COMPETITION COMMISSION

VPS Holdings Limited and SitexOrbis Holdings Limited

A report on the completed acquisition by VPS Holdings Limited of SitexOrbis Holdings Limited

17 August 2012

Website: www.competition-commission.org.uk

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The Competition Commission has excluded from this published version of the final report information which the Inquiry Group considers should be excluded having regard to the three considerations set out in section 244 of the Enterprise Act 2002 (specified information: considerations relevant to disclosure). The omissions are indicated by [✂]. Non-sensitive wording is indicated in square brackets. Some numbers have been replaced by a range. These are shown in square brackets.

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Summary

1. On 5 March 2012, the Office of Fair Trading (OFT) referred the completed acquisition by VPS Holdings Limited (VPS) of SitexOrbis Holdings Limited (SitexOrbis) to the Competition Commission (CC) for investigation and report. The CC must publish its report by 19 August 2012 on the questions: *(a)* whether a relevant merger situation has been created; and *(b)* if so, whether the creation of that situation has resulted or may be expected to result in a substantial lessening of competition (SLC) within any market or markets in the UK for goods or services.

2. VPS is the holding company for the VPS group of companies, an international business. VPS's ultimate owners are TDR Capital Nominees Limited and TDR Fund II (TDR), a private equity fund. In the UK, VPS manages services for vacant properties including: risk assessments; 'cleaning and clearing' of properties (ie cleaning and clearing waste, room strip-outs, decontamination services and specialist cleans); property maintenance services; the provision of alarms; security patrols and inspections; and vacant property security fittings. In the UK, VPS is largely focused on the commercial sector,[1] but also has a significant presence in the social housing sector.

3. SitexOrbis was the holding company for a group of companies providing integrated property and people security services in the UK and other European countries. In the UK, the majority of SitexOrbis's business is in the social housing sector.

4. The parties overlap in the supply of vacant, or void, property services. In particular, both parties supply services designed to keep vacant properties secure. The parties install and supply prefabricated steel screens and doors, steel sheeting 'cut to size' to cover openings to the property, plastic (polymer) screens and battery-powered wireless security alarms (hereafter, security services for vacant properties (SSVP)). Customers of security services for vacant properties can be split into two distinct groups: social housing customers (eg local authorities and registered social landlords) and commercial customers (eg insolvency practitioners and facilities management companies).

5. On 27 September 2011 VPS acquired the entire business of SitexOrbis following a sales process administered on behalf of SitexOrbis's owners by Ernst & Young. The acquisition was structured as two separate sale and purchase agreements with the Continental European subsidiaries of SitexOrbis acquired separately from the UK businesses.

6. With regard to the first of the two reference questions—ie whether a relevant merger situation has been created (paragraph 1)—we concluded that, as a result of the transaction described in paragraph 5, VPS and SitexOrbis were brought under common ownership, and we were satisfied that VPS and SitexOrbis have ceased to be distinct enterprises. We were satisfied that the parties' combined share of supply of the provision of SSVP to both social housing and commercial customers was greater than a one-quarter share of supply in the UK and that the acquisition had led to an increase in the combined share of supply. We therefore concluded that a relevant merger situation had been created.

7. We assessed the competitive effects of the merger relative to the competitive situation without the merger (the 'counterfactual'). We considered two possible scenarios in the event that SitexOrbis had not been sold to VPS:

[1] That is, construction companies, finance and insurance companies, insolvency practitioners, property services companies, facilities management companies, retail companies and pub/brewery companies.

(a) SitexOrbis remained an independent entity under the same ownership; and

(b) SitexOrbis were bought by an alternative buyer.

8. We spoke to VPS, SitexOrbis, the former owners of SitexOrbis, a potential purchaser of SitexOrbis and Ernst & Young. On the basis of our analysis, we concluded that, if VPS had not purchased SitexOrbis in September 2011, then the business would either have continued to be financed by its owners for the foreseeable future or would have been purchased by an alternative buyer who would not have posed any competition concerns. In relation to the counterfactual, we noted that prior to the merger VPS had no presence in Northern Ireland.

9. We considered whether vacant property security services other than SSVP (eg using wooden boarding or 'live-in guardians' to secure vacant properties) might be an effective substitute for customers using SSVP. We found that the supply of SSVP was an appropriate relevant market within which to assess the effects of the merger. We found that the geographic scope of this product market has national, regional and local dimensions.

10. Based on our analysis of catchment areas around suppliers' depots and evidence concerning customer requirements for the supply of SSVP, we found that the relevant markets for the purposes of answering the second of the two reference questions (paragraph 1) were:

(a) the supply of SSVP to social housing customers at a local level (up to 40 miles from a supplier's depot);

(b) the supply of SSVP to commercial customers at a regional level (up to 70 miles from a supplier's depot); and

(c) the supply of SSVP to commercial customers at a national level (that is, to protect vacant properties across Great Britain).

11. We assessed the competitive effects of the merger according to its likely unilateral effects in each of these markets. We assessed the merger in relation to both the loss of actual competition (as SitexOrbis is no longer an independent competitor in the market) and the loss of potential competition (in those areas where pre-merger only one of the merger companies was present, the merger may remove or reduce potential post-merger competition from the other merger company).

12. We found that vacant property security services other than SSVP were unlikely to be a suitable substitute for SSVP for most social housing or commercial customers. We found that, with the exception of Northern Ireland (see paragraph 26), the merging parties competed across the UK for both social housing and commercial customers.

13. Starting with the likely unilateral effects of the merger on social housing customers, we noted that indicators of market share suggested that the merged company would have a very high post-merger share of supply of SSVP to customers. We assessed how closely the merging companies competed against each other. We evaluated a number of sources of evidence, including the parties' internal documents, information based on tenders in which the parties had participated, views expressed in customer hearings, and our customer survey. The evidence we considered indicated that the merging parties were, for most customers, each other's closest competitor. The evidence indicated that there was a second tier, consisting of Clearway Services (Clearway) and SPS Doorguard (SPS), which may act as a constraint on the parties

for some customers; and a third tier of smaller suppliers which are unlikely to be considered close substitutes by many customers.

14. We considered the profitability of a hypothetical post-merger price rise by looking at the importance of price in the choice of supplier, possible substitution away from the merging parties in response to a post-merger price rise, and the parties' margins. Based on our analysis we concluded that we would expect the merged company to have the incentive and ability to raise prices to most social housing customers, absent countervailing factors.

15. We found that any countervailing buyer power would not protect social housing customers from a post-merger price rise. Nor did we see evidence of efficiencies which might enhance rivalry post-merger and reduce the lessening of competition.

16. We looked closely at the likelihood, timeliness and sufficiency of whether post-merger entry and/or expansion in the supply of SSVP might offset the lessening of competition. We spoke to existing competitors and potential new entrants from adjacent sectors (such as the security and facilities management sectors). We found that the key inputs to a business supplying SSVP were not costly and were readily available. The evidence from third parties, the merging parties' economies of scale, scope and density, and the economics of expansion in the social housing sector, led us to find that entry and expansion within the social housing sector was not likely to occur on a scale sufficient to constrain effectively the merged company so as to defeat a post-merger price rise. We therefore concluded that the merger would give rise to an SLC for social housing customers across Great Britain.

17. We considered next the likely unilateral effects of the merger on commercial customers following a similar approach to our assessment in relation to social housing customers (paragraph 13). We found that, whilst our analysis indicated that Clearway and SPS were important SSVP suppliers to commercial customers, the merging parties appeared to be each other's closest competitors, particularly when considering the evidence of the parties' own internal documents and the similarity and size of their range of operations and depots. It was clear that for some customers there were other suppliers who would also be viewed as close competitors, although our survey generally found that there was low awareness of other suppliers and each of the merging parties was felt to be the other's closest (or equal closest) competitor. Generally, the greater the geographic range of the customer's operations, the fewer the suppliers that would be considered to be credible suppliers.

18. In relation to commercial customers with national SSVP requirements, we found that, at present, VPS, SitexOrbis, SPS and Clearway had the depot infrastructure sufficient to cover most of Great Britain, albeit that VPS and SitexOrbis had significantly larger depot networks and Clearway in particular would have faced long journeys to cover Wales and Scotland. We noted that the customers we spoke to appeared to have quite specific requirements which may have served to restrict the pool of potential SSVP suppliers. Therefore for most customers the merger represented, at best, a reduction from four to three suppliers, where one supplier was very large and the other three main suppliers pre-merger were much smaller (and of similar size to each other). We noted that the merging parties' depot network appears to give the parties a small but not insignificant cost advantage, and that they benefited from other economies of scale, density and scope. Based on our analysis, we concluded that, in a situation where VPS and SitexOrbis had, at best, for most customers two competitors (which appear to be more distant competitors than the merging parties are to each other), the merger would lead to price increases absent countervailing factors.

19. In relation to commercial customers with regional SSVP requirements, we expected that, in regions where they had depots, SPS and Clearway were likely to be stronger competitors than they were for national contracts. We also considered that smaller competitors (notably SecureSite, but also other suppliers) were more likely to provide a degree of competition, at the regional level, and hence a degree of competitive constraint post-merger. Taken together, we found that it would be possible for a combination of competitors to provide sufficient competitive constraint to prevent an SLC in some regions. However, given the lack of competitive constraint from SSVP suppliers in other parts of Great Britain (namely, Scotland, South Wales, south-west England and north-east England), we concluded that the merger would give rise to an SLC in these regions absent countervailing factors.

20. We found that any countervailing buyer power would not protect national or regional commercial customers from a post-merger price rise. Nor did we see evidence of efficiencies which might enhance rivalry post-merger and reduce the lessening of competition for these customers.

21. We looked closely at whether post-merger entry and/or expansion might offset the losses of competition identified above (paragraphs 18 and 19). We considered that entry into the commercial market was more likely than for the social housing market.

22. In relation to commercial customers with national SSVP requirements, whilst we considered that new entry by large companies in adjacent sectors was possible, we expected that this would be on a regional or on a contract-by-contract basis initially and hence we found that it was more likely than not that there will be no significant new entry into the supply of national customers within the next two years such as to constrain effectively the merged parties.

23. In relation to commercial customers with regional SSVP requirements, we assessed that expansion was most likely to be seen in areas adjacent to existing competitors' depots and/or in areas where there was a density of commercial opportunities. We therefore assessed that in some areas expansion could be likely, timely and sufficient to constrain the merged parties. In the SLC areas, however (see paragraph 19), whilst we did not rule out the possibility that entry or expansion may occur, we saw no evidence that new entry would be likely. Further, the SLC areas are not adjacent to existing competitors' depots and it may be difficult for new entrants to secure a sufficient toehold to justify the investment required to open a new depot. Accordingly, we found that in the case of each of the SLCs we identified in these parts of the country the balance of evidence was such that we could not form an expectation that either entry or expansion was likely to occur in a sufficient and timely form so as to defeat the SLCs in these parts of the country.

24. Given our conclusions above we found that the merger may be expected to result in an SLC leading to prices for SSVP being higher than the pre-merger level:

(a) to social housing customers across Great Britain; and

(b) to commercial customers in some parts of Great Britain (namely, in Scotland, South Wales, south-west England and north-east England); and

(c) to commercial customers with national SSVP requirements.

25. Against our counterfactual (see paragraph 8), we considered whether the loss of VPS as a *potential* competitive constraint on SitexOrbis may be expected to lead to an SLC in the provision of SSVP to customers in Northern Ireland.

26. Prior to the merger, VPS was not active in Northern Ireland. Furthermore, at the time of the merger VPS had no presence on the island of Ireland and would not have been able to bring to bear the economies of scale, scope and density it has in Great Britain to compete for new business. As a potential new entrant into Northern Ireland, VPS would have been in a similar position to other larger SSVP suppliers such as SPS or Clearway, and as such VPS would not have been a particularly close competitor to SitexOrbis in Northern Ireland. For these reasons, we concluded that the merger may not be expected to result in an SLC in the supply of SSVP in Northern Ireland.

27. We considered what action should be taken for the purpose of remedying, mitigating or preventing the SLCs we identified or any adverse effects which may be expected to result from them, having regard to the effect of any action on any relevant customer benefits (RCBs, as defined in the Act) arising from the merger.[2]

28. We concluded that divestiture of SitexOrbis (ie the business which VPS acquired including SitexOrbis's depot in Northern Ireland) (SitexOrbis UK) would be an effective remedy that would comprehensively address all of the SLCs that we had identified. As this would involve no change to the existing situation in the UK before the merger, and SitexOrbis UK was effectively operating as a stand-alone business as it has been held separate from VPS since the time of the merger, there would be very little risk that this remedy would not be effective.

29. We concluded that divestiture of the assets of SitexOrbis Great Britain (ie the business which VPS acquired excluding SitexOrbis's depot in Northern Ireland) (SitexOrbis GB) was also likely to be an effective remedy that would comprehensively address all of the SLCs that we had identified. Whilst the exclusion of SitexOrbis's Northern Ireland business would affect the financial profile of the remaining SitexOrbis GB business we concluded that the composition risk of this divestiture was acceptable. We concluded that the separation of the Northern Ireland business could be effected without significant risk to the remaining SitexOrbis GB business. Accordingly, we concluded that there was only a low risk that this remedy would not be effective, and that this risk could be managed as part of the divestiture process.

30. We considered a series of alternative divestiture proposals put forward by TDR (the TDR proposals).[3] Whilst we accepted that the TDR proposals in principle would address all of the SLCs that we had identified, we had significant concerns that the TDR proposals would pose significant composition risk to the remaining SitexOrbis business. We concluded that the composition risks were such that the TDR proposals would not be effective.

31. On the basis that we concluded that both the divestiture of SitexOrbis UK and SitexOrbis GB would be effective in remedying the SLCs we had identified, we have decided to require TDR to divest SitexOrbis GB as this represents the least intrusive remedy.

32. In our judgement, this remedy represents as comprehensive a solution as is reasonable and practicable to the SLCs arising from the merger.

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[2] We concluded that there were no RCBs arising from the merger.
[3] We also considered a behavioural remedy put forward by TDR but we had significant concerns that this remedy would not be effective in addressing the SLCs we had identified.

Findings

1. The reference

1.1 On 5 March 2012, the OFT referred to the CC for investigation and report the completed acquisition by VPS of SitexOrbis. The reference required us to determine:

- whether a relevant merger situation had been created; and
- if so, whether the creation of that situation had resulted or may have been expected to result in an SLC within any market or markets in the UK for goods or services, including the supply of vacant property security services.

1.2 We were required to publish our final report by 19 August 2012. Our terms of reference, together with information about the conduct of the inquiry, are set out in Appendix A.

1.3 This document, together with its appendices, constitutes our final report which contains our decisions on the statutory questions set out in our terms of reference. Non-commercially sensitive versions of submissions received from the main and third parties, as well as summaries of hearings we held with third parties and the results of our customer survey, can be found on our website.[4]

2. The parties to the merger

2.1 VPS is the holding company for the VPS group of companies, which manages services for vacant properties in the UK, USA, France, Italy and Germany. These services include: risk assessment; 'clean-and-clear' services (ie cleaning and clearing waste, room strip-outs, decontamination service and specialist cleans); property maintenance; guarding and monitoring solutions; providing alarms for vacant properties; security patrols and inspections; and vacant property security fittings. In the UK, VPS is largely focused on the commercial sector but also has a significant presence in the social housing sector.[5] In the year ended 31 March 2011, the UK turnover for VPS was £[✂] million and worldwide turnover was £[✂] million.

2.2 VPS's UK arm was known as Safe Estates prior to rebranding in March 2011. VPS s [✂] per cent owned by TDR Capital Nominees Limited as nominees for investors in TDR Fund II[6] which is ultimately managed by TDR Capital LLP (TDR). TDR is a private equity fund manager with approximately €[✂] of commitments (ie funds) under management.

2.3 SitexOrbis was the holding company for a group of companies providing integrated property and people security services in the UK and other European countries (France, the Netherlands, Germany, Belgium and the Republic of Ireland). These services included: physical vacant property security; monitored alarms; clean-and-clear services; regeneration (for example, disconnection of utility services and repair work); vacant property insurance; people protection services (for example, lone worker protection) and an alarm response centre. In the UK, the majority of SitexOrbis's business is in the social housing sector.[7] In the year ended 31 March

[4] www.competition-commission.org.uk/our-work/vps-holdings-limited-of-sitexorbis-holdings-limited/evidence.
[5] See Table 2 below.
[6] This fund was raised in 2006 (see initial submission, paragraph 2.6).
[7] Initial submission, paragraph 2.11.

2011, UK and Republic of Ireland turnover for SitexOrbis was £30.7 million and worldwide turnover was £49.6 million.

2.4 Prior to its sale to VPS, SitexOrbis was owned by two banks and two hedge funds. They had originally been debt providers to the business and acquired equity ownership through a pre-pack administration (an insolvency process in which a restructuring process is agreed in advance and assets are sold immediately the company enters administration) in January 2008. Following the pre-pack administration, the new owners provided all debt and equity financing to the business and the board appointed new management, led by David Walker as Chief Executive Officer and joined by Oliver Cunningham as Chief Finance Officer in January 2009. We were told that the appointment of David Walker was the starting point for a three-year plan to turn around the business with a view to selling the business in due course. The new financing was set to expire in January 2011.

3. The merger

3.1 On 27 September 2011 VPS acquired the entire business of SitexOrbis for a total consideration of £[✂] million.

3.2 The acquisition was structured as two separate sale and purchase agreements with the continental European subsidiaries of SitexOrbis acquired separately from the UK businesses. The consideration for the UK businesses was about £[✂] million, of which about £[✂] million was debt and about £[✂] million was equity. Following the transaction, SitexOrbis comprised only the UK, Guernsey and Republic of Ireland businesses.[8]

3.3 VPS/TDR told us that the acquisition of SitexOrbis was intended to provide a number of benefits:[9]

- *Geographic synergies*. VPS/TDR said that the acquisition would enable VPS to expand its geographic coverage, particularly outside the UK, and create larger businesses in its current geographic locations. TDR said that it believed this would make the VPS group more attractive to an eventual buyer and to lenders.[10]

- *A broader set of products and services, enhancing customer benefits*. VPS/TDR said that they believed VPS inspection services and new alarm technology would be attractive to SitexOrbis customers. Additionally, VPS told us that it believed the UK businesses were complementary as SitexOrbis had a greater focus on social housing customers [✂] and VPS on commercial customers [✂].[11]

- *Cost savings*. TDR said that cost savings formed a critical part of TDR's due diligence.[12] It said that its initial hypothesis was that total merger cost savings would be greater than [✂].[13]

3.4 The parties said that 'it is expected that some variable cost savings will accrue as a result of the transaction'.

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[8] During the CC's inquiry, VPS/TDR requested consent to integrate SitexOrbis's Republic of Ireland businesses with VPS. The CC consented to this request. Accordingly, at the time of this report SitexOrbis comprises only the UK and Guernsey businesses of SitexOrbis. The Guernsey business underwrites vacant property insurance in the UK on behalf of customers of SitexOrbis.
[9] Initial submission, p11.
[10] Initial submission, p11.
[11] Initial submission, p12.
[12] Initial submission, p12.
[13] Initial submission, p12.

3.5 We consider the expected cost savings further in paragraphs 10.86 to 10.89.

4. Jurisdiction

4.1 Under section 35 of the Enterprise Act 2002 (the Act) and our terms of reference (see Appendix A), we were required to report on whether a relevant merger situation has been created.

4.2 Section 23 provides that a relevant merger situation is created if:

(a) two or more enterprises have ceased to be distinct within the statutory period for reference; and

(b) if either the share of supply test or the turnover test specified in that section of the Act is satisfied.

4.3 The Act defines an 'enterprise' as 'the activities or part of the activities of a business'.[14] By reason of their activities described in paragraphs 2.1 and 2.3 above, we were satisfied that each of VPS and SitexOrbis are enterprises for the purpose of section 23. Enterprises will 'cease to be distinct' if they are brought under common ownership or control (section 26 of the Act). As a result of the transaction described in paragraphs 3.1 and 3.2 above, VPS and SitexOrbis were brought under common ownership. Consequently, we were satisfied that VPS and SitexOrbis have ceased to be distinct enterprises.[15]

4.4 The share of supply test is satisfied if the merger creates or increases a share of at least one-quarter in the supply of goods or services of any description in the UK, or in a substantial part of the UK. The concept of goods or services of 'any description' is very broad. For the purpose of the jurisdiction test in section 24 of the Act, the CC is able to measure shares of supply by reference to such criterion or such combination of criteria as it considers appropriate.

