

Anticipated acquisition by G4S plc of Global Solutions Limited

ME/3493/08

The OFT's decision on reference under section 33(1) given on 2 May 2008. Full text of decision published 28 May 2008.

Please note that square brackets indicate figures or text which have been deleted or replaced at the request of the parties for reasons of commercial confidentiality.

PARTIES

1. G4S plc (G4S) operates worldwide in two sectors, namely the provision of security services (including manned security, security systems and care and justice services) and the provision of cash services (that is, secure transport and storage of cash and valuables between premises and the processing of cash within the secure premises of the company).
2. Global Solutions Limited (GSL) is divided along three business divisions: GSL Care and Justice Services; GSL Integrated Services; and GSL Data and Managed Services. The only division which is relevant to this assessment is GSL Care and Justice Services, which consists of four specialist units offering services in the UK (as well as operations in South Africa and Australia): offender management (management of prisons and rehabilitation) and immigration services (management of immigration detention centres); prisoner escort and court custody services; police services (including custody support services); and children's services (including secure training centres). In 2006, GSL generated a worldwide turnover of around £402.4 million (of which approximately £[] was generated in the UK).

TRANSACTION

3. G4S proposes to acquire the entire issued share capital of DeFacto 1119 Limited, the holding company for GSL.
4. An informal submission was deemed received from G4S on 10 March 2008. The 40 day administrative deadline expires on 7 May 2008. The 45 day statutory deadline expires on 20 May 2008.¹

JURISDICTION

5. The aggregate Community-wide turnover of each of the parties exceeds €250 million and the parties combined aggregate worldwide turnover exceeds €5,000 million. Although GSL achieves more than two thirds of its Community turnover within the UK, G4S does not. Therefore, the undertakings concerned do not each achieve more than two thirds of their aggregate Community-wide turnover within one and the same Member State, as envisaged by Article 1(2) of the EC Merger Regulation² (ECMR). The concentration therefore meets the requirements of a Community dimension pursuant to Article 1(2) ECMR.
6. On 8 February 2008, the parties submitted a Form RS to the European Commission, requesting the referral of this transaction to the UK pursuant to Article 4(4) ECMR. On 7 March 2007, the European Commission agreed to the Article 4(4) request from which date the OFT assumed jurisdiction.
7. As a result of the transaction, the parties have ceased to be distinct.
8. The UK turnover of GSL was approximately £[] in 2006. The turnover test pursuant to Section 23(1)(b) of the Enterprise Act 2002 (the Act) is therefore satisfied. The OFT believes, therefore, that it is or may be the case that arrangements are in progress or in contemplation which, if carried into effect, will result in the creation of a relevant merger situation.

¹ Calculated according to section 34A of the Enterprise Act 2002.

² 139/2004/EC, OJ L24, 29.1.2004

BACKGROUND

9. G4S and GSL have been party to a number of transactions in the past which have been examined by the UK competition authorities or the European Commission.
10. Group 4 Falck acquired The Wackenhut Corporation (TWC) in 2002. At the time, TWC's subsidiary, Wackenhut UK Ltd, provided custodial and facility management services in the UK. TWC also provided custodial services in the UK through the Premier Custodial Group, a joint venture company it had formed with Serco. Group 4 Falck operated in this segment through its then subsidiary, GSL. The Competition Commission (CC) examined the acquisition and identified four relevant markets: design, construction, management and finance (DCMF) contracts for prisons, management only (MO) contracts for prison services, MO services for immigrant detention centres (IDCs) and DCMF contracts for secure training centres (STC). The CC also considered the market for the provision of prisoner and immigrant detainee transport services. The CC ultimately concluded that there were no competition concerns arising from Group 4 Falck's acquisition of TWC in respect of any of these markets.
11. In 2004, Group 4 Falck disposed of GSL to two private equity investors, Cognetas Fund and Englefield Capital, before the completion of the merger between Securicor and Group 4 Falck. The European Commission concluded that no substantive competition issues were raised by that disposal.³
12. The 2004 merger between Group 4 Falck and Securicor which resulted in the creation of G4S was examined by the European Commission.⁴ The Commission did not consider justice services, because these had been de-merged into GSL prior to its disposal to Cognetas Fund and Englefield Capital. The Group 4 Falck/Securicor transaction was cleared subject to a number of divestments in the areas of cash-in-transit and manned guarding services. These markets are not relevant to the current transaction.

³ Case COMP/M.3482.

⁴ Case COMP/M.3396.

