however, the ACCC considers that the acquisition may increase these advantages, particularly in relation to rights in the Tatts jurisdictions.

4.159. After the acquisition, the PRAs in the Tatts jurisdictions will become dependent on Tabcorp for significant portion of their funding. While the funding arrangements are set out in agreements, this dependence makes it difficult for PRAs to consider any options other than Sky.

4.160. While Tabcorp contends that, despite the current vertical integration with Sky and the wagering operator in their respective states, PRAs in Victoria and NSW have provided their rights to competitors to Sky/Tabcorp, it is important to note that NSW and Victoria are the largest wagering jurisdictions. Their PRAs have significantly more bargaining power than smaller racing bodies.[197]

Flow on effects of lessening of competition with Sky

4.161. A lessening of potential competitive constraint against Sky could have a range of flow-on detriments to a number of industry participants, including the racing industry, corporate bookmakers and punters. For example, it may lead to a lowering of the fees racing clubs are able to obtain for their media rights, due to the lack of competitive tension in negotiations. Such fees are an increasingly important part of industry funding.

4.162. There are also potential impacts on wagering competition. As outlined above, there is a strong interrelationship between racing media and competition in the wagering market. If rivals to Sky cannot grow and corporate bookmakers cannot access digital media rights due to Sky gaining exclusive bundled rights, the competitive threats to Tabcorp's wagering operations will be reduced.[198] Given the increasing popularity of digital wagering, digital media rights are likely to become of increased importance over time.[199]

4.163. Preventing competitors from obtaining rights to racing vision may also impact on consumers and the racing industry by preventing access to racing vision for the wider public through free-to-air, television broadcast or more readily available online streaming.

Gaming

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[196] See Hines at [81(a)-(b)].

[197] Hines at [79].

[198] Hines at [86].

[199] Form S at [18.30], page 116.

Overview

4.164. In all states and territories in Australia, electronic gaming machines (EGMs, or colloquially, 'pokies') are available at licensed venues, except Western Australia where EGMs are only allowed at Crown Perth Casino.[200]

4.165. Tabcorp and Tatts supply EGM-related services to licensed venues. These services can be categorised as monitoring services, gaming systems and related services, and field services. Tabcorp and Tatts are not involved in manufacturing EGMs or the development of the various games played on EGMs.[201]

Monitoring services

4.166. In every state and territory except the ACT, relevant regulations require EGMs to be monitored for integrity and taxation purposes.[202] To facilitate this, EGMs in licensed venues must be connected to a monitoring system, which is typically provided by a commercial operator and is licensed by the relevant state or territory government.

4.167. Monitoring services include tracking and authorising the movement of EGMs, ensuring the correct functioning of EGMs and calculating the taxes payable by licensed venues.[203]

Gaming systems and related services

4.168. Gaming systems and related services comprise software and hardware designed to allow licensed venues to manage and enhance the operation of their EGMs. They include player loyalty programs, business intelligence software to analyse venue data, in-venue/multi-venue jackpot systems and cashless gaming solutions (e.g. ticket-in-ticket-out machines).[204]

4.169. Some gaming systems and related services can be provided on a stand-alone basis, although often venues acquire a bundle as part of an integrated solution.

Field services

4.170. Field services refer to repair and maintenance of EGMs and gaming systems.[205]

Relevant markets

4.171. The ACCC's view is that it is relevant to consider separate product markets for monitoring services, gaming systems and related services, and field services.[206] The ACCC agrees with Tabcorp's submission that there are likely to be state- and territory-based markets for the supply of these services to licensed venues.[207]

Tabcorp and Tatts gaming businesses

4.172. Tabcorp's gaming services business comprises Odyssey Gaming (**Odyssey**), eBET Gaming Systems (**eBET**)[208,] and Tabcorp Gaming Systems (**TGS**). Tatts provides

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[200] Form S at [4.73], page 31.

[201] Form S at [4.68], page 30.

[202] Form S at [4.88], page 35.

[203] Statement of Rytenskild, Chief Operating Officer - Keno & Gaming at Tabcorp dated 8 March 2017 (**Rytenskild**) at [222] as cited in the Form S at [4.89], page 35.

[204] Form S at [4.70], [4.71], [4.83], [4.84], [4.85] and [4.86], pages 30-34.

[205] Form S at [4.87], page 35..

[206] Form S at [5.16], page 52.

[207] Form S at [5.13], page 52.

[208] Tabcorp acquired eBET and Odyssey when it acquired Intecq in December 2016.

gaming services through its gaming business known as MAX, which comprises, Maxgaming and Bytecraft.

4.173. Tabcorp's and Tatts' gaming services businesses supply services in Queensland, NSW and Victoria as follows:

- In Queensland:
  a) Odyssey and Maxgaming supply monitoring services and field services
  b) eBET and Maxgaming supply gaming systems and related services
- In NSW:
  a) Maxgaming holds the exclusive licence to supply monitoring services
  b) eBET, TGS and Maxgaming supply gaming systems and related services
  c) TGS and Bytecraft supply field services[209]
- In Victoria:
  a) eBET, TGS and Maxgaming supply gaming systems and related services
  b) TGS and Bytecraft supply field services.[210]

Merger of the only two active monitoring service providers in Queensland

4.174. In Queensland, there are currently two active suppliers of monitoring services, one owned by Tabcorp (Odyssey) and one owned by Tatts (Maxgaming). Tabcorp and Tatts both also supply gaming systems and related services.

4.175. Tabcorp has proposed, as a condition of authorisation, to divest Odyssey to address potential competition concerns arising from the combination of Maxgaming and Odyssey.

4.176. An issue for consideration is whether Tabcorp's proposed divestment of Odyssey is likely to effectively address the detriments arising from the combination of the two active suppliers of monitoring services in Queensland.

4.177. As part of its authorisation application, Tabcorp offered to divest the Odyssey business if the Tribunal has concerns in relation to the supply of EGM monitoring and repair and maintenance services in Queensland.[211] Tabcorp provided a draft section 87B undertaking at Annexure E to the Form S, which amongst other things, requires the ACCC to approve the potential purchaser.[212] On 14 April 2017, Tabcorp entered into an agreement with Australian National Hotels Pty Limited (Federal Group) for the sale of Odyssey. The ACCC received copies of the confidential sale documents on 19 April 2017.

4.178. The ACCC still needs to consider:

- The confidential sale agreement documents in greater detail

[209] eBET provides software support for its gaming system but does not provide any hardware repairs for EGMs. See Rytenskild at [154].

[210] eBET provides software support for its gaming system but does not provide any hardware repairs for EGMs. See Rytenskild at [154].

[211] Form S at [4.103], page 38.

[212] Under section 95AZJ(1) of the Act, the Tribunal may grant an authorisation subject to such conditions as are specified in the authorisation. Section 95AZJ(2) provides that authorisation may be subject to the condition that the person to whom the authorisation is granted must take, and comply with, an undertaking to the ACCC under section 87B of the Act. Section 87B of the Act allows the ACCC to accept a written undertaking given by a person in connection with a merger authorisation. Section 87B undertakings are binding agreements that are given statutory force and effect by section 87B of the Act. If the ACCC considers that a person who gave such an undertaking has breached any of its terms, the ACCC can apply to the court for a range of orders.

- The appropriateness of Federal Group as the proposed purchaser[213]
- Whether the updated terms of the proposed section 87B undertaking, a copy of which is still to be provided by Tabcorp, are sufficient to ensure the key terms of the proposed divestment are enforceable.

4.179. There remains concerns among industry participants regarding Odyssey's potential loss of exclusivity should the new purchaser choose to offer a new in-venue gaming system which competes with Maxgaming,[214] and the data that may be available to the merged entity after the sale of Odyssey.[215] However, market participants have not been provided with a copy of the confidential sale agreements, only certain information about the overall agreement as provided by Tabcorp.

4.180. When the ACCC has completed its assessment of the proposed divestment and Federal Group as the proposed purchaser, it proposes to file a supplementary report if it identifies any concerns on those issues.

Exclusive monitoring operator and largest supplier of gaming systems in NSW

4.181. Currently in NSW, Tatts (via Maxgaming) is the exclusive licensed monitoring operator, while Tabcorp (via eBET and TGS) is the largest supplier of gaming systems and related services.

4.182. There are two potential issues with the merged entity being the exclusive supplier of monitoring services and the largest supplier of gaming systems and related services to licensed venues in NSW following the proposed acquisition. These issues relate to whether the merged entity would have the ability and incentive to use its position as the licensed monitoring operator to obtain a competitive advantage, and potentially foreclose competitors, in gaming systems and related services by either:

- Misusing commercially sensitive information collected in the course of supplying monitoring services
- Restricting the operation or functionality of third-party gaming systems and related services.

