Hills Motors' Salvaging Capabilities: Inability to Compete for National Insurance Contracts

1. EXECUTIVE SUMMARY

According to the CMA's Provisional Findings ("**PFs**"), insurance customers overwhelmingly considered that Hills Motors was not capable of meeting their requirements for national salvaging contracts (none of Copart's customers considered Hills Motors capable). The PFs nonetheless go on to state:

> *In our assessment, we have focussed on Hills Motors' ability to service, and therefore compete for, national insurance contracts… while Hills Motors' model for servicing the Ageas contract has some unique features, the evidence suggests that it is capable of being replicated, with certain adjustments, for other large national contracts.*[1]

And that:

> *We have not received compelling evidence that Hills Motors' operating model and approach to risk, or management capacity, are material barriers to it continuing to compete for national insurance contracts, including large national insurance contracts.*[2]

This paper now provides a significant body of additional compelling evidence that Hills Motors does not have, and would not be able to achieve, the capabilities necessary to compete effectively for national insurance contracts and address the capability gap highlighted by customers. The evidence in this paper therefore gives the CMA Panel the basis to revise its provisional conclusions.

The PFs do not consider or recognise just how radically different the counterfactual inherent in the CMA's provisional conclusion is to the *status quo ante* and how big a speculative and unfounded leap the PFs assume Hills Motors would take absent the merger in competing for national insurance contracts. There is very little evidence suggesting that this is realistic (let alone more likely than not as required by Phase 2).

The burden of proof to show an SLC on the balance of probabilities lies with the CMA. In the context of national insurance customers overwhelmingly indicating that the parties do not compete, that Hills Motors is not capable of meeting their salvaging requirements, and that the merger will be positive for competition, the CMA has dismissed these views in order to reach an

[1] PFs, paragraph 8.70 and 23(c).

[2] PFs, paragraph 8.47.

SLC. The parties believe that the CMA needs to provide evidence demonstrating that Hills Motors is instead, contrary to these views, capable of supplying a national insurance contract (and likely to compete effectively for such contracts in the future) in order the meet the requisite legal standard. The evidence provided in this paper suggests such a conclusion is not tenable.

A more detailed analysis of the requirements of supplying a national insurance contract demonstrates the extensive investment that Hills Motors would need to undertake and fund, the risk, liabilities and costs that Hills Motors would need to take on, and the impact this would have on Hills Motors' business and competitiveness. The PFs are predicated on Hills Motors being able and willing to expand hugely and take on very significant risk in supply of salvage services to the insurance sector.

The insuperable obstacles are summarised as follows and further evidenced in this paper:

Hills Motors cannot compete for national contracts in competition with e2e

- A counterfactual that assumes Hills Motors can both compete for national contracts and remain a member of e2e is not realistic as Hills Motors would have to resign from e2e and would no longer be able to sell vehicles through the e2e platform. There would be no incentive for e2e members to allow this to happen. The Ageas contract is entirely exceptional in this regard.

Hills Motors cannot use outsourced agents to supply a national contract

- Salvage agents would be required to sell the vehicles on Hills Motors' platform due to the inherent nature of the consignment model. Salvage agents would never agree to such an arrangement, as they would not earn sufficient margin, would risk undermining e2e (that they have invested significantly in), and would incur additional costs. There would be a fundamental conflict of interest between the salvage agents and Hills Motors.

Hills Motors would need to undertake significant investment to compete for and supply a national insurance contract

- Hills Motors does not under any circumstances have the spare capacity to take on a national insurance contract and so it would either need to rely even more on sub-contractors (which is not feasible) or to invest in additional capacity itself.
- An insurer would expect salvaging to commence within a three-month period from award of the contract. Hills Motors would therefore need to invest speculatively in advance in order to bid for a contract without knowing if it will be able to win a contract and obtain a return on its investment.
- Hills Motors therefore faces a 'chicken and egg' situation (it cannot compete for national insurance contract without investment and is unwilling to invest without certainty around winning a contract) that means Hills Motors will not undertake such investment in the counterfactual, and will therefore not compete for national insurance contracts.
- The investment requirement involves specific acquisitions with long lead times meaning that Hills Motors would need to commit well in advance.

- The investment required would be very significant and a fundamental shift in the business model of Hills Motors (in terms of the long-term debt and risk it would have to take on) that the scenario envisaged in the PFs is hugely different from the *status quo ante*.

Significant up-front investment requirement would total at least £29 million and involve a lead time of 2-3 years including:

- **Salvage transport capacity**. Hills Motors would need a significant increase in its fleet if it is to collect additional vehicles under a national insurance contract.
- **Site capacity**. Hills Motors currently has spare capacity for only [✂] vehicles so would need to find, acquire and develop a new site with significant acreage for storage of vehicles to sell and potentially for dismantling as well.
- **Dismantling equipment**. Should Hills Motors envisage dismantling and sourcing green parts under a hypothetical national insurance contract, which seems likely given this is its core business, it will require additional dismantling capacity.
- **Staffing expansion**. Hills Motors does not have the staffing resources to supply another national insurance contract and would need to undertake a substantial recruitment drive.
- **Auction development**. Hills Motors will not be able to use the e2e platform if it competes for national insurance contracts (as the counterfactual in the PFs envisages) and thus will be reliant on developing its own. Hills Motors does not currently have an auction platform. If it is able to launch one, it would be unproven and have no buyers registered. Hills Motors will not be able to compete unless it can demonstrate that its auction can deliver strong returns comparable to competing salvagers. The investment in the auction platform to achieve this would be very significant and have to occur over multiple years to develop sufficient brand equity and registered buyers. The key capability from an insurer perspective is not having an auction platform *per se* but an auction platform that delivers high selling prices.
- **Potentially additional services**. To compete to supply some national insurers, Hills Motors would need to invest in and develop certain additional services that are a key requirement for them and which Hills Motors' currently does not have the capability to provide.

Hills Motors has limited scope for funding this investment and limited debt capacity

- Any of the investments above on a standalone basis would require greater borrowing than Hills Motors has ever taken on at any point in its history. In the context of a company that has typically taken on no long-term debt, the assumption inherent in the PFs that Hills Motors would suddenly fundamentally shift its business model to take on this significant debt is not realistic or credible.
- This debt would lead to an extraordinary shift in Hills Motors' balance sheet: the debt would be (at least) equivalent to [✂]x Hills Motors' EBIT and would involve Hills Motors increasing its leverage from [✂]% to [✂]%. Not only does Hills Motors not have the debt capacity to make such up-front investment, this debt would be taken on speculatively without any prospect of a return. This fundamental shift in Hills Motors risk-taking is in the context of Ian Hill, operator of a small family business, explicitly stating to the CMA that he would never take on this risk.

- Taking account of the unprecedented up-front investment, the low likelihood of future cash flows and the very high risk-adjusted discount rate (or certainty equivalent) points to an irrational investment decision that would not be undertaken and emphasises how unrealistic the counterfactual assumed in the PFs is.
- Debt repayment would be significant with annual estimated payments of £[✂] million (in the context of Hills Motors never taking on material long-term debt) suggesting Hills Motors would be increasing insolvency risk to an extent that contradicts the risk-aversion of the owner.

Advanced charges would also lead to an increase in Hills' short-term debt

- National insurance contracts impose on salvagers a commitment to provide the insurer with short-term trade credit. The salvager must pay in advance for storage and recovery costs and sometimes does not receive repayment from the insurers for a month or more. These advanced charges are significant and range from £[✂] million to £[✂] million across the year, imposing additional working capital requirements on salvagers.

Contractual and contingent liabilities are substantial for a national insurance contract

- Hills Motors would be individually responsible for all liabilities under a national insurance contract, including from any actions undertaken by sub-contractors. Potential liabilities can range from £[✂] million to £[✂] million dependent on the insurer.
- Contingent liabilities inherent in SLAs and penalties if these are not met are also significant. SLAs are extensive and penalties severe.
- Hills Motors does not have the financial capability to take on these liabilities.

Even if Hills Motors invests significantly there will be a residual capability gap that means that it would not be competitive for a national insurance contract

- For example, the estimated revenue earned by Hills Motors on a national insurance contract would be insufficient to cover its cost of capital, would be less than required to cover collection agent fees on a per vehicle basis, and insufficient to cover the additional transport costs Hills Motors will have to incur relative to e2e, IAA, Copart and Recycling Lives.

The CMA suggests that the set-up for Ageas can be replicated for other national insurance contracts, implying that if Hills Motors can overcome these provisions to supply Ageas, then it ought to be relatively easy for it to do so for other national contracts. This is incorrect as Ageas is fundamentally different to other national insurance contracts. Ageas does not impose the same conditions as other insurers and does not seek the same commercial return (instead prioritising use of green parts). There is no evidence another insurer would ever take a similar approach.

2. BACKGROUND AND APPROACH

A more detailed analysis of the requirements of supplying a national insurance contract demonstrate the very extensive investment that Hills Motors would need to undertake and fund, the risk, liabilities and costs that Hills Motors would need to take on, and the impact this would have on Hills Motors' business and competitiveness. The PFs are predicated on Hills Motors being able and willing to expand hugely and take on very significant risk in supply of salvage services to the insurance sector.

In a hypothetical counterfactual where Hills Motors competes for national insurance contracts, it is non-contentious that insurers require national coverage[3] and Hills Motors cannot provide national coverage itself. We go on to show that Hills Motors is severely capacity constrained and cannot compete for or supply a national contract without access to additional capacity. Under the counterfactual outlined in the PFs, to provide both national coverage and sufficient capacity, Hills Motors therefore has to either use outsourced salvage agents or expand its own capacity (or a combination of both). We assess the scope for Hills Motors to do either or both.

We follow the approach in the PFs and focus the assessment on Hills Motors ability to compete to supply national insurance contracts and, in particular, large national insurance contracts where the PFs consider the Parties to be two of a small number of players.[4]

3. ASSESSMENT OF CAPABILITIES

3.1. Hills Motors cannot compete for national contracts in competition with e2e

The PFs take as the counterfactual:

> *"We therefore consider the counterfactual of the pre-Merger conditions of competition is one in which Hills Motors would have… remained on the board of directors and a collecting member of e2e."* [5]

At Phase 2, the CMA must select the most likely conditions of competition as the counterfactual against which to assess the merger. As a basic requirement, the counterfactual must therefore be feasible and consistent with the evidence. Hills Motors is not able to compete for a national contract while remaining a member of e2e. If Hills Motors competes for a national contract, Hills Motors would have to resign from e2e and would no longer be able to sell vehicles through the e2e platform.[6] Hills Motors both competing for national insurance contracts and remaining a member of e2e is therefore not possible (let alone the most realistic scenario).

