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Simon Pomery
Director, Competition Exemptions
Australian Competition & Consumer Commission
17/2 Lonsdale Street
Melbourne VIC 3000

Miriam Kolacz
Assistant Director, Competition Exemptions
Australian Competition & Consumer Commission
17/2 Lonsdale Street
Melbourne VIC 3000

Dear Mr Pomery, Ms Kolacz,

Proposed merger between Armaguard and Prosegur

Next Payments Pty Ltd (***Next Payments***) welcomes the opportunity to provide a submission in relation to the draft section 87B undertaking and response to the ACCC's Statement of Preliminary Views 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***.

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;
- 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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Supplementary submission by Next Payments – Armaguard and Prosegur merger authorisation application

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1 Summary

If the ACCC authorises the Proposed Merger, including with the proposed undertaking, the merged entity will raise prices, lower service quality, and squeeze out competing ATM deployers.

The Proposed Merger would entrench a market structure with a monopolist CIT services provider that is vertically integrated at every stage of cash delivery – from CIT services, to ATM deployment, to ATM maintenance.

Next Payments competes actively and directly in the independent ATM deployer market. Next Payments currently has [redacted] active ATMs in Australia, including [redacted] ATMs in regional areas (ie, ATMs deployed outside of state and territory capital cities).

In order to maintain its competitive position, Next Payments attempts to maintain the lowest ATM withdrawal fees in order to be a value for money provider.

A major contributor to the ability of Next Payments to compete effectively is access to CIT services supplied by Prosegur. Prosegur offers Next Payments competitive pricing and cash supply terms. Next Payments considers that the competitiveness of Prosegur's terms is a direct result of Prosegur seeking to win volumes and business from Armaguard.

If the Proposed Merger proceeds and the Applicants are not required to divest their ATM networks, it is highly unlikely that the merged entity will offer competitive pricing or cash supply terms to Next Payments or other independent ATM deployers – the Applicants will favour their own ATM businesses.

Without a divestment of the Applicants' ATM networks, Next Payments will be foreclosed as a competitor in ATM deployment services, and this will result in consumers, especially vulnerable segments of the community who rely on cash, having less access to ATMs and paying more for cash. If the merger is approved without the Applicants' divestment of their ATM networks, Next Payments considers it will need to progressively reduce the number of ATMs servicing regional communities and materially increase the cost of providing cash.

Cash is a fundamental part of the economy. It remains an important means of payment and store of wealth for many parts of the Australian community. As a result of the Proposed Merger, consumers, especially vulnerable segments of the community who rely on cash, will have less access to ATMs and will pay more for accessing this essential service. Consumers need competition in ATM deployment to ensure security of supply and affordable prices. The banks are shutting down cash services – with ANZ announcing on 30 March 2023 that customers would not be able to withdraw cash over the counter at some branches.[1] This leaves consumers reliant on independent ATM networks. If the Proposed Merger is authorised that essential service will be left to a vertically integrated monopolist.

To avoid a dire outcome, Next Payments urges the ACCC not to authorise the Proposed Merger.

If the ACCC does however intend to authorise the Proposed Merger, Next Payments urges the ACCC to reject the proposed undertaking. The proposed undertaking will not prevent the merged entity from foreclosing competing ATM deployers, like Next Payments. The only way that this can be avoided is if the Applicants divest their ATM networks. Only a divestment will avoid the creation of a vertically integrated monopolist with the ability and incentive to squeeze out competing ATM deployers who will rely on the monopolist's CIT services.

[1] 'Cashless ANZ move: now Westpac, NAB, CBA reveal plans', *The Australian*, 3 April 2023.

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Next Payments agrees with the concerns raised by the ACCC in its Statement of Preliminary Views. The Applicants' response to that Statement does not address the ACCC's validly held concerns:

- **The counterfactual against which to assess the Proposed Merger is not disorderly exit by one of the Applicants.** Next Payments recognises that the Applicants face challenges in continuing to profitably provide CIT services. However, the Applicants paint a picture of inevitable and imminent disorderly exit which is not consistent with public statements made by Prosegur regarding the state of its business. Further, the Proposed Merger is not the only option to address the challenges faced by the Applicants:
    - The Applicants could raise prices to sustainable levels, without one of them exiting the market. [redacted]
    - The Applicants could rationalise costs or take other steps to improve their businesses. [redacted] For example, Next Payments understands that Prosegur has delayed rebranding the majority of the approximately 750 Westpac ATMs it acquired in 2019 due to (relatively inexpensive) rebranding costs. For those ATMs that remain Westpac-branded, Prosegur is constrained in the revenue it can earn as it cannot implement transaction fees that it would otherwise charge. Prosegur has also implemented a costly cashless card program in Sydney that is incurring losses for Prosegur and is an area Prosegur has limited expertise in developing.
    - The Applicants could take steps that fall short of a full merger that would sustain their CIT businesses without damaging competition. The Applicants have failed to provide compelling evidence that a joint venture, infrastructure sharing arrangements, or other cost-reductions and efficiencies could not be adopted to avoid entrenching a vertically integrated monopoly.

  Next Payments respectfully submits that it is against those counterfactuals that the Proposed Merger should be assessed.