MARKET DEFINITION

Product scope

13. The merging parties overlap in the provision of certain types of care and justice services in Great Britain, in particular:
 - i. The operation and construction of adult custodial facilities (prisons)
 - ii. The operation and construction of youth justice facilities
 - iii. The provision of support services to police forces (including the operation and construction of police custody suites), and
 - iv. The secure transportation of offenders, immigrants and asylum seekers.

In addition, both G4S and GSL have bid to provide electronic tagging and monitoring services in Great Britain, although only G4S provides these services at present.

14. Prison custodial services comprise a diverse range of services which historically were carried out by the government. In Great Britain, the first prison to be put out to tender to the private sector was HMP Wolds in 1992. At this time, the contracting authority and the incumbent supplier of services for the operation of prisons were one and the same. An important change in the regulatory framework occurred in 2004, when the British government separated the management of prisons from the procurement of custodial services. The former was assigned either to Her Majesty's Prison Service (HMPS) or to private contractors. The latter function became the responsibility of the National Offender Management Service (NOMS), a newly created agency which is currently part of the Ministry of Justice.
15. The OFT understands that in Scotland the separation of functions is less defined and at present the Scottish Prison Service (SPS) manages custodial facilities and also procures care and justice services. The Scottish Executive recently withdrew Bishopbriggs prison from a public tender process and awarded the contract directly to SPS and the OFT understands that the policy of the Scottish Executive going forward will be for all new prisons to be operated by the SPS. In Northern Ireland, there is no involvement of the private sector in custodial services. The OFT understands that the outsourcing of care and justice and, in particular, custodial services to the private sector is very limited in other European

countries. The countries, other than Great Britain, where the outsourcing of such services is most prevalent are the USA, Canada, Australia, New Zealand and South Africa. The outsourcing of custodial services is still, in this sense, a relatively immature market.

16. The OFT understands that this sector will undergo significant expansion in Great Britain in the next few years. This will result in a number of contracts for the construction and operation of new prisons being put out to tender over the next five years. A number of MO contracts for the operation of existing prisons may also come up for tender. The OFT received evidence indicating that the expansion in the provision of adult custodial services is likely to have a knock-on effect causing an increase in demand for the other care and justice services.
17. The parties submit that, from a demand-side perspective, there is some substitutability between different types of care and justice services. Prisoners may, for example, be held temporarily within secure police accommodation when prisons are overcrowded. Similarly, secure facilities can be reconfigured to cope with increases in demand for particular types of custody. However, the parties acknowledge that this demand-side substitutability is relatively limited. For example, government entities have to operate within the constraints of primary legislation, differing government policy guidelines, legal requirements and judgments of the courts when allocating detainees to prisons, youth facilities, immigration removal centres and police facilities. Accordingly, from the evidence available, the OFT concluded that demand-side substitutability between different types of care and justice services is limited.
18. The parties also argue supply-side substitutability between different types of care and justice services and between care and justice services and other kinds of facilities management services. The evidence received by the OFT suggests that supply-side substitutability between different care and justice services may be asymmetric, in that it is easier for a company providing prison operation and management services also to provide other types of care and justice services (in particular because the training requirements for staff are very similar), but that it is much less easy to make the transition the other way. The OFT acknowledges that some of the skills and experience of a facilities management services provider may be common to those of a care and justice service provider.

19. The OFT has also considered the different bases upon which care and justice services are outsourced. Prison services in Great Britain may be outsourced to the private sector either on the basis of a public private partnership (PPP) (typically in the form of a private finance initiative (PFI)) or, alternatively, on a management-only (MO) basis. The parties submit that, although there are differences between PFI and MO contracts, the type and range of care and justice services required under each contract are broadly similar. The parties argue that, in relation to the provision of a particular type of care and justice service, no distinction should be made between contracts for such service awarded on a PFI or an MO basis. The parties submit that a care and justice services provider operating a PFI contract would have no difficulty operating a management-only contract and that the reverse is also true because any provider of care and justice services wanting to provide those services on a management-only basis could find a construction and/or finance partner with whom to form a consortium to bid for a PFI contract.

20. PFI and MO contracts have different design and management regime requirements. The requirements for bidding on each contract differ and a more diverse range of tasks is required under the PFI regime. Accordingly, while the OFT has not received any evidence to dispute the parties' argument that it would be relatively easy for an existing PFI provider of a given care and justice service to undertake an MO contract for the same service (on the basis that MO services are a sub-set of those provided under a PFI contract), the evidence on whether the reverse is also the case is more mixed. Therefore, on the basis of the evidence available to it, the OFT has taken a cautious approach and concluded that provision of care and justice services under the PFI and MO regimes represent separate frames of reference.