4.5 For the purpose of assessing whether or not the share of supply test was met we focused on the supply of vacant property security services (SSVP) (see paragraph 5.2) in the UK, which is the activity in respect of which the merging parties overlap. As explained below, the parties provide SSVP to two broad types of customers: social housing and commercial customers. We assessed whether or not the share of supply test was met by reference to the UK supply of SSVP to social housing and commercial customers respectively.[16]

4.6 We estimated that the parties' combined shares of supply of the provision of SSVP in the UK were [80–90] per cent in the social housing sector and [70–80] per cent in the commercial sector (see Tables 3 and 6). The merger strengthened what were already shares well in excess of a one-quarter share of supply in the UK for each of the social housing and commercial sectors. Consequently, the share of supply test in

[14] Section 129(1).
[15] With regard to the statutory period for reference in section 24 of the Act, the merger transaction completed on 27 September 2011. Under section 25(2) of the Act, the OFT extended the four-month statutory deadline for making the reference until 5 March 2012. The reference was made by the OFT to the CC on 5 March and so was made within the circumstances falling with section 24.
[16] The group of goods or services to which the jurisdictional test is applied need not amount to a relevant economic market of the type used in the substantive competition assessment.

section 23 of the Act was met.[17] The turnover test in section 23(1)(b) of the Act was not met.

4.7 We therefore found that the acquisition of SitexOrbis by VPS had resulted in the creation of a relevant merger situation.

5. Industry background

5.1 This section describes the supply of vacant property services in the UK, certain differences between supply to the social housing and commercial sectors, and provides a brief description of the main suppliers of vacant property services.

Vacant property security services

5.2 The main parties overlap[18] in the supply of vacant property security services[19] (SSVP) comprising the installation of prefabricated demountable[20] steel screens and doors, 'permasteel' (that is, steel sheets which are cut to size and affixed over openings to the property), polymer screens and battery-powered security alarms.

5.3 Other means of securing vacant properties include:

(a) alternative physical security products, eg wooden boarding; and

(b) alternative non-physical security products, eg CCTV, security guards, and live-in guardians.

5.4 Vacant properties are secured (or their existing security is enhanced) to reduce risks to the vacant property/its contents. These risks include: theft, vandalism/property damage, unlawful occupation (eg squatting), arson, water egress and other potential liabilities (including liabilities under the Occupiers' Liability Act 1957 and Occupiers' Liability Act 1984). Different security measures may be appropriate in different circumstances, primarily dependent on the risk profile of the property and the owner/manager's aversion to that risk. While there are no hard-and-fast rules in deciding the type and level of security needed, customer groups may demonstrate particular needs and buying patterns—for example, the level of security is typically enhanced for vacant properties in high-risk neighbourhoods, for high-value properties, and/or for risk-averse owner/managers.

5.5 SSVP are typically supplied on a rental basis (for example, on a weekly basis). Steel screens/doors and alarms are generally fitted and removed by the supplier at the beginning and end of any rental period. At times, security products may also be sold rather than let, such as on a 'fit and forget' basis (for example, in relation to demolition properties where the steel sheets are not to be removed when the building is demolished), or if a customer prefers to purchase certain products rather than rent them.

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[17] These shares of supply are taken from Tables 3 & 6 below. Notwithstanding the caveats set out in paragraphs 10.22 and 11.26 concerning the possibility that those shares are overstated, we considered them to be so far in excess of the 25 per cent threshold that any such overstatement would have no material effect on this assessment of jurisdiction.
[18] The main parties also supply non-security vacant property services such as 'clean-and-clear'. We consider vacant property security services and non-security vacant property services more fully in paragraphs 7.7–7.22.
[19] The term 'void property' is often used instead of 'vacant property.
[20] ie they can be 'de-mounted' and so used again.

5.6 SSVP are procured locally, regionally and/or nationally. Prices tend not to be uniform, as services and pricing are typically individually negotiated.[21] Further, the manner in which a ‘negotiation’ takes place may vary: negotiations range from EU-compliant public procurement tender processes to ‘quote and order’ business where the purchaser requests a price for individual orders when needed.

Customer segmentation

5.7 The main parties told us that there were ‘two broad types of end customers, namely social housing customers and commercial customers’.[22,23] This is consistent with the evidence provided to us by third parties.[24] Broadly, the two customer groups have different needs and (to an extent) different methods of purchasing. Prices and margins appear to differ between the two groups[25] and some suppliers focus primarily or entirely on one group, or have focused on one group in the past.

Social housing sector

5.8 Social housing customers include local authorities and other ‘registered social landlords’ (including housing associations, trusts and co-operatives). Social housing customers manage portfolios of social properties generally concentrated in a local or regional area and tend to purchase vacant property security services: by individual tenders; under framework agreements; or on a ‘quote and order’ basis, ie as required.[26]

5.9 Tenders typically involve two stages:

(a) First is a pre-qualification questionnaire (PQQ), which generally establishes the supplier’s ability to provide services and checks that the supplier is large enough relative to the size of the contract to be awarded; one supplier told us that the PQQ might require the provision of, for example, three years of accounts and references.

(b) Second is a full tender process involving submission of prices and an assessment of quality. We were told that prices were typically given a weighting of between 60 and 100 per cent. Larger-sized contracts (those above approximately £170,000) are subject to EU public procurement rules.

Both stages of the process can be complex and time consuming, requiring considerable resources from participants; but in other cases they can be very short, requiring only the provision of pricing.

5.10 Social housing customers may choose to utilize public sector framework agreements to procure services in accordance with public procurement rules.[27] Fusion 21, LHC and other similar parties such as Efficiency East Midlands offer framework agreements for vacant property security services. In other cases, social housing cus-

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[21] Some sales may be under fixed price schedules (such as framework agreements) but even these prices are usually individually negotiated at the time the schedule was put in place.
[22] Initial submission, Section 4, Introduction.
[23] We also noted that [✂].
[24] See Appendix G, paragraph 10.
[25] See eg paragraph 11.77. See also Appendix G, paragraph 12.
[26] VPS estimated its social revenue in 2011 to be split as follows: [✂] per cent for sales under contract (including [✂] per cent under framework agreements) and [✂] per cent on a ‘quote and order’ basis.
[27] These framework agreements set out detailed supply terms which are then incorporated into an individual supplier agreement or form the basis of a mini-tender among approved framework agreement suppliers. Customers are not obliged to purchase from framework agreements and can choose to enter into negotiations with potential suppliers directly.

tomers contract with 'intermediaries' (often large private sector companies) for the supply of a wider set of property management services, including vacant property security services. These intermediaries may either provide the services themselves or subcontract to specialist SSVP suppliers. In some cases, social housing customers may procure vacant property security services from direct labour organizations (DLOs—organizations within the public sector which provide services to social landlords).

5.11 Both the merging parties and a number of other suppliers and customers told us that demand in the social housing sector was either flat or declining. Due to greater pressures on council budgets and better management of 'key-to-key time' (ie the period of time from when a key is handed in by the departing tenant to an incoming tenant receiving a key), rental periods for vacant property security services have declined. There has also been a reduction in the number of vacant properties requiring these services. Margins have been negatively affected by the fall in volumes and decrease in rental periods as well as, it appears, price competition between providers of vacant property security services.

Our customer survey

5.12 Social housing customers generally operate at a local level and make decisions on the same basis. In our customer survey,[28] 84 per cent of those responding said that they operated at a local or regional level,[29] and 87 per cent made decisions about SSVP on this basis.

5.13 Many social housing customers manage a large number of properties. In our survey,[30] almost half managed more than 5,000 with a further quarter managing over 500. Typically, over half of social housing customers had less than 5 per cent of their properties vacant, and over half physically secured less than 5 per cent of their vacant properties. A quarter secured more than half of their vacant properties, with 16 per cent securing all of their vacant properties.

5.14 Properties were most frequently secured when they were awaiting reoccupation or likely to be vacant for a long time. The factor most often noted by respondents was that properties needed to be secured in certain locations (mentioned by 46 per cent of social housing respondents). These respondents particularly mentioned areas prone to vandalism or theft (74 per cent), squatting (12 per cent), and deprived areas generally (8 per cent).[31]

5.15 The period for which vacant properties would be secured varied, with one-fifth of our survey respondents unable to give an answer for a typical vacancy period. Of those who could respond, under a week was rare but 39 per cent said between a week and a month, 30 per cent said between a month and three months, and the remaining 30 per cent said longer than six months (over two years in some cases).[32] By comparison, VPS told us that the average vacant period for the social housing properties it protected was around [✂] weeks. Clearway, another supplier of SSVP, told us that the average rental period, in weeks, of steel security for social housing had reduced from the high 30s to under 26 weeks. The evidence suggests that the majority of

[28] See survey report.
[29] The survey company defined 'local' as 'town or county', and 'regional' as a broader area but sub-national (ie less than the whole of either England, Scotland or Wales).
[30] Survey Q3–5, excluding Don't knows.
[31] Survey Q6. The comparable percentages for commercial customers were 55, 15 and 21 per cent.
[32] Survey Q7.

properties are protected for less than the mean of 24 to 26 weeks, but there are a significant number of longer vacancies.

Commercial sector

5.16 Commercial customers include construction companies, finance and insurance companies, insolvency practitioners, property services companies, facilities management companies, retail companies (eg supermarkets) and pub/brewery companies. Some commercial customers manage portfolios of commercial properties located across the UK. Commercial customers may often be influenced by insurance requirements when taking their purchasing decisions.[33]

5.17 Commercial customers purchase vacant property security services in a number of ways including: 'quote and order' (which make up the majority of sales in this sector), formal tender processes (which are relatively uncommon) and preferred supplier arrangements.

5.18 The commercial sector differs from the social housing sector in that:

(a) Individual commercial properties are typically larger, the security needs are more complex, and vacant periods are typically longer,[34] so rental revenues (per property) are typically higher than in the social housing sector.

(b) Margins are typically higher than in the social housing sector.[35]

(c) A greater range of steel screens and doors is required for the commercial sector, because door and window openings are less likely to be standard sizes.[36]

(d) Commercial customers typically have greater certainty about when properties will become vacant and so work can be scheduled with more notice.

(e) Multi-sourcing is more common for commercial customers as they rarely tender or have contracts that tie them to one supplier for any given period of time.

(f) Commercial customers tend to have fewer properties than social housing customers, but the number of properties managed by commercial customers varies widely.[37]

(g) Commercial customers tend to operate at a regional, country-wide (that is, England, Scotland, or Wales)[38] or national (that is, Great Britain)[39] level. Customers with national SSVP requirements can purchase at the national level, purchase at the regional level but from a nationally-approved list of suppliers, or make all decisions at a regional level.

(h) Commercial customers appear to have a greater emphasis on quality and service delivery than social housing customers, who tend to be more price-driven.[40]

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[33] The provision of vacant property security services is not a requirement of insurers of commercial property, albeit suppliers tend to encourage insurance companies to recommend their services. Insurers therefore are not direct customers in this market, but do often use their market position to negotiate rates with preferred suppliers on behalf of property owners.
[34] See Appendix G, paragraph 14.
[35] Paragraph 5.7 above.
[36] The main parties told us that sheets of perforated steel could be used instead of steel screens/doors.
[37] See Appendix G, paragraph 15.
[38] In this report, by 'country-wide' we mean England, Scotland or Wales (unless otherwise stated).
[39] In this report, by 'national' we mean Great Britain (unless otherwise stated).
[40] See Appendix G, paragraph 10.

(i) While some segments of the commercial customer base could be considered mature, such as pubs, the broader commercial sector is less developed than the more mature social housing sector and appears to be a growth area.

5.19 Traditionally, commercial property owners/managers have secured their vacant properties using a broader range of security services than social housing customers. Large security companies (eg G4S and Securitas) may also offer vacant property security services, but they usually act as intermediaries outsourcing the supply of these services to specialist SSVP suppliers. More recently, suppliers of vacant property security services have had some success in selling their services to commercial customers by supplying SSVP as part of a broader range of vacant property services.

Our customer survey

5.20 We found that the number of properties managed by commercial customers varies widely. In our survey, one-quarter managed more than 5,000 but another quarter managed fewer than 50.[41] Vacant commercial properties were slightly more likely to be secured than vacant social housing properties: 17 per cent of customers had more than half their properties typically vacant, and a third of customers secured all of their vacant properties, with a further 9 per cent securing more than half their vacant properties.

5.21 Properties were most frequently secured when they were awaiting reoccupation or likely to be vacant for a long time. Another factor often noted by respondents was that properties needed to be secured in certain locations (mentioned by 35 per cent of commercial respondents).[42]

5.22 The period for which vacant properties were secured varied but was typically longer than in the social housing sector, although 28 per cent of customers were unable to give an answer for a typical vacancy period. Of those who could estimate, 17 per cent said less than a month, 21 per cent said one to three months, 25 per cent said three to six months and 19 per cent said six to twelve months, 13 per cent said one to two years and 6 per cent said more than two years.[43]

Suppliers of vacant property security services

5.23 Both of the main parties are suppliers of SSVP as well as non-security vacant property services. The parties supply both social housing customers and commercial customers nationally although, at the time of the merger, only SitexOrbis operated in Northern Ireland and VPS did not supply any customers in Northern Ireland.

5.24 The parties deliver SSVP out of a number of depots. By 'depot' in this report we mean a basic operational facility where stock (ie steel screens/doors and wireless alarms) is kept and from which customers are supplied and personnel operate. Management supervision may be exercised at depot level or centrally (from a central head office or at a regional ('branch') level). Depots are basic facilities and may serve a mixture of social housing and commercial customers.[44,45]

[41] Survey Q3–5, excluding 'Don't knows'.
[42] Survey Q6.
[43] Survey Q7.
[44] Suppliers may, in some cases, also use 'lock-ups' (which are typically small unmanned storage locations). Suppliers may also have third party storage facilities. For instance, this could be the case when property management intermediaries

Other providers of vacant property security services

5.25 SPS provides vacant property services in the UK, as well as other environmental and property management services to property owners. For the year ended 31 March 2011, the UK business turnover was £[✄] million. SPS operates nationally from four depots[46] across the UK.

5.26 Clearway provides vacant property services in the UK, as well as other environmental and property management services to property owners. For the year ended 31 March 2011, Clearway's turnover was approximately £[✄] million. Clearway operates nationally from two depots in the UK,[47] and is part of the Clearway Group, which provides property services more generally.

5.27 SecureSite provides vacant property services in the UK, as well as other environmental services to property owners. For the year ended 31 March 2011, SecureSite's turnover was £[✄] million. At the time of our report, SecureSite operated from one depot in the South-East of England.[48] It told us that it was planning to open a new depot in the Midlands and was also considering opening a new depot in the North of England at some point.

5.28 Table 1 shows the UK revenues of the largest suppliers of SSVP, Table 2 shows their revenues from SSVP only, and Figure 1 shows the locations of their depots. This list is not exhaustive of all suppliers of SSVP in the UK but we have tried where possible to gather information on all companies advertising the supply of steel doors and shutters. VPS told us that the market included a large number of local/regional suppliers of SSVP. There are likely to be additional suppliers not listed in Tables 1 or 2 (or shown in Figure 1) which operate mainly at a local or regional level (including a very small number of DLOs that provide services to other purchasers of SSVP); but we have seen very little indication that such suppliers provide significant competition to the larger specialist suppliers. We have excluded intermediaries which subcontract to the specialist suppliers in the tables, to reflect the companies that actually provide the services and avoid double counting. The tables also exclude self-supply (including DLOs that self-supply).

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subcontract SSVP to specialist suppliers. In such cases, those storage facilities will usually be used exclusively to serve the intermediaries' customers. We have not included either type of facility within our definition of a depot.

[45] We sought to explain our definition of a depot to SSVP suppliers to ensure we captured information from different suppliers in a consistent way; but we acknowledged that different suppliers may have slightly different definitions.

[46] SPS also has a small number of third party storage facilities. See footnote to paragraph 5.24.

[47] VPS/TDR told us that Clearway's website indicated that Clearway has 'nine fully-equipped operating centres with trained staff throughout the UK'. Clearway told us that this website was its old website and contained out-of-date information which it was in the process of removing. Clearway told us that it has only two operational depots in the UK (in Sheffield and Kent) and that it additionally had a couple of unmanned 'lock-ups' (in Birmingham and Liverpool).

[48] It also had a sales office in London.

TABLE 1 **Total UK revenues of suppliers of SSVP**

			£'000
Supplier	*Total revenue*	*Social housing revenue*	*Commercial revenue*
VPS	[✂]	[✂]	[✂]
SitexOrbis	[✂]	[✂]	[✂]
SPS	[✂]	[✂]	[✂]
Clearway	[✂]	[✂]	[✂]
Veritas*	[✂]	[✂]	[✂]
SecureSite	[✂]	[✂]	[✂]
North Star Estates	[✂]	[✂]	[✂]
Maltaward	[✂]	[✂]	[✂]
PSS*	[✂]	[✂]	[✂]
Pro-tex	[✂]	[✂]	[✂]
GMS	[✂]†	[✂]	[✂]

Source: Individual parties, CC analysis.

*Post provisional findings this table was expanded to include Veritas Property Management (Veritas), an SSVP supplier which appears to be capable of supplying parts of two regions in which we had provisionally found an SLC, and PSS, an SSVP supplier based in Scotland, one of the other regions in which we had provisionally found an SLC.
†GMS's total revenue includes a range of property services. Its revenue from vacant property services is £[✂] million.
Notes:
1. Data for most recent financial year available. May not sum due to rounding.
2. Loxal and Secure Empty Property were recent entrants and have been excluded from this table. We also excluded Shieldcom, a supplier whose main focus was on other activities and which earned a very small amount of revenue from SSVP.

TABLE 2 **UK SSVP revenues of suppliers of SSVP**

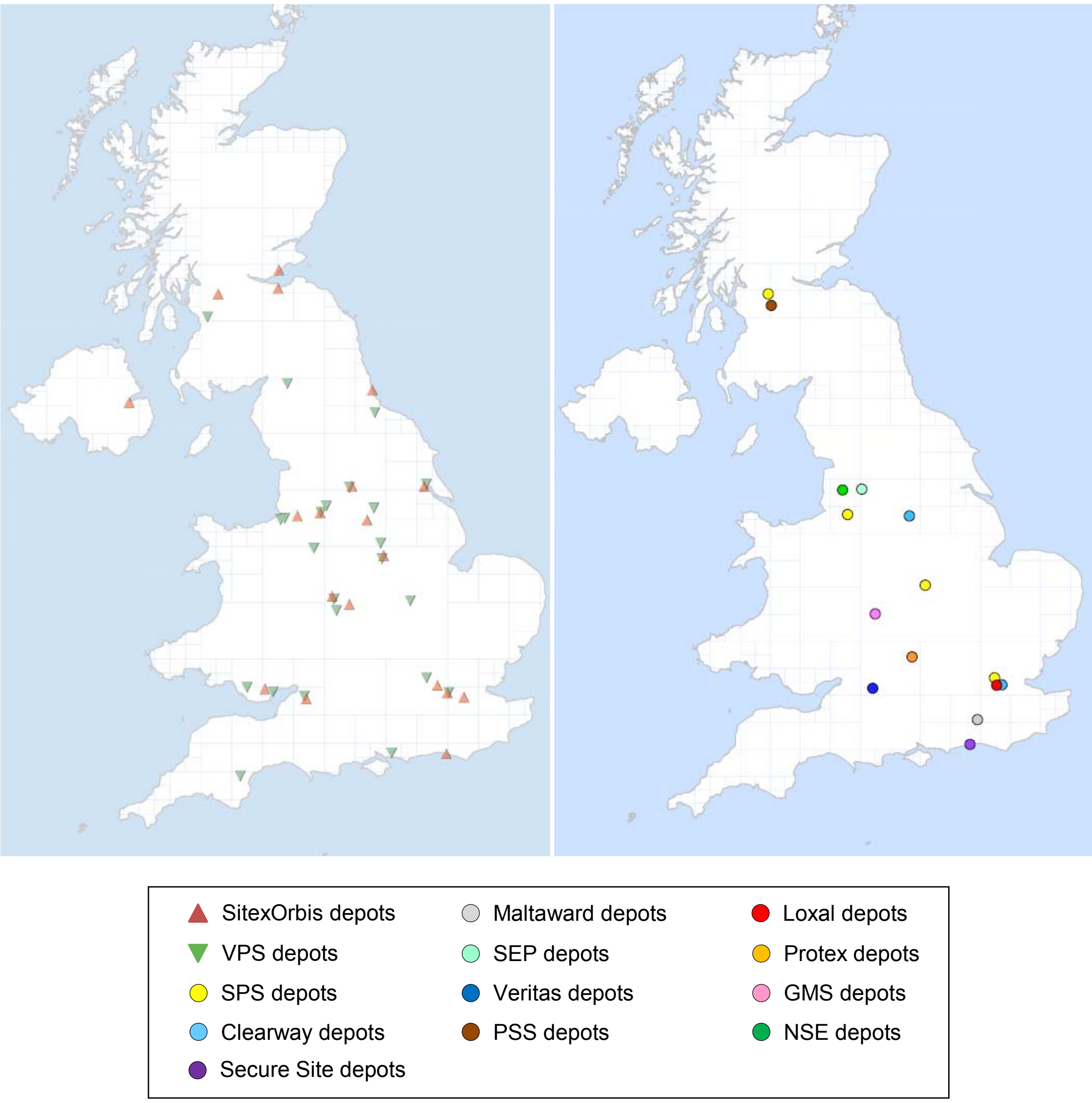
			£'000
Supplier	*Total revenue*	*Social housing revenue*	*Commercial revenue*
VPS	[✂]	[✂]	[✂]
SitexOrbis	[✂]	[✂]	[✂]
*SPS**	[✂]	[✂]	[✂]
Clearway	[✂]	[✂]	[✂]
Veritas	[✂]	[✂]	[✂]
SecureSite	[✂]	[✂]	[✂]
North Star Estates	[✂]	[✂]	[✂]
Maltaward	[✂]	[✂]	[✂]
PSS	[✂]	[✂]	[✂]
Pro-tex	[✂]	[✂]	[✂]
GMS	[✂]	[✂]	[✂]
Total	[✂]	[✂]	[✂]

Source: Individual parties, CC analysis.