- **The Proposed Merger will result in a substantial lessening of competition and significant public detriments.** The Proposed Merger will create a monopolist that is vertically integrated at every level of the supply chain. Next Payments is not aware of a comparable industry in Australia characterised by such an inherently anti-competitive structure. It is the consumer, and those most vulnerable, who will be the losers – they will lose access to cash and pay more for it.

- **A behavioural undertaking does not address the harm to competition and the public interest.** Behavioural undertakings are fraught. They are not adept at addressing structural competition issues – especially vertical foreclosure risks. They can be gamed and are extremely difficult to monitor and enforce. This merger raises serious competition and public interest concerns. Those concerns cannot be remedied by a behavioural undertaking. The only way to avoid the inevitable vertical foreclosure risks is for the Applicants to divest their

ATM networks. That is the only solution to remove the Applicants' ability and incentive to squeeze out competition in ATM deployment.

- **The Proposed Undertaking is wholly inadequate.** The proposed undertaking will not remedy the competition lost or the public detriments caused by the Proposed Merger.
  - The Applicants have proposed a complex pricing structure which will not protect Next Payments, and other ATM deployers, from being squeezed by the merged entity in favour of the merged entity's ATM network. In particular, the proposed pricing mechanism leaves considerable scope to manipulate the allocation of costs in a way that forecloses competing ATM deployers, and does not conform to more established and transparent 'cost-plus' methods of regulated pricing that specifically link pricing to the costs of the relevant services provided to different customers. The Applicants have also proposed that an independent auditor effectively acts as price regulator for the industry – this is unprecedented.
  - The proposed undertaking sets out three short bullets that are meant to guarantee levels of supply from the merged entity to other ATM deployers (clause 4.36). This is wholly inadequate. The clause reads as if it were an after-thought. The merged entity will not only use price squeezes to foreclose competitors; it will engage in other forms of discriminatory behaviour – 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. As soon as an ATM is down, customers cannot use it and they lose confidence. This will be the death knell for competing ATM deployers. Meanwhile, the merged entity will promote its network as the only reliable one that can guarantee consistent cash supply. The proposed undertaking does not address these risks. Indeed, no behavioural undertaking could ever address these risks satisfactorily – this is why divestment is the only solution.
  - The proposed monitoring regime is wholly inadequate. The proposed undertaking contemplates: (i) a yet to be designed complaints handling process (which is not subject to ACCC approval); and (ii) six monthly reporting to the ACCC. By the time any non-compliance is detected, the harm will already have been done to competing ATM deployers.

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

Next Payments recognises that the Applicants face challenges in continuing to profitably provide CIT services. However, the Applicants paint a picture of inevitable and near-term disorderly exit which is not consistent with public statements made by Prosegur regarding the state of its business.

Further, the Proposed Merger is not the only option to address the challenges faced by the Applicants:

- The Applicants could raise prices to sustainable levels, without one of them exiting the market.
- The Applicants could rationalise costs within their business.
- The Applicants could take steps that fall short of a full merger that would sustain their CIT businesses without damaging competition.

2.1 Prosegur's statements to the market do not suggest it is on the brink of exit

The Applicants rely heavily on the argument that near-term and disorderly exit by one of them is inevitable. This is not consistent with what Prosegur has told the market in recent statements.

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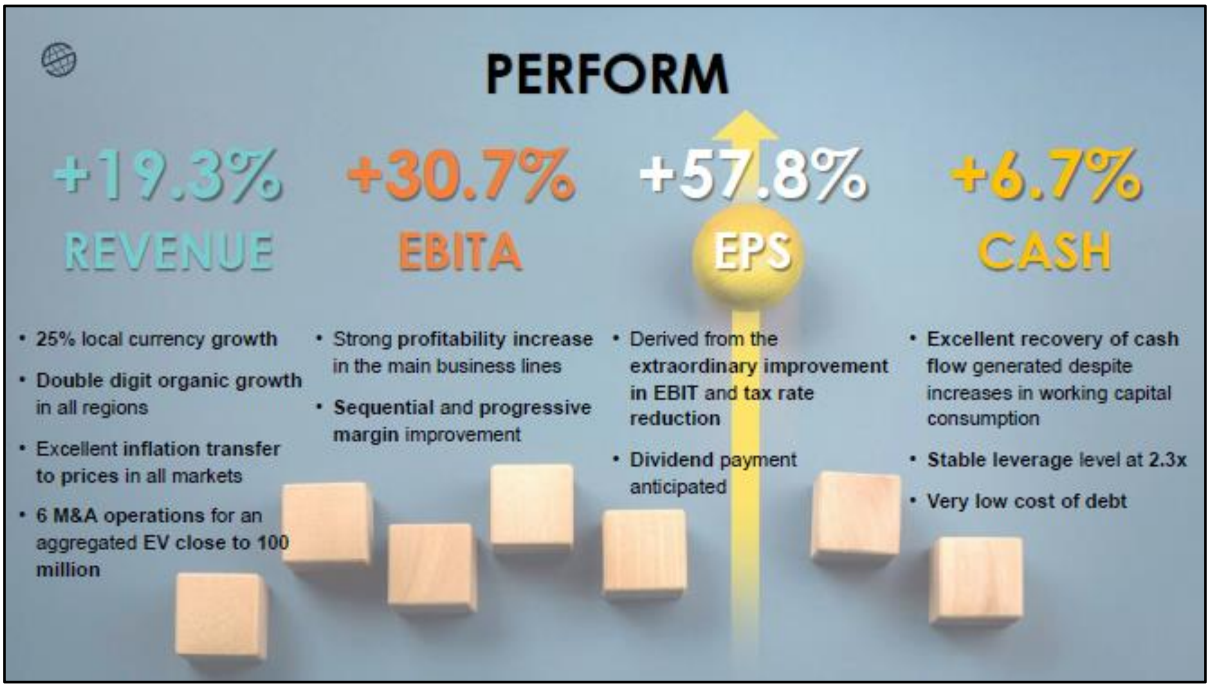
(a) Prosegur claims to be growing

