

Statement of Preliminary Issues

Osmosis Buyer Limited / Firewall Holdings S.À R.L.

29 March 2022

Introduction

1. On 1 March 2022, the Commerce Commission registered an application (the Application) from Osmosis Buyer Limited (Osmosis, or the Applicant) seeking clearance to acquire all of the shares in Firewall Holdings S.À R.L. (Firewall) as part of a global transaction (the Proposed Acquisition).¹
2. Osmosis owns Zenith Heaters Limited, which trades as Zenith Water (Zenith). Firewall owns Waterlogic New Zealand Limited, which trades as Merquip. Zenith and Merquip compete in New Zealand in the supply and servicing of certain drinking water solutions – principally multi-function taps (MFTs). A multi-function tap is a tap which purifies or filters water and also heats, cools, boils or carbonates it.²
3. As part of the Application, Osmosis has offered an undertaking (Proposed Divestment Undertaking) to divest the entire Merquip business (Proposed Remedy).
4. The Commission will give clearance if it is satisfied that the Proposed Acquisition will not have, or would not be likely to have, the effect of substantially lessening competition in a market in New Zealand. In doing so, we will consider whether the Proposed Divestment Undertaking will be effective in addressing any competition concerns.
5. This statement of preliminary issues sets out the issues we currently consider to be important in deciding whether or not to grant clearance.³
6. We invite interested parties to provide comments on the likely competitive effects of the Proposed Acquisition and the effectiveness of the Proposed Divestment Undertaking in addressing those likely effects. We request that parties who wish to make a submission do so by **12 April 2022**.
7. If you would like to make a submission but face difficulties in doing so within the timeframe, please ensure that you register your interest with the Commission at

¹ A public version of the Application is available on our website at: <http://www.comcom.govt.nz/business-competition/mergers-and-acquisitions/clearances/clearances-register/>.

² Examples of multi-function taps, along with the other products supplied by Zenith and Merquip, can be found at **attachment A**.

³ The issues set out in this statement are based on the information available when it was published and may change as our investigation progresses. The issues in this statement are not binding on us.

registrar@comcom.govt.nz so that we can work with you to accommodate your needs where possible.

The parties

8. Osmosis is a portfolio company of BDT Capital Partners, LLC. It controls entities that operate the Culligan group, an international provider of water treatment solutions. In relation to New Zealand, Culligan controls Zip Industries, whose principal business is Zenith Water.
9. Zenith Water supplies and services MFTs that dispense instant filtered, boiled, chilled and sparkling water from a single outlet.
10. Firewall is a portfolio company of Castik Capital Partners GmbH. It is the majority shareholder in Waterlogic Group Holdings Limited, which owns Billi Australia Pty Limited, an Australian-based business that makes, sells, and supplies Billi-branded multi-function taps. In October 2021, Firewall indirectly acquired the business and assets of Merquip Limited through a newly incorporated entity called Waterlogic New Zealand Limited (Merquip), which itself became part of the broader Waterlogic group of companies.
11. Merquip is a New Zealand distributor and service provider of water solution products for use in homes, commercial settings, offices and hospitality throughout New Zealand. Merquip distributes drinking water products through third-party retailers,⁴ as well as to commercial customers and tradespeople that purchase on behalf of residential or commercial end-users.⁵

Our framework

12. Our approach to analysing the competition effects of the Proposed Acquisition is based on the principles set out in our Mergers and Acquisitions Guidelines.⁶ As required by the Commerce Act 1986, we assess mergers and acquisitions using the substantial lessening of competition test.
13. We determine whether an acquisition is likely to substantially lessen competition in a market by comparing the likely state of competition if the acquisition proceeds (the scenario with the acquisition, often referred to as the factual), with the likely state of competition if the acquisition does not proceed (the scenario without the acquisition, often referred to as the counterfactual).⁷ This allows us to assess the degree by which the Proposed Acquisition might lessen competition.

⁴ Such as Kitchen Things, Kitchen Studio, Reece, Chesters, Mico Plumbing, Plumbing World, Franklin, Southern Hospitality and Oakleys.

⁵ The Application at [3.9(b)].

⁶ Commerce Commission, *Mergers and Acquisitions Guidelines*, July 2019. Available on our website at www.comcom.govt.nz.

⁷ *Commerce Commission v Woolworths Limited* (2008) 12 TCLR 194 (CA) at [63].

