
Anticipated acquisition by Serco Group plc of ITNET plc

The OFT's decision on reference under section 33 given on 1 February 2005

PARTIES

1. **Serco Group plc (Serco)** is involved in the provision of services to national and local governments and private sector clients throughout the world. Serco operates in a range of sectors including public transport and traffic management, defence and aerospace, justice, science, health, education and local government. Its work ranges from the management of facilities, projects and IT systems, through to the creation of entirely new businesses.
2. **ITNET plc (ITNET)** is primarily involved in the provision of what are described as business transformation services (including the provision of IT infrastructure support, management consulting, application services and business process management). For the year ended 31 December 2003, the UK turnover (the company only operates in the UK) of ITNET was £188 million.

TRANSACTION

3. Serco proposes to acquire all the shares in ITNET. The proposed transaction has been notified to the OFT by way of a Merger Notice, which expires on 1 February 2005.

JURISDICTION

4. As a result of this transaction Serco and ITNET will cease to be distinct. The UK turnover of ITNET exceeds £70 million, so the turnover test in section 23(1)(b) of the Enterprise Act 2002 is satisfied. The OFT therefore believes 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.

RELEVANT MARKET

Product scope

5. ITNET is active in the provision of business transformation services. Such services provide a customer with a technology led solution to improve and oversee processes and information management and are provided in the form of an overall package or business transformation contract (BTC). A BTC includes one or more of the following component services: IT infrastructure support, management consulting, application services and business process management. The value of a BTC will generally be higher than the sum of the value of component services provided under the contract. Serco is active in the provision of individual component services which make up BTCs, but is not active in the provision of BTCs. ITNET is also active in the provision of individual component services outside of its provision of BTCs.
6. The parties overlap in the supply of the following component services:
 - **IT infrastructure support** involves the outsourcing to a third party supplier the provision of infrastructure support services, such as help-lines.
 - **Management consultancy** services aim to establish strategy and provide training and capability through skills and knowledge transfer.
 - **Application services** include the provision of services around the supply, implementation and support of major applications (e.g. applications that support customer contact and resource management).
 - Business process management comprises the management of functions such as call centres and various business support functions (e.g. finance and payroll).
7. If component services are further sub-divided (for example, dividing IT support services into operational services, application management services and help desk management services), the parties combined share of supply in overlap areas would not exceed 10 per cent on any reasonable segmentation.
8. For completeness the OFT has also considered what overlaps exist in terms of the customers served by the parties. However, direct overlaps are limited and again there is no customer type where the parties would jointly supply over 10 per cent of such services.

Types of supplier

9. The parties submit that the suppliers of BTCs and component services can be categorised into three broad groups:
 - **First-tier suppliers** are generally viewed as those that are active on a global basis and are regularly involved in contracts worth over £50m per annum. Such suppliers include BT, Fujitsu, CSC, EDS, Accenture, Cap Gemini, IBM and Siemens.
 - **Second-tier suppliers** are generally viewed as those that are regularly involved in contracts worth between £5m and £50m per annum. There are around 15 such suppliers in the UK, including Liberata, Northgate, Steria, Capita, LogicaCMG, Amey, ATOS, Agilysis, Vertex, KPMG and HBS. The parties submit that they fall within this category.
 - **Third-tier suppliers** are generally viewed as suppliers that are regularly involved in contracts worth up to £5m per annum. There are a wide range of suppliers in this category including Vivista (Securicor), Anite and Saffron.

10. The parties submit that while much of the competition for contracts takes place within the three tier bands, there is nevertheless evidence of significant competition for contracts between firms in different tiers, particularly for contracts worth under £50 million per annum. While this suggests that supply side substitution between the tiers exists, there is no need for the OFT to conclude on whether segmentation by size of supplier is appropriate, as on any definition, shares of supply do not exceed 10 per cent.

Conclusion on product scope

11. As the combined share of supply of the parties is less than 10 per cent whether the sectors are segmented by types of supplier or type of end customer, or when IT infrastructure support is sub-divided, it has not been necessary for the OFT to reach a conclusion on the product scope in this analysis as no competition concerns arise even on the narrowest definition.

Geographic scope

12. The parties submit that if separate frames of reference are identified for each of the product segments outlined in paragraph 6 above, then their geographic scope would be likely to be at least the UK and possibly wider. As evidence for this they point to factors such as pricing levels being

similar throughout the UK, the fact that almost all suppliers of component services compete for business throughout the UK and some compete internationally and that many of the services that fall within component services (such as call centres or IT support services) can be provided remotely throughout the UK and beyond.

13. The European Commission has previously found that due to customised solutions according to language and local business peculiarities, the market for individual component services is national, rather than international, although the sector is becoming increasingly internationalised.¹ On the basis of the evidence received it has not been necessary to depart from the European Commission's definition and the appropriate geographic frame of reference is considered to be at least the UK.

HORIZONTAL ISSUES

Shares of supply

14. The parties were unable to estimate shares of supply for 2004 for the various segments identified with any degree of accuracy, given their limited access to current third party data. However, shares of supply to all end users in 2000 were provided, based upon third party data provided by Total Romatec, a UK market research company. There is no evidence to suggest that the sector has changed significantly since this time.
15. ITNET and Serco believe that their contracts for component services are generally worth less than the average value of contracts within the relevant segment. On this basis, therefore, the parties suggest that their share of supply measured by value would be less than that measured by number of contracts. Even on the basis of the number of contracts, the parties highest combined share of supply is in the provision of IT Infrastructure Support at 7.8 per cent with an increment of less than 0.5 per cent. Combined shares of supply in the other segments are below this level.
16. The available evidence shows that ITNET has several larger competitors in each of the segments. The increment is minimal, with Serco not having a share in excess of 1 per cent of any of the segments. Even on a very narrow frame of reference (sub-dividing component services or considering supply to particular types of customers or by firm size), the parties' combined shares do not exceed 10 per cent. There is no evidence to

¹ COMP/M.1561 Getronics/Wang, COMP/M.2478 IBM Italia/Business Solutions/ JV, COMP/M.2946 IBM Consulting/PWC Consulting.

suggest that the parties were close competitors pre-merger or that Serco was the next best alternative to ITNET. The parties have not bid against each other in the past four years.

VERTICAL ISSUES

17. No vertical competition concerns arise as a result of this transaction.

THIRD PARTY VIEWS

18. No third parties have expressed competition concerns about this transaction.

ASSESSMENT

19. While ITNET is active in the provision of business transformation contracts, Serco is active in the provision of a number of individual component services which make up BTCs. The parties overlap in the supply of a number of these component services in the UK. The combined shares of supply of the parties in the various overlapping segments are, however, low with minimal increments. Several large competitors remain and there is no evidence to suggest that the parties were close competitors pre-merger.
20. 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 for goods and services.

DECISION

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