Hills Motors' behaviour in relation to the [✄] benchmarking exercise is consistent with this. Hills Motors knew, first, that it could not feasibly supply [✄] (and [✄] confirmed that Hills Motors is not capable of meeting its requirements) so no competition took place in any event and, second, that Hills Motors would not be able to bid for [✄] independent from e2e. Instead, Hills Motors

3 PFs, paragraph 8.42.

4 PFs, paragraph 23(a). Large national insurance contracts typically have a volume requirement of 20-40k.

5 PFs, paragraph 5.13.

6 Hills Motors would also not be able to meet the requirements of a national tender as it would not be able to sell vehicles without an existing auction facility, given that it would no longer be able to use the e2e platform.

responded in a way that allowed it to put forward its green parts offer while not competing for salvaging services.[7]

Furthermore, note that there would be no incentive for other e2e members to allow Hills Motors to compete for a national contract (thereby sanctioning possible lost volumes) or support it in doing so (facilitating lower volumes and lower margins would be self-defeating). The e2e members would be shifting sales volumes to a poorer performing auction platform (and thus became liable to higher costs such as storage and relisting fees when vehicles are not sold) where they do retain the buyer fees.

The Ageas contract is exceptional with regard to e2e. [✂] under the *status quo ante* and, as a result, was not considered a competitive risk to possible e2e volumes.

Should the CMA speculatively allege that, contrary to the evidence available and the incentives of e2e, Hills Motors would remain a member of e2e while still competing against it for national insurance contracts, the Parties would welcome sight of the evidence the CMA is relying on to support this conclusion to ensure the Parties have a fair chance to respond.

3.2. Hills Motors cannot use outsourced agents to supply a national contract

Customers seek national coverage from salvagers[8] and Hills Motors cannot supply a national contract itself as it does not have the capability to meet the insurers requirements (for example, it does not have the transport or site capacity to collect within the time periods required or the liquid auction platform to generate maximum value from sale of the vehicle).

The PFs confirm that all national insurers require national coverage and most national insurers would not accept national coverage to be provided via subcontracting.

> *"… six of the thirteen insurance customers identified as having volume requirements of over 10,000 vehicles annually told us that it is acceptable for national coverage to be provided via subcontracting"*

3.2.1. Limited number of insurers that Hills Motors can supply

There is extremely limited scope for competition to supply those customers open to sub-contracting. Less than half of insurers would consider using subcontractors at all. Of those that would consider doing so, these are noted as six of the following: [✂]. Hills Motors is therefore, even on the CMA's view, not a viable supplier for any national insurer other than these. Of these, only four ([✂]) have volume requirements over 10,000 vehicles.[9] Of these four contracts, [✂] did

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7 One of the key consequences of this is that, should Hills Motors compete for a national contract it would need to do so without access to the e2e auction platform. As part of a tender for a national insurance contract, the insurer requires demonstrable historic results to show auction performance and likely returns. This would be impossible for Hills Motors as it does not have its own auction platform yet, has not sold a single vehicle from it, and can provide no data to insurers to support sales results. This is considered further below.

8 PFs, paragraph 8.42.

9 As the PFs note, [✂] has less than 10,000 (PFs, footnote 487), as does [✂], while the recent [✂] tender specified a volume requirement of [✂] (see Annex 3 (Appendix 6) to the FMN). We assume this is an error and the PFs meant to refer to four of 13.

not consider Hills Motors capable of meeting its requirements[10] while Hills Motors self-evidently cannot compete for the [✂] contract head-to-head against e2e while also remaining a collecting member of e2e (as assumed would be the case in the CMA's counterfactual outlined in the PFs). As the CMA is aware, Ageas did not invite Copart to tender as it does not meet its green parts requirements.

3.2.2. Salvage agents would not agree to the required outsourcing arrangement

For those customers that would consider outsourcing, Hills Motors cannot use subcontracted salvage agents to supply national insurance contracts. The national insurers that Hills Motors would be competing to supply in the CMA's counterfactual will typically be using, and have a strong preference for, the consignment model as it provides for higher returns.[11] The salvage agents would therefore be required to sell vehicles on Hills Motors' auction platform rather than on e2e. This would be a necessary requirement of Hills Motors bidding separately. Hills Motors' auction platform and the e2e platform cannot be used interchangeably for a national insurer (the profit share model and claims process would preclude this). However, under no circumstances would salvage agents ever agree to this for several reasons. First, they would not earn sufficient margin from the arrangement – there would be no incentive in receiving only a collection fee. Second, it would risk undermining e2e, the vehicle through which they bid for national contracts, and which they have invested significant amounts in developing. Third, they would lose the control that they have through e2e. Fourth, they would essentially be shifting to a poorer auction that achieves lower sales values. Finally, as a result of this, they would incur additional costs (e.g. additional storage fees, relisting fees).

This is in contrast to the Ageas arrangement where salvage agents retain the vehicles for a small fee (see below) and sell it (either through e2e or otherwise) or dismantle it themselves. For the avoidance of doubt, even under Ageas, the current sub-contracted salvage agents would never agree to collect vehicles for a collection fee, only for these vehicles to be sold on Hills Motors' auction platform. The salvage agents would see this as a threat to their own business.

3.2.3. Use of sub-contracted agents would make Hills Motors uncompetitive

Many national insurance contracts do not allow for a margin sufficient to use outsourced salvage agents. Use of outsourcers is inevitably more expensive, making Hills Motors relatively uncompetitive.

There are two types of agents used by Hills Motors under Ageas. The use of both leads to a significantly lower margin and makes it more difficult for Hills Motors to break even on a national insurance contract:[12]

- ***Salvage agents***: Hills Motors' own recoveries account for approximately half of total required collections under Ageas. The remaining half is collected by salvage agents for

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10 PFs, paragraph 8.93(a).

11 See customer views submitted by Copart indicating that almost all insurers prefer the profit share model and the reasons provided by the insurers (higher returns).

12 As the CMA is aware, different companies perform the two functions. For example, salvage agents include [✂] while collection agents include [✂].

which Hills Motors receives a fixed fee. This fixed fee is necessarily very low (averaging £[✂] per vehicle) in order to persuade salvage agents to collect under Ageas. As a consequence of the necessarily low fee, the revenue that Hills Motors can earn on a national insurance contract is significantly lower than a salvager collecting the volumes themselves. This 'opportunity cost' means that for half of the volumes of a national insurance contract Hills Motors necessarily earns only approximately [✂]% of the revenue it does on its own recoveries. With such a significantly lower return than competitors can achieve, Hills Motors will always struggle to compete for national insurance contracts.

- ***Collection agents***: Even for Hills Motors' own recoveries (around half of total collections), [✂]% are collected by a third-party collection agent, which Hills Motors must pay, typically £[✂] per vehicle (average £[✂]). The use of these collection agents reflects that Hills Motors does not have the capacity or capability to collect the volumes required with a national insurance contract. This collection fee even on a standalone basis is higher than the Hills Motors' estimated revenue for many national insurance contracts. While these costs apply to only [✂]% of Hills Motors' own recoveries, the total cost of these under a national insurance contract ranges from £[✂] to £[✂].[13] Thus, considering these collection fees alone points to an increase in Hills Motor's costs base for every prospective national contract. This cost disadvantage is considered again (and explained in further detail) below.

  [✂]

Thus, taken together, the foregone revenue of the sub-contracted salvage agents and the actual cost of the sub-contracted collection agents, both required due to Hills Motors lack of capabilities, point to Hills Motors being uncompetitive for national insurance contracts.

No evidence has been provided in the PFs to suggest that subcontracting salvage agents would ever agree to such a model or that considers how Hills Motors would operate a network to supply a national insurance contract and breakeven. If the CMA has obtained such evidence as part of its investigation, the Parties request that this is shared so that Parties have a fair chance of rebutting this evidence.

3.3. Required investment in salvage transport capacity *ex-ante*

Hills Motors would need to collect an additional 10,000-40,000 vehicles annually to supply a national insurance contract.[14] Collection of vehicles is subject to strict requirements imposed by insurers and must take place within either one or two working days of instruction (dependent on

13 And the remaining volumes that Hills Motors collects directly are subject to higher transport costs.

14 Hills Motors currently has one national insurance contract with a volume of approximately [✂] vehicles, of which it collects around half. A typical national insurance contract is 20-30k. As outlined above, Hills Motors would not be able to use outsourced salvage agents to collect vehicles under a national insurance contract. However, even if we assume such a network can be established and Hills collects half of the vehicles of a national contract, it would still need to collect at least 10,000 vehicles.

the contract). To do this, Hills Motors estimates that it would need, at the very minimum, an additional [✂] multi-car transporters ("wagons") and [✂] mid-size car transporters.[15]

An insurer would expect salvaging to commence within a three-month period.

The waiting time to order a *single* new salvage wagon would be 19 months with the full order required to supply a national contract taking until autumn 2025. A wagon has two elements, a chassis and the addition of the car transporter body. There are limited suppliers of both elements and the Parties have requested lead times from the suppliers of both:[16]

- The current delivery of a chassis for an order placed now for either a 26 tonne XD chassis for wagon or a 16 tonne LF chassis for a mid-size transporter, is towards the end of Q1 2024.[17]
- The current order books for transport bodies are extremely full. The earliest that the body could be supplied would be early 2025 for two transporters with a further two delivered per month for the next six months, which would take the full order through to autumn 2025.[18]

Hills Motors would not be able to wait until it has won a contract to source the transport vehicles if it is to fulfil the contract. Hills Motors would instead need to invest speculatively in advance of bidding for the contract in the hope of winning a future contract. If Hills Motors was then unable to win a future contract, there would be no return on this investment.

