[PUBLIC VERSION]

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

STATEMENT OF JAMES MELLSOP

Statement of:	James Mellsop
Address:	NERA Economic Consulting, Level 18, 151 Queen Street, Auckland 1010, New Zealand
Occupation:	Managing Director at NERA Economic Consulting
Date:	27 April 2017

Filed on behalf of	Australian Competition and Consumer Commission		
Prepared by	Simon Uthmeyer		
Law firm	DLA Piper		
Tel	+61 3 9274 5470	Fax	+61 3 9274 5111
Email	Simon.Uthmeyer@dlapiper.com		
Address for service	DLA Piper 140 William Street Melbourne VIC 3000		

I, James Mellsop, of Level 18, 51 Queen Street, Auckland 1010, New Zealand, say as follows:

QUALIFICATIONS AND EXPERIENCE

1. I am an economist and a Managing Director of NERA Economic Consulting, a global economic consulting firm. NERA Economic Consulting specialises in applying economic, finance, and quantitative principles to complex business and legal challenges.

2. My background and experience can be briefly summarised as follows:

   (a) I have a Masters degree in economics (with distinction), an Honours degree in economics (First Class), an undergraduate degree in accountancy and a law degree, all from Victoria University of Wellington; and

   (b) Broadly my consulting practice involves the application of economic analysis to legal issues, particularly in the areas of competition, regulation, contractual disputes, damages, fair trading, tax, and resource management.

3. Now shown to me and marked **Annexure JM-1** is a copy of my current curriculum vitae.

INSTRUCTIONS

4. I have prepared this statement at the request of DLA Piper Australia (**DLA**), solicitors for the Australian Competition and Consumer Commission. I have been requested by DLA to act as an independent expert to the Australian Competition Tribunal in relation to an application by Tabcorp Holdings Limited (**Tabcorp**) to the Australian Competition Tribunal for authorisation of its proposed merger with Tatts Group Limited (**Tatts**).

5. Now shown to me and marked **Annexure JM-2** is a copy of my letter of instructions dated 25 April 2017.

6. I have been provided with and read the Federal Court of Australia Expert Evidence Practice Note (GPN-EXPT), including the Harmonised Expert Witness Code of Conduct annexed to that practice note (together, the **Expert Guidelines**). I confirm

that I have read and complied with the Expert Guidelines which are attached to the letter of instructions dated 25 April 2017, contained at **JM-2**.

REPORT

7. Now shown to me and marked **Annexure JM-3** is a copy of my report dated 27 April 2017.

8. This report contains information which is highly confidential to Tabcorp and Tatts, and information derived from the confidential information of those parties. Material that is confidential in this report is marked accordingly.

9. I confirm that I have made all due inquiries and there are no matters within my knowledge that are of significance or relevance that I have excluded from my report. I acknowledge that the opinions I express in my report are based wholly or substantially on the specialised knowledge I have as a result of the qualifications and experience set out above.

Dated: 27 April 2017

Signed:. . . . . .

JAMES MELLSOP

INDEX OF ANNEXURES TO STATEMENT OF JAMES MELLSOP

Annexure	Title	Confidentiality
JM-1	Curriculum Vitae of James Mellsop	
JM-2	Letter of Instructions for James Mellsop	
JM-3	Report of James Mellsop dated 27 April 2017	Restriction of part publication claimed.

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ACT 1 of 2017

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Applicant:	Tabcorp Holdings Limited

ANNEXURE CERTIFICATE

This is the annexure marked **JM-1** annexed to the statement of **James Mellsop** dated 27 April 2017.

Annexure JM-1

Curriculum Vitae of James Mellsop

Filed on behalf of	Australian Competition and Consumer Commission		
Prepared by	Simon Uthmeyer		
Law firm	DLA Piper		
Tel	+61 3 9274 5470	Fax	+61 3 9274 5111
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James Mellsop

Managing Director

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james.mellsop@nera.com
www.nera.com

Overview

James Mellsop specialises in the application of economic analysis to legal issues, particularly in the areas of competition, regulation, contractual disputes, damages, fair trading, tax, and resource management.

James' experience includes analysing the economic implications of mergers and acquisitions, joint ventures and other contracts, and market behaviour and regulatory interventions in a variety of sectors and industries, including media, telecommunications, electricity, gas, water, mining, post, health, retailing, supermarkets, transport, manufacturing, agriculture, software, building products, banking and finance, ports, airports and waste.

He has also analysed and quantified:

- The economic and environmental effects of resource management decisions; and
- Damages as a result of breach of contract, collusion and misrepresentation.

James has provided expert evidence before the New Zealand High Court, the New Zealand Environment Court, the New Zealand Commerce Commission, arbitrators and Resource Management Act Commissioners. He has worked on projects in New Zealand, Australia, and Asia, and has been engaged by both the Australian Competition & Consumer Commission and the New Zealand Commerce Commission.

Prior to joining NERA in 2008, James directed the New Zealand competition practice of another international economics consultancy. In addition, he worked for the New Zealand Treasury on microeconomic policy issues, particularly competition, regulatory and telecommunications policy. From 1992 to 1996, James worked as a lawyer for Bell Gully, with a focus on competition, corporate, and oil and gas law.

Qualifications

2001	**Victoria University of Wellington** MCA Economics (Distinction)
1999	**Victoria University of Wellington** BCA (with Honours) in Economics (1st Class)
1992	**Victoria University of Wellington** LLB
	BCA in Accountancy

Career Details

	NERA Economic Consulting
2008-present	Managing Director, Auckland and Sydney
	CRA International
2004-2008	Vice President, Auckland
2001-2004	Principal, Wellington
	New Zealand Commerce Commission
2001	Chief Advisor (three-month contract), Wellington
	New Zealand Treasury
1998-2001	Senior Analyst, Wellington
1996-1998	Analyst, Wellington
	Bell Gully
1992-1996	Solicitor, Wellington

Non-confidential Project Experience

Mergers, Acquisitions and Joint Ventures

Economic analysis for:

- Seven West Media in respect of its proposed acquisition of *The Sunday Times* publication and website from News Limited (2016);
- Sky TV and Vodafone in respect of their proposed merger (2016);
- The New Zealand Racing Board in respect of its proposed betting pool "commingling" arrangement with Tabcorp (2016);
- Fairfax and NZME in respect of their proposed merger (2015-2017);

- Z Energy in respect of its proposed acquisition of Chevron New Zealand (2015-2016);
- Staples in respect of its proposed acquisition of OfficeMax, in both Australia and New Zealand (2015);
- Cavalier Wool Holdings in respect of its proposed acquisition of New Zealand Wool Services International (2014-2016);
- The Commerce Commission in respect of its investigation into Wilson Parking's acquisition of parking leases and management agreements from Tournament Parking, including econometric analysis of car parking data (2014);
- Austron and Evolution in respect of their proposed acquisition (and privatisation) of Acurity, a transaction relating to the private hospital market in Wellington (2014);
- IAG in respect of its proposed acquisition of Lumley from Wesfarmers (2014);
- Bluescope/New Zealand Steel in respect of its proposed acquisition of Pacific Steel from Fletcher Building (2013-2014);
- Telecom New Zealand in respect of its proposed acquisition of 700MHz spectrum for 4G mobile services (2014);
- The Australian Competition & Consumer Commission in respect of Murray Goulburn's application to the Australian Competition Tribunal for authorisation to acquire Warrnambool Cheese and Butter (2013-2014);
- PropertyIQ in respect of its proposed acquisition of Terralink (2013);
- The Commerce Commission in respect of the proposed acquisition by Vector of Contact Energy's gas metering business (2013);
- Hirepool in respect of its proposed acquisition of Hirequip (2012);
- Southern Community Laboratories in respect of its proposed acquisition of MedLab South (2012);
- Pact Group in respect of its proposed acquisition of the plastic pails business of Viscount Plastics (2011-2012);
- Fonterra and Silver Fern Farms in respect of the creation of Kotahi, a vehicle to coordinate export and import container transport services (2011-12);
- Southern Cross Health Trust in respect of its proposed Palmerston North private surgical hospital joint venture with Aorangi (2008-2011);
- Cavalier Wool Holdings in respect of its proposed acquisition of New Zealand Wool Services International (2011);
- Tegel in respect of its proposed acquisition of Brinks (2008);
- Foodstuffs in respect of its proposed purchase of The Warehouse, including providing expert evidence before the High Court (2007);
- ARW (owner of Angus & Robertson and Whitcoulls) in respect of its proposed purchase of Borders in New Zealand and Australia (2007);

- Southern Cross Health Trust in respect of its proposed Rotorua private surgical hospital joint venture with QE Health (2007);
- Manawatu Waste Limited in respect of the proposed acquisition by Transpacific Industries Group of various assets from Enviro Waste Services (2007);
- Infratil Limited and New Zealand Bus Limited (NZBL) in respect of litigation brought against them by the Commerce Commission to prevent the acquisition by NZBL of Mana Coach Service Limited, including providing expert evidence before the High Court (2006);
- Fonterra in respect of its acquisition of Kapiti Fine Foods (2006);
- Sky TV in respect of its acquisition of Prime (2006);
- Sonic Healthcare and Abano Healthcare in respect of the merger of their Wellington and Hutt Valley pathology businesses (2006);
- Lion Nathan in respect of its potential acquisition of Independent Liquor (2006);
- Rank Group in respect of its asset swap with Fonterra (2005);
- GE Finance in respect of its acquisition of Pacific Retail Finance (2005);
- Wrightson and Pyne Gould Guinness in respect of their merger (2005);
- Allied British Foods plc in respect of its acquisition of New Zealand Food Industries Limited (2004);
- Pacific Radiology Limited in respect of its acquisition of Wakefield Radiology Limited (2004);
- The Pohokura gas field joint venture parties on marketing issues (including quantification of welfare effects), in the context of an authorisation application to the Commerce Commission (2003);
- Contact Energy in respect of its acquisition of Taranaki Combined Cycle power station (2002-2003);
- Brambles in respect of its acquisition of a plastic crates business from General Electric (2002-2003);
- Avis in respect of its acquisition of Budget (including merger simulation modelling) (2002); and
- Foodstuffs in respect of the merger between Progressive and Woolworths (2001).

Litigation

Economic analysis for:

- Kiwibank in respect of a Commerce Act claim brought against it by E-Trans International Finance, including providing expert evidence before the High Court (2015-2016);
- Kiwi Pacific Foods (owned by Veritas) in respect of a dispute with Antares Restaurant Group (master franchisee of Burger King in New Zealand), including providing expert evidence before an arbitrator (2015);

- Richard Tankersley and related companies in respect of litigation against John Meroiti and other defendants, regarding the value of certain intellectual property (2015);
- ASB in respect of the Commerce Commission's Fair Trading Act investigation into the selling of swaps to farmers (2014);
- The receiver of a finance company, analysing losses in the context of proceedings brought against the auditor of that finance company (2014);
- Motor Trade Finances Limited in respect of proceedings brought by the Commerce Commission under the Credit Contracts and Consumer Finance Act 2003 regarding the reasonableness of certain fees, including providing expert evidence before the High Court (2012);
- Three Nelson-based industrial users of water in respect of a water pricing dispute with Tasman District Council, including providing expert evidence before an arbitrator (2012);
- An engineering contractor in respect of a contractual dispute (before an arbitrator), including filing expert evidence regarding damages (case settled during hearing) (2011-12);
- Turners & Growers in respect of its claim that ZESPRI has behaved anticompetitively in kiwifruit markets, including providing expert evidence before the High Court (2011);
- A firm being sued by the Commerce Commission for breach of the Fair Trading Act, regarding the firm's alleged misrepresentation of the quality of the firm's product (econometric analysis to estimate damages) (2010);
- South Port in respect of a dispute with New Zealand Aluminium Smelters over the pricing of wharf access, including providing expert evidence before an arbitrator (2010);
- The purchaser in respect of a dispute over a cancelled contract for the acquisition of a mine, including providing expert evidence before an arbitrator (2010);
- A wharf owner (Otehei Bay Holdings Limited) in respect of an access dispute, including filing expert evidence in the High Court (2010);
- Progressive Enterprises in respect of a dispute under the Resource Management Act, including filing expert evidence in the Environment Court (2010);
- A bank in respect of the credit card interchange proceedings brought by the Commerce Commission (settled in 2009) (2007-2009);
- Foodstuffs in respect of its proposed purchase of The Warehouse, including providing expert evidence before the High Court (2007);
- Infratil Limited and New Zealand Bus Limited (NZBL) in respect of litigation brought against them by the Commerce Commission to prevent the acquisition by NZBL of Mana Coach Service Limited, including providing expert evidence before the High Court (2006);

- Wairakei Pastoral Limited in respect of water allocation for a proposed conversion of forestry land to dairy, including support for the evidence of Professor Lewis Evans (2007-2011);
- The Waiareka Preservation Society on a proposal to build a cement plant near Oamaru, including providing expert evidence before Resource Management Act Commissioners (2007);
- The Inland Revenue Department on the structured finance tax avoidance cases against the BNZ and Westpac, including support for the evidence of Professor Lewis Evans (2009);
- Telecom New Zealand in respect of the 0867 litigation brought by the Commerce Commission, including support for the evidence of Professor Lewis Evans (2007);
- Auckland Regional Transport Network in respect of litigation regarding access to slots at the Half Moon Bay ferry terminal, including support for the evidence of Professor Lewis Evans (2005);
- The Inland Revenue Department on the "Trinity" tax avoidance case, including support for the evidence of Professors Lewis Evans and Bradford Cornell (2005); and
- AFFCO on competition issues in the context of meat industry litigation with Anzco, including providing expert evidence before the High Court (2004).

Other Competition Advice

Economic analysis for:

- Fonterra in respect of the Commerce Commission's "Review of the state of competition in the New Zealand dairy industry" (2015-2016);
- Fletcher Building in respect of the Commerce Commission's investigation of alleged price fixing between certain PlaceMakers and Carters building supplies stores, including estimating the "overcharge" (2013);
- SKY TV in respect of the Commerce Commission's investigation of SKY's reseller contracts (2012-2013);
- A manufacturer in respect of damages caused to it by collusion between input suppliers (2012);
- A port in respect of pricing for access by a competitor (2011);
- A transport firm in respect of pricing for access to a potential new infrastructure investment (2010);
- A duty free retailing firm in respect of pricing for access to its scarce space (2010-2011);
- AmBreed regarding dairy database access pricing (2008-2009);
- Meridian Energy on competition issues (2002-2009);
- Two New Zealand airports on competition issues (2007-2010);
- A manufacturing firm in respect of rationalisation options (2008); and
- Manufacturing firms in respect of their retail rebate policies (2007 and 2009).

Regulatory

Economic analysis for:

- Meridian Energy on transmission pricing issues (2013-2017);
- Maui Development Limited in respect of Maui pipeline balancing issues (2014-2015);
- The Commerce Commission in respect of the price to be charged by Chorus for unbundled copper local loop and unbundled bitstream access services (2014-2015);
- Eastland Port in respect of pricing issues (2014);
- Aurizon (Queensland) on cost of capital issues (2013);
- Orion on issues relating to loss recovery following the Christchurch earthquakes (2013);
- Vector on gas pipeline governance issues (2012);
- The Gas Industry Company on gas pipeline capacity allocation and investment issues (2012-2013);
- Telecom on market definition, competition, the mandatory wholesaling regime, unbundling of the local loop and subloop, mobile termination rates and the TSO, including providing expert evidence before the Commerce Commission (2001-2013);
- New Zealand Post on regulatory issues (2007-2016);
- Auckland Airport on regulatory issues and price setting issues (2009-2013);
- Wellington Electricity on regulatory issues (2009);
- Vector on pricing and cost of capital issues (2005-2007);
- The New Zealand Treasury on economic regulation policy (2007);
- Unison in respect of the Commerce Commission's proposal to price control it (2005);
- Fonterra in respect of the regulatory proceedings brought before the Commerce Commission by Open Country Cheese Company (2005);
- NGC on the Commerce Commission's gas pipelines price control inquiry, and on governance issues in the gas industry (2003);
- Ergon Energy Corporation Limited on regulatory issues (2002);
- The Commerce Commission on the design of the new price control regime for electricity lines companies (2001); and
- The Singaporean Energy Market Authority on performance-based regulation (2001).

Public Policy

Economic analysis for:

- Perpetual Guardian regarding the value of the government guarantee to Public Trust (2015);
- Google in respect of the role of the internet and mobile computing on the competitiveness of Australian small business (2014);

- The Crown Law Office in respect of its review of the Crown prosecution services in the Auckland region (2014-2015);
- The Ministry of Agriculture and Forestry in respect of its review of the potential extension of regulation on Fonterra (2010);
- Turners & Growers in respect of the impact of the Zespri kiwifruit export monopoly on innovation incentives (2009);
- The Ministry of Agriculture and Forestry in respect of its review of the regulatory requirement on Fonterra to sell raw milk to rivals (2008);
- The Flexible Land Use Alliance in respect of the proposed treatment of pre-1990 forests under the proposed emissions trading system (ETS) (2008);
- Education New Zealand in respect of the efficiency of the export education levy (2005);
- The Department of Prime Minister and Cabinet of the competition implications of the proposed "competitiveness-at-risk" criteria for exemption from an emissions charge (2005);
- The Ministries of Transport and Economic Development of market power issues in the ports industry (2002); and
- A New Zealand company on business opportunities in an agribusiness sector (2001).

While Working at the New Zealand Commerce Commission (3-month contract)

- Advice on the design of the new price control regime for electricity lines companies (2001).

While Working at the New Zealand Treasury

- Telecommunications policy: Developed the Government's 2000 telecommunications reforms (in conjunction with Ministry of Economic Development officials).
- Radio spectrum allocation policy: Designed the spectrum caps and information disclosure rules in respect of the 2 GHz auction (in conjunction with Ministry of Economic Development officials).
- Competition policy: Appointed as Leader of the Treasury Competition Policy Cluster. Work included the analysis of the static-dynamic efficiency trade-off and price control issues.
- Dairy industry reform: Advised on the competition and regulatory policy aspects of the proposed merger between the two dominant processing co-operatives (Kiwi and New Zealand Dairy Group) and the New Zealand Dairy Board.
- Miscellaneous: Advised on various postal, electricity, e-commerce and capital markets policy issues.
- Retirement savings policy: Designed the regulatory policy aspects of the proposed Compulsory Retirement Savings Scheme.

While Working at Bell Gully

- Competition law: Advised on various Commerce Act matters, including a successful application to the Commerce Commission for clearance of a merger between two electricity supply authorities; presented seminars on competition law and policy in respect of utilities and essential facilities.
- Oil and gas sector: Advised on, drafted and negotiated oil and gas acquisitions, joint ventures and contracts; seconded for six weeks to a New Zealand oil and gas company.
- General corporate and commercial law: Advised on and negotiated mergers and acquisitions, and other business transactions; advising on various capital markets issues.

Publications, Speeches, Presentations, and Reports

Presenter at a debate organised by the Law and Economics Association of New Zealand on reform of section 36 of the Commerce Act, 3 November 2016.

"Levelling the Playing Field: The Role of the Internet and Mobile Computing in Improving the Efficiency and Competitiveness of Small Business", report prepared for the Australian Competition Policy Review at the request of Google, with Lawrence Wu, Professor Stephen King, Kristen Terris and Will Taylor, 17 November 2014.

Presenter on market definition at the Commerce Commission's "Competition Economists Roundtable", 27 February 2014.

Commentator on a paper titled "Price/margin squeezing", presented by Matt Sumpter (Partner, Chapman Tripp), at the Competition Law and Policy Institute of New Zealand 24th Annual Workshop, 3 August 2013.

"Quantifying Benefits and Costs under the Resource Management Act: Lessons from Commerce Commission Decision-making", with Kevin Counsell, NERA Working Paper, May 2013.

Economics editor of the loose-leaf/on-line updating service for *New Zealand Competition Law and Policy*, authored by Matt Sumpter, 2010, CCH New Zealand Limited, Auckland, 2012.

Commentator on a paper titled "Competition Policy and Digital Platforms", presented by Professor Howard Shelanski (Director, Bureau of Economics, Federal Trade Commission, and Professor of Law (on leave) Georgetown University), at the Competition Law and Policy Institute of New Zealand 23rd Annual Workshop, 3 August 2012.

Presenter at "Industrial Organisation and Competition Policy" course for New Zealand government officials, arranged by the New Zealand Institute for the Study of Competition and Regulation, 25-25 January 2011, Wellington.

"Objective RMA decision-making: Cost benefit analysis as an economic and practical framework", in *Resource Management Journal*, with Kevin Counsell and Lewis Evans, November 2010.

Contributor to *New Zealand Competition Law and Policy*, authored by Matt Sumpter, 2010, CCH New Zealand Limited, Auckland.

Commentator on a paper titled "Other Options for Reform and Policy/Economic Considerations", presented by Geoff McLay (Reader in Law, Victoria University of Wellington), at the *Leaky Homes – Saving the Titanic* conference held by the Legal Research Foundation, 17 September 2010.

"Assessing the Implications of Upstream Buyer Power on Downstream Consumers", in *Antitrust Insights*, with Kevin Counsell, Summer 2009. http://www.nera.com

"Competition Law in Hard Times – Some Comments", presented at the 20th Annual Workshop of The Competition Law and Policy Institute of New Zealand, 8 August 2009.

"Evolution of Electricity Lines Price Control," presented at an Institute for the Study of Competition and Regulation workshop, February 2008.

"Buyer Power – The Economic and Legal Framework," presented at the 8th Annual Competition Law and Regulation Review, with Kevin Counsell and David Blacktop, February 2008.

"Recent Developments in the Economic Analysis of Mergers," presented at the Advanced Competition and Fair Trading Law Conference 2007, 31 May 2007.

"Partial Acquisitions – The Economic Framework," presented at the 7th Annual Competition Law and Regulation Review, February 2007.

"The PGG/Wrightson Merger – Competition Issues," presented at the 5th Annual Mergers and Acquisitions Summit, March 2006.

"Market Definition with Differentiated Products," presented at the 6th Annual Competition Law and Regulation Review, February 2006.

"Recent Developments in the Commerce Commission's Economic Analysis of Mergers," presented at the 4th Annual Mergers and Acquisitions Conference, March 2005.

"Economics and Competition Law," presentation and booklet with James Palmer, for the New Zealand Law Society, September 2004.

"The Forest for the Trees," presented to the Competition Law Workshop, August 2004.

"Transaction Costs, Coordination, and Governance in Markets," presented to the Ministry of Economic Development, March 2004.

"Commerce Act Update," presented to the Auckland District Law Society, March 2004.

"The Economics of Unbundling Telecom's Fixed Network," presented at the 4th Annual Competition Law and Regulation Conference, February 2004.

"Regulation and Economic Efficiency - Some Thoughts on Policy and Practice," presentation and paper for the New Zealand Law Society, October 2003.

"The Practice of Collusion," presented to the Law and Economics Association of New Zealand, June 2003.

