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Lyn Camilleri
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Australian Competition and Consumer Commission
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Dear Ms Camilleri,

Proposed merger between Armaguard and Prosegur – Submission on Proposed Undertaking

I refer to your consultation letter dated 21 March 2023. The Australian Hotels Association (**AHA**) provided a submission on the application for merger authorisation on 28 October 2022. AHA still holds serious concerns that the merger will result in significant harm to its members and everyday consumers, and agrees with the ACCC's preliminary views.

However, the focus of this submission is on the Applicant's response to the ACCC's Statement of Preliminary Views, particularly the Proposed Undertaking. The AHA considers that the Proposed Undertaking is not suitable in its current form and will not appropriately address the potential competitive harm from the merger. We have suggested some practical amendments and recommendations which may improve the Proposed Undertaking in terms of monitoring and compliance, should the ACCC accept one.

Unless otherwise defined, defined terms in this submission have the same meaning as in the Proposed Undertaking and ACCC Statement of Preliminary Views

1. No undertaking would be sufficient to address the substantial competition issues

The AHA agrees with the ACCC's preliminary view that the merger is likely to lead to significant competitive detriments. Given the number, nature and extent of those competitive detriments and the obvious difficulties in monitoring and enforcing a behavioural undertaking, the AHA has serious doubts that any behavioural undertaking could effectively address the competitive harms of the merger.

The risks of accepting a weak undertaking are particularly high in this case. Given the merger to monopoly removes the only other supplier of CIT services with the infrastructure and national reach to offer CIT services to many AHA members, and the high barriers to entry and expansion, an inadequate undertaking (or failure to rigorously monitor and enforce it) is likely to lead to competitive harm that cannot easily be undone.

However if, despite these risks, the ACCC were to accept a behavioural undertaking, the AHA submits that the Applicant's Proposed Undertaking in its current form is not suitable and should be not accepted as an adequate remedy. The Proposed Undertaking has serious flaws and could be measurably improved in several ways.

2. The Pricing Process should be tested by an alternative independent expert to ensure it does not facilitate engineered outcomes that benefit the monopolist

It is a priority for AHA members that any undertaking constrains the merged entity's ability and incentive, as a monopolist, to unilaterally increase prices above a competitive level. Given the complexity of the formulae, inputs and methodology used in the Pricing Process, AHA members are not in a position to test its appropriateness as a model for determining price in the market.

Accordingly, AHA submits that the ACCC should require that the model for the Pricing Process is reviewed and tested by an alternative independent expert, and publish that expert's report for interested parties to review and comment on. The ACCC (and interested parties including AHA members) can only be satisfied that the Pricing Process is appropriate if it has been independently and rigorously tested.

Without having the benefit of a truly independent alternative critique, AHA members are concerned that the Pricing Process appears to give the merged entity full discretion over the inputs that will be used to determine its prices under the Pricing Process – for example, its revenue forecasts, Target Operating Expenditure, and the inputs used in the calculation of the maximum cost increase allowed when a customer changes its volume requirements.

Further, while an Independent Auditor will be able to verify the calculations involved in the Pricing Process, there is no mechanism for ensuring that the merged entity does not artificially inflate or reduce certain inputs to engineer a pricing outcome that maximises its profitability. Operating post-merger without any competitive constraints, the merged entity would have a clear ability and incentive to engineer a desired outcome. An Independent Auditor can only verify that the Pricing Process has been complied with; it cannot remedy or change a flawed Pricing Process.

An additional measure to impose accountability for any pricing outcomes on the merged entity would be to require the merged entity to include a negotiate/arbitrate mechanism. This would provide customers with a potential avenue for redress should a customer dispute the correctness or appropriateness of an input in, or the outcome of, the Pricing Process. If negotiations cannot resolve the dispute, an independent arbitrator or the ACCC should be empowered to make a binding arbitration decision on the applicable pricing level.

3. The service offering / improvement commitments are incapable of being measured and monitored

Even if the merged entity could be prevented from increasing prices above competitive levels through the effective implementation of a Pricing Process with sufficient safeguards, the merged entity would still have the ability and incentive to reduce the quality of its service offering. In fact, that incentive would increase in circumstances where the monopolists' ability to maximise profits by charging higher prices is constrained.

AHA members do not have confidence in a vague statement that "the merged entity will continue to supply CIT services to the same standard as before the merger" will prevent it from reducing its service quality. There are no criteria or benchmarks for measuring the standard of service being provided, and therefore monitoring compliance with the service offering commitment. The burden involved in making a complaint in relation to a reduction in service quality is unclear.

It is also unclear what the consequences would be if a customer asserts that the standard of service has decreased. In any case, the merged entity would surely dispute any complaint, especially when it can claim to have satisfied a commitment without any objective criteria or definitive benchmarks.

Similarly for the improvement commitment, the promise to "work with customers and suppliers to identify, approve and implement productivity improvements" is a vague overarching statement with no objective criteria for monitoring compliance. For example:

- What minimum level or types of improvement should be achieved?
- What is the consequence if service offerings stagnate (even if they do not decline)?