21. On the basis of the evidence on demand-side and supply-side substitutability between different care and justice services and between services provided under PFI and MO contracts, the OFT has taken a cautious approach and considers the transaction on the basis of the following frames of references:
 - i. operation of adult custodial facilities (prisons) under MO contracts
 - ii. operation and construction of adult custodial facilities (prisons) under PFI contracts
 - iii. operation of young offender institutes (YOIs) under MO contracts

- iv. operation and construction of YOIs under PFI contracts
 - v. operation and construction of Secure Training Centres (STCs) under PFI contracts
 - vi. operation of immigration removal centres (IRCs) under MO contracts
 - vii. operation and construction of IRCs under PFI contracts
 - viii. operation of police custody suites under MO contracts
 - ix. operation and construction of police custody suites under PFI contracts
 - x. secure transportation of offenders, immigrants and asylum seekers
 - xi. provision of electronic tagging and monitoring services.
22. This approach is consistent with that taken by the CC in its inquiry into the Group 4 Falck/WTC transaction. However, given the lack of competition concerns arising in relation to any of the narrow frames of reference identified above, it has not been necessary for the OFT to conclude on the precise market definition in this case.

Geographic scope

23. The parties overlap in the provision of care and justice services in Great Britain. Contracts for the provision of these services are awarded throughout Great Britain. The parties submit that the market for these services is at least the whole of Great Britain and may be wider because providers of care and justice services operating in North America, South Africa and Australia can bid for contracts in Great Britain and have done so in the past. The parties argue that it is not necessary to have an office or other physical presence in a particular country in order to mount a credible bid.
24. The OFT considers that companies supplying care and justice services in one part of Great Britain are an immediate supply-side constraint on companies bidding for such services in another part of Great Britain. Therefore, the geographic market is at least the whole of Great Britain. The OFT acknowledges the arguments submitted by the parties that the market may be wider than Great Britain and accepts that suppliers of care and justice services in countries outside Great Britain may be potential entrants if not actually part of a wider market.

25. Even on the narrowest basis, namely Great Britain, the OFT has found no evidence that the transaction gives rise to any competition concern. As such, it does not consider that it is necessary to come to a conclusion on the precise geographic market definition in this case.

HORIZONTAL ISSUES

Unilateral effects

Operation and construction of adult custodial facilities (prisons) under PFI contracts

26. NOMS and SPS⁵ are the sole procurers of adult prison facilities under PFI (and MO) contracts in Great Britain through open competitive tenders which are advertised on the EU's Official Journal. The parties submit that, in addition to themselves, there are currently four companies which have successfully pre-qualified in tenders for the operation and construction of prisons in Great Britain under PFI contracts: Kalyx, Serco, The Geo Group and Reliance. Of the six companies which have successfully pre-qualified, four have been awarded and currently hold PFI contracts for prisons. Serco and Kalyx hold four PFI prison contracts each, GSL holds two and G4S holds one. The Geo Group and Reliance do not currently hold a PFI prison contract, although The Geo Group has past experience of providing custodial and other care and justice services in Great Britain. NOMS and other third party respondents indicated that they considered these two companies to be credible bidders for PFI contracts.
27. The parties submit that HMPS is a competitive constraint on private sector bidders for PFI contracts for the construction and operation of prisons. The current PPP (public private partnership) model in Great Britain is designed to reduce the burden of capital expenditure on the State by seeking private sector financing for large projects. Allowing HMPS to bid for PFI contracts would defeat the object of putting the contracts out to tender. However, the parties argue that, since the separation of NOMS from HMPS, NOMS could structure PFI contracts so that the custodial services are performed by HMPS and the remaining elements are contracted out to private sector bidders. Alternatively, HMPS could team up with a facilities management

⁵ The OFT understands that the policy of SPS going forward will be for all new prisons to be operated by SPS.

provider in a consortium in order to compete for PFI contracts against the private sector.

28. HMPS does not currently bid for PFI contracts for the construction and operation of prisons and, therefore, is not a current competitive force in the market for these contracts. The OFT considers that HMPS may be a future competitive constraint, but only to the extent that NOMS could change the structure of the current PFI contract model if it considered that private sector companies bidding for contracts did not represent sufficient competition in the market. Accordingly, the OFT has not included HMPS in its consideration of the competitive constraints on the parties post-merger in the construction and operation of prisons under PFI contracts.
29. On the basis of the evidence available, the OFT concludes that five strong credible bidders post-transaction (including the merged entity) will maintain sufficient competition in relation to future tenders for the construction and operation of prisons under PFI contracts. This conclusion is corroborated by the fact that NOMS, the sole customer in this segment, did not express any concerns about the merger in this respect. As such, the OFT is able to exclude that the transaction raises any significant competition concerns in relation to this segment.