"Exchanging Price Information Can Be Efficient: Per Se Offences Should Be Legislated Very Sparingly," New Zealand Institute for the Study of Competition and Regulation Working Paper, with Lewis Evans (16 January 2003)
http://papers.ssrn.com/sol3/papers.cfm?abstract_id=374940

"What is the Objective of the Commerce Act,", in *Competition & Regulation Times*, New Zealand Institute for the Study of Competition and Regulation, Inc. (April 2002).

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IN THE AUSTRALIAN COMPETITION TRIBUNAL

ACT 1 of 2017

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Applicant:	Tabcorp Holdings Limited

ANNEXURE CERTIFICATE

This is the annexure marked **JM-2** annexed to the statement of **James Mellsop** dated 27 April 2017.

Annexure JM-2

Letter of instructions for James Mellsop

Filed on behalf of	Australian Competition and Consumer Commission		
Prepared by	Simon Uthmeyer		
Law firm	DLA Piper		
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Email	Simon.Uthmeyer@dlapiper.com		
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NEW ZEALAND

Your reference
ACT 1 of 2017

Our reference
ARP/ARP/3010528/638043
AUM/1215351564.1

25 April 2017

By Email : James.Mellsop@nera.com

Dear James

ACT 1 OF 2017 (APPLICATION BY TABCORP FOR MERGER AUTHORISATION) - LETTER OF INSTRUCTIONS

1 On 13 March 2017, Tabcorp Holdings Limited (**Tabcorp**) applied to the Australian Competition Tribunal (**Tribunal**) under section 95AU of the *Competition and Consumer Act 2010* (Cth) for merger authorisation for its proposed acquisition of the issued share capital of Tatts Group Limited (**Proposed Acquisition**).

2 The role of the Australian Competition and Consumer Commission (**ACCC**) in relation to Tabcorp's application is to assist the Tribunal.

3 You are retained by DLA Piper on behalf of the ACCC to provide an expert opinion on the following questions:

3.1 Review and comment upon the reports of Flavio Menezes, Christopher Pleatsikas, Ric Simes and Patrick Smith filed by Tabcorp.

3.2 Identify and assess any public detriments that are likely to arise as a result of the Proposed Acquisition, including in particular any competitive detriments.

3.3 Comment on whether the public benefits of the Proposed Acquisition claimed by Tabcorp have a real chance of happening, would be a result of the proposed merger, and are of substance, durable, quantifiable and of a lasting nature.

3.3.1 In assessing the public benefits, assume that transfers from corporate bookmakers to Tabcorp are welfare neutral and do not fall within section 95AZH(2)(a)(ii) of the Competition and Consumer Act.

3.3.2 In addition, as an alternative, assess the public benefits on the basis that Dr Simes' assumption at paragraph 53 of his report is adopted for additional revenue that could

be revenue taken from corporate bookmakers (in particular, that 50% of that additional revenue is allocated as the amount of substitution of overseas produced goods and services for domestically produced goods and services).

3.3.3 Comment on Dr Simes' assumption at paragraph 53 of his report.

3.4 Comment on whether the claimed public benefits of the Proposed Acquisition outweigh any public detriments that are likely to arise as a result of the Proposed Acquisition.

4 Where you reach conclusions in your report which are based on particular assumptions or other material, please make specific reference to the assumptions or materials which form the basis for your conclusions.

5 Attachment A to this letter contains a list of the documents we have provided to assist you with your opinions on the questions set out above.

Expert Guidelines

6 Attachment B to this letter is the Federal Court of Australia Expert Evidence Practice Note (GPN-EXPT) including Annexure A (Harmonised Expert Witness Code of Conduct) to that Practice Note. Please read the Practice Note carefully and ensure that your report complies with each of its elements. Please also confirm in your report that you have read and agree to be bound by the Practice Note.

Limitations and qualifications

7 You must qualify the opinion given in your report if either of the following apply:

7.1 you consider your report may be incomplete or inaccurate without the qualification; or

7.2 you are unable to form a conclusive opinion because of insufficient research, insufficient information, or for any other reason.

If you change your opinion

8 You must provide a supplementary report if you change your opinion after giving us your original report.

Confidentiality

9 Attachment C to this letter are the directions made by Justice Middleton of the Australian Competition Tribunal on 23 March 2017 in relation to access to and disclosure of confidential information in this matter. The directions impose obligations upon, amongst other people, independent experts engaged by the ACCC. Accordingly, you must comply with these directions.

We look forward to receiving your report.

Yours sincerely

ANNA PARKER
Senior Associate
DLA PIPER AUSTRALIA

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Anna.Parker@dlapiper.com

SIMON UTHMEYER
Partner
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Enc

ATTACHMENT A - DOCUMENTS

1 Tabcorp's Form S Application and Annexures filed 13 March 2017

2 Tabcorp and Tatts Lay Witness Statements and Expert Reports (including annexures) of:

- 2.1 David Attenborough
- 2.2 Doug Freeman
- 2.3 Damien Johnston
- 2.4 Fiona Mead
- 2.5 Adam Rytenskild
- 2.6 Flavio Menezes
- 2.7 Christopher Pleatsikas
- 2.8 Ric Simes
- 2.9 Patrick Smith
- 2.10 Gregory Aldam
- 2.11 Richard Burt
- 2.12 John Dumesny
- 2.13 Eliot Forbes
- 2.14 Luke Gatehouse
- 2.15 Michael Grant
- 2.16 Ray Gunston
- 2.17 Andrew Harding
- 2.18 Paul Innes
- 2.19 David Jewell
- 2.20 Andrew Nicholl
- 2.21 Andrew O'Toole
- 2.22 Damien Raedler
- 2.23 Brenton Scott
- 2.24 Peter Stubbs

2.25 Peter V'landys

2.26 Genny Weston

2.27 John Yovich

2.28 Matthew Corby

2.29 Brett Dixon

2.30 John Lewis

2.31 Vaughn Lynch

2.32 James Watters

2.33 Robert Cooke

2.34 Frank Makryllos

2.35 Susan van der Merwe

2.36 Anne Tucker

3 Intervener Lay Witness Statements and Expert Reports (including annexures) of:

3.1 Nicholas Keenan

3.2 Timothy Moore-Barton

3.3 Andrew Twaits

3.4 Nicholas Tyshing

3.5 Andrew Catterall

3.6 Josh Blanksby

3.7 Alan Clayton

3.8 David Martin

3.9 Giles Thompson (second and third statement)

3.10 Simon Barrile

3.11 Julian Christian

3.12 Greg Houston

3.13 Tom Hird

4 Statement of Robert Hines.

ATTACHMENT B - FEDERAL COURT EXPERT EVIDENCE PRACTICE NOTE

FEDERAL COURT OF AUSTRALIA

EXPERT EVIDENCE PRACTICE NOTES (GPN-EXPT)

General Practice Note

1. INTRODUCTION

1.1 This practice note, including the *Harmonised Expert Witness Code of Conduct* ("**Code**") (see **Annexure A**) and the *Concurrent Expert Evidence Guidelines* ("**Concurrent Evidence Guidelines**") (see **Annexure B**), applies to any proceeding involving the use of expert evidence and must be read together with:

(a) the Central Practice Note (CPN-1), which sets out the fundamental principles concerning the National Court Framework ("**NCF**") of the Federal Court and key principles of case management procedure;

(b) the Federal Court of Australia Act 1976 (Cth) ("**Federal Court Act**");

(c) the *Evidence Act 1995* (Cth) ("**Evidence Act**"), including Part 3.3 of the Evidence Act;

(d) Part 23 of the *Federal Court Rules 2011* (Cth) ("**Federal Court Rules**"); and

(e) where applicable, the Survey Evidence Practice Note (GPN-SURV).

1.2 This practice note takes effect from the date it is issued and, to the extent practicable, applies to proceedings whether filed before, or after, the date of issuing.

2. APPROACH TO EXPERT EVIDENCE

2.1 An expert witness may be retained to give opinion evidence in the proceeding, or, in certain circumstances, to express an opinion that may be relied upon in alternative dispute resolution procedures such as mediation or a conference of experts. In some circumstances an expert may be appointed as an independent adviser to the Court.

2.2 The purpose of the use of expert evidence in proceedings, often in relation to complex subject matter, is for the Court to receive the benefit of the objective and impartial assessment of an issue from a witness with specialised knowledge (based on training, study or experience - see generally s 79 of the Evidence Act).

2.3 However, the use or admissibility of expert evidence remains subject to the overriding requirements that:

(a) to be admissible in a proceeding, any such evidence must be relevant (s 56 of the Evidence Act); and

(b) even if relevant, any such evidence, may be refused to be admitted by the Court if its probative value is outweighed by other considerations such as the evidence

being unfairly prejudicial, misleading or will result in an undue waste of time (s 135 of the Evidence Act).

2.4 An expert witness' opinion evidence may have little or no value unless the assumptions adopted by the expert (ie. the facts or grounds relied upon) and his or her reasoning are expressly stated in any written report or oral evidence given.

2.5 The Court will ensure that, in the interests of justice, parties are given a reasonable opportunity to adduce and test relevant expert opinion evidence. However, the Court expects parties and any legal representatives acting on their behalf, when dealing with expert witnesses and expert evidence, to at all times comply with their duties associated with the overarching purpose in the Federal Court Act (see ss 37M and 37N).

3. INTERACTION WITH EXPERT WITNESSES

3.1 Parties and their legal representatives should never view an expert witness retained (or partly retained) by them as that party's advocate or "hired gun". Equally, they should never attempt to pressure or influence an expert into conforming his or her views with the party's interests.

3.2 A party or legal representative should be cautious not to have inappropriate communications when retaining or instructing an independent expert, or assisting an independent expert in the preparation of his or her evidence. However, it is important to note that there is no principle of law or practice and there is nothing in this practice note that obliges a party to embark on the costly task of engaging a "consulting expert" in order to avoid "contamination" of the expert who will give evidence. Indeed the Court would generally discourage such costly duplication.

3.3 Any witness retained by a party for the purpose of preparing a report or giving evidence in a proceeding as to an opinion held by the witness that is wholly or substantially based in the specialised knowledge of the witness[1] should, at the earliest opportunity, be provided with:

(a) a copy of this practice note, including the Code (see Annexure A); and

(b) all relevant information (whether helpful or harmful to that party's case) so as to enable the expert to prepare a report of a truly independent nature.

3.4 Any questions or assumptions provided to an expert should be provided in an unbiased manner and in such a way that the expert is not confined to addressing selective, irrelevant or immaterial issues.

[1] Such a witness includes a "Court expert" as defined in r 23.01 of the Federal Court Rules. For the definition of "expert", "expert evidence" and "expert report" see the Dictionary, in Schedule 1 of the Federal Court Rules.

4. ROLE AND DUTIES OF THE EXPERT WITNESS

4.1 The role of the expert witness is to provide relevant and impartial evidence in his or her area of expertise. An expert should never mislead the Court or become an advocate for the cause of the party that has retained the expert.

4.2 It should be emphasised that there is nothing inherently wrong with experts disagreeing or failing to reach the same conclusion. The Court will, with the assistance of the evidence of the experts, reach its own conclusion.

4.3 However, experts should willingly be prepared to change their opinion or make concessions when it is necessary or appropriate to do so, even if doing so would be contrary to any previously held or expressed view of that expert.

Harmonised Expert Witness Code of Conduct

4.4 Every expert witness giving evidence in this Court must read the *Harmonised Expert Witness Code of Conduct* (attached in Annexure A) and agree to be bound by it.

4.5 The Code is not intended to address all aspects of an expert witness' duties, but is intended to facilitate the admission of opinion evidence, and to assist experts to understand in general terms what the Court expects of them. Additionally, it is expected that compliance with the Code will assist individual expert witnesses to avoid criticism (rightly or wrongly) that they lack objectivity or are partisan.

5. CONTENTS OF AN EXPERT'S REPORT AND RELATED MATERIAL

5.1 The contents of an expert's report must conform with the requirements set out in the Code (including clauses 3 to 5 of the Code).

5.2 In addition, the contents of such a report must also comply with r 23.13 of the Federal Court Rules. Given that the requirements of that rule significantly overlap with the requirements in the Code, an expert, unless otherwise directed by the Court, will be taken to have complied with the requirements of r 23.13 if that expert has complied with the requirements in the Code and has complied with the additional following requirements. The expert shall:

(a) acknowledge in the report that:

(i) the expert has read and complied with this practice note and agrees to be bound by it; and

(ii) the expert's opinions are based wholly or substantially on specialised knowledge arising from the expert's training, study or experience;

(b) identify in the report the questions that the expert was asked to address;

(c) sign the report and attach or exhibit to it copies of:

(i) documents that record any instructions given to the expert; and

(ii) documents and other materials that the expert has been instructed to consider.

5.3 Where an expert's report refers to photographs, plans, calculations, analyses, measurements, survey reports or other extrinsic matter, these must be provided to the other parties at the same time as the expert's report.

6. CASE MANAGEMENT CONSIDERATIONS

6.1 Parties intending to rely on expert evidence at trial are expected to consider between them and inform the Court at the earliest opportunity of their views on the following:

(a) whether a party should adduce evidence from more than one expert in any single discipline;

(b) whether a common expert is appropriate for all or any part of the evidence;

(c) the nature and extent of expert reports, including any in reply;

(d) the identity of each expert witness that a party intends to call, their area(s) of expertise and availability during the proposed hearing;

(e) the issues that it is proposed each expert will address;

(f) the arrangements for a conference of experts to prepare a joint-report (see Part 7 of this practice note);

(g) whether the evidence is to be given concurrently and, if so, how (see Part 8 of this practice note); and

(h) whether any of the evidence in chief can be given orally.

6.2 It will often be desirable, before any expert is retained, for the parties to attempt to agree on the question or questions proposed to be the subject of expert evidence as well as the relevant facts and assumptions. The Court may make orders to that effect where it considers it appropriate to do so.

7. CONFERENCE OF EXPERTS AND JOINT-REPORT

7.1 Parties, their legal representatives and experts should be familiar with aspects of the Code relating to conferences of experts and joint-reports (see clauses 6 and 7 of the Code attached in Annexure A).

7.2 In order to facilitate the proper understanding of issues arising in expert evidence and to manage expert evidence in accordance with the overarching purpose, the Court may require experts who are to give evidence or who have produced reports to meet for the purpose of identifying and addressing the issues not agreed between them with a view to reaching agreement where this is possible ("**conference of experts**"). In an appropriate case, the Court may appoint a registrar of the Court or some other suitably qualified person ("**Conference Facilitator**") to act as a facilitator at the conference of experts.

7.3 It is expected that where expert evidence may be relied on in any proceeding, at the earliest opportunity, parties will discuss and then inform the Court whether a conference of experts and/or a joint-report by the experts may be desirable to assist with or simplify the giving of expert evidence in the proceeding. The parties should discuss the necessary arrangements for any conference and/or joint-report. The arrangements discussed between the parties should address:

(a) who should prepare any joint-report;

(b) whether a list of issues is needed to assist the experts in the conference and, if so, whether the Court, the parties o r the experts should assist in preparing such a list;

(c) **t**he agenda for the conference of experts; and

(d) arrangements for the provision, to the parties and the Court, of any joint-report or any other report as to the outcomes of the conference ("**conference report**").

Conference of Experts

7.4 The purpose of the conference of experts is for the experts to have a comprehensive discussion of issues relating to their field of expertise, with a view to identifying matters and issues in a proceeding about which the experts agree, partly agree or disagree and why. For this reason the conference is attended only by the experts and any Conference Facilitator. Unless the Court orders otherwise, the parties' lawyers will not attend the conference but will be provided with a copy of any conference report.

7.5 The Court may order that a conference of experts occur in a variety of circumstances, depending on the views of the judge and the parties and the needs of the case, including:

(a) while a case is in mediation. When this occurs the Court may also order that the outcome of the conference or any document disclosing or summarising the experts' opinions be confidential to the parties while the mediation is occurring;

(b) before the experts have reached a final opinion on a relevant question or the facts involved in a case. When this occurs the Court may order that the parties exchange draft expert reports and that a conference report be prepared for the use of the experts in finalising their reports;

(c) after the experts' reports have been provided to the Court but before the hearing of the experts' evidence. When this occurs the Court may also order that a conference report be prepared (jointly or otherwise) to ensure the efficient hearing of the experts' evidence.

7.6 Subject to any other order or direction of the Court, the parties and their lawyers must not involve themselves in the conference of experts process. In particular, they must not seek to encourage an expert not to agree with another expert or otherwise seek to influence the outcome of the conference of experts. The experts should raise any queries they may have in relation to the process with the Conference Facilitator (if one has been appointed) or in

accordance with a protocol agreed between the lawyers prior to the conference of experts taking place (if no Conference Facilitator has been appointed).

7.7 Any list of issues prepared for the consideration of the experts as part of the conference of experts process should be prepared using non-tendentious language.

7.8 The timing and location of the conference of experts will be decided by the judge or a registrar who will take into account the location and availability of the experts and the Court's case management timetable. The conference may take place at the Court and will usually be conducted in-person. However, if not considered a hindrance to the process, the conference may also be conducted with the assistance of visual or audio technology (such as via the internet, video link and/or by telephone).

7.9 Experts should prepare for a conference of experts by ensuring that they are familiar with all of the material upon which they base their opinions. Where expert reports in draft or final form have been exchanged prior to the conference, experts should attend the conference familiar with the reports of the other experts. Prior to the conference, experts should also consider where they believe the differences of opinion lie between them and what processes and discussions may assist to identify and refine those areas of difference.

Joint-report

7.10 At the conclusion of the conference of experts, unless the Court considers it unnecessary to do so, it is expected that the experts will have narrowed the issues in respect of which they agree, partly agree or disagree in a joint-report. The joint-report should be clear, plain and concise and should summarise the views of the experts on the identified issues, including a succinct explanation for any differences of opinion, and otherwise be structured in the manner requested by the judge or registrar.

7.11 In some cases (and most particularly in some native title cases), depending on the nature, volume and complexity of the expert evidence a judge may direct a registrar to draft part, or all, of a conference report. If so, the registrar will usually provide the draft conference report to the relevant experts and seek their confirmation that the conference report accurately reflects the opinions of the experts expressed at the conference. Once that confirmation has been received the registrar will finalise the conference report and provide it to the intended recipient(s).

8. CONCURRENT EXPERT EVIDENCE

8.1 The Court may determine that it is appropriate, depending on the nature of the expert evidence and the proceeding generally, for experts to give some or all of their evidence concurrently at the final (or other) hearing.

8.2 Parties should familiarise themselves with the *Concurrent Expert Evidence Guidelines* (attached in Annexure B). The Concurrent Evidence Guidelines are not intended to be exhaustive but indicate the circumstances when the Court might consider it appropriate for

concurrent expert evidence to take place, outline how that process may be undertaken, and assist experts to understand in general terms what the Court expects of them.

8.3 If an order is made for concurrent expert evidence to be given at a hearing, any expert to give such evidence should be provided with the Concurrent Evidence Guidelines well in advance of the hearing and should be familiar with those guidelines before giving evidence.

9. FURTHER PRACTICE INFORMATION AND RESOURCES

9.1 Further information regarding Expert Evidence and Expert Witnesses is available on the Court's website.

9.2 Further information to assist litigants, including a range of helpful guides, is also available on the Court's website. This information may be particularly helpful for litigants who are representing themselves.

J L B ALLSOP
Chief Justice
25 October 2016

Annexure A

HARMONISED EXPERT WITNESS CODE OF CONDUCT[2]

APPLICATION OF CODE

1. This Code of Conduct applies to any expert witness engaged or appointed:

   (a) to provide an expert's report for use as evidence in proceedings or proposed proceedings; or

   (b) to give opinion evidence in proceedings or proposed proceedings.

GENERAL DUTIES TO THE COURT

2. An expert witness is not an advocate for a party and has a paramount duty, overriding any duty to the party to the proceedings or other person retaining the expert witness, to assist the Court impartially on matters relevant to the area of expertise of the witness.

CONTENT OF REPORT

3. Every report prepared by an expert witness for use in Court shall clearly state the opinion or opinions of the expert and shall state, specify or provide:

   (a) the name and address of the expert;

   (b) an acknowledgment that the expert has read this code and agrees to be bound by it;

   (c) the qualifications of the expert to prepare the report;

   (d) the assumptions and material facts on which each opinion expressed in the report is based [a letter of instructions may be annexed];

   (e) the reasons for and any literature or other materials utilised in support of such opinion;

   (f) (if applicable) that a particular question, issue or matter falls outside the expert's field of expertise;

   (g) any examinations, tests or other investigations on which the expert has relied, identifying the person who carried them out and that person's qualifications;

   (h) the extent to which any opinion which the expert has expressed involves the acceptance of another person's opinion, the identification of that other person and the opinion expressed by that other person;

   (i) a declaration that the expert has made all the inquiries which the expert believes are desirable and appropriate (save for any matters identified explicitly in the report), and that no matters of significance which the expert regards as relevant have, to the

[2] Approved by the Council of Chief Justices' Rules Harmonisation Committee

knowledge of the expert, been withheld from the Court;

(j) any qualifications on an opinion expressed in the report without which the report is or may be incomplete or inaccurate;

(k) whether any opinion expressed in the report is not a concluded opinion because of insufficient research or insufficient data or for any other reason; and

(l) where the report is lengthy or complex, a brief summary of the report at the beginning of the report.

SUPPLEMENTARY REPORT FOLLOWING CHANGE OF OPINION

4. Where an expert witness has provided to a party (or that party's legal representative) a report for use in Court, and the expert thereafter changes his or her opinion on a material matter, the expert shall forthwith provide to the party (or that party's legal representative) a supplementary report which shall state, specify or provide the information referred to in paragraphs (a), (d), (e), (g), (h), (i), (j), (k) and (l) of clause 3 of this code and, if applicable, paragraph (f) of that clause.

5. In any subsequent report (whether prepared in accordance with clause 4 or not) the expert may refer to material contained in the earlier report without repeating it.

DUTY TO COMPLY WITH THE COURT'S DIRECTIONS

6. If directed to do so by the Court, an expert witness shall:

(a) confer with any other expert witness;

(b) provide the Court with a joint-report specifying (as the case requires) matters agreed and matters not agreed and the reasons for the experts not agreeing; and

(c) abide in a timely way by any direction of the Court.

CONFERENCE OF EXPERTS

7. Each expert witness shall:

(a) exercise his or her independent judgment in relation to every conference in which the expert participates pursuant to a direction of the Court and in relation to each report thereafter provided, and shall not act on any instruction or request to withhold or avoid agreement; and

(b) endeavour to reach agreement with the other expert witness (or witnesses) on any issue in dispute between them, or failing agreement, endeavour to identify and clarify the basis of disagreement on the issues which are in dispute.

ANNEXURE B

CONCURRENT EXPERT EVIDENCE GUIDELINES

APPLICATION OF THE COURT'S GUIDELINES

1. The Court's Concurrent Expert Evidence Guidelines ("**Concurrent Evidence Guidelines**") are intended to inform parties, practitioners and experts of the Court's general approach to concurrent expert evidence, the circumstances in which the Court might consider expert witnesses giving evidence concurrently and, if so, the procedures by which their evidence may be taken.