14. If the lessening of competition as a result of the Proposed Acquisition is likely to be substantial, we will not give clearance. When making that assessment, we consider, among other matters:
- 14.1 constraint from existing competitors – the extent to which current competitors compete and the degree to which they would expand their sales if prices increased;
 - 14.2 constraint from potential new entry – the extent to which new competitors would enter the market and compete if prices increased; and
 - 14.3 the countervailing market power of buyers – the potential constraint on a business from the purchaser’s ability to exert substantial influence on negotiations.

Market definition

15. We define markets in the way that we consider best isolates the key competition issues that arise from the Proposed Acquisition. In many cases this may not require us to precisely define the boundaries of a market. A relevant market is ultimately determined, in the words of the Commerce Act, as a matter of fact and commercial common sense.⁸
16. Osmosis has submitted that there is a single drinking water market, which includes not only MFTs, bottle-free coolers (BFCs), bottled water coolers (BWCs), fountains, and wall-mounted boilers, but also in-fridge filtration, bottled water, vending machines, and SodaStream-type water carbonation solutions.⁹
17. Ultimately, however, Osmosis submits that it is not necessary for the Commission to reach a concluded view on market definition given that the Proposed Acquisition will not result in a substantial lessening of competition in any market in New Zealand, because:¹⁰
- 17.1 Zenith and Merquip are not close competitors for the supply and servicing of any other products, and their sales in New Zealand of other products are minimal; and
 - 17.2 the divestment of Merquip will remove the only substantive area of overlap between Osmosis and Firewall in New Zealand (namely, the supply and servicing of MFTs).
18. We will test Osmosis’ submissions on market definition and also assess whether there are any other relevant markets affected by the Proposed Acquisition.

⁸ Section 3(1A). See also *Brambles v Commerce Commission* (2003) 10 TCLR 868 at [81].

⁹ The Application at [9.1].

¹⁰ The Application at [9.10].

Without the acquisition

19. We will consider what the parties would do if the Proposed Acquisition did not go ahead. Osmosis claims that, if the Proposed Acquisition does not proceed, its business plan for New Zealand would not change. On that basis, it says the counterfactual is the status quo. Firewall similarly argues that the counterfactual is the status quo.
20. We will consider the evidence on whether the without-the-acquisition scenario is best characterised by the status quo, or whether the parties would seek alternative options; for example, whether:
 - 20.1 Firewall would be sold to a different buyer; or
 - 20.2 Billi Australia would enter New Zealand to compete directly (rather than supplying products into New Zealand through Merquip).

Preliminary issues

21. We will investigate whether the Proposed Acquisition would be likely to substantially lessen competition in the relevant market (or markets) by assessing:
 - 21.1 the unilateral effects that may result from the Proposed Acquisition;
 - 21.2 whether the Proposed Acquisition is likely to result in coordinated effects;
 - 21.3 whether the merged entity would be able and have the incentive to foreclose rivals due to vertical effects; and
 - 21.4 the effectiveness of the Proposed Remedy in addressing the above effects (to the extent that we consider they arise).
22. We will consider whether, taking into account the effect of the Proposed Divestment Undertaking, we can be satisfied that the Proposed Acquisition is not likely to give rise to the above concerns.

Unilateral effects: would the merged entity be able to profitably raise prices¹¹ by itself?

23. Where two suppliers compete in the same market, a merger could remove a competitor that would otherwise provide a competitive constraint, allowing the merged entity to raise prices.¹²
24. Osmosis acknowledges that Zenith and Merquip are the largest and second largest suppliers of MFTs in New Zealand, but argued that the Proposed Remedy would, in substance, remove the only material competitive aggregation arising from the Proposed Acquisition, such that the Proposed Acquisition would not give rise to any

¹¹ References in this document to increases in price can also be understood as references to a reduction in non-price factors such as quality or service levels.

¹² *Mergers and Acquisitions Guidelines* above n6 at [3.62].

substantial lessening of competition in any market in New Zealand.¹³ We will test these submissions.

Coordinated effects: would the Proposed Acquisition make coordination more likely?

25. An acquisition can substantially lessen competition if it increases the potential for the merged entity and all or some of its remaining competitors to coordinate their behaviour and collectively exercise market power or divide up the market such that output reduces and/or prices increase. Unlike a substantial lessening of competition which can arise from the merged entity acting on its own, coordinated effects require some or all of the firms in the market to be acting in a coordinated way.¹⁴
26. Osmosis is of the view that the Proposed Remedy would, in substance, remove the only material competitive aggregation arising from the Proposed Acquisition, such that the Proposed Acquisition would not give rise to any substantial lessening of competition arising from coordinated effects in any market in New Zealand. We will test these submissions.

