PUBLIC VERSION

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Australian Competition & Consumer Commission
17/2 Lonsdale Street
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Miriam Kolacz
Assistant Director, Competition Exemptions
Australian Competition & Consumer Commission
17/2 Lonsdale Street
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Dear Mr Pomery, Ms Kolacz,

Proposed merger between Armaguard and Prosegur

Next Payments Pty Ltd (***Next Payments***) provides a submission regarding the revised draft section 87B undertaking submitted in relation to the proposed merger of Armaguard and Prosegur (the ***Proposed Merger***). Armaguard and Prosegur are referred to in this submission as the ***Applicants***.

The Proposed Merger will lead to the creation of a vertically integrated monopolist that will control every stage of cash delivery to consumers.

The ability and incentive of MergeCo to squeeze out independent ATM deployers by price and non-price means is clear. The ACCC clearly articulates this in its thorough Statement of Preliminary Views. Next Payments and NCR Australia Group have provided multiple, evidence-based, submissions setting out why the Proposed Merger is likely to lead to vertical foreclosure. Those submissions were supported by reports from independent economic experts.

By contrast, the Applicants have not engaged with this issue and have not provided any evidentiary basis as to why vertical foreclosure, and a consequent lessening of competition in ATM markets, is not a likely consequence.

The Applicants did not address this issue at all in their initial submission (nor did their economist). Having been forced to engage with the issue, in their response to the Statement of Preliminary Views, the Applicants make a cursory assertion that it would be 'irrational' for them to discriminate against independent ATM deployers as those entities are sources of CIT revenue. The Applicants ignore the fact that by squeezing out independent ATM deployers they will make handsome gains in ATM markets (as explained in Next Payments' submission of 31 October 2022). The Applicants' initial draft undertaking did not address the vertical foreclosure issue aside from a vague commitment that MergeCo 'will offer "ATM Specific Services"'. Now, a matter of weeks before the ACCC is due to take its decision and with impacted industry participants accorded only 5 business days to comment, the Applicants propose a further undertaking (supported by cursory assertions that there is no vertical foreclosure issue) which again will not prevent, or even curtail, MergeCo's ability or incentive to squeeze out competing ATM deployers.

The proposed undertaking does not address the vertical foreclosure issue:

- The proposed undertaking will not prevent MergeCo from engaging in non-price forms of discrimination. The Applicants commit to complying with Existing Arrangements for only three years. The terms of Next Payments' current agreement with Prosegur will not prevent MergeCo from reducing the quality of CIT services (or from favouring its own ATM business) in order to hamper Next Payments' ability to compete.

- In terms of price-discrimination, the undertaking allows for prices for existing customers to increase each year by inflation plus 7.5%. This commitment does not tie prices to efficient costs and is unlikely to replicate the outcome of a competitive market. It does not remedy the horizontal concerns that the ACCC has identified. The price commitment also does not preclude prices from increasing to levels that squeeze the margins of competing ATM deployers and CIT service providers.

In its assessment as to whether it can be satisfied in all the circumstances that there is no substantial lessening of competition or there is a net public benefit, the ACCC is faced with vague assertions from the Applicants that are not backed by evidence or economic expert opinion and a proposed undertaking that does not remedy the vertical foreclosure issue.

Furthermore, Next Payments continues to consider that the counterfactual against which to assess the Proposed Merger is not disorderly exit by one of the Applicants, following continued statements by Prosegur of the sound performance of its business.

Next Payments respectfully submits that, on this basis, the ACCC should not authorise the Proposed Merger.

If the ACCC is to authorise the Proposed Merger then only a structural remedy – in the form of divestment of the Applicants' ATM businesses or a market share cap – can address the vertical concerns. This is the only means by which the Applicants' incentive and ability to quash competition in ATM markets can be satisfactorily addressed.

If the ACCC is to authorise the Proposed Merger without a structural divestment, the only way in which a substantial lessening of competition could be avoided would be for a non-vertically integrated CIT service provider to service Next Payments and other independent ATM deployers. The only other provider of any size is Authentic Security. As explained in Next Payments' submission of 31 October, Authentic Security does not currently have the scale to meet Next Payments' requirements. To give Authentic Security the chance to reach that scale, it will need sufficient access to MergeCo's CIT infrastructure. This means ongoing access to ACCs on fair and commercially viable terms – as opposed to access limited to three years. It also means access to the surplus infrastructure that the Applicants will divest following the merger. In this regard, it is critical that Authentic Security can acquire any trucks and related equipment that the Applicants divest. The undertaking does not provide for this. Without access to those trucks, Authentic Security will not have the chance of increasing its scale in sufficient time to adequately service independent ATM deployers.

Next Payments provides further comments on the proposed undertaking in Attachment A to this letter.