Prosegur has indicated that it has experienced recent growth and profitability in relation to FY22 performance across its CIT business.

In its most recent financial results, Prosegur's global management states that Prosegur has experienced '*double digit growth **across all regions**, with strong volume recovery*' (with overall revenue growth of 19.3% for the financial year).[2] The extract from Prosegur's FY22 Results Presentation in Figure 1 illustrates this.

Figure 1 – Extract from Prosegur's FY22 Results Presentation, p 3.[3]



(b) Any recent underperformance is influenced by the COVID pandemic

Prosegur has projected growth following the COVID-19 pandemic. On 28 February 2022, Prosegur's CEO, José Antonio Lasanta Luri, stated that:

> *regarding the operation of Australia, mainly of APAC, but mainly Australia, I have to say that this is going to be the first quarter in which we are going to be without any restrictions in Australia with any pandemia. Hopefully this year, we're going to see all the results of all the measures that we have been taking in the last two years.*[4]

This is supported by Prosegur's global FY22 Results Presentation which indicates substantial improvement of Prosegur's financial performance for FY22 when compared to FY20 and FY21, as extracted in Figure 2 below.

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[2] Prosegur, media release, 23 February 2023. https://www.prosegur.com/en/media/article/press/prosegur-profitability-up-57-with-consolidated-net-profit-of-65-million.

[3] Prosegur, Results Presentation FY 2022, 28 February 2023, p3. https://www.prosegur.com/dam//Prosegur/CORP/pdf/accionistas_inversores/informes-trimestrales-ing/2022/230228---Prosegur-FY-2022-Results--1-.pdf

[4] Prosegur, Q4 2021 Earnings call, 28 February 2022.

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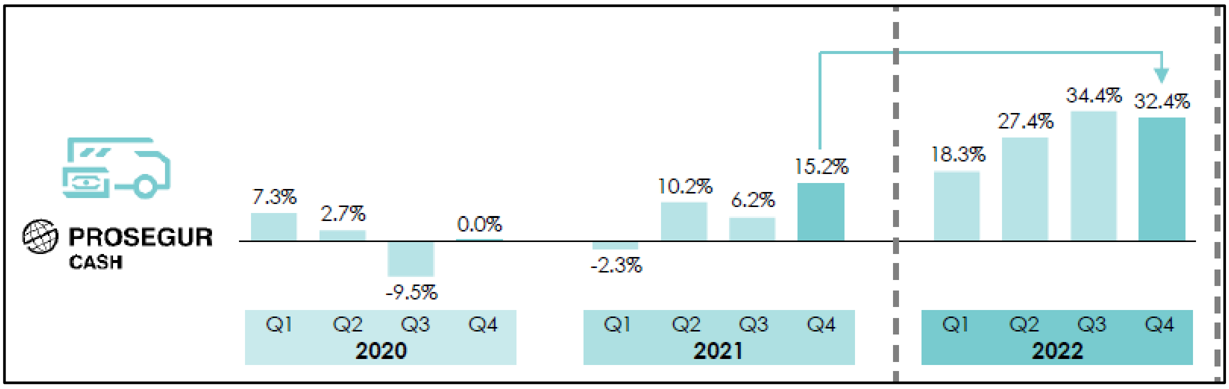
Figure 2 – Extract from Prosegur's FY22 Results Presentation[5]



(c) Prosegur's Australian CIT business operations are improving

Prosegur's CEO has also indicated that Prosegur's Australian CIT services business performance is improving:

> ***I think we are improving our numbers or our operation in Australia****. But for us, our main plan is to go for this merger with our competitor. And we are in the process that we cannot comment much on it, but we foresee that it's going to be – we are going to have a final resolution before first half of this year, hopefully, will be at the beginning of the second quarter.*
>
> *And yes,* ***the business in Australia I think is improving because of [transcript unclear] bonus and because of all the actions we have taken****. But we keep our strategy of the merger because we believe this is the best outcome for the future.*[6]

In recent public announcements Prosegur has not indicated an ongoing decline in its Australian CIT services business or a significant deterioration in market conditions:

> *In terms of percentages over total sales, these were 21.4% a year ago and have increased by 200 basis points in a year to 23.4%...* ***As it was the case with overall local sales, all regions have contributed to this increasing penetration****. Only Europe has not because of the mentioned divestments.*[7]

Prosegur's statements are inconsistent with the Applicants' submission that it is facing significant decline and ongoing losses in its Australian CIT business that are likely to lead to disorderly exit in the near-term. Rather, Prosegur's public statements and recent financial reports indicate that its Australian CIT business is recovering following a period of underperformance during the COVID pandemic, and it is experiencing improved growth and a return to profitability.

