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9 May 2023

BY EMAIL: Armaguard-Prosegur-Merger@accc.gov.au

Lyn Camilleri
General Manager
Australian Competition & Consumer Commission
23 Marcus Clarke Street
Canberra ACT 2601

Dear Lyn

As you know, we act for a multi-store retail chain.

Thank you for the opportunity to comment on the revised draft undertaking proposed by Linfox Armaguard Pty Ltd (**Armaguard**) and Prosegur Australia Holdings Pty Limited (**Prosegur**) on 1 May 2023 (**Revised Proposed Undertaking**).

Our client has considered the Revised Proposed Undertaking in the short time available and sets out below its comments on the Revised Proposed Undertaking for the Commission's consideration.

In this letter, capitalised terms have the same meaning as in previous submissions made by our client or in the Revised Proposed Undertaking. The proposed undertaking offered by the merger parties on 9 March 2023 is referred to as the **First Proposed Undertaking**.

1. THE REVISED PROPOSED UNDERTAKING IS INADEQUATE AND SHOULD BE REJECTED

1.1 The Revised Proposed Undertaking does not address our client's fundamental concern that the Proposed Transaction would lead to the *immediate* elimination of competition from the CIT market, in circumstances where this would not occur (at least not in the short, and perhaps longer, term) in the absence of the Proposed Transaction.

1.2 The Revised Proposed Undertaking does not alter the position outlined in our letter of 6 April 2023 that, should the Proposed Transaction be authorised, customers of the parties, including our client, will have no choice but to deal with a monopoly CIT operator indefinitely and will lose the ability to switch, or leverage the ability to switch to negotiate a better deal for the provision of CIT services.

1.3 The loss of competition in the market for CIT services will harm not only our client and other customers of the merger parties, but also Australian consumers who in turn are likely to face higher costs for the goods and services they purchase from our client and other of the

parties' customers. This loss of competition is a significant, irreversible and perpetual public detriment that will outweigh any minor public benefits that could reasonably be said to arise.

1.4 For these reasons alone, our client maintains that the Commission should reject the Revised Proposed Undertaking and should not authorise the Proposed Transaction.

2. CONCERNS ABOUT SPECIFIC ASPECTS OF THE REVISED PROPOSED UNDERTAKING

2.1 Our client acknowledges that the parties have made efforts to address certain specific concerns outlined in our client's letter of 6 April 2023 and other interested party submissions.

2.2 However, in addition to the fundamental concern which remains unaddressed, significant concerns with the detail, scope and terms of the Revised Proposed Undertaking remain, and the Revised Proposed Undertaking is in fact worse in some respects than the First Proposed Undertaking.

2.3 In particular:

(a) *A 3 year term is clearly inappropriate*

The merger parties have misconstrued the concern raised by our client and other interested parties about the indefinite nature of the First Proposed Undertaking, purporting to address the concern by limiting the term of the undertaking to 3 years.

The concern was not that the duration of the undertaking should be shorter; it was that the Proposed Transaction would create a market structure where oversight could not conceivably be relaxed at some point in the foreseeable future. That is, the undertaking would need to be maintained indefinitely, creating a considerable burden for the Commission and customers and giving rise to substantial monitoring and compliance risks.

The merger parties' proposal to limit the undertaking to a 3 year term is an unusual response to that concern and leaves entirely unaddressed (by the merger parties) what should, could or is likely to occur beyond the end of that 3 year period. A 3 year term is very likely to result in a significantly poorer outcome for customers compared to the previous proposal as it would, in the absence of anything further put forward by the merger parties, mean the monopoly CIT operator created by the Proposed Transaction would be unconstrained by any court-enforceable undertaking from the end of the 3 year period.

If the Commission were ultimately minded to authorise the Proposed Transaction subject to an undertaking, which our client submits it should not do, our client considers that the undertaking must apply indefinitely until withdrawn by the Commission, or at a minimum the undertaking must include a mechanism which allows the Commission to decide to extend, or to require the extension of, the application of the undertaking into further terms.

(b) *There is no mechanism for service improvements or innovation*

The Revised Proposed Undertaking contains no mechanism by which MergeCo is required to *improve* service levels or *innovate*. Instead, it takes an entirely static view of MergeCo's obligations and merely requires MergeCo to offer ongoing supply in accordance with the "Existing Arrangements" with existing customers.

As we outlined in our letter of 31 October 2022, when our client last sought tenders for CIT services, it obtained a significantly better deal than was then-currently the

case, as a result of the competition between the parties to win our client's business. The Revised Proposed Undertaking does not address this concern and the Proposed Transaction will accordingly foreclose the possibility of improved service levels or innovation, which is the expected, natural outworking of the competitive process.

If the Commission were ultimately minded to authorise the Proposed Transaction subject to an undertaking, which our client submits it should not do, our client considers that the undertaking must include a mechanism to require or incentivise MergeCo to improve service levels and innovate.

(c) *The pricing proposal is worse than the previous offer and is unjustified*

The merger parties have proposed a pricing term that would permit MergeCo to increase prices by Inflation + 7.5% annually once our client's existing contract expires.