*[✂] Hence this will overstate its SSVP revenue overall and in each of social housing and commercial.
Notes:
1. Data for most recent financial year available. May not sum due to rounding.
2. Loxal and Secure Empty Property were recent entrants and have been excluded from this table. We also excluded Shieldcom, a supplier whose main focus was on other activities and which earned a very small amount of revenue from SSVP.

FIGURE 1

Locations of the parties' depots (left) and competitors' depots (right)



Source: Depot locations from each individual supplier, CC analysis.
Note: The list of depot locations is provided in Appendix D.

Horizontal overlap

5.29 VPS and SitexOrbis are the two largest specialist providers of vacant property security services in the UK, providing very similar products and services. In particular, the physical products offered by the merging parties are similar, and are in many ways similar to the products offered by various competitors. We understand that the demountable steel screens, steel doors and permasteel offered by various suppliers do not vary greatly, if at all. Alarm systems may differ slightly but are broadly similar, and the Videofied alarm system supplied by RSI Technologies[49] is used by a number

[49] The Videofied alarm system is a video-activated monitoring alarm which, when triggered, sends a 10-second video clip to a security company's alarm monitoring station.

of companies. There are some differentiators, such as keyless doors, but we understand that these are not widely used.

5.30 VPS and SitexOrbis have a similar number of depots across the UK and their depot networks show similar geographic profiles: SitexOrbis has 20 depots in the UK, including one depot in Northern Ireland, and VPS has 23 depots[50] in Great Britain, but no presence in Northern Ireland. Depots and key inputs (such as stocks of steel screens and doors) to the merging parties' businesses are used to serve social housing and commercial customers interchangeably. Both parties' networks tend to show higher density of depots in the urban areas of Greater London; Bristol and Wales; the Midlands; and Northern England.

6. The counterfactual

6.1 We assessed the competitive effects of the merger relative to the competitive situation without the merger (the 'counterfactual'). Our Merger Assessment Guidelines explain that we may examine several possible counterfactual scenarios and must select the most likely scenario absent the acquisition.[51] The Guidelines note that the CC will typically incorporate into the counterfactual only those aspects of scenarios that appear likely on the basis of the facts available to it and the extent of its ability to foresee future developments.[52]

6.2 The main parties provided individual confidential submissions as to what would have happened to their businesses absent the merger. We also incorporated the views of other parties where relevant.

Summary of the parties' views on the counterfactual

6.3 VPS stated that:

> … it is appropriate to consider SitexOrbis' financial difficulties when considering the counterfactual against which to assess the competitive impact of the acquisition of SitexOrbis by VPS. The financial restructuring in 2008 which resulted in SitexOrbis' lenders taking a majority equity stake and control of the company, and the further restructuring in 2011 when debt could not be repaid, demonstrate that the prospect of prevailing conditions continuing is not realistic. SitexOrbis clearly would have become a significantly weaker competitive constraint absent the merger, as under its previous owners SitexOrbis would have continued to suffer due to its inability to invest in future growth as a result of its high levels of debt.[53]

6.4 TDR said that:

> Given recent debt market conditions and SitexOrbis' history of multiple debt restructurings, it is TDR's belief that under a continuation of the previous ownership, SitexOrbis would have been unable to refinance

[50] VPS has two depots in each of Bradford, Kilmarnock and Tipton. We counted these as one depot in each location to avoid overstating VPS's presence.
[51] *Merger Assessment Guidelines, CC2* (the Guidelines), paragraph 4.3.6.
[52] The Guidelines, paragraph 4.3.6.
[53] Initial submission, p38.

externally without a substantial reduction in the level of debt outstanding (i.e. a write-off for the debtholders).[54]

6.5 VPS/TDR believed that the former owners of SitexOrbis 'would not have agreed'[55] to a debt write-down and as a result 'would not have necessarily exited the market, but would have nevertheless have been in financial difficulty and would have been a weakened competitive force in the future' and therefore 'the competitive constraint imposed by SitexOrbis would have been highly unlikely to continue'.[56]

Assessment

6.6 In order to assess the appropriate counterfactual we considered two possible scenarios in the event that SitexOrbis had not been sold to VPS:

(a) SitexOrbis was not sold and remained an independent entity under the same ownership. In this scenario, we considered whether in the absence of an acquisition SitexOrbis would have been likely to remain a viable independent competitive entity.

(b) SitexOrbis was bought by an alternative buyer. In this scenario, we consider whether SitexOrbis would have been likely to have been acquired by an alternative purchaser and whether any alternative purchaser might cause competition concerns.

6.7 In our assessment of the counterfactual, we considered what would have happened to the SitexOrbis group (which included the Continental European businesses of SitexOrbis plus the UK, Republic of Ireland and Guernsey businesses of SitexOrbis) because the sales process covered the SitexOrbis group and we have not seen any evidence that the Continental European operations would have been sold separately (despite the fact that the transaction was structured as two separate purchase agreements of Continental Europe and the UK, Republic of Ireland and Guernsey businesses).

6.8 We summarize our analysis below. Appendix C sets out more fully the evidence we reviewed concerning the counterfactual.

Would SitexOrbis have remained a viable independent competitive entity?

6.9 To assess the viability of SitexOrbis as an independent entity, we considered:

(a) financial performance; and

(b) access to funding.

6.10 Management accounts to August 2011 (the first five months of FY2012) showed that, rather than deteriorating, EBITDA improved [✂]. The group also had £[✂] within its existing facilities.

6.11 In our view, the SitexOrbis group financial profile was not consistent with a failing firm likely to exit the marketplace in the foreseeable future. Nor did the financial profile

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[54] Initial submission, p38.
[55] Initial submission, p39.
[56] Initial submission, p39.

suggest that SitexOrbis would have exerted a significantly weaker competitive constraint absent the merger.

Access to funding

6.12 In exploring whether financing would have been an issue in the foreseeable future, we assessed SitexOrbis's financing arrangements, its ability to service its loan and the views of the former owners.

6.13 VPS and TDR said that:

> Information received from E&Y suggests that SitexOrbis was not able to afford its interest payments in the periods leading up to January 2011. Specifically, TDR was informed that, in the first half of the 2010/11 financial year (April–September 2010), the cash flow of £[✂] generated by SitexOrbis Group was not sufficient to cover interest payments on the outstanding debt.

6.14 In assessing this claim we noted that SitexOrbis's internal documents from September 2010 show £[✂] million in undrawn facilities. SitexOrbis said that undrawn facilities were £[✂] million. We considered therefore that SitexOrbis had adequate resources to cover a shortfall of the magnitude described by VPS/TDR.

6.15 We also noted that SitexOrbis management accounts for the year to January 2011 showed operating free cash flow of £[✂] million, cash flow before interest of £[✂] million, a debt service cost of £[✂] million and [✂].

6.16 TDR said that the statutory accounts showed cash generation of £[✂] million over FY09–11. TDR said that its own analysis showed that, adjusting for working capital so that it reflected typical levels for SitexOrbis, SitexOrbis would have generated £[✂] million in cash over FY2009 to FY2011 and a £[✂] million cash outflow in FY2011. We agreed that the cash inflow in FY2011 was principally generated by positive working capital management but found that even if we were to adjust for working capital in this way:

(a) The size of the outflow [✂] was small relative to available undrawn facilities and we did not find one small cash outflow to be evidence of a company suffering material cash-flow problems.

(b) The adjusted outflow must be set in the context of positive adjusted cash generation in FY2009 and FY2010 and an improvement in trading subsequent to FY2011.

6.17 We also note that SitexOrbis told us that its expansion plans in the commercial sector, where it planned to continue to grow, required no capital investment (but rather working capital finance) as the infrastructure had already been built.

6.18 In relation to whether or not there had been [✂].

6.19 [✂]

6.20 We spoke to the former owners of SitexOrbis as we considered that their evidence regarding the availability of future funding was important in assessing whether access to finance for SitexOrbis would have been materially reduced in the event that SitexOrbis had not been sold. Their evidence is shown in Appendix C (paragraphs 28 to 31). On the basis of this evidence, we considered that the former owners would have been very unlikely to reduce the availability of financing to SitexOrbis.

Our assessment on whether SitexOrbis would have remained a viable independent competitive entity

6.21 Our analysis indicated that prior to the merger SitexOrbis was functioning as a competitor, generating sufficient cash to continue trading in a similar way to prior to the merger and did not have significant financing issues. [✂]

6.22 In the absence of a bid, it is our view, based on the evidence of the former owners, that the former owners of SitexOrbis would have been very unlikely to restrict financing to the group. We considered that it would not have been in their interests to do so as it would have damaged the value of their investment in the business.

6.23 We considered that SitexOrbis would not have needed to access new external debt financing, as this would have continued to be provided by the former owners for the foreseeable future. We found that it was likely that if the former owners did continue to own the business, they would have sought further efficiencies, amended the covenants and/or extended the maturity of the debt if it became necessary, and that, as a result, the business would have continued to function as an effective competitor.

Would SitexOrbis have been purchased by an alternative buyer?

6.24 We now consider the second question in the counterfactual, namely in the absence of a bid from VPS would SitexOrbis have been purchased by an alternative buyer?

6.25 The sales process was conducted by E&Y following TDR's formal approach in March 2010. There were a number of interested parties, and a number of indicative offers were made in addition to the TDR bid (see Appendix C).

6.26 The bid from [✂] ('Bidder 1') developed furthest; the other indicative bids did not progress beyond the indicative bid stage of the sales process.

6.27 'Bidder 1' told us that it thought the SitexOrbis management team was credible. It knew that there was a strong buyer in the background (VPS) which could likely pay more for the business. 'Bidder 1' felt that it would be a strong contender if the VPS bid fell away.

6.28 'Bidder 1' told us that it planned to finance the transaction through equity and debt. It told us that it thought the planned debt finance of £[✂] million on the transaction was very deliverable given that the business was producing about £[✂].

6.29 SitexOrbis told us that E&Y determined that the 'Bidder 1' bid was credible, the most competitive to TDR's bid and had the support of management.

6.30 It was our view, based on the evidence of E&Y (see Appendix C) and 'Bidder 1', that if TDR had not bid and the owners had wanted to sell the business then they would have been able to do so. It was our view that 'Bidder 1' would have been a strong contender to buy the business in this scenario and that this potential purchaser would not have posed any competition concerns. In reality, [✂], in which case the owners would have continued to run the business (see paragraph 6.23).

Findings on the counterfactual

6.31 On the basis of our analysis, we found that, if VPS had not purchased SitexOrbis in September 2011, then the business would either have continued to be financed by its owners for the foreseeable future or have been purchased by an alternative buyer (such as 'Bidder 1') who would not have posed any competition concerns.

6.32 We noted that in both outcomes the counterfactual is the same; namely that SitexOrbis would have continued to be a viable independent business and the competitive conditions would be similar to those existing before the merger.

6.33 We concluded that the [✂]. Therefore it was more likely that the owners would have continued to manage the business rather than sell [✂], at least for the foreseeable future. However, whether SitexOrbis was sold or managed by its owners made no difference to the substance of the counterfactual.

6.34 In relation to Northern Ireland, we noted that post-merger, the SitexOrbis Republic of Ireland business was transferred to VPS whilst the Northern Ireland business continued to be part of SitexOrbis. However, our finding of the appropriate counterfactual was the continuation of the SitexOrbis business under the former owners (see paragraphs 6.31 to 6.33). In that case (and also in the event of a sale to another bidder), the appropriate counterfactual for Northern Ireland is that SitexOrbis would have continued to operate in Northern Ireland and VPS would not be physically present, so only one of the merging parties would be active there. We considered whether, against this counterfactual, the merger had resulted or may be expected to result in an SLC in Northern Ireland as part of our assessment of the competitive effects of the merger (see Sections 10 and 11).

7. The relevant markets

7.1 The Guidelines state[57] that the purpose of market definition is to provide a framework for the analysis of the competitive effects of the merger. The Guidelines go on to state that the CC and OFT (Authorities) will identify the market within which the merger may give rise to an SLC. The Authorities' aim when identifying the relevant market is to include the most relevant constraints on the behaviour of the merged companies.

7.2 The Guidelines also note that in practice the analysis leading to the identification of the market or markets and assessment of competitive effects in the market(s) will overlap, with many of the factors affecting market definition being relevant to the assessment of competitive effects and vice versa.[58] In this section, we set out the relevant markets in which we have reached our conclusions on the SLC test, with reference to the competitive assessment in the subsequent sections.

Main parties' view of the relevant market

7.3 VPS and SitexOrbis said[59] that the relevant product market should be defined no more narrowly than the supply of integrated vacant property services, including:

(a) physical security (steel/wooden screens and doors, polymer screens, steel perma-screens and electronic key management services);

[57] The Guidelines, paragraph 5.2.1.
[58] The Guidelines, paragraph 5.1.1.
[59] Initial submission, paragraph 5.1.

(b) ‘proactive security’ (inspection services, lock changes, first-response service, live-in guardians and manned guarding);

(c) alarms (including first-response services);

(d) clean-and-clear services; and

(e) facilities services.

7.4 The parties submitted that ‘the relevant geographic market for the purposes of assessing the potential competitive effects of the Acquisition should be defined as having national, local and regional aspects’.[60] In particular, the parties argued[61] that:

(a) most customers were close to the depot from which they were supplied;

(b) prices generally depended on local conditions; and

(c) prices set out in agreements with national coverage were still affected by local conditions.

Product market

7.5 The OFT referred to us the merger between VPS and SitexOrbis, with a particular view to the supply of security services for vacant properties consisting, in particular, of the sale, rental or installation of steel and polymer screens, steel doors, perma-steel sheeting and battery-powered GSM alarms in order to secure vacant property, which we have referred to collectively as SSVP for the purposes of this report. In addition to these services, the parties also overlap in the supply of non-security vacant property services (eg clean-and-clear, facilities services).

7.6 We took as our starting point the supply of SSVP as the narrowest likely relevant product market. In this section, we assess the evidence on the extent to which customers were willing to switch from SSVP, first to non-security vacant property services, and secondly to other types of vacant property security services. The structure of our analysis was that if we found that any of these services were close enough substitutes to constitute a sufficient constraint on the pricing of SSVP, we would expand our product market definition to include the relevant service. If not, we would assess the merger within the framework of a product market for SSVP but we would still consider the constraint imposed by these other ‘out-of-market’ services.

Non-security vacant property services

7.7 We note that security services were often procured under the same contracts, and from the same suppliers, as other vacant property services (clean-and-clear services and facilities services). However, this in itself was insufficient to demonstrate that security and non-security services were within the same relevant market. They did not appear to be for the following reasons.

7.8 By their nature and purpose, non-security services were not direct substitutes for security services. Although they were often supplied together, they could also be supplied separately and often were, and we did not consider that many customers had a strong requirement to purchase them together (although there may be some

[60] Initial submission, paragraph 6.1.
[61] Initial submission, paragraph 6.7.

convenience value to doing so). For example, in our survey only 2 per cent of SitexOrbis customers and no VPS customers said that product range was the main reason for using that supplier; and 'product range' and 'ability to provide other services' were two of the three least important factors when choosing an SSVP supplier.[62] According to the parties' internal documents, customers could see the difference between specialists and general security companies and customers have different sourcing arrangements for different products.

7.9 Even when supplied together, it was the need to secure (ie protect) a vacant property which drove a customer's choice of provider, rather than, for example, clean-and-clear services. Moreover, there appeared to be a wide range of suppliers for non-security property services, ranging from large facilities management companies and small local firms, whereas relatively few companies supplied SSVP.

7.10 For these reasons, we found that non-security services did not constrain directly the prices charged for SSVP and were not part of the relevant product market.

Vacant property security services other than SSVP

7.11 The parties submitted that demand for SSVP was 'highly price sensitive due to the limited (if any) product differentiation within physical security products and within alarms, and the wide variety of alternative approaches available to customers of vacant property services'. Among these alternative security approaches the parties included 'board-up, use of [live-in] guardians, measures to disguise vacant properties to make them look occupied or simply doing nothing'.[63]

7.12 The parties submitted that there were [✂]. Clearly each type of security product had its advantages and disadvantages, which must be set against the differences in price between them. Our concern was whether alternatives to the parties' vacant property security services were close enough substitutes that they would constrain a price rise (or reduction in service quality) post-merger.

7.13 We divided vacant property security services other than SSVP into two categories:

(a) alternative physical security products, eg wooden boarding; and

(b) alternative non-physical security products, eg CCTV, manned guardians, live-in guardians.

Alternative physical security products

7.14 The parties supplied some examples of customers switching to alternative physical security products, which we discuss in Appendix G. However, the consensus from most third party comments was that customers had specific requirements for the level of security they needed and that different physical security products were perceived as appropriate for distinct security requirements. These requirements could vary by property, but most customers were reluctant to change the level of security for a given property.[64]

7.15 In particular, wooden boarding was felt to be less secure and more easily vandalized, did not provide proper ventilation, degraded in winter and was subject to an arson

[62] Survey Q15a/17a & Q32.
[63] Initial submission, paragraph 5.4.
[64] See Appendix G for some examples (paragraphs 37–49).

risk. It might be used as a temporary measure but was not generally considered to be a good substitute for steel (or polymer, which was considered to be a better substitute for steel[65]). We saw some examples of wood being used for properties scheduled for demolition where security needs were not as stringent and ventilation was less important.[66] SitexOrbis told us that wood was not a security product: it was a substitute for glass, and it used wood only to replace broken glass overnight for police and emergency services. It said that its customers did not require or ask for wood.

7.16 Our customer survey indicated that steel and wood are used for very different reasons. The main reason for using steel instead of other security measures was that it is 'more secure', cited by 55 per cent of commercial and 58 per cent of social customers, with the second most common reason being durability (11 per cent and 15 per cent respectively). 'For specific locations' was also mentioned by 10 and 8 per cent respectively. The reasons for using wood were cost factors (51 per cent of commercial customers who used wood, 26 per cent social) and also as a temporary solution (16 per cent commercial, 18 per cent social); only 7 and 3 per cent respectively said that wood was 'more secure'. This suggested that wooden boarding was unlikely to be a close substitute for steel screens/doors for most customers.

7.17 Our survey also found that a number of customers said they would consider a 'cheaper alternative' if prices rose.[67] This was consistent with our view that a minority of customers would be willing to consider other physical security products (primarily wooden boarding) as a substitute for steel or polymer, but suppliers would be able to identify these customers when they discussed their needs with suppliers and asked for prices.[68] Therefore we did not find that wooden boarding was a sufficiently close substitute for sufficient customers to warrant inclusion within the relevant market.

Alternative non-physical security products

7.18 The parties also provided some examples of social housing customers using non-physical security products like CCTV and manned guarding for vacant properties as an alternative to physical security.

7.19 However, these examples did not appear to reflect switching in response to price rises; they may simply reflect a more suitable solution for certain customers or properties. In particular, we were told that manned guarding was a very expensive solution and we would not expect it to be a significant constraint on physical security or alarms.