Confidentiality

Parts of Next Payments' submission that have been highlighted red and are preceded by the word "**CONFIDENTIAL:**" contain confidential and commercially sensitive information of Next Payments and could cause harm to Next Payments if disclosed. Next Payments requests that the ACCC treat that information as strictly confidential and not disclose that information to any person without the prior written consent of Next Payments, except that, in accordance with the ACCC's usual confidentiality regime:

- there is no restriction on the internal use, including future use, that the ACCC may make of confidential information consistent with the ACCC's statutory functions;

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- confidential information may be disclosed to the ACCC's external advisors and consultants on the condition that each such advisor or consultant will be informed of the obligation to treat the information as confidential;
- the ACCC may disclose the confidential information to third parties (in addition to its external advisors or consultants) if compelled by law or in accordance with section 89(7) or section 155AAA of the *Competition and Consumer Act 2010* (Cth).

Next Payments would be happy to respond to any queries the ACCC may have or discuss any matter in relation to its submission.

Yours sincerely

[redacted]

Tim Wildash
Executive Chairman
Next Payments Pty Ltd
[redacted]

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Attachment A – Supplementary submission on proposed undertaking

1 The counterfactual against which to assess the Proposed Merger is not disorderly exit by one of the Applicants

The Applicants continue to suggest there will be disorderly exit in the near term. However, Prosegur continues to make statements concerning its financial performance that are inconsistent with this claim.

Most recently, on 4 May 2023, Prosegur made the following statements to the market in releasing its financial results for Q1 2023 (emphasis in Prosegur's own statements):[1]

- Prosegur has experienced '***Double digit*** *increase of* ***sales*** *in* ***all regions***', with '*Continuous* ***volume recovery***' and '*Excellent performance [in]* ***all geographies***.[2]
- The revenue for the 'Rest of World' region which includes Australia experienced 14.8% revenue growth compared to Q1 2022.[3]

As Next Payments has previously raised, Prosegur's statements and recent financial reports indicate its Australian CIT business is performing soundly and recovering from any temporary underperformance (ie, associated with the COVID pandemic). The public statements do not suggest any serious trouble in the business. Next Payments does not consider the Proposed Merger is required to sustain the Applicants' businesses, and there remain alternatives to the Proposed Merger that will avoid the significant harms to competition that it presents.

2 The proposed undertaking does not address the vertical foreclosure issue

The Applicants assert that there is no vertical foreclosure issue because independent ATM deployers impose a constraint in relevant ATM markets. This assertion is not coherent. Independent ATM deployers, like Next Payments, do constrain the Applicants' ATM business. This is precisely why the Applicants will have the incentive to use their absolute control of CIT services to quash competing independent ATM deployers.

The Applicants further assert that it would be irrational for MergeCo to discriminate against independent ATM deployers as they are a source of CIT service revenue. The Applicants ignore the fact that by squeezing out independent ATM deployers they will make handsome gains in ATM markets (as explained in Next Payments' submission of 31 October).

The Applicants then claim that they have proposed a revised undertaking that 'directly responds to any perceived concerns raised by Independent ATM Deployers'. They have not.

Due to the Applicants' eleventh-hour proposal to the ACCC, Next Payments has been accorded 5 business days to consider the proposed undertaking – a commitment which purports to appease concerns raised by Next Payments and NCR Australia Group about their ongoing ability to compete and, as the Applicants claim, continue to provide a 'significant competitive constraint'.

[1] https://www.prosegur.com/dam//Prosegur/CORP/pdf/accionistas_inversores/informes-trimestrales-ing/2023/230504---Prosegur-1Q---2023-Results-Presentation.pdf
[2] Ibid, pp 3, 10.
[3] Ibid, p 4.

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Nevertheless, it is clear from the face of the proposed undertaking that the Applicants have not seriously engaged with the vertical foreclosure issue. They have proposed a vaguely worded undertaking that will allow them to engage in the price and non-price discrimination that Next Payments has previously articulated and that the ACCC acknowledged in its Statement of Preliminary Views.

(a) Price discrimination

The price increases allowed for under clause 5 of the proposed undertaking do not tie prices to efficient costs and are unlikely to replicate the outcome of a competitive market. They do not remedy the horizontal concerns that the ACCC has identified. The price commitment also do not preclude prices from increasing to levels that squeeze the margins of competing ATM deployers and CIT service providers.

It will expose Next Payments and other independent ATM deployers to margin squeeze.

In Next Payments' case, [redacted]

A price increase of CPI plus 7.5% year on year is too high. There is no explanation as to how this was arrived at and there is no commitment to tie the price increases to efficient costs. By contrast, new customers would be provided Open Book pricing, which is based on a cost-plus method (clause 5.3). As set out in Next Payments' submission of 4 April 2023 a cost-plus method of pricing is more appropriate – and should be provided to all customers. Failing that, any pricing mechanism would need to be capped at no higher than CPI or 7.5%, whichever is lower.