Operation of adult custodial facilities (prisons) under MO contracts

30. In relation to the operation of prisons under MO contracts, the parties submit that, as well as those companies bidding for PFI contracts for the construction and operation of prisons, HMPS is also a strong competitor in this segment. 142 prisons are currently operated by the public sector in Great Britain: HMPS operates 130 prisons and SPS operates 12. The parties do not currently overlap in this segment. The private sector currently holds only two MO contracts for the operation of prisons, those for Doncaster (which was won by Serco) and Wolds (which was won by GSL). Three other MO contracts for the operation of prisons have been put out to tender: one of these (Manchester) was won by HMPS from the outset; the other two (Buckley Hall and Blackenhurst) were originally awarded to the private sector (GSL and Kalyx, respectively) and then won back by HMPS at the next round of tendering.
31. The parties submit that HMPS also imposes a competitive constraint on other operators because of its position as provider of last resort, where

private sector providers are not meeting their contractual requirements. On the basis of the evidence provided by the parties and input received from third parties, the OFT considers that HMPS represents a competitive constraint on private operators in relation to MO contracts for the operation of prisons.

32. As mentioned in the market definition section above, the OFT has not received any evidence to suggest that an operator of a PFI contract for the construction and operation of a prison could not relatively easily operate a prison under an MO contract (the requirements of an MO contract effectively form a sub-set of those under a PFI contract). On this basis, the OFT is able to exclude that the current transaction raises any significant competition concerns in relation to future tendering in this segment given the presence of five credible private sector bidders (the current MO providers, Serco and GSL, and the three additional private sector bidders, Kalyx, The Geo Group and Reliance), as well as a significant competitive constraint from HMPS.

Operation of YOIs under MO and PFI contracts

33. In relation to YOIs, the OFT understands that no MO contracts have been awarded to-date. As regards PFI tenders for the construction and operation of YOIs, the only two contracts awarded to date were awarded as part of a prison facility (Parc, which was awarded to G4S, and Ashfield, which was awarded to Serco). As such, the OFT has considered YOIs within its competitive assessment of prisons and did not identify any additional issues or concerns in relation to this segment.

Operation and construction of STCs under PFI contracts

34. The Youth Justice Board (YJB) is the sole procurer of STC operation and construction services in Great Britain through open competitive tenders which are advertised on the EU's Official Journal. There are currently four STCs, all of which are operated by the private sector under PFI contracts. Post-transaction, the merged entity will operate three out of the four STCs. The fourth STC is operated by Serco. Therefore, the transaction will reduce the number of existing holders of STC operation and construction contracts from three to two.

35. None of the current STC contracts will come up for renewal for almost five years. In addition, the parties indicated that the YJB will not build any new STC's in the near future. The YJB confirmed to the OFT that at least for the [] it does not intend to commission any new STCs. Since the terms of PFI construction and operation contracts are set at the time the contracts are awarded, the OFT is able to exclude that this transaction will have any effect on competition within this segment for almost the next five years.
36. Further, in relation to future re-tendering of the four existing STC contracts, the parties submit that, in addition to existing providers, other bidders in the past have included Reliance and the Castle Care Group. Although the OFT has not been able independently to verify whether Reliance and the Castle Care Group have bid in the past, it does not exclude that these companies are capable bidders and, moreover, accepts that there are other potential credible bidders in the form of bidders for prison contracts (Kalyx and The Geo Group). The OFT has seen no evidence to suggest that these companies will not still be credible bidders when the contracts are next put out to tender. On this basis, the OFT is able to exclude that the transaction raises any significant competition concerns in relation to this segment.

Operation of IRCs under MO contracts

37. There are currently 11 IRCs operational in Great Britain, eight of which are managed by the private sector on behalf of the UK Border Agency (UKBA)⁶. The remaining three IRCs are operated by HMPS. The OFT saw no evidence of HMPS bidding for contracts to operate IRCs in recent tenders. Therefore, the OFT has excluded that HMPS represents a significant competitive constraint on private operators in this segment. Of the eight IRC contracts outsourced to the private sector, two of these were put out to tender on a PFI basis and are discussed below.
38. Post-transaction, the merged entity will hold four of the six IRC contracts put out to tender on an MO basis. The other two contracts will be held by The Geo Group and Serco. The proposed transaction will reduce the number of holders of IRC MO contracts from four to three, and the number of credible bidders from six to five.