OBJECTIVES OF CONCURRENT EXPERT EVIDENCE TECHNIQUE

2. The use of concurrent evidence for the giving of expert evidence at hearings as a case management technique[3] will be utilised by the Court in appropriate circumstances (see r 23.15 of the *Federal Court Rules 2011* (Cth)). Not all cases will suit the process. For instance, in some patent cases, where the entire case revolves around conflicts within fields of expertise, concurrent evidence may not assist a judge. However, patent cases should not be excluded from concurrent expert evidence processes.

3. In many cases the use of concurrent expert evidence is a technique that can reduce the partisan or confrontational nature of conventional hearing processes and minimises the risk that experts become "opposing experts" rather than independent experts assisting the Court. It can elicit more precise and accurate expert evidence with greater input and assistance from the experts themselves.

4. When properly and flexibly applied, with efficiency and discipline during the hearing process, the technique may also allow the experts to more effectively focus on the critical points of disagreement between them, identify or resolve those issues more quickly, and narrow the issues in dispute. This can also allow for the key evidence to be given at the same time (rather than being spread across many days of hearing); permit the judge to assess an expert more readily, whilst allowing each party a genuine opportunity to put and test expert evidence. This can reduce the chance of the experts, lawyers and the judge misunderstanding the opinions being expressed by the experts.

5. It is essential that such a process has the full cooperation and support of all of the individuals involved, including the experts and counsel involved in the questioning process. Without that cooperation and support the process may fail in its objectives and even hinder the case management process.

[3] Also known as the "hot tub" or as "expert panels".

CASE MANAGEMENT

6. Parties should expect that, the Court will give careful consideration to whether concurrent evidence is appropriate in circumstances where there is more than one expert witness having the same expertise who is to give evidence on the same or related topics. Whether experts should give evidence concurrently is a matter for the Court, and will depend on the circumstances of each individual case, including the character of the proceeding, the nature of the expert evidence, and the views of the parties.

7. Although this consideration may take place at any time, including the commencement of the hearing, if not raised earlier, parties should raise the issue of concurrent evidence at the first appropriate case management hearing, and no later than any pre-trial case management hearing, so that orders can be made in advance, if necessary. To that end, prior to the hearing at which expert evidence may be given concurrently, parties and their lawyers should confer and give general consideration as to:

   (a) the agenda;

   (b) the order and manner in which questions will be asked; and

   (c) whether cross-examination will take place within the context of the concurrent evidence or after its conclusion.

8. At the same time, and before any hearing date is fixed, the identity of all experts proposed to be called and their areas of expertise is to be notified to the Court by all parties.

9. The lack of any concurrent evidence orders does not mean that the Court will not consider using concurrent evidence without prior notice to the parties, if appropriate.

CONFERENCE OF EXPERTS & JOINT-REPORT OR LIST OF ISSUES

10. The process of giving concurrent evidence at hearings may be assisted by the preparation of a joint-report or list of issues prepared as part of a conference of experts.

11. Parties should expect that, where concurrent evidence is appropriate, the Court may make orders requiring a conference of experts to take place or for documents such as a joint-report to be prepared to facilitate the concurrent expert evidence process at a hearing (see Part 7 of the Expert Evidence Practice Note).

PROCEDURE AT HEARING

12. Concurrent expert evidence may be taken at any convenient time during the hearing, although it will often occur at the conclusion of both parties' lay evidence.

13. At the hearing itself, the way in which concurrent expert evidence is taken must be applied flexibly and having regard to the characteristics of the case and the nature of the evidence to be given.

14. Without intending to be prescriptive of the procedure, parties should expect that, when evidence is given by experts in concurrent session:

(a) the judge will explain to the experts the procedure that will be followed and that the nature of the process may be different to their previous experiences of giving expert evidence;

(b) the experts will be grouped and called to give evidence together in their respective fields of expertise;

(c) the experts will take the oath or affirmation together, as appropriate;

(d) the experts will sit together with convenient access to their materials for their ease of reference, either in the witness box or in some other location in the courtroom, including (if necessary) at the bar table;

(e) each expert may be given the opportunity to provide a summary overview of their current opinions and explain what they consider to be the principal issues of disagreement between the experts, as they see them, in their own words;

(f) the judge will guide the process by which evidence is given, including, where appropriate:

(i) using any joint-report or list of issues as a guide for all the experts to be asked questions by the judge and counsel, about each issue on an issue-by-issue basis;

(ii) ensuring that each expert is given an adequate opportunity to deal with each issue and the exposition given by other experts including, where considered appropriate, each expert asking questions of other experts or supplementing the evidence given by other experts;

(iii) inviting legal representatives to identify the topics upon which they will cross-examine;

(iv) ensuring that legal representatives have an adequate opportunity to ask all experts questions about each issue. Legal representatives may also seek responses or contributions from one or more experts in response to the evidence given by a different expert; and

(v) allowing the experts an opportunity to summarise their views at the end of the process where opinions may have been changed or clarifications are needed.

15. The fact that the experts may have been provided with a list of issues for consideration does not confine the scope of any cross-examination of any expert. The process of cross-examination remains subject to the overall control of the judge.

16. The concurrent session should allow for a sensible and orderly series of exchanges between expert and expert, and between expert and lawyer. Where appropriate, the judge may allow for more traditional cross-examination to be pursued by a legal representative on a particular issue exclusively with one expert. Where that occurs, other experts may be asked to comment on the evidence given.

17. Where any issue involves only one expert, the party wishing to ask questions about that issue should let the judge know in advance so that consideration can be given to whether

arrangements should be made for that issue to be dealt with after the completion of the concurrent session. Otherwise, as far as practicable, questions (including in the form of cross-examination) will usually be dealt with in the concurrent session.

18. Throughout the concurrent evidence process the judge will ensure that the process is fair and effective (for the parties and the experts), balanced (including not permitting one expert to overwhelm or overshadow any other expert), and does not become a protracted or inefficient process.

ATTACHMENT C - CONFIDENTIALITY DIRECTIONS

[PUBLIC VERSION]

COMMONWEALTH OF AUSTRALIA

***Competition and Consumer Act 2010* (Cth)**

IN THE AUSTRALIAN COMPETITION TRIBUNAL

File No:	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 (ACN 063 780 709

DIRECTIONS

TRIBUNAL:	Justice Middleton (President)
DATE OF ORDER:	23 March 2017
WHERE MADE:	Melbourne

THE TRIBUNAL DIRECTS THAT:

1. This order is made by the Australian Competition Tribunal for the purposes of section 106(2) of the *Competition and Consumer Act 2010* (Cth).

Definitions used in these directions

2. The following defined terms apply for the purposes of these Orders:
   (a) **Act** means *Competition and Consumer Act 2010* (Cth).
   (b) **Commission** means the Australian Competition and Consumer Commission.
   (c) **Confidentiality Claimant** means, in respect of particular Confidential Information, the person or entity who made a claim of confidentiality in respect of that information.
   (d) **Confidential Information** means all information filed with the Tribunal in the Proceeding in respect of which a claim of confidentiality has been made and which has not been refused by the Tribunal and which has been marked either 'Confidential' or 'HIGHLY Confidential'.
   (e) **Intervener** means a person or entity which:

i. has made an application for leave to intervene in the Proceeding which has not been refused by the Tribunal; or

ii. is permitted by the Tribunal pursuant to section 109(2) of the Act to intervene in the Proceeding.

(f) **Orders** means these orders dated 23 March 2017.

(g) **Proceeding** means ACT 1 of 2017 (including any appeals from a decision of the Tribunal in the Proceeding).

(h) **Support Staff** means persons providing administrative assistance and includes secretaries, administrative assistants, graduates, IT staff, print room staff and staff of external printing vendors.

(i) **Tabcorp** means Tabcorp Holdings Limited.

(j) **Tatts** means Tatts Group Limited.

(k) **Tribunal** means Australian Competition Tribunal.

Access to Confidential Information

3. The following persons have unrestricted access to the Confidential Information marked either 'Confidential' or 'HIGHLY Confidential', provided such persons keep that material confidential in accordance with these Orders:

(a) the Tribunal, Tribunal staff and any other person assisting the Tribunal;

(b) the Commission, Commission staff and any other person assisting the Commission in relation to the Proceeding including the Commission's external barristers and solicitors;

(c) external consultants and independent experts engaged for the purpose of the Proceeding by the Commission (or the Commission's external solicitors), provided that the Commission's external solicitors have notified the relevant Confidentiality Claimant of the names of such persons; and

(d) Support Staff of the persons listed in 3(a)-(c) of these Orders.

4. The following persons have unrestricted access to the Confidential Information marked either 'Confidential' or 'HIGHLY confidential', provided that such persons have signed the confidentiality undertaking in the form attached and marked "Confidentiality Undertaking":

(a) external barristers and solicitors retained by Tabcorp or by Tatts or by any Intervener for the purpose of the Proceeding;

(b) independent experts retained for the purposes of the Proceeding by Tabcorp or by Tatts or by any Intervener (or their external solicitors), with the prior written consent of the Confidentiality Claimant;

(c) any other person, with the prior written consent of the Confidentiality Claimant; and

(d) Support Staff of the persons listed in paragraphs 4(a)-4(c) of these Orders.

5. The following persons have unrestricted access to the Confidential Information marked 'Confidential', provided that such persons have signed the confidentiality undertaking in the form attached and marked "Confidentiality Undertaking":

(a) internal legal counsel of Tabcorp or Tatts who directly assist with the day to day conduct of the Proceeding;

(b) any other person, with the prior written consent of the Confidentiality Claimant; and

(c) Support Staff of the persons listed in paragraphs 5(a) of these Orders.

General orders as to confidentiality

6. On 2 days' notice to the Confidentiality Claimant, the Commission, Tabcorp, Tatts, any other Intervener and any other interested person has liberty to apply for a direction seeking access to Confidential Information. The relevant Confidentiality Claimant and the Commission will be provided with an opportunity to be heard before the Confidential Information is disclosed to any person other than as permitted by these Orders.

7. Until further order of the Tribunal, Confidential Information is not to appear in any transcript of the Proceeding before the Tribunal other than in a confidential copy of the transcript, which shall only be made available to the persons referenced in paragraph 3 of these Orders and otherwise, as permitted by these Orders.

8. Any notice given, or materials that are filed and served in the Proceeding may be given or filed and served by email to the following email addresses:

(a) Email address for the Tribunal is registry@competitiontribunal.gov.au

(b) Email addresses for Tabcorp are Grant.Marjoribanks@hsf.com and smuys@gtlaw.com.au

(c) Email address for the Commission is Simon.Uthmeyer@dlapiper.com

(d) Email address for Tatts is mcorrigan@claytonutz.com

9. Tabcorp, the Commission, any Intervener and any interested person have general liberty to apply for further directions.

Date entered: 23 March 2017

REGISTRAR
Australian Competition Tribunal

[PUBLIC VERSION]

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

ANNEXURE CERTIFICATE

This is the confidential annexure marked **JM-3** annexed to the statement of **James Mellsop** dated 27 April 2017.

Annexure JM-3

Report of James Mellsop

Filed on behalf of	Australian Competition and Consumer Commission		
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[PUBLIC VERSION]

Tabcorp/Tatts: expert economic report of James Mellsop

DLA Piper

27 April 2017

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1. Introduction

1. I am an economist and a Managing Director of NERA Economic Consulting, a global economic consulting firm. NERA Economic Consulting specialises in applying economic, finance, and quantitative principles to complex business and legal challenges.
2. My background and experience can be briefly summarised as follows:
   a) I have a Masters degree in economics (with distinction), an Honours degree in economics (First Class), an undergraduate degree in accountancy and a law degree, all from Victoria University of Wellington; and
   b) Broadly my consulting practice involves the application of economic analysis to legal issues, particularly in the areas of competition, regulation, contractual disputes, damages, fair trading, tax, and resource management.
3. More specifically of relevance to the present proceedings:
   a) I have analysed the competitive effects of numerous mergers in Australia and New Zealand. Particularly when these projects have involved authorisation applications, I have quantified both the competitive detriments and the public benefits of the proposed transactions; and
   b) I quantified the competitive effects and public benefits of the New Zealand Racing Board's proposed betting pool "commingling" arrangement with Tabcorp in 2016 (which was authorised by the New Zealand Commerce Commission).
4. In respect of the proposed merger between Tabcorp Holdings Limited (**Tabcorp**) and Tatts Group Limited (**Tatts**), I have been asked in my letter of instructions from DLA Piper on behalf of the ACCC to provide an expert opinion on the following questions:
   a) Review and comment upon the reports of Flavio Menezes, Christopher Pleatsikas, Ric Simes and Patrick Smith filed by Tabcorp;
   b) Identify and assess any public detriments that are likely to arise as a result of the Proposed Acquisition, including in particular any competitive detriments;
   c) Comment on whether the public benefits of the Proposed Acquisition claimed by Tabcorp have a real chance of happening, would be a result of the proposed merger, and are of substance, durable, quantifiable and of a lasting nature;
      i. In assessing the public benefits, assume that transfers from corporate bookmakers to Tabcorp are welfare neutral and do not fall within section 95AZH(2)(a)(ii) of the Competition and Consumer Act;
      ii. In addition, as an alternative, assess the public benefits on the basis that Dr Simes' assumption at paragraph 53 of his report is adopted for additional revenue that could be revenue taken from corporate bookmakers (in particular, that 50% of that additional revenue is allocated as the amount of substitution of overseas produced goods and services for domestically produced goods and services);
      iii. Comment on Dr Simes' assumption at paragraph 53 of his report; and

d) Comment on whether the claimed public benefits of the Proposed Acquisition outweigh any public detriments that are likely to arise as a result of the Proposed Acquisition.

5. I have also had an initial read of the expert statements of Mr Greg Houston (on behalf of CrownBet) and Dr Tom Hird (on behalf of Racing Victoria, Greyhound Racing Victoria and Harness Racing Victoria). However, because these statements were only filed on 21 April 2017, I have not had a chance to review them as carefully as I have the expert statements on behalf of the applicant. Accordingly, I do not have a particular focus on them in this report.
6. Following an executive summary (section 2), I start my report with an explanation of some key economic concepts that I will use in my report (section 3).
7. I then comment on each of the statements of the applicant's experts in turn (section 4 to 7). I then pull together my views on competitive effects, and the benefits and detriments of the proposed merger (section 8).
8. In preparing this report, I have been assisted by my colleagues Kevin Counsell, Craig Malam and Barbara Kaleff. However, the opinions in this report are my own and I take full responsibility for them.
9. I confirm that in the course of preparing this report, I have been provided with a copy of and read, understood and complied with the Federal Court of Australia Expert Evidence Practice Note (GPN-EXPT) including Annexure A (Harmonised Expert Witness Code of Conduct) to that Practice Note.

2. Executive summary

2.1. Competitive effects of merger

10. The quantity data filed in these proceedings show that tote turnover is decreasing, while fixed odds turnover for corporate bookmakers, Tabcorp and Tatts is increasing (dramatically). These data suggest that:

    a) Tote products and fixed odds products might be in the same market; and

    b) Corporate bookmakers might compete against Tabcorp and Tatts.

11. However, the filed pricing data raise questions about whether fixed odds products are in the same market as tote products. In particular:

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

    b) [redacted]

12. Taking the price and quantity data together suggests that, at a minimum, tote and fixed odds products are differentiated, and consistent with this, there appears to be value in owning a tote licence.[1]

13. In my view, Tabcorp and Tatts are each other's closest competitors. This competition occurs directly through the online channel, and is likely to intensify under the counterfactual. For as long as there continues to be no price (or other) discrimination between online and retail, retail customers would also benefit from this competition.

14. On balance, I think the experts for the applicant:

    a) Overstate the competitive constraint from corporate bookmakers; and

    b) Understate the competitive tension between Tabcorp and Tatts.

15. Accordingly I think the proposed merger is likely to lessen competition in the wagering market and there would be competitive detriments.

16. Indeed, I note that on the applicant's own analysis the merger is expected to result in an effective price increase [**Confidential to Tabcorp**] [redacted]. This would result in a detriment to consumers (punters).

17. 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.

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

2.2. Benefits of merger

19. There are two broad categories of benefits claimed by the applicant:

    a) Cost savings of [**Confidential to Tabcorp**] [redacted] from year 3 onwards; and

    b) Revenue synergies of [**Confidential to Tabcorp**] [redacted] from year 3 onwards.

20. A key consideration is whether the cost savings are merger-specific, and this has not been assessed by any of the applicant's experts, nor has there been a general test of their veracity. I would expect in a matter such as this that claimed cost savings would be independently verified. However if the Tribunal were to determine the claimed cost savings are merger-

[1] For example, see the analysis of Dr Hird at [170] of his affidavit. I note that Tabcorp paid $410m for the Victorian licence in 2012 (see https://www.tabcorp.com.au/news-media/media-releases/tabcorp-finalises-victorian-wagering-and-betting-l]) and $105.5m for the ACT TAB in 2014 (see https://www.tabcorp.com.au/news-media/media-releases/tabcorp-to-acquire-acttab).

specific and robust I have included cost savings (net of specific transfers) in my analysis. I also carry out come sensitivity testing of the cost savings in section 8.

21. Regarding the revenue synergies, these appear to reflect an increase in market share at the expense of corporate bookmaker rivals, or in some cases an effective price increase. If this is correct, they do not represent a public benefit, but simply a transfer (and possibly a detriment).

22. Relying on section 95AZH(2)(a)(ii) of the Competition and Consumer Act, Dr Simes (one of the experts for the applicant) states that a transfer of surplus from foreigners to Australians should be treated as a public benefit [46]. However, I have been instructed to assume that transfers from corporate bookmakers to Tabcorp are welfare neutral and do not fall within section 95AZH(2)(a)(ii). Accordingly, in my "base case" calculation of the benefits of the proposed merger, I do not include any of the claimed revenue synergies as benefits. However, I have also been instructed to run an alternative test in which I include some of these claimed revenue synergies.

23. Table 1 below reports the results of my (base case) benefits estimation in net present value (NPV) terms, using a 7% discount rate and different time periods over which the benefits are assessed (2, 5, and 10 years).[2] I also deduct some specific costs that are incurred to achieve the benefits (but which are separate to the competitive detriments, discussed below).

Table 1
NPV results of benefits less specific costs, base case [Confidential to Tabcorp]

Timeframe	NPV of benefits specific costs at 7% discount rate
2-year timeframe	$[redacted]
5-year timeframe	$[redacted]
10-year timeframe	$[redacted]

24. To provide some context to the materiality of the benefit results, I estimate how large the effective wagering market price increase (or equivalently, quality decrease) would have to be for the competitive detriments to offset the estimated benefits. This analysis is conservative, because I focus only on allocative efficiency detriments, when I would also expect there to be productive and dynamic efficiency detriments.

[2] I have also calculated the NPV over a 15-year timeframe, which returns a result of [**Confidential to Tabcorp**] [redacted].

25. The base case results are reported in Table 2 below, for a range of different increases (0.5%, 2.5% and 5%) in the effective average wagering price and different time periods over which the benefits are assessed (2, 5, and 10 years).[3]

Table 2
NPV results of allocative efficiency detriment for all wagering market, base case
[Confidential to Tabcorp]

Timeframe	NPV of allocative efficiency detriment at 7% discount rate 0.5% price increase	NPV of allocative efficiency detriment at 7% discount rate 2.5% price increase	NPV of allocative efficiency detriment at 7% discount rate 5% price increase
2-year timeframe	$[redacted]	$[redacted]	$[redacted]
5-year timeframe	$[redacted]	$[redacted]	$[redacted]
10-year timeframe	$[redacted]	$[redacted]	$[redacted]

26. It can be seen from Table 2 that a price increase (or equivalent quality decrease) of as little as 2.5% would more than offset the claimed benefits of the merger as set out in Table 1 above.

27. On balance, my analysis indicates that the claimed public benefits of the proposed merger are unlikely to outweigh the public detriments that I have analysed so far.

3. Key economic concepts

3.1. Introduction

28. Before reviewing the statements of the various experts, I explain some important economic concepts that I will use in my analysis in this report.

3.2. The price and quantity of wagering products

29. Competition analysis generally focuses on how prices and quantities of goods and services are impacted by particular actions (such as a merger), and how this in turn affects the benefits and costs of consumers and producers. For wagering products in particular, prices and quantities differ slightly from how they might be considered for other products, such as manufactured goods.

30. The total quantity of wagering services can be measured by the total dollar value of bets placed with the wagering providers. This is referred to as "turnover" in the wagering industry. Turnover differs from the wagering provider's revenue, which is the total dollar

[3] I have also calculated the NPV over a 15-year timeframe, which returns a result of [**Confidential to Tabcorp**] [redacted] for a 0.5% price rise, [**Confidential to Tabcorp**] [redacted] for a 2.5% price rise, and [**Confidential to Tabcorp**] [redacted] for a 5% price rise.

amount withheld or retained by the provider out of the bets that are placed. The difference between turnover and revenue is the amount of money that is paid out to winning punters. Suits (1979, p.156) points out that, even though wagering turnover and wagering revenue are both denominated in dollars, they are "conceptually distinct, and care should be taken to avoid confusing them. The total volume of wagers handled is no more "revenue" to a betting establishment than the total value of houses traded constitutes "revenue" to a real estate agent".[4]

31. 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".[5] Suits notes that this is the case regardless of how this take-out rate is arrived at, e.g., in pari-mutuel betting the take-out rate is set by the provider independently of the probability of winning, but in other forms of gambling it can be determined by the relationship between the amount paid to winners and the probability of winning. This take-out rate can be calculated as the revenue of the wagering provider as a percentage of turnover.

32. As a simple example, if 100 punters each bet $1 with a tote provider on the outcome of, say, a horse race, then the provider's turnover would be $100. At a take-out rate of 15%, the provider retains an average of 15c on each bet, or $15 revenue in total. It is this 15% rate that is the effective price of wagering: it is the amount paid by punters to the provider for the wagering service.

33. Consistent with this, Mr Nicholas Tyshing in his evidence refers to the price of wagering as the take-out rate that wagering providers retain from every dollar of bets placed with them [83], and this applies for both totalisator providers [84] and fixed odds providers [85]. I note also the evidence of Mr Damien Johnston defines the "yield" from fixed odds betting as "the proportion of turnover that fixed odds bookmakers retain after the payment of winnings", [66(b)]. Therefore the yield on fixed odds betting can be thought of as the effective price paid by punters.

3.3. Surplus, efficiency and transfers

34. Given the price and quantity of a wagering service, it is possible to conceptualise a standard downward sloping demand curve and upward sloping supply curve, as illustrated in Figure 1. The "equilibrium" price and quantity is given where the demand and supply curves intersect – at the price-quantity combination of P1-Q1.