Each wagon costs £202,978[19] and each mid-size car transporter costs £138,716.[20] Supplying a national insurance contract would therefore involve a total required investment of approximately £[✂] million. This investment would need funding. This sum alone is greater than Hills Motors

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15 Hills currently has [✂] car carrying vehicles: [✂] multi-car transporter (with capacity for 7-8 cars), [✂] mid-size car transports (3-4 cars), [✂] (2 cars) and [✂] single car transporters.

16 There is no second hand market for these vehicles as far as the Parties are aware (or else Copart would not wait so long for a delivery).

17 See **Exhibit 0X: Evidence supporting transporter chassis lead times.** Email from DAF trailers with lead time and confirming costs for new transporters

18 See **Exhibit 0X: Evidence supporting transporter body lead times**. Email from Belle (manufacturers of transporter bodies) with lead times.

19 Cost of a 7 Car Transporter: £99,500 for a DAF 26t XD chassis and £65,496 for Belle 6/7 Car Transporter body plus an additional £4,152 for other equipment (cameras/telematics/livery) giving a total of £169,148 + VAT per transporter.

20 Costs of a 3 Car Transporter: £61,500 for a DAF 16t LF chassis and £49,945 for Belle 3/4 Car Transporter body plus an additional £4,152 for other equipment (cameras/telematics/livery) giving a total of £115,597 + VAT per transporter.

has ever borrowed in the past. Given the scale of the overall investment, Hills Motors would be required to borrow to fund the investment.[21]

Required up-front investment in transporters: £[✄] million
Required lead time: ~2.5 years

3.4. Required investment in site capacity *ex-ante*

Hills Motors would need capacity to store the additional vehicles that it would be required to sell and/or dismantle (and store the additional green parts inventory). To supply a national insurance contract, Hills Motors would be required to sell 10,000-40,000 vehicles annually. Hills Motors currently sells [✄] vehicles annually (2022) and, in order to sell these, has approximately [✄] vehicles on its sites at any one time:

- **Hills' Skelmersdale HQ site** has a maximum capacity of [✄] vehicles. Hills Motors currently has [✄] vehicles stored on site. These vehicles are all for dismantling, including approximately [✄] in varying states of dismantling, [✄] in stock awaiting dismantling (the backfill of vehicles) and [✄] awaiting to be cleared for dismantling. Thus, the HQ site has spare capacity of approximately [✄] vehicles.
- **Hills Motors HQ satellite sites** at Stanley and Burscough have capacity to store maximum [✄] and [✄] vehicles, respectively. Hills Motors currently has [✄] vehicles stored at Stanley and [✄] stored at Burscough, giving spare capacity of [✄] vehicles.
- **Hills Motors' Dumfries site** has capacity for [✄]-[✄] vehicles. Hills Motors currently has approximately [✄] stored on site, giving spare capacity of [✄]-[✄] vehicles.
- **Hills Motors Gloucester site** has a maximum capacity of [✄] vehicles and currently has [✄] stored there, giving spare capacity of [✄] vehicles.

In total, Hills Motors has spare capacity to store an additional [✄] vehicles, meaning that it would, without question, need to acquire significant additional capacity to supply a national insurance contract.

If Hills Motors were to take on an additional national contract, it could either sell all the vehicles. or dismantle or scrap those it could not sell (or that are suitable for green parts). This provides for some flexibility in the site capacity requirements. These are considered below.

3.4.1. Salvage storage site capacity

Hills Motors currently sells [✄] vehicles annually, the vast majority of which are sourced as part of its Ageas contract. To supply another large national insurance contract, Hills Motors would have

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21 There is no scope to lease or hire such vehicles. If transporters were considered in isolation, there may be scope to fund the investment through cash and retained earnings (Hills Motors had earnings of £[✄] in its latest financial year). Hills Motors could also potentially resell the wagons (even if at a lower value) if it does not win a national insurance contract following the investment so the risk taken on with the purchase of transporters alone is lessened. However, given the scale of other simultaneous investment required, we consider this outlay (and the risks associated with it) alongside other investment.

to sell at least 10,000 vehicles and up to possibly 40,000 vehicles (dependent on the contract, the seller requirements, and use of sub-contracted salvage agents). As part of competing for the contract, Hills Motors must demonstrate sufficient site capacity to store these vehicles for sale (at the time of tender). For any single national insurance contract, there will therefore need to be site capacity for between 4,000 and 10,000 vehicles.

Alongside the volume of vehicles, two factors have a particularly significant effect on storage requirements:

- **Racking not typically feasible.** Hills' HQ sites – both its HQ site and satellite site – store vehicles in racks that stack vehicles vertically. While Hills Motors has been able to use these to service its Ageas contract, these would not typically be suitable for other national insurance contracts (Ageas is exceptional in this regard due to its focus on green parts).[22] This storage method can subject the vehicles to a higher likelihood of damage and, in particular, increased fire risk (when a car sets alight on a rack system, it spreads upwards very quickly, causing the rack systems to collapse and create a bonfire of vehicles). While well-suited for vehicles to be dismantled, racking cannot typically be used for vehicles for sale (as it can create additional risks for an insurer achieving the best return on its vehicles or in penalties incurred by the salvager, as for most contracts the insurer owns the vehicles and the salvager is liable for them). Without the use of racks, Hills Motors would require additional space to store vehicles for sale.
- **Long-term storage requirements**. In addition, national insurance contracts have requirements for long-term storage of vehicles that cannot be sold, for example, safeguarded vehicles, personal injury claims, children's accidents, or where the insurer is subject to a substantial claim and wishes to retain the possibility of reduced liability in the future. For these vehicles, the salvager is unable to sell them and must provide storage under the terms of the contract, which can extend in some cases for multiple years.

Table 1: Current site usage for national insurance contracts

Seller	Total vehicles on site currently	Proportion stored long term (days)		
		31+	61+	91+
Admiral	[✂]	[✂]	[✂]	[✂]
Hastings	[✂]	[✂]	[✂]	[✂]
First Central	[✂]	[✂]	[✂]	[✂]
Aviva	[✂]	[✂]	[✂]	[✂]
AXA	[✂]	[✂]	[✂]	[✂]
Markerstudy	[✂]	[✂]	[✂]	[✂]
Esure	[✂]	[✂]	[✂]	[✂]

Taking these factors into account, alongside Hills Motors' extremely limited existing spare capacity, the Parties are able to estimate the acreage required to store vehicles solely for the

22 The other exceptions are possibly [✂] and [✂], which have been tolerant of vertical stacking. As far as the Parties are aware, no other insurer would sanction this.

purpose of sale of vehicles for national insurance contracts. These are the minimum site capacity Hills Motors would require for each contract.

Thus, in order to compete for and supply a national contract, Hills Motors would need to acquire (or obtain access to) a site of approximately [✂] acres in order to store and sell the volumes of vehicles processed under the contract (assuming it sells all the vehicles). When all customers have indicated the Hills Motors does not have the capability to meet their requirements, site capacity will be one of the key factors considered.

Table 2: Required storage capacity for national insurance contracts

Seller	Approx. volume	Required storage capacity (acres)
Direct Line	[✂]	[✂]
Admiral	[✂]	[✂]
Hastings	[✂]	[✂]
Aviva	[✂]	[✂]
Markerstudy Group	[✂]	[✂]
esure	[✂]	[✂]
1st Central	[✂]	[✂]
AXA	[✂]	[✂]
Ageas	[✂]	[✂][23]
Tesco	[✂]	[✂]

These acreage figures are extremely conservative as they are based on Copart's land usage for each contract. However, Copart has a well-developed auction platform with high levels of liquidity that ensure vehicles are sold relatively quickly and do not remain on site for any length of time (with the exception of contractually restricted cases). Hills Motors would be reliant on its own auction platform that has not been launched, has never sold a single vehicle, does not have a single registered buyer, no brand awareness or visibility, no marketing spend and is entirely unproven. It is reasonable to expect that the speed of sale on Hills' auction to be very slow and the likelihood of a sale to be very low relative to Copart (and other developed platforms).

Thus, the acreage that Hills Motors would require is likely to be at least 20-30% higher than that of Copart and more likely to be [✂] acres. Taking a conservative approach, we consider a [✂] acre range for the purposes of this assessment.

3.4.2. Dismantling and green parts site capacity

While Hills Motors could feasibly sell all the additional vehicles, its core business is as a dismantler and green parts supplier. Hills Motors only salvaged regionally to supply it with sufficient vehicles as inputs for its dismantling and green parts operations. Under the Ageas contract, Hills Motors dismantled those vehicles suitable for dismantling (and all Category B vehicles). Presumably, if it

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23 Acreage shown if not vertically stacked as with other insurers.

were to compete for national contracts (as assumed in the PFs counterfactual), it would do so on the basis of its strength in green parts and thus its dismantling capability.

Thus, it is reasonable to assume that Hills Motors would dismantle all (or a large proportion) of those vehicles suitable for dismantling. As a proxy, we consider the volume of Cat. B vehicles under a national insurance contract. A typical national insurance contract would involve 5,000-10,000 Cat. B vehicles.[24]

While Hills Motors would not be able to rely on sub-contracted salvage agents to supply a national contract (see above), assuming (conservatively) that Hills Motors only dismantled approximately half of the Cat. Bs ([✂]) and accounting for the fact that only approximately [✂]% of vehicles dismantled are Cat. Bs, a national insurance contract would involve dismantling around [✂]-[✂] vehicles.

Dismantling storage. Based on annual dismantling volumes of [✂] in 2022, Hills Motors currently has [✂] vehicles on site in storage for dismantling.[25] To dismantle [✂]-[✂] additional vehicles associated with a national insurance contract, Hills Motors would therefore need to acquire capacity to store an additional [✂] to [✂] vehicles for dismantling.

Dismantling activity. Hills Motors would need capacity to dismantle an additional [✂] vehicles. Hills Motors currently dismantles [✂] vehicles annually (2022 data) so, if Hills Motors dismantled all the Cat. Bs it sourced, this would involve an increase of [✂]% dismantling volumes. Hills Motors current dismantling capacity is approximately [✂] vehicles so it would be able to absorb very few vehicles with current capacity. Hills Motors would therefore need to invest in and open a new dismantling site.