⁶ The UK Border Agency changed its name from the Border and Immigration Agency on 1 April 2008.

39. The OFT received bidding data from UKBA on the four tenders which have been organised for IRCs since 2006. For these four tenders, UKBA received between three and six bids from a pool of six different bidders, comprising the current holders of MO contracts, as well as Reliance and Kalyx. The parties submit that Kalyx's ability as a credible bidder for these contracts is demonstrated by its success in the PFI tender for the Harmondsworth IRC contract.
40. UKBA told the OFT that G4S and GSL competed against each other to a great extent on the basis that they bid for each of the four tendered contracts. Although UKBA thought its ability to negotiate for the provision of this service could be reduced, it acknowledged that the number of remaining bidders would still remain competitive. The bidding data generally indicated a good level of rivalry amongst the six different bidders in relation to past tenders. The bidding data also indicated that the parties may not be each other's closest competitors. For example, in one tender awarded in 2008 (Brook House), GSL won the contract and G4S' bid was ranked fifth out of six by UKBA and in none of the other three tenders were the parties ranked next to each other.
41. On the basis of the above evidence, the OFT has concluded that the existence of two active providers (Serco and The Geo Group) in addition to the merged entity, as well as credible past bidders in Kalyx (which has won one of the PFI contracts for IRCs) and Reliance, will maintain sufficient competition in relation to the provision of IRC services under future MO contracts. As such, the OFT is able to exclude that the transaction raises any significant competition concerns in relation to this segment.

Operation and construction of IRCs under PFI contracts

42. Two contracts for the operation and construction of IRCs have been put out to tender under the PFI model. One of these (Colnbrook) was awarded to Serco and the other (Harmondsworth) was awarded to Kalyx. There is no overlap between the merging parties in relation to the operation of IRCs under PFI contracts. The OFT does not have information on whether or not the parties bid in the tender for the Colnbrook contract in 2004 and, at the time of the Harmondsworth tender (2000), G4S and GSL were part of the same organisation.

43. The present transaction will have no effect on the current market structure. In relation to future tenders, the OFT accepts the parties' submission that The Geo Group and Reliance would both be credible bidders in addition to the current providers (Kalyx and Serco) and, therefore, that there will be a sufficient pool of potential bidders. As such, the OFT is able to exclude that the transaction raises any significant competition concerns in relation to this segment.

Operation of police custody suites under MO contracts

44. Of the eight contracts for the operation of police custody suites put out to tender on an MO basis, G4S will hold one and GSL will hold four. The remaining three contracts are all held by Reliance. Serco has submitted bids in previous tenders and some police authorities have confirmed that Serco and The Geo Group would both be credible bidders in future tenders. Therefore, the transaction will result in the number of current operators of police custody suites under MO contracts falling from three to two, and the number of credible bidders from five to four. The parties also argue that Kalyx would be a credible bidder, as might pure facilities management services providers.
45. Evidence available to the OFT indicated that this is a small and immature market which is likely to expand as more police authorities become aware of possible cost savings resulting from outsourcing non-core services to the private sector. Currently, only 12⁷ out of a potential total of 51 police authorities have outsourced the operation of police custody services to the private sector. Any expansion is expected to attract more interest in this area, from operators such as Kalyx. While considered plausible, the OFT has not needed to conclude on the likelihood of Kalyx as a credible bidder as the evidence before it indicates that the presence of an alternative existing provider (Reliance) and two additional credible bidders (Serco and The Geo Group) for future contracts will constrain the parties' conduct after the merger and ensure sufficient competition is maintained. As such, the OFT is able to exclude that the transaction raises any significant competition concerns in relation to the operation of police custody suites under MO contracts.

⁷ 12 police authorities have outsourced 13 contracts (8 MO and 5 PFI contracts) to the private sector. This is because Gloucestershire police authority has put two contracts out to tender: a PFI contract for Gloucester Police Headquarters awarded to Reliance; and an MO contract for custodial services awarded to GSL.

Operation and construction of police custody suites under PFI contracts

46. Of the five contracts for the operation and construction of police custody suites put out for tender under the PFI regime, one was awarded to GSL. The other four are held by Reliance. The parties do not, therefore, currently overlap in relation to this segment of the market. The OFT considers that there are other credible bidders in this market which, together with Reliance as the most significant incumbent supplier, will impose a significant competitive constraint on the parties post-transaction. Accordingly, the OFT finds no evidence that the transaction leads to any competition concerns in relation to this area.

