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Statement of Preliminary Issues

Verifone/Smartpay

11 February 2020

Introduction

1. On 31 January 2020, the Commerce Commission (the Commission) registered an application (the Application) from Verifone New Zealand (Verifone) to acquire the assets used by Smartpay Holdings Limited (and its subsidiaries) to operate the Smartpay business in New Zealand (Smartpay) (Proposed Acquisition).[1]

2. 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.

3. This statement of preliminary issues sets out the issues we currently consider to be important in deciding whether or not to grant clearance.[2]

4. We invite interested parties to provide comments on the likely competitive effects of the Proposed Acquisition. We request that parties who wish to make a submission do so by **25 February 2020**.

The parties

5. Verifone, through its subsidiary Eftpos New Zealand Limited, supplies payment terminals directly to merchants under the EFTPOS brand. It also supplies payment terminals to resellers on a wholesale basis and provides payment processing services. The parent company of Verifone, Verifone, Inc., is a global manufacturer and supplier of terminals and payment processing services.

6. Smartpay operates in New Zealand through subsidiary companies, namely Smartpay Limited, Smartpay New Zealand Limited, Smartpay Software Limited, Viaduct Limited, Smartpay Rental Services Limited and Smartpay Ethos Limited. Smartpay is a supplier of payment terminals to merchants in New Zealand.

Our framework

7. Our approach to analysing the competition effects of the Proposed Acquisition is based on the principles set out in our Mergers and Acquisitions Guidelines.[3] As

[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] 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.

required by the Commerce Act 1986, we assess mergers and acquisitions using the substantial lessening of competition test.

8. 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).[4] This allows us to assess the degree by which the Proposed Acquisition might lessen competition.

9. 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:

    9.1 constraint from existing competitors – the extent to which current competitors compete and the degree to which they would expand their sales if prices increased;

    9.2 constraint from potential new entry – the extent to which new competitors would enter the market and compete if prices increased; and

    9.3 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

10. 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.[5]

11. In the Application, Verifone submitted that the relevant market for assessing the Proposed Acquisition is the national market for the retail supply of payment terminals in New Zealand.[6]

12. We will test whether this market definition is appropriate and whether any other markets may be relevant to our assessment of the Proposed Acquisition. In particular, we will consider whether:

    12.1 there should be one broad market for the retail supply of payment terminals, or more narrowly defined markets based on merchant type or size (eg small to medium enterprise customers versus large retailers); and

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

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

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

[6] The Application at [49].

12.2 any other product or functional markets are relevant to our assessment of the Proposed Acquisition (eg a market for the wholesale supply of payment terminals).

Without the acquisition

13. Verifone submitted that if the Proposed Acquisition did not occur, Smartpay and Verifone would be likely to continue to supply terminals as separate entities.[7]

14. We will consider what the parties would do if the Proposed Acquisition did not go ahead. We will consider the evidence on whether the without-the-acquisition scenario is best characterised by the status quo, or whether the counterfactual may be something other than the status quo.

Preliminary issues

15. The parties overlap in the supply of payment terminals to retailers and merchants in New Zealand.

16. We will investigate whether the Proposed Acquisition would be likely to substantially lessen competition in the relevant markets by assessing whether horizontal unilateral, coordinated and/or vertical effects might result from the Proposed Acquisition.

Horizontal unilateral effects

17. Unilateral effects arise when a firm merges with a competitor that would otherwise provide a significant competitive constraint (particularly relative to remaining competitors) such that the merged firm can profitably increase price above the level that would prevail without the merger without the profitability of that increase being thwarted by rival firms' competitive responses. The question that we will be focusing on is would the loss of competition between the parties enable the merged entity to profitably raise prices or reduce quality or innovation by itself?

18. In the Application, Verifone submitted that the Proposed Acquisition would not be likely to substantially lessen competition due to unilateral effects because:[8]

    18.1 the combined market share of Verifone and Smartpay falls within the Commission's concentration indicators;

    18.2 the merged entity would continue to be constrained by a large number of existing competitors;

    18.3 the merged entity would also be constrained by the potential entry or expansion of other payment providers, and very low barriers to entry; and

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[7] The Application at [24].