2.2 The Proposed Merger is not the only option to address the challenges faced by the Applicants

There are alternative steps that the Applicants could take, short of a merger, to address the challenges they face.

(a) The Applicants could increase prices

[redacted]

[5] Prosegur, Results Presentation FY 2022, 28 February 2023, p6.
[6] Prosegur, Q4 2022 Earnings call, 28 February 2023.
[7] Prosegur, Q2 2022 Earnings call, 29 July 2022.

- [redacted]
- [redacted]
- [redacted]

[redacted]

(b) The Applicants could rationalise costs within their business

[redacted] For example, Next Payments has observed delays in Prosegur's re-branding of Westpac ATMs it acquired in 2019, which prevents Prosegur from receiving revenue from non-Westpac cardholders at those ATMs (due to legacy arrangements with these ATMs, Prosegur is only reimbursed by Westpac for Westpac customer transactions, and is constrained from charging non-Westpac cardholders transaction fees). Prosegur has also not rationalised other parts of its business that experience losses – for example, cashless card projects at Royal Sydney Show and Taronga Zoo that Next Payments understands are costly for Prosegur.

To date, Next Payments has not been invited to any constructive discussions with Prosegur as to how Prosegur can reduce costs, or structure its services to Next Payments in a more efficient and sustainable way. For example by:

- rationalising cash replenishment delivery runs for ATMs;
- sub-contracting with a smaller CIT service provider such as Authentic Security in certain areas; or
- working with Next Payments to switch some of the most difficult to reach merchants in regional or rural areas to self-cash their ATMs (ie, Prosegur would continue to provide a range of CIT services to the merchants' ATMs, including maintenance, but the customer would source the cash for their ATM directly from a bank or from other merchants), therefore becoming less reliant on frequent cash delivery.

(c) The Applicants could take steps that fall short of a full merger that would sustain their CIT businesses without damaging competition

There are other structures that could address the Applicants' challenges without result in damaging competition and harming the public interest.

Next Payments considers, as per its initial submission, that this could be achieved through a joint venture or infrastructure sharing arrangements between the Applicants. This would achieve the purpose of increasing efficiency and ensuring a sustainable upstream CIT services supply chain, while preserving competition in price and service delivery to CIT services customers.

A joint venture to share CIT services infrastructure could include the following characteristics to increase efficiency and preserve competition:

- **Shared core CIT infrastructure,** (eg, cash depots and armoured trucks) in the areas where the Applicants experience significant duplication of operations. This would reduce costs and increase efficiency, and is a key rationale for the Proposed Merger submitted by the Applicants. A joint venture at this level would provide access to cash infrastructure and CIT services to the merged entity's own business on the same terms as it would to competing smaller CIT services providers that need access to this cash infrastructure and also to downstream ATM deployers that compete with the merged entity's ATM network.
- **Separate downstream service delivery operations,** so Armaguard and Prosegur continue to vigorously compete for end customers on price and service quality.
- **No merger of ATM businesses,** so as to preserve competition between Armaguard's and Prosegur's ATM networks.

This alternative could be accompanied by a commitment (in the form of an enforceable undertaking to the ACCC) that provides fair and reasonable access and pricing to Armaguard's and Prosegur's shared core CIT infrastructure for smaller CIT services providers that compete with the Applicants.

3 The Proposed Merger will result in a substantial lessening of competition and lead to significant public detriments

The Proposed Merger will create a vertically integrated monopolist free from competitive constraint with the ability and incentive to stamp out competition from ATM deployers.

(a) Creation of a monopolist CIT services provider

The Proposed Merger is a merger to monopoly. It will combine the two largest suppliers of CIT services in Australia with a market share above 90%, and the only suppliers able to support large customers such as banks, ATM networks, and major retailers.

The merged entity will not be constrained by smaller CIT services providers. Such providers do not compete effectively with the Applicants as they do not have the economies of scale, distribution network, or the range of services (including specialised security services) that the Applicants provide.

There is no credible threat of new entry or expansion in CIT services markets post-transaction. There are high barriers to entry to CIT services markets, including significant upfront costs and resources in establishing a network with sufficient scale and range of services to compete with the merged entity. This is extremely unlikely to occur in circumstances where the merged entity will have a 90% market share, which will deter any potential new provider from making the required investment.

As cash is a commoditised product that remains unchanged throughout the value chain to end usage by consumers, a monopoly provider of CIT services (who essentially controls cash once it is distributed from RBA distribution sites) will be able to control all aspects of the cash supply chain in Australia. There is no scope for competing CIT services providers, who rely on access to cash infrastructure, or for downstream providers (eg,

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ATM deployers), once access to cash is restricted, to modify their products and services in response, and they will be forced to reduce their service quality, or raise prices, or both.

(b) Entrenching a vertically integrated monopolist

Equally as concerning as the creation of a monopolist at the CIT level is the fact that that monopolist is vertically integrated at every stage of cash delivery – from CIT services, to ATM deployment, to ATM maintenance and related services.