Secure transportation of offenders, immigrants and asylum seekers

47. Post-transaction, the parties will hold six out of a total of 12 contracts for the secure transportation of offenders, immigrants and asylum seekers. Reliance holds three of the other contracts and Serco, The Geo Group and ITA hold one each. Therefore, the transaction will reduce the number of current suppliers of secure transport services from five to four.
48. The geographic scope of these contracts has been reconfigured in the past, such that it has been difficult for contractors to gain a strong foothold in a specific area. []. The OFT also understands that the impact of increased capacity in prisons will have the effect of expanding demand for these services. NOMS, which is the procuring authority for these services, indicated that it has been approached by a number of companies outside of the traditional care and justice sector which have expressed interest in providing these services in the future. On the basis of the evidence available to it, in particular the existence of at least four alternative credible bidders, the OFT was able to exclude that the transaction would lead to any significant competition concerns in this sector.

Provision of electronic tagging and monitoring services

49. G4S holds three of the six electronic tagging and monitoring contracts in Great Britain. The other three are held by Serco. Electronic tagging and monitoring contracts have a duration of five years and may be extended for a further two years. Although GSL does not hold a contract for electronic tagging and monitoring, it did submit a bid in the latest round of tenders. A number of other bidders also submitted bids, including Reliance, Chubb,

Siemens, Elmo-Tech, Securitas, BI Incorporated, ADT Fire and Security plc and Guidance Monitoring Ltd. The OFT understands that this is an expanding market and, as such, is likely to attract the interest of several bidders when the current contracts expire. On this basis, the OFT does not consider that the transaction raises any competition concerns in relation to this area.

Coordinated effects

50. The OFT has considered whether the transaction could raise potential coordinated effects concerns in relation to any of the care and justice services segments identified. The OFT guidance refers to three conditions that must be met or created by a merger for collusion to be successful or for it to become more likely⁸: (i) there must be ability to align behaviour; (ii) there must be incentives to maintain the coordinated behaviour; and (iii) the behaviour must be sustainable. The OFT has obtained no evidence to suggest any of these criteria are met in this case.
51. Notwithstanding the reduction in the number of actual or potential bidders as a result of the transaction, the evidence available to the OFT indicates that robust competition will be maintained. First, the very limited scope for transparency in relation to price and other bidding information (because of the sealed-bid design of the tender process) will continue to limit suppliers' ability to align their behaviour - in the absence of explicit collusion (of which the OFT has seen no evidence), all companies bidding for a particular tender have to assume that other bidders are submitting their lowest prices. This is all the more so where, as here, contracts are of high value and are put out to tender only infrequently. Second, the infrequency of contract tenders will continue to limit suppliers' incentives to align behaviour by reducing the potential for a workable punishment mechanism for 'cheaters'. Finally, the presence of a strong buyer (in the form of NOMS, UKBA, YJB and various police authorities) as well as the potential for entry further reduces the likelihood of coordinated behaviour being sustainable.

⁸ OFT *Mergers – Substantive assessment guidance*, para 4.12.

Barriers to entry and expansion

52. The OFT considers that it would be relatively easy for a holder of a PFI contract for the construction and operation of prisons to fulfil prison operation services on an MO basis.
53. In relation to STCs, to the extent that there is any doubt that the existing providers and past credible bidders cannot ensure sufficient competition when the next STC contracts come up for tender, the OFT accepts that there are potential credible bidders in the form of bidders for prison contracts which would ensure an adequate level of rivalry is maintained.
54. In relation to the other care and justice segments, there will be sufficient competition post-transaction and so it has not been necessary to come to any further conclusions on entry and expansion.

Buyer power

55. The parties submit that in each sector the relevant contracting authority possesses significant buyer power.⁹ These contracting authorities are sophisticated purchasers. Some have the power to determine which tenders are put to the market and specifically design how each tender process is run. They have the ability to encourage more bidders to participate in a given tender process and the OFT has seen evidence that they have done this in the past.
56. It is anticipated that there will be expansion in the number of prison places in the near future, as well as in relation to some of the other care and justice services (such as secure transportation and the provision of police custody suites). It can be expected that current and potential providers of services will be keen to secure this future work. This is likely to confer even greater negotiating power on the contracting authorities.

⁹ The contracting authority in each case is as follows: NOMS for prisons in England and Wales, secure transportation of offenders and electronic tagging and monitoring; SPS for prisons in Scotland; the Scottish Executive for electronic tagging and monitoring services in Scotland; the YJB for YOI's, STCs and the secure transportation of youth offenders; UKBA for IRCs and the secure transportation of immigrants and asylum seekers; and the police authorities for the provision of police custodial services. Although YOIs are contracted out as part of prisons, the contracting authority is the YJB.