7.20 VPS told us that it would not expect smaller residential properties (eg a semi-detached council house) or smaller commercial properties such as pubs to be protected with CCTV or manned guarding.

7.21 Live-in guardians do not appear to be a suitable substitute for SSVP either. Although Camelot told us that they could be used for any property type, live-in guardians were mostly used to protect commercial properties which are part of demolition and/or re-furbishment programmes, and suppliers of live-in guardians were not present on any vacant property security procurement frameworks.

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[65] See Appendix G, paragraph 51.
[66] See Appendix G for some examples (paragraphs 37–49).
[67] Discussed in more detail in paragraph 9.14 below. Customers did not specify what a cheaper alternative would be and it was not necessarily a cheaper physical security alternative.
[68] In paragraphs 9.11–9.13 below we explain why the existence of a minority of customers who would be willing to substitute to wood is not likely to protect other customers from price rises.

7.22 Our view was that neither alternative physical security services nor non-physical security services were likely to be a suitable substitute for SSVP for most customers in the social housing or commercial sectors. While in some circumstances there may have been some degree of substitutability, our view was that vacant property security services other than SSVP could not be expected to impose effective constraints on the pricing of SSVP.

Reduction in the demand for security services

7.23 Finally, the parties submitted that they were aware of instances where customers had 'reduced or completely switched away from using vacant property security services'.[69] They provided the example of [✄] decision to remove VPS alarms and said they understood that this decision was taken due to a reduction in budget. Other cases cited by the parties illustrated situations where customers used services other than SSVP. These examples did not generally appear to reflect switching in response to price rises; they may have simply reflected a more suitable solution for certain customers or properties. Third party comments suggested that customers generally had little scope for reduction in the purchasing of security services given the risk of costly property damages and/or insurance requirements. For instance, Ealing Council said that using steel security measures would remain cost effective even after a 10 per cent price increase in steel security measures.

Geographic market

7.24 In this section, we present our view on the geographic aspects of the provision of SSVP to social housing and commercial customers. This analysis was relevant both to the definition of the relevant geographic market and to the assessment of unilateral horizontal effects at local or regional level. This corresponded to the first theory of harm in our issues statement:

> The first theory of harm is that the merger would remove an important competitive constraint at the local or regional level. Currently, it appears that the merging parties have significant geographic reach at a local and regional level via their depot networks. Following the merger, the loss of SitexOrbis as a competitive constraint on VPS at a local or regional level could lead to higher prices and/or a lower quality of service offering.

7.25 We shared the view submitted by the parties that for the purposes of assessing the competitive effects of the merger, the relevant geographic market 'should be defined as having national, local and regional aspects'.[70] When assessing catchment areas—especially for commercial customers where there seems to be greater variation—we considered the sensitivity of our assessment to variations in the assumed distances that suppliers may be willing to travel. Our first objective was to ensure that we have captured any geographical areas where there may have been a competition problem as a result of the merger, and our second was to check that our conclusions on whether there was a problem were sensitive to the assumptions we had made on distances.

[69] Initial submission, paragraph 5.32.
[70] Initial submission, paragraph 6.1.

Local/regional demand for SSVP

7.26 Social housing customers and most commercial customers managed properties located within a limited geographic area and did not require their suppliers to be able to operate on a national basis. Although vacant property security services could in principle be provided from a distant depot, a number of factors suggest that customers preferred suppliers located reasonably nearby:

(a) social housing customers in particular required their vacant properties to be secured at short notice and asked their suppliers to offer short response times; and

(b) some customers preferred suppliers who had local knowledge so that they could assess the risk associated to each property and recommend the appropriate security measures to be adopted.

7.27 On the supply side, transportation costs were likely to constrain suppliers' willingness to serve a property from a distant depot, particularly for social housing customers, and we thought that economies of scale and density may emerge from securing a number of nearby properties.

7.28 The combination of both demand and supply factors suggested that competition took place at a local level for social housing customers and at a regional level for some commercial customers. In addition, some commercial customers had national SSVP requirements (see paragraphs 7.38 to 7.44).

Catchment area analysis

7.29 VPS submitted, on the basis of its own data, that 'on average 80 per cent of social housing customers were located within [approximately 20–30] miles of the depot'.[71] According to data provided by VPS, the corresponding figure for commercial customers was [40–50] miles. VPS reported average maximum distances travelled by VPS to be [60–70] miles for social housing customers and [90–100] miles for commercial customers.[72]

7.30 VPS/TDR's economic advisers, CRA, suggested that 'on the basis of the available data [50–60] miles for social and [70–80] miles for commercial are reasonable to use as the limit of coverage of competitor depots'.

7.31 We used data on actual travel distances provided by the parties to perform a catchment area analysis. This analysis helped us to identify the size of the local markets and the extent to which the parties overlapped with each other and with their competitors at the local level. Catchment area analysis was also useful to assess the geographical coverage of each of the main parties and their competitors. This was relevant to identify market players' ability to operate at a local, regional and national scale. A detailed description of the analysis is presented in Appendix D.

7.32 Considerable variation across depots in the size of the areas within which 80 per cent of customers were located suggested that a number of depots were operating within limited geographic areas, not fully exploiting their potential geographical reach. This may be due to two main factors:

[71] Initial submission, paragraph 6.9.
[72] Initial submission, paragraph 6.11.

(a) Depots could have been located in local areas with a high density of properties and operated at full capacity just by serving close-by properties.

(b) Depots of the same supplier could have been located relatively close to each other in densely populated areas, reducing the distances they needed to travel.

7.33 Suppliers may have been willing to travel longer distances than they actually did and these longer distances may still have proved economical when travelled on a regular basis. In order to obtain a measure of how far it was typically economical to travel, we focused our attention on VPS and SitexOrbis depots whose geographical coverage did not appear to be constrained by either of these two factors.

7.34 Our approach focused primarily on 80 per cent travel distances to exclude atypical journeys, and was based only on certain of the parties' depots, to exclude those that were close to other depots and thus travelled artificially short distances. This approach tended to maximize the size of these catchment areas, as actually most of the parties' depots serviced significantly smaller geographic areas. Therefore, our results may have overestimated the distances that an SSVP supplier could competitively travel on a regular basis. We also noted that we had analysed distances travelled on a 'straight-line' basis rather than likely driving distances and this should be kept in mind when interpreting the results.

7.35 Following this approach, we defined the following ranges as catchment areas indicating how far it was typically economical to travel to serve social housing and commercial customers:

(a) up to 40 miles to serve social housing customers; and

(b) up to 70 miles to serve commercial customers.

7.36 These definitions were consistent with the views expressed by alternative SSVP providers in response to market questionnaires and in oral hearings (see Appendix D). We noted that these ranges are not dissimilar to those suggested by the parties' economic advisers (see paragraph 7.30). Nevertheless, in the assessment of the competitive constraints imposed on the parties by alternative suppliers of SSVP, we tested the impact of assuming even larger catchment areas of up to 100 miles in the provision of SSVP to commercial customers (although this was likely to provide an indication of the distances they were willing to travel for a valuable customer rather than a distance they were willing to travel on a regular basis). We are aware that suppliers sometimes travelled further than 100 miles and hence won business in a region a long way from their depot, but we understand that this was generally either as part of a wider contract with a valuable customer (ie the trip would not be profitable on its own but the customer relationship is profitable) or because they expect to be able to earn enough from the installation (eg from a high price or because the security products will be installed for a long enough period) to make it viable.

7.37 CRA, on behalf of VPS, suggested an alternative, customer-centred approach. It submitted that, for example, [✂] per cent of its commercial customers had at least two alternative suppliers (in addition to VPS and SitexOrbis) within 70 miles of their location.[73] We considered that this approach was reasonable in principle, but was effectively the inverse of our depot-centred approach and carrying out the analysis on this basis would produce equivalent results. In other words, if we found a region of the country which was not covered by circles centred on competitors' depots, we

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[73] We note that the figure of 85 per cent produced by CRA and VPS was based on a different set of competitor depots (including a number of alleged Clearway depots that we found did not exist) and hence the figure is incorrect.

would also find that each circle centred on a customer in that region would have no competitors' depots within it. Therefore it was not necessary to carry out this approach in order to identify a possible SLC. We were also concerned that if we centred our analysis on VPS's customers, we would omit many potentially affected customers (including those that currently use SitexOrbis and prospective customers) and, in any case, we would still have concerns over the remaining customers ([✂] per cent in the example above). We discuss CRA's analysis further below (see paragraphs 10.16 to 10.19 and 11.16 and 11.17).

National demand for SSVP among commercial customers

7.38 A proportion of commercial customers managed properties located across the UK and exhibit a preference for suppliers that can operate on a national basis. This was especially the case for large commercial customers that managed the purchasing of SSVP on a centralized basis.

7.39 In our customer survey, we found that 31 per cent of commercial respondents operated on a nationwide (Great Britain) basis, and a further 15 per cent operated on a country-wide (ie England, Scotland or Wales) basis. Of these two groups of customers, 47 per cent said that national coverage was very important to them.[74] Not all of these customers made decisions about their SSVP supplier at the same level; 20 per cent of them made decisions on a Great Britain basis, and a further 11 per cent on a country-wide basis. Of these two groups of customers, 57 per cent said that national coverage was very important to them.

7.40 VPS told us about its large-scale customers. It said that it had [✂] commercial customers who used its services throughout Great Britain and contracted and commissioned work on a centralized basis, accounting for [✂] per cent of the commercial properties it protected and [✂] per cent of its commercial revenues.[75] In total (ie including the above figures), customers using services from more than one VPS depot accounted for [✂] per cent of the commercial properties VPS protected and [✂] per cent of its commercial revenue.

7.41 We noted that there were customers who may commission on a regional basis but still have a strong preference for a nationwide supplier. For example, [a major grocery retailer] commissioned on a regional basis but told us that it handled its procurement of vacant property security services centrally. This retailer told us that it used SitexOrbis and VPS on an ad-hoc basis, but they were the only two suppliers that could currently service its needs, despite its regional commissioning. Other commercial customers, including Enterprise, Axa and Spirit, told us that they required a supplier which could offer a single price and level of service for properties across Great Britain, a requirement that would be difficult to meet by using a range of regional suppliers.

7.42 Taken together, our evidence suggested that competition takes place at a national level for a number of customers, notably large commercial customers with portfolios of properties spread across Great Britain. Accordingly, we have assessed the effects of the merger on commercial customers with nationwide requirements.

7.43 On the basis of our catchment area analysis, we concluded that SSVP providers are prepared to travel up to 70 miles to serve a commercial customer, and perhaps in some circumstances up to 100 miles.

[74] Rated 4 or 5 out of 5 in importance.
[75] SSVP revenues only.

7.44 National requirements were likely to be less of a consideration in the social housing sector, although we noted that intermediaries providing property management services to social housing customers typically manage properties located across Great Britain. When outsourcing SSVP to third parties, they may have preferred a supplier offering nationwide coverage. Similarly, framework providers may have found it convenient to appoint suppliers on a nationwide basis. However, we have seen no evidence that this is a necessary requirement and so we have not assessed the social housing market on a national basis.

Findings as to the relevant markets

7.45 The parties provided vacant property security services to two broad types of customers: social housing and commercial customers. As the requirements of each type of customer were distinct,[76] we concluded that it was appropriate to assess the effects of the merger for the two sectors of customers separately. Where appropriate, we considered interactions between the two customer sectors.

7.46 In relation to the scope of the relevant product market, we found that vacant property security services other than SSVP (see paragraph 7.13) were unlikely to be a suitable substitute for SSVP for most customers in the social housing or commercial sectors and the evidence did not support a view that switching to other security services would constrain a price rise by a hypothetical monopolist in SSVP.[77] The competitive effects of the merger were therefore assessed in the market for SSVP.

7.47 In relation to the geographic scope of the relevant market, we found that the relevant geographic market should be defined as having national, local and regional aspects.

7.48 Therefore, we concluded that the relevant markets for the purposes of our statutory questions in this inquiry were:

(a) the supply of SSVP to social housing customers at a local level (up to 40 miles of travel distances);

(b) the supply of SSVP to commercial customers at a regional level (up to 70 miles of travel distances); and

(c) the supply of SSVP to commercial customers at a national level.

7.49 Although the competitive effects of the merger were assessed for each of these markets separately, we took account of interactions between them as appropriate.

8. Theories of harm

8.1 In our issues statement, we set out three theories of harm. All of these theories involved unilateral horizontal effects: at the local or regional level; at the national level; and for certain categories of customer. The Guidelines say that unilateral effects can arise in a horizontal merger when one firm merges with a competitor that previously provided a competitive constraint, allowing the merged firm profitably to raise prices on its own and without needing to coordinate with its rivals.[78]

[76] See paragraph 5.7 above.
[77] See Appendix G.
[78] The Guidelines, paragraph 5.4.1.

8.2 We did not identify any theories of coordinated effects or vertical effects which were likely to be relevant to this merger.

9. Assessment of the merger

9.1 In accordance with our assessment as to the appropriate relevant markets for the purposes of our statutory questions, we assessed the merger according to its unilateral effects on:

(a) social housing customers at the local level;

(b) commercial customers at the regional level; and

(c) commercial customers at the national level.

9.2 We assessed the merger in relation to both the loss of actual competition and the loss of *potential* competition. The latter concept was relevant in local/regional areas where only one of the merging parties was active. In these areas, we considered whether the party that was not active may nevertheless have constrained the active party through the threat of entry into that area. If so, then the merger could have removed or reduced *potential* competition in that area.[79]

9.3 We first summarize features common to the supply of SSVP to all customers (Section 9); then address competitive effects in the social housing market (Section 10); and then address competitive effects in the commercial market (Section 11), noting where effects may be different for customers requiring a nationwide supplier and for customers requiring services at a regional level.

9.4 Given our finding regarding the counterfactual, we considered the supply of SSVP throughout Great Britain and Northern Ireland separately. Our analysis below is focused on competition in Great Britain unless otherwise stated.

Nature of the merging parties' products and services

9.5 The Guidelines say that if products are not differentiated, unilateral effects resulting from the merger are more likely where: the market is concentrated; there are few companies in the affected market post-merger; the merger results in a company with a large market share; there is no strong competitive fringe of companies; the merger involves a company with a reputation for aggressive price cutting; or customers have little choice of alternative supplier.[80]

9.6 Where products are differentiated, for example by branding or quality, unilateral effects are more likely where the products of the merging companies are close substitutes; where variable profit margins are high; or where customers are relatively insensitive to changes in the prices of the merging companies' products.[81]

[79] See in particular paragraphs 10.13 & 10.77.
[80] The Guidelines, paragraphs 5.4.4 & 5.4.5.
[81] The Guidelines, paragraph 5.4.9. The size of the (gross) margins is relevant because in a typical unilateral effects scenario, the merging firms consider raising prices. Prior to the merger, each firm would lose some sales to competitors. After the merger, some of those lost sales are 'recaptured' by the other merging firm. The higher the variable margin, the greater the value of recaptured sales, and so the more profitable the price rise becomes.

9.7 In this case, it appeared that the physical products offered by the merging parties were similar, and are in many ways similar to the products offered by various competitors, as we noted above.[82, 83]

9.8 However, there were differentiators between the services offered by companies in this sector. For example, we have been told that quality and reliability are among important factors in choosing a supplier,[84] which implied that suppliers were likely to differ in these respects and would try to compete on these measures. Secondly, SSVP were often supplied in conjunction with other services (such as non-security vacant property services; see paragraphs 7.7 to 7.10), which some suppliers may not have offered and which other suppliers may have subcontracted (although we did not consider that this was a major differentiator for the majority of customers[85]). Thirdly, the geographical location of suppliers and/or the extent of their depot networks was an important consideration for many customers and was a clear point of differentiation between the merging companies and other suppliers.[86]

9.9 In our competitive assessment, we considered all the factors identified in paragraphs 9.5 and 9.6 above; but we gave particular weight to evidence as to whether the merging parties were close competitors (for some or all customers) and how close other competitors were, because a simple count of the number of competitors is less informative than consideration of the identity and closeness of competitors. We return to these points in our competitive assessment below.

Arguments made by VPS about the nature of competition

9.10 In this section, we consider two arguments made by VPS in support of an argument that a merger between two large suppliers, with few other active suppliers, will not lead to an SLC. The first of these arguments was that the existence of 'marginal' customers prevented companies raising prices to customers who perceived less effective competition post-merger. The second of these arguments was that in some types of bidding market, 'two is enough'—in other words, there did not need to be many active suppliers because any second supplier would sufficiently constrain the price of the first. We summarize each of these arguments below; a more detailed discussion can be found in Appendix F.

Protection provided by marginal customers

9.11 Our concern was that the main parties may have increased their prices post-merger. If they did so, we would expect that some customers would have stopped buying from the merged entity, or reduced their purchases, and we refer to these customers as 'marginal customers'. Other customers would have continued to purchase as before, and we refer to them as 'infra-marginal customers'. VPS submitted to us that our focus needed to be on marginal customers, not infra-marginal ones:

> That is to say that, in addition to focusing on alternative suppliers (or new entrants) and alternative products, the focus in this case should be on those customers who currently purchase the Parties' products but

[82] See paragraphs 5.29 & 7.11.
[83] There were some product differentiators, such as keyless doors (although we understood that these were not widely used).
[84] See paragraphs 10.54, 11.65 & 11.66 below.
[85] See paragraph 7.8 above.
[86] See Figure 1 for a comparison of depot networks.

who would either stop doing so or who would buy less if post-merger prices were to rise.[87]

9.12 In other words, VPS argued that it did not matter if there was a large proportion of customers that would accept a price rise (infra-marginal); what mattered was whether there were enough customers who would move away from the merged company (marginal), so if it increased prices to all customers, the lost profit from these marginal customers would outweigh the increased profit from infra-marginal customers. If there were enough marginal customers, the merged company would be deterred from raising prices to infra-marginal customers.

9.13 As we discuss in Appendix F, we did not consider that this argument applied well to this sector, which was characterized by individually negotiated services and pricing; for example, [✂].

9.14 We found evidence that the parties had the ability to set different prices for different customers even before the merger. We investigated pricing data provided by SitexOrbis and identified substantial price variation across customers (including both social housing and commercial customers) for the same services. Figure 2 shows a histogram representing the range of weekly rentals charged by SitexOrbis in 2010 and 2011 for a key-operated steel door[88] and the share of customers that were charged each level of prices. Almost 35 per cent of SitexOrbis customers in the sample were charged between £[✂] and £[✂] per week for a steel door, another 30 per cent were charged less than £[✂] per week and the rest paid weekly rentals above £[✂]. Some customers paid more than £[✂] per week for a steel door, as reflected in the histogram.[89]

FIGURE 2

SitexOrbis weekly rentals for a keyed steel door

[✂]

Source: CC analysis based on data provided by SitexOrbis.

9.15 Although VPS did not provide extensive data on prices charged to customers, it submitted a limited number of bespoke price lists sent by VPS to some of its largest commercial customers. The median price for a keyed steel door in the price lists submitted by VPS was £[✂] per week, very similar to the median for SitexOrbis prices which was £[✂]. However, in 2011 VPS offered some customers weekly rates of £[✂] for a keyed steel door, while other customers were offered the same service at a weekly rate of £[✂]. This variation in prices charged for a relatively homogeneous product showed that the parties had the ability to set different prices for different customers and that it was common practice for them to do so.

9.16 VPS argued that this price dispersion was driven by the need to structure prices depending on factors specific to a particular job, such as whether there ware fit and remove charges; the length of the rental period; other services provided; the number of assets (ie steel screens/doors etc) fitted; and drive-time from the nearest depot.[90]

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[87] Initial submission, paragraph 10.3.
[88] The data submitted by SitexOrbis included the weekly rental paid by each customer for each service provided. In some cases a single figure included a mix of services. We excluded these observations and restricted the sample to those observations for which the figure provided referred unambiguously to the weekly rental of a single key-operated steel door. The final sample used to produce the histogram had [✂] observations.
[89] [✂] We viewed that complexity as a further means of differentiating prices.
[90] VPS & TDR response to CC provisional findings, paragraph 3.52.

We acknowledged that price structures can be complex, although this in itself facilitates price discrimination by making it difficult for customers to compare prices offered by different suppliers and by making it difficult for customers to compare the price they paid with the prices other customers paid.