The merger parties have provided no explanation as to how they arrived at that formulation of a reasonable, justifiable proposed yearly price increase. Our client is concerned that MergeCo's 'baking-in' of a consistent, yearly price rise:

(i) is entirely unjustifiable. This is particularly the case in circumstances where the merger parties have asserted that the Proposed Transaction will allow them to generate significant synergies through the more efficient allocation of resources, thereby reducing costs across their combined network. If that is indeed the case, then it is unclear why the merger parties should be entitled to *increase* prices when they will benefit from a material, enduring reduction in costs;

(ii) will result in price increases greater than would occur in the absence of the Proposed Acquisition once a customer's existing contract ends. In that regard, our client notes that its existing contract with one of the parties, agreed only a few years ago in a competitive setting, permitted an annual price adjustment of no greater than the increase in the Consumer Price Index as published by the Australian Bureau of Statistics; and

(iii) when combined with the absence of any mechanism for service improvements or innovation, will mean that under the Proposed Revised Undertaking customers of MergeCo will not only pay more, but be very likely to pay *more* for *less* than they would be likely to receive in the absence of the Proposed Acquisition where competition will continue and encourage better service levels and innovation (at least for some period).

In addition, our client notes that the merger parties have proposed a pricing mechanism that, while simpler, is *worse* than the First Proposed Undertaking because it is likely to guarantee annual price rises of Inflation + 7.5% rather than the previous proposal which at least *could have* resulted in lower price increases by operation of the revenue and cost models set out therein.

If the Commission were ultimately minded to authorise the Proposed Transaction subject to an undertaking, which our client submits it should not do, our client considers that the pricing mechanism should allow for price rises of no greater than the yearly increase in the Consumer Price Index as published by the Australia Bureau of Statistics and should include incentives for MergeCo to *lower*, rather than *increase*, prices. In that respect, our client notes that the last time it negotiated its contract for CIT services it achieved materially better pricing than it had in its previous contract because of the competitive tension imposed by the other supplier.

(d) *Uncertainty about expanded geographic coverage*

Our client considers that there remains uncertainty as to whether it could obtain expanded geographic coverage for any new sites it might open in the future because MergeCo is only obliged to expand geographic coverage if the location is "reasonably capable" of being serviced. As it is not explained by the merger parties what "reasonably capable" means, the term is ambiguous and it is, in any event, unnecessary. Our client considers that any site in Australia at which a retailer elected to open a store should be "reasonably capable" of being serviced, including because in a competitive market absent extreme or extraordinary circumstances, a provider of CIT services would be incentivised to service that site.

The resolution of any dispute between our client and MergeCo as to whether a new site is reasonably capable of being serviced could take a long time and be costly – and result in a worse outcome for our client than if it had the ability to seek alternative supply from the other party in a competitive market.

If the Commission were ultimately minded to authorise the Proposed Transaction subject to an undertaking, which our client submits it should not do, our client considers that the ambiguous and unnecessary term "reasonably capable" should be omitted from MergeCo's obligation to ensure it provides expanded geographic coverage on request.

(e) *The dispute resolution process is not equivalent to the constraint imposed by competitive pressure*

Even though the merger parties have now included a detailed complaint handling process in the Proposed Revised Undertaking and included a mechanism for an "Independent Expert" to resolve complaints about MergeCo's compliance with certain aspects of the Proposed Revised Undertaking, there is no guarantee that our client's concerns about service levels or MergeCo's conduct could or would be adequately addressed nor that such processes would yield an equivalent or superior outcome to that generated from switching or threatening to switch to an alternative provider in a competitive market.

2.4 Accordingly, our client submits that the Commission should reject the Revised Proposed Undertaking and not authorise the Proposed Transaction.

2.5 If, however, the Commission were minded to accept an undertaking of this kind – and recognising the difficulties with anticipating deficiencies with behavioural undertakings and the strategic behaviour that MergeCo might engage in in the future to circumvent its obligations or the spirit of the undertaking, and the limited time our client has had to review this substantially revised proposal – in addition to requiring the undertaking be amended to address the concerns raised above, the Commission should also require a term be included in the undertaking permitting the Commission to unilaterally impose additional or varied conditions should third parties such as our client identify further inadequacies with the undertaking or MergeCo's behaviour in the future.

3. CONCERNS ABOUT THE PARTIES' CONDUCT TO DATE

3.1 Our client is concerned that the only two national suppliers of CIT services appear to have now spent many months closely examining each other's business and books, and communicating with each other to reach a consensus view on the 'appropriate' or 'sustainable' level of price increases that they believe ought to persist in the market going forward (Inflation + 7.5%). If this has occurred, it has occurred in circumstances where the merger parties no doubt appreciate (and will or ought to have appreciated from the outset

of the process) that there is a substantial risk that the Commission will not authorise the Proposed Transaction and it will not proceed.

3.2 Our client is concerned that any such communications between the merger parties about future price rises – in conjunction with any knowledge gleaned about the other parties' commercial arrangements and costs – could, at a minimum, influence the pricing and other strategic behaviour of the parties if the Proposed Transaction is not authorised and does not proceed. For example, any such communications and knowledge could remove some (or more) of the uncertainty about future pricing conduct or capacity to discount that might have otherwise persisted in the market.

3.3 Without any knowledge of the arrangements that may have been in place between the merger parties to manage such issues, our client is not in a position to and does not impugn the conduct of either merger party. However, our client does submit that the Commission should consider whether close scrutiny of the parties' pricing and other strategic behaviour is warranted in the future should the Commission decline to authorise the Proposed Transaction and it does not proceed.

Please let us know if you would like to discuss any aspect of this letter.

Your sincerely

Ross Zaurrini
Partner

John McKellar
Senior Associate

ashurst