57. Comments from third parties support the parties' view that the contracting authority in each case has buyer power and the OFT acknowledges that buyer power may be relevant in this case. However, given that the transaction does not raise competition concerns in any of the individual segments for the provision of care and justice services identified, it is not necessary for the OFT to conclude on the issue of buyer power in this case.

VERTICAL ISSUES

58. The OFT saw no evidence suggesting that the transaction raises vertical issues.

THIRD PARTY VIEWS

59. No third parties contacted by the OFT expressed any substantiated concerns about the transaction. In particular, NOMS, UKBA and the YJB (the contracting authorities for the operation and construction of prisons, YOIs, STCs and IRCs as well as the provision of secure transportation services and electronic monitoring and tagging services) did not consider that the transaction would raise any significant competition concerns. They all considered that a sufficient number of existing providers and credible bidders would remain in order to ensure that future tenders were competitive. The police authorities which responded to the OFT's questionnaires also did not raise any significant concerns in relation to the levels of future competition for the operation and construction of police custody suites. No competitors raised any significant concerns in relation to the transaction. Specific issues that were raised by third parties have been dealt with in the OFT's analysis.

ASSESSMENT

60. The parties overlap in relation to the operation and construction of adult custodial facilities, the operation and construction of youth justice facilities, the provision of support services to police forces and the secure transportation of offenders, immigrants and asylum seekers. Both parties have also bid for the provision of electronic tagging and monitoring services, although only G4S has been successful in winning a contract. Contracts for the provision of these services can be awarded either on a PFI basis for construction and operation or on a management only (MO)

basis. The parties submit that the market should be looked at as one for the provision of care and justice services in general.

61. On the basis of the evidence on demand-side and supply-side substitutability between the various care and justice services and between services provided under PFI and MO contracts, the OFT has decided to consider the transaction under the following frames of reference:
- i. operation of adult custodial facilities (prisons) under MO contracts
 - ii. operation and construction of adult custodial facilities (prisons) under PFI contracts
 - iii. operation of young offender institutes (YOIs) under MO contracts
 - iv. operation and construction of YOIs under PFI contracts
 - v. operation and construction of secure training centres (STCs) under PFI contracts
 - vi. operation of immigration removal centres (IRCs) under MO contracts
 - vii. operation and construction of IRCs under PFI contracts
 - viii. operation of police custody suites under MO contracts
 - ix. operation and construction of police custody suites under PFI contracts
 - x. secure transportation of offenders, immigrants and asylum seekers
 - xi. provision of electronic tagging and monitoring services.

Given the lack of competition concerns arising in relation to any of the narrow frames of reference identified, the OFT does not need to come to a conclusion on the precise relevant product market in this case.

62. The parties submit that the geographic market for the provision of these care and justice services is at least the whole of Great Britain and may be wider because providers of care and justice services operating elsewhere in the world can and do bid for contracts in Great Britain. The OFT accepts that the geographic market is at least the whole of Great Britain. It acknowledges the parties' arguments in relation to a wider market. However, given the lack of competition concerns on even the narrowest basis, the OFT does not consider it necessary to conclude on the precise geographic scope of the market.
63. Six companies have reached the pre-qualification stage of PFI tenders for the construction and operation of a prison in Great Britain. To-date, PFI

prison contracts have been awarded to four of these bidders (Kalyx, Serco, G4S and GSL). The parties submit that the other two pre-qualifying bidders (The Geo Group and Reliance) are credible bidders which impose a competitive constraint on the four current contract holders. This view is supported by third parties. The OFT does not accept that HMPS is a current competitor in this segment, although it cannot entirely exclude that it exerts some competitive constraint or may do so in the future. The OFT's conclusion on the basis of the evidence available is that the existence of five credible bidders for future PFI contracts for the construction and operation of prisons is sufficient to ensure that competition is maintained in this case. The OFT considers that the significant anticipated expansion in the number of prison places will make this segment even more attractive.