9.17 The data available was not amenable to more complex analysis, but we considered that the simple price dispersion evidence above was a strong indicator of price discrimination in the absence of evidence to the contrary. We also noted that there was a range of other evidence of price and margin variation, including:

(a) It was widely acknowledged that margins were higher in the commercial sector than in the social housing sector.

(b) VPS told us that within the social housing sector, prices and margins for quote and order work were [✂] than for tendered contracts.

(c) When giving us a 'ready reckoner' of prices, VPS told us that 'there is considerable variance in pricing in the market'.

(d) Some customers had seen their prices vary by a very large amount from contract to contract—for example, Nottingham City Homes told us that [✂].

(e) We have been told that the prices paid by [✂] varied considerably: [✂].

9.18 For these reasons we found that the parties had the ability, as well as the incentive, to set different prices for different customers. We expected the merged company to have the ability to identify which customers were price sensitive and avoid price rises for them while increasing prices to less sensitive customers. Therefore the existence of a body of marginal customers was unlikely to protect infra-marginal customers from price rises.

Bidding markets

9.19 Many of the ways in which the parties negotiated prices could be described as 'bidding markets'. For example, tenders could involve a supplier submitting a price list and quality of service assurances without knowing what competitors are offering. The quote and order sales process could also be interpreted as a supplier submitting a bid without knowing what other suppliers have already bid or what they might subsequently bid. VPS/TDR appeared to agree with this interpretation.

9.20 VPS/TDR claimed that where companies did not know their competitor's bid and had no opportunity to vary their own bid, two competitors were sufficient for competition, and so long as there were at least two companies post-merger, competition was not affected by an increase in concentration.

9.21 It may be that under certain 'ideal' conditions, two companies may provide enough competition to give rise to a fully competitive outcome. However, in our view, this market did not fit those conditions.

9.22 Professor Paul Klemperer has identified[91] a number of conditions he considers to be necessary to satisfy the 'typical definition of an ideal "bidding market"', which we describe in Appendix F. However, Professor Klemperer considered that, once any of the extreme assumptions of an 'idealized bidding market' are relaxed, 'we are quickly

[91] See www.competition-commission.org.uk/our_role/analysis/bidding_markets.pdf.

back into the familiar world of problems of dominance and unilateral and coordinated effects'.

9.23 As discussed in Appendix F, many of these conditions did not hold here. Therefore we would not expect a single competitor—especially one that was less similar to the merged party than the merging parties are to each other—to be an effective competitive constraint and that it was not possible to expect that two bidders post-merger would be enough to prevent any SLC regardless of the identity of the competing bidders.

10. Assessment of the competitive effects of the merger: social housing sector

10.1 The merging parties both supplied social housing customers, with [✄] per cent of SitexOrbis's SSVP revenues and [✄] per cent of VPS's coming from this sector.[92] As we noted above (paragraphs 5.8 to 5.15 and 7.26), the key features of the social housing market were that customers tend to have local needs and demand fast response times; the sector had been flat or declining for a number of years; and revenues and margins had been falling.

10.2 In this section, we consider the extent to which social housing customers thought other products were a good substitute for SSVP; the distances suppliers were willing to travel to serve social housing customers; the closeness of competition between the merging parties; the ability and willingness of customers to self-supply; and evidence about customer responses to a hypothetical price increase (which incorporates all customers' possible options in response to a price increase). We also consider the likelihood that entry or expansion would constrain a price increase, and the role of economies of scale. Finally, we consider whether there were any other countervailing factors that may prevent a price increase: buyer power for some customers and relevant efficiencies for the merging parties.

10.3 We assessed whether the merger was likely to cause prices to rise above pre-merger levels for a sustained period. VPS argued that this was the wrong benchmark since 'the current price … appears to be below the sustainable competitive price'. However, the argument that pricing in any of the SSVP markets was not sustainable pre-merger was not supported by our analysis of the counterfactual. We saw no evidence that pre-merger prices were unsustainable for the merger parties (although we did have a concern that other, smaller suppliers do not appear able or willing to compete at the levels at which VPS and SitexOrbis bid for work, as we discuss in paragraphs 10.101 to 10.104). We also found that the parties' gross margins in the social housing sector were [✄] (in the region of [✄] per cent) and that fixed costs were shared with other services. This did not suggest that social housing prices were unsustainable, especially as part of a wider business. We therefore considered that the correct benchmark for our analysis was whether the merger was likely to give rise to prices above pre-merger levels for a sustained period, consistent with our practice in merger control analysis.[93]

Alternative products/services

10.4 We assessed the extent to which alternative products were likely to impose a constraint on the prices of SSVP in Appendix G. We noted that there were some

[92] See Tables 3 & 7.
[93] The Guidelines, section 5.4 (Horizontal Mergers—Unilateral Effects).

examples of social housing customers using alternative security measures. Customers told us that they assessed the security needs for each property and were reluctant to accept a lower level of protection (such as wooden boarding, CCTV or security guard patrols) in order to make a cost saving. Customers also told us that cost savings would be outweighed by the risk of high costs of damage that could be caused if properties were not sufficiently protected.[94]

10.5 Our customer survey found that a number of customers said they would consider a 'cheaper alternative' if prices rose: we estimated that 10 to 15 per cent of customers would seriously consider doing so following a 5 per cent price increase applied to all customers by both parties.[95] As discussed in paragraph 7.17 above, this was consistent with our view that a minority of customers would be willing to consider other physical security products (primarily wooden boarding) as a substitute for steel or polymer, but this willingness would become apparent when they discussed their needs with suppliers and asked for prices.[96] Therefore suppliers were likely to be able to identify which customers are willing to substitute to alternative services and which were not, and set prices accordingly.

10.6 VPS indicated that manned guarding and CCTV were unlikely to be suitable alternatives for many types of property, including social housing. Customers also told us that for social housing properties manned guarding was prohibitively expensive and not a viable option. Few customers considered that live-in guardians were a viable option for them.

10.7 Our investigation found that customers were more willing to accept a lower level of protection for properties scheduled for demolition or extensive renovation—for example, wooden boarding accompanied by a steel door or even bricked-up doorways. This suggested that wooden boarding may have been a closer substitute for steel for such properties. However, in our view suppliers were likely to know when they were making offers for contracts for housing identified for demolition or renovation, and so even if wooden boarding was a constraint here, it was unlikely to provide a significant constraint for other properties.

10.8 Accordingly, we conducted our assessment of unilateral effects within the context of a merger of companies supplying SSVP.

Geographic scope

10.9 We assessed the distances that suppliers are willing to travel in order to supply social housing customers. The merging parties told us that, generally, suppliers travelled relatively short distances.[97] This was partly because relatively small properties and [✂] in supplying social housing made it uneconomic to travel large distances, and partly because customers often required properties to be secured at short notice (as short as two hours in some cases), which made a local presence necessary. Some smaller suppliers told us that they would and did travel longer distances to supply social housing customers, but generally for small customers and at higher rates than those prevailing among VPS and SitexOrbis's customers.

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[94] For example, Nottingham City Homes considered that when choosing the type of protection, it had a duty to mitigate the risk of any losses.
[95] We discuss this point in more detail in paragraph 10.60. Respondents did not specify what a cheaper alternative would be, and so it was difficult to assess whether or not respondents had in mind a cheaper physical security alternative or some other cheaper alternative.
[96] In paragraphs 9.11–9.13 we explained why the existence of a minority of customers who would be willing to substitute to wood was not likely to protect other customers from price rises.
[97] VPS provided us with an analysis of its customers for each depot, showing that 80 per cent of its social housing customers were located within an average of [20–30] miles from the serving depot.

10.10 As discussed in more detail in Appendix D, we formed the view that a catchment area of up to 40 miles is appropriate to show how far it was typically economical to travel to serve social housing customers.

10.11 This implied that geographic markets were local, and that many social housing customers had the choice of only one or two suppliers in their local area, namely VPS and/or SitexOrbis. We have used the term 'local markets' to refer to geographical markets of this size.

10.12 However, the merging parties told us that it was straightforward to open a new depot to serve a social housing contract, and that suppliers without a local depot could and did bid for contracts with the intention of opening a new depot if successful. This implied that current geographic conditions (ie locations of existing depots) did not provide complete information about potential competition at the local level.

10.13 As discussed in paragraph 10.94 and Appendix E, we found that there were no substantial structural barriers to opening new depots for existing suppliers,[98] and there were a number of examples of VPS and SitexOrbis opening and closing local depots, mainly in response to gaining and losing social housing contracts. Furthermore, the merging parties already had depots and customers in most regions of the country, which would have facilitated the opening of a new depot in another part of an existing region (eg by serving some existing customers more efficiently from the new depot). Therefore it appeared that there were few if any local areas where it would not be attractive to the merging parties to compete for social housing contracts, across Great Britain, either serving them from their existing depots[99] or by opening new depots.[100] Accordingly we found that the merger could lead to some reduction in actual and/or potential competition in every local market in Great Britain and we have assessed it on this basis. We consider this issue further below.

10.14 It follows that there are three possible outcomes for our assessment of the competitive effects of the merger for social housing customers:

(a) We might find that no other competitors are able to replicate the competitive constraint on VPS that SitexOrbis currently exerts, which would imply a pervasive SLC across all local markets in Great Britain (pending entry or other countervailing factors).

(b) We might find that a competitor, or combination of competitors, provides sufficient competitive constraint, but they are not willing or able to open new depots. This would imply that there would be no SLC in local areas close to depots of these competitor(s) but there would be an SLC in other local areas.

(c) We might find that a competitor, or combination of competitors, provides sufficient competitive constraint, and that those competitors, like the parties, are willing and able to open new depots to serve local customers. This would imply that there is no SLC in any local area.

10.15 We consider below which of these scenarios was most likely.

10.16 CRA told us that, based on analysis by VPS, most of VPS's social housing customers had one or more specialist SSVP suppliers (other than the merging parties)

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[98] We consider whether economies of scale, density and scope may hinder the likelihood of timely and sufficient entry or expansion by other suppliers in paragraphs 10.122–10.132.
[99] See Appendix D, Figure 8, for the areas of overlap served by VPS and SitexOrbis's existing depots.
[100] We consider separately the ability of other suppliers to open new depots in paragraph 10.90ff.

located within [50–60] miles. It said that [✂] per cent of customers had one or more supplier; [✂] per cent of customers had two or more; and [✂] per cent of customers had three or more.

10.17 The large difference between two and three suppliers reflected the fact that for many customers (including all customers north of the Midlands, in Wales and in Scotland), SPS and Clearway were the only two alternative suppliers in CRA's analysis. We noted that CRA's analysis was based on Clearway having eight depots; Clearway told us that it had only two depots, and so this analysis overstated the proportion of customers that could be served by Clearway. On the other hand, CRA's analysis did not include certain smaller suppliers (such as Veritas and North Star Estates).

10.18 We therefore considered that the numbers CRA submitted provided some relevant information, but should in any case be interpreted with care since it was not only VPS's customers that would have been affected by the merger. For example, we were told that VPS had few customers in Scotland, where SitexOrbis was stronger and had more depots. This suggested that the numbers submitted may have overstated the proportion of customers that could be served by multiple competitors to the merging parties.

10.19 We also did not consider that it was sufficient to look purely at the number of competitors; it was also important to consider their identities and how close a competitor each was. We assess this closeness of competition below.[101]

Share of supply

10.20 Table 3 shows the revenues earned from supplying SSVP to social housing customers, to give an indication of the relative size of the main SSVP suppliers.

TABLE 3 **Revenue and share of supply for SSVP suppliers (social housing sector)**

Supplier	*Total UK revenue £'000*	*Total revenue from vacant property services to social housing customers £'000*	*Revenue from SSVP to social housing customers £'000*	*Share of social housing SSVP market %*
VPS	[✂]	[✂]	[✂]	[20–30]
SitexOrbis	[✂]	[✂]	[✂]	[50–60]
SPS*	[✂]	[✂]	[✂]*	*[0–10]**
Clearway	[✂]	[✂]	[✂]	[0–5]
Veritas	[✂]	[✂]	[✂]	[0–5]
SecureSite	[✂]	[✂]	[✂]	[0–5]
North Star Estates	[✂]	[✂]	[✂]	[0–5]
Maltaward	[✂]	[✂]	[✂]	[0–5]
PSS	[✂]	[✂]	[✂]	[0–5]
Pro-tex	[✂]	[✂]	[✂]	[0–5]
GMS	[✂]	[✂]	[✂]	[0–5]
Total		[✂]	[✂]	100

Source: The parties.

*[✂] Hence this will overstate its SSVP revenue and share.
Note: Loxal and Secure Empty Property were recent entrants and have been excluded from this table. We also excluded Shieldcom, a supplier whose main focus was on other activities and which earned a very small amount of revenue from SSVP.

10.21 The first column of figures shows the suppliers' total revenues in the UK from their entire operations; the second column shows the revenues they earned from all services provided to vacant social housing properties; the third column shows the

[101] Paragraph 10.24ff.

revenues they earned from providing SSVP to social housing customers. Finally, the fourth column shows each supplier's share of the revenues in the third column. Our focus was on the third and fourth columns, but the first two columns provided a useful illustration of the broader scale of these suppliers.

10.22 The table excludes companies (such as [✂]) that subcontracted these services to specialist SSVP suppliers since to include them would have resulted in some double-counting. It may exclude some small suppliers for which we did not have information, and it excludes self-supply, since it was difficult to estimate the level of self-supply.[102] Hence the table was likely to overstate the true shares of supply of SSVP for all the companies listed. We also did not rule out the possibility that small SSVP suppliers omitted from the table exerted some level of competitive constraint, as we discuss below, but we nevertheless considered that the table was a useful guide to the relative size of VPS and SitexOrbis and the other main suppliers of SSVP.

Views of competitors

10.23 Several competitors told us that they did not seek to compete with VPS and SitexOrbis since they could not compete with them on price. They aimed to find other niches of the market and service customers who, for one reason or another, did not wish to use VPS or SitexOrbis. They aimed to provide a better service but at a higher price. They told us that their biggest social housing customers were small. They said that generally they did not participate in tenders because both the PQQ stage and the subsequent tender stage were lengthy processes involving a lot of work; the tender stages were almost always weighted heavily towards price; and they did not believe that they could compete with VPS and SitexOrbis on price, or were not willing to do so, so they would not win the tender anyway.

Closeness of competition

10.24 The merging parties were the two biggest suppliers of SSVP to social housing customers, with an [80–90] per cent share of supply—see Table 3 above. Combined, they were approximately eight times as big as the next biggest supplier of SSVP, and the combined share of all other suppliers was [10–20] per cent.

10.25 VPS/TDR told us that there were a number of existing competitors who constrained VPS and SitexOrbis and who would continue to constrain the merged entity. These existing competitors included Clearway, SPS, SecureSite, Loxal and Pro-tex and, in addition, a 'large number of other local/regional suppliers of vacant property security products and services' (such as Shieldcom and PSS). VPS/TDR also said that we should consider the impact of DLOs which, apart from self-delivering security services, also 'extend their capability to provide security services for other social housing providers such as Local Authorities, Housing Associations and RSLs [ie Registered Social Landlords]'. We consider the competitive constraints imposed by both existing competitors and DLOs below.

10.26 We evaluated a number of sources of evidence, including the parties' internal documents, information based on tenders in which the parties had participated, views expressed in customer hearings, and our customer survey. We summarize each of these in turn below, and then consider other competitive constraints on the merged company.

[102] In any case, self-supply forms a slightly different form of constraint to that provided by competitors, and we assessed it separately.

Views expressed in internal documents

10.27 We saw relatively few internal documents that were specific to the social housing sector. We noted that a SitexOrbis October 2009 Customer Satisfaction Survey [✂] as the main other providers used by customers (albeit among a fairly small sample).

Tender information from the parties

10.28 The parties told us that income from contracts won via a tender process accounted for [✂] per cent of VPS's social housing revenue in 2011 (including [✂] per cent via framework agreements, the largest of which are [✂][103]) and [✂] per cent of SitexOrbis's revenue (excluding central commercial accounts, so this may overstate as a proportion of its total revenue).[104,105] Therefore we considered that tender information was likely to provide useful information on competitive behaviour and the preferences of customers who procure via tenders or framework agreements.

10.29 Tender data from VPS and from SitexOrbis suggested that the two parties were each other's closest competitor.[106] In each party's data, the merging parties won the large majority of relevant tenders for which we were provided with information, especially when one of them was the incumbent or when both of them bid.[107] For example, in VPS's data, out of [✂] tenders, VPS won [✂] and SitexOrbis [✂].[108] The only other winners were [✂] which SitexOrbis apparently did not bid) and a contract for mobile guarding and key holding for which VPS did not have sufficient capacity in the area and for which [✂].

10.30 From SitexOrbis's data we saw that SitexOrbis won [✂] per cent of the social housing tenders for which it submitted information, and VPS won [✂] of the remainder. In tenders where SitexOrbis was an incumbent, no bidders other than the merging parties won. And for the tenders won by VPS where SitexOrbis could identify a runner-up, that runner-up was in all cases SitexOrbis.

10.31 From VPS's data we also saw that, according to VPS's beliefs about its competitors in individual tenders, SitexOrbis bid against VPS more frequently than any other competitor; VPS thought that SitexOrbis had bid for [✂], compared with [✂] for SPS, [✂] for Clearway and no other current competitor[109] appearing more than once.

10.32 In relation to framework agreements, we noted that framework agreements were used by a number of customers and would be an option for others. It was, in our view, significant that the merging parties were the only parties approved under the nationwide void security framework agreements set up by LHC and Fusion 21. Fusion 21 told us that it advertised its framework on a regional basis and would prefer to have at least five approved suppliers for each region. The fact that no other competitor[110] seriously sought to be appointed even on a regional basis suggested that suppliers other than the merging parties would not impose a competitive constraint on the merged entity in the context of customers who preferred to purchase through a framework agreement (even though they had the option to purchase outside the agreement) and suggested that the main parties were each other's closest

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[103] Initial submission, paragraph 4.13.
[104] Initial submission, paragraph 10.13.
[105] In each case these figures related to SSVP revenues.
[106] We discuss this in more detail in Appendix F.
[107] The latter applied only to VPS's data; from SitexOrbis's data we did not know who bid.
[108] Some tenders were awarded to more than one supplier.
[109] [✂]
[110] Two building companies also participated in the tender for the framework agreement: [✂] and [✂]. The former ranked very low after the interview and the latter did not complete the process.

competitors. It also caused us to question the extent to which other competitors wished to compete seriously with the merging parties for the same customers.

10.33 VPS told us that the current situation with framework agreements would not lead to an SLC because:

(a) the frameworks did not represent a large proportion of the parties' revenues (in VPS's case frameworks account for only [✄] per cent of VPS's social housing revenues);

(b) frameworks were non-exclusive so customers could buy outside the framework and did so in the majority of cases;

(c) it was not necessary to have nationwide coverage to become a supplier under the framework and customers were not national;

(d) an adequate supplier base would have remained to join a national framework, including SPS, Clearway, SecureSite and MITIE;

(e) the procurement regime prevented start-ups from being artificially excluded; and

(f) prior to 2009, [✄] had been the only preferred bidder under the two previous LHC contracts.

10.34 As discussed below, we considered that framework agreements were likely to offer limited, if any, price protection to customers when the current framework agreements become due for renewal. We also found that the lack of other suppliers seeking or gaining approval on frameworks may have been indicative of those suppliers' lack of willingness to supply social housing customers at or around current price levels, even though operators of framework agreements were willing to accept suppliers on to the framework on a regional basis. We discuss framework agreements further below (see paragraphs 10.82 to 10.84).

Customer views

10.35 Based on our hearings with customers, most seemed to consider that the two parties were each other's closest competitor, due to their size, locations, experience and pricing. Some customers indicated that they perceived one or two other companies (Clearway and/or SPS) to be similar to the merging parties and equally capable of serving them.[111]

Customer survey

10.36 In relation to the customer survey, we noted that 71 per cent of social housing respondents did not know of any other suppliers for SSVP; and there was low (less than 10 per cent) awareness of other SSVP providers. Even when prompted, the companies that customers said they would consider using were predominantly general security companies which did not currently provide SSVP, rather than SSVP specialists. We noted that the survey sampled mainly existing VPS and SitexOrbis customers (although almost a third were prospective customers) and so the higher awareness of VPS and SitexOrbis may be expected to some extent, but the low

[111] We discuss this in more detail in Appendix F.

awareness of other suppliers did suggest that many customers did not actively test the market.

10.37 SitexOrbis told us that it was not surprised by the low awareness of other competitors because there was not really anyone else (other than VPS) who did what it did. VPS suggested that respondents could easily find other suppliers but had not felt the need to do so yet because they knew they were in control of the procurement process, and said that a broader group of suppliers were brought into the frame when respondents were given, as part of the customer survey, a list of possible suppliers.