Potential misuse of commercially sensitive information

Information collected through Maxgaming's monitoring system

4.183. Maxgaming's monitoring system collects information about each EGM, in each licensed venue in NSW including:

- The type of EGM[216]
- How that EGM is set up (e.g. the game, denomination, jackpot configuration and return-to-player percentages)[217]
- How frequently the EGM is being played and at what times[218]

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[213] When the ACCC considers whether to accept a section 87B undertaking for the divestment of a business in its informal merger review process, it undertakes a formal assessment of the proposed purchaser. The factors the ACCC will have regard to in making its decision on whether to approve or reject Federal Group as the purchaser of Odyssey include, the independence of Federal Group from Tabcorp, whether Federal Group is of good financial standing, whether Federal Group intends to maintain and operate Odyssey as a going concern and is able to conduct Odyssey effectively, and whether the divestiture of Odyssey to Federal Group will address the ACCC's competition concerns (and not in itself raise any competition concerns).

[214] Wright at [34]-[38]; Costain at [29]-[30].

[215] Wright at [39]-[43].

[216] White at [25].

[217] White at [25].

- Metering data—transactional data associated with an EGM such turnover, wins and payouts[219]
- Events data—data relating to certain activities of an EGM that could give rise to potential security issues including EGM malfunctions and door openings.[220]

Tabcorp's access to gaming information with and without the proposed acquisition

4.184. Following the proposed acquisition, Tabcorp will have access to a significantly larger amount of commercially sensitive information because it will have access to the raw information about EGMs in *all* licensed venues in NSW, not just the information that it collects about venues that acquire TGS' and eBET's gaming systems and related services.

4.185. Tabcorp claims the raw nature of data collected from the monitoring system would be of limited utility to gaming services providers other than the licensed monitoring operator.[221] However, from the raw information, it is possible to determine the profitability of individual EGMs and of a venue's EGM operations as a whole.[222] This type of information could be valuable to Tabcorp's TGS business, which provides consultancy advice and services to licensed venues to improve the profitability of their gaming operations such as advice on the set up of their gaming floor, the return to player setting on an EGM (which a venue can adjust) and marketing strategies.[223] In relation to the commercial value of this information to TGS, Mr White states:

> *[TGS' access to the monitoring information] will allow TGS to improve the profitability of its clients' venues by copying the gaming operations of clubs with successful gaming operations, at the expense of clubs that do not use TGS's gaming services. This will give TGS an unfair competitive advantage over other providers of gaming services. It will also give clubs that retain TGS's services an unfair advantage over independent clubs that do not retain TGS's services, as they will get the benefit of informed decisions based on commercially valuable data…*[224]

4.186. Mr White also comments that by TGS improving the gaming performance of its existing customers, it may enable TGS to sign up more customers.[225] Tabcorp has been expanding its TGS business in NSW since entering in 2013. In the 2014 financial year, TGS had 118 EGMs under contract. This increased to 1974 EGMs in the 2016 financial year.[226]

4.187. Tabcorp claims that concerns about misusing commercially sensitive information from the monitoring system are inconsistent with market experience. Tabcorp argues that if Maxgaming had been able to leverage its position as the licensed monitoring operator, one would expect it to have done so and, as a result, it would have a substantially larger position in the supply of gaming systems in NSW.[227]

4.188. However, Maxgaming's gaming systems and related services operations in NSW differ from those of TGS for the following reasons:

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[218] White at [25].

[219] Rytenskild at [236] as cited in the Form S at [16.9], page 106.

[220] Rytenskild at [236] as cited in the Form S at [16.9], page 106.

[221] Rytenskild at [238] as cited in the Form S at [16.11], page 106.

[222] White at [26].

[223] White at [29].

[224] White at [29].

[225] White at [31].

[226] Annexure B to the Form S, page 71.

[227] Form S at [16.7], page 106.

- Maxgaming supplies a loyalty-based gaming system to only one pilot site in NSW and it does not proactively market gaming systems to customers.[228]
- Maxgaming does not provide consultancy advice and services to licensed venues to improve the profitability of their gaming operations.

4.189. For these reasons, the monitoring system information may not be as commercially valuable to Maxgaming's gaming systems and related services operations as compared to TGS.

Regulatory and contractual restrictions

4.190. Tabcorp has identified the following provisions in the *Gaming Machines Act 2001* (NSW) (the **Gaming Machines Act**) to support its position that the merged entity would neither have the ability nor incentive to misuse commercially sensitive data and information collected from the monitoring system:

- Section 139(1): all rights associated with monitoring system information[229] are vested in the Crown[230]
- Section 139(2): the licensee must not use or divulge information to any person without the written consent of the Minister or as otherwise authorised in accordance with the licence, the Gaming Machines Act or the regulations[231]
- Section 136B(b): the licensee must not use the monitoring system infrastructure or information otherwise than in accordance with the Gaming Machines Act, the regulations or the licence.[232]

4.191. Sections 139(2) and 136B(b) of the Gaming Machines Act are likely to be the most relevant legislative provisions at restricting the licensed monitoring operator in NSW from using or disclosing the information it collects. The ACCC understands that for breaches of section 139(2), a penalty of $11,000 can be imposed by the court. Also, for breaches of sections 139(2) and 136, the relevant Minister can take 'disciplinary action' which may result in:

- A penalty of up to $250,000 plus $50,000 for each day the contravention continues[233]
- Cancellation or suspension of the licence.[234]

4.192. Tabcorp submits that a breach of the relevant legislation could expose it to substantial pecuniary penalties and/or suspensions or cancellation of the licence. As its licences are its most valuable assets, Tabcorp submits that it will be highly motivated to ensure appropriate measures are in place to ensure a breach would not occur.[235]

4.193. Tabcorp and Tatts also claim there are restrictions on the use of monitoring system information in Maxgaming's monitoring licence.[236] The ACCC only received a copy of Maxgaming's monitoring licence in NSW on 24 April 2017, and is continuing to consider the restrictions. Tatts has a licence that is currently in operation but which

[228] Statement of Frank Makryllos, Chief Operating Officer - Gaming, dated 9 March 2017 (**Makryllos**) at [82(c)]. Note that Tatts also holds the exclusive licence to supply a state-wide linked jackpot service.

[229] The term 'central monitoring system information' is defined in section 4 of the Gaming Machines Act.

[230] Form S at [16.4], page 105.

[231] Rytenskild at [240].

[232] Rytenskild at [240].

[233] Section 132A of the *Gaming Machine Regulations 2010* (NSW); sections 172(1)(b1) and (2) of the Gaming Machines Act.

[234] Sections 172(1)(a) and (2) of the Gaming Machines Act.

[235] Rytenskild at [241].

[236] Makryllos at [25], Form S at [16.7], page 106.

expires on 30 November 2017 (**Current Licence**). A new licence commences on 1 December 2017 (**New Licence**).

4.194. [**HIGHLY Confidential to Tatts**] [redacted]

4.195. [**HIGHLY Confidential to Tatts**] [redacted]

4.196. The Minister is also able to take 'disciplinary action' under section 172(1) of the Gaming Machines Act, if a CMS licensee fails to comply with a condition of its licence.[239]

4.197. The ACCC notes that while there are penalties under the Gaming Machines Act for improperly using or disclosing information collected by the licensed monitoring operator, as well as restrictions under the monitoring licence, there may be considerable difficulty in detecting breaches of the relevant non-disclosure provisions which occur within a single corporate group. This may largely be a matter of self-reporting by Tabcorp.

Conditions

4.198. Tabcorp has been in discussions with ClubsNSW to establish an arrangement to address potential industry concerns about the use of information that may arise from the proposed acquisition.[240] [**HIGHLY Confidential to Tabcorp**] [redacted]. Tabcorp has also met with Liquor and Gaming NSW and [**Confidential to Tabcorp**] [redacted].[241]

4.199. To the extent the Tribunal considers that further protections to deal with the potential misuse of commercially sensitive information are required in NSW gaming, and that such protections would resolve the competition concerns, the ACCC does not consider long term behavioural commitments to be an appropriate solution. The ACCC has not had sufficient time to consider the [**HIGHLY Confidential to Tabcorp**] [redacted], and therefore it cannot comment on whether those particular commitments are likely to be effective at addressing any competition concerns. The ACCC's view is that long term behavioural commitments require ongoing monitoring and enforcement. Ideally, this might be handled by Liquor and Gaming NSW, however, it is very unlikely any possible additional regulation will be in place by the time of the Tribunal's decision.