[8] The Application at [68, 71, 73 and 83].

18.4 retailers/merchants have significant countervailing power and can readily switch between payment terminal suppliers or to new alternative payment acceptance methods.

19. We will consider:

19.1 the degree of constraint that Verifone and Smartpay impose upon one another;

19.2 to the extent that any constraint is material, we will assess whether the lost competition between the merging parties could be replaced by rival competitors;

19.3 how easily rivals could enter and/or expand and whether that is likely in a timely manner; and

19.4 whether customers have special characteristics that would enable them to resist a price increase by the merged entity.

Coordinated effects

20. A merger can substantially lessen competition if it increases the potential for the merged entity and all or some of its remaining rivals to coordinate their behaviour and collectively exercise market power such that output reduces and/or prices increase across the market. 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.

21. In the Application, Verifone submitted that the Proposed Acquisition would not be likely to substantially lessen competition due to coordinated effects because:[9]

21.1 the relevant market is highly competitive, and includes large global suppliers as well as small regional resellers, has a range of different customers (who are price sensitive) and business models, and has limited price transparency;

21.2 barriers to entry are low, and existing suppliers could readily expand and others could enter which reduces the likelihood of coordination;

21.3 the market is also subject to disruption as a result of innovation in the payments industry and the development of alternative payments technology that removes the need for a terminal;

21.4 retailers/merchants have countervailing power, as they can readily switch between payment terminal suppliers and alternative payment acceptance methods; and

21.5 there is no history of anti-competitive coordination in the relevant market.

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[9] The Application at [84].

22. We will assess whether the Proposed Acquisition would make coordination more likely, more complete or more sustainable. We will consider whether any of the relevant markets are vulnerable to coordination, and whether the Proposed Acquisition would change the conditions in the relevant markets. We will assess whether the Proposed Acquisition would make it easier for Verifone to monitor and punish the behaviour of rivals and hence make coordination more likely.

Vertical effects

23. A vertical merger is a merger between firms operating at different levels of a supply chain (for example, a wholesaler and a retailer). Vertical mergers can provide merged entities the ability and incentive to foreclose downstream rivals, including by raising the costs of rivals or by changing the conditions of entry to make it harder to enter or expand.

24. In the Application, Verifone submitted that the Proposed Acquisition would not be likely to substantially lessen competition due to vertical effects because:[10]

    24.1 Verifone is already a vertically integrated payment company, and the Proposed Acquisition would not change Verifone's ability or incentive to foreclose any market;

    24.2 at the wholesale level, the Proposed Acquisition would not change Verifone's incentive to supply terminals to resellers at the wholesale level, and resellers can readily acquire terminals from a number of other suppliers; and

    24.3 in terms of payment switching, Verifone would not have the ability to foreclose other terminal suppliers to access switching services, and it would continue to be significantly constrained by the ability of suppliers to switch to Ingenico/Paymark's switch.

25. We will assess whether the Proposed Acquisition might give Verifone the ability and incentive to foreclose rivals. In particular, we will consider:

    25.1 whether Verifone would have the ability to foreclose, through having control over an important input;

    25.2 whether Verifone would have the incentive to foreclose, through earning additional profit from the strategy that outweighs the costs of lost sales; and

    25.3 whether the competition lost from any foreclosed competitors would be sufficient to have the likely effect of substantially lessening competition.

Next steps in our investigation

26. The Commission is currently scheduled to make a decision on whether or not to give clearance to the Proposed Acquisition by **30 March 2020**. However, this date may

[10] The Application at [85].

change as our investigation progresses.[11] In particular, if we need to test and consider further the issues identified above, the decision date is likely to extend.

27. 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.

Making a submission

28. If you wish to make a submission, please send it to us at registrar@comcom.govt.nz with the reference "Verifone/Smartpay" 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 **25 February 2020**.

29. 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.

30. 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.

[11] 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.