Vertical or conglomerate effects: would the merged entity be able to foreclose rivals?

27. A merger between suppliers (or buyers) who are not competitors but who operate in related markets can result in a substantial lessening of competition due to vertical or conglomerate effects. This can occur where a merger gives the merged entity a greater ability or incentive to engage in conduct that prevents or hinders rivals from competing effectively.
28. We will consider whether we can be satisfied that the Proposed Acquisition, taking into account the effect of the Proposed Divestment Undertaking, is not likely to give rise to vertical effects through the restricted supply of key inputs used in the servicing of some or all of the relevant products.

The Proposed Divestment Undertaking

29. Where a merger raises competition concerns, an applicant can provide an undertaking to sell assets or shares as a condition of clearance.¹⁵ For a divestment undertaking to remedy competition concerns, we must be satisfied that the divestment will result in sufficient additional competitive constraint on the merged firm so that a substantial lessening of competition is no longer likely.¹⁶
30. To assess whether a divestment undertaking remedies competition concerns, we consider all the relevant risks associated with any proposed divestment. We assess three kinds of risk associated with any divestment:
- 30.1 composition risk – the risk that the scope of any divestment undertaking may be too limited, or not appropriately configured, to attract a suitable

¹³ The Application at [1.5].

¹⁴ *Mergers and Acquisitions Guidelines* above n6 at [3.84].

¹⁵ *Mergers and Acquisitions Guidelines* above n6 at [F.2].

¹⁶ *Mergers and Acquisitions Guidelines* above n6 at [F.12].

purchaser or to allow a successful business to be operated in competition with the merged entity;

- 30.2 asset risk – the risk that the competitiveness of a divested business will deteriorate prior to the completion of any divestment; and
- 30.3 purchaser risk – the risk that there may not be a purchaser that is acceptable to us and/or the risk that the applicant has an incentive to sell to a party who would not be a strong competitor.

The Proposed Divestment Undertaking, and what Osmosis has submitted

- 31. Under the Proposed Divestment Undertaking, the entire Merquip business would be divested to an approved purchaser.
- 32. Osmosis has submitted:
 - 32.1 the scope of Merquip business being divested is comprehensive and will include all components necessary for the ongoing competitive operation of Merquip in New Zealand;¹⁷
 - 32.2 the Merquip business is an established stand-alone business, and has only been owned by Firewall for approximately four months. Prior to October 2021, it operated completely independently of the broader Waterlogic group and has retained that independence and separation since being acquired by Waterlogic New Zealand Limited;¹⁸
 - 32.3 the competitiveness and saleability of Merquip will be preserved in the period between completion of the Proposed Acquisition and divestiture to the approved purchaser so as to minimise any perceived asset risk.¹⁹
- 33. While it does not form part of the proposed divestment remedy before the Commission, we note that Osmosis is also simultaneously offering the Australian Competition and Consumer Commission (ACCC) an undertaking to divest the Billi Australia Pty Ltd (Billi) business in Australia.²⁰

How we will assess the Proposed Divestment Undertaking

- 34. We will consider whether divestment of Merquip is likely to address the potential competition effects of the Proposed Acquisition, and whether the Proposed Divestment Undertaking contains sufficient safeguards to address the composition, asset or purchaser risks associated with the divestment of Merquip.
 - 34.1 In terms of composition risk, we will consider the extent to which the business and assets to be divested are appropriately configured to attract a

¹⁷ The Application at [11.10].

¹⁸ The Application at [11.12].

¹⁹ The Application at [11.26].

²⁰ <https://www.accc.gov.au/system/files/public-registers/documents/Culligan%20Waterlogic%20-%20market%20inquiries%20letter.pdf>

potential purchaser, or whether the divested entity would need additional assets or contracts in order to viably constrain the merged entity and to be attractive to a potential purchaser.

34.2 In terms of asset risk, we will consider whether:

34.2.1 the nature of the Merquip business is such that it is susceptible to devaluing/degrading over the divestment period; and

34.2.2 the Proposed Divestment Undertaking contains sufficiently robust preservation obligations and associated protections to mitigate the risk that the Merquip business devalues/degrades prior to completion of the divestment.