10.38 The Guidelines[112] say that the closeness of substitution between suppliers' products can be indicated by the diversion ratio between them. The diversion ratio between X and Y indicates what proportion of firm X's customers would move their business to firm Y when firm X raises its prices. Absent a merger between X and Y, the profits earned on those customers would be lost to firm X. Post-merger, those customers would switch to Y and so be recaptured by the merged firm. Therefore the higher the diversion ratio between X and Y, the more likely it is that a price rise will be profitable post-merger.

10.39 In our customer survey, we asked which supplier customers would use if their current supplier no longer existed. The other merging party was by far the most common supplier named and no other supplier was named by more than 3 per cent of customers of either merging party.

10.40 We noted that a high proportion of customers (41 per cent of those currently using VPS and 52 per cent of those currently using SitexOrbis) said that they did not know who they would use and a further 12 and 14 per cent respectively said that they would have to research or tender it. In each case, as we note in Appendix F, we were cautious about deriving diversion ratios from the data: we calculated a lower bound of 19 per cent (from SitexOrbis to VPS) or 34 per cent (from VPS to SitexOrbis) but if we excluded the 'Don't know' answers those figures became 58 or 76 per cent respectively.[113] This suggests that diversion ratios between the merging parties were high.

Other competitive constraints

10.41 We considered whether intermediaries (ie large facilities management companies or large general security companies) were likely to act as a direct competitive constraint. In our view, intermediaries that subcontracted SSVP services (eg as [✂] did to [✂]) were likely to act only as indirect competitive constraints since intermediaries did not appear to compete against the parties on a stand-alone basis for 'pure' SSVP contracts, but rather competed against each other for more general contracts which had an SSVP component (ie where customers have decided to contract for a wide range of vacant property services with a single supplier). In these cases, SSVP suppliers competed to supply the contractor rather than competing to supply the end-customer directly, but the number of bidders was unchanged unless the contractor was willing to consider self-supply as an additional option.[114]

10.42 We considered whether DLOs were likely to impose a competitive constraint. VPS/TDR told us that a number of DLOs provided some form of security services for

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[112] The Guidelines, paragraph 5.2.15.
[113] See Appendix F, paragraphs 53–56, for the derivation of these figures. By excluding the 'Don't Know' responses, we effectively assume that those respondents who did not give an answer would behave in the same proportions as those who did answer. This is standard practice in analysing survey responses.
[114] We consider this possibility under the heading of entry and expansion: see paragraph 10.101 below.

vacant properties to some social landlords (although it was not clear whether they were exclusive suppliers or what type of security they provided). However, provision by DLOs was not mentioned in our survey and, when asked at our hearings, social housing customers did not appear to consider DLOs as a source of supply to other social housing providers (InCommunities was an exception). We viewed the economics of DLO provision as being very similar to those of self-supply, which we discuss from paragraph 10.45 onwards; and we consider whether DLOs are likely to commence provision of SSVP in paragraph 10.98. We also noted that one customer we spoke to, Northern Ireland Housing Executive (NIHE), told us that it primarily used [✂] but its own DLO supplied some of its district offices; however, after taking overheads into consideration, [✂].

10.43 We also considered whether local non-specialist suppliers (such as general building companies) imposed a competitive constraint on the larger specialist suppliers. However, we saw very little indication in our survey or hearings that customers viewed local suppliers as a viable option or that larger SSVP suppliers (other than VPS) viewed local suppliers as a competitive constraint. Accordingly we did not expect local suppliers to impose a significant constraint either pre- or post-merger (although we did not rule out the possibility that, for smaller jobs, local suppliers may be more suitable and so impose a larger constraint).

Conclusion on closeness of competition

10.44 All the evidence we discussed above (and described in more detail in Appendix F) indicated that the merging parties were, for most customers, each other's closest competitor. It suggested that there was a second tier, consisting of Clearway and SPS, which may act as a constraint on the merging parties for some customers; and a third tier of smaller suppliers which were unlikely to be considered close substitutes by many customers. DLOs may have been a potential competitive constraint in some local areas and 'intermediaries' may have changed the competitive process where SSVP requirements were included in a larger package of customer requirements (we noted that intermediaries may 'bargain hard' with SSVP suppliers with which they contracted). However, we found that neither DLOs nor 'intermediaries' were likely to be close substitutes for most customers.

Self-supply

10.45 Our customer survey indicated that very few (3 per cent) of social housing customers would consider self-supply of SSVP products (Q14c) in response to an across-the-board price increase by both merging parties. When asked what customers would do if VPS and SitexOrbis increased their prices, 5 per cent of VPS/SitexOrbis social housing customers said that they would consider self-supply (Q38).

10.46 We asked a number of customers in hearings about the possibility of self-supply for social housing organizations.

10.47 Leicester City Council (Leicester Council) said that it self-supplied physical security for its vacant property and had done so for approximately 15 years. It told us that many years ago, when it switched to self-supply, this was a viable option because the number of vacant properties was higher and vacancy periods were longer. It was not difficult to buy a truck or find storage space for the screens/doors. Since it had already acquired the necessary materials and trained employees, it continued to self-supply even though its demand was now much lower. Those employees were not dedicated to SSVP; they also performed other duties. It told us that switching to self-supply would be economic only for a council with quite a large volume of vacant properties. Leicester Council estimated that switching to self-supply might be feasible at about 20 to 30 property installations per week but closer consideration would be required for about ten properties per week, whereas on average it currently secured four or five.

10.48 Bolsover District Council said that it did not install steel screens internally due to the set-up costs (£30,000+), and the lack of storage space; it was more convenient to outsource due to the fluctuation of work needed.

10.49 InCommunities told us that it was reviewing its current voids process, as it believed outsourcing was something it should typically try to avoid; [✂]. This review was at an early stage and InCommunities was not able to tell us how likely it was that it would be able to self-supply.

10.50 Nottingham City Homes told us that it would potentially consider providing security services in-house if there was a price increase, though it might not be cost-effective; it had not previously considered providing these services in-house due to the cost of purchasing and installing steel screens; it was cheaper to outsource.

10.51 Based on the evidence of our customer survey and the views of social housing customers we spoke to, we found that self-supply was unlikely to be a credible option for many social housing customers. We recognized that this could change if prices rose significantly and other suitable suppliers were not available, but we did not consider that it would be sufficient to constrain prices to pre-merger levels. Self-supply may have been more feasible for customers managing large numbers of vacant properties, but increased efficiency of management of vacant properties over the last decade has made such customers less common and we noted that Leicester Council, which did currently self-supply, appeared to do so only because it had been efficient many years earlier to switch to self-supply, but would not have made such a switch at its current level of vacancies.

10.52 We were also not persuaded that the ability or willingness of a small number of customers to self-supply would protect other customers. VPS and SitexOrbis told us that once a potential customer had launched a tender process, it was rare for that contract not to be awarded. This suggested to us that self-supply rarely competed directly against traditional suppliers and, at the point when suppliers were asked to submit prices, it was unlikely to be a strong constraint.

Profitability of a hypothetical price increase

10.53 As noted in paragraph 9.6, the incentives for the merged company to increase prices would depend partly on the extent to which customers would substitute away (to other suppliers of SSVP, or to alternative vacant property security services, or indeed cease to use any form of security services), and partly on the margins they earned. One factor that would influence the former was the importance of price in the choice of supplier. Below we assess in turn the importance of price, substitution and margins.

Importance of price

10.54 Our survey suggested that price was one of the important factors in choosing a supplier of SSVP, but not the only important factor.[115]

10.55 SitexOrbis told us that tenders were more competitive than quote and order work because the orders were larger and there was more risk around the blend of work and duration of voids: [✄]. SitexOrbis told us that quote and order tended to be for specific properties with more certainty over details such as duration of vacancy and other relevant factors; [✄].

10.56 We were aware that in the majority of social housing tenders, price was given the largest weighting of all factors. VPS told us that in its experience, price was given a weighting of between 60 and 100 per cent. This was subject to prospective suppliers completing the PQQ process where they had to meet certain non-price criteria.

10.57 It appeared that price was the key characteristic at the bidding stage, but customers were likely to need a minimum level of size and experience to pass the PQQ stage (as, for example, Loxal indicated), and past customer experience during day-to-day operations—good or bad—may be influential. For example, SitexOrbis told us that 'if they want you to win the contract, within the bounds of what is legal they will bend over backwards to try and make sure you win it … It can work the other way, of course. If they want you out, they will do everything they can to make it difficult for you'.

Substitution to other products or suppliers

10.58 We received evidence on the likelihood of substituting away from the parties that pointed in different directions. On the one hand, our hearings gave us a fairly consistent view that customers would find it difficult to reduce the level of protection on their properties or to find alternative suitable suppliers who could offer prices at the current level.[116] We also noted that the main parties told us that the social housing market was characterized by a degree of customer inertia (see paragraph 10.99). All these factors suggested that customers had a low likelihood of changing their behaviour in response to price rises.

10.59 On the other hand, respondents in our survey gave the indication of being highly price sensitive. In response to a hypothetical across-the-board price rise (of an unspecified size) by both parties, 40 per cent told us that they would consider use of a cheaper alternative, 32 per cent would consider a different supplier and reduce business with their current supplier, and 22 per cent would consider moving their business to a different supplier (Q38).[117]

10.60 It is common when asking customers hypothetical questions about their likely response to changes in prices to find that customers overstate the way in which they would react; this is known as stated preference bias. In order to allow for this possibility, and to gauge responsiveness to price increases of different sizes, we asked each respondent a follow-up question as to how likely they would be actually to carry

[115] See Appendix F, paragraph 47.
[116] See paragraph 7.14, Appendix G (paragraphs 45–58) and Appendix F (paragraphs 68–73).
[117] Multiple responses were allowed and so these figures included a small amount of double counting, but 77 per cent of respondents gave at least one of these answers. All these figures were calculated excluding customers who answered 'Don't Know' or refused to answer from the denominator, ie we effectively assumed that those respondents ('Don't know' and refused to answer) would give answers in the same proportions as those who did reply. Excluding them made little difference to the results.

out the stated response at different levels of price increase. They could be 'very likely', 'quite likely', 'quite unlikely' or 'very unlikely', or they could say 'Don't know'. We would expect to get a more representative view of the likelihood of switching by considering what weight to give to each type of response. Below we present the proportion that said they were 'very likely', and the larger proportion who said either 'very likely' or 'quite likely' (which we group together under 'likely'). This approach led to the following results:

(a) For a 5 per cent price increase, we found that:[118]

(i) 6 per cent were *very likely* to reduce their business and 6 per cent to move it; and

(ii) 13 per cent were *likely* (either 'very' or 'quite') to reduce their business and 13 per cent to move it.

(b) For a 10 per cent price increase, we found that:

(i) 13 per cent were *very likely* to reduce their business and 11 per cent to move it; and

(ii) 22 per cent were *likely* to reduce their business and 20 per cent to move it.[119]

(c) We did not prompt respondents for their likelihood of switching to a cheaper alternative, but, we expected[120] this to be in the order of:

(i) for a 5 per cent price increase, 7 to 11 per cent would have been *very likely* to use a cheaper alternative and 15 to 22 per cent would have been *likely* to do so; and

(ii) for a 10 per cent increase, 15 to 20 per cent would have been *very likely* to use a cheaper alternative and 26 to 34 per cent would have been *likely* to do so.

10.61 Our survey also asked whether customers thought the merger would have any effect on them. 58 per cent of social housing customers said that they did not think the merger would have any effect on them (53 per cent of customers of VPS or SitexOrbis, ie excluding prospective customers); and only 15 per cent thought it would have a negative effect.[121]

10.62 We viewed these responses to our survey as indicating a willingness to switch (paragraph 10.59)/a lack of concern (paragraph 10.61) which needed to be assessed in context with other factors. It seemed to us that these responses needed to be considered alongside the very low awareness of other suppliers among survey respondents.[122] Around two-thirds of respondents who said that they would consider a

[118] Again, these figures excluded those who answered 'Don't know' when asked what they would do from the denominator. However, for customers who said what they would do but answered 'Don't Know' to the follow-up question about how likely they were to carry out the action they considered, we assumed that they were not 'likely' to carry it out in practice. Similarly anyone who did not say they would consider a particular response to the opening question was considered unlikely actually to carry out that response. The aim of the follow-up question was to get an idea of how many respondents were confident that their answer was something they would actually do, and we viewed 'Don't know' as being less than likely in this context.
[119] We also asked about 20 per cent and higher price increases and slightly more customers became likely to reduce or switch purchases.
[120] Based on the proportions of those who said they would consider reducing or moving their business that said they were likely to do so.
[121] Survey Q37.
[122] See paragraph 10.36 above.

different supplier did not know who they would move to; a further fifth said 'other';[123] and the only SSVP specialists mentioned were Clearway (by 7 per cent) and SecureSite (by 2 per cent).[124]

10.63 We considered that customers with experience only of (one or both of) the merging parties might have reasonably expected to be able to elicit similar quality and prices from other suppliers. In practice, if they had tried to find a new supplier, and they were able to identify the suppliers we have identified, our analysis suggested that the majority of customers would have been unlikely to find one willing and able to supply under similar terms as VPS or SitexOrbis currently offered.[125] This was because of the cost and other advantages (especially depot coverage) which VPS and SitexOrbis had (see paragraphs 10.122 to 10.121). If there were suppliers willing and able to supply on those terms, we would have expected those suppliers to be more successful in competing with the merging parties pre-merger. Our evidence suggested that they were not.

10.64 A second factor which we considered was the nature of the transactions between customers and suppliers and the likelihood of price discrimination.[126] The survey results reported above represent a possible reaction if the merging parties increased their prices across the board to all customers by the same proportion. We did not think this was likely.

10.65 We have explained that we expected there to be some customers who had better alternatives than others (see paragraph 7.17)—for example, because their security needs could be met by different types of security—and we knew that prices were generally set individually and could vary widely from customer to customer. We expected that the merged company would try to identify which customers would bear a price increase, and what size of price increase, and set prices accordingly post-merger. We expected the merged company to have good knowledge of the majority of social housing customers; partly from discussions as to their needs and partly because the merged company would be the incumbent supplier for the large majority of customers (see Appendix F, paragraph 9). Therefore, we expected it to be able to avoid substantial price rises to most of its price-sensitive customers and to focus price rises on less price-sensitive customers. As discussed in paragraph 7.17, we did not think that the existence of some customers who were willing to switch to alternative security products would constrain a price rise for other customers. Taking this into account, a possible interpretation of the results of the simple uniform price rise question in our customer survey was that there would be substantial switching; but this interpretation was likely to be misleading because it would overstate the amount of switching that would take place assuming a strategy of targeted price increases, which we considered to be more likely than equal price increases for all customers.

10.66 We noted that budgets for many social housing providers were tight (especially in the current macroeconomic climate) and that some social housing customers might have find it difficult to increase their expenditure if prices rose. We found it plausible that those customers would, reluctantly, reduce their usage of SSVP services in the event of a post-merger price rise. However, our view was that these customers would effectively be paying the same total amount for reduced services and the merged entity would have earned the same revenue with lower costs. Therefore this type of action would not defeat or constrain a price increase. Furthermore, we noted that

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[123] Almost all of those who replied 'other' said that they would go to tender or do research, suggesting that they also did not know which company they would use.
[124] Survey Q40.
[125] See Appendix F, paragraphs 68–73, for several examples of social housing customers who told us that other suppliers were substantially more expensive than the merging parties.
[126] See paragraph 9.13 above.

some customers told us that they would not be willing to reduce the level of protection because the costs of doing so were too high (for example, the risk of having an expensive boiler stolen from a property—because of its scrap metal value—or other property damage far outweighed the costs of protection).[127]

10.67 Taking all of the above into account, we considered that, whilst in principle customers may have been willing to switch away from the merging parties, many customers may in practice have been unlikely to do so. To the extent that some customers may have had other options that they could switch to (for example, if they were large customers and self-supply would have been feasible, or they had properties scheduled for demolition for which other products such as wooden boarding may have been a good substitute), we would have expected the merging parties to be able to identify them and avoid price increases for those customers while increasing prices for other customers without such options. This was particularly true since the merging parties between them currently supplied the large majority of social housing customers and could be expected to have good knowledge of their requirements. Moreover, at the very least, we expected that the merged company would be able to raise prices to many customers by a significant amount without becoming more expensive than other providers.[128]

Margins

10.68 We noted that there was some difficulty in deriving margins in this sector, and in particular in separating margins for commercial and social housing customers, since they were typically served with a shared infrastructure. We assessed the extent to which different types of costs were truly variable. We thought that the appropriate definition of margins may have been different for *(a)* a single job on a quote and order basis, where the only financial costs were the labour and transport costs of installation and removal; and *(b)* a large contract which might have justified opening a depot or storage facility, buying new stocks of doors and screens, and/or hiring additional employees. In *(b)*, once we have taken these costs into account we would be looking at something like a net margin rather than the gross margin in *(a)*. Therefore it would be consistent to say that gross margins on individual jobs were high but net margins (or profitability) were low.

10.69 SitexOrbis told us that for social housing it sought a [✂] per cent gross margin based on [✂]. It told us that although margins often [✂] of this aspiration in practice, it would [✂] a gross margin of [✂] on tenders of any significant size, and margins between [✂] and [✂] per cent would require justification by the General Manager to directors.

10.70 SitexOrbis also submitted its gross margins in different regions of the country, which showed that its average gross margin was [✂] per cent. We understand that these margins are [✂] since [✂]. We understood that this was a blended margin which includes services such as clean–and-clear, which tend to be lower-margin activities, indicating that the margin on SSVP is likely to be higher than [✂] per cent.

10.71 VPS told us that its gross margin (excluding depreciation) for rental services in social housing was [✂] per cent, and its overall gross margin (excluding depreciation) for social and commercial rental services was [✂] per cent. Including depreciation, its overall margin across all service lines and across both social and commercial was [✂] per cent.

[127] See paragraphs 5.4, 7.23 & 10.4.
[128] See Appendix F, paragraphs 68–73.

10.72 As explained above, [✂] are generally viewed as more likely to lead to price increases. Accordingly we regarded the levels of these gross margins as being supportive of a view that the parties would have an incentive to increase prices post-merger.[129]

Conclusions in the absence of countervailing factors

10.73 We concluded that, absent countervailing factors, the merger was likely to lead to an SLC in the provision of SSVP to social housing customers in Great Britain. We found that competition in the social housing sector appears to be almost entirely driven by VPS and SitexOrbis, who were each other's closest competitors.[130] Other suppliers appeared to be reluctant to supply at current prices, and there was low awareness of them among customers.[131] There were also many areas of the country which could be served by existing depots of VPS and SitexOrbis, whereas most or all other parties would have had to open a new depot (we consider the likelihood of new entry in local areas below and the economics of a new depot specifically in paragraphs 10.110 to 10.119). Some customers may have had broader options (for example, some customers exhibited more willingness to substitute towards other products or self-supply), but we expected the parties to be able to identify them and target price increases at other customers.[132] Therefore we expected the merged company to have the incentive and ability to raise prices to most social housing customers throughout Great Britain, absent countervailing factors.

Northern Ireland

10.74 As VPS was not present in Northern Ireland pre-merger, we found that the merger will not lead to a loss of actual competition in Northern Ireland. Accordingly, we considered whether the loss of VPS as a *potential* competitive constraint on SitexOrbis may have been expected to lead to an SLC in the provision of SSVP to social housing customers in Northern Ireland.

10.75 SitexOrbis told us that the majority of business it carried out in Northern Ireland was [✂] business that came from [✂], which SitexOrbis had supplied for a number of [✂]. This may on its face be taken as evidence that the merger could be expected to lessen competition in Northern Ireland.

10.76 We spoke to [✂] and it told us that [✂]. VPS told us that [✂].[133]

10.77 Furthermore, at the time of the merger VPS had no presence on the island of Ireland and would not have been able to bring to bear the economies of scale, scope and density it has in Great Britain to compete for new business. As a potential new entrant into Northern Ireland, VPS would have been in a similar position to other larger SSVP suppliers such as SPS or Clearway, and as such VPS would not have been a particularly close competitor to SitexOrbis in Northern Ireland. Therefore, we concluded that it was more likely than not that the merger would not result in an SLC for social housing customers in Northern Ireland.