64. The competitive position in relation to MO contracts for the operation of prisons in Great Britain is comparable to that in relation to PFI contracts discussed in the previous paragraph as the OFT considers that PFI providers could relatively easily bid for and perform an MO contract. The OFT also received evidence that HMPS can and does bid in relation to these contracts and is the provider of last resort for NOMS. As such, HMPS is a significant competitive constraint on private sector bidders for MO contracts for the operation of prisons. Therefore, the OFT concludes that the transaction does not give rise to any competition concerns in relation to MO contracts for prison services.
65. No MO contracts for YOIs have been awarded to-date. The only two PFI contracts for YOIs were awarded as part of a prison facility. The OFT has analysed YOIs in the context of its assessment of prisons and does not consider that any additional issues or concerns arise.
66. The merged entity will hold three of the four PFI contracts for operation and construction of STCs. The fourth contract was awarded to Serco. The OFT understands that none of the current contracts will come up for renewal for almost five years and no new construction of STCs is planned within this period. The terms of PFI contracts are set at the time the contract is awarded. As such, the OFT does not consider that this transaction will have any effect on competition within this segment for almost the next five years. In relation to future contracts put out to tender after that date, the OFT understands that Reliance and the Castle Care Group have bid for contracts in the past and accepts that there are other potential credible bidders in the form of bidders for prison contracts (Kalyx

and The Geo Group). As such, the OFT does not consider that the transaction raises competition concerns in this area.

67. Of six MO contracts for the operation of IRCs put out to tender to the private sector, the merged entity will hold four. The other two contracts are held by The Geo Group and Serco. The parties submit that Kalyx, which has won a PFI contract for the operation and construction of an IRC, is also a credible bidder, as is Reliance, which has bid for these contracts in the past. The OFT analysed bidding data from UKBA which indicated that there has been a strong degree of rivalry amongst all six bidders in past tenders and that the parties are not each other's closest competitors. On this basis, the OFT is able to exclude any competition concerns in relation to this segment.
68. Two contracts for the operation of IRCs were put out to tender to the private sector on a PFI basis. The parties did not win these contracts and so do not overlap in relation to this segment. Given the lack of concerns in relation to MO contracts for the operation of IRCs, the OFT concludes that the transaction also raises no competition concerns in relation to this area. In relation to future tenders, the OFT accepts that, other than the existing providers, The Geo Group and Reliance both constitute credible bidders in addition to the merged entity.
69. The merged entity will hold five out of the eight contracts for the operation of police custody suites put out to tender on an MO basis. The other three contracts are held by Reliance. The parties submit that Serco and The Geo Group have submitted bids in previous tenders and that Kalyx and a number of other operators are credible bidders and represent a competitive constraint. Only 12 out of a potential total of 51 police authorities have currently outsourced the operation of police custody services to the private sector. This is an area of the care and justice sector which is likely to expand in the coming years and, as such, may be attractive to other bidders. The OFT concludes that, in addition to the merged entity, the two current providers as well as a number of additional credible bidders will ensure that future tenders are competitive. Therefore, the transaction does not raise any concerns in relation to the operation of police custody suites under MO contracts.
70. In relation to PFI contracts for the operation of police custody suites, one of these was awarded to GSL and the other four to Reliance. Given the

lack of overlap between the parties in this area, the fact that Reliance is by far the most significant operator and the number of other credible bidders for future tenders, the OFT does not consider that the transaction raises any competition concerns in relation to this segment.

71. The merged entity will hold six out of the 12 contracts for secure transportation of offenders, immigrants and asylum seekers. Four other companies hold the other contracts: Reliance (three), Serco (one), The Geo Group (one) and ITA (one). The OFT understands that the significant increase in the number of prison places will have a knock-on effect in terms of expanding demand for these services. Given that post-transaction there will still be four companies which have submitted credible bids in past tenders, the OFT is able to conclude that the transaction will not lead to competition concerns in relation to the provision of secure transportation of offenders, immigrants and asylum seekers.
72. G4S holds three contracts for the provision of electronic tagging and monitoring services. The other three are held by Serco. GSL bid for these contracts in the latest round of tenders, as did a number of other operators. The OFT understands that this is an expanding market which is likely to attract a significant number of bidders when the contracts come up for renewal. As such, the OFT does not consider that the transaction raises any competition concerns in relation to this area.
73. In relation to future tenders for STCs, to the extent that there is any doubt about the competitive constraint on the merged entity imposed by the existing providers and past credible bidders, the OFT considers that potential credible bidders for STC PFI contracts in the form of credible bidders for prison contracts will ensure that an adequate level of competition is maintained. In relation to the other individual segments for the provision of care and justice services identified, the OFT does not consider that it is necessary to come to a conclusion on the ease and likelihood of new entry or expansion, or on the issue of buyer power given that the transaction does not raise significant competition concerns.
74. Consequently, the OFT does not believe that it is or may be the case that the merger may be expected to result in a substantial lessening of competition within a market or markets in the United Kingdom.

DECISION

75. This merger will therefore not be referred to the Competition Commission under section 33(1) of the Act.