34.3 In terms of purchaser risk, we will consider whether:

34.3.1 there is a risk that there may not be a purchaser acceptable to the Commission available; and

34.3.2 Osmosis has any particular incentive to sell Merquip to a weak competitor.

35. We also intend to consider the linkages between the Merquip business proposed to be divested in New Zealand, and the Billi business proposed to be divested in Australia, and to test whether the competitiveness of Merquip would be materially different if those two businesses were divested to separate purchasers as opposed to a single purchaser. Currently, the relationship between these two businesses is intra-company, and in a separate purchaser scenario would become inter-company.

36. We need to test whether this change in dynamic between the two could impact the competitiveness of the divested business, when compared to a scenario where they are divested together.

Next steps in our investigation

37. The Commission is currently scheduled to make a decision on whether or not to give clearance to the Proposed Acquisition by **29 April 2022**. However, this date may change as our investigation progresses.²¹ In particular, if we need to test and consider the issues identified above further, the decision date is likely to extend.



38. As part of our investigation, we will be identifying and contacting parties that we consider will be able to help us assess the preliminary issues identified above.



²¹ The Commission maintains a clearance register on our website at <http://www.comcom.govt.nz/clearances-register/> where we update any changes to our deadlines and provide relevant documents.

Making a submission

39. If you wish to make a submission, please send it to us at registrar@comcom.govt.nz with the reference "Osmosis / Firewall" in the subject line of your email, or by mail to The Registrar, PO Box 2351, Wellington 6140. Please do so by close of business on **12 April 2022**.
40. Please clearly identify any confidential information contained in your submission and provide both a confidential and a public version. We will be publishing the public versions of all submissions on the Commission's website.
41. All information we receive is subject to the Official Information Act 1982 (OIA), under which there is a principle of availability. We recognise, however, that there may be good reason to withhold certain information contained in a submission under the OIA, for example in circumstances where disclosure would unreasonably prejudice the supplier or subject of the information.

Attachment A – Products supplied by Zenith and Merquip in New Zealand

Product category	Description	Example
<p>Multi-function taps (MFTs)</p>	<p>MFTs are mains fed, but supply water in the form of a tap. In contrast to traditional taps, the MFT filters or purifies mains water, and adds functionality (i.e. heats / boils, chills, and/or carbonates it). The unit is placed either under the sink or under the counter, so these systems are often referred to as ‘under-the-counter’ or ‘under-the-sink’ or ‘in-the-sink’ systems. These systems feed in a tap which dispenses from above the sink or countertop.</p> <p>MFTs can be used in commercial settings (e.g., offices) and residential settings (e.g., in a home kitchen).</p>	
<p>Bottle free coolers (BFC)</p>	<p>BFCs (also known as “point of use/POU”, “mains-fed”, or “plumbed-in water coolers”) are connected to the customer’s plumbed water system, improving the quality of water via filtration or purification methods.</p> <p>Dispensed water can be ambient, cold, hot or sparkling, depending on machine functionality.</p> <p>Machines can be available as freestanding or countertop units.</p>	

Product category	Description	Example
Fountains (bubblers)	<p>Fountains/bubblers are water dispensers connected to mains water which are used in environments where a robust and impact resistant water machine is required (e.g. outdoor or public spaces). Fountains/bubblers are configured to have a bubbler outlet or spout for drinking and may also include a carafe outlet to refill water bottles. Fountains dispense water at chilled temperatures.</p> <p>Fountains/bubblers are used in various environments, including in commercial environments (e.g. airports and construction sites), in public spaces (e.g. in parks and recreational areas), and in schools.</p>	
Wall mounted boilers	<p>Wall mounted boilers are mains fed units affixed to a wall which deliver only boiling water. Water may be supplied filtered or unfiltered.</p> <p>Wall mounted boilers are a convenient way of dispensing high volumes of boiling water without using an electric kettle. Wall mounted boilers are used by governmental departments, small and large commercial suppliers, worksites and community organisations. Wall mounted boilers are also supplied on a wholesale basis to small and large suppliers.</p>	
Other: solutions for customers with higher volume needs	<p>Customers with relatively higher volume needs (such as hotels, restaurants and cafes) use taps allowing them to offer filtered still and sparkling water to their customers to serve larger volumes of water consumed in those contexts. These taps replace the need for single use bottled filtered chilled and sparkling packaged water or tap water in hospitality venues as they are offered to customers for use in conjunction with reusable and refillable branded glass bottles.</p>	