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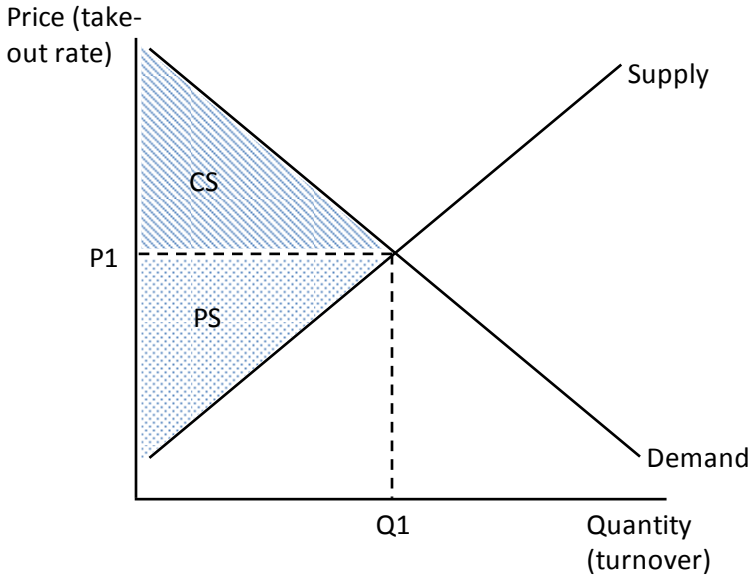
4 Daniel B. Suits (1979), "The elasticity of demand for gambling", *Quarterly Journal of Economics*, 91(3), 155-162.

5 Daniel B. Suits (1979), "The elasticity of demand for gambling", *Quarterly Journal of Economics*, 91(3), 155-162. See also Gruen (1976, p.174), stating that the take-out rate "serves the economic function of the purchase price of a bet" (Arthur Gruen (1976), "An Inquiry into the Economics of Race-Track Gambling", *Journal of Political Economy*, 84(1), 169-177); and more recently Gallet (2015, footnote 1) who states "Essentially, the price of gambling is measured by the expected loss of gambling, which is tied to the take-out rate (i.e., the percent of wagers not returned to the gambler)" (Craig A. Gallet (2015), "Gambling Demand: A Meta-Analysis of the Price Elasticity", *Journal of Gambling Business and Economics*, 9(1), 12-22).

35. Figure 1 also illustrates the economic concept of "surplus". Surplus, also referred to as welfare, represents the net benefits to consumers and producers from undertaking a transaction. It consists of consumer surplus and producer surplus. Consumer surplus is the total value that the consumer derives from purchasing goods or services (i.e., the maximum amount the consumer would be willing to pay), less the price that the consumer actually pays. It is shown in Figure 1 by the shaded triangle labelled "CS" – the area below the demand curve and above the price. Producer surplus is the price the producer receives less the amount that would be required to just induce the producer to supply the good or service. Producer surplus is the area above the supply curve and below the price, given by the shaded triangle labelled "PS".

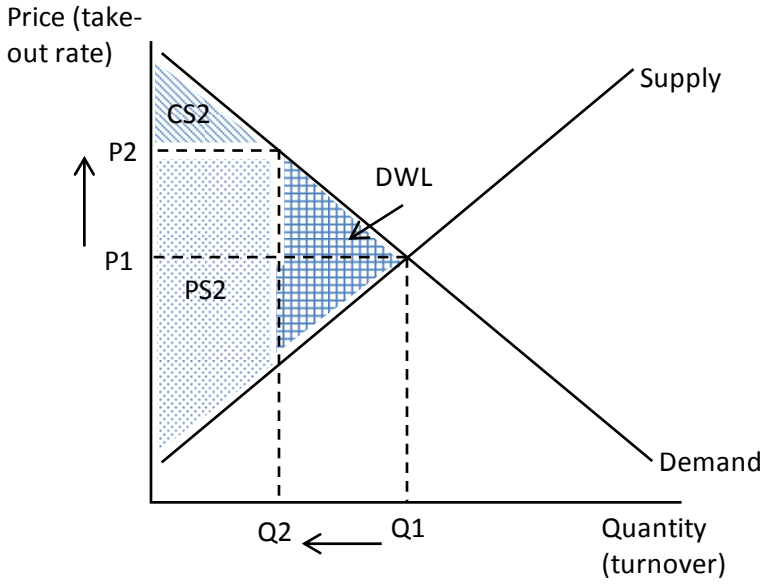
Figure 1
Stylised illustration of supply and demand in a wagering market



36. The equilibrium price and quantity of P1-Q1 is the point at which surplus is maximised. This is also sometimes referred to as the point at which economic efficiency is achieved. If prices and quantities deviate from this equilibrium, then there will be a reduction in surplus. Consider now Figure 2 in which the quantity of wagering has fallen to Q2 and the price has risen to P2 (due to, for example, a merger that lessens competition). The new consumer surplus and producer surplus are shown by the shaded areas labelled "CS2" and "PS2" respectively. The triangle labelled "DWL" is the reduction in consumer and producer surplus arising from the price and quantity changes. This is referred to as "deadweight loss" or an "allocative inefficiency", and represents a loss of surplus due to the changes in price and quantity. This reflects the fact that there are some consumers who would be willing to pay (as represented by the demand curve) more than it costs society to produce (as represented by the supply curve) the quantity between Q1 and Q2, but such transactions do not occur at a price-quantity combination of P2-Q2.

37. Figure 2 also illustrates the concept of a "transfer". It can be seen that, at the price-quantity combination P2-Q2, there is a rectangle between P2 and P1 and across to Q2 that makes up part of producer surplus. However, prior to the price and quantity changes, this rectangle was part of consumer surplus. This gain in producer surplus is therefore purely at the expense of a loss in consumer surplus. Changes in surplus of this nature represent transfers – they do not reflect a net change in total surplus, but rather a transfer of surplus from consumers to producers. While it is not shown in the diagram, surplus that is gained from one producer at the expense of other producers would also be categorised as a transfer, as would such changes to one consumer at the expense of other consumers.

Figure 2
Stylised illustration of surplus changes in a wagering market



4. Statement of Christopher Pleatsikas

4.1. Introduction

38. In this section I set out my comments on the evidence of Dr Christopher Pleatsikas. My headings follow those of Dr Pleatsikas.

4.2. Section IV – "Economic Theory and Principles for Competition Analysis"

39. In this section of his statement Dr Pleatsikas sets out the theory and principles that are generally relevant to competition analysis. I have no particular comments on this section, as it is essentially uncontroversial.

40. The only exception is where Dr Pleatsikas starts to discuss "measurement of other indicators of economic benefit" at [34]. I think some of the indicators he mentions are not orthodox from a competition analysis perspective (particularly "flow-on effects", employment and "fostering the growth in related economic activity"), and can in fact be quite problematic. Dr Pleatsikas does not really do much more than float these indicators, whereas the statement of Dr Simes is more focused on them (with the exception of employment). Accordingly I return to these issues in more detail in my discussion of Dr Simes' statement.

41. In respect of employment, Dr Pleatsikas states that *increases* in employment can be considered an indirect benefit of the proposed merger, at [34] and [181]. However, he provides no specific evidence that this will be the case, or what the impact would be. [**Confidential to Tabcorp**] [redacted]

4.3. Section V – "Economic Impact of the Proposed Acquisition"

4.3.1. Section V.1 – "Market Definition"

4.3.1.1. Licences

42. At [94], I interpret Dr Pleatsikas to be arguing that there is no need to define separate markets for:

    a) Acquiring licences; and

    b) Providing downstream (e.g., wagering) services that these licences are an input into.

43. While I agree that the value a bidder would place on one of these licences would be a function of competition in downstream markets, I still think it is appropriate to analyse competition to obtain licences separately from competition for downstream services. To use Dr Pleatsikas' own market definition framework [56-57], a licence is obtained at a different functional level to the downstream activities.

44. Indeed, I note that the statement of Professor Menezes focuses solely on bidding competition for licences, implying that this competition does take place in its own market. As Professor Menezes states [20], "the merger of two oil companies can have different competitive effects in auctions for oil and gas exploration rights and the wholesale market for oil, requiring separate analysis".

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

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

4.3.1.2. Wagering products

45. I agree with Dr Pleatsikas [97-98] that lotteries and Keno are likely to be in separate markets to wagering.

46. Regarding whether the various classes of wagering products (e.g., tote versus fixed odds, horse racing versus other sports) are in the same market, optimally we would have information on punter responses to relative price or quality changes (effectively an application of the SSNIP test that Dr Pleatsikas describes at [44-46]). I am not aware of such evidence in the present proceedings.

47. I agree with Dr Pleatsikas [102] that there is likely to be a high degree of supply-side substitutability across the various products. However, I understand that only state-licenced firms can offer tote products. Therefore it is important to consider whether tote products are constrained on the demand-side by other products (e.g., fixed odds products).

48. Some of the assumptions provided to Dr Pleatsikas are consistent with such a constraint, particularly the declining tote turnover at the same time as the increasing fixed odds turnover [Pleatsikas assumptions 137]. While not a test of punter responses to relative price changes, this evidence is at least suggestive of a substitutability relationship.

49. However, the pricing data contained in the assumptions are not consistent with this. I have graphed firstly (in Figure 3) the take-out rate (wagering revenue as a proportion of turnover - i.e. price) for each participant in the wagering industry, over the period FY12 to FY16. I have then graphed separately the take-out rate for each of Tabcorp and Tatts, split into totes, fixed odds, and sports wagering – see Figure 4 and Figure 5 respectively. Note that the Tabcorp data is over a longer time period (FY06 to FY16) than that for Tatts and the entire industry (both FY12 to FY16).

50. From these graphs, it can be seen that [**Confidential to Tabcorp**] [redacted][9].

[8] Analysis of data in Tab 2 of CP-2, TBP.001.018.5686.

[9] [**Highly Confidential to Tabcorp**] [redacted].

Figure 3
Wagering revenue as a proportion of turnover, all wagering industry, FY12-FY16[10]
[Confidential to Tabcorp and Tatts]

[10] I have excluded ToteTAS from this graph as there is only a single data point (for FY12) in the dataset, of [**Confidential to Tabcorp and Tatts**] [redacted]. Note also that the CrownBet data is obscured behind the "Others" line, but I have tried to illustrate the former's data points (which are only for FY15 and FY16) using a green X.

Figure 4
Tabcorp wagering revenue as a proportion of turnover by wagering type, FY06-FY16 [Confidential to Tabcorp]

Figure 5
Tatts wagering revenue as a proportion of turnover by wagering type, FY12-FY16 [Highly Confidential to Tatts]

51. This data raises some serious questions about whether fixed odds products do constrain tote products, and suggests that at the minimum, the products are differentiated. Corroboratively, I note the evidence of Mr Tyshing that around 2014 Tabcorp successfully lobbied for an increase in the maximum take-out rate in Victoria [345].

52. Statements by Mr Tyshing are consistent with Tabcorp and Tatts being able to charge higher prices, e.g., their less sophisticated, higher-margin, recreational customers [74] and the higher-value multi-channel customers [135] (according to a Tabcorp presentation annexed to Mr Tyshing's statement, "multi-channel customers deliver eight times more value than digital only customers"). [**Confidential to Tabcorp**] [redacted].

53. If fixed odds products compete with tote products, then it follows that the market is national, as Dr Pleatsikas states [105]. Even if we define separate tote and fixed odds product markets, the ability to buy both online also suggests that both markets would be national.

54. The strength of competition from digital on retail is not clear. I note from [Pleatsikas assumption 128] that retail turnover has [**Confidential to Tabcorp**] [redacted] in nominal terms between 2006 to 2015, which implies a [**Confidential to Tabcorp**] [redacted]. At the same time digital turnover has grown from [**Confidential to Tabcorp**] [redacted]. Therefore it appears that digital has grown the market, rather than cannibalise retail to a material degree. In his second statement, Mr Thompson makes a similar point [41]:

    The growth of corporate bookmakers and the increasing popularity of fixed-odds wagering, while attracting some previous customers of pari-mutuel wagering products, have also attracted considerable numbers of new customers into wagering.

55. Of course, the retail channels of Tabcorp and Tatts do not compete directly, as they are exclusively licenced by state. But this analysis is relevant when considering relative competitive advantage, which I return to in section 4.3.2 below, and for the discussion about wagering licences (see 6.2.5 below).

56. Furthermore, I note also that Mr Andrew Twaits in his statement states there is no price discrimination between retail tote customers (who Mr Twaits states are less price sensitive) and online tote customers (who Mr Twaits states are more price sensitive) [38(b)]. This suggests that the retail customers would benefit from competition for the online customers. As I discuss in respect of Mr Smith's evidence below, I think there is evidence of competition between Tabcorp and Tatts for online customers.

57. Finally, I agree with Dr Pleatsikas [107] that there may well be a distinct market for premium customers. As well as the pricing to these customers being quite distinct, I understand that these customers cannot use corporate bookmakers, as noted by Mr Tyshing [90]. On the other hand, these customers might have more global options.

58. I have not spent any time analysing market definition for lotteries and Keno products, as the proposed merger does not appear to raise any competition issues in respect of these products.

4.3.1.3. Broadcasting

59. Dr Pleatsikas' analysis of broadcasting market definition and more broadly broadcasting competition issues is not sufficient. In particular:
    a) He does not analyse the importance (or otherwise) of racing coverage to providers of wagering products; and
    b) He does not analyse whether there is a market for acquiring rights, and whether that market should be divided based on distribution mode (digital, FTA and pay TV).

4.3.2. Section V.2 – "Competitive Effects of the Proposed Acquisition"

4.3.2.1. Section V.2.1 – "Exclusive/Near Exclusive Licences"

60. Dr Pleatsikas argues the merger would not have any output effects in any markets for acquiring licences [137]. This is correct, in the sense that a state government would probably still issue a licence even if the merged entity was able to exercise market power.
61. Dr Pleatsikas then analyses whether the merger would have any effect on licence fees.
62. His first argument is that any effect would be so far into the future (2024) as to have little value in today's money [139(a)]. I think there are two issues to consider here:
    a) Whether there would be a competitive effect; and
    b) If so, the value we should ascribe to that effect in any cost benefit analysis today.
63. Regarding the former, I do not think distance in the future is relevant to this, except to the extent that the further into the future we look, the more uncertainties there are, and therefore the harder it is to make predictions.
64. Regarding the latter, it is true that the time value of money will reduce any quantified value of the detriment. But seven years' discounting does not make something valueless – as an example, $1 received today has a value of $0.62 in seven years' time, discounted at a 7% discount rate.[11]
65. Despite the views of Dr Pleatsikas, I note that Professor Menezes analyses bidding for licences in 2024, and I think this is close enough in time to be considered.
66. Dr Pleatsikas' second argument is that "there are apparently significant potential competitors for licences that do come up for renewal" [141]. This is of course a factual question, but I think the key issue is the relative strength of these potential bidders. This is not an issue that Dr Pleatsikas analyses in much detail (there is just a brief discussion at [143]), but it is at the core of Professor Menezes' evidence, and so I return to this issue when discussing his statement.

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[11] 7% is the discount rate used by Dr Simes [footnote 43].

67. Dr Pleatsikas points out at [144] and [147] that the price of exclusive licences is likely to be constrained by the ability of firms to instead compete using a non-exclusive licence. If, for example, we consider tote wagering and fixed odds wagering to be in the same market, then this is likely to be correct. However, the question of competition to provide wagering is distinct from that of competition to acquire the licenses. It is not relevant to the question of whether the proposed merger might result in a lower price being paid for exclusive licences compared to the counterfactual.

68. Dr Pleatsikas' third argument is that state governments can design the bidding rules in a way that mitigates any market power of bidders. This is likely to be correct to an extent, but does depend on the specific issues that might give rise to market power. Dr Pleatsikas does not analyse these issues in detail, but Professor Menezes does, and I return to these issues in my review of his evidence.

4.3.2.2. Section V.2.2 – "Market for Wagering Products"

69. I have already described the pricing evidence that raises questions about the constraint imposed by fixed odds products on tote products. I return to the implications of a narrower market definition later in my report (section 8.3). But at this stage I assume that Dr Pleatsikas is correct to define a broad wagering market.

70. At [153] Dr Pleatsikas refers to the assumptions he has been given regarding the claimed competitive advantages of bookmakers over totalisators. These assumptions are consistent with [**Highly Confidential - derived confidential information**] [redacted], as set out in Figure 3, Figure 4 and Figure 5 above, and the evidence of the increasing share of corporate bookmakers in the wagering market.

71. However, Mr Tyshing states that totes have competitive advantages over bookmakers [376]. If Mr Tyshing is correct, this might explain why it is that [**Highly Confidential - derived confidential information**] [redacted]. See Figure 3, Figure 4 and Figure 5 again. I note that [**Highly Confidential to Tabcorp**] [redacted][12]

72. I think 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 and Tatts**] [redacted] have been growing their turnover over the last five years,[13] 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.

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[12] Tab 47 of DF-3, TBP.003.001.1096_1104.

[13] See [Simes assumptions 26].

73. Dr Pleatsikas also refers at [157] to claims that Tabcorp and Tatts have responded in various ways to the corporate bookmaker competition, such as Tabcorp's launching of Luxbet and introduction of other products. While these are consistent with responding to corporate bookmaker pressure, they are also consistent with responding to pressure from each other, particularly in the online channel.

74. However, one issue that Dr Pleatsikas does not mention is whether corporate bookmakers are disadvantaged by the way that ownership and distribution of racing vision occurs. The evidence of Mr Tyshing is that corporate bookmakers have been unable to obtain access to racing vision, because:

    a) In most cases it is bundled across delivery platforms (pay TV, free to air TV and digital), which precludes corporate bookmakers from acquiring rights for just a single platform [181]; and

    b) Tabcorp, as the holder of most of the rights via Sky Racing, has precluded all corporate bookmakers from access or redistributing the content [214].

75. Dr Pleatsikas concludes that the evidence is consistent with the view that "there would be no significant anticompetitive effects and no net public detriments from the proposed merger on the wagering market" [159]. However, I find it difficult to reconcile this conclusion with the [**Highly Confidential - derived confidential information**] [redacted], which casts doubt on the level of constraint imposed by corporate bookmakers on totalisators. Furthermore, Dr Pleatsikas does not analyse the level of competition between Tabcorp and Tatts through the online channel that would be lost with the merger. Mr Smith does consider this issue, and I return to it when discussing his statement.

76. If it is correct that tote and fixed odds products fall within the same market, I think there is a degree of differentiation. Indeed, there would only be value in acquiring an exclusive tote licence if there was some degree of differentiation between tote and fixed odds products. As I note at [54] above, turnover through retail channels has remained relatively static. I note also the statement of:

    a) Mr Tyshing that [74] "Tabcorp and Tatts have historically had a customer base of less sophisticated, higher margin customers. Corporate bookmakers in contrast have historically had more sophisticated, first adopter, lower margin customers"; and

    b) Mr Thompson (second statement) that some customers particularly value the retail experience [42(a)] and some "have a strong preference for unique aspects of pari-mutuel wagers" [42(d)].

77. I return to the issue of product differentiation later in my report.

4.3.2.3. Section V.2.6 – "Broadcasting Markets"

78. Dr Pleatsikas allocates just one paragraph to potential broadcasting competition issues, and does not discuss any possible vertical issues.

4.3.3. Section V.3 – effect on total economic welfare

4.3.3.1. Cost synergies

79. Dr Pleatsikas refers to the assumptions he has been given regarding cost (including capex) synergies [175], and turns these into a present value. Dr Pleatsikas correctly reduces these synergies by any amount that is just a transfer rather than a resource saving (see footnote 206).

80. The assumptions provided to Dr Pleatsikas (and the other economic experts for the applicant) do not explain how the claimed cost synergy figures have been arrived at. However, Mr Johnston provides detail in his statement. In my experience, these types of figures would be carefully tested by the competition authority, for example, by engaging an independent accounting expert. I note Mr Thompson is sceptical of the claimed synergies because the benefits that were claimed when Tabcorp purchased Tab Limited failed to materialise [4, third statement].

81. As well as a general test of their veracity, a key issue is whether the claimed synergies would be merger-specific, or whether they could also be achieved under the counterfactual. This is a particularly important avenue of investigation in the present case, given the applicant claims it and Tatts are at a cost disadvantage to corporate bookmakers. If correct, this would place significant cost pressure on the totes under the counterfactual.

82. I also note that Dr Pleatsikas has chosen to analyse the claimed synergies over a period of ten years. This is despite his earlier argument that any price effect on licence bidding should be de-emphasised because it would not occur for seven years.

83. There is no "right answer" to the question of timeframe. The longer the timeframe:

    a) The larger the effect of discounting; and

    b) The more uncertainty there is.

84. For the sake of reference, I note that:

    a) When evaluating the potential effects of a merger on competition, the ACCC focusses on the "foreseeable future," which it describes as "generally within one or two years." (ACCC Merger Guidelines, p.12); and

    b) When investigating merger authorisation applications, the New Zealand Commerce Commission tends to adopt as a base case a five year time period, with sanity checking to ten years.[14]

[14] See the New Zealand Commerce Commission's analysis in "Cavalier Wool Holdings and New Zealand Wool Services International Limited", NZCC 31, 12 November 2015 at [386.1].

4.3.3.2. Revenue synergies

85. Dr Pleatsikas is similarly uncritical regarding the claimed "revenue synergies" – he essentially just repeats the key figures from the assumptions he has been provided [176]. However, reviewing those assumptions, there are some obvious issues to be tested, which I now describe.

86. The first claimed revenue synergy is increased revenue from improving Tatts' average fixed odds yield [Pleatsikas assumptions 277-279]. The 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]. There does not appear to be any consumer (punter) benefit here, just a profit benefit to the merged entity.

    a) In concept a profit benefit to the merged entity could be a valid merger benefit, provided it results from an efficiency gain rather than a price increase (or quality decrease). However, it is the profit increase (or more technically, "producer surplus") that would be the benefit, not the revenue increase. Any costs incurred in generating that revenue would need to be netted off; and

    b) It is also not clear how much of this fixed odds yield benefit should be considered merger-specific. If Tabcorp developed the relevant systems over [**Highly Confidential to Tabcorp**] [redacted] [Pleatsikas assumptions 277], then there is a valid question about whether Tatts could do the same under the counterfactual (Mr Tyshing makes this same point at [462], as does Mr Thompson in his third statement at [36]). If so, then any benefit would be limited to the increased speed of improving the fixed odds yield under the factual compared to the counterfactual. Indeed, I note the assumptions provided to Dr Pleatsikas state that any similar investment by Tatts "either will not be implemented by Tatts or will not be implemented as rapidly or in the same timeframe as if the Merger occurs" [Pleatsikas assumptions 286(b)]. While this assumption is vague as to exactly what occurs in the counterfactual, it still raises the question as to whether it is just the benefit of the increased speed that is relevant here.