(b) Non-price discrimination

To address the non-price discrimination issues raised by Next Payments and recognised by the ACCC, the Applicants commit to meeting the obligations under Nex Payments' agreement with Prosegur for three years.

This commitment will not prevent MergeCo from engaging in discriminatory conduct. The service level commitments set out in Next Payments' current agreement with Prosegur will not prevent MergeCo from:

- Reducing CIT service levels provided to Next Payments, including – reducing the frequency of ATM provisioning, cancelling cash delivery routes, reducing maintenance of ATMs, providing banknotes that cause ATM jams, and providing fewer out of hours services.
- Providing higher CIT services to its own ATM network.

The agreement with Prosegur was negotiated in a context where Next Payments could choose between Prosegur and Armaguard. It was not negotiated to protect Next Payments from a monopolist with the ability and incentive to engage in vertical foreclosure strategies.

[redacted]

[redacted]

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- [redacted]
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- [redacted]

(c) No effective dispute resolution

If MergeCo does not meet its obligations under its agreement with Next Payments, there is no practical recourse for Next Payments:

- As explained above, Next Payments' current agreement with Prosegur does not protect it against MergeCo's discriminatory conduct. It was not written to curtail a vertically integrated monopolist.
- If MergeCo fails to meet its obligations under the agreement with Next Payments, Next Payments and others must engage in a convoluted and lengthy complaints handling process (cl 5.24). Only after that may a dispute be raised with the independent expert as to MergeCo's compliance with existing arrangements with Next Payments (cl 6.2). The Independent Expert cannot compel MergeCo to provide services on fair, reasonable and non-discriminatory terms – it can only 'accept, reject or vary MergeCo's proposed CIT price and / or non-price terms and conditions for the supply of CIT Services to the Customer' (cl 6.9(e) and 6.10).
- The Independent Audit function proposed in cl 7 does not provide any practical protection. By the time any discriminatory conduct is revealed via that process, it will be too late. The damage to

competition will have been done. It only takes one instance of an ATM outage for customers to lose faith in the machines and service provided by independent ATM providers.

(d) No effective confidentiality measures

The confidentiality and ring-fencing provisions in clause 14 are deficient and cannot be characterised as proper ring-fencing measures. They will enable MergeCo to exploit commercially sensitive data obtained from Next Payments and others to benefit MergeCo's interests.

The proposed undertaking does not include any requirements as to the separation of staff, information databases and systems, and the use of secure encryption methods, to prevent inappropriate sharing of commercially sensitive information within MergeCo.

Without such measures staff that are involved in the provision of CIT services to Next Payments or other competitors of the merged entity can be concurrently involved in competing *against* Next Payments and other customers. Without separate information storage and encryption there is nothing to prevent staff of MergeCo's ATM business unit inappropriately accessing commercially sensitive information of Next Payments and other ATM deployer customers.

(e) Insufficient duration

The Proposed Merger will lead to a permanent structural change. Any undertaking should last as long as the vertical foreclosure risks are present, even if that means it is indefinite subject to variation by the ACCC (as initially proposed by the Applicants).

3 The vertical foreclosure issues are not capable of remedy by a behavioural undertaking

The vertical foreclosure risk created by the Proposed Merger cannot be addressed by a behavioural undertaking.

Pricing controls are too difficult to enforce. Non-price forms of discrimination are too difficult to detect and police.

The behavioural undertaking proposed by the Applicants falls well short of others accepted by the ACCC. Next Payments sets out below the types of protections commonly seen in those undertakings which are absent from that proposed by the Applicants. This is not to say that if the Applicants' undertaking addressed these issues then no competition risks would arise. Rather it shows how complicated it is to use a behavioural undertaking to address the specific vertical foreclosure risks raised by the proposed merger:

- **There must be objective service level KPIs that prevent non-price discrimination.** Any behavioural undertaking must include expressly stated and comprehensive obligations to provide services on fair, reasonable and non-discriminatory terms. For example, previous behavioural undertakings accepted by the ACCC and the Federal Court have included provisions that clearly commit the merged entity to:

- Comply with non-discrimination obligations that expressly preclude the merged entity from providing more favourable terms to its own business or that of a related entity, or from discriminatory treatment against a third party.[4]
- Clearly specify objective service level criteria, or key performance indicators, as a condition of non-price obligations – for example, by requiring the merged entity to comply with expressly stated service levels in the undertaking itself.[5]
- Obligations to self-report in relation to the merged entity's performance against the service level criteria, and to report non-compliance with the above non-discrimination commitments, to the ACCC and the relevant independent auditor.[6]

- **There must be robust confidentiality and ring-fencing measures.** These involve the separation of staff, information databases and systems, and the use of secure encryption methods, to prevent inappropriate sharing of commercially sensitive information within the merged entity.[7]
- **There must be a practical and effective consequence for non-compliance.** For example a swift and effective dispute resolution mechanism that forces MergeCo to cease engaging in discriminatory practices.[8]

4 Only a structural remedy will suffice

The Applicants have shown that they are not serious about proposing a behavioural undertaking that addresses the vertical foreclosure issues.