[129] See footnote to paragraph 9.6 and Guidelines, paragraph 5.2.15.
[130] Paragraph 10.44 above.
[131] See paragraphs 10.23, 10.34 & 10.36 above.
[132] Paragraph 9.13 above.
[133] Although we note that VPS has, [✂].

Countervailing factors

10.78 The Guidelines suggest that an SLC may be prevented if there are countervailing factors such as buyer power, relevant efficiencies or entry or expansion. We consider each of these in turn below.

Buyer power

10.79 In some circumstances, an individual customer may be able to use its negotiating strength to limit the ability of a merged company to raise prices. We refer to this as countervailing buyer power. However, often only some—not all—customers of the merged company possess countervailing buyer power. In such cases, we assess the extent to which the countervailing buyer power of these customers may be relied upon to protect all customers.[134] We also assess whether buyer power that exists pre-merger will continue to exist post-merger. If customers have buyer power pre-merger because they can make a realistic threat to switch from one of the merging parties to the other, that source of buyer power would not apply post-merger. We considered that in order to apply buyer power, customers must have a realistic option to switch away from the merged company post-merger, either to another competitor or to self-supply or alternative security services.

10.80 In this case, it was plausible that some social housing customers—especially large customers—had a degree of buyer power pre-merger. However, this buyer power was likely to derive from their option to switch from VPS to SitexOrbis or vice versa, since all the indications were that these two companies were each other's closest competitors pre-merger. Post-merger this would not be an option, and customers' bargaining positions would be severely reduced unless they could credibly threaten to switch to self-supply or a third party supplier in the event of any price increase. Our analysis above suggested that this would not be a credible threat for most customers.

10.81 The parties said that significant intermediaries (including providers of framework agreements and contractors such as large facilities management companies, who may have been larger purchasers than the typical social housing customer) had both the ability and incentive to switch to alternative suppliers, self-supply or sponsor new entry and therefore neutralize any attempt by the merged company to raise prices post-merger or reduce non-price factors. The parties said that these intermediaries already had established relationships with social housing customers, and they understood that [✂] had considered [✂] instead of one of the parties under the [✂]; they also said that VPS provided subcontracted void security services to several major contractors in the social housing sector, for example [✂] and [✂].[135]

10.82 Organizations operating framework agreements may have been able to exercise some buyer power on behalf of their members due to their scale. However, they were still constrained by the choice of suppliers available to them. As far as we were aware, the merging parties were the only current suppliers of SSVP to framework agreements. If framework agreements, by their nature, could only appoint relatively large suppliers with good geographical coverage (either because the operator of the agreement wished to do so or because smaller suppliers were not interested in being appointed), then there may have been no other suitable alternative suppliers at the time of the merger, and the merger would have removed the primary competitive constraint; we did not expect the scale of the framework agreement would prevent price rises in this scenario. Customers using framework agreements would not be

[134] The Guidelines, paragraph 5.9.1.
[135] Initial submission, paragraphs 10.39–10.41 and Response to Issues Statement, paragraph 5.10.

able to carry out mini-tenders since there would be only one approved supplier, and the ability to buy outside the framework agreement did not offer any protection if there were no other equally suitable suppliers available at pre-merger prices.

10.83 In its response to our provisional findings, VPS argued that we had misunderstood the manner in which frameworks operated and placed undue emphasis on the fact that the merging parties were the only suppliers appointed to framework agreements.[136] We disagreed that we had placed undue emphasis on the role of framework agreements. Our competitive assessment in relation to the social housing market was based on a number of pieces of evidence, not just the role of framework agreements. In relation to VPS's arguments about framework agreements specifically:

(a) Fusion 21 told us that, over the past 12 months, prices awarded using mini-competitions had been 'really similar' to the direct framework prices. However, we were concerned that if direct framework prices were to rise due to reduced competition following the merger, there would be no potential for framework users to get lower prices using mini-competitions.

(b) VPS said that [✄] was the only approved supplier under the two previous [✄] frameworks before [✄], and that prices [✄]. We expected that the prices that each of VPS and SitexOrbis bid in order to be approved were constrained pre-merger by the expectation that the other party would (or might) bid. The set of (perceived) likely bidders at the time of a tender is most relevant to the bid a prospective supplier makes, not the ex post observed successful bidders; and we did not consider that [✄] historic prices for [✄] would be very informative as to likely post-merger pricing.[137] Post-merger the merged company would not expect to face a strong competitor and so would not be as constrained in its pricing.

(c) We understood that current prices were fixed until May 2013 for the LHC framework and were reviewed annually for the Fusion 21 framework. We also understood that either VPS or SitexOrbis could terminate their agreement with Fusion 21 on no less than six months' notice, meaning that the merged entity could in effect withdraw one of the two price schedules (presumably, whichever is more favourable to customers). Therefore existing agreements would have offered some but incomplete protection to Fusion 21 customers, but only limited protection for LHC customers unless new entry or expansion took place in time for additional companies to be appointed to a retendered LHC framework. LHC told us that '[✄]'.

(d) VPS told us that it was cheaper for the provider of the framework agreement to deal with fewer suppliers and that was why framework suppliers preferred a national supplier, and so national coverage was not necessary. VPS said that post-merger 'it is almost certain that … the framework suppliers would simply add regional operators to the framework and/or sponsor growth or expansion by other SSVP suppliers'.[138] However, we were told that it was not possible to appoint new providers to existing agreements, and we saw no evidence that framework suppliers had the ability or incentive to encourage or sponsor new entry when a new agreement was put in place. For example, Fusion 21 told us that although it would have liked at least five approved suppliers, it only had two and had not actively sought any more. It told us that in 2010 it advertised on a region-by-

[136] VPS & TDR response to CC provisional findings, paragraph 4.6.
[137] In the absence of further information about [✄] beliefs about other bidders, which would be difficult to verify for tenders completed some years ago.
[138] VPS & TDR response to CC provisional findings, paragraph 4.6.

region basis and suppliers could be added to the framework for individual regions but it could not encourage service providers to bid in tenders. It said that having one service provider was not good for it or its clients and this might lead it to conduct an 'open-book' process as there would be no competition and it would have to look at other ways to confirm value for money. We also noted that if LHC had had only one approved supplier for several years, there was no certainty that it would try to add extra suppliers if the merger reduced it to a single supplier.

10.84 For these reasons we considered that any countervailing buyer power arising from framework agreements was likely to be limited and would offer limited if any price protection to customers after the expiry of the current framework agreements.

10.85 We concluded that buyer power was unlikely to offset the SLCs we identified.

Efficiencies

10.86 Efficiencies arising from a merger may enhance rivalry. In order to prevent an SLC from arising, the efficiencies must be timely, likely and sufficient, and must be merger-specific. The Guidelines explain that cost savings are most likely to enhance rivalry where they reduce marginal (or short-run variable) costs as these tend to stimulate competition and are more likely to be passed on to customers in the form of lower prices.[139]

10.87 The parties did not claim that significant marginal cost reductions will result from the transaction, but said that some relevant 'variable' cost savings would arise in the form of direct cost savings at the depot level (which we understood to include being able to schedule travel to customers of the merged entity more efficiently) and reduced costs associated with customer-driven activity (such as centralized order-taking, job scheduling, and invoice processing).[140]

10.88 We did not consider that the latter category of costs was likely to lead to lower marginal costs or lower prices, especially since [✂]. Moreover, we were not provided with any evidence that relevant marginal cost savings were likely to be significant. We noted in this context that VPS planned to [✂] to reduce fixed costs; this may lead to higher costs, such as [✂] to customers located near a [✂]. Absent any further information, we were not in a position to say whether marginal costs would, on average, increase or decrease.

10.89 Hence we concluded that there was no evidence of significant merger-related efficiencies to offset any lessening of competition.

Entry/expansion to supply social housing customers

10.90 In this section, we consider whether new entry or expansion in social housing would have been on a scale sufficient to prevent any lessening of competition resulting from the merger.

10.91 The Guidelines set out that in assessing whether entry or expansion may mitigate or prevent an SLC, the CC will consider whether such entry or expansion would be timely, likely and sufficient to offset the SLC. This assessment incorporates an evaluation of potential barriers to entry and expansion (for example, legal and technical advantages for current market players, intrinsic/structural advantages, econ-

[139] The Guidelines, paragraphs 5.7.1–5.7.9.
[140] Response to issues statement, paragraphs 5.12 & 5.13.

omies of scale and strategic advantages).[141] When considering entry and expansion, the CC considers less than two years as timely.[142]

10.92 Our analysis is set out below:

(a) We considered whether there were barriers to entry and expansion in the availability or cost of SSVP products, labour and transport, access to depots or regulatory requirements (paragraphs 10.94 and 10.96).

(b) We considered the history of expansion (paragraphs 10.97 and 10.98).

(c) We considered whether customer inertia might have been an issue (paragraph 10.99).

(d) We considered what appetite there was among competitors and new entrants for expansion/entry in the social housing market (paragraphs 10.100 to 10.103).

(e) We considered whether entry and expansion may have been constrained by the economics of depot expansion (paragraphs 10.108 to 10.119).

(f) Finally, we considered whether a company with a large depot infrastructure (such as the merging parties) would have advantages of economies of scale, density and scope and whether this constitutes a barrier to entry (paragraphs 10.122 to 10.132).

10.93 We considered whether potential entry might be sufficient to constrain the merged company or whether actual entry would be required. We thought that potential entry would be much less effective than actual entry in constraining prices. In the case of tendered contracts, we thought that customers were unlikely to award contracts of any significant size to companies that were not already operating in the market, given the risks involved. For quote and order customers, we thought that the most likely outcome of a potential entrant approaching a customer of the merged company with a cheaper price would be that the customer would use that price to negotiate with the merged company. Therefore there would be little incentive for the merged company to keep its prices low in case of entry, because it could lower them in response to entry instead and thus benefit from higher prices until entry occurred, but still have a good chance of retaining the customer post-entry.

Barriers to entry/expansion

10.94 The parties told us that barriers to entry were extremely low and that a low skills base and little technology were required. They told us that an entrant could obtain, without significant difficulty, everything that was required to run an SSVP business. They told us that entry and expansion were expected to be timely and sufficient to constrain the merged company and that local players were sufficient to do this since customers were more interested in having a local supplier.[143]

10.95 We consider barriers to entry and expansion in detail in Appendix E. We found that acquiring SSVP stock (ie steel screens/doors and wireless alarms), a suitable workforce and transport in order to supply SSVP to social housing customers were straightforward and that access to these inputs did not constitute a barrier to entry.

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[141] The Guidelines, paragraphs 5.8.3 & 5.8.5.
[142] The Guidelines, paragraph 5.8.11.
[143] Initial submission, pp33–36.

10.96 We also found that regulatory or reputational barriers to entry were not significant, certainly no more so than in any other business-to-business market (although a requirement by some local authorities for three years of accounts for tenders would preclude some new entrants in some areas). We also recognized that in an industry where service quality was important, reputation may nevertheless provide some incumbency advantage (see Appendix E and paragraph 10.57).

History of entry/expansion

10.97 The parties submitted a number of examples of potential new entrants as well as companies capable of expanding into the supply of SSVP. They also submitted examples of recent entry and expansion in the sector,[144] and said that entry from DLOs might occur post-merger.

10.98 We consider the evidence on the history of entry/expansion in detail in Appendix E. We discuss a number of potential new entrants in paragraph 10.101. In relation to DLOs: we noted that whilst new entry from DLOs may occur at the local level (eg Incommunities told us that if it decided to in-source SSVP it would consider selling services to other social housing providers), we saw no evidence to suggest that new entry from DLOs on any significant scale was likely.

Customer inertia

10.99 We considered whether customer inertia or conservatism was an issue for entry and expansion in the social housing sector. Our customer survey suggested that around three-quarters of social housing customers of VPS or SitexOrbis had used their current supplier for longer than three years.[145] The [✂] Report said that SitexOrbis's customer account churn rate was low, around 6 per cent per year. These points did not seem consistent with an industry with low barriers to entry and expansion. Lack of awareness of other suppliers even when prompted suggested that customers did not actively test the market.[146] Both SitexOrbis and VPS said that strong customer inertia existed in the social housing market and that customer relationships were important, although they also said that customer price expectations still had to be met.[147] VPS told us that void services were a relatively small part of social housing customers' overall housing related spend, which we considered may also contribute to inertia and reduce price sensitivity. Overall, we considered that incumbency was likely to provide an advantage over a new entrant or competitor expanding into a new area and so make new entry more difficult.

The attractiveness of the social housing market for new entrants and expanding competitors

10.100 VPS/TDR submitted an entry/expansion model for the social housing sector showing that attractive returns could be made through expansion and new entry at current prices, especially for an existing competitor or contractor (eg a facilities management company).

[144] Initial submission, pp33, 35.
[145] DJS customer survey. The figures were similar for each of VPS customers and SitexOrbis customers.
[146] See paragraph 10.36 above.
[147] For example, SitexOrbis explained inertia in this way: ''You are sometimes working on a three-year contract with two years to extend ... it is really just a matter of falling into a routine with the housing officers ... and if you are providing a good service, delivering what they want, and we are making okay margins out of it, everything is stable.'

10.101 We found little evidence that competitors or businesses in adjacent sectors found the returns on offer in social housing attractive or wished to expand in the sector. We found that those competitors which the parties told us were most likely to expand in the social housing market expressed little interest in doing so:

(a) Clearway said that social housing contracts were not priced at an economic level and that they could not make money from them. It also told us that there were no social housing contracts that were big enough and profitable enough to justify opening a new depot. It said that whilst it occasionally tendered for social housing contracts, it had no expectation of winning any tenders. It also told us that for it to be worthwhile setting up a local depot for a social housing contract, prices would need to rise from current prices of £[✂]–£[✂] per week to £[✂]–£[✂] per week based on an average 26- to 27-week rental (for an average property with one door and six openings). This suggested that Clearway would have required a price rise of almost [✂] per cent in order to compete more aggressively in the social housing market. This evidence is consistent with Clearway's growth profile over the last three financial years (FY09 to FY11) in SSVP. In this period it has grown revenues over [✂] per cent in the commercial sector whilst revenues in its social housing business have not grown.

(b) SPS told us that it did not have large customers in the social housing sector. It said that the social housing sector was a changing market. It said that some large formal tenders had very time-consuming PQQ and tender processes, and price was always given a large weighting in the tender.

(c) Loxal said that the opportunity to expand was limited by the very low margins available on some social housing contracts. It told us that it intended to enter the social housing market in two or three years' time.

(d) Secure Empty Properties, a recent start-up, said that it was interested in supplying some social housing customers, mainly in north-west England, but had no plans to target [✂] in the immediate future, [✂]. It said that some [✂] customers were willing to pay more for a good service.

(e) MITIE, an intermediary, said that it did not have any plans to supply its own steel screens/doors for the next 12 to 18 months and that social housing margins were very low.

(f) G4S, an intermediary, said that it was reviewing the commercial market and not the social housing market as the social housing market tended to opt for the cheapest provider.

(g) Securitas, an intermediary, told us that it had made a decision around two years ago not to service social housing customers but the decision was not 'set in stone'.

(h) Morrison and VSG, both intermediaries, were not considering self-supply at all.

10.102 We considered whether it might be in the interests of companies to play down any plans for expansion in social housing during the period of our investigation. However, these same companies in many cases expressed more interest in expanding into the commercial market (we consider their appetite to expand into the commercial market below). It seemed to us that this difference in appetite for entry and expansion was due to the lower profitability and poorer growth prospects of the social housing sector (see paragraph 10.101). Both parties confirmed that there was little or no growth in social housing; and that margins [✂].[148]

10.103 In this context, we noted that VPS and SitexOrbis had chosen a different business model from their competitors: they had a large number of depots and thus incurred relatively high rent but low transport costs (taking into account both their social housing and commercial sector activities), while their competitors had few depots and so would have paid less rent but incurred higher transport costs to travel longer distances. It seemed to us that social housing customers who required local depots fit the VPS/SitexOrbis business model better than that of their competitors; and that to reach comparable scale in the social housing sector, competitors would have had to create new depots, which may not have been prohibitively costly but would have required a change in their business model. This was likely to explain why there was little appetite among actual or potential competitors to compete strongly for many social housing contracts.

10.104 The CC has in the past allowed the merger of two companies that were each other's closest competitors in a market where it was rare for suppliers other than the merging parties to tender for business (Kerry/Headland[149]). We noted that the findings in CC inquiries were fact-specific and did not set a 'precedent' for future inquiries. Nevertheless, we have considered below the possible relevance of the issues arising in the Kerry/Headland case to the present inquiry.

10.105 VPS/TDR submitted that the Kerry/Headland merger had close parallels to this merger in that this merger also involved current closest competitors (in the social housing sector) and switching had been mostly between the merger parties. They pointed out that in the Kerry/Headland case, there was a recognition by the CC that incentives would change post-merger, that there were no barriers to switching and that available capacity to supply was more important than market shares.

10.106 VPS/TDR also noted that the main difference between this merger and Kerry/Headland was that in the Kerry/Headland merger, the CC was able directly to observe evidence of switching and market reaction in its investigation. While this is not the case here, they asserted that the CC could have a high degree of assurance that the market would react quickly and that prices could not be sustained above costs due to very low barriers to entry and expansion and lack of barriers to switching.

10.107 We agreed with VPS that there were some similarities between the two mergers. However, the main feature which distinguished the two mergers related to the ability and incentive of other companies to enter the relevant markets in order to defeat any post-merger price increases. In this merger, we found that entry and expansion were not likely to occur on a scale sufficient to constrain the merged company effectively. Our analysis and conclusions in relation to barriers to entry and expansion and the timeliness, likelihood and sufficiency of entry and expansion in the commercial and social markets are set out in detail below (see paragraphs 10.133 to 10.139 and 11.141 to 11.153). Overall, we did not expect that entry and/or expansion, including the type of entry that was observed in Kerry/Headland, would materialize in either the social housing or commercial markets under consideration in this merger.

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[148] SitexOrbis told us that the margin that it made from the social housing sector was [✂] where it would be viable.
[149] *Kerry Foods Limited/Headland Foods Limited merger inquiry: a report on the completed acquisition by Kerry Foods Limited of the frozen ready meals business of Headland Foods Limited*, 2 December 2011.

The economics of depot expansion

10.108 The service requirements of social housing and commercial customers differed in several important respects. Social housing customers tended to require SSVP across, potentially, a large number of housing units in a particular local or regional area (though not nationally) and generally required these services to be delivered rapidly, say within a few hours of notification to the supplier.

10.109 As a consequence, it was important for a supplier of SSVP to social housing customers with more than a few vacant properties to have access to a local facility (see paragraph 10.9), be it a depot or other local storage facility (eg a lock-up) and locally-based fitters in order to:

(a) be able to respond very quickly to the customer's requirements; and

(b) do so profitably, ie without incurring significant travel and labour costs in getting from the depot to the vacant property.

10.110 We considered whether it would be necessary for a company to acquire depot facilities prior to bidding for this type of business. Most social housing customers told us that they would just need an assurance that a local depot would be set up if a contract was won.[150] We therefore considered that although a social housing customer would be likely to require that a supplier had a depot close to its properties, it would be sufficient for the supplier to acquire one once it had won the business.

10.111 [✂] VPS also told us that it was possible to service social housing customers remotely until transport costs reached a level which justified making an investment in local infrastructure (which it said was £[✂] per year).[151]

10.112 VPS/TDR said that a business servicing [✂] vacant properties could rent a depot for £10,000 a year and be staffed at a cost of around £55,000 a year.[152] We were told by VPS that this level of overhead was relevant to establishing a small depot and would equate to one van, two people and half a supervisor. Functions such as sales, accounting and administration were not included in this estimate. This level of overhead was therefore most relevant to an expanding competitor with existing depot infrastructure which it could leverage into a new locality rather than a completely new entrant to the sector.

10.113 Our view was that an expanding competitor using this model was unlikely to be an effective competitor without some sales support (eg a sales person), either centrally or at a local level, and this cost should also be taken into account when considering depot expansion. For example, VPS gave the example of needing Scottish people in Scotland to drive its business in Scotland.

10.114 Clearway told us that to set up a new depot would cost £20,000 in rent, rates and fitting plus a further £10,000 in monthly running costs. This implied annual running costs of around £140,000. It told us that it took about a month to set up a depot.

10.115 It also told us that to justify a new depot it would need revenues of £30,000 a month (or £360,000 a year). It said that this would require securing around 400+ properties.

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[150] For example, Ealing Council.
[151] VPS told us that the extra cost of driving 50 miles every day of the week was £15,000 a year.
[152] Initial submission, paragraph 8.9.

10.116 We note that SitexOrbis management accounts for August 2011 show that its [✂]. This was consistent with Clearway's new depot analysis, which suggested that monthly sales of £30,000 were required to open a profitable new depot.

10.117 We consider in Table 4 an illustrative example of the amount of business and number of customers which a new entrant (or existing competitor expanding its depot network) would require in order to consider opening a new depot. We noted that complementary revenue lines such as clean-and-clear services could make a contribution to the overhead.

TABLE 4 **Social housing depot expansion**

	Lower estimate	*Higher estimate*
Annual depot overhead (£'000)	[✂]	[✂]
% overhead covered by clean-and-clear services*	[✂]	[✂]
Overhead to cover from SSVP	[✂]	[✂]
Assumed SSVP gross margin (pre-labour, %)	[✂]	[✂]
SSVP revenue required to cover overhead (£'000)	[✂]	[✂]
Average 2012 quartile 4 customer revenue (£'000)	[✂]	[✂]
Average 2012 quartile 3 customer revenue (£'000)	[✂]	[✂]
Average 2012 quartile 2 customer revenue (£'000)	[✂]	[✂]
Average 2012 quartile 1 customer revenue (£'000)	[✂]	[✂]
Number of quartile 4 customers to cover overhead	[✂]	[✂]
Number of quartile 3 customers to cover overhead	[✂]	[✂]
Number of quartile 2 customers to cover overhead	[✂]	[✂]
Number of quartile 1 customers to cover overhead	[✂]	[✂]

Source: VPS customer data, CC calculations, PWC Project NASA.

*[✂]

Note: For the lower cost estimate we used VPS/TDR's depot expansion estimate and for the higher estimate we use the Clearway estimate. We assumed a pre-labour gross margin of [✂] per cent, [✂]. It implied a gross margin after direct labour of around [✂] to [✂] per cent. We knew from VPS data that the average rental revenue from a social housing customer in FY2012 was £[✂]. However, we noted that this disguised a wide dispersion with the average revenue for the [✂] per cent largest (quartile 1) social housing customers being £[✂] in FY2012 and the [✂] per cent smallest (quartile 4) £[✂]. We also noted that quartile 1 social housing customers were over five times bigger than quartile 2 social housing customers.

10.118 This example was illustrative and likely to be conservative as Clearway suggested that revenues of £360,000 were required (compared with our estimate of £187,000) based on its estimate of a new depot overhead. Whilst the example involved a number of assumptions, it did suggest that in order to justify an expansion into a new area with just a basic facility (two people, one van and some sales support), it was likely to be necessary to win the very largest (quartile 1) type social housing customers. Furthermore, the example suggested that suppliers need to secure at least one such large social housing customer *plus other customers* in order to cover the costs of even a basic depot (we considered the lower estimate to be an investment in a very limited facility). The analysis suggested that a depot was unlikely to be economic without a number of customers as the supplier would not otherwise be able to cover the overhead associated with the depot.

10.119 Our view was that an entrant into a new locality would need to quickly establish enough credibility to compete with the incumbent provider(s) on larger-scale social housing tenders. Our view was that this would be made more difficult as we were told by both parties that incumbent providers seemed to benefit from an inertia effect in the social housing sector (see paragraph 10.99).[153,154]

[153] See paragraph 10.36 above.
[154] SitexOrbis gave the example of its loss-making [✂] lock-up which had experienced exactly this problem.

- *Tender data*

10.120 Given the seeming importance of winning larger tenders, we assessed tender data from the main parties (discussed more fully in paragraphs 10.24 to 10.44) to see what evidence there was of competitors successfully competing against the parties in tenders. The tender data indicated that other competitors were less likely to bid, and rarely won (especially when competing against both VPS and SitexOrbis, or when one of the main parties was an incumbent).

10.121 This suggested to us that other competitors may not have been credible alternative suppliers in social housing tenders. It suggested that post-merger these competitors would find it difficult to compete effectively against the merged entity for social housing tenders, making them less likely to be able to expand their infrastructure in a timely manner. If competitors did not expand their infrastructure, then they would be much less likely to be able to constrain the merged parties.

Economies of scale, density and scope

10.122 We assess below whether, even if the cost of opening new depots did not constitute in itself a barrier to entry or expansion, a company with a large network of depots (such as VPS and SitexOrbis) would enjoy economies of scale, density and scope which would hinder the likelihood of timely and sufficient entry or expansion. We considered potential advantages in economies of scale, density and scope at two levels for social housing customers:

(a) local; and

(b) national which may impact at a local level.[155]

- *Local*

10.123 We considered whether economies of scale, density and scope could provide an advantage at the local level.

10.124 We concluded that in local areas where VPS and/or SitexOrbis were already present, their existing customer base was likely to provide them with economies of scale, density and scope. A higher density of customers in a given area would reduce average costs of serving existing customers as well as the incremental cost of serving an additional customer in the area, and may also reduce the cost of serving commercial customers in the area. Vehicles and labour could be used more efficiently if distances between customers were shorter and fuel could be saved. As a consequence, the incremental cost of serving an additional customer in the area was likely to be relatively low for incumbent suppliers, and competitors not present in the area may have found it difficult to win sufficient business to match the economies of scale, density and scope enjoyed by incumbent suppliers, and thus difficult to expand profitably.

10.125 We found that our assessment was consistent with a number of pieces of evidence:

(a) SitexOrbis told us that any new business it brought in was [✄] because the depot was [✄].

[155] We considered national economies of scale in relation to serving national customers in our assessment of possible entry/expansion to serve commercial customers.

(b) TDR told us that ‘once you have the infrastructure, which SitexOrbis does … you are more than adequately positioned to compete effectively at anything above zero profitability if that is what you want to call it, because new contracts are always going to be ones which are profitable for you, otherwise you would not bid for them’.

(c) Clearway told us that having a network of depots was important to competition and this was where SitexOrbis and VPS had an advantage over Clearway. (For example, social housing customers required urgent response times and having a nearby depot was important for these contracts.) Clearway had bid for social housing business outside the 20- to 30-mile radius of its depots but it had been very difficult to win contracts.

(d) Loxal told us that incumbent suppliers had an advantage due to a lower cost base from their existing presence.

10.126 CRA, on behalf of VPS/TDR, suggested that local scale effects did not act as a barrier to entry as otherwise local markets would be dominated by a local incumbent enjoying both high local market share and high profits. Our view was that local scale effects did exist and that it was the rivalry between the merging parties pre-merger which was likely substantially to prevent higher profits. In particular, the tender data summarized in paragraph 10.121 suggested that there was currently a high degree of rivalry between the main parties for social housing contracts but little effective rivalry with other suppliers.

- *National which impact at a local level*

10.127 We considered whether national economies of scale, density and scope could provide an advantage at the local level. In particular, we considered whether this advantage may have applied to expansion in local areas.

10.128 We concluded that, in local areas where VPS and/or SitexOrbis were not present, they may still have been able to benefit from depots in neighbouring areas. For example, by reassigning commercial and/or social housing customers from existing depots to new depots and adjusting the capacity of their depots, the main parties could take advantage of their larger network of depots and reduce the average costs of serving their customers.

10.129 We found that our assessment was consistent with evidence from the main parties:

(a) SitexOrbis told us how it had moved customers from existing depots to new depots [✂]. It said:

> We tried to identify those customers that were in the Bristol area, and we migrated them from the Cardiff branch to the brand new Bristol branch, established a brand new salesman in Bristol, a contract manager, moved a couple of the teams from Cardiff so they were based in Bristol, and then set up and built from there. So we would not have just set up cold from Bristol.

(b) VPS said that it would be unusual to move customers around as it was normally apparent where a customer was located and that ‘if they [ie the customer] have a dense population of properties it would be apparent where they sit’. However, VPS gave us examples of how it had serviced customers from existing depots before opening a new depot and serving the same customer from the new depot (eg [✂]).

10.130 We considered whether the main parties may have benefited from having comparatively large stocks of steel screens/shutters and alarms compared with their competitors. For example, SitexOrbis told us that when it was entering the pub market, because the social housing sector had been [✂]. SitexOrbis also told us that 'all steel stocks in the UK are managed centrally. Re-distribution (ie re-balancing of stock levels) of screens, doors and alarms between branches is common'. Loxal told us that:

> Established competitors had an advantage over new entrants in terms of how they had accounted for the depreciation of their stock items, which had allowed them to make a more competitive offering to customers. Through Loxal's experience, the practical effect was that once a company had stock and needed to utilize it, it could be more competitive with its pricing.

However, we viewed the issue of depreciation as principally an accounting issue rather than as likely to give a large supplier a competitive advantage.

10.131 We formed the view that SitexOrbis and VPS were likely to have an advantage from holding existing stocks of steel screens/shutters and alarms in that this enabled them to cope with unexpected or large demand more easily than competitors with less stock (operational efficiency) and to maintain high stock utilization rates. However, we did not expect this advantage to flow through to pricing to a material extent.

- *Conclusion*

10.132 Taking the above into account, we concluded that the merging parties had important advantages in relation to economies of scale, scope and density over other SSVP suppliers. We found that whilst there were no insurmountable obstacles to opening individual new depots, *(a)* the merging parties' local customer base and large depot infrastructure constituted a barrier to expansion by other smaller SSVP suppliers and *(b)* potential entrants from adjacent sectors would have found it possible to overcome this barrier to entry if they could have leveraged off an existing depot network (eg as some large facilities management or security companies may have had) but still would have been at a disadvantage until they acquired a sufficient local customer base.

Our assessment of entry and expansion in the social housing sector

10.133 Based on the evidence above, and in line with the Guidelines, we have considered entry and expansion under the following framework:[156]

(a) whether entry or expansion is likely (whether firms have the ability and incentive to enter the market, or the intent to do so—see the Guidelines, paragraph 5.8.8);

(b) if it is likely, could it occur soon (usually within less than two years—see the Guidelines, paragraph 5.8.11); and

(c) if it did occur, would it be likely to occur on a sufficient scale to constrain the merged parties.

[156] Consistent with our guidance in the Guidelines, paragraphs 5.8.3–5.8.13.

10.134 VPS said 'it is in our view unprecedented to see a merger effectively blocked in the absence of significant barriers to entry or expansion',[157] but our assessment—consistent with the Guidelines—was not based simply on the presence or absence of barriers to entry. Even in the absence of high barriers to entry in the form of, for example, sunk costs or intellectual property, it was possible that incumbents may have benefited from economies of scale or scope and there was an apparent lack of appetite for entry among potential entrants. The appropriate framework for assessing entry in merger cases is that summarized in paragraph 10.133.

10.135 We found that the key to entry and expansion for a new entrant or existing business expanding into a new area was building sufficient local scale in a timely manner. If this were possible, then the advantages of scale, scope and density enjoyed by incumbent provider(s) could be overcome and a depot established. We viewed the ability to establish a depot (either before or after a customer is won) as necessary (but not sufficient) in order to be able to compete effectively.

10.136 In social housing, which tended to be serviced locally, establishing a local presence through a depot required a greenfield new entrant or expanding competitor to win larger contracts in order to justify expansion and so benefit from local scale advantages and be able to compete effectively with the merged company. This would have been possible, but would have taken time. It was made more difficult as incumbent providers benefited from inertia among social housing customers.[158] Moreover, there was little evidence that suppliers other than the merged parties were capable of competing effectively and winning social housing tenders to any significant extent.[159]

10.137 In addition, we found little evidence of any appetite for expansion in the social housing market among either existing competitors or businesses in adjacent sectors (eg the facilities management and security sectors) because of perceived low profitability and poor growth prospects in the social housing sector (both acknowledged by the main parties). We considered that, in the event of a post-merger price rise, any new entry or expansion would have happened in a cautious and incremental manner.[160] This meant that while entry or expansion was possible, we did not expect it to take place rapidly in a way that would enable a new entrant to challenge the merged company effectively within a reasonable timescale.

10.138 We found that there were also advantages in having a large national depot network, which impacted at the local level by allowing new depots to be opened in areas which would be uneconomic for new entrants without this advantage. This was because customers can be migrated between depots, something which a business with only a small network will not benefit from.

10.139 Taking all the above into account, we concluded that entry and expansion within the social housing sector was not likely to occur on a scale sufficient to constrain effectively the merged company so as to defeat a post-merger price rise.

Findings: social housing

10.140 We found that the supply of SSVP was highly concentrated, and the merged company would have a very large share of supply.[161] Absent entry, there would be few other suppliers post-merger, and we saw no evidence that these suppliers were a

[157] VPS & TDR response to CC provisional findings, paragraph 4.5.
[158] See paragraph 10.99 above.
[159] See paragraph 10.121 above.
[160] See paragraph 10.101 above.
[161] See Table 3.

strong competitive fringe; on the contrary, many of them told us that they tried to avoid competing against the merging parties.[162] We were told that other suppliers tended to compete on quality rather than price, and so the merger would remove one of only two companies with a reputation for aggressive pricing.

10.141 We also found that although the physical products (that is, steel screens/doors, polymer screens and wireless alarms) used by SSVP suppliers appear to be fairly homogeneous, other aspects of service differed.[163] In this respect, we found that the merging companies were each other's closest substitutes, and most competing companies appeared to be relatively distant substitutes for customers of the merging parties. Our analysis suggested that, although some customers may wish to react to price increases, there appeared to be no other supplier that they considered to be a close substitute,[164] and for most customers self-supply was not considered a viable option.[165]

10.142 Accordingly, we found that the merged company would have the incentive and ability to increase prices to many of its customers. In this regard, we noted that direct margins in each transaction were high.[166] Some customers may have been willing and able to switch to self-supply or alternative suppliers when faced with a small but significant price rise, but we considered that due to the individualized nature of pricing and services, this would be unlikely to protect other customers.[167]

10.143 We have considered whether a potential SLC might be overcome by entry, buyer power or cost-reducing efficiencies. We did not consider that sufficient entry or expansion was likely in an appropriate time frame to maintain prices at or near to current levels: our analysis suggested that, due to perceived low profitability and poor growth prospects, the social housing sector was not attractive to existing competitors or entrants at or near to pre-merger prices even allowing for a post-merger price rise which might attract entry.[168] We considered that, to the extent that there was buyer power pre-merger, much of it derived from competition between the merging parties (which were large companies that could serve most customers, or from the existence of intermediaries who could be supplied by those two large companies), and so this buyer power would have been diminished significantly post-merger;[169] and buyer power for some customers was unlikely to protect all customers. Finally, we saw no evidence that there were likely to be significant relevant efficiencies arising from the merger.[170]

10.144 We therefore found that the merger could be expected to result in an SLC for social housing customers across Great Britain.

Northern Ireland

10.145 For the reasons given in paragraph 10.77, we found that the merger may not be expected to result in an SLC for social housing customers in Northern Ireland.

162 See paragraph 10.23 above.
163 See paragraph 9.8 above.
164 See paragraphs 10.62 & 10.67 above.
165 See paragraph 10.51 above.
166 See paragraph 10.72 above.
167 See paragraph 9.13 above.
168 See paragraph 10.139 above.
169 See paragraph 10.80 above.
170 See paragraph 10.89.

11. Assessment of the competitive effects of the merger: commercial sector

11.1 The merging parties both supplied commercial customers, with [✄] per cent of VPS's SSVP revenues and [✄] per cent of SitexOrbis's coming from this sector. In this section, we consider the extent to which commercial customers considered other products to be a good substitute for SSVP; the distances suppliers were willing to travel to serve commercial customers; the closeness of competition between the merging parties; the ability and willingness of customers to self-supply; and evidence about likely customer responses to a hypothetical price increase.

11.2 We then consider separately for customers which operated at a national level and customers which operated at a regional level the likelihood that the merger would lead to an SLC. For each, we also consider the likelihood that entry or expansion would constrain a price increase, and the role of economies of scale. Finally, we consider whether there were other countervailing factors that may prevent a price increase: buyer power for some customers and relevant efficiencies for the merging parties.

Alternative products/services

11.3 We found that customers expressed a range of views. Most commercial customers that we spoke to viewed wooden boarding as a poor substitute for steel. For example, AXA told us that plywood was too easily removed, degraded in winter and was a fire risk in summer; it was also easily vandalized which attracted undesirable attention. However, we note that AXA rarely used either steel (except on doors) or wood since it made properties less attractive for sale or rental. [A major grocery retailer] also told us that wooden boarding was not suitable for similar reasons. On the other hand, some customers were willing to switch to wooden boarding: for example, Enterprise Inns told us that steel screens were fully interchangeable with other options such as timber boarding, and it might use VPS to fit a steel door and alarm with its partner contractor providing timber boarding to the windows.[171]

11.4 In our survey, the main reason commercial customers used wood was because of cost factors (51 per cent of customers using wood), which may indicate some sensitivity to cost considerations in the choice of vacant property security protection but also suggested that wood's advantage is not security (55 per cent of customers using steel screens and/or doors gave security as the main reason for doing so). We also found that some customers expressed a willingness to consider a cheaper alternative (not limited to cheaper physical security measures) if the merging parties were to increase their prices across the board.[172]

11.5 The greater size of some commercial properties and the higher costs of SSVP (compared with the social housing sector) suggested that commercial customers were more willing to view non-physical products as a substitute. For example, we were told that manned guarding was not practical for social housing but was suitable for some commercial properties. Therefore to some extent we expected providers of SSVP to compete with manned guarding and CCTV and in individual cases these services could be expected to act as some level of constraint on pricing (albeit that manned guarding was typically much more expensive and CCTV cheaper so the constraint was likely to come in the form of a trade-off rather than directly comparable prices for similar products, which may have diluted the constraint). However, the general view of commercial customers we spoke to was that measures such as manned guarding

[171] See Appendix G for more detail on these examples.
[172] See paragraph 11.69ff.

and CCTV were to some extent substitutes to each other, but would generally be used in conjunction with, rather than as a replacement for, SSVP.[173]

11.6 We found that live-in guardians may have been acceptable to some commercial customers, but not all. For example, [a major grocery retailer] told us that live-in guardians would not be suitable for it because its vacant properties were not habitable and because of its obligations under occupier's liability laws. We were told that live-in guardians were generally viewed as preventing squatting but did not provide any physical security measures and so would not be suitable for all properties.[174]

11.7 We also took into account the fact that for many commercial customers, their security requirements were determined by other parties (eg insurers)[175] and so their decisions were driven by the cheapest and most reliable way of achieving a specified form of security; they would not have the flexibility to seek a different or better-value alternative.

11.8 Accordingly, we conducted our assessment of unilateral effects within the context of a merger of companies supplying SSVP; but we were aware that some customers would exhibit a willingness to substitute to different forms of security and hence alternative products were likely to impose a degree of competitive constraint on suppliers of SSVP in some cases. However, we expected that for the majority of customers there would be no close substitute and, in an industry with individually negotiated prices, we did not expect that the existence of 'marginal' customers with good alternative options would protect those who relied on SSVP (see also paragraphs 9.11 to 9.15).

Geographic scope

11.9 We considered the distances that suppliers were willing to travel in order to supply commercial customers. The merging parties told us that generally suppliers travelled relatively long distances, and that between 2005 and 2008 VPS served all its commercial customers from just two depots [✂]. VPS said that this was partly because relatively large properties and long vacant periods made it economic to travel larger distances compared with social housing; and partly because customers generally gave longer notice for properties to be secured which reduced the need to be located close to customers' vacant properties. All the suppliers we spoke to told us that they would travel relatively long distances to serve commercial customers. Distances of up to 100 miles were mentioned (and in some cases, even further), although suppliers typically had the majority of their customers located much closer to their depots.[176]

11.10 Clearway told us that, for example, Scotland was a long way from the Clearway depots and this distance became problematic when securing a property, especially if there were security issues at the property and multiple trips needed to be made. We were told that 80 per cent of Clearway's customers were within 30 miles of its Erith depot and within 10 miles of its Sheffield depot. We were also told that Clearway had just taken on a project which meant that this would rise to 60–70 miles for its Sheffield depot.

11.11 SecureSite told us that, as far as commercial clients were concerned, it would travel economic distances. It would not generally wish to travel more than 100 miles for a

[173] See, for example, Appendix G, paragraphs 58 & 59.
[174] Appendix G, paragraphs 55–57.
[175] See, for example, Appendix G, paragraph 34.
[176] See Appendix D for more details.

one-off job but would travel further for individual jobs where the work was part of a larger commercial contract (for example, a customer with most of its properties in the South-East but a small number of properties in Scotland). SecureSite would also travel to more remote locations (examples given were Fort William in Scotland and Redruth in Cornwall) where the size of the job was large enough to justify the travel costs.