87. I noted above that there does not appear to be any consumer (punter) benefit from the improved fixed odds yield. In fact, it appears there might be some punter detriment. In his statement, Mr Johnston defines the yield as "the proportion of turnover that fixed odds bookmakers retain after the payment of winnings" [66(b)]. Mr Johnston states that the claimed [**Confidential to Tabcorp**] [redacted] [81]. However, I note that in his model that calculates the [**Confidential to Tabcorp**] [redacted].[15] In other words, to the degree the increase in revenue comes from yield increase, for every dollar spent by punters on Tatts' products post-merger, an extra [**Confidential to Tabcorp**] [redacted] cents would be kept by the merged entity.

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[15] Tab 4 of DJ-1, TBP.100.001.0002.

88. If this interpretation is correct, then:

    a) Any producer surplus gain from the initiative due to yield increase should not be treated as a public benefit; and

    b) The initiative suggests that the fixed odds products of the merged entity would not be constrained by those of the corporate bookmakers.

89. The second claimed revenue synergy is broadly described as resulting from "wagering business improvements" [Pleatsikas assumptions 276(b)]. This is then broken down into three subsets.

90. The first subset is "introducing new products and expanding the availability of other products in Tatts states" [Pleatsikas assumptions 280(a)]. Conceptually this could increase both consumer surplus and producer surplus. The assumptions appear to focus just on the latter. However, the measures used to quantify this are not appropriate:

    a) As discussed above, the correct measure is producer surplus, i.e., the excess of revenue over costs. The assumptions instead refer to turnover, which will overstate the benefit, and revenue, which may overstate the benefit, depending on whether there are any variable costs; and

    b) It is possible that the producer surplus gained by the merged entity would be at the expense of producer surplus to rivals, to the degree the merged entity competes away punters from rivals. From a public benefit point of view, what matters is the increase in total producer surplus across all producers, if any – simple transfers of surplus do not produce a public benefit.

91. I note also the third statement of Mr Thompson, in which he states that certain new products could simply be introduced by Tatts today without merging with Tabcorp [38] and [40]. [**Highly Confidential to Tatts**] [redacted]. Only merger-specific effects can be treated as benefits.

92. Furthermore in relation to merger-specificity, the assumptions provided to Dr Pleatsikas refer to all of the claimed revenue synergies of the proposed merger resulting in [**Confidential to Tabcorp**] [redacted] [Pleatsikas assumptions 285]. However, [**Highly Confidential to Tatts**] [redacted]. This again goes towards the possible (lack of) merger-specificity of the claimed revenue synergies.

93. The second subset is "re-branding and improving the retail network in the Tatts states" [Pleatsikas assumptions 280(b)]. I have three comments on this claimed benefit:

    a) It is not clear why this claimed benefit should be considered merger-specific, or in other words why Tatts could not undertake this benefit itself. Indeed, [Pleatsikas assumptions 286(a)] states that Tatts would invest in its retail networks absent the merger, and [**Highly Confidential to Tatts**] [redacted]

[redacted]. It is only the merger-specific part of the benefit that is relevant, and this has not been quantified;

b) Once again the metric provided for this benefit is either turnover or revenue, when what matters is increased profits (or more technically, producer surplus). Any costs incurred in generating that revenue would need to be netted off; and

c) It is possible that the producer surplus gained by the merged entity would be at the expense of producer surplus to rivals, to the degree the merged entity competes away punters from rivals. From a public benefit point of view, what matters is the increase in total producer surplus across all producers, if any.

94. The third subset is "Tabcorp being able to take on a greater number of fixed odds bets" [Pleatsikas assumptions 280(c)], "because a bigger fixed odds book can make it easier to manage risk" [Pleatsikas assumptions 283]. It is unclear whether the anticipated increase in the number of fixed odd bets would be due to an expansion of the market or competing bets away from rivals (I return to this issue in section 8.2 of my evidence). If the latter, as already noted, a transfer of surplus is not a public benefit. And for both, as already noted, the correct metric is producer surplus, not turnover or revenue.

95. Moreover, I note also that it appears from Mr Johnston's model that the calculation of the [**Confidential to Tabcorp**] [redacted] If this is correct, then any part of the producer surplus increase that is due to an increase in yield should not be treated as a public benefit.

96. In a similar vein, Dr Pleatsikas simply recites the assumptions he has been given regarding claimed synergies in respect of Keno in South Australia. But once again it is not clear why the [**Confidential to Tabcorp**] [redacted] dollars proposed to be invested in South Australian Keno [Pleatsikas assumptions 288] could not be made under the counterfactual.

4.3.3.3. Flow through

97. Dr Pleatsikas then discusses the flow-through of cost and revenue synergies to the racing industry. If there are legitimately cost synergies from the merger, and they are passed through to the racing industry, it is appropriate to consider this as a benefit, as long as there is no double-counting. In other words, cost synergies can only be counted as a benefit once, and any transfers of those synergies are simply that, transfers.

98. Likewise, if there are legitimately producer surplus benefits from the merger, and these are passed through to the racing industry, it is appropriate to consider this as a benefit, as long as there is no double-counting. It is not clear to me whether the figures set out in the table

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

under [Pleatsikas assumptions 292] were also part of the figures set out in the tables under [Pleatsikas assumptions 279 and 284]. To be clear, an increase in surplus can only be counted once.

99. Furthermore, a key factor here is likely to be that some fraction of the figures set out in the table under [Pleatsikas assumptions 292] are likely to result from producer surplus transferred from rivals, rather than created, and so would not count as a public benefit. I return to this issue later in my report.

100. At [180], Dr Pleatsikas refers to "higher-order benefits from these synergies". It is not clear to me what he means by this, although he does refer later in the paragraph to, for example, increasing employment. This appears to segue into the type of analysis carried out by Dr Simes, which I review in section 7 of my evidence.

5. Statement of Patrick Smith

101. In this section I set out my comments on the evidence of Mr Patrick Smith. I restrict my comments to the key analytical findings of Mr Smith. My headings follow those of Mr Smith.

5.1. Section III.C – "The parties' activities"

102. Mr Smith concludes that "the primary scope for competition between the parties is in phone and online channels, where each of the parties' wagering products are offered to punters across Australia" [47]. I agree with this, given that there are exclusive licences by state and territory for retail and on-course wagering. In effect, the internet has lowered the barriers to competition between Tabcorp and Tatts, and [**Confidential to Tabcorp**] [[17] the scope for competition between Tabcorp and Tatts is increasing.

103. [**Confidential to Tabcorp**] .

5.2. Section III.D.v – "Trends – retail and online wagering"

104. Figure 4 of Mr Smith's evidence depicts "TAB turnover, FY 1990-2015". Mr Smith describes this as basically being turnover through retail outlets [73]. Figure 4 shows turnover peaking in FY2009, and then declining, although the source note does state that some turnover is missing for FY2014 and FY2015.

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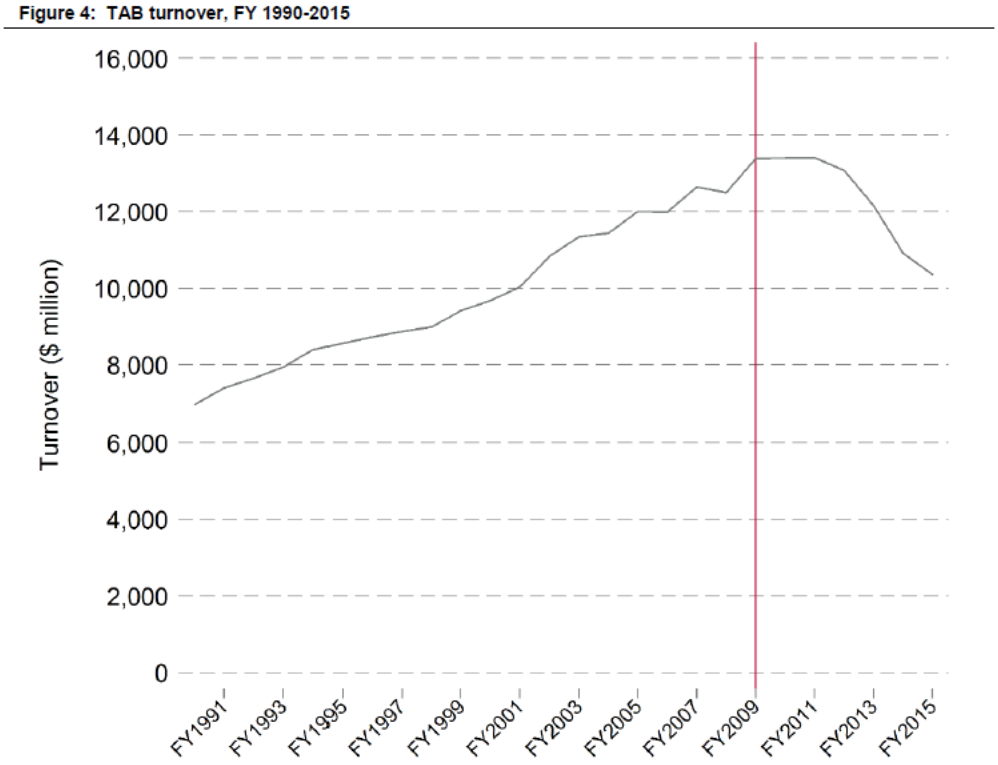
[17] Excluding premium.

105. I bring Figure 4 to the particular attention of the Tribunal, which I have reproduced below, because it depicts a slightly different picture to other data in the assumptions provided to Mr Smith (and the applicant's other experts). The table at [Smith assumptions 128] shows nominal retail wagering turnover to be [**Confidential to Tabcorp**] [redacted] between FY06 and FY15 – I have reproduced the relevant row of that table in Table 3 below.

Figure 4 from Mr Smith's evidence



Source: RBB Economics analysis of Australian Gambling Statistics data, "TAB Turnover" (page 20). Note: Total turnover is incomplete in FY2014 and FY2015 due to unavailable figures for South Australia. Turnover figures are nominal.

Table 3
Industry wagering turnover for retail channel, FY06-FY16 [Confidential to Tabcorp]

	FY06	FY07	FY08	FY09	FY10	FY11	FY12	FY13	FY14	FY15
Industry wagering turnover in the retail channel ($b)	[redacted]									

106. Presumably this discrepancy is explicable by slightly different data being captured by each – in particular, it might be that Figure 4 of Mr Smith's statement includes on-course data, whereas the table at [Smith assumptions 128] separates this out (showing a decline over the period). I note that Mr Smith does graph this latter data in his Figure 5.

107. I raise this issue because, as already noted in this statement, it is not clear to me that the retail channel has become materially less important over time, in a nominal, dollars sense – I do not think it is accurate for Mr Smith to state that Tabcorp's retail wagering turnover [**Highly Confidential to Tabcorp**] [redacted] [78]. This is relevant when considering some of the competition issues raised by the proposed merger.

108. [**Highly Confidential to Tabcorp**] [redacted]

5.3. Section III.E.i – "Different totes"

109. Mr Smith graphs Tabcorp tote average payout rates for NSW and Victoria over time in his Figures 11 and 12. I note that these have [**Highly Confidential to Tabcorp**] [redacted] over the 2011-2016 period analysed. Mr Smith does not discuss this, but I think it is worthy of analysis. A [**Highly Confidential to Tabcorp**] [redacted]. As I have noted, this seems odd, at the same time as corporate bookmakers are allegedly competing hard and gaining share from the totes.

110. Even if this apparently [**Highly Confidential - derived confidential information**] [redacted].

111. Similarly Mr Smith does not analyse the [**Highly Confidential to Tabcorp**] [redacted]. [**Highly Confidential to Tatts**] [redacted]

5.4. Section III.F.i – "Limited scope for competition – tote racing wagering"

112. In this section of his statement, Mr Smith analyses data regarding online and phone tote wagering. He summarises the results at [161, footnote omitted]:

> *While **[HIGHLY Confidential to Tabcorp and Tatts]** [redacted] of punters domiciled in states and territories where Tabcorp is the local retail licensee have chosen to place online and phone (account) tote bets into the smaller Tatts tote pools, **[HIGHLY Confidential to Tabcorp and Tatts]** [redacted] of punters located in states and territories where Tatts is the local retail licensee have chosen to place online and phone (account) tote bets into the larger Tabcorp tote pools.*

113. Mr Smith explains the [**Highly Confidential to Tabcorp and Tatts**] [redacted]. I think this is a possible explanation, although there are others, such as whether Tabcorp might have superior advertising opportunities through its media rights.

114. Mr Smith concludes that [167], "Based on the evidence available to me, it is difficult to discern significant competitive interaction between the parties' tote bet offerings." It is true that [**Highly Confidential to Tabcorp and Tatts**] [redacted] in each firm's states place (tote) bets with the other firm, particularly given that we are only analysing online and phone wagering. However, I do not think we can ignore the pressure that Tatts in particular might feel from Tabcorp, [**Highly Confidential to Tabcorp and Tatts**] [redacted]. This is particularly the case given that the key growth channel is online – this competition may get stronger in the counterfactual.

115. There is also evidence to suggest that Tabcorp's tote prices constrain Tatts' tote prices, despite the exclusive licensing for retail products. Mr Andrew Twaits states that while Tabcorp charges at the maximum statutory take-out rate, Tatts does not [38]. Rather, Mr Twaits notes that Tatts' take-out rates are very close to those of Tabcorp's, despite the former having much higher statutory maximums. [**Highly Confidential - derived confidential information**] [redacted].

116. I note also that Mr Twaits states there is no price discrimination between retail tote customers (who Mr Twaits states are less price sensitive) and online tote customers (who Mr Twaits states are more price sensitive) [38(b)]. This suggests that the retail customers would benefit from competition for the online customers. Mr Smith argues that [**Highly Confidential to Tabcorp and Tatts**] [redacted] are likely to be well informed punters, with "the best ability to counteract any putative harm that might arise from the merger" [170]. It is possible that these minorities are well informed. However, to counteract any harm from the merger, they would need to consider the fixed odds products of corporate bookmakers as substitutes, an issue I return to below.

5.5. Section III.F.ii – "Limited scope for competition – fixed odds racing wagering"

117. A similar [**Highly Confidential to Tabcorp and Tatts**] [redacted] exists for fixed odds wagering. As Mr Smith states at [175] (footnote omitted):

> *Considering only the turnover placed with one of the parties (as discussed further below, turnover placed with corporate bookmakers was far larger), in FY 2016, **[HIGHLY Confidential to Tabcorp and Tatts]** [redacted] of turnover from punters domiciled in states and territories where Tabcorp is the local retail licensee was placed in online and phone (account) fixed odds bets with Tatts; **[HIGHLY Confidential to Tabcorp and Tatts]** [redacted] of turnover from punters domiciled in states and*

[18] E.g., at [165].

territories where Tatts is the local retail licensee was placed in online and phone (account) fixed odds bets with Tabcorp.

118. This [**Highly Confidential to Tabcorp and Tatts**] [redacted] is interesting, and Mr Smith does not seek to explain it. For example, it would be interesting to analyse whether Tabcorp is perceived as having a superior brand to Tatts.

119. Mr Smith's Figure 39 is interesting, because it shows that [**Highly Confidential to Tabcorp and Tatts**] [redacted]. I disagree with Mr Smith when he says at [179] the "proportion of wagering activity does not appear to respond to the [**HIGHLY Confidential to Tabcorp and Tatts**] [redacted] payout rates between the Tabcorp and Tatts fixed odds operations".

120. Mr Smith concludes as follows [187]:

In conclusion, it appears that there is limited scope for competition between the parties' wagering services, and that the parties are relatively distant competitors with one another, even in the online and phone channels.

121. For the reasons outlined above, I think this conclusion is too strong. I think there is competitive tension between Tabcorp and Tatts that would be lost if they merge, and given the key growth channel for wagering is online, this tension might increase under the counterfactual. Indeed, I note that [**Highly Confidential to Tabcorp**] [redacted],[19] and Mr Tyshing discusses the public statements by Tatts about its expansion plans [384-389]. Accordingly, the counterfactual is likely to be more competitive than the status quo.

5.6. Section III.F.iii – "Luxbet"

122. Mr Smith states that [189] "the competitive interaction between Tatts and Luxbet is unlikely to significantly affect the overall competitive assessment". I think that is a fair conclusion. I calculate that Luxbet has only about a [**Confidential to Tabcorp**] [redacted] share of FY16 corporate bookmaker turnover,[20] and several of the other corporate bookmakers appear to be materially larger [Smith assumption 120].

5.7. Section III.G – "Competition between the parties and corporate bookmakers"

123. Figure 42 of Mr Smith's statement depicts the changing shares of Tabcorp, Tatts and the corporate bookmakers. The figure is certainly interesting, but I do not think this is the best

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[19] See Tab 47 of DF-3 TBP.003.001.1096_1097 and TBP.003.001.1096_1192.

[20] Analysis of Tab 2 of CP-2, TBP.001.018.5686.

way to assess competition between the parties and corporate bookmakers, because it effectively assumes they are competing – this is inherent in the fact they are being compared.

124. What I find more relevant is the raw turnover numbers that underlie Figure 42. These are contained in the spreadsheets listed under Figure 42, and they show actual tote turnover for the merging parties [**Highly Confidential to Tabcorp and Tatts**] [redacted], over the last five years.

125. The analysis carried out by Mr Smith depicted in Figure 43 is particularly useful at illustrating the [**Highly Confidential to Tabcorp and Tatts**] [redacted].

126. At [217] Mr Smith refers to the assumptions he has been given regarding the claimed competitive advantages of bookmakers over totalisators. My comments on this topic are the same as I make in respect of Dr Pleatsikas (see section 4.3.2.2 above).

127. Mr Smith then analyses payout data for corporate bookmakers [219-220], and concludes they are generally [**Highly Confidential to Tabcorp and Tatts**] [redacted] those offered by the merging parties' tote and fixed odds operations. This is consistent with the data I analyse above (see Figure 3, Figure 4 and Figure 5). Mr Smith concludes the evidence suggests that corporate bookmakers will continue to exert "a significant competitive constraint on the merged entity". I think this is a fair reading of the evidence he refers to, but Mr Smith does not explain:

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

b) How the merged entity could increase the yield on Tatts' fixed odds products if corporate bookmakers would exert "a significant competitive constraint on the merged entity".

128. Furthermore, Mr Smith does not analyse whether corporate bookmakers are disadvantaged by the way that ownership and distribution of racing vision occurs.

5.8. Section III.H.i – "Cost synergies"

129. I agree with Mr Smith that any variable costs savings (approximately [**Confidential to Tabcorp**] [redacted] should in theory be passed on in the form of lower prices [227], at least over time and to some extent. However, in the scheme of things this is unlikely to have any material impact on prices, given the combined wagering revenues of Tabcorp and Tatts are approximately [**Confidential to Tabcorp and Tatts**] [redacted].[21]

130. In concept, I also agree with Mr Smith that "fixed cost savings may still be considered a public benefit that could outweigh a potential public detriment" [228] – whether or not that is the case for the present merger is of course one of the key questions for the Tribunal. Mr

[21] Based on FY16 wagering revenues of [**Confidential to Tabcorp and Tatts**] [redacted] for Tabcorp and [redacted] for Tatts, [Simes assumptions 26].

Smith then goes on [229] to argue that "even annual fixed costs savings may have a positive effect on competition". To the extent such cost savings are invested in new products or quality improvements, I agree with this, although I am less convinced by the other example Mr Smith gives (promotional expenditure), as this is less likely to raise consumer (punter) welfare in a material way.

131. Regardless, the benefit should only be counted once. If the cost savings are to be used to invest in higher quality products, this would lead to punter welfare improvements, but the cost would need to be deducted. Therefore the most appropriate thing to do is to count the cost savings as a benefit, and be done with it.

132. As I have mentioned earlier in my statement, a cost synergy should only be considered a benefit if it is merger-specific, and Mr Smith does not test this.

133. At [230], Mr Smith refers to a proportion of the expected cost savings being passed through to the racing industry. As I have already discussed, the cost savings should not be double-counted.

5.9. Section III.H.ii – "Business improvements"

134. Mr Smith's discussion of the claimed revenue synergies does not go beyond the discussion by the other experts, and so I have nothing further to add beyond my earlier comments in respect of Dr Pleatsikas' statement. I do return to these issues later in my report (section 8.2).

5.10. Section III.H.iii – "Tote pools"

135. Mr Smith argues that the pools of Tabcorp and Tatts are complements [237-241], in the same way that left and right shoes are complements – a price increase for a left shoe would reduce demand for the right shoe.[22] However, Mr Smith does not offer any evidence for the claim that tote pools are complements, i.e., that an increase in the price of a pari-mutuel bet by Tabcorp would reduce the demand for pari-mutuel betting with Tatts. Accordingly, I do not think Mr Smith has established the pools as being complements.

136. Mr Smith states that combining Tabcorp's and Tatts' pari-mutuel pools would make them more attractive to customers [242]. Assuming this is correct (I note Mr Thompson's statement that there are diminishing benefits to pool size [48, third statement], and Mr Twaits also questions the benefits from larger pools [126]), there is an issue as to whether this benefit is merger specific. Mr Smith asserts that the merger would remove a commercial barrier to combining the pools, but does not expand on this. I think this issue should be analysed more carefully, because there are several examples of comingling of pools without a merger, both within Australia and between Australian and overseas pools.[23]

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[22] See [240] of Smith.

[23] See [68] of Smith.

137. Indeed, there is a conflict between what Mr Smith says about there being a commercial barrier to pooling, and what Professor Menezes says, which is that Keno pooling can be achieved by commercial agreement [133], and that wagering pooling arrangements may be reached by commercial agreement [204].

138. Interestingly Tabcorp has not merged its SuperTab and NSW pools (Thompson [48, third statement]). If there are benefits in doing so, this lack of pooling suggests there is some other impediment to doing so, one that would not be addressed by the proposed Tabcorp/Tatts merger.

5.11. Section IV.B – "Funding arrangements"

139. In this section of his evidence, Mr Smith sets out evidence that he argues shows "it appears unlikely that the merger will have any significant adverse effect on the relationship between wagering turnover and funding for racing" [276].

140. I think what Mr Smith's discussion suggests is that the growth of Tabcorp into a multi-state licence holder over time has not had any significant adverse effect on the relationship between wagering turnover and funding for racing. But this is distinct from analysing the effect of merging the two strongest potential bidders for licences, and any related link between wagering turnover and funding for racing. To put this another way, regardless of the interstate consolidations that built Tabcorp and Tatts into what they are today, the two firms have always existed as potential bidders for licences, and it is this that would change as a result of the proposed merger.

6. Statement of Flavio Menezes

141. In this section I set out my comments on the evidence of Professor Flavio Menezes. My headings follow those of Professor Menezes.

142. The statement of Professor Menezes is focussed on just one potential competition issue raised by the proposed merger. As Professor Menezes states at [21]: "I have been asked to consider the competitive effects and total economic welfare effects of the proposed merger on future processes for awarding State Government retail wagering licences (including the potential sale of RWWA), lottery licences and Keno licences".

6.1. "The conceptual framework: the economics of bidding markets"

143. At [17 to 87], Professor Menezes sets out the economic framework for considering mergers that affect auction markets. I agree with most of what Professor Menezes sets out in these paragraphs, and so restrict my comments on them to just one issue.