That monopolist will have the ability and the incentive to extinguish competition from independent ATM deployers. The result will be more ATM closures and higher prices for consumers accessing cash. This will have a direct effect on many Australians who continue to use cash for their transactions daily – particularly in a context where banks are already withdrawing from providing cash services (as demonstrated by ANZ's recent decision to cease providing cash withdrawals over the counter at some branches).

Independent ATM deployers who rely on CIT services from the Applicants will have no choice but to deal with the merged entity. The merged entity will have both the ability and incentive to engage in a range of vertical foreclosure strategies to squeeze out independent ATM deployers that compete with Armaguard's and Prosegur's ATM networks.

This will be achieved through price squeezes – the monopolist charging higher prices to independent ATM deployers than it would to its own network. More importantly, the monopolist will engage in other forms of discrimination that will undermine the reliability of independent ATM deployers' networks. For example, the monopolist would:

- withhold or reduce CIT services provision, for example, by reducing the frequency of ATM provisioning and / or cancelling cash delivery routes;
- reduce the quality of CIT services, for example:
  - reducing security quality;
  - slowing ATM provisioning and maintenance;
  - reducing maintenance quality;
  - providing banknotes that do not meet quality standards for use in ATMs, thereby causing ATM jams; and
  - providing fewer out of hours services;
- withhold innovation and service improvements from competitors; and
- leverage its upstream CIT business to create an unlevel playing field in downstream ATM deployment services. The merged entity will have unrivalled competitive advantage by having guaranteed access to reliable CIT services.

The merged entity will have a strong incentive to target Next Payments' or other independent ATM deployer's sites through the above means. The merged entity would gain substantially more profit from ATM sites that are diverted from competing ATM deployers than the revenue it would lose from supplying CIT services to those competing ATM networks.

Furthermore, as soon as an ATM is down, customers lose confidence. Merchants (eg, site owners or operators and shopping centre landlords who want ATMs deployed to their sites) will also quickly lose confidence in ATM deployers whose ATMs are down. This loss of confidence will be the death knell for competing ATM deployers. Meanwhile, the merged entity will promote its network as reliable and the only one that can guarantee consistent cash supply. In Next Payments' experience, merchants are very sensitive to the issue of ATM reliability and will readily switch ATM deployers following the suggestion that only the merged entity's ATMs will be reliable.

Removing competition at the ATM level will mean vulnerable consumers will have less access to cash and will pay more for that access.

Increases in CIT costs and reduced access to wholesale cash will substantially impact independent ATM deployers' ability to deploy ATMs in less profitable locations, particularly in regional and remote communities where the cost of provisioning ATMs is highest and transaction volumes are generally lower.

(c) Specific claims by the Applicants

The Applicants make a number of claims without properly addressing the vertical foreclosure risk.

Applicants' submissions	Next Payments' comments

The Applicants claim that post-merger there is a credible threat of new entry or expansion in CIT services, including through sponsorship by banks.	• This claim is not accurate and cuts across the very rationale for the Proposed Merger. The Applicants say the market cannot sustain two CIT services providers but also claim there will be a credible threat of new entry.
	• There are significant barriers to new CIT services providers entering, or existing smaller providers expanding, to compete with the merged entity, requiring:
	  • sufficient scale to offset the high fixed costs associated with maintaining a CIT network, and to ensure high levels of security and reliability (eg, a national network of cash depots, armoured trucks, and specialised and armed security guards);
	  • access to capital to fund sufficient banknotes to operate a CIT business on a profitable scale;
	  • significant investment in quality sorting and handling equipment and expertise;
	  • expertise in the operational and accounting aspects of managing a large-scale CIT services business;
	  • significant time and resources in obtaining Approved Cash Centre Operator accreditation; and
	  • strict security and insurance requirements required to deliver cash on a wholesale basis.
	• To date, no alternative provider has been successful in overcoming the above barriers to effectively compete with the Applicants.

The Applicants claim that customers could insource CIT services or use smaller 'soft skin' competitors.	• Insourcing CIT services is not an option, as it would require significant capital investment to develop a national CIT services network with the requisite breadth and depth of coverage, equipment, and specialised skills. In addition, Next Payments would lack the demand to justify insourcing CIT services at an efficient scale and scope. Insourcing would accordingly cost significantly more than what Next

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	Payments currently pays for CIT services, and a monopolist supplier of CIT services could set its prices up to that level.
	• Smaller 'soft skin' competitors are not a viable alternative because they:
	  • are more expensive than the Applicants, as they lack economies of scale;
	  • do not have the national distribution network required to supply CIT services across an ATM network with nationwide or significant geographic coverage;
	  • cannot provide the level of security required for cash delivery to ATM deployers; and
	  • [redacted]
	• As a result, independent ATM deployers and other large customers of CIT services have no choice but to use the Applicants for CIT services.