Green parts inventory storage. Even if Hills Motors has spare capacity in its current warehouse in Skelmersdale, it would need new warehousing to store spare parts dismantled at its separate dismantling site (to avoid having to ship ever part not sold immediately to Skelmersdale).

Based on current usage, and the site capacity of competing dismantlers reported by the PFs, we consider total dismantling site capacity would require at least [✂] acres while this would be offset by a reduction in sales storage site capacity of approximately [✂] acres, giving a net increased site requirement for dismantling of [✂] acres. Thus, to the extent Hills Motors dismantled vehicles of the national contract it competes for, this would require a total additional site capacity of [✂] acres.

3.4.3. Acquiring and developing site capacity

In total, Hills Motors would be required to acquire (or obtain access to) [✂] acres if it focused on only selling the additional vehicles and [✂] acres if it were also to dismantle.

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24 For example, in 2022 [✂] had [✂], [✂], [✂], [✂].

25 As noted above, there are approximately [✂] vehicles in varying states of dismantling, [✂] vehicles in stock awaiting dismantling and [✂] vehicles awaiting clearance to be dismantled.

Timing and likelihood

In order to acquire this site capacity, Hills Motors would need to appoint a property agent. Suitable sites and land for development is scarce. Land searches can take several months depending on requirements. Suitable sites of [✄] acres or [✄] acres are both incredibly difficult to source.

From a commercial perspective, suitability requires consideration of layout, accessibility, contamination risk, national coverage requirements, purchase price and development costs.

Any land under consideration requires appropriate ground condition surveys to be conducted. Good sub-soil for heavy use and with good drainage is required to avoid subsidence. Separate storage facilities are required for motorbikes, fitters sheds for minor repairs to transporter fleet and office accommodation for site staff. Sites require secure perimeter fencing with 24-hour security monitoring all of which require planning consent.

Purchase is usually subject to positive planning consent for B8 open storage for cars and granting of a permit for storage of End of Live Vehicles from the Environment Agency. Hills Motors would be required to install a large concrete area which is bunded with an interceptor to catch any contaminants which also requires planning consent. The planning process is onerous and dependent on several local factors. The *pre*-planning application process of site design, assessments for BNG, ecology, drainage, flood risk, and environmental contamination surveys can take upwards of 12 months. The statutory determination period for a standard planning application is 12 weeks however these usually take up to six months and can take significantly longer. The planning approval process for Copart's last three sites ([✄], [✄] and [✄]) took multiple years.

Once a planning consent is received, the purchase is completed and development can then begin subject to any planning constraints and pre-development requirements. It can take around 3 months to find and engage a suitable contractor through a tender process. It can take anywhere for 6-12 months for a site to be fully developed for use depending on size once contractors have been instructed.

In total, based on evidence from recent site acquisitions, it would likely take Hills Motors at least 3 years to acquire, develop and open a new site suitable for supplying a national insurance contract (assuming a site can be found) for processing and storage of vehicles only.

An insurer expects salvaging to commence within a three-month period following the award of a contract so Hills Motors would not be able to wait until it has won a contract to source the site capacity required to fulfil a national insurance contract. Hills Motors would instead need to invest speculatively in advance of bidding for the contract in the hope of winning a future contract. If Hills Motors was then unable to win a future contract, there would be no return on this investment.

If Hills Motors also wanted to dismantle and supply green parts as part of the contract, it would also need to find a site suitable for dismantling.

Neither Copart nor Hills Motors is aware of any new ATF's being licensed over the last five years. The Environment Agency from an environmental perspective are looking to close any ATFs that are not able to demonstrate advanced processes for the management of waste. The EA monitors sites closely and proactively and has a particular focus on discharges to water courses. The planning process for dismantling sites can be extremely long and burdensome with only limited chance of success.

Cost

Based on evidence of recent site acquisitions by Copart, the cost of a new site with relevant planning consent would be at least £[✂] million per acre and potentially significantly more. For example, [✂].[26] Further development costs (including professional fees) would be approximately £[✂] per acre to bring the land into use.

The total cost for Hills Motors to acquire a site suitable for supplying a national insurance contract would be approximately £20 million to £40 million.

This investment would need funded and, given the extremely large scale of the required investment, would require Hills Motors to borrow. As outlined in detail below, this sum is many multiples greater than Hills Motors has ever borrowed in the past. The conclusions in the PFs are predicated on Hills Motors fundamentally altering its entire business and taking on more risk and leverage by many multiples than ever before. Such unfounded and unsubstantiated speculation is entirely inconsistent with the relevant counterfactual being the most realistic scenario absent the merger.

Required up-front investment in site capacity: £20-40 million

Required lead time: ~3-4 years

3.4.4. No site alternatives available through other means

We understand that the CMA may look for ways to dismiss the evidence provided above and look for ways in which Hills Motors would be able to supply a national contract and increase its volumes substantially without acquiring a new site. In anticipation of such a dismissal, the Parties provide the following context:

- First, Hills Motors' existing site does not *under any circumstances* have the capacity to fulfil another national insurance contract. Due partly to its extensive dismantling facilities and limited site size, Hills Motors existing facilities for salvaging (specifically storing vehicles for sale) are inadequate to supply a national insurance contract other than Ageas even currently. As noted above, Hills Motors' sites stack vehicles vertically, which is entirely unsuitable for vehicles being sold (particularly on behalf of an insurer). Even if this were not the case, Hills Motors has space to store only an additional [✂] vehicles, which is insufficient to bid for and supply a national insurance contract.[27]
- Second, the evidence is entirely consistent with the views expressed by customers who indicated that Hills Motors is not capable of meeting their requirements. While the CMA does not seem to have asked specifically what those requirements are that Hills Motors does not meet, site storage capacity is likely to be one of the more important criteria that Hills Motors cannot meet (among many others).

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26 See **Exhibit 0X: Recent land acquisitions and site development costs**

27 Even relatively small national insurance contracts, such as [✂] and [✂] ([✂]) would involve volumes that would significantly exceed Hills Motors' current spare capacity.

- Third, sub-contracted salvage agents would not be able or willing to store vehicles for Hills Motors (many are capacity constrained and, even to the extent Hills Motors could leverage personal relationships, a significant fee would be charged). Hills Motors would not be able to process the vehicle for claims purposes if the salvage agent has possession so would likely also have to delegate the vehicle for processing to the salvage agent, which raises similar issues as described above). Note that the investment in site capacity already considers (conservatively) that Hills Motors only collects and stores half the vehicles under the national insurance contract ([✂]), despite use of outsourcers being unlikely. Such a set-up would also risk imposing prohibitive delays on the insurance claims process (if Hills Motors were to try to retain agency for the vehicle while stored at another site) or would impose prohibitive costs on Hills Motors (storage).
- Fourth, alternatives to acquisition such as long-term leases or short-term rental are not practical.
  - Short-term rental is not possible in this sector, given the requirements under a national insurance contract, including the site-specific investment required for de-pollution, requisite planning and environmental permits, requirements for disposing of hazardous waste, fuel usage, etc.
  - Long-term leases are not a practical alternative. These typically involve higher costs and lead times and are poorly suited to the sector. Landowners are very reluctant to lease to a salvager due to potential contamination risk and daily processing of hazardous waste. Planning consent for B8 open storage together with environmental permits are costly and onerous processes which are site-linked and mean that leases are commonly not conducive to operational requirements. Environmental permits require a concrete slab for severely damaged vehicles with self-contained drainage and interceptors which can be cost prohibitive on leased land especially if the lease includes a full-repairing obligation.[28] Inclusion of a dismantling site on lease-hold land (as would be assumed for Hills Motors for which dismantling is its core business) is extremely challenging. Most salvagers sites are owner-managed (Copart for example would not lease an operational site).[29]

Any suggestion that Hills Motors could supply a national insurance contract without incurring these site acquisition costs would therefore be speculative and unfounded. If the CMA has evidence to suggest otherwise, the Parties request that this is shared so that Parties have a fair chance of rebutting this assertion.

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28 Leases also generally include provision for break clauses and rent increases, particularly in the context of the landowner retaining optionality for future residential or alternative commercial development (which a salvaging site makes difficult), and obligations for ongoing repair and maintenance including dilapidations.

29 Copart [✂]. The only other lease arrangement the Parties are aware of are Synetiq's lease of the original Motorhog and Car Transplants yards (that were part of the acquisition arrangements).

3.5. Required investment in dismantling equipment *ex-ante*

As noted above, Hills Motors' core business is as a dismantler and green parts supplier. Presumably, if it were to compete for national salvage contracts (as assumed in the PFs counterfactual), it would do so on the basis of its strength in green parts and thus its dismantling capability. Thus, it is reasonable to assume that Hills Motors would dismantle all (or a large proportion) of those vehicles suitable for dismantling. As outlined above, Hills Motors does not have capacity to dismantle more vehicles on its existing site and would need to acquire an additional dismantling site (notwithstanding the barriers to doing so already set out above).

In addition to the difficulties and costs of acquiring the necessary land, in this hypothetical scenario, Hills Motors would also require additional specialist dismantling equipment including a baler, cranes, depollution areas with separate fluid storage containers for diesel petrol/oil/hydraulic fluids, storage containers for engines, wheels/tyres and other hazardous waste, racking to stack dismantling vehicles vertically (due to the extended period on site for vehicles being dismantled), a storage facility including racking for green parts, and handling and picking machinery and equipment to store at height.

Hills Motors estimates that it would need up-front investment of approximately £[✂] million to cover the costs of necessary equipment. Hills Motors has just recently had two forklifts (a relatively cheap piece of machinery starting at £40k upwards) delivered that it ordered 18 months ago. Most other machinery requires orders to be made at least a year, and commonly two years, in advance to place an order. The exception may be depollution equipment (which Hills Motors estimates would be six months plus).

Table 3: Required dismantling equipment and cost

Dismantling equipment	Estimated cost
Baler	[✂]
Crane (x2)*	[✂]
Fluid storage containers (for depollution)**	[✂]
Hazardous waste storage containers***	[✂]
Racking to store vehicles (400)T	[✂]
Storage facility	[✂]
Picking machinery and handing equipmentϕ	[✂]
TOTAL	[✂]

Notes: * Two cranes would be required: one for loading the baler and one to process cars.