144. This relates to Professor Menezes discussion at [29 to 40].[24] He sets out the theory that leads to the following conclusion [35]:

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[24] Professor Menezes discusses these issues again at [115 to 125.]

> *It follows that if the total welfare is defined as total surplus from the auction, then irrespective of what happens to the auction price, total welfare will increase for a merger that creates synergies. It also follows that total welfare is unchanged by a merger that does not alter, through synergies or dissynergies (sic), the value of the object for sale.*

145. This is a very important finding, because it implies that any merger affecting bidding markets should be authorised (assuming there are no dis-synergies), *even if the merger would lead to reduced auction prices* (in the situation when the auctioneer is the seller, as the state governments would be).

146. This finding does assume that we should treat a dollar in the hands of the merged entity's shareholders the same as a dollar in the hands of a taxpayer or participants in the racing industry. Professor Menezes briefly discusses this issue at [40]. Whether a dollar in different hands should be treated equally or distinctly is a distributional issue rather than a question of economics.

147. However, I think there are some other important caveats to Professor Menezes' findings. His analysis focuses on how the bidders' value would change with merger synergies, and the division of surplus between seller and winning bidder (via the auction price). But competition can affect dimensions beyond only the (auction) price. In particular:

a) Bidding competition might result in innovative offers being made to the state government, e.g., new ways to help fund the racing industry, or new aspects to the retail network. For example, I note that [Menezes assumption 207(d)] refers to "a requirement of the bidding process that the applicants had to agree to arrangements with the Victorian racing industry (including in relation to funding) that were no less favourable than the existing arrangements that were in place with Tabcorp at that time". Given this constraint, it is still possible that reduced bidding competition could result in less favourable arrangements with the Victorian racing industry than would occur if there was competition (Mr Tyshing and Mr Simon Barrile make a similar point at [442] and [33] of their statements respectively);

b) Bidding competition might result in higher quality for aspects of the wagering and funding arrangements. For example, I note the ACCC's Issues List refers to a potential "unwillingness to support less attractive retail outlets with limited turnover as required by state and territory governments" (page 3). Perhaps reduced bidding competition would result in a diluted commitment to operate a network of retail outlets; and

c) Bidding competition is likely to sharpen the bidders' incentives to be productively efficient.

148. Accordingly I think it is plausible that the merger could reduce total welfare, even if there are synergies and we treat a dollar in the hands of the merged entity's shareholders the same as a dollar in the hands of a taxpayer or participants in the racing industry. I do not know enough about the nature of the arrangements that are determined by licence bidding to be able to form a view on welfare changes in the present case. However, I do note that Mr Thompson states [52, second statement]:

Maintaining competitive tension for future tenders issued by State governments, including the Victorian Government, is therefore of obvious importance to achieving the best outcome for users of totalisators, retail wagering customers, racing participants, race-goers, racing bodies and the State government itself.

6.2. "The assessment of the impact of the proposed merger on bidding markets"

6.2.1. Willingness to pay

149. The first thing Professor Menezes does under this section of his statement is review the claimed cost and revenue synergies, and analyse whether they would increase the willingness to pay of the merged entity for licences. He concludes that the cost savings would, but is not able to say the revenue synergies would. I think Professor Menezes' conclusions are reasonable, although my earlier comments about cost synergies continue to apply.

150. As Professor Menezes notes at [105], an increased willingness to pay may not result in a higher auction price, because other factors will also affect this, which he then moves on to analyse.

6.2.2. Timeframes

151. Professor Menezes then discusses timeframe issues. He concludes that it is appropriate to analyse bidding competition for the expected 2024 auction, but not for the next auction, expected in 2033. This is because he thinks it is too difficult to predict likely bidding strength that far out, in light of the changing dynamics in the wagering market now.

152. I think this conclusion and analysis are reasonable.

153. Professor Menezes than applies the framework he has set out to auctions of licences for Keno, lotteries and wagering.

6.2.3. Keno licences

154. Professor Menezes argues that the merger is unlikely to have a significant impact on future auction prices for Keno licences, primarily because:

a) Any incumbency advantages are unlikely to be material;

b) Existing Keno licences are not just held by Tabcorp and Tatts, but by other providers as well; and

c) Barriers to entry are not significant.

155. I am relying on the facts as presented by Professor Menezes, but given that caveat, I think his analysis is reasonable.

6.2.4. Lotteries licences

156. Regarding the next auction for the exclusive licence to offer lotteries in Victoria, I note from [Menezes assumption 220] that [**Highly Confidential to Tabcorp**] [redacted]

[redacted]. Professor Menezes does not refer to that assumption, although does in effect get to the same place, stating [157]: "I will proceed under the conservative assumption that there are significant incumbency advantages and assess whether the proposed merger is likely to result in lower future auction prices than in the counterfactual."

157. Professor Menezes points out [159] that there is no evidence of Tabcorp being the likely second highest bidder in the counterfactual, given it does not currently operate a lotteries business. I think this is a fair point.

158. Nevertheless, Professor Menezes goes even further, and analyses what strategies the Victorian government could implement to counter any increase in market power on the bidding side. He argues that the government could estimate the likely value to a bidder of the licence, and accordingly could set a reserve price to reflect this.

159. For the case of a licence to operate the lottery in Victoria, I think this is a fair point. As far as I am aware, the Victorian lottery is a relatively predictable business (compared to wagering, which I will come back to), and so the government's historical information should be informative, when combined with public information about merger synergies.

6.2.5. Wagering licences and RWWA

160. Professor Menezes then turns to the 2024 auction of the Victorian tote wagering licence, and the likely sale of RWWA.

6.2.5.1. Victorian wagering licence

161. Regarding Victoria, Professor Menezes argues that the physical infrastructure and systems associated with operation of the licence are unlikely to provide a material incumbency advantage for two reasons [201].

162. Firstly, he points to a "Wagering and Betting Agreement" between Tabcorp and the Victorian government, containing transition provisions. However, neither Professor Menezes nor the assumptions specified for him provide any details on this agreement. In the absence of analysis of those details, I do not think it is sufficient to point to this agreement as undermining any incumbency advantage.

163. Secondly, Professor Menezes argues that [201] the "shift from traditional retail to online betting has decreased the value of the physical infrastructure to potential bidders". However, as I have already noted in this statement, it is not clear that there has been such a shift, or at least not a material one. The table at [Menezes assumptions 128] shows that retail revenue has been [**Confidential to Tabcorp**] [redacted]. While it is clear that revenue spent on digital wagering has increased dramatically, this appears to have been mainly from growth in overall wagering, rather than substitution from retail.

164. Therefore I think Professor Menezes is too sanguine in arguing that any physical infrastructure incumbency advantage is unlikely to be material.

165. Professor Menezes then moves on to discuss whether the ability to pool totalisator bets across Australian jurisdictions provides an incumbency advantage. He argues it does not, for two reasons.

166. The first is that any advantage from pooling may become less valuable, as more customers shift to fixed odd bets [204]. However, this argument is inconsistent with one of the apparent rationales for the proposed merger, which is to enable further pooling so that the merged entity can better compete against corporate bookmakers – see, for example, [Smith assumption 185(b)]. If it is correct that punters are switching away from tote wagering to fixed odd wagering, then the ability for a tote operator to pool probably becomes more, not less, important. Indeed, I note that Mr Smith describes pooling arrangements entered into by Tabcorp "[i]n response to the growth of corporate bookmakers" [69].

167. I note that both Mr Thompson [71, second statement] and Mr Barrile [35] consider that the ability to pool would provide an incumbency advantage and an advantage to Tatts over other potential bidders (other than Tabcorp) for the Victorian licence.

168. The second is that pooling arrangements can be reached by commercial arrangements. In general I think this is correct, but the issue raised by the merger is that for any rival licence bidder, there would only be one option (the merged entity, leaving aside RWWA) for it to negotiate with in respect of pooling arrangements, and that option would also be bidding for the same licence. This may give the merged entity a strategic incentive to refuse to deal with the rival bidder, or to at least offer a price for access that makes it hard for the rival to lodge a competitive bid for the licence. Professor Menezes does not analyse this issue.

169. Professor Menezes then discusses a third potential source of incumbency advantage, being customer accounts and information. Professor Menezes states he is "uncertain about the extent to which such an advantage is significant" [206], and I agree that on the available evidence it is difficult to know. However, I disagree with the statement that Professor Menezes then makes [207]:

> *Even if existing customer account information may indeed confer incumbency advantages in the way the Victorian wagering business may operate today, the market trends discussed in paras. 194-195 challenge the relevance of any such advantage going forward.*

170. The market trends Professor Menezes is referring to include the shift towards fixed odds products, the digital channel, etc. I have two concerns with the quoted statement:

a) The correct comparison is not the merger against the status quo, but the merger against the forward looking counterfactual. So the trends discussed at [194-195] would apply to both the factual and the counterfactual; and

b) Mr Tyshing states that having a retail network gives the provider an advantage in obtaining digital business [277].

171. So to summarise to this point, I am concerned that there are incumbency advantages to being an existing wagering licence holder. Professor Menezes concludes that he is "uncertain about the significance of any existing incumbency advantage" [208], but to be conservative, he assumes there is some.

172. Professor Menezes then argues that the Victorian government could implement various strategies to counter the potential negative impact of the merger on the auction price. Key among these is "setting the reserve price strategically to account for the synergies" [211]. However, I think this would be much harder to do for a wagering licence than it would be to do for a lotteries licence. This is because of the same trends that Professor Menezes discusses at [194-195]. The value of a wagering licence would be much harder for the government to estimate, given these trends.[25]

173. Professor Menezes also argues that the Victorian government could allow foreign corporations to bid, and refers to bookmakers such as Ladbrokes having a retail network in the UK.

174. The difficulty with this argument is that these corporate bookmakers would still face the incumbency advantage of the merged entity in Victoria.

175. In summary, I disagree with Professor Menezes' conclusion [212] that the necessary conditions for the proposed merger to lower prices are unlikely to hold. I also note Mr Thompson's statement that, "In recent license sales processes (in either Tabcorp or Tatts territories), Tabcorp and Tatts have always been the last two bidders considered" [70, second statement].

176. I also note that Professor Menezes does not discuss the role of access to racing media content in respect of licence bidding. Mr Tyshing [451] and Mr Thompson [second statement, 71] both refer to the importance of this as an input.

177. Finally in respect of the Victorian auction, Professor Menezes analyses a negotiation between the government and the merged entity. Professor Menezes' view is that the government would hold the greater bargaining power, and would in effect be able to extract some of the synergy gains from the merged entity, resulting in the possibility of the price actually being higher in the factual than under the counterfactual.

178. I have two concerns with this line of argument:

a) It appears to assume that the value placed on the licence by "Bidder A" (being the third strongest bidder after Tabcorp and Tatts) would not be that much lower than Tatts' value. But given the discussion above about the advantages of Tabcorp and Tatts in any auction, I do not think this assumption has been justified; and

b) It appears to assume that the government could obtain a higher price through negotiation than through an auction. On Professor Menezes' own framework, the factual auction price would be close to Bidder A's valuation, whereas under a negotiation Professor Menezes is arguing the price could be higher than Bidder A's valuation. It is not clear to me how the Victorian government could be worse off running a bidding competition than having a negotiation.

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[25] Mr Twaits notes also that placing a reserve price on a licence means that it would effectively revert back to government ownership, which he does not consider would be acceptable from a policy perspective [68].

6.2.5.2. RWWA

179. The final issue that Professor Menezes analyses is the implications of the proposed merger for the sales price of RWWA.

180. If RWWA is sold as a going concern, Professor Menezes points out that there would be no advantage to either Tabcorp or Tatts as bidders for RWWA arising from ownership of infrastructure and systems. I agree with this.

181. Professor Menezes then analyses whether Tabcorp or Tatts would have an advantage over other potential purchasers of RWWA arising from their existing pools.

182. Professor Menezes first points out that [**Confidential to Tabcorp**] [redacted]. This would certainly help, although it is not clear how long this agreement lasts for, and would still leave the issue of an alternative buyer having to deal with the merged entity for a renewal at the end of the agreement. [**Highly Confidential to Tabcorp**] [redacted]

183. Regarding the length of that agreement, I note the ACCC Issues List states (page 4):

> *Tabcorp has agreed to continue to provide RWWA, or any acquirer of the WA TAB, with pooling services on equivalent commercial terms for up to 27 years. The supply of pooling services post 2024 is conditional on Tabcorp holding the Victorian licence after its expiry in 2024, or if Tabcorp does not hold that licence, it must hold another wagering licence with a substantial totalisator pool so that it can provide access to alternative or comparable pools.*

184. On the basis of the arguments I have made earlier in my statement, I would expect that if the merger goes ahead, it is likely that Tabcorp (the merged entity) would hold the Victorian licence post-2024.

185. Professor Menezes then argues that the value to a bidder of pooling with other Australian jurisdictions may be lower now than in the past, and it may decline further in the future, because of the trends I have already referred to above. However, as I have already pointed out, the value of such pooling may actually be increasing as competition from other wagering products intensifies.

186. Professor Menezes argues that even if pooling would provide a significant advantage to Tabcorp and Tatts, other potential bidders might enjoy their own advantages – he lists possibilities at [225].

187. I agree this is possible. However, given that a rationale for the merger is tote pooling, I would think that these other advantages would have to be significant.

188. Professor Menezes also argues that the Western Australian government would have sufficient information through its ownership of RWWA to set a reserve price to counter any merger-induced market power. Compared to the situation for the Victorian government, I

agree that the Western Australian government would be in a better position to do this, although the changing dynamics in the industry would complicate things.

189. Finally Professor Menezes argues that the Western Australian government would also have the option of an IPO or retaining ownership if not satisfied with the auction outcome [231]. However, if access to pooling is an issue, then the value of both of these options would also reduce with the merger.

190. Professor Menezes concludes that [232], "In summary, I consider it unlikely that the proposed merger could result in a decrease in the sales price of RWAA (sic)." I do not think that Professor Menezes has demonstrated this, although I do not think the issues are as acute as they are in respect of the Victorian licence.

7. Statement of Dr Ric Simes

191. In this section I set out my comments on the evidence of Dr Ric Simes. My headings follow those of Dr Simes, from his sections D through to L.

7.1. Section D - "Direct Benefit 1: Cost savings"

192. Dr Simes states that the [**Confidential to Tabcorp**] [redacted] should be considered a transfer rather than an efficiency [31]. I agree with this, and with his reasoning.

193. Otherwise my comments are the same as those I make in respect of Dr Pleatsikas' statement at section 4.3.3.1 above.

7.2. Section E - "Direct Benefit 2: A wider range of and/or higher quality product offerings"

194. At [35 to 37] Dr Simes repeats the assumptions he has been given regarding the claimed revenue synergies. He notes that the total of [**Confidential to Tabcorp**] [redacted] contains "aspects of both improvements in productive efficiency and transfers from other areas of economic activity", and that with "the Assumptions provided to me it is not possible to provide a view on the extent to which the [**Confidential to Tabcorp**] [redacted] in additional revenue can be attributed to each effect" [38].

195. As I noted above in respect of Dr Pleatsikas' statement, if surplus is simply won from another (Australian) provider, such a transfer should not be considered a public benefit. This is the same view Dr Simes has. (I discuss the issue of surplus won from overseas providers in the next section.) Therefore for this and the reasons already discussed at section 4.3.3.2, the [**Confidential to Tabcorp**] $[redacted] is likely to be an overstatement of the merger benefits.

196. Dr Simes also points out that "consumers choosing to consume more of the Merged Entity's goods and services as a result of improved products and an increased range will do so because it is welfare increasing for them" [43]. I agree with this – this is a benefit that has not been quantified by the applicant, although I note that any increased costs of producing the goods and services should also be taken in to account. I also agree with the subsequent two

paragraphs of Dr Simes' statement where he states that some consumers would be made worse off because of restrictions by the merged entity's new fixed odds management system.

7.3. Section F - "Direct Benefit 3: A substitution of domestic products for imported goods and services"

197. Dr Simes notes the assumptions provided to him state that most of the claimed [**Confidential to Tabcorp**] [redacted] of wagering revenue increase would come from overseas based firms – I interpret this to mean that the merged entity would compete wagers away from the overseas firms. I have already noted, as has Dr Simes, that if the merged entity wins a wager from a rival, there is unlikely in general to be an efficiency gain, as opposed to a transfer. However, Dr Simes points to section 95AZH(2)(a)(ii) of the Competition and Consumer Act as authority for treating such a transfer as a public benefit if the transfer is from a foreigner to an Australian. Nonetheless, I have been instructed to assume that transfers from corporate bookmakers to Tabcorp are welfare neutral and do not fall within section 95AZH(2)(a)(ii).

198. As noted earlier in respect of Dr Pleatsikas' statement, it appears that the [**Confidential to Tabcorp**] [redacted] claimed revenue synergy (from improving Tatts' average fixed odds yield) comes entirely from an increase in yield. Even if I were to assume that a transfer from overseas firms to Australian firms were to be treated as a public benefit, this does not involve any such transfer, and so it would not be treated as a public benefit regardless.

199. Because some of the corporate bookmakers do have Australian employees, as well as incur some domestic property and marketing costs, Dr Simes scales down by 50% the revenue synergy that should be counted as a benefit under this section [53].[26] This 50% scalar is arbitrary, and there is not sufficient information to be accurate. Even if we knew how much the corporate bookmakers had spent on Australian resources historically, we do not know whether this might change in the future.

7.4. Section G - "Direct Benefit 4: Increased funding to racing bodies, sporting bodies, retail wagering venues and Keno retail venues"

200. In this section of his evidence Dr Simes refers to the assumptions provided to him relating to the revenues that are claimed will flow through to the racing bodies, etc.

201. As I noted in respect of Dr Pleatsikas' evidence, if there are legitimately cost synergies from the merger, and they are passed through to the racing industry, it is appropriate to consider this as a benefit, as long as there is no double-counting. Assuming for the moment that the [**Confidential to Tabcorp**] [redacted] is legitimately considered as cost savings, then it appears that [**Confidential to Tabcorp**] [redacted] of this would flow through to the racing industries pursuant to a profit sharing arrangement [Simes assumption 4]. Therefore

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[26] The resulting claimed benefit is [**Confidential to Tabcorp**] [redacted]. Dr Simes assumes that this benefit grows in real terms in line with the wagering industry [54], which he assumes is equal to forecast GDP growth. Dr Simes does not apply a growth rate to any of the other claimed benefits.

the [**Confidential to Tabcorp**] [redacted] cannot be added to the [**Confidential to Tabcorp**] [redacted]

202. Likewise, if there are legitimately producer surplus benefits from the merger, and these are passed through to the racing industry, it is appropriate to consider this as a benefit, as long as there is no double-counting. It is my interpretation that the pass through amount of [**Confidential to Tabcorp**] [redacted] is a subset of the [**Confidential to Tabcorp**] [redacted], and therefore cannot be added.

7.5. Section H - "Direct Benefit 5: Increased Commonwealth, State and Territory taxation revenue"

203. Dr Simes refers to his assumptions that the merged entity would pay an additional [**Confidential to Tabcorp**] [redacted] in taxes, because of its higher profits. But once again, this would simply be a transfer of benefits that have already been counted at the merged entity level – to include them as an additional item would be double counting.

204. Moreover, 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.[27]

7.6. Section I - "The effect of combining Tabcorp's and Tatts' pari-mutuel pools"

205. [Simes assumption 25] states that combining Tabcorp's and Tatts' pari-mutuel pools would make them more attractive to customers. Assuming this is correct (I note Mr Thompson's statement that there are diminishing benefits to pool size [48, third statement]), there is an issue as to whether this benefit is merger specific. [Simes assumption 23] asserts that the merger would remove a commercial barrier to combining the pools, but does not expand on this, and neither does Dr Simes. I think this issue should be analysed more carefully, because there are several examples of comingling of pools without a merger, both within Australia and between Australian and overseas pools.[28]

206. Indeed, there is a conflict between what Dr Simes says about there being a commercial barrier to pooling, and what Professor Menezes says, which is that Keno pooling can be

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[27] See E.J. Mishan (1978), *Elements of Cost-Benefit Analysis*, George Allen and Unwin: London, at chapter 10. The New Zealand Treasury's *Guide to Social Cost Benefit Analysis* (July 2015, at [17]) states "It is usual practice to ignore gainers and losers who are parties to transfer payments, such as taxes, subsidies and welfare payments. This is merely for convenience, because the benefits to the recipients are assumed to offset the costs to the payers. The cash component of a transfer does not involve the creation or destruction of resources". The New Zealand Treasury does go on to point out that raising taxes can have welfare impacts (a deadweight cost) due to their distortionary impact on consumption and investment choices. While an increase in tax paid by the merged entity may reduce this deadweight cost (as less tax has to be raised elsewhere), any assessment of this would be complicated due to the need to also incorporate distortions from the increased tax payments on the merged entity's behavior, as well as any decrease in tax paid by corporate bookmakers.

[28] See [68] of Smith.

achieved by commercial agreement [133], and that wagering pooling arrangements may be reached by commercial agreement [204].

207. As noted above, interestingly Tabcorp has not merged its SuperTab and NSW pools (Thompson [48, third statement]). If there are benefits in doing so, this lack of pooling suggests there is some other impediment to doing so, one that would not be addressed by the proposed Tabcorp/Tatts merger.

7.7. Section J - "Potential Detriment: Increased problem gambling"

208. At [68] to [75], Dr Simes discusses the potential detriment of problem gambling. He notes that to the extent the merger would result in higher punter expenditure, it may also increase the number of problem gamblers. This seems a reasonable point, and to the degree there are consequent surplus reductions, this should be considered a detriment of the merger. (And the reverse is true too – if the merger resulted in a price increase for wagering, etc, then this could result in a reduction in the costs of problem gambling, much like a rise in cigarette prices might result in a reduction in the social costs of smoking).

209. Dr Simes argues that there "is reason to think that any increase in problem gambling is likely to be small" [73], relying on Productivity Commission analysis. This includes [75] the Productivity Commission's finding that the increase in consumer welfare associated with gambling offsets the corresponding detriment with an increase in problem gambling. The Productivity Commission assessed the costs and benefits of gambling, taking the consumer surplus benefits to recreational gamblers and tax benefits to the government (which were assessed as being in the range of $12.1b-$15.8b per annum) and balancing these against the social costs of problem gambling (of $4.7b-$8.4b per annum).[29] While the benefits do indeed exceed the costs, the costs are nevertheless material, and cannot be ignored.

7.8. Section K - "Flow on benefits from the Proposed Transaction: the racing industry"

210. Dr Simes argues that "the racing industry produces a public good, which is then subject to a free rider problem" [79]. This is the justification provided for the high level of funding provided to the industry by wagering operators.

211. This is an interesting characterisation, as it is not immediately clear why a horse race is any different from, say, an AFL match. The difference may relate to the historical dependence of horse racing on wagering, whereas a sport like AFL might have relied more on gate takings and broadcasting funding. If that is the case I can see the free riding argument in respect of horse racing – if one wagering operator funded a race, other operators could offer bets on it without contributing to the funding.[30]

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[29] Productivity Commission (2010), "Gambling", Inquiry Report Volume 1 No.50, 26 February, at p.6.39.