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[237] [**HIGHLY Confidential to Tatts**] [redacted] filed with the Tribunal on 24 April 2016 in response to a notice issued pursuant to section 95AZD(1) of the Act.

[238] [**HIGHLY Confidential to Tatts**] [redacted] filed with the Tribunal on 24 April 2016 in response to a notice issued pursuant to section 95AZD(1) of the Act.

[239] Section 172(2)(d) of the Gaming Machines Act.

[240] Form S at [16.12], page 106.

[241] Form S at [16.13], page 107.

Interface between monitoring systems and gaming systems and related services

4.200. Currently in NSW, there is only one EGM operating system/protocol to connect EGMs to the monitoring system, the X-Series protocol.[242] With this operating system, a gaming system (such as eBET's Metropolis system) connects to the EGM via a separate port to the monitoring system. Hence, there is no connection between the monitoring system and gaming system.[243]

4.201. The NSW regulatory regime is changing to allow gaming venues to choose between the current operating system (X-Series) and two new EGM operating systems, QCom and G2S.[244] Similar to X-Series, [**HIGHLY Confidential to Tatts**] [redacted].[245] Comparatively, with the QCom protocol, gaming systems must connect to the EGM via the monitoring system.

4.202. QCom is used in all other Australian states and territories.[246] With this protocol, gaming system suppliers must develop their system to ensure it is compatible with the monitoring system.[247] However, generally, the licensed monitoring operator would provide an 'application programming interface' (**interface**), which would enable the gaming systems provider to ensure compatibility.[248]

4.203. The proposed acquisition combines the exclusive licensed monitoring operator, Maxgaming, with the largest supplier of gaming systems and related services, eBET. The merged entity, as the monitoring operator, may have an incentive not to facilitate the connection of third party gaming systems, in order to gain a competitive advantage in the supply of gaming systems and related services. For example, the merged entity could develop an interface to its own gaming system (such as eBET's Metropolis system) but not provide an interface to third party gaming systems or potentially do so on unreasonable terms and conditions. An example of this issue is the situation in Queensland, where gaming systems must connect to the EGM via the monitoring system but there is no requirement for a licensed monitoring operator to facilitate the connection. Tabcorp's Odyssey monitoring business only provides an interface to Tabcorp's own eBET gaming system, but not to any third party gaming systems. However, Tatts' Maxgaming business provides an interface to three third-party suppliers of gaming systems.[249]

4.204. Tabcorp claims there is no commercial incentive to foreclose third party suppliers of gaming systems and related services because any attempt would affect the relevant venue's operations, which will ultimately affect monitoring revenues.[250]

4.205. While the merged entity may not have an incentive to affect a licensed venue's operations, to the extent it has the ability to hinder or prevent a third party's gaming systems from interfacing, without impacting on a venue's operations, the merged entity may have an incentive to engage in such conduct. For example, this may occur in circumstances where a delay in connecting a third party supplier of gaming

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[242] Makryllos at [26(a)].

[243] Form S at [16.5], page 105.

[244] Makryllos at [26].

[245] [**HIGHLY Confidential to Tatts**] [redacted]

[246] Makryllos at [26(b)].

[247] Rytenskild at [206].

[248] Rytenskild at [206].

[249] Rytenskild at [208].

[250] Rytenskild at [250] as cited in the Form S at [16.6], page 106.

systems may result in a venue choosing to obtain those services from the merged entity (so the venue's operations may not be impacted).

Regulatory and contractual restrictions

4.206. Tatts claims Maxgaming will be [**Confidential to Tatts**] [redacted].[251] Tatts did not provide any evidence in support of this claim, [**Confidential to Tatts**] [redacted]. The ACCC has only received a copy of Maxgaming's monitoring licence in NSW on 24 April 2017.

4.207. Mr Rytenskild, Chief Operating Officer - Keno & Gaming at Tabcorp, cited section 136C of the Gaming Machines Act to support his claim that the licensed monitoring operator does not have the ability or incentive to foreclose competing suppliers of gaming systems and related services by preventing access to the monitoring hardware. Under section 136C the Minister may, by notice in writing, direct a licensed monitoring operator to provide additional specified services in relation to the management and operation of the monitoring system or the use of the monitoring system infrastructure or information.[252]

4.208. Mr Rytenskild also stated that under section 138 of the Gaming Machines Act, the Minister may alter the conditions of the licence by imposing an additional condition or by amending, substituting or revoking a condition.[253]

4.209. The ACCC is not in a position to comment on whether or not the Minister would use its powers under sections 136C and 138 to require Maxgaming to facilitate third party gaming systems.

Combination of the largest suppliers of field services

4.210. Bytecraft (Tatts) and TGS (Tabcorp) are the two largest suppliers of field services in Victoria with market shares of [**Confidential to Tatts**] [redacted] and 33 per cent, respectively.[254] Despite the significant market shares, the proposed acquisition should not lessen competition in this market because Bytecraft and TGS have different business models and therefore do not compete closely. Bytecraft provides standalone field services while TGS' field services are provided as part of a bundle of other gaming services (in TGS' 'full service solution').[255]

Other public detriments

Combination of the merger parties' customer information databases

4.211. The proposed acquisition appears likely to result in other public detriments. Following the proposed acquisition, the merged entity will have a significantly more extensive customer information database compared to the current database of either Tatts or Tabcorp. The merged entity would therefore have an increased ability to engage in customer profiling, targeted digital marketing and cross selling of a range of gambling products to customers on this database, which will inevitably include vulnerable problem gamblers.

[251] Makryllos at [27].

[252] Rytenskild at [249] as cited in the Form S at [16.6], page 106.

[253] Rytenskild at [250].

[254] Annexure B to the Form S, Part 5.2, pages 73-74; Annexure C to the Form S, Part 6, page 67.

[255] Rytenskild submitted that generally, TGS does not offer a de-bundled service. See Rytenskild at [157].

4.212. The ACCC is not in a position to assess the implications of the merged entity having access to a more extensive customer database but notes that this issue has been raised in evidence before the Tribunal.[256]

4.213. The ACCC also notes that the Productivity Commission's Inquiry Report into Gambling (2010) states that the risks of problem gambling are low for people who only play lotteries and scratchies, but rise steeply with the frequency of gambling on table games, wagering and, especially, gaming machines.[257] In that Report, the significant social cost of problem gambling was estimated by the Productivity Commission as at least $4.7 billion a year.

4.214. Recent research by the Australian National University found that problem gamblers tend to bet on a range of products – the average being four different products.[258] A separate study recently prepared for the NSW Office of Liquor, Gaming and Racing found that problem/moderate risk gamblers were most likely to have gambled on pokies (73 per cent) and horse/greyhound races (61 per cent), lottery products (54 per cent), scratchies (47 per cent) and keno (37 per cent).[259]

5. Public benefits

The public benefits section of this report has been separated into the following six topics:

- Claimed cost savings
- Claimed revenue increases
- Pass-through of costs savings and revenue increases
- Claims that the proposed acquisition addresses a free rider problem or underfunding problem
- Claims that the proposed acquisition will result in national pooling or creation of larger pools
- Use of a CGE model to estimate public benefits

Overview

5.1. Tabcorp claims that a number of direct quantifiable public benefits will result from the proposed acquisition, as it will lead to:

- Cost savings of [**Confidential to Tabcorp**] [redacted] p.a. by the third year following its completion
- Revenue increases of [**Confidential to Tabcorp**] [redacted] p.a. by the third year following its completion.[260]

5.2. These combined cost savings and revenue increases of approximately [**Confidential to Tabcorp**] [redacted] p.a. are claimed to lead to indirect public benefits as:

- 55 per cent[261] (or [**Confidential to Tabcorp**] [redacted] p.a.) will be passed through, to varying degrees, to racing bodies; sporting bodies; the Federal government; State governments; and pubs, clubs and agencies[262]

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[256] Tyshing at [374]; Freeman at [332]; Twaits at [104]; Mellsop at [200].

[257] Productivity Commission, *Inquiry Report, Gambling – Volume 1*, June 2010, page 2.

[258] Centre for Gambling Research- Australian National University, *2014 Survey on Gambling, Health and Wellbeing in the ACT*, Final Report, December 2015, page 50.

[259] Sposton, Hing & Palankay, *Prevalence of Gambling and Problem Gambling in New South Wales*, April 2012, Chapter 8.1.