** A two car system would be £[✂]+

*** £[✂] each.

T Hills Motors currently has approximately [✂] four car racks on its HQ site alone used solely for vehicles for dismantling. This excludes satellite sites used for salvaging. Racking is not suitable for a national insurance contract other than for dismantling.

ɸ Forklift and packing machines start at £40k+ each.

Required up-front investment in dismantling equipment: £[✄] million+

Required lead time: ~2 years

3.6. Required investment in staffing expansion *ex-ante*

Hills Motors would need to hire staff to salvage and dismantle the additional vehicles. Hills Motors would need to hire staff to salvage and dismantle the additional vehicles. Hills Motors currently employs approximately [✄] staff with a total annual cost of approximately £[✄] million.

An additional national insurance contract would involve [✄] insurance contract volumes (and increasing total vehicle volumes by approximately [✄]%).

- **Salvaging, dismantling and green parts staff** vary with output. The requirements of a national insurance contract are significant. While Hills Motors may save on staffing costs by selling all vehicles rather than dismantling (thereby saving dismantling staff increases) as outlined above, Hills Motors' core business is a dismantler and green parts supplier. Presumably, if it were to compete for national contracts (as assumed in the PFs counterfactual), it would do so on the basis of its strength in green parts and thus its dismantling capability. Thus, salvaging, dismantling and green parts staff costs are likely to increase by at least [✄]% and likely more.
- **Management costs**. While management costs might normally be less variable, Hills Motors would be required to deliver on a national insurance contract with stringent SLAs, intensive reporting and monitoring, and severe penalties, monitor a disparate network of salvage agents the work and performance of which it is 100% liable for. [✄] and operating a national insurance contract with another provider other than Ageas or a second national insurance contract would need additional management staff. For example, the funding requirements presupposed by the PFs would require a full time Finance Director to be hired (Hills Motors currently has one part-time finance staff member that works one day a week). Similarly, the staffing expansion presupposed by the PFs would require a full-time HR Director to be hired (currently Ian Hill's wife is responsible for payroll and works less than once a week). Thus, management staffing costs would increase by at least [✄]% and likely more.
- **Site-specific staff** such as security would likely [✄] given the requirement for Hills Motors to acquire an additional site (or sites). Conservatively, we assume these staff would increase in line with other staff.

Hiring experienced staff is very difficult in the current tight labour market environment and such a large recruitment drive to enable supply of a national contract would take an extended period of time.

- **Time and likelihood**. Hills Motors estimates that, with a very intensive and long-running recruitment campaign, it would it take at least one year to hire this amount of staff (and this would still be very ambitious) and another 3-6 months to train the new staff sufficiently so that they could work on a national insurance contract (with the associated performance metrics, stringent SLAs and risk of penalties).

- **Cost**. Based on the above, we assume conservatively that staffing costs would need to increase by at least [✂]%. While these staffing costs are recurring, the ongoing opex expense is not considered here. Instead, we focus on the up-front investment cost. In addition, Hills Motors would need to engage recruitment agencies and place job adverts on specific advertising sites. Standard recruitment terms for agencies are 15% of salary for a standard position and up to 20% or more for managerial and senior roles. A job advert costs £1-2k per month. As a guide, Copart spends up to £[✂] per annum on recruitment costs. Hills Motors would also have to incur considerable additional training costs post recruitment (e.g. Health & Safety is critical for a dismantling operation while dismantlers are highly specialise, and those involved in green parts require extensive knowledge of vehicle makes and models and the versatility and adaptability of parts). Hills Motors also estimates that to increase its staff by this amount would require additional management capacity or outsourced recruitment. Hills Motors expects that the recruitment effort, including agency costs, additional recruitment management staff, advertising, and training and development for this volume of staff hired over such an intense period would be at least £[✂].

As with salvage collection capacity and site capacity, an insurer would expect salvaging to commence within a three-month period. As a result, Hills Motors would not be able to wait until it has won a contract to then hire staff if it is to fulfil the contract. Hills Motors would instead need to invest speculatively in advance of bidding for the contract in the hope of winning a future contract. If Hills Motors was then unable to win a future contract, there would be no return on this investment. Similarly, to the extent staff are hired prior to the award of a contract, the staff opex occurring during the intervening period would need to be included in the up-front investment estimates (potentially [✂] staffing costs).

Taking this into account gives it a conservative up-front investment in staffing of £[✂] million.

Required up-front investment in staffing: £[✂] million **Required lead time: ~1.5 years**

3.7. Requirement for a high performing proven auction platform

Continuing to use e2e would not be possible

The PFs take as the counterfactual:

> *"We therefore consider the counterfactual of the pre-Merger conditions of competition is one in which Hills Motors would have continued developing its auction platform and remained on the board of directors and a collecting member of e2e."*

As outlined above, rather than the most likely scenario as required at Phase 2, Hills Motors considers this to be the least likely scenario if the counterfactual also presupposes that Hills Motors competes for national contracts (directly in-head-to-head competition with e2e) for three reasons.

- **Contractually infeasible and counter to incentives**. First, if Hills Motors bids for a national contract other than Ageas,[30] it will have to resign from e2e and would no longer be able to use the more established and liquid e2e auction platform. It should be self-evident that there would be no incentive – indeed it would be self-defeating – for e2e members to allow Hills Motors to sell vehicles through the e2e platform. As a basic requirement, the counterfactual must be feasible and consistent with the evidence.
- **Cannibalising own investment is irrational**. Second, if Hills Motors does remain a member of e2e and has access to the e2e platform to sell its vehicles, there is no incentive for it to develop its own auction platform. It would be irrational for Hills Motors to invest in the development of the e2e platform, including in marketing spend to facilitate buyer growth,[31] while simultaneously investing in its own platform, including in marketing spend to facilitate buyer growth, but only cannibalising its investment in the e2e platform. Hills Motors would be duplicating its investment to build two platforms that only cannibalise each other. The counterfactual must at least be logically consistent. If Hills Motors has access to the e2e platform (with substantial liquidity, supply of vehicles and registers buyers), it would make little sense to then use its own, which would be untested and unproven.
- **Inconsistent with counterfactual of Hills Motors competing for national contracts**. Third, if Hills Motors competes for national insurance contracts, it would have to offer a consignment model (in order for Hills Motors to be competitive and meet the preferences and requirements of insurers – see below). In most cases, contracts with national insurers mandate a consignment model and vehicles must be sold through the salvager's own platform (not a third-party platform) in order to satisfy the monitoring associated with an insurance claim and administering the profit share.

Hills Motors confirmed this to the CMA Panel:

<u>**Ian Hill**</u>: "[✄]" [32]

Ian Hill went on to say that the auction was [✄] and [✄]").[33]

For the purposes of assessing Hills Motors' capabilities, we consider the scenario where Hills Motors develops its own auction platform and uses this to sell vehicles, and does not have access to the e2e platform. This is an inherent assumption of the PFs that is at least logically consistent, even if it is the opposite of what Hills Motors has told the CMA would have been most likely to happen (i.e. Hills Motors would have remained a member of e2e, e2e would have continued to bid for national insurance contracts on behalf of its members, and Hills Motors continued to take up its e2e allocation and sell vehicles on the now well-established e2e platform).

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30 And possibly Tesco, given the similar historical context as Ageas.

31 Not only that; impacting further since is the e2e auction cost as well. Page 21

32 Hills Motors Main Party Hearing Transcript, page 16.

33 Hills Motors Main Party Hearing Transcript, pages 5 and 18.

Building capability of own auction very difficult

To compete for a national insurance contract, Hills Motors would need, first, to demonstrate that it could obtain minimum values for the salvage vehicles through its auction platform that would make it competitive with e2e and other salvagers, and, second, then generate competitive values using its own auction. Neither of these are possible (at least within a period of a few years and without significant investment).

Hills Motors would not have any sales data from an auction that has never been launched and is unproven. Hills Motors would not be able to show historic results, how much a vehicle makes on salvage, auction performance and functionality, and auction development over time.

Note that this data realistically could not come from the Ageas contract as Ageas was exceptional and volumes would always have been allowed to go through the e2e platform. Assuming Hills, competing for a national contract, was restricted from accessing e2e, then it would have been forced to use its own platform to sell the Ageas vehicles. However, it would have been extremely difficult to generate any value from an unproven, newly launched auction with no buyers. Ageas did not seek an auction platform and were not seeking the returns from auction in the same way other insurers are, they just wanted green parts.

In order to develop an auction platform with sufficient liquidity to generate returns for the seller involves significant marketing spend. While Hills Motors sell only [✂]-[✂] vehicles a week, the e2e platform sells approximately 2,000 vehicles a week while IAA and Copart sells significantly more. The PFs focus on the £[✂] million spent by Hills Motors on developing its back-up auction. However, Copart spends [✂] times this on salaries for its auction marketing team alone. As Ian Hill stated to the CMA: "[✂]"[34]

Auction performance is driven by buyer volume and selling stock, which together driver higher selling prices. Auction platforms have extremely high indirect network effects making it difficult for new entrants to compete. Hills Motors' auction platform has not yet launched and has no buyers. By comparison, Copart's auction, for example, has:

- [✂] registered buyers, over [✂] of which are active, and close to [✂] new members per month. This has taken Copart approximately 14 years to build this buyer base.
- Annual ongoing marketing staff (Marketing, Vehicle Remarketing & Membership teams) with a total cost of £[✂].
- Marketing spend to draw in buyers of £[✂] per year, cumulative over a 14 year period.

Copart incurs further costs including marketing to drive renewals, system costs such as Lexis Nexis, GDPR cyber security cost, buyer-related claims compensation costs.

While Copart may be a particularly strong performing auction platform, the same principle applies to IAA and e2e, and other established auction platforms. Hills Motors would have no critical mass of buyers and no brand equity to achieve competitive returns for insurers. To do so would take significant time and investment in both marketing and technology (which also drives auction

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34 Hills Motors Main Party Hearing Transcript, pages 5.

performance), and member recruitment will initially be slower and more expensive than competing established platforms.

Hills Motors cannot sell the vehicles of a national insurance contract through its own platform and compete effectively: Hills Motors' own auction platform would not be able provide the insurer with the requisite return to be competitive, it simply does not have the capabilities and would not be able to easily obtain those capabilities without significant investment. This is another key capability that the PFs does not consider in any way.