The Applicants claim that any attempt to increase prices or reduce service levels to CIT services customers will result in an accelerated decline in the usage of cash by end-consumers.	• Cash remains an essential method of payment for parts of the Australian community. This is particularly true of older or more vulnerable members of the Australian community, persons with lower household income, limited access to internet or digital forms of payment, or in regional or remote areas, who continue to rely on cash. These consumers will continue to rely on cash even if the Applicants charge higher prices or reduce service quality to CIT customers and such costs are passed on to end customers.
The Applicants claim that they would be constrained from increasing prices or reducing service levels by the theoretical threat of the RBA intervening.	• The theoretical threat of regulatory intervention is not a sufficient constraint on anti-competitive conduct post-transaction. • Anti-competitive conduct can take subtle and covert forms, including discrimination in service quality and frequency, imposing more onerous contractual terms, pricing, and foreclosure or delays in access to essential CIT services. It is too difficult for any regulatory agency to effectively identify and enforce against all such conduct on an ongoing basis. • Even if a regulatory agency could identify some anti-competitive conduct, there would inevitably be significant delays in enforcement and further regulatory action. There would be even more significant delays and issues in introducing corrective regulations to undo harms after they have occurred.
The Applicants claim it would be irrational for the merged entity to discriminate by vertically foreclosing ATM competitors.	• The merged entity will have the ability to vertically foreclose independent ATM deployers as, post-merger, ATM deployers will have no alternative but to rely on the merged entity for crucial CIT services to operate their respective ATM networks.

	• The merged entity would also have significant incentives to engage in vertical foreclosure, in areas such as shopping centres and high street locations where the merged entity competes most closely with Next Payments and other independent ATM deployers. The merged entity would earn profits on any ATM sites diverted from Next Payments that would exceed any loss in revenue from supplying the relevant Next Payments' (or other independent ATM deployer's) sites. • The result would be an entrenchment of market power for the merged entity in ATM deployment in addition to CIT services supply.
The Applicants claim that the Proposed Merger would create resilience and certainty in the cash supply chain.	• A merger to monopoly would reduce resilience in the cash supply chain. The cash supply chain would be dependent on one supplier which increases the risks associated with that supplier experiencing business failure or service interruptions.
The Applicants claim that the Proposed Merger would Preserve the complimentary expertise of each Applicant, including Prosegur's global knowledge and experience in innovation, such as smart safes, together with Armaguard's deep understanding of local conditions and logistics expertise.	• Armaguard's and Prosegur's distinct expertise, knowledge, experience, and innovation currently spurs the Applicants to vigorously compete with each other. This competitive tension will be lost with the Proposed Merger.

4 A behavioural undertaking does not address the harm to competition and the public interest

Behavioural undertakings are fraught. They are not adept at addressing structural competition issues – especially vertical foreclosure risks. A behavioural undertaking cannot remedy the serious competition concerns and public detriments that the Proposed Merger will create.

A structural solution is required. That is, either the Proposed Merger does not proceed, or the Applicants divest their ATM businesses – this is the only way to ensure competitive ATM deployment.

Behavioural undertakings such as the one proposed by the Applicants are generally ineffective in addressing competition concerns of a merger. The ACCC has noted that (emphasis added):

> *The ACCC has a strong preference for structural undertakings — that is, undertakings to divest part of the merged firm to address competition concerns.* ***Structural undertakings provide an enduring remedy with relatively low monitoring and compliance costs****.*
>
> ***On occasion****, behavioural undertakings — that is, undertakings by the merged firm to do, or not do, certain acts (for example, meet specified service levels) —* ***may be appropriate as an adjunct to a structural remedy****.* ***Behavioural remedies are rarely appropriate on their own to address competition concerns****.*[8]

Next Payments also notes the ACCC's joint statement with the UK Competition and Markets Authority and the German Bundeskartellamt, that (emphasis added):

> *The increasing complexity of dynamic markets and the need to undertake forward-looking assessments require competition agencies to favour structural over behavioural remedies.* ***It is***

[8] ACCC, Merger Guidelines (2017), page 59.

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> ***widely acknowledged that complex behavioural remedies that create continuing economic links and dependencies are unlikely to recreate the pre-merger competitive intensity of the market, can raise significant circumvention risks, and can quickly become outdated as market conditions change****. In some circumstances they can also distort the natural development of the market.* ***Behavioural remedies also place a burden on competition agencies and businesses by necessitating extensive post-merger monitoring of companies and their conduct****.*[9]

Those concerns hold true in this case, especially as the merged entity could easily circumvent behavioural obligations and engage in a range of subtle discriminatory tactics.

As noted in the ACCC's review of the *Pacific National and Linfox / Aurizon* transaction, which also involved significant vertical issues, '[a]*n owner or operator has so many subtle ways of discriminating against, or damaging* [a competitor]'.[10]

In line with the ACCC's guidance, the only way the Proposed Merger could proceed without extinguishing competition at the ATM level would be for the Applicants to divest their ATM businesses. A structural divestment remedy would:

- Remove the merged entity's ability and incentive to foreclose competitors.
- Avoid the creation of an anti-competitive market structure.
- Remove the need for the ACCC to monitor and enforce behavioural commitments.
- Increase competition in ATM markets. A divestiture undertaking may facilitate increased competition in downstream ATM deployment services through the entry or expansion of another participant in these markets, and preserve choice for merchants and consumers.

A behavioural undertaking could be implemented to temper the creation of a monopolist of CIT services but only as an adjunct to divestment of the Applicants' ATM networks.