[260] Form S at [21.1], page 125.

[261] Annexure A to the Form S at [303], page 97.

[262] Form S at [21.2], page 125.

- Those specific amounts passed through to racing industries will help to address a “free rider” problem associated with the funding of race meets[263]
- [**Confidential to Tabcorp**] [redacted] p.a. of the cost savings and [**Confidential to Tabcorp**] [redacted] p.a. of the revenue increases will flow through to other parts of the economy in a way that generates increases in GNI of $174.5 million and $179.5 million p.a. This estimate is derived from use of a CGE model.[264]

5.3. The relationship between these claimed public benefits is depicted in Figure 4 below. An important feature of these inter-relationships is that any concerns regarding the extent of the claimed direct cost saving and revenue increases will flow through to also create concerns about the extent of the indirect benefits, as depicted in Figure 4.

Figure 4 - Relationship between direct and indirect claimed benefits [**Confidential to Tabcorp**]

[redacted]

5.4. Tabcorp also claims that the proposed acquisition is likely to result in another public benefit by removing a commercial barrier to creating a national totalisator pool.

5.5. Whilst the proposed acquisition may result in some of the public benefits claimed, the magnitude and likelihood of the benefits are uncertain.

5.6. Regarding the claimed direct benefits:

- Some cost savings are likely to be achieved by removing duplication, though some of the savings estimates may overstate the benefit by, for example, including economic transfers and excluding integration costs
- It is unclear whether the revenue increases asserted by Tabcorp are public benefits for four reasons:
  - a) Gross revenue may not be an appropriate measure of welfare or surplus[265]
  - b) It seems likely the revenue increases could be achieved by Tatts without the proposed acquisition[266]
  - c) The costs of achieving these revenue increases have not been taken into account[267]

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[263] Simes at [98].

[264] Simes at [145], Table 2, and Attachment B, Table 1.

[265] Mellsop at [90] and [94].

[266] Houston part 5.3.3; Mellsop at [86b], [91]-[93] and [96].

[267] Mellsop at [86], [90] and [93].

d) Increased revenue from fixed odds betting increases yield for Tatts and means that consumers effectively pay more for less.[268]

5.7. Regarding the other claimed benefits:

- The pass-through of direct benefits to other parties should not be double-counted as additional benefits. However, the Tribunal may wish to consider what, if any, weight should be accorded to benefits which are passed through, depending on how widely they are shared.
- It seems unlikely that the proposed acquisition is the only avenue for correcting the claimed free rider problems, or achieving a national totalisator pool.

5.8. Finally, the GNI modelling is likely to be of little utility in assessing the public benefits flowing from the proposed acquisition. This is because this type of modelling does not measure changes to economic surplus or welfare, lacks transparency, is reliant on the untested assumptions provided by Tabcorp, and ignores any off-setting impact of cost increases and competitive detriment associated with the proposed acquisition.

Claimed cost savings

5.9. Tabcorp asserts that the proposed acquisition will lead to savings of [**Confidential to Tabcorp**] [redacted] per year,[269] which includes annual savings of:

- [**Confidential to Tabcorp**] [redacted] in wagering costs[270]
- [**Confidential to Tabcorp**] [redacted] in technology costs[271]
- [**Confidential to Tabcorp**] [redacted] in corporate costs[272]
- [**Confidential to Tabcorp**] [redacted] in procurement costs[273]
- [**Confidential to Tabcorp**] [redacted] in property and field services.[274]

5.10. It is likely that some of these cost savings will be achieved through the removal of duplication resulting from the proposed acquisition. However, for the reasons discussed below, Tabcorp's estimates are likely to be overstated.

Economic transfers are included in Tabcorp's claimed savings

5.11. The first reason the savings may be overstated is because Tabcorp has identified [**Confidential to Tabcorp**] [redacted] of savings that are economic transfers resulting from the merged entity's ability to negotiate improved terms from suppliers,[275] as noted by Dr Simes of Deloitte Access Economics.

5.12. Economic transfers describe a redistribution of resources that 'has no net benefit as it is simply transferring money from one firm to another'.[276] The ACCC agrees with Dr Simes that it is not appropriate to count these as public benefits.[277]

Removal of duplicated fixed costs does not properly account for variable costs

[268] Mellsop at [87], Houston part 5.3.2.
[269] Form S at [21.1], page 125.
[270] Johnston, section C.2.1.
[271] Johnston, section C.2.2.
[272] Johnston, section C.2.3.
[273] Johnston, section C.2.4.
[274] Johnston, section C.2.5.
[275] Simes at [31] and [32].
[276] Simes at [21] and [32].
[277] See also Houston at [375]; Mellsop at [192].

5.13. The second reason that Tabcorp's estimates are likely to be overstated is that some of the removed duplication of costs do not take into account costs that may reasonably be expected to increase for a significantly larger merged entity. For instance:

- Tabcorp has removed [**Confidential to Tabcorp**] [redacted],[278] despite stating elsewhere that the merger parties' businesses are largely complementary.[279]
- Tabcorp has also removed [**Confidential to Tabcorp**] [redacted].
- Tabcorp eliminates [**Confidential to Tabcorp**] [redacted] for other costs, for example, its costs regarding ASX listing costs[281] and [**Confidential to Tabcorp**] [redacted].[282] Tabcorp's ASX-related costs include [**Confidential to Tabcorp**] [redacted],[283] which are reasonably expected to be higher for a much larger and more complex merged entity than for either Tabcorp or Tatts alone.

5.14. Whilst some cost synergies are likely to arise from the proposed acquisition, it is not likely that they are accurately estimated by reference to 100 per cent of the cost base of either Tabcorp or Tatts.

Significant integration costs excluded from claimed savings

5.15. The third reason that Tabcorp's estimates are likely to be overstated is that the integration costs of achieving these savings have not been included in the calculation. These costs have been separately identified by Tabcorp as [**Confidential to Tabcorp**] [redacted] of likely one-off integration costs associated with combining the Tabcorp and Tatts businesses.[284] This estimate is comprised of:

- [**Confidential to Tabcorp**] [redacted]
- [**Confidential to Tabcorp**] [redacted].

5.16. Further, this [**Confidential to Tabcorp**] [redacted] estimate appears to be inconsistent with material provided to the ASX where Tabcorp estimated net one-off integration costs and capital expenditure at $110 million.[285]

Other concerns regarding cost savings estimates

5.17. There are other indications that Tabcorp may be overstating the cost savings resulting from the proposed acquisition.[286] For example, it is difficult to reconcile the reduced technology, marketing and [**Confidential toTabcorp**] [redacted] costs claimed

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[278] Johnston at [34(d)(i)].

[279] Form S at [4.133], page 44.

[280] Johnston at [38(a)(i)].

[281] Johnston at [34(b)].

[282] Johnston at [29(c)(ii)].

[283] Johnston at [34](b)].

[284] Johnston at [46].

[285] Presentation regarding proposed acquisition provided to the ASX on 19 October 2016, slide 8: http://www.asx.com.au/asxpdf/20161019/pdf/43c31b8j32v25b.pdf - Pleatsikas, Tab 8 of Exhibit CP-1 [TBP.006.001.0121].

[286] See also Houston at [346] and [372].

with the merged entity's forecast strategic initiatives and improvements that will focus on improved digital offerings and extended trading hours.[287]

5.18. These inconsistencies are discussed further in paragraphs 5.31 to 5.34 below.

5.19. Finally, in many cases Tabcorp's estimated savings are not accompanied by sufficient explanation such that an independent reviewer can comment on whether they are realistic or reasonable estimates in the circumstances, or the likelihood that they will be passed through or shared more widely.[288] The lack of clarity regarding Tabcorp's methodology for estimating the claimed cost savings detracts from their reliability.

Claimed increases in revenue

5.20. Tabcorp asserts that the proposed acquisition will result in increased annual revenue of approximately [**Confidential to Tabcorp**] [redacted] million per year, from the third year following completion.[289] The claimed revenue increases are expected to flow from:

- [**Confidential to Tabcorp**] [redacted] from improvements to Tatts fixed odds performance by implementing Tabcorp's superior fixed odds risk management system;[290] and increasing the offering of higher yielding products[291]
- [**Confidential to Tabcorp**] [redacted] from improvements to wagering[292] including introducing new products and broadening the availability of other products in Tatts states; re-branding Tatts retail and digital business with the 'TAB' brand, and improving the retail network in Tatts states; and [**Confidential to Tabcorp**] [redacted][293]
- [**Confidential to Tabcorp**] [redacted] from improvement to the Keno business.[294]

5.21. There are four issues with claiming these revenue increases as public benefits:

- Gross revenue is not an accurate measure of welfare or surplus
- These revenue increases do not appear to be merger-specific
- The costs of achieving these revenue increases do not appear to have been taken into account
- Increased revenue from fixed odds betting that increases yield for Tatts is likely to result in consumer detriment.