The ACCC's guidelines state that undertakings must be "detailed, specific and free from ambiguity." The service offering and improvement commitments are none of these.

Without the credible threat of being able to switch to alternative suppliers, AHA members require far more protection against decreases or stagnation in service quality. In the first instance, this requires specifying the metrics that will be criteria for these commitments, the methods for measuring compliance and the consequences of non-compliance. Only when those details are received can the ACCC be in a position to assess the likely efficacy of any service offering and improvement commitments.

4. The complaint handling process is one-sided and will not be effective

As a preliminary issue, AHA members request further details on what is required for a complaints handling process to be compliant with the Australian Standard on Complaints Management; this standard is not freely accessible to the public.

Further, AHA members are not confident that a requirement on the merged entity "to investigate and respond to such a complaint" is sufficiently specific or strict. AHA understands that the complaints handling process will be published on the merged entity's website. At a minimum, the published process should specify a deadline for responding, the steps to be taken to investigate and resolve a complaint, and the possible outcomes and remedies available to consumers.

As with the Pricing Process, AHA submits that before it is accepted as part of an undertaking, the proposed complaint handling process should be independently reviewed by an expert in the complaints handling field to test and evaluate whether it is appropriate in these circumstances. That evaluation or report should be made available by the ACCC for interested parties to comment on. The ACCC and interested parties cannot be confident in the process' ability to operate effectively without an expert third-party having reviewed the Applicants' proposal. An independent evaluation may also offer ways to address the further concerns below.

The real issue with any complaints handling process – however designed – is the lack of independent oversight over whether complaints are being appropriately investigated and responded to in a timely and effective manner. The reporting obligations only extend to a description of any complaints made, not their resolution. In any case, the merged entity will have full editorial control of those reports, and may gloss over, or downplay complaints, or overstate their resolution, undermining the intended aim of providing transparency.

AHA members support the inclusion of a complaints handling process in any undertaking. However, the process should include the ability to escalate the complaint to an independent third party or the ACCC if the complainant is not satisfied that their complaint has been adequately handled.

The complaints process should ensure the complainant's views are adequately reported – this could be done by the merged entity giving the complainant an opportunity to draft or review the section of the merged entity's report to the ACCC in advance, or by making clear that the initial complaint will be included in the report to the ACCC.

5. The reporting obligations will not be an effective safeguard against the competitive harms of the merger

AHA members have serious doubts that the process of reporting compliance with the undertaking to the ACCC and the RBA will be sufficient to ensure the undertaking is adequately addressing the competition harms arising from the transaction.

First, the effectiveness of compliance reporting is clearly undermined when some of the key aspects of the undertaking – namely, the service offering commitment and complaint handling process – do not have clear, measurable metrics against which compliance can be assessed and reported on.

Second, given the merged entity is required to draft the audit plan, it could theoretically propose an audit plan that is surface-level only and to its benefit — for example, a plan that could prevent the Independent Auditor from contacting customers. This would fetter the "Independent" Auditor's powers and discretion to investigate and challenge assertions of compliance, and make proper recommendations to improve the integrity of the audit process.

Finally, even if such concerns did not arise, AHA members consider that an annual audit will mean that customers will have to suffer the consequences of any degradation in service levels for more than one year before they are surfaced, let alone remedied.

The AHA considers that any undertaking and audit plan should provide the Independent Auditor more autonomy to determine the best method of auditing the merged entity, rather than allowing the merged entity to set the terms of its own audit. Further, reports should be required 6-monthly, at least.

6. Stronger measures are needed to ensure compliance with the undertaking

Regardless of its form, the ACCC's enforcement options if the merged entity does not comply with the undertaking are limited. All the ACCC can do is take the merged entity to court, and seek an order requiring it to comply.

AHA has no confidence that this usual enforcement mechanism will be a strong enough deterrent to ensure compliance by a merged entity that will become a monopolist and have the ability and incentive to behave one. A bigger stick – which targets those incentives in the first place – is needed.

AHA proposes that undertaking should require that, if the ACCC considers that there has been non-compliance with the undertaking, the merged entity will no longer operate the business. Instead, an independent manager would be appointed to operate the business, while the merged entity would remain an owner or investor in the business. The separation of ownership from operation of monopoly assets and essential infrastructure is common in other industries and AHA considers is analogous to and appropriate for the current acquisition.

In contrast to the current enforcement option available to the ACCC, the risk of appointing an independent manager would introduce a stronger incentive for the merged entity to comply with the undertaking.

The ACCC could also consider taking this a step further, and require an independent operator of the merged entity as an upfront requirement of the Undertaking and condition of authorisation (i.e., without the need for non-compliance first), to remove the merged entity's incentive to operate the business in a way that maximises profit through monopolistic behaviour. AHA considers that the

appointment of an independent operator is as close to a structural remedy as is likely to be available, given the inherent challenges associated with behavioural undertakings.

Thank you for the opportunity to have made this submission.

Yours faithfully,

STEPHEN FERGUSON
NATIONAL CEO