In this case, for the reasons previously outlined by Next Payments, the only way to resolve those risks is via structural remedies.

The most effective of those would be the divestment of the Applicants' ATM business. This would remove MergeCo's incentive to foreclose and preserves competition in ATM markets for the benefit of consumers.

An alternative approach would be to impose a market share cap that prevents MergeCo from increasing its ATM network above a certain size. This would preserve competition among the other independent ATM deployers and would remove MergeCo's incentive to squeeze out competing ATM deployers.

[4] Melbourne International RoRo & Auto Terminal Pty Ltd (a wholly owned subsidiary of Wallenius Wilhelmsen Logistics AS of Norway) - proposed acquisition of automotive terminal at the Port of Melbourne (Clause 5 and Schedule 1).
[5] Undertaking given by Pacific National Pty Limited, Annexure to the Federal Court's reasons in *Australian Competition and Consumer Commission v Pacific National Pty Limited (No 2)* [2019] FCA 669 (Clause 5, Schedules 1 and 3).
[6] Melbourne International RoRo & Auto Terminal Pty Ltd (a wholly owned subsidiary of Wallenius Wilhelmsen Logistics AS of Norway) - proposed acquisition of automotive terminal at the Port of Melbourne (Clause 8); Australian Amalgamated Terminals Pty Ltd (AAT) – proposed acquisition of Automotive and Ro-Ro Terminal at the Port of Fremantle (Clause 8).
[7] See for example the s87B undertaking provided in Melbourne International RoRo & Auto Terminal Pty Ltd (a wholly owned subsidiary of Wallenius Wilhelmsen Logistics AS of Norway) - proposed acquisition of automotive terminal at the Port of Melbourne, which included, among other things, physical and information access controls set out in a confidentiality policy that formed part of the undertaking and was made publicly available (Clause 7 and Schedule 2).
[8] Australian Amalgamated Terminals Pty Ltd (AAT) – proposed acquisition of Automotive and Ro-Ro Terminal at the Port of Fremantle (Clauses 10 and 11, Schedules 4 and 5).

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5 More is needed to facilitate competition in the supply of CIT services by third party providers

If the ACCC were to authorise the Proposed Merger, without a structural divestment, the only way in which a substantial lessening of competition could be avoided would be for a non-vertically integrated CIT service provider to service Next Payments and other independent ATM deployers.

The only other provider of any size is Authentic Security. As explained in Next Payments' submission of 31 October, Authentic Security does not currently have the scale to meet Next Payments' requirements.

To give Authentic Security the chance to reach that scale, it will need sufficient access to MergeCo's CIT infrastructure.

The proposed undertaking includes provisions to grant access to ACCs to third party CIT service providers. However, these provisions are inadequate. To give Authentic Security the chance to become a viable option for independent ATM deployers, the following is required.

- **Access to trucks:** In rationalising costs, MergeCo will divest infrastructure, including trucks. It is critical that Authentic Security be given access to those divested trucks in a timely manner. If MergeCo were to withhold those trucks from Authentic Security it would hamper Authentic's expansion. MergeCo should be required to make those trucks available to Authentic Security on fair and reasonable terms.
- **More robust service access requirements:** The proposed undertaking does not include express obligations to provide access to ACCs and related services (cash processing services and ancillary services) on fair, reasonable and non-discriminatory terms. Instead the proposed undertaking indicates third party CIT providers will be provided access and related services '*on terms no less favourable than the [relevant] standard terms and conditions*' – subject to compliance with the merged entity's (discretionary) policies and procedures.

  In fact, the third party CIT provider standard terms provided do not contain any express minimum service standards or requirements to provide open access in a fair, reasonable and non-discriminatory way. They instead provide that the merged entity has the '*right to perform the Services in our sole and absolute discretion in the method we deem appropriate*' (clause 2.2) and subject to the merged entity's rights to unilaterally terminate the agreement without cause (clause 12.7(a)).
- **Indefinite access:** The undertaking is proposed to last for only 3 years. Third party CIT service providers should be given access to ACCs on an indefinite basis otherwise they will not provide a viable long term source of CIT services for independent ATM deployers.