Increased revenue not indicative of efficiency or synergies

5.22. Tabcorp's submissions focus on increases in revenue. Increases in revenue do not necessarily indicate improvements in efficiency or give an indication of any change in welfare (i.e. they are not helpful in understanding whether producer surplus has increased).[295]

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[287] See Houston at [377]. See also Hines at [94b-c] and [95b-d].

[288] As noted in Mellsop at [80].

[289] Annexure A to the Form S at [302(b)]

[290] Johnston at [78(a)]

[291] Johnston at [78(b)]

[292] See Johnston part E.4.1, part E.4.2 and part E.4.3

[293] Johnston at [85].

[294] See Johnston at [108]

[295] Mellsop at [90(a)].

5.23. As noted by Mr Mellsop and discussed further below at paragraphs 5.27 to 5.34, using revenue measures to estimate producer surplus may overstate the public benefit, depending on whether there are any variable costs.[296]

Claimed additional revenue not merger specific

5.24. The revenue increases claimed by Tabcorp are not merger specific. That is, Tatts is likely to have the ability and incentive to implement many of the improvements that would result in increased revenue on a standalone basis, absent the proposed acquisition.[297]

5.25. These include Tatts being able to:

- Make changes to its risk management system either independently or by merging with any fixed odds wagering business (corporate bookmaker)[298]. Notably, [**Confidential to Tatts**] [redacted], and there is little reason why that could not lead to Tatts generating additional revenue in the future.[299]
- Offer higher yielding products (such as 'fixed odds multi bets with more than 10 legs'[300])[301]
- Introduce additional bet types and new wagering products[302]
- Invest in its retail network in order to improve services and facilities available to punters.[303] The specific improvements suggested by Tabcorp are not special to the merger. For example, [**Confidential to Tabcorp**] [redacted][304]
- Improve its Keno offering in South Australia.[305]

5.26. Based on the evidence filed by Tabcorp, it is not clear that any of these improvements are reliant on the proposed acquisition.

Costs associated with achieving improvements not counted

5.27. The revenue increases claimed by Tabcorp may not consider all of the costs required to achieve them. It is also not clear whether the revenue increase claimed by Tabcorp refers to gross revenue estimates or net revenue estimates. The extent to which the claimed additional revenue would be affected after deducting related expenses is unknown. Consequently, the additional revenue claimed by Tabcorp may not be indicative of potential public benefits, as the gross revenue should be offset with the costs of generating that revenue.

5.28. Mellsop emphasises this point, stating that producer surplus is more appropriate as a measure of welfare benefit as it calculates the extent to which revenue exceeds the

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[296] Mellsop at [90(a)].

[297] See Houston, part 5.3.3 and Report of Dr Tom Hird, Director of Competition Economists Group, dated 21 April 2017 (**Hird**) at [296].

[298] See Third Affidavit of Giles Thompson dated 13 April 2017 (**Third Affidavit of Thompson**) at [36] and Hines at [102].

[299] See Pleatsikas at [176], Johnston at [77], Tyshing at [461-463], Thompson at [37] and Mellsop at [86b].

[300] Johnston at [78(b)].

[301] See Third Affidavit of Thompson at [38].

[302] Mellsop at [91].

[303] [**Highly Confidential to Tatts**] [redacted].

[304] See Johnston at [89(b)(ii)].

[305] Mellsop at [96].

marginal costs incurred by the producer.[306] Other evidence before the Tribunal also makes this point.[307]

Revenue Synergies

5.29. It is a common occurrence that parties to a merger or acquisition overvalue the revenue synergies to be generated by the transaction,[308] and in this case it has been suggested that the revenue synergies claimed by Tabcorp may be overstated.[309] The evidence of Mr Julian Christian, General Manager - Finance for Racing Victoria Limited and Company Secretary of VicRacing Pty Ltd, suggests that [**Confidential to Tabcorp**][**Confidential to Racing Victoria**] [redacted].[310]

5.30. In addition, it should be noted that the cost savings outlined at paragraph 5.9 do not align with the revenue increases claimed.

5.31. For instance, Freeman discusses Tabcorp's strategic initiatives and improvements for retail wagering in Tatts states, which include: [**Confidential to Tabcorp**] [redacted][311]

5.32. [**Confidential to Tabcorp**] [redacted] can be expected to result in increased operating costs that should be accounted for in any estimate of net cost savings. The [**Confidential to Tabcorp**] [redacted], may also result in increased operating costs in relation to IT infrastructure and operations, though Tabcorp estimates a [**Confidential to Tabcorp and Tatts**] [redacted][312]

5.33. Tabcorp's estimated [**Confidential to Tabcorp**] [redacted] Freeman's statement that Tabcorp's digital strategy is 'reflected in its growing in-house digital team and capital investment' that has caused Tabcorp's in-house digital team to increase from three in FY2013 to 95 in FY2016.[314]

5.34. In short, there is an inconsistency between Tabcorp's estimate that the merged entity will [**Confidential to Tabcorp**] [redacted] and its strategy to introduce new products and increased coverage as well as investing in branding, the retail network and customer account management in each of South Australia, Queensland, Tasmania and the Northern Territory.[315]

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[306] Mellsop at [35] and [90].

[307] See Houston at [418], Third Affidavit of Thompson at [38] and Hird at [295].

[308] 'Where mergers go wrong', May 2004, http://www.mckinsey.com/business-functions/strategy-and-corporate-finance/our-insights/where-mergers-go-wrong

[309] Houston [at 394], Hines at [105] and [107]. See also 'Horses for Courses: Tabcorp scrips or cash', Australian Financial Review, 21 April 2017, http://www.afr.com/street-talk/horses-for-courses-tabcorp-scrip-or-cash-20170419-gvo900.

[310] See Affidavit of Julian Christian, General Manager - Finance of Racing Victoria and Company Secretary of VicRacing Pty Ltd, dated 26 April 2017 at [27]-[34].

[311] Freeman at [325].

[312] Johnston at [32(b)(iv)].

[313] Johnston.

[314] Freeman at [340].

[315] See Simes at [35].

Revenue increase may involve significant consumer detriment

5.35. Tabcorp's evidence suggests that the merged entity's improvement of Tatts' fixed odds performance will likely result in punters being charged a higher price for wagering products. The claimed revenue increases attributable to improvements in fixed odds performance cannot be achieved without intrinsic consumer detriment.[316]

5.36. Mr Mellsop considers that "[t]he idea of this synergy appears to be that Tabcorp could extend to the Tatts book Tabcorp's superior fixed odds management systems, [**Confidential to Tabcorp**] [redacted]."[317]

5.37. Mr Johnston defines the yield as "the proportion of turnover that fixed odds bookmakers retain after the payment of winnings".[318] Accordingly, Mr Mellsop characterised the fixed odds yield on betting as the "effective price paid by punters".[319] Improvements made to Tatts' fixed odds 'yield' can therefore be considered an increase in the price paid by punters.[320]

5.38. To the extent that the revenue increase results from improved yield, Mr Mellsop states that "there does not appear to be any consumer (punter) benefit here, just a profit benefit to the merged entity."[321]

5.39. The evidence of Mr Tyshing explains that:

In layman's terms, Tabcorp is claiming that the ability to extract an additional $61 million per annum from fixed odds punters placing bets with Tatts post-transaction, or put another way – the ability to impose a 21% 'price rise' on Tatts fixed odds punters, is a public benefit.[322]

5.40. Mr Tyshing summarises the effect of this as being "the average punter will simply have ended up paying 'more for less'".[323]

5.41. Dr Simes also identifies that some consumers who currently benefit from wagering under Tatts' fixed odds management system *will be worse off* as a result of Tabcorp's planned improvements.[324]

Substitution of domestic products for imported goods

5.42. Tabcorp asserts that the proposed acquisition is likely to result in the benefit of increasing substitution of domestic products for imported goods.[325] Whether this will occur, however, is not clear for three reasons.