3.8. Potential requirement for additional services to be provided

To compete for a national insurance contract, salvagers are increasingly expected to provide additional services. Without the capability to provide these services, the salvager may not be competitive or considered a credible competitor. This underpins the entire rationale for the transaction (as Copart has been asked by insurers to provide a green parts service). Copart has been forced over time to provide a wider range of services demanded by the insurers. If it did not do this, it risks losing the contract. Many of these additional services are not reimbursed through increased payments from the insurers.

Specifically, Copart provides:

- **Claims management and settlement** including MIAFTR entry and finance clearance, physically funding & paying the customer on behalf of the insurer & claiming this back, alongside managing an escrow account for payment of total loss settlement payments. This requires a purpose built system for claims settlement, multi-channel communication system compliant with the FCA's consumer duty, vulnerable customer management, data protection (secure data with multi-back-up sites), secure payment facility and funding of claims settlement in advance on behalf of insurance customers. The provision of a full claims management service – including management of finance and MIAFTR entries – involves significant staffing resources due to its compliance heavy nature. Hills Motors does not have the skill set in house to manage this.
- **Engineering services**, including vehicle condition report, desktop engineering, and full engineering service. Hills Motors provides only very limited engineering services (a vehicle condition report) and not an engineering service, and has no experience providing it. In principle, Hills Motors could provide this through a third-party. These are provided to the majority of national insurance customers.

While these additional services are not demanded or required by *all* insurers – or offered by all salvagers – they are very important for some insurers and, without these services, it would be very difficult to compete to supply some national insurance contracts.[35] The PFs are clear: none of Copart's customers consider Hills Motors to have the capabilities to meet their requirements. For some insurers, these additional services will be one of the more important criteria that Hills Motors cannot meet (among many others), thereby limiting the pool of customers that Hills Motors can

35 Insurers impose stringent SLAs that salvagers must meet associated with these additional services confirming how important these additional services are to the insurer.

compete for (and thus the extent of possible competition between the Parties even with the investment outlined above) if Hills Motors does not invest to provide these services.

[✄]

	Claims management	**Claims settlement**	**Engineering services**
[✄][36]	[✄]	[✄]	[✄]
[✄][37]	[✄]	[✄]	[✄]
[✄][38]	[✄]	[✄]	[✄]
[✄][39]	[✄]	[✄]	[✄]
[✄][40]	[✄]	[✄]	[✄]
[✄][41]	[✄]	[✄]	[✄]
[✄][42]	[✄]	[✄]	[✄]
[✄][43]	[✄]	[✄]	[✄]
[✄][44]	[✄]	[✄]	[✄]
[✄][45]	[✄]	[✄]	[✄]
[✄]	[✄]	[✄]	[✄]

To provide a full **claims management and settlement service** costs across all of Copart's customers involves [✄] staff with annual salary costs of £[✄] million. The claims advisers are trained in claims management, regulations and compliance. Total costs of providing the service are approximately £[✄] million annually.

36 Hills Motors does not meet its requirements (PFs: 8.89) and would not allow use of sub-contractors (PFs: 8.43).

37 Hills Motors does not meet its requirements (PFs: 8.89). Sufficient competition would remain post-merger (PFs: 8.92).

38 Hills Motors does not meet its requirements (PFs: 8.89), would not allow use of sub-contractors (PFs: 8.43), Parties not close competitors (PFs: 8.91).

39 Hills Motors does not meet its requirements (PFs: 8.89), would not allow use of sub-contractors (PFs: 8.43), Parties not close competitors (PFs: 8.91).

40 Hills Motors does not meet its requirements (PFs: 8.89), would not allow use of sub-contractors (PFs: 8.43), Parties not close competitors (PFs: 8.91).

41 Hills Motors does not meet its requirements (PFs: 8.89), would not allow use of sub-contractors (PFs: 8.43), Parties not close competitors (PFs: 8.91).

42 Hills Motors does not meet its requirements (PFs: 8.89) and Parties not close competitors (PFs: 8.91).

43 Would not allow use of sub-contractors (PFs: 8.43) and Parties not close competitors (PFs: 8.91).

44 Hills Motors does not meet its requirements (PFs: 8.89) and Parties not close competitors (PFs: 8.91).

45 Does not consider Parties close competitors (PFs: 8.91).

While Hills Motors would not need [✂] staff for a single national insurer, it would need to invest in fixed costs of developing the expertise of claims management, hire dedicated staff and premises to accommodate them. Hills Motors has never been involved in this area before and has no relevant expertise and so this would also represent a fundamental shift in its business model.

Even if we assume Hills Motors could do this for ~10% of the costs Copart incurs, this would be equivalent to £[✂]k. Where this is required by an insurer, it would be stipulated in the tender (with salvaging typically starting within three months of contract award) meaning that this would represent further up-front investment.

To provide a full **engineering service**, Copart employs approximately [✂] engineers with a salary cost of £[✂] million and a total cost of £[✂] million. These are highly qualified and licensed engineers (AQP qualified) that need to be licensed and trained every three years (£[✂] pp). While Hills Motors provides some engineering processing functions, these are limited relative to the additional services (full engineering) that Copart provides. While Hills Motors would not need to employ [✂] engineers, as with claims management, these are specialised and skilled staff that are difficult to hire and that Hills Motors has no expertise in currently so this would also represent a fundamental shift in its business model.

Even if we assume Hills Motors could do this for ~10% of the costs Copart incurs, this would be equivalent to £[✂], which would again represent up-front investment to develop the capability for a tender.

Required up-front investment in additional services: £[✂] million
Required lead time: ~1 year

3.9. Limited scope for funding and debt capacity

The conclusions of the PFs take are predicated on Hills Motors competing for national insurance contracts without recognising the implications of such a scenario. While almost all customers have indicated that Hills Motors does not have the capabilities to supply them, rather than understand those requirements and Hills Motors limited capabilities to meet them, the PFs speculate and make assumptions without any substantiating evidence.

A closer examination of the requirements of supplying a national insurance contract show that Hills Motors would have to make up-front investments in transporters, site capacity, dismantling equipment and staffing. Together these investments would be between £29-49 million. An insurer would typically expect salvaging to commence within a three-month period of contract award and so there would be very limited scope to make these investments gradually.[46] This range does not consider this significant additional required investment in creating a liquid auction platform that

46 While investment in transporters and equipment could potentially be spread over the two to three year lead time for the equipment to be delivered subject to a proportion of payment being made on delivery, for the site acquisition this would not be possible (as outlined below, leases are typically ill-suited to this sector).

generates high sales values or the possible additional services required to meet the requirements of some insurers. Thus, the estimate investment is highly conservative.

We anticipate that the CMA may seek to dismiss this evidence by speculatively claiming, for example, that an insurer could sponsor entry or similar. However, not a single customer has raised concerns with the transaction. Indeed, evidence provided to the CMA indicates that insurers overwhelmingly believe the transaction will have a positive impact on competition. Thus, in this context, it is unclear why customers would ever feel they need to sponsor entry.

Required up-front investment in…	
Transporters	**£[✂]m**
Site	**£20-40m**
Dismantling equipment	**£[✂]m**
Staffing	**£[✂]m**
TOTAL	**£29-49m**

In order to fund this up-front investment, Hills Motors would without question need to borrow the vast majority of the required funds. Hills Motors cannot fund this investment through earnings or cash on hand. In its latest financial accounts, Hills Motors' annual earnings are only £[✂] million.[47] Hills Motors historically have never taken on long-term debt. Indeed, any of the up-front investment items (transporters, site, dismantling equipment, staffing) on a standalone basis would involve greater borrowing than Hills Motors has ever taken on at any point in its history.

In this context, of a company that has typically taken on no long-term debt, the assumption inherent in the PFs that Hills Motors would suddenly fundamentally shift its business model to take on this significant debt, is not realistic or credible. The relevant counterfactual must be scenario that is remotely likely not a speculative, unfounded paradigm shift.

Indeed, no evidence has been provided in the PFs to suggest that Hills Motors could fund this investment. If the CMA has obtained such evidence as part of its investigation, the Parties request that this is shared so that Parties have a fair chance of rebutting this evidence.

Nonetheless, the Parties analyse what taking on this level of debt would mean for Hills Motors.

Figure 2: Hills' long-term debt: currently and supplying a national contract[48]

[✂]

This debt (using the bottom end of the range estimated) would be equivalent to [✂]x Hills Motors' EBIT and would involve Hills Motors increasing its leverage (the proportion of debt to equity)

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47 While Hills Motors' turnover was £[✂] million, this is not indicative of its debt capacity as it had COGS of £[✂] million and a further £[✂] million in fixed costs. Other options such as raising money via equity, access to capital markets, forming a partnership or VC money are far removed from anything Hills Motors has ever considered and are unrealistic.

48 Long-term debt is creditors with amounts owed greater than one year.

from [✂]% to [✂]%.[49] Not only does Hills Motors not have the debt capacity to make such up-front investment, this debt would be taken on speculatively without any prospect of a return (i.e. Hills Motors would still need to win a national insurance contract).

Figure 3: Hills Motors does not have the debt capacity for such up-front investment

[✂]

The conclusions in the PFs presuppose that Hills Motors would secure this debt financing, which is not certain given the risk inherent in the project (see below) and debt capacity of the company.