5 The proposed undertaking is wholly inadequate

The proposed undertaking will not remedy the competition lost or the public detriments caused by the Proposed Merger:

- **The pricing mechanism will not prevent the merged entity squeezing competing ATM deployers.** The pricing mechanism is very complex and lacks transparency, with poorly defined variables. It relies on a form of revenue cap that purports to address the horizontal competition concerns in relation to the supply of CIT services, without directly regulating the prices that the merged entity would charge. This complexity together with the scope the merged entity has to determine prices within the revenue cap increases the risk that the merged entity could 'game' the pricing mechanism or exploit loopholes to increase its prices for CIT services over the long term. Customers of CIT services face an information asymmetry in how the price would be calculated and face the burden of raising the issue through the merged entity's complaint handling process, with no access to independent oversight or dispute resolution. In order to address the vertical concerns, the Applicants propose attributing a share of the overall revenue cap to the merged entity's own ATM deployment business. There are more established and transparent methods of regulating pricing to prevent margin squeeze. For example, a 'cost-plus' method that links prices to ATM deployers to the costs of the services provided to those customers and which is separate to the costs of providing

[9] CMA, ACCC, Bundeskartellamt, Joint statement on merger control enforcement (20 April 2021), page 4.
[10] Court dismisses ACCC proceedings opposing rail freight consolidation (ACCC media release, 15 May 2019).

other CIT services. The revenue attribution approach in the proposed undertaking leaves considerable scope for the merged entity to manipulate that allocation of costs in a way that may foreclose competing ATM deployers.

- **Inadequate safeguards to prevent discriminatory conduct, particularly qualitative discrimination.** The proposed undertaking lacks measures to prevent discriminatory conduct and ensure continuity of service quality in the supply of CIT services, particularly to independent ATM deployers. Most concerningly, the proposed undertaking does not mitigate the risk that the merged entity could withhold, reduce, or delay CIT services that independent ATM deployers rely on, eg, cash replenishment and secure cash transport, first line maintenance, and escorting by security guards for second line maintenance. Independent ATM deployers rely on these critical service inputs to provide reliably functioning ATMs. Contrary to the Applicants' claim (at paragraph 113 of their Response to the ACCC's Statement of Preliminary Views) the proposed undertaking does not require the merged entity to deal with independent ATM deployers on a non-discriminatory basis. It also does not include any measures to keep the upstream CIT services business of the merged entity separate from its downstream ATM business (including through separate management teams, and ring-fencing measures) to further mitigate discriminatory conduct.
- **Lack of safeguards to ensure fair access to crucial inputs.** The proposed undertaking lacks mechanisms to ensure fair and equitable access to critical CIT infrastructure for third party CIT services providers – other than a vaguely described promise to supply on 'reasonable commercial terms'. This is insufficient to ensure access on fair and reasonable terms, and provides no obligation to negotiate in good faith, so as to mitigate the risk of foreclosure of smaller CIT services providers. In the event of an access dispute, smaller CIT services providers will not have access to any independent dispute resolution measures and are in the hands of a complaints handling process controlled by the merged entity.
- **Significant monitoring and enforcement risk.** The complexity of the pricing mechanism and lack of objective and measurable standard of service obligations would make it difficult for customers, the independent auditor, and the ACCC to identify and enforce non-compliance with the proposed undertaking. Although remedies are available for breaches of the proposed undertaking, enforcement will be time consuming, resource intensive and given their retrospective nature will not proactively prevent discriminatory conduct from occurring.

Proposed measures	Deficiencies in the proposed undertaking
Price of CIT services [Cl 4.1 to 4.31]: The undertaking proposes to regulate the price of CIT services through a complex formula.	• **Pricing mechanism is complex, providing opportunities for misconduct:** The pricing mechanism is very complex with a number of variables that are not clearly defined. This increases the risks that the merged entity will seek to use loopholes in the pricing mechanism to engineer anti-competitive pricing outcomes (eg, by artificially inflating variables). The pricing mechanism that is proposed purports to address vertical foreclosure in a way that is open to manipulation rather than adopting a more conventional and transparent cost-plus method of setting prices. • **Information asymmetry:** There are no mechanisms to correct the inherent information asymmetry in pricing CIT services. The merged entity will have wide-ranging discretion in the price-setting process. There are no mechanisms to ensure customers are provided information regarding the price setting process so as to verify compliance and to inform equitable and good faith negotiations.

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Independent audit of pricing is inadequate: The proposed independent audit is ill-equipped to identify and prevent non-compliance as: (i) an independent auditor will not have the resources and expertise to monitor complex pricing issues, which is conventionally the task of a regulatory agency such as the ACCC or RBA; and (ii) even if the independent auditor were to identify non-compliance, it will not prevent customer detriment given the retrospective nature of identifying, reporting, and then taking enforcement action against non-compliance.

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<td>Service offering [Cl 4.32, 4.33, 4.35 and 4.36]: The undertaking proposes that MergeCo will continue to supply 'CIT services' to customers in accordance with existing standards of service and that MergeCo will continue to offer 'ATM specific services' to independent ATM deployers.</td>
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Scope of service offering commitments is ill-defined and too narrow: Neither 'CIT services' nor 'ATM specific services' adequately cover the range of CIT services that Next Payments and other independent ATM deployers rely on as critical inputs to continue operating ATM networks, and that cannot be provided by an alternative provider or in-sourced by Next Payments (these are set out more fully in Next Payments' initial submission), such as:

Secure transport of cash to and from ATMs, in addition to cash replenishment;
First line maintenance to fix minor operational faults, eg, cash / card reader jams;
Escorting by security guards to ensure Next Payments' technicians can securely conduct second line maintenance; and
Installation and maintenance of remote locking mechanisms.