5.43. First, there is conflicting information on the amount of likely transfers from overseas-based corporate bookmakers. Whilst Dr Simes assumes that that most of the claimed [**Confidential to Tabcorp**] [redacted] of wagering revenue increases come from transfers from overseas-based firms, Mr Mellsop notes that a significant portion of the revenue increase arises from improving Tatts' average fixed odds yield and therefore does not involve any transfers from competitors.[326]

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[316] Mellsop [86]-[88].
[317] Mellsop at [86].
[318] Johnston at [66b]; Mellsop at [87].
[319] Mellsop at [33].
[320] See Mellsop at [30]-[33].
[321] Mellsop at [86].
[322] Tyshing at [462].
[323] Tyshing at [464]
[324] Simes at [44]-[45]; Mellsop at [196].
[325] Annexure A to the Form S at [304]; Simes at [159]. This benefit must be considered under section 95AZH(2)(a)(ii) of the Act.
[326] Mellsop at [198]; Pleatsikas, Assumption 279 [TBP.001.027.1829_0074].

5.44. The second reason for uncertainty relates to how this claimed benefit is quantified. As noted by Dr Simes, overseas-based bookmakers are likely to incur some costs in Australia (such as labour, property, and marketing costs), though the amount of these costs is uncertain.[327] Mr Mellsop notes that the 50 per cent discount applied by Dr Simes "is arbitrary, and there is not sufficient information to be accurate".[328]

5.45. The third uncertainty arises from Tabcorp's foreign shareholders, who will benefit from the 45 per cent of the claimed cost savings and revenue increases that accrue directly to the merged entity.[329] It is not clear what proportion of Tabcorp is owned by foreign shareholders and whether the benefits accruing to these shareholders directly have been appropriately accounted for in Tabcorp's estimates.

Pass-through of direct benefits to other parties

Pass-through is not a separate benefit

5.46. Tabcorp asserts that approximately 55 per cent of the direct benefits claimed from cost savings and revenue increases discussed above will be shared with the racing industries, State and Federal governments, retail venues and sporting bodies.[330]

5.47. In *Re Qantas,* the Tribunal indicated that a modified total welfare standard may be appropriate in some cases:

> *whilst the Tribunal does not require that efficiencies generated by a merger or set of arrangements necessarily be passed on to consumers, it may be that, in some circumstances, gains that flow through only to a limited number of members in the community will carry less weight.*[331]

5.48. If the Tribunal is minded to apply such a standard in these circumstances, any pass-through of the direct benefits may be relevant to the weighting of these direct benefits. However, pass-through is not an additional benefit on top of the direct benefits and should not be double-counted as such.[332]

5.49. In undertaking this exercise the Tribunal should take into account that, to the extent that Tabcorp has overestimated any of the direct benefits, this will reduce any benefit that is passed through to other parties.[333]

5.50. Tabcorp has made some specific claims about how these benefits will flow through to the racing industry, help overcome free-riding issues and help achieve national pooling. It has also provided modelling which attempts to measure the effect the proposed acquisition will have on Australia's gross national income. The following sections consider these claims.

Net impact on racing industry, retail venues and sporting bodies uncertain

5.51. Regarding the racing industry, Dr Simes was instructed to assume that [**Confidential to Tabcorp**] [redacted] of the direct benefits would be passed through to the various state-based racing industries.[334] Separately, Tabcorp asserts that [**Confidential to Tabcorp**] [redacted] will be passed through to sporting bodies;

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[327] Simes at [52]-[53].

[328] Mellsop at [199].

[329] Percentages estimates provided by Tabcorp. See Simes, Figure 6, page 27; Annexure A to the Form S at [303].

[330] Annexure A to the Form S, page 97.

[331] *Re Qantas* at [185].

[332] Mellsop at [97] and [201]-[204].

[333] Simes, page 27, Figure 6 summarises the 'Assumptions provided on financial flows as a result of the Proposed Transaction', which shows that the pass-through includes the [**Confidential to Tabcorp**] [redacted] transfer amount.

[334] Simes at [55] and Figure 6, page 27.

[**Confidential to Tabcorp**] [redacted] to pubs, clubs and agencies; and [**Confidential to Tabcorp**] [redacted] of the increased Keno revenue to South Australian pubs and clubs.[335]

5.52. In the immediate future, the proposed acquisition is likely to increase the funding received by the racing industries to some extent. This is a result of the current funding arrangements between totalisator/retail wagering operators and each state-based racing industry providing that contributions must be paid to the racing industries.

5.53. The extent of this pass-through is not clear, as the funding arrangements contain both fixed and variable contributions to the racing industries. The variable contributions, some of which are capped, are also calculated using different metrics including revenue and profit.[336]

5.54. In the longer term, however, the proposed acquisition could decrease the funding received by the racing industries. The funding arrangements between totalisator/retail wagering operators and the racing industries are often a condition of the wagering licences granted by the State and Territory governments.[337]

5.55. As discussed above, the proposed acquisition would remove Tatts as the only other credible bidder to Tabcorp.[338] This lessened competitive tension in the bidding for wagering licences could, in turn, decrease the racing industries' ability to negotiate favourable funding contributions in the future.

5.56. Overall, therefore, the net impact of the proposed acquisition on funding to the racing industry is uncertain.

5.57. Similar uncertainty exists around the net effect the acquisition will have on the amount of funding that will pass through to retail venues and sporting bodies.

Taxes paid to Federal and state governments

5.58. Tabcorp asserts that the proposed acquisition will result in 'increased Commonwealth, State and Territory taxation revenue'[339] of around [**Confidential to Tabcorp**] [redacted].[340] This is comprised of:

- Increased State taxation revenue of [**Confidential to Tabcorp**] [redacted] flowing from wagering revenue increases and [**Confidential to Tabcorp**] [redacted] flowing from the Keno revenue increases.
- Increased Federal taxation revenue of [**Confidential to Tabcorp**] [redacted] in Goods and Services Tax (**GST**) and [**Confidential to Tabcorp**] [redacted] in corporate tax.

5.59. Changes in taxation revenue are economic transfers that do not constitute efficiency gains that result in net benefits. This is consistent with the evidence of Mr Mellsop and Dr Simes.[341]

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[335] Simes at [56]-[57].

[336] Freeman at [237], Figure 23.

[337] Freeman at [85]: "The extent of the State TABs' racing industry funding contributions is primarily due to the terms of the state and territory wagering licences and the racing industry funding agreements with the racing industries in those jurisdictions."

[338] This is not considered in Dr Simes' report, as Dr Simes was instructed by Tabcorp to provide assume that the proposed acquisition 'is not likely to result in a public detriment from a lessening of competition': see HSF letter to Dr R Simes, *Instructions letter – Australian Competition Tribunal merger authorisation application*, 6 March 2017 at page 1.

[339] Mellsop at [204] states "taxes *per se* are generally not counted as a benefit in this sort of cost benefit analysis, because they represent a transfer payment from one entity (in this case, the merged entity) to another (state and federal governments) without any change in resource use."

[340] Annexure A to the Form S at [303]; Johnston at [24(d)-(e)].

[341] See Mellsop at [204] and Simes at [17]-[24] and [62].

5.60. Whether the proposed acquisition will lead to an actual increase in revenue that the government would not have otherwise received is also unclear because:

- There is significant uncertainty regarding the increased revenue estimates that underpin Tabcorp's State taxation revenue estimates (as discussed above)
- GST increases 'are unlikely to provide significant increases in net government revenue' and 'the increase in payments in GST are likely to be offset by a similar reduction in GST payments by other firms'[342]
- Increases in corporate tax paid by the merged entity is likely to be offset by other corporate entities paying less tax.

5.61. In light of the above considerations, it is the ACCC's view that there are no benefits from increased taxation. Even if it is appropriate to place more weight on the portion of the direct benefits that are passed through as increased taxes than on the portion that directly accrues to the merged entity, it remains unclear how much of the pass-through amount constitutes new taxation revenue that the governments would not have otherwise received.

Addressing a free rider or underfunding problem

5.62. Tabcorp asserts that the pass-through of claimed direct benefits to the racing industry constitutes a further public benefit because it will help to address a 'free rider' problem in the racing industry[343], as well as prevent the racing industry from becoming underfunded.

5.63. The racing industry may exhibit some of the economic characteristics of a public good and absent regulation a free rider problem could lead to underfunding of the racing industry. However a free rider problem does not currently exist as state and territory legislation requires totalisator, corporate bookmakers and other wagering operators to satisfy licencing requirements.[344] These licensing requirements allow the racing industry to control both access to racing products and the funding obligations of product users.