[30] One of the characteristics of a public good is that it is "non-excludable", such that people cannot be excluded from consuming the good. It may be possible to exclude providers from offering wagering products through the regulatory

212. For present purposes I will assume the public good/free riding argument is a valid one. My main concern actually relates to [98] of Dr Simes statement, where he states that the "[**Confidential to Tabcorp**] [redacted] in additional revenue paid as a result of the Proposed Transaction could be characterised as acting to help address a market failure brought about by the free rider problem". This statement assumes that any free rider problem is not already addressed efficiently by existing funding levels, or more accurately funding levels under the counterfactual. No evidence is put forward for this assumption. In the absence of such evidence, I do not think it is possible to speculate what component, if any, of the [**Confidential to Tabcorp**] [redacted] should be regarded as efficiently addressing any under-funding (and noting again that the [**Confidential to Tabcorp**] [redacted] should only be counted once).

213. The remainder of this part of Dr Simes' evidence discusses the flow through of the extra funding to various parts of the broader racing industry and regional economies. I return to the appropriateness (or otherwise) of this in the next section of my evidence.

7.9. Section L - "Estimating selected benefits of the Proposed Transaction"

7.9.1. Description of Dr Simes' methodology

214. Dr Simes plugs certain of the assumed synergies into a computable general equilibrium (**CGE**) model,[31] which he uses to assess the impact of those synergies on gross national income (**GNI**).

215. To be specific, Dr Simes inputs into his CGE model:

a) The cost synergies of [**Confidential to Tabcorp**] [redacted] (from year three), which represents only the cost savings due to the removal of duplication. As noted earlier, Dr Simes correctly concludes that cost savings [**Confidential to Tabcorp**] [redacted] are transfers and so are not part of this input into the model; and

b) Half of the assumed revenue synergies, which equates to [**Confidential to Tabcorp**] [redacted] (from year three), reflecting Dr Simes' assumption that 50% of these are drawn from overseas wagering operators.[32]

216. For the reasons I have already described, the cost figure saving of [**Confidential to Tabcorp**] [redacted] may overestimate the benefits and the revenue figure of [**Confidential to Tabcorp**] [redacted] would definitely overestimate the benefits.

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regime requiring providers to have a licence (as detailed in [Pleatsikas assumptions 50-59]). However, this depends on the ease with which it is possible to obtain a licence.

[31] At the time of writing I have not had the opportunity to review the workings of the model itself.

[32] This figure also increases (at 2% per annum) reflecting growth in the wagering industry.

217. I note also that the proposed merger gives rise to some one-off integration and other costs, as set out in the evidence of Mr Johnston (at [46], [90] and [105]). These costs do not appear to be captured in Dr Simes' model – they are not discussed in his evidence, and nor are they mentioned in the "Inputs" into his model at Attachment B-Table 1. I have also considered Mr Johnston's spreadsheet in which the merger cost savings are calculated,[33] and while it is difficult to ascertain, it does not appear as if the one-off integration and other costs are netted off the cost savings in this model.

218. Dr Simes implements each of these inputs into his CGE model as "shocks" to the economy [131], although he does not specify exactly how this is done. He refers to both of these synergies being "transmitted to the representative agent through a decrease in price of goods and services in the gambling sector" (at [137]), although it is not clear how an increase in profit to the merged entity (via the [**Confidential to Tabcorp**] [redacted][34] and revenue synergies) can be translated into a decrease in price (particularly if there would be an effective price increase for Tatts' fixed odds products, as per my discussion at [87] above).

219. I note that Dr Simes has not explicitly included the flow-through funding to the racing industry, taxes, etc, as an input into his CGE model – for the reasons already explained, I think this is the correct modelling choice. Furthermore, my understanding is that CGE models in general capture how an initial shock to, for example, expenditure or production flows through to other sectors of the economy. In this sense, Dr Simes' CGE model incorporates the flow-through of the modelled synergies to various parts of the broader racing industry, regional economies and governments – I interpret this to be what he is saying at [133] and [135].

220. However, the way Dr Simes presents the results in Table 2 implies these flow-through funds should be added to the CGE results – for the reasons already given, I disagree. I do note Dr Simes says at [146] that, "Not all of the numbers in the table should not (sic) be considered as additive", although he does not provide any explanation.

221. Dr Simes' CGE model also uses an estimate of the elasticity of demand for gambling as an input, for which Dr Simes uses -0.93 [141] with a sensitivity test of -0.6 [144]. Dr Simes notes that this is broadly consistent with the Productivity Commission's (1999) review of the literature on elasticities, finding elasticities of between -0.3 and -1.3 depending on the type of gambler [143]. I note that the Productivity Commission's literature review actually found elasticities in a wider range, from -0.03 to -3.05.[35] However, there was considerable

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[33] Tab 3 of DJ-1, TBP.100.001.0001.

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

[35] Productivity Commission (1999), "Australia's Gambling Industries", Inquiry Report, Volume 3: Appendices, 26 November, at Table C.1, p.C.5.

variability depending on the type of gambling and the jurisdiction in which it occurs,[36] and the Productivity Commission settled on the narrower range of -0.3 to -1.3 for its analysis. While it is possible that demand may be more inelastic than the figures Dr Simes uses, it is also possible that demand may be more elastic. Given that Dr Simes' results (as reported in his Table 2) do not appear to be particularly sensitive to his elasticity estimate, his use of -0.93 with a sensitivity test of -0.6 is a reasonable approach.

222. It is also worth noting that Dr Simes' CGE model does not necessarily "multiply" the inputs to produce outputs. Rather, some of the inputs are multiplied (scaled up), but others are scaled down. The cost saving input (of [**Confidential to Tabcorp**] [redacted]) [Attachment B-Table 1] is scaled up to [**Confidential to Tabcorp**] [redacted] [Table 2]. However the import substitution input (of [**Confidential to Tabcorp**] [redacted] [Attachment B-Table 1] is scaled down to [**Confidential to Tabcorp**] [redacted] [Table 2].

7.9.2. Interpretation and discussion of CGE results

223. Dr Simes states that "an increase in GNI can be interpreted as an increase in the purchasing power of consumers, and therefore is closely associated with their welfare" [25]. However, I think this statement overstates the connection between GNI and welfare, at least if the term "welfare" is used in its standard microeconomic sense.

224. Welfare (also often referred to interchangeably as "social welfare", "economic welfare" or "surplus") is defined in microeconomics as the aggregate well-being of society, in terms of the total utility (or satisfaction) of individual people and businesses in society.[37] It is essentially a measure of how much "better off" society is from a particular action or transaction.

225. Measures of economic activity, such as GDP and GNI, are not measures of welfare, for various reasons.[38] One is that an increase in economic activity that brings about a rise in GNI will often require the application of additional inputs, such as labour and capital. In many circumstances these additional inputs will have a cost, being their "opportunity cost": the foregone value that could have been received from otherwise applying the labour and capital inputs to an alternative activity. Measures of GNI do not net off the opportunity cost of inputs such as labour and capital.

226. GNI also does not measure consumer surplus – the value to consumers from purchasing goods and services over and above what they actually pay for those goods and services. Similarly GNI does not include measures of "non-market" goods and services, such as

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[36] Related to this, Feess and Schumacher (2013) note that wagering elasticities are "considerably affected by the institutional framework" and the racing tax system in the US might explain the (generally) persistent elasticity results well above one (in magnitude) for racing wagering found in the US literature. E. Feess and C. R. Schumacher (2013), "The elasticity of demand for wagering in an unregulated market", *Applied Economics*, 45, 2083-2090.

[37] See, e.g., Robert S. Pindyck and Daniel L. Rubinfeld (2009), *Microeconomics*, Seventh Edition, Pearson Education, Inc.: New Jersey, at p. 598.

[38] Dr Simes notes [25] that GNI is GDP plus net income from abroad.

environmental or recreational benefits and costs, which also have an influence on the welfare of society.

227. These points are made in the economics literature on CGE modelling. For example, Abelson (2011, p.55-56) states that "CGE models are designed principally to estimate market output (GDP or GSP) and not welfare" and that these models "do not account directly for the opportunity cost of labour, consumer surpluses or non-market third party effects".[39] Similarly, Dwyer and Forsyth (2009, p.491) state that "[t]he change in GSP is an exaggeration of how much better off the country, and more precisely, its residents are when additional resources are used to enable this activity".[40]

228. The point is also made clearly by the Australian Bureau of Statistics in its *Concepts, Sources and Methods* document regarding the calculation of GDP where it states (at [8.20]) "GDP is a measure of production and not a measure of economic welfare…changes in GDP do not necessarily correspond to changes in the overall welfare of the community".[41]

229. I note that it is possible to use CGE models to obtain an estimate of welfare changes,[42] but this is not what is provided where the output of the CGE model is GNI (as in Dr Simes' evidence).

230. The fact that the GNI output from CGE models does not measure changes in welfare is perhaps why these models rarely appear to have been used in competition analysis anywhere around the world, as far as I can tell (I come back to the one exception I am aware of below). Competition analysis focuses on changes in willingness to pay, cost, price and output in directly affected markets (measured by allocative and productive efficiency), and investment incentives (affecting dynamic efficiency). The analysis does not generally measure flow-on effects in downstream markets, as is analysed using CGE models. Indeed, when welfare effects are evaluated in directly affected markets using equilibrium supply and demand curves (which is typically the case),[43] and downstream markets are not materially distorted (e.g., through monopoly power or product taxes), then the welfare impacts in the directly affected market already capture the change in welfare across all vertically related markets.[44]

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[39] Peter Abelson (2011), "Evaluating Major Events and Avoiding the Mercantilist Fallacy", *Economic Papers*, 30(1), 48-59.

[40] Larry Dwyer and Peter Forsyth (2009), "Public Sector Support for Special Events", *Eastern Economic Journal*, 35, 481-499

[41] Australian Bureau of Statistics (2015), *Australian System of National Accounts: Concepts, Sources and Methods*, ABS Catalogue No. 5216.0

[42] Dwyer and Forsyth (2009, *op cit.*, p.494) state that "[s]ome CGE models are explicitly designed to measure changes in welfare".

[43] Equilibrium supply and demand curves indicate how quantity supplied and quantity demanded (respectively) respond to price changes, once prices in all affected markets have fully adjusted to a shock, i.e., once the economy returns to equilibrium. As Boardman et al (2006) note, these are the supply and demand curves that are usually empirically estimated and available for use in estimating welfare effects. Anthony Boardman, David Greenberg, Aidan Vining, and David Weimer (2006), *Cost-Benefit Analysis: Concepts and Practice*, Fourth edition, Pearson.

[44] See Chapter 5 of Anthony Boardman, David Greenberg, Aidan Vining, and David Weimer (2006), *Cost-Benefit Analysis: Concepts and Practice*, Fourth edition, Pearson.

231. In those jurisdictions that also look at offsetting benefits, the analysis is similarly focussed on surplus changes. This of course makes sense, as we want to compare apples with apples. For example, in New Zealand, in a merger authorisation in the wool scouring industry, the benefits assessed by the New Zealand Commerce Commission were related to cost savings and efficiencies gains from freeing up surplus resources (land and buildings).[45] The Supreme Court of Canada recently issued a 2015 decision which permitted the merger of Tervita Corp. with Complete Environmental Inc. and Babkirk Land Services on the grounds that the overhead efficiency gains created by the merger outweighed the anti-competitive effects.[46]

232. A second reason why CGE analysis may not be used in competition analysis is that the modelling is less transparent than an analysis of surplus changes in the directly affected market. When quantifying changes in surplus in the directly affected market, there are only a handful of variables to be defined, and the complete effects can be illustrated in a simple demand and supply curve diagram. This provides for transparency in the underlying assumptions and results, and allows all of those involved in the process to independently test those assumptions.

233. In contrast, Abelson (2011, p.56) states, "CGE models are large and generally non-transparent black boxes".[47] Abelson notes that it is often hard to determine how particular assumptions drive the results, or more generally to understand what occurs within a CGE model.

234. Abelson provides an example of the Monash Multi-Region Forecasting CGE model, which generated gains of $500m when run by the Productivity Commission for a particular policy, but when another party used the exact same assumptions generated gains of between -$26m to +$66m.[48]

235. It might also be difficult for a competition regulator to develop or even operate its own CGE model, given their complexity. Abelson states that "any carefully constructed CGE modelling and report would generally not be a low-cost exercise. There are thousands of variables and equations in most CGE models. CGE models are complex and require significant expertise to run.[49]

236. Even if application of a CGE model was appropriate for estimating the benefits in competition analysis, for consistency it should also be applied to estimate the detriments. Indeed, this is the primary reason that both the Commerce Commission and the High Court in

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[45] "Cavalier Wool Holdings and New Zealand Wool Services International Limited", NZCC 31, 12 November 2015.

[46] *Tervita Corp. v. Canada*, [2015] 1 SCR 161, available at: https://scc-csc.lexum.com/scc-csc/scc-csc/en/item/14603/index.do

[47] Abelson (2011), *op cit.*

[48] *Ibid.*, at footnote 12.

[49] Abelson (2011, p.56).

New Zealand rejected the use of a CGE model in the Qantas-Air New Zealand case,[50] this being the only competition case I am aware of where a CGE model has been used.

237. I comment also on Dr Simes' use of a 15-year timeframe for his CGE modelling [119]. This is a relatively long timeframe to use for competition analysis, and as I noted earlier, the longer the timeframe the more uncertainty there will be as to whether the merger benefits will indeed be realised.[51]

8. Conclusions on competitive detriments and benefits

8.1. Competitive detriments

238. Drawing on the evidence filed by the applicant's four economic experts, and the other statements referred to in my report, I have the following conclusions on competitive detriments of the proposed merger.

239. Dr Pleatsikas and Mr Smith have made the argument that there is a single wagering market, which includes (among other things) tote and fixed odds products, sold through various channels.

240. I agree there is evidence consistent with a market definition that includes both tote and fixed odds products, particularly the decline in tote turnover at the same time as the incline in fixed odds turnover (referred to above at [48]). However, there is also evidence that is inconsistent with this market definition, particularly:

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

b) [redacted]

241. On balance, 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.[52]

242. Because the products are differentiated, and only licensed totes can sell tote products, it follows that Tabcorp and Tatts are each other's closest competitors. This is also implied by

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50 *Air New Zealand v Commerce Commission*, [2004], 11 TCLR 347, at [355] and [367].

51 A longer timeframe also results in a larger impact from discounting. As an example, $1 received today has a value of $0.36 in 15 years' time, discounted at a 7% discount rate (as used by Dr Simes).

52 For example, see the analysis of Dr Hird at [170] of his affidavit. I note that Tabcorp paid $410m for the Victorian licence in 2012 (see https://www.tabcorp.com.au/news-media/media-releases/tabcorp-finalises-victorian-wagering-and-betting-l]) and $105.5m for the ACT TAB in 2014 (see https://www.tabcorp.com.au/news-media/media-releases/tabcorp-to-acquire-acttab).

[**Highly Confidential - derived confidential information**] [redacted].

243. The competition between Tabcorp and Tatts occurs directly through the online channel, and is likely to intensify under the counterfactual. For as long as there continues to be no price discrimination between retail and online, retail customers will also benefit from this competition.

244. On balance, I think that the experts for the applicant:

a) Overstate the competitive constraint from corporate bookmakers; and

b) Understate the competitive tension between Tabcorp and Tatts.

245. Accordingly I think that the proposed merger is likely to lessen competition in the wagering market.

246. Indeed, I note that on the applicant's own analysis the merger is expected to result in an effective price increase [**Confidential to Tabcorp**] [redacted]. This would be associated with a detriment to consumers (punters).

247. I am 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.

248. Similar concerns exist in respect of the proposed privatisation of the RWWA, although I think the issues are less acute.

8.2. Benefits

8.2.1. Introduction

249. In the preceding sections of my statement, I have reviewed the benefits analysis of the four experts on behalf of the applicant. In this section I set out my views on how the benefits of the proposed merger should be calculated, subject to the constraint of only having access to the evidence filed in these proceedings.

8.2.2. Cost savings

250. The cost savings arising from the proposed merger have been identified as [**Confidential to Tabcorp**] [redacted] in year 1, [**Confidential to Tabcorp**] [redacted] in year 2, and [**Confidential to Tabcorp**] [redacted] from year 3 onwards [Simes assumptions 2]. As noted earlier in my evidence, Dr Pleatsikas and Dr Simes correctly identified that [**Confidential to Tabcorp**] [redacted], which is a transfer rather than a resource saving. This should be subtracted off the year 3 amount (and all subsequent years), giving [**Confidential to Tabcorp**] [redacted].

251. The equivalent amount to be deducted off the year 1 and 2 amounts is not specified in the assumptions. However, Dr Simes' Attachment B – Table 1 shows the cost savings net of any transfer, and based on this it appears that the amount to subtract off as a transfer is [**Confidential to Tabcorp**] [redacted] in year 1 (giving [**Confidential to Tabcorp**] [redacted]) and [**Confidential to Tabcorp**] [redacted] in year 2 (giving [**Confidential to Tabcorp**] [redacted]).

252. As I have discussed earlier, a key consideration is whether the remaining cost savings are merger-specific, and this has not been assessed by any of the experts, nor has there been a general test of their veracity. I note that Mr Thompson [4, third statement] has expressed his scepticism about the cost saving claims, although without the benefit of having access to the full set of confidential information. To assist the Tribunal, for my base case calculations I will assume that these remaining cost savings are merger-specific and otherwise robust, and should be reflected as a benefit.

253. However, I will also do some sensitivity testing. I am not aware of any evidence that would provide an alternative estimate of the cost savings for the purposes of sensitivity testing. However, as an indication, I sensitivity test a scenario in which the cost savings are reduced by 50% relative to the base case. While this figure is arbitrary, I use it in order to assist the Tribunal by providing a basis upon which to test the sensitivity of the benefits to changes in the cost savings.

8.2.3. Revenue synergies

254. Dr Pleatsikas and Dr Simes have identified certain increases in revenue that will arise from the proposed merger. However, as noted in my earlier assessment of their statements, it is increases in producer surplus that matter, not increases in revenue.

255. The various assumptions of the experts do not have any information on how producer surplus changes as a result of the proposed merger. However, the model developed by Mr Johnston does measure changes in revenue less certain "variable costs".[53] Mr Johnston refers to this in his model as "EBITDA", and this is also how it is referred to in the assumptions provided to the experts.

256. However, the costs that are identified as "variable costs" all relate to transfers from the merged entity to other parties. In particular, the costs relate to taxes (GST and State tax), variable fees payable to the racing industry, and variable fees payable to the licensees of retail wagering outlets.

257. I emphasise that these are not variable costs in the normal economic sense, in that they are not costs paid by the merged entity for goods or services directly provided to the merged entity. Rather, I would characterise them as transfers for the purposes of measuring welfare.

258. It is possible that there are no "true" variable costs associated with the increases in revenue referred to in the statement of Mr Johnston and in the assumptions – this is not clear

[53] Tab 4 of DJ-1, TBP.100.001.0002.

to me (I am leaving aside for the moment any integration or investment costs incurred to obtain these revenues). To assist the Tribunal, I will proceed on the basis that there are none, and that accordingly the best measure of producer surplus is the revenue. I note that if in fact there are variable costs, then revenue will overstate the true measure of public benefit. As a sensitivity test, I calculate a measure of variable costs based on Tabcorp's annual accounts, which I discuss in more detail below.

259. The revenue synergies identified by Dr Pleatsikas and Dr Simes relate to:

a) Improving the merged entity's fixed odds performance;

b) Introducing new and expanded products;

c) Re-branding and improving the retail network in Tatts states;

d) Increasing the number of fixed odds bets; and

e) Investing in the Keno retail network and brand.

260. I discussed earlier in my assessment of Dr Pleatsikas' evidence how an increase in producer surplus to the merged entity would not be treated as a benefit if it is simply the result of a transfer from rivals, as opposed to growing the market.

261. It is not possible from the assumptions to determine what proportion of the revenue increase is due to each of these effects. However I note that Dr Simes states (at [48]) that most of the revenue increases associated with the various revenue synergies (with the exception of Keno) will come from overseas based firms, which I interpret to mean that the merged entity would compete wagers away from (overseas based) rivals.

262. I note also that the calculation of the [**Confidential to Tabcorp**] [redacted] arising from the revenue synergies, which is referred to by Dr Simes at [47] and Mr Johnston at [102], implicitly assumes that the revenue increase comes from competing wagers away from rivals. This is because it is calculated by taking Tatts' current turnover, adding the increase in turnover from the revenue synergies, and dividing by the *current* market turnover. That is, the increased turnover from the revenue synergies is assumed not to result in any increase in market turnover, implying it is merely a transfer of turnover between wagering providers.

263. In respect of the Keno revenue increases, I have not been able to determine from any of the evidence or Mr Johnston's calculation of these increases whether this is more likely to result from growth in the market or a transfer from rivals. However, I note that Dr Simes does not attempt to attribute any of the revenue increase to growth in the market [38].

264. Accordingly, it seems reasonable to assume that all of the revenue increase for all of the synergies referred to above results from drawing punters away from rivals, and therefore should not be treated as a benefit.

265. Dr Simes states that one exception to this is where the transfer of surplus is from foreigners to Australians [46]. However, I have been instructed to assume that transfers from corporate bookmakers to Tabcorp are welfare neutral and do not fall within section 95AZH(2)(a)(ii). Accordingly, in my calculation of the benefits of the proposed merger, I do not include any of the claimed revenue synergies as benefits in my "base case" calculation.

However, I have also been instructed to, as an alternative, assess the public benefits on the basis that Dr Simes' assumption at [53] of his report is adopted for additional revenue that could be revenue taken from corporate bookmakers (in particular, that 50% of that additional revenue is allocated as the amount of substitution of overseas produced goods and services for domestically produced goods and services).

266. If there is some component of the revenue increases that arises from bringing new punters into the market, then there is also likely to be an increase in consumer surplus. Even if punters simply switch from overseas rivals to the merged entity this might also increase consumer surplus, as punters switching from the rival to the merged entity must be because it is beneficial to them. There may also be consumer surplus gains to the extent that the increase in the merged entity's purchasing power results in variable cost reductions that are passed through to punters in the form of lower prices (although as noted earlier this is unlikely to have any material impact on prices, given it is a relatively small proportion of the merged entity's revenues).

267. On the other hand, there may also be consumer surplus losses, to the extent that wagering is restricted by the merged entity's new fixed odds management system (as noted by Dr Simes at [44-45]). I also note that any consumer surplus gains would be offset to some extent by the welfare losses arising from increases in problem gambling. As already noted, the various experts have not attempted to quantify this. I note, however, that the Productivity Commission's quantification of the welfare losses from problem gambling (referred to earlier in my evidence) finds that these losses are in the range of approximately 40%-50% of the consumer welfare gains from gambling.