This huge increase in debt and risk that the PFs presuppose are in the context of the ownership of Hills Motors having no desire to grow in this way, to compete for national insurance contracts or take on such risk. Ian Hill operates a family run small business with personal assets at stake, not a large corporation with more 'risk-loving' managers aiming to maximise value for shareholders. This personal situation and risk-aversion, which is hugely instructive of the likelihood with which Hills Motors would compete for a national insurance contract has been ignored:

Ian Hill: "[✂]"[50]

3.10. An irrational investment decision

On any standard measure of investment appraisal, the assumptions inherent in PFs make no sense. For example, suppose Hills Motors appraises the investment to 'step-up' its capabilities to enable it to compete for a national insurance contract uses a simple NPV (and payback period) model. The following factors must be considered and what the available evidence suggests about each:

- **Unprecedented up-front investment**: as noted above, the investment required is larger than Hills Motors has ever made before by many multiples. As a result, Hills Motors would not be able to wait until it has won a contract to then hire staff if it is to fulfil the contract. Hills Motors would instead need to invest speculatively in advance of bidding for the contract in the hope of winning a future contract. If Hills Motors was then unable to win a future contract, there would be no return on this investment.
- **Low likelihood of future cash flows**. Hills Motors would need to increase its capabilities in advance, bid for a national insurance contract and win a contract before any earning any cash flows from the project. These future cash flows are therefore entirely predicated on Hills Motors winning a national insurance contract. The likelihood of Hills Motors winning a national insurance contract is already limited by the fact that Hills Motors would necessarily be operating a sub-contracting model that over half of the insurers have rejected.[51] For those insurers that would consider using a network, Hills Motors may not

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49 Debt relative to EBIT is total debt (short- and long-term). Leverage is presented as standard gearing ratio (total liabilities/(total liabilities + total equity)).

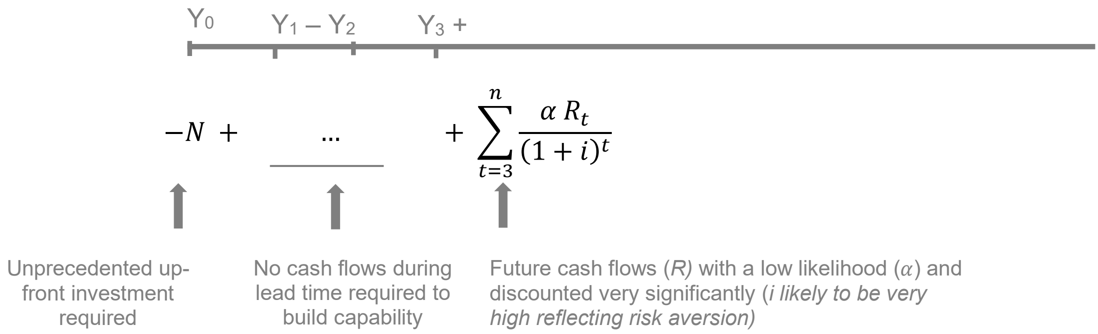
50 Hills Motors Main Party Hearing Transcript, page 21.

51 According to the PFs, the majority (seven of 13) insurers spoken to the CMA indicated that it would not be acceptable for national coverage to be provided via sub-contracting.

be a suitable alternative, even after investment, for other reasons.[52] Thus, the likelihood of Hills Motors winning a national contract is very small.[53]

- **Very high risk-adjusted discount rate**. The discount rate accounts for two elements, the time value of money and the level of risk involved in an investment. With regard to the latter, this can capture the highly uncertain and low likelihood of future cash flows *and* the risk aversion of Hills Motors. The higher the perceived risk, the higher the discount rate. In the context of Ian Hill comments noted above with regard to taking on risk, the highly uncertain and low likelihood of future cash flows must be discounted significantly.[54] This is supported by the absence of any long-term debt taken on by Hills Motors historically.

Figure 4: NPV assessment



Any parameterisation of this shows that while Hills Motors needs a much higher certainty equivalent cash flow in the future to undertake the investment, the expected cash flows are actually very small and the risk-adjusted discount factor (and risk premium) very high, making those possible future cash flows worth less to Hills Motors in present value.

Together these factors strongly point to the assumptions inherent in the conclusions in the PFs being not just remote, but completely speculative and far-fetched. Under no circumstances would

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52 For example, the PFs do not consider how Hills Motors could compete to supply DLG, an existing e2e customer, in competition with e2e while continuing to sell on the e2e platform. Such a situation would be unfathomable (indeed e2e would never approach Hills Motors independent of e2e). More generally, according to the PFs, Hills Motors would be both a member of e2e and competing against e2e so the likelihood of Hills Motors winning a national contract is based on an insurer approaching Hills Motors (rather than e2e) and awarding a contract to Hills Motors instead of e2e (which further reduces the likelihood of Hills Motors competing and winning for national contracts). Further, Hills Motors would not be competitive for many contracts given its greater transport costs and use of collection agents (even with expansion to an additional site).

53 To understand this likelihood, there is no evidence in the PFs of the Parties ever competing, with only one insurer even pointing to *possible* competition between the Parties (one of 37 auto insurers listed by the ABP). Thus only 3% of insurers consider competition possible and for this 3% Hills Motors must still win the contract.

54 This can be thought of in certainty equivalent terms. The certainty equivalent is the amount of money an investor will accept now instead of taking a risk to get more money in the future. Ian Hill has a very high certainty equivalent because he is less willing to risk everything he has built up over many years for the prospect of future returns from another national insurance contract. The future cash flows from a hypothetical national insurance contract become certainty equivalent cash flows, the probability-weighted value of each cash flow (αR_t above) discounted by a very high risk premium (i.e. i above is very high). As a result, Hills Motors requires a much higher future cash flow to undertake the investment.

Hills Motors ever undertake these investments with such a significant and unprecedented up-front investment, with a significant lead time before it can compete, with such uncertainty over future cash flows (with a high chance that none would be achieved), and with such a significant discount rate reflecting Hills Motors risk aversion.

In the context of national insurance customers overwhelmingly indicating that the Parties do not compete, that Hills Motors is not capable of meeting their salvaging requirements, and that the merger will be positive for competition, the PFs do not consider how Hills Motors might actually meet the capabilities required by customers going forward. Without such an assessment, the PFs do not meet the requisite standard for showing that Hills Motors will compete effectively in the future, without which there is no basis to support an SLC on a balance of probabilities. A proper assessment of what would be required for Hills Motors to obtain the capabilities to compete shows that this would involve a radical and speculative shift in its existing business model, a huge increase in risk and debt that Hills Motors has never even contemplated before, and which no evidence suggests it would take on going forward.

3.11. Debt repayments would be significant

Taking account of current borrowing rates, the size of Hills, its cash on hand, and the risk associated with such a large increase in activity and borrowing relative to historical borrowing (with virtually no experience or history in commercial lending), with no return except if a contract is won (and the relatively low likelihood of winning a contract), the cost of debt is likely to be high. Hills Motors could take out a commercial investment mortgage or a collateral-based commercial loan. Given the risk and scale of borrowing involved, borrowing rates are likely to be high regardless of the type of borrowing. We estimate the likely cost of debt for Hills Motors to be approximately 8-10%.[55]

As a result, using the bottom end of the range for required investment (£29 million), Hills Motors would be subject to annual debt repayments of £[✂] million (or £[✂] per month). These debt payments will significantly increase Hills Motors' credit risk. In the context of the liabilities that Hills Motors will need to take on (see below), the loss severity and the debt repayments may suggest significantly increased credit risk. Given Ian Hill stated risk aversion and high certainty equivalence, any increase in default or insolvency risk would be avoided at all costs. The PFs do not seem to consider this implication of Hills Motors addressing its capability gap.

Below we also consider the impact of these debt repayments, alongside other material cost differences, on Hills Motors' competitiveness for national insurance contracts.

Figure 6: Annual debt repayments assumed by PFs

[✂]

55 The curve on UK government debt shows yields on short-dated gilts of close to 5% while longer dates yields are 4.5-4.6%, while spreads on top of this are likely to be high given the circumstances on Hills Motors outlined. Given recent sterling corporate bond issuance yields for SMEs and typical hire purchase rates, 8-10% seems conservative.

Hills Motors' long-run pricing must enable it to cover its cost of capital. Under the counterfactual, Hills Motors would *start* competing, or competing more, against existing suppliers of national insurance contracts. In order to raise debt finance, it must show a return on capital and must be a viable business as current prices.[56] Furthermore, prices will reflect the length of the contract (which is typically long-term, 3-5 years[57]). As shown above, even at the bottom end of the range of estimates for required investment, annual debt repayments are likely to be £[✂]. Hills Motors will need to cover these debt payments in bidding for a long-term national insurance contract with typical duration of 3-5 years.

The results show that Hills Motors' estimated revenue from national insurance contracts would not be sufficient to cover its debt repayments.

Figure 5: Hills Motors cannot cover cost of capital from contract (cost per vehicle)[58]

[✂]

In order to be competitive, Hills Motors would therefore need to have a substantially lower cost base, which as the subsequent points show is likely not the case.

3.12. Required advanced charges would increase short-term debt

National insurance contracts require that salvagers make advanced payments for recovery and storage charges prior to the release of a vehicle. These are often statutory charges and reflect the cost incurred by the recovery agent that collected the vehicle. For example, when a vehicle is involved in a collision it is taken by roadside recovery agents to a place of storage. When the vehicle is assigned to the salvager, it is required to make payment of recovery and storage charges on behalf of the insurer. Vehicles are not released by the third party holding them until the payment has been made.

The insurer pays back the salvager. Salvagers that supply national insurance contracts must therefore have the capability to provide this short-term credit facility. Essentially this represents a large increase in trade credit that salvagers must fund from their own cash flow and must absorb on their balance sheet as additional working capital.

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56 Given the prospective nature of the investment, any dismissal of this assessment (i.e. demonstrating a return on capital) on the basis of only marginal costs affecting prices would be flawed.

57 PFs, paragraph 12.21.

58 Given Hills Motors reliance on outsourced salvage agents, revenue generated from the contract is assumed to be [✂]% of that of Copart's core revenue to account for the reduced revenue that can be generated. Given the differential in revenue generated from Hills Motors direct volumes and that collected by salvage agents, this seems highly conservative. If this adjustment is not made, revenue for all contracts remains below revenue required to cover cost of capita with exception of [✂] (£[✂]) and [✂] (£[✂]).

Table 4: Advanced charges for national insurance contracts

Year	Recovery	Storage	Other[59]	Total Average
2019	[✂]	[✂]	[✂]	[✂]
2020	[✂]	[✂]	[✂]	[✂]
2021	[✂]	[✂]	[✂]	[✂]
2022	[✂]	[✂]	[✂]	[✂]
2023 YTD	[✂]	[✂]	[✂]	[✂]

For Hills Motors to supply a national insurance contract, it would need to have the cash flow to fund these advanced payments. These advanced payments can be significant. For example, over the course of the full year 2022, the Hastings contract had advanced charges of £[✂] million while AXA has advanced charges of £[✂] million. DLG has even larger advanced charges of approximately £30 million. Thus, the salvager must be able to provide this short term debt – and take on these short-term liabilities – across the year.