5.64. Accordingly, in addition to the racing industries' funding arrangements with state totalisators, the racing industries have a number of other sources of revenue. These include race field fees from bookmakers and from interstate wagering activity on the races conducted within that state, sporting body fees, and fees for the distribution of racing media content.

5.65. Racing industries are able to control their various funding mechanisms.[345] For instance, racefield fees were originally introduced to arrest the funding imbalance that arose due to the growth of corporate bookmakers.[346] In 2014 Racing Victoria revised the racefield fees it charged in response to growing popularity of fixed odds and derivative betting (as opposed to pari-mutuel).[347] [**Confidential to Racing Victoria**] [redacted].[348]

[342] Simes at [62].

[343] Form S at [21.1] and [21.2], page 125.

[344] To provide wagering services in Australia, wagering operators are required to be licensed, or to hold a relevant permit. Each state and territory has its own regulatory regime for gambling conducted in its jurisdiction; which governs who can offer wagering services, the products that can be offered, and the advertising permitted (Freeman at [93]).

[345] Houston at [436]-[437].

[346] Victorian Race Fields Policy, 16 May, 2014: https://rv.racing.com/news/2014-05-16/victorian-race-fields-policy.

[347] Ibid.

[348] Third Affidavit of Thompson at [46].

5.66. The funding contributions currently required from corporate bookmakers and totalisators are clearly asymmetric. However, the funding imbalance is not a result of free-riding, rather it is largely a result of the exclusive licences which state totalisators enjoy. That is, the different contributions paid by wagering operators reflect the different operating rights they are afforded by the racing industries. Totalisators negotiated their exclusive retail and on-course wagering licences, and as such the contributions payable by those totalisators represent the consideration they have provided for monopoly retail wagering and totalisator wagering rights.

5.67. Separately, Mr Mellsop questions whether additional revenue paid to the racing industry as a result of the proposed transaction will efficiently address any free rider problem. He notes that Tabcorp's claim "assumes that any free rider problem is not already addressed efficiently by existing funding levels…under the counterfactual".[349]

5.68. Finally, as discussed above, it is not clear that the proposed acquisition is likely to result in a net increase to the funding received by the racing industries, given that any additional funding contributions from revenue increases may be offset by the merged entity's ability to negotiate decreased funding arrangements in the future.

5.69. Accordingly, it is not likely that the proposed acquisition will result in any public benefits from addressing a free rider problem in the racing industries.

National pooling or creation of larger pools

5.70. Tabcorp submits that the proposed acquisition is likely to result in the removal of a commercial barrier to co-mingling the pari-mutuel wagering pools of Tabcorp and Tatts, creating a pathway to national pooling.

5.71. Tabcorp asserts that national pooling creates a public benefit because it is expected to improve products and services being supplied to punters, increase funding being passed through to the state racing industries[350], and improve competition with corporate bookmakers in Tatts states.[351]

5.72. However, it is not clear:

- Which commercial barrier discussed by Tabcorp is likely to be overcome by the proposed acquisition
- Whether removing any single commercial barrier is likely to result in national pooling, due to the existence of numerous other barriers that are not overcome by the proposed acquisition.[352]

5.73. Racing industry and government approvals appear to be significant barriers to national pooling that are unlikely to change with the merger. For example, it would appear that these barriers have prevented Tabcorp from merging the Victorian and NSW pools even though it currently has exclusive licences over both.

5.74. While Tabcorp asserts that the proposed acquisition will reduce the concerns of the NSW government,[353] there is little detail in the evidence to show how this will occur.

Claimed benefits regarding alternative pooling scenarios are negligible

5.75. If national pooling is not achieved, Tabcorp submits that the proposed acquisition may lead to two alternative pooling scenarios:

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349 Mellsop at [212].

350 Form S at [21.1] and [21.3], pages 125-126.

351 Form S at [21.2], page 125.

352 See Annexure A to the Form S at [145]; Freeman at [152] and [156]-[157]. See also Hines at [113]; Mellsop at [207].

353 Freeman at [166].

- Co-mingling Tabcorp's Victorian SuperTAB pari-mutuel pool with Tatts' pool. Mr Johnston estimates that this would increase the merged entity's revenue by [**Confidential to Tabcorp**] [redacted], increasing EBITDA by [**Confidential to Tabcorp**] [redacted][354]
- Co-mingling Tabcorp's NSW TAB pari-mutuel pool with Tatts' pool. Mr Johnston estimates that this would increase the merged entity's revenue by [**Confidential to Tabcorp**] [redacted], increasing EBITDA by [**Confidential to Tabcorp**] [redacted].[355]

5.76. It is unlikely that these scenarios can only be realised by the proposed acquisition, because there are a number of ways to increase pool size that do not require the co-mingled pool to be controlled by a single merged entity. For instance, numerous co-mingled pools controlled by different entities currently exist both in Australia and overseas.[356]

Increases to GNI (as measured by a CGE model)

5.77. Tabcorp claims the proposed acquisition will generate additional indirect public benefits because it will lead to increases in economic activity in the broader Australian economy.

5.78. In support of this claim, Tabcorp refers to the evidence of Dr Simes. Dr Simes utilises a CGE model to measure the effects on GNI of the following claimed direct benefits of the proposed acquisition:

- Cost savings estimated at [**Confidential to Tabcorp**] [redacted] p.a.
- Revenue increases for wagering products estimated at [**Confidential to Tabcorp**] [redacted] p.a.,[357] of which Dr Simes estimates 50 per cent (i.e. [**Confidential to Tabcorp**] [redacted] per annum) may reflect a substitution of domestic products for imported goods and services.[358]

5.79. Dr Simes' CGE model treats these claimed direct benefits as "shocks" to the economy, which are modelled as being akin to a decrease in the price of goods and services provided in the gambling sector of the economy.[359] Dr Simes' model then traces how this price decrease would flow through the broader economy, and estimates it will lead to an increase in GNI of between $174.5 million and $179.5 million per annum[360]. This is summarised in Figure 5 below. Dr Simes estimates this will translate into an increase in GNI over the next 15 years of between $1.516.3 billion and $1.561.6 billion in net present value (NPV) terms.

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[354] Johnston at [131], Table 33 (scenario 2).

[355] Johnston at [131], Table 33 (scenario 3).

[356] Form S at [4.16], page 20.

[357] Tabcorp estimates [**Confidential to Tabcorp**] [redacted] p.a. in total revenue increases. However, only [**Confidential to Tabcorp**] [redacted] comes from wagering services with the remainder relating to improvements to Tatts' South Australian Keno business.

[358] Simes at [53].

[359] Simes at [137].

[360] By the third year following completion of the proposed acquisition.

Figure 5 - Flow chart of CGE model [**Confidential to Tabcorp**]

[redacted]

5.80. When conducting his analysis, Dr Simes was instructed to assume that the proposed acquisition is not likely to result in a public detriment from a lessening of competition.[361]

5.81. The ACCC:

- Cautions that a GNI CGE model does not measure changes to economic surplus or welfare
- Has significant concerns about the lack of transparency associated with Dr Simes' model
- Notes Dr Simes has not been instructed to consider [**Confidential to Tabcorp**] [redacted] of offsetting cost increases that Tabcorp has elsewhere identified in its evidence when asked to analyse cost savings assumed to result from the proposed acquisition[362]
- Believes Dr Simes' assumption that most of the claimed wagering revenue increase results from sales won from corporate bookmakers[363] does not reflect the source of the revenue increases from increased yield and decreased turnover[364]
- Considers Dr Simes has been wrongly instructed to assume no detriments would result from the proposed acquisition.

5.82. As a result of these issues, the Tribunal should place little weight on the findings of Dr Simes' GNI CGE modelling analysis. These issues are elaborated on further below.

Increases to GNI do not equate with increases in economic welfare

5.83. CGE models are an economic tool often used to measure the broader economic consequences of a proposed policy change. They come in a number of forms, with different models seeking to estimate different types of economic effect.

5.84. The particular model utilised by Dr Simes seeks to measure the impact on GNI of certain aspects of the proposed acquisition. As noted by Dr Simes, GNI is:

[361] HSF letter to Dr R Simes, *Instructions letter – Australian Competition Tribunal merger authorisation application*, 6 March 2017 at page 1.

[362] Johnston at [46(a) and (b)] and [90].

[363] Simes at [48].

[364] HSF letter to Dr R Simes, *Instructions letter – Australian Competition Tribunal merger authorisation application*, 6 March 2017, page 1.