268. In Table 4 below I provide a summary of my treatment of the cost and revenue synergies in my base case quantification (figures reported are from year 3 onwards).

Confidential

Table 4
Summary of cost and revenue synergies [Confidential to Tabcorp]

Claimed cost/revenue synergy	Cost/revenue synergy used by Dr Simes	Cost/revenue synergy used in my quantification	Comments
Cost savings, [redacted]	Cost savings attributable to [redacted] are deducted, giving [redacted]	Cost savings attributable to [redacted] are deducted, giving [redacted]	I assume that the cost savings are merger-specific and otherwise robust, although I note this is disputed by Mr Thompson [third statement, 4]. I sensitivity test this assumption.
Revenue increase from improved fixed odds performance, [redacted]	50% of the revenue increase is treated as a benefit, on the basis that this amount is transferred from foreign rivals to the merged entity, giving [redacted]	Not included	The claimed benefit relates entirely to an effective price increase, so should not be treated as a public benefit. In any case, I have been instructed to assume that transfers from corporate bookmakers to Tabcorp are welfare neutral and do not fall within section 95AZH(2)(a)(ii).
Revenue increase from new products, [redacted]	50% of the revenue increase is treated as a benefit, on the basis that this amount is transferred from foreign rivals to the merged entity, giving [redacted]	Not included	I have been instructed to assume that transfers from corporate bookmakers to Tabcorp are welfare neutral and do not fall within section 95AZH(2)(a)(ii).
Revenue increase from retail improvements, [redacted]	50% of the revenue increase is treated as a benefit, on the basis that this amount is transferred from foreign rivals to the merged entity, giving [redacted]	Not included	I have been instructed to assume that transfers from corporate bookmakers to Tabcorp are welfare neutral and do not fall within section 95AZH(2)(a)(ii). It is also unclear if this is merger-specific, as the investment in retail improvements could be incurred by Tatts in the counterfactual.
Revenue increase from increased Tatts fixed	50% of the revenue increase is treated as a benefit, on the	Not included	I have been instructed to assume that transfers from corporate

odds bets, [redacted]	basis that this amount is transferred from foreign rivals to the merged entity, giving [redacted]		bookmakers to Tabcorp are welfare neutral and do not fall within section 95AZH(2)(a)(ii). I note also that some of the claimed benefit relates to an effective price increase.
Revenue increase from increased Tabcorp fixed odds bets, [redacted]	50% of the revenue increase is treated as a benefit, on the basis that this amount is transferred from foreign rivals to the merged entity, giving [redacted]	Not included	I have been instructed to assume that transfers from corporate bookmakers to Tabcorp are welfare neutral and do not fall within section 95AZH(2)(a)(ii).
Revenue increase from Keno improvements, [redacted]	Not included, as cannot determine what relates to efficiency improvements and what relates to transfers	Not included	As in Dr Simes' analysis, it is difficult to determine what portion of the revenue increase relates to efficiency improvements and what relates to transfers.
Consumer surplus gains and losses (excluding allocative efficiency detriments – see below)	Not included	Not included	There may be some consumer surplus gains for punters switching to the merged entity, but there may also be losses from punters restricted by the new fixed odds management system and losses from increases in problem gambling.

269. As noted above, I also run an alternative test in which I include some of these claimed revenue synergies. My treatment of the revenue synergies in this sensitivity test is as follows:

a) Improving the merged entity's fixed odds performance: as discussed earlier, the modelling of this benefit appears to show that the revenue increase results entirely from an effective price increase. Accordingly, I have not treated this as a public benefit in my sensitivity test;

b) Introducing new and expanded products: in my sensitivity test I assume that 50% (based on Dr Simes' analysis at [53]) is a transfer from foreigners to Australians, and can be treated as a benefit;

c) Re-branding and improving the retail network in Tatts states:

i. In my sensitivity test I assume that 50% (based on Dr Simes' analysis at [53]) is a transfer from foreigners to Australians, and can be treated as a benefit;

ii. But in any case, it is not clear if this claimed benefit is merger-specific. Indeed, it is specified in [Pleatsikas assumptions 286(a)] that Tatts would invest in its retail networks absent the merger, but not as rapidly or to the same extent as if the merger occurs. In this case it is only the present value of the timing difference of the profit increase that would be treated as a benefit. While the exact timing difference is unknown, the approach that I use for the purposes of quantification in my sensitivity test is to scale down the assumed revenue increase by a further factor of 50% (i.e., on top of the 50% already applied). This figure is arbitrary, as is Dr Simes' application of the 50% figure to adjust the revenue synergies for substitution from foreign to domestic firms, I use it in order to assist the Tribunal by providing a basis upon which to quantify the timing difference in the absence of more robust data;

d) Increasing the number of fixed odds bets:

i. In my sensitivity test I assume that 50% (based on Dr Simes' analysis at [53]) is a transfer from foreigners to Australians, and can be treated as a benefit; and

ii. This benefit also appears to be due, in part, to an effective price increase. Mr Johnston's model calculates the [**Confidential to Tabcorp**] [redacted] benefit from increased fixed odds bets for Tatts as an increased fixed odds turnover multiplied by the yield that has been increased by the [**Confidential to Tabcorp**] [redacted] percentage points. If, however, the increased turnover were multiplied by the counterfactual yield (i.e., without the [**Confidential to Tabcorp**] [redacted] percentage point increase), the benefit would be [**Confidential to Tabcorp**] [redacted].[54] It is this latter figure that I use in my sensitivity test (scaled down by 50% as noted); and

e) Investing in the Keno retail network and brand: for my sensitivity test I assume that this benefit comes entirely from new customers to the market, and therefore should be treated as a public benefit in its entirety.

270. Note that in the above sensitivity test I have assumed that the best measure of producer surplus is given by revenue, as discussed above. However, as an alternative to this I have calculated a measure of variable costs based on Tabcorp's annual accounts. Tabcorp's FY16 Annual Report reports "operating expenses" of $378.2m for the wagering and media segment, which is approximately 20% of revenue for this segment (of $1,873.0m). These operating expenses appear to include employment costs, communication and technology costs,

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[54] [**Confidential to Tabcorp**] From Mr Johnston's model [Tab 4 of DJ-1TBP.100.001.0002], the calculation of the [redacted] benefit is based on increased turnover of [redacted] multiplied by a yield of [redacted]. If, alternatively, the increased turnover of [redacted] were multiplied by a yield of [redacted] (i.e., the [redacted] yield less [redacted] percentage points), the benefit is approximately [redacted]. I note also that the [redacted] figure applies from year two onwards – the equivalent figure for year one is [redacted] [Johnston, Table 24]. There is not sufficient information in Mr Johnston's model to enable me to specifically adjust this year one figure for the yield difference. I therefore adjust it in proportion to the relationship between the [redacted] figures to determine [redacted] (that is, [redacted] as a proportion of [redacted] is the same as [redacted] as a proportion of [redacted]).

advertising and promotional costs, and property costs.[55] I cannot tell from the accounts which of these costs are variable, and they are likely to include some fixed costs. However, I am concerned that an assumption of zero variable costs might be quite extreme, and so I think there is value in running a sensitivity test assuming that variable costs equate to 20% of revenue. I therefore run an alternative scenario based on the above described sensitivity test but with variable costs estimated as 20% of revenue.

8.2.4. Flow-on benefits

271. Many of the benefits discussed by Dr Pleatsikas and Dr Simes are in the form of flow-through benefits to the racing industry. These claimed benefits result from the flow-through of the initial cost and profit synergies for the merged entity. As previously discussed in my evidence, these benefits should only be counted once, and as such any further flow-through of these benefits should not be counted. My interpretation of the flow-through amounts discussed by Dr Pleatsikas and Dr Simes is that these have already been counted in the original cost and revenue synergies for the merged entity, and I have therefore not included any further flow-through benefits in my calculations.

8.2.5. Costs

272. In addition to the various benefits listed in the assumptions, there are also various costs that are also referred to. To properly reflect the *net* benefit of the proposed merger, these should be deducted from the benefits assessed above.

273. The costs identified in the assumptions are:

a) [**Confidential to Tabcorp**] [redacted], [Johnston 46];

b) [**Confidential to Tabcorp**] [redacted] [Johnston 90]; and

c) [**Confidential to Tabcorp**] [redacted] [Johnston 105].

274. I note that the second and third of these costs are associated with revenue increases that I have not treated as public benefits in my base case quantification, as the claimed benefits result from a transfer between wagering providers. Despite this, these costs are still incurred by the merged entity, and should therefore be considered a social cost in the net benefits assessment. I note, however, that the cost associated with re-branding the retail network is also likely to be incurred in the counterfactual, albeit with a timing delay. Consistent with

[55] The full breakdown of "operating expenses" is not mentioned in Tabcorp's FY16 Annual Report, although the Income Statement on p.74 lists these categories of expenses.

the assumption noted above regarding the treatment of this as a benefit in my sensitivity test, I scale down this cost by a factor of 50% to account for this delay.

8.2.6. Results

275. I calculate the benefits (net of the costs referred to above) of the proposed merger over a two-year, five-year, and ten-year timeframe, and calculate the net present value (NPV) over each of these time periods. I calculate the NPV using a discount rate of 7%, as used by Dr Simes [footnote 43].

276. The results of this calculation for my base case are set out in Table 5 below.

Table 5
NPV results of benefits less specific costs, base case[56] [Confidential to Tabcorp]

Timeframe	NPV of benefits less specific costs at 7% discount rate
2-year timeframe	$
5-year timeframe	$
10-year timeframe	$

277. As noted above, I also test the sensitivity of my results to changes in the cost savings, where I scale these cost savings down by 50%. I report these results in Table 6.

Table 6
NPV results of benefits less specific costs, sensitivity test with reduced cost savings[57]
[Confidential to Tabcorp]

Timeframe	NPV of benefits less specific costs at 7% discount rate
2-year timeframe	
5-year timeframe	
10-year timeframe	

[56] I have also calculated the NPV over a 15-year timeframe, which returns a result of [Confidential to Tabcorp] $.

[57] I have also calculated the NPV over a 15-year timeframe, which returns a result of [Confidential to Tabcorp] $.

278. The results of my sensitivity test, where I include some of the claimed revenue synergies as discussed above (assuming revenue is the best measure of producer surplus, and using the base case cost savings), are reported in Table 7.

Table 7
NPV results of benefits less specific costs, sensitivity test with revenue as producer surplus[58] [Confidential to Tabcorp]

Timeframe	NPV of benefits less specific costs at 7% discount rate
2-year timeframe	$
5-year timeframe	$
10-year timeframe	$

279. As noted above, I also ran a further adjustment to this sensitivity test where I assumed variable costs of 20% of revenue. The results of this are shown in Table 8.

Table 8
NPV results of benefits less specific costs, sensitivity test with revenue less variable costs as producer surplus[59] [Confidential to Tabcorp]

Timeframe	NPV of benefits less specific costs at 7% discount rate
2-year timeframe	$
5-year timeframe	$
10-year timeframe	$

8.3. Detriments

280. By themselves, the benefits results have little meaning – for example, is a present value benefit of [Confidential to Tabcorp] $ large or small?

281. One way to provide some context for the benefit results is to estimate how material any competitive detriments would have to be to offset the estimated benefits.

[58] I have also calculated the NPV over a 15-year timeframe, which returns a result of [Confidential to Tabcorp] $.

[59] I have also calculated the NPV over a 15-year timeframe, which returns a result of [Confidential to Tabcorp] $.

282. Three types of competitive detriments can flow from a merger – allocative, productive and dynamic efficiency detriments. At this stage I focus just on allocative inefficiency. As explained in section 3 of my report, this is the loss of surplus arising from a price rise, or equivalently, quality reduction, resulting from a merger.

283. At the moment, I also limit my analysis to the wagering market, but note that I think the merger would result in competitive detriments in tote licencing markets as well.

284. I note at the outset that tote prices (as given by the take-out rate) are already at their price controlled level, at least in respect of Tabcorp [Smith assumptions 72] (Mr Tyshing appears to suggest that both totalisator operators have charged up to the price controlled level, [64], although Mr Twaits states that Tatts does not charge take-out rates at this level [38]). If that is correct, they are not able to be increased further, at least for Tabcorp. However the following evidence suggests it is not clear that prices could not be increased:

a) The relevant counterfactual is not the status quo, but what would happen over time in absence of the merger. As I have noted, we might expect the competitive tension between Tabcorp and Tatts to increase over time under the counterfactual, because of the growth of wagering through the channel. This might result in tote prices dropping below the regulated level under the counterfactual. Furthermore, if corporate bookmakers are placing material competitive pressure on totes, then further pressure would be placed on tote prices in the counterfactual;

b) [**Confidential to Tabcorp**] [redacted];[60] and

c) Even if price does not increase from any lessening of competition, quality could be negatively affected. Mr Tyshing makes a similar point regarding how the proposed merger might negatively influence the incentives of the merged entity to invest and innovate [395]. It is possible to proxy the reduction in quality by an increase in price.

285. If the merged entity were to increase prices/reduce quality, then there would be an incentive for its rivals to also increase prices or reduce quality (although not necessarily by as much as the merged entity does).[61] Accordingly, we can consider the effect of the merger in terms of the market-wide (average) increase in price (or reduction in quality) that results.

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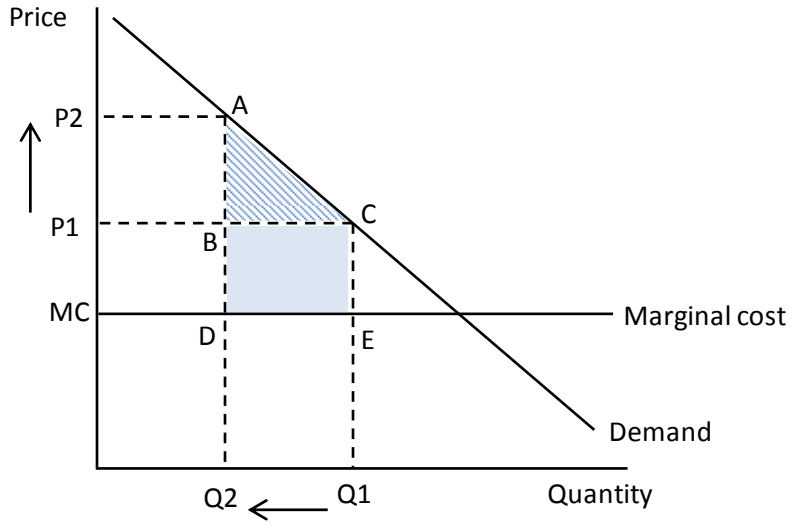
60 [**Confidential to Tabcorp**] [redacted]

61 This follows from the standard conceptual economic framework for analysing the unilateral effects of mergers. See, for example, Michael D. Whinston (2007), "Antitrust Policy Toward Horizontal Mergers", in M. Armstrong and R. Porter (eds.), *Handbook of Industrial Organization*, Elsevier, at p.2376; and Massimo Motta (2004), *Competition Policy: Theory and Practice*, Cambridge University Press, at p.246

286. The assumed increase in price (reduction in quality) can be conceptualised in a standard supply-demand framework, as shown in Figure 6. This graph illustrates a downward sloping (linear) demand curve and a constant marginal cost (supply) curve, with the starting price and quantity of P1 and Q1. If the merger leads to an increase in prices (or equivalently, a reduction in quality), then this leads to a new price-quantity combination of P2-Q2. The increase in price leads to a loss of consumer surplus (which is measured by the shaded triangle ABC above P1 and below the demand curve) and a loss of producer surplus (the shaded rectangle BCDE below P1 and above the marginal cost curve). The combined loss of consumer and producer surplus is the loss of allocative efficiency arising from the price increase.

Figure 6
Illustration of allocative efficiency detriment arising from a price increase



287. With estimates of the price and quantity P1 and Q1, marginal cost MC, the elasticity of demand and an assumed percentage price increase (which provides us with P2), it is possible to calibrate the above model and estimate an allocative efficiency loss represented by the shaded areas.[62]

288. I have undertaken these calculations assuming a single market for all wagering at the national level, which as noted earlier in my evidence is the relevant market argued by Dr Pleasikas and Dr Smith.

289. My calculations use the following inputs:

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[62] The elasticity of demand is given by the equation $e = \frac{dQ}{dP}\frac{P1}{Q1}$, which can be re-arranged to determine Q2, using the relationships $dQ = Q2 - Q1$ and $dP = P2 - P1$. The allocative efficiency detriment is then given by the area of triangle ABC, $0.5 \times (Q2 - Q1) \times (P2 - P1)$, and the area of rectangle BCDE, $(Q2 - Q1) \times (P1 - MC)$.

a) Total wagering market turnover for FY16, [**Confidential to Tabcorp and Tatts**] [redacted] [Simes assumption 26] – this is equivalent to Q1 in the graph above;

b) An initial price (take-out rate) of [**Confidential to Tabcorp and Tatts**] [redacted] (P1), calculated using the total wagering market revenue for FY16 of [**Confidential to Tabcorp and Tatts**] [redacted] [Simes assumption 26] as a proportion of the FY16 turnover figure just noted;

c) A range of assumed price rises, ranging from 0.5% to 5%, which when applied to the initial price P1 provide an estimate for the post-merger price of P2. To be clear:

   i. I note that when I apply a 5% price increase to a take-out rate, I first express the take-out rate in decimal form (e.g., [**Confidential to Tabcorp and Tatts**] [redacted]) and then increase this by 5% (to [**Confidential to Tabcorp and Tatts**] [redacted], and then convert the increased take-out rate back to a percentage ([**Confidential to Tabcorp and Tatts**] [redacted]). This is not the same as adding 5 *percentage points* to the take-out rate (i.e., increasing [**Confidential to Tabcorp and Tatts**] [redacted]), which would not be the correct approach; and

   ii. The assumed price increase is for all wagering products, e.g., tote and fixed odds products; and

d) A demand elasticity of -0.93, although I also sensitivity test a more inelastic demand curve of -0.6, both of which are as used by Dr Simes [141].

290. As context for the assumed price rise range of 0.5% to 5%, I note that:

a) The [**Confidential to Tabcorp**] [redacted] increase in Tatts' FY16 fixed odds yield is a change in yield from 12.1% (Johnston Table 18) to [**Confidential to Tabcorp**] [redacted], equivalent to a [**Confidential to Tabcorp**] [redacted] price rise; and

b) The change in Tatts' FY16 tote take-out rate referred to above, from [**Confidential to Tatts**] [redacted] in FY16 to [**Confidential to Tabcorp**] [redacted] in FY17 with the merger, is equivalent to a [**Confidential to Tabcorp**] [redacted] price rise.

291. I also require an estimate of marginal cost. A reasonably proxy for this is variable cost, although as noted in my assessment of the benefits of the proposed merger, the applicant has not put forward any variable costs that relate to the use of real resources (the costs that vary with turnover and revenue are transfers from the wagering firms to the racing industry and government). I therefore assume (in my base case) that variable cost is equal to zero, which is the same assumption made by the applicant's experts and in my base case benefits analysis above. However, I also run a sensitivity test with variable costs of 20% of revenue using data from Tabcorp's annual accounts, as discussed above.

292. Based on this data, I have calculated the allocative efficiency detriment for the assumed price increases arising from the proposed merger and applied to the total wagering market. I note that, although I have used the take-out rate (measured in percentage terms) as the "price", this is consistent with how the economics literature defines the price for wagering, as discussed earlier in my evidence. It is also appropriate to apply demand elasticities in the

standard way to this measure of price, i.e., an increase in price reduces quantity based on the demand elasticity.[63]

293. The resulting annual allocative efficiency detriments, for various assumed price increases, and for an elasticity of -0.93, are shown in Table 9 below. I have calculated each annual allocative efficiency detriment using the methodology discussed above and then, assuming that this detriment applies for each year over a relevant timeframe, calculated the NPV of the detriment (using a 7% discount rate).

Table 9
NPV of allocative efficiency detriment for all wagering market, base case[64] [Confidential to Tabcorp]

Timeframe	NPV of allocative efficiency detriment at 7% discount rate 0.5% price increase	NPV of allocative efficiency detriment at 7% discount rate 2.5% price increase	NPV of allocative efficiency detriment at 7% discount rate 5% price increase
2-year timeframe	$ [redacted]	$ [redacted]	$ [redacted]
5-year timeframe	$ [redacted]	$ [redacted]	$ [redacted]
10-year timeframe	$ [redacted]	$ [redacted]	$ [redacted]

294. As one sensitivity test on the above results, I estimated the allocative efficiency detriment using an elasticity of -0.6. The results are shown in Table 10.

Table 10
NPV of allocative efficiency detriment for all wagering market, -0.6 elasticity[65]
[Confidential to Tabcorp]

Timeframe	NPV of allocative efficiency detriment at 7% discount rate 0.5% price increase	NPV of allocative efficiency detriment at 7% discount rate 2.5% price increase	NPV of allocative efficiency detriment at 7% discount rate 5% price increase
2-year timeframe	$ [redacted]	$ [redacted]	$ [redacted]
5-year timeframe	$ [redacted]	$ [redacted]	$ [redacted]
10-year timeframe	$ [redacted]	$ [redacted]	$ [redacted]

63 See Suits (1979), *op cit*.

64 I have also calculated the NPV over a 15-year timeframe, which returns a result of [**Confidential to Tabcorp**] [redacted].

65 I have also calculated the NPV over a 15-year timeframe, which returns a result of [**Confidential to Tabcorp**] [redacted].

295. As a second sensitivity, I return to my base case elasticity assumption of -0.93, but assume some variable costs of 20% of revenue, as described above. The results of this are shown in Table 11.

Table 11
NPV of allocative efficiency detriment for all wagering market, -0.93 elasticity and variable costs[66] [Confidential to Tabcorp]

Timeframe	NPV of allocative efficiency detriment at 7% discount rate 0.5% price increase	NPV of allocative efficiency detriment at 7% discount rate 2.5% price increase	NPV of allocative efficiency detriment at 7% discount rate 5% price increase
2-year timeframe	$	$	$
5-year timeframe	$	$	$
10-year timeframe	$	$	$

296. As an example of how the calculated detriments can give context to the benefit estimates, I estimated earlier in my evidence an NPV benefit of [**Confidential to Tabcorp**] $ over a 10-year period (using 7% as the discount rate). With an elasticity of -0.93, a price increase in the wagering market of less than 2.5% would result in allocative efficiency detriments that exceed this, e.g., at 2.5% the NPV of the detriment is [**Confidential to Tabcorp**] $ (in the base case).

297. As a final sensitivity test, I have also calculated allocative efficiency detriments for the wagering market using a non-linear "constant elasticity" demand specification. I have not presented the results here, but the results are slightly lower detriments from those presented above – for example, for a 5% price increase and elasticity of -0.93 the 10-year NPV of the allocative efficiency detriment is [**Confidential to Tabcorp**] $ (compared with [**Confidential to Tabcorp**] $ in Table 9).

[66] I have also calculated the NPV over a 15-year timeframe, which returns a result of [**Confidential to Tabcorp**] .

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