Lack of robust standard of service obligations: The proposed undertaking does not include service quality commitments that would mitigate the significant risk of a reduction in the frequency and quality of CIT services to independent ATM deployers / other customers. The proposed commitments to maintain services in accordance with existing service standards to customers is vague and unenforceable, given service standards may vary significantly between customers and there is no readily observable benchmark.
Risk of subtle discrimination is high: There are no non-discrimination obligations to mitigate the risk of discrimination between customers, particularly vertical foreclosure against independent ATM deployers that compete with the Applicants' ATM networks. The proposed undertaking does not address risks of subtle and covert forms of discrimination such as:

Imposing onerous contractual terms for CIT / ATM services on competing ATM deployers;
Favouring the merged entity's own ATM business with faster / more frequent / higher quality cash replenishment, first line maintenance, and other crucial services. This would provide a subtle but significant competitive advantage of vertical integration that other ATM deployers could not compete with; and
Withholding, delaying or reducing the crucial services to independent ATM deployers, eg, reduced or delayed cash replenishment, reduced security levels, fewer out of hours services, providing banknotes that cause ATM jams, or failing to restore services in a timely manner following service interruptions.

Risk of exploiting transaction or other commercially sensitive data: The proposed undertaking does not include any ring-fencing or other keep separate measures to mitigate the risk of commercially sensitive information obtained through CIT services delivery (ie, from independent ATM deployers) being used to advantage the merged entity's own ATM business. Undertakings accepted by the ACCC to address vertical foreclosure and discriminatory practices have included robust confidentiality and ring-fencing measures, including ring-fencing of employees. There is a significant risk that the merged entity's CIT business exploits confidential data obtained from independent ATM deployers (eg, through cash replenishment and reconciliation of ATMs) to advantage its own downstream ATM networks.

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National coverage [Cl 4.34]: The undertaking proposes that MergeCo will offer CIT services on a national basis.	• **Scope of national coverage commitment is too narrow:** There is no national coverage commitment for ATM services to independent ATM deployers.
Third party access to cash centres [Cl 4.37 to 4.40]: The undertaking proposes that MergeCo will supply cash processing and related services to third party CIT providers at its Access to Cash Centres across Australia.	• **Smaller CIT providers not a strong constraint:** It is unclear whether the commitments will enable third party CIT providers to effectively compete with the merged entity, as: ◦ The price, or pricing methodology, at which third party CIT providers will be charged for access is undefined; ◦ There are no non-discrimination obligations with respect to the terms of access to third party CIT providers; and ◦ Third party CIT services providers that rely on access will be forced to negotiate with the monopolist merged entity with no defined, independent dispute resolution or oversight mechanism to prevent the merged entity from withholding or delaying access to CIT infrastructure, or only providing access on unfavourable terms. • **Lack of robust standard of service obligations:** Beyond supplying third party cash services on 'reasonable commercial terms and conditions', the commitments do not include any standard of service obligations to ensure fair and equitable access.
Complaint handling process [Cl 4.41 to 4.43]: The undertaking proposes that MergeCo will have a complaint handling process.	• **Process is undefined and inadequate:** The commitments do not set out in any detail the proposed complaint handling process. In particular, the commitments do not outline any processes for independent dispute resolution or include any commitments to investigate and respond to complaints within a reasonable timeframe. • **Does not require ACCC approval:** The complaint handling process is left entirely to the merger parties to design and is not subject to ACCC approval. Customers have no assurance that the complaint handling process that is designed by the merger parties will be adequate or effective. • **Unlikely to prevent discriminatory conduct:** Even if the merged entity investigates and responds to complaints, or complaints are escalated to the ACCC through the independent audit process, this is likely to be too slow to prevent discriminatory conduct from occurring.
Compliance auditing and monitoring [Cl 4.44 to 4.60]: The undertaking proposes an independent audit process and self-reporting obligations to the ACCC.	• **Difficult to monitor compliance:** The commitments are unlikely to enable the independent auditor and ACCC to effectively monitor the merged entity's compliance. The complexity of the pricing mechanism, the nature of CIT services markets, and vague obligations to provide services at existing levels, are difficult to audit effectively. The auditor will also be reliant on information and cooperation from the merged entity. • **Significant burden on auditor and ACCC:** The long-term nature and complexity of the undertaking places a considerable burden on the independent auditor and ACCC to monitor and address non-compliance. It will be too difficult for the independent auditor or the ACCC to identify the myriad of subtle discrimination methods that are likely to occur. • **Reporting and audits are too infrequent:** Six-monthly reporting to the ACCC and 12-monthly audits are too infrequent and would not effectively mitigate the risk of harm occurring and then subsequent delays in identifying, reporting, and then enforcing against non-compliance. • **High burden of enforcement:** Whilst court action can deter breach of a section 87B undertaking, it is time consuming and uses significant public resources.