*… the total amount of goods and services produced in an economy less net exports (known as gross domestic product (**GDP**)) plus net income from abroad.*[365]

5.85. This means that increases in GNI should not be equated to increases in economic welfare. That is, increases in GNI reflect increases in the market value of goods and services produced in the economy. However, economic welfare – at least in the sense previously considered by the Tribunal – measures something different. Economic welfare is the difference between the value consumers place on the goods they consume and the costs (including opportunity costs) of producing those goods. In this context, something that increases the market value for goods and services produced in the economy may not lead to an increase in economic welfare.[366]

5.86. This point is made in the expert evidence of Mr Mellsop, who notes that:

- Measures of economic activity, such as GDP and GNI, are not measures of economic welfare
- GNI does not measure consumer surplus
- The economics literature and the Australian Bureau of Statistics are clear that GDP is not a measure of economic welfare.[367]

The CGE model used by Dr Simes is an opaque "black box"

5.87. Dr Simes notes that:

"Results from CGE models must be interpreted carefully, and like any economic analysis are subject to a range of assumptions and judgements."[368]

5.88. He also notes that the model he has utilised in preparing his expert evidence is:

"… a large scale, dynamic, multi-region, multi-commodity CGE model of the world economy."[369]

5.89. Implicit within the limited material provided by Dr Simes to date to describe his model is the understanding that it contains a substantial number of equations representing assumed linkages between different sectors of the economy. The model is also likely to contain a substantial number of assumptions regarding key parameters.

5.90. As noted by Mr Mellsop when referring to the writings of Abelson:

"… CGE models are large and generally non-transparent black boxes" … it is often hard to determine how particular assumptions drive the results, or more generally to understand what occurs within a CGE model."[370]

5.91. Due to confidentiality claims, a copy of Dr Simes' CGE model has not been provided to the Tribunal, the ACCC or CGE modelling experts engaged by the ACCC to assist in this matter. It is noted, however, that two workshops have been organised at dates after the submission of this report (and before the commencement of the hearing in this matter) that are intended to provide further information regarding the workings of Dr Simes' model.

5.92. Without full access to Dr Simes' CGE model, the Tribunal is unlikely to be able to determine whether the assumptions and linkages contained within his model are

[365] Simes at [25].

[366] Mellsop at [223]-[226].

[367] Mellsop at [225]-[228].

[368] Simes at [116].

[369] Simes at [118].

[370] Mellsop at [233] per Abelson (2011, page 56).

reasonable. If this is the case, little weight can be placed on the Dr Simes' estimates of the increases in economic activity that are likely to result from the proposed acquisition.

5.93. Even if the CGE model used by Dr Simes was found to be suitable for measuring changes in GNI, there are also significant concerns with both of the key inputs used by Dr Simes in his analysis. These concerns are set out below.

It is unclear how Dr Simes translates cost decreases into decreases in the price of gambling services

5.94. The first key input used by Dr Simes in his model relates to the [**Confidential to Tabcorp**] [redacted] per annum in cost savings Tabcorp has asked him to assume will result from the proposed acquisition.

5.95. There are two key concerns with this input. First, and for the reasons sets out above under the heading 'Tabcorp's claimed cost savings', [**Confidential to Tabcorp**] [redacted] per annum are likely to represent an over-estimate of the merger specific cost savings that will result from the proposed acquisition. To the extent the assumed cost savings are overinflated, it follows that any consequent estimate of the broader impacts on GNI will also be over-estimated.

5.96. Second, it is not clear precisely how Dr Simes has converted his assumed cost savings into price decreases for the purposes of his model. While Dr Simes does indicate that these assumed cost savings are "transmitted to the representative agent [of his model] through a decrease in price of goods and services in the gambling sector",[371] there is no further material available at the date of this report to indicate how this has been done. For instance, it is unclear whether all cost savings assumed to result from the proposed acquisition are passed through in full to consumers in the form of lower prices for gambling services; or whether some portion is retained by the merged entity in the form of higher profits. Similarly, it is unclear whether Dr Simes has treated any of the cost savings as being in the nature of fixed costs that do not vary with the level of output of gambling goods and services; or whether he has treated all cost savings as reductions in the variable cost of providing these goods and services.

5.97. The way in which the assumed cost savings have been treated has profound implications for the welfare effects of the proposed acquisition. While reductions in costs that result directly from (and are therefore specific to) the proposed acquisition will be likely to give rise to some level of public benefit, the extent of this benefit will depend greatly on whether these cost savings are fixed or variable in nature; and the extent to which these savings are passed through to consumers.

5.98. Some of these matters may be addressed in the CGE model workshops proposed for the period between submission of this report and the hearing in this matter. However, without the ability to closely examine the way in which Dr Simes has treated the cost savings he has been asked to assume, it is impossible to assess whether Dr Simes' estimates of the impact of the proposed acquisition on GNI are reasonable.

Dr Simes appears to erroneously treat some revenue increases for Tabcorp as a reduction in the price of gambling services

5.99. The second key effect Dr Simes addressed in his model relates to increases in revenue Tabcorp expects to earn as a result of the proposed acquisition. These increases in revenue are said to be a public benefit as Dr Simes has been asked to assume the majority of this revenue increase comes from sales won from corporate

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[371] Simes at [137].

bookmakers, and that this represents a substitution of imports for domestically produced goods and services.

5.100. There are three underlying issues with how the assumption given to Dr Simes is incorporated into his analysis:

- It is not clear that the assumed substitution of domestic products for imported goods is correct in this case (as discussed at paragraphs 5.42 to 5.45 above)
- It seems to misunderstand the nature of the increased revenue from fixed odds services ([**Confidential to Tabcorp**] [redacted] is not derived from extra sales from competitors; but instead from increased yield or price for Tatts' services)
- it is not clear how he has translated a revenue increase into a price decrease (especially when it seems to imply a price increase in evidence).

Dr Simes only models a subset of possible effects of the proposed acquisition

5.101. The modelling exercise undertaken by Dr Simes considers only two possible effects of the proposed acquisition – i.e. those relating to certain assumed cost savings and revenue increases given to him by Tabcorp.

5.102. However, this provides only a partial view of the possible consequences of the proposed acquisition. In particular, it neglects to consider at least three significant other consequences of the proposed acquisition that would be likely to have offsetting negative effects on the level of GNI in the economy.

5.103. First, Dr Simes has been instructed by Tabcorp to assume that no public detriments will result from the proposed acquisition. For this reason, the model does not appear to consider the consequences on GNI resulting from any of the public detriments discussed in section four of this report including any:

- Lessening of competition for media rights
- Lessening of competition for wagering services
- Increased prices for Tatts' fixed odds products leading to a reduction in turnover .

5.104. While quantification of some of these detriments might be difficult, it is not appropriate to draw conclusions regarding the overall effect of the proposed acquisition on GNI if detriments are simply assumed not to occur (and therefore not modelled). If the Tribunal concludes that some detriments are likely to result from the proposed acquisition, these would also need to be modelled to fully understand the overall impact on GNI.

5.105. This was considered by the New Zealand High Court in *Air NZ v Commerce Commission*, where it observed with respect to the use of a CGE model that:

> *… we agree with the Commission that the same type of model should be used for calculating competitive detriments and public benefits. … If a general equilibrium model were to be adopted for the purpose of calculating benefits, an adjustment would have to be made when detriments and benefits were compared.*[372]

5.106. Second, it does not appear that Dr Simes has sought to model the offsetting effects of any increases in costs Tabcorp believes it will incur following the proposed acquisition. The statement of Mr Johnston and the assumptions provided to Dr Pleatsikas both indicate that, following the proposed acquisition, Tabcorp expects it will incur additional costs of approximately:

[372] *Air New Zealand v Commerce Commission (No 6)* (2004) 11 TCLR 347 at [367].

- [**Confidential to Tabcorp**] [redacted][373]
- [redacted][374]
- [redacted][375]

5.107. To the extent that cost savings for Tabcorp flow through Dr Simes' CGE model in a way that leads to increased GNI throughout the economy, it is expected that the cost increases identified by Tabcorp will be likely to have a significant offsetting effect on GNI growth in the economy.

5.108. Third, Dr Simes does not break down broader effects. Whenever there is a change in relative prices, resources will flow away from other industries. Dr Simes does not break down the consequences of his modelled changes on those industries that would be likely to be made worse off as a result of his assumed decrease in the price of gambling goods and services.

[373] Johnston at [46(a)]; Pleatsikas Assumptions at [275].

[374] Johnston at [46(b)]; Pleatsikas Assumptions at [275].

[375] Johnston at [90]; Pleatsikas Assumptions at [282].