Table 5: Advanced charges for each of Copart's national insurance contracts

Insurer	Approx. volume	Advanced charges (2022)
[✂]	[✂]	[✂]
[✂]	[✂]	[✂]
[✂]	[✂]	[✂]
[✂]	[✂]	[✂]
[✂]	[✂]	[✂]
[✂]	[✂]	[✂]
[✂]	[✂]	[✂]
[✂]	[✂]	[✂]
[✂]	[✂]	[✂]
[✂]	[✂]	[✂]

The extent of the additional working capital required to service a national insurance contract varies across contracts.[60] For example, [✂].[61] As a result, the impact on working capital can be significant.

3.13. Substantial and potentially prohibitive contractual and contingent liabilities

Hills Motors is individually responsible for liabilities under a national insurance contract

Under e2e, the members are collectively responsible for liabilities under a national insurance contract (reflecting in shared contributions to the e2e bond). This was the rationale for setting up e2e in the first place. None of the constituent members were capable of taking on the liabilities of

59 Other costs include use of specialist equipment, cranes, off-road incidents, extra staff, etc.

60 Working capital is calculated as current assets less current liabilities.

61 The average time for sale for [✂] is [✂] days even when excluding vehicles that took longer than [✂] days ([✂]% of vehicles) to clear. However, these time periods would likely be very significantly longer for Hills Motors with an auction platform that has not even launched and has no registered buyers.

a large national contract themselves, and only through the collective risk sharing (including through the bond payments made by e2e members to cover the liabilities associated with a national insurance contract) were they able to participate in tenders for large national insurance contracts.

With Hills Motors competing for national insurance contracts itself, it takes on the full liabilities. Supporting this, for example:

[✂]

Contractual liabilities are significant

Total potential liabilities for national insurance contracts range from £[✂] million (e.g. [✂]) to £[✂] million ([✂]) annually based on asset value to the insurer. As outlined above, if Hills Motors were to win a national contract, it would be liable for the full amount of any incurred costs, i.e. Hills Motors would take on these full potential liabilities.[62] For example, most insurers have a strong preference for the consignment model as it provides for higher returns.[63] For Hills Motors to compete for national insurance contracts, it would likely have to offer the consignment model. Under the consignment model, Hills Motors would act as an agent to the insurer's assets and become liable for any damage to those assets.

Major liability incidents are not uncommon, for example Motorhog suffered a fire in August 2020 with 900 cars destroyed[64] and there have been [✂]. Fire risk is particularly high due, for example, to vehicles self-combusting.

As an illustration of how these liabilities need to be covered, under e2e, a bond arrangement was in place where each collecting member must contribute a bond to cover these liabilities (equivalent to the purchase value of the vehicle (% of the PAV)). This covered for losses outside the scope of insurance, lack of insurance or voided claim. For example, Hills Motors still has a £[✂] bond held by e2e from when it was a member. However, this was only Hills Motors' *shared contribution* of the potential liabilities.

Under circumstances where Hills Motors wins a national contract, Hills Motors is *individually liable* for the total potential liabilities, including vehicles processed by outsourced salvage agents (and collected by pick-up agents), which it does not have control over. This is one of the key reasons

62 These liabilities reflect damage in transit, damage at operating centre, property damage during collection process, road traffic accidents, loader damage while in operating centre, liability for serious misdescription (e.g. wrong category), fire incidents, stolen vehicles.

63 See customer views submitted by Copart indicating that almost all insurers prefer the profit share model and the reasons provided by the insurers (higher returns). The PFs dismiss these customer views on the basis that Copart asked the question and referenced the merger, but, first, the CMA appears to have made no attempt to verify this evidence with the limited number of insurers in the market and, second, the PFs provide no reasoning why this might lead to biased results for a question that asks: *When selecting a supplier to collect and process salvage vehicles on your behalf, which of the following do you prefer?* With response options: *The salvager to sell the vehicle on your behalf via auction to the highest bidder returning you a proportion of the auction value*; or *The salvager to purchase the vehicle from you outright for a fixed price*. Followed by a question that asks: *And why do you prefer this model?* Free text.

64 See: https://www.examinerlive.co.uk/news/local-news/motorhog-speak-out-after-900-18706223

why e2e exists: the collective sharing of risks so that Hills Motors is liable for only the £[✂] not the multiple millions across the whole membership.

Hills Motors could potentially seek to mitigate this risk by seeking a bond from the outsourced salvage agents. However, the possibility for the outsourced salvage agents to provide a bond to Hills Motors for Hills Motors' benefit in competing for national contracts while simultaneously providing a bond to e2e is highly unlikely. The outsourced salvage agents would have no incentive to do so. Under Ageas, Hills Motors has not sought a bond and so is liable for the full amount. Neither Hills Motors nor Copart considers this sustainable when competing for other national insurance contracts (the exceptional nature of the Ageas contract has allowed this).

Note that Hills Motors can insure to cover these costs. However: first, as with the e2e bonds, there are significant liabilities outside the scope of insurance or resulting from voided claims that need to be covered and; second, Hills Motors insurance premiums are already £[✂] annually, having increased by [✂]% over only two years (2020-2022) and this reflects some implicit self-insurance that would not be possible on significantly increasing volumes; and third, Hills Motors would likely need to significantly increase its insurance cover.[65]

Hills Motors does not have the financial capability to take on these liabilities and this is not recognised or discussed at all in the PFs. In the context of customer indicating that Hills Motors does not have the capability to meet their requirements, no assessment has been undertaken of the capabilities that it lacks and the ability for it to meet them.

Contingent liabilities are significant

National insurance contracts have very stringent SLAs in place that salvagers need to meet. Where these are not met, the salvager is subject to severe penalties and charges (or 'service credits'). If Hills Motors competes for and wins a national insurance contract, it would be liable for these penalties, irrespective of whether it is itself at fault or one of the sub-contracting salvage agents. This means that Hills Motors either has to take on the contingent liability or must seek a substantial bond from the sub-contracting salvage agents to cover any losses (which as described above is very difficult).

These SLAs can be extensive. For example, [✂] contract includes [✂] separate SLAs while [✂] has [✂] plus [✂] KPIs that need to be met. These include collection, processing, destruction, compliance and IT, and support services. As an illustration:

Illustrative SLAs imposed in national insurance contracts

[✂]

There detailed and stringent requirements impose significant staffing resource and administrative costs on the salvager. For several of the SLAs above, Hills Motors does not even have the capability to comply, let alone meet the performance or time requirements. To do so, would involve a fundamental shift in its business model. Hills Motors is not set up to operate with extensive office

65 Requirements can include: public liability insurance coverage of £10 million, employers liability of £10 million, loss of injuries or damage of £5 million.

and administrative support or to offer the complex web-based monitoring systems and apps that the insurers require.

If these SLAs are not met, the salvager can be subject to a penalty (or 'service credit') for each of those it fails to meet. The level of penalty varies across insurer and SLA but can be as high as 20% of the fees that the salvager is paid in that month. For example, Copart was paid £[✂] in March by [✂] and so, if it did not meet even one of the SLAs, Copart would be liable to pay a penalty of £[✂] for that month. Others are less severe but still very substantial. For example, [✂] applies to [✂]% of Copart revenue in that month. April revenue was £[✂] so the penalty would be £[✂]. Equivalent to the revenue generated from sale of multiple vehicles. These penalties are cumulative across SLAs.

At the time of a contract, a salvager will undertake stress testing of possible penalties to understand the repercussions if things start to go wrong (for example, if sites are full or if transporters not operational).

For Hills Motors, it is liable for these penalties if sub-contractors pull out or cannot collect a vehicle. Supplying a national contract using a network of sub-contracts but being individually liable is not feasible. This is why e2e was created.

Other costs and liabilities

The administrative burden, additional costs and liabilities associated with supplying a national insurance contract are significant and have not been considered by the CMA in the PFs. These include:

- Regular audits for services, GDPR & data security.
- Processing of personal data on behalf of the insurer and as such significant risk and potential penalties in the event of a breach.
- Obligated to meet Science Based Targets for meeting Net-Zero.
- Measurement of Scope 1, 2 & 3 targets.
- Expectation that a salvager holds ISO standards for compliance;
- Engineering qualifications (AQP).
- Expected to help insurers reduce their leakage (i.e. claim costs).
- surge-management (dedicated team) including roamer-drivers in the event of regional incidents that lead to localized surges in numbers of vehicles.
- Expectation that Copart follow FCA regulations on Consumer Duty and management of Vulnerable Customers.
- Management of Corporate Risk Register
- Disaster Recovery Business Continuity Provision
- Expectation to be compliant with Modern day slavery requirements, Bribery, Corruption and Sanctions list compliance.
- Environmental penalties if contamination caused by Copart – activities suspended if contamination assessed which brings operational risk and remains closed until site remediated.
- Road blockages/single-site closure due to incident can lead to operational restrictions.
- Hazardous waste management penalties.

- Traffic commissioner regulation (e.g. bridge-strike/ TC enforcement action in Bristol and North-East)
- Compliance with Health & Safety Executive
- Compliance with Trading Standards Regulation

Copart has significant staffing teams to provide these and ensure compliance to the requisite standards demanded by insurers. Hills Motors has very limited capability to take on this administrative burden, ensure compliance with these provisions and assume the potential liabilities. For most insurance contracts, Hills Motors would need to demonstrate these capabilities in advance of being awarded the contract and so would need to invest in and develop this capacity in advance of bidding.

4. Conclusion

The CMA's PFs conclude that Hills Motors can readily compete for national insurance contracts. This is despite customers overwhelmingly indicating that Hills Motors is not capable of meeting their requirements. The PFs do not examine Hills Motors capabilities and customer requirements in any detail to understand whether Hills Motors could meet them going forward. A closer assessment of these requirements and the steps Hills Motors would need to take to meet those requirements clearly shows that Hills Motors would not be able to compete for a national contract, and confirms that the Ageas contract is exceptional and not indicative of Hills' capabilities to supply other insurers. Based on this, the evidence points to there being no possibility of an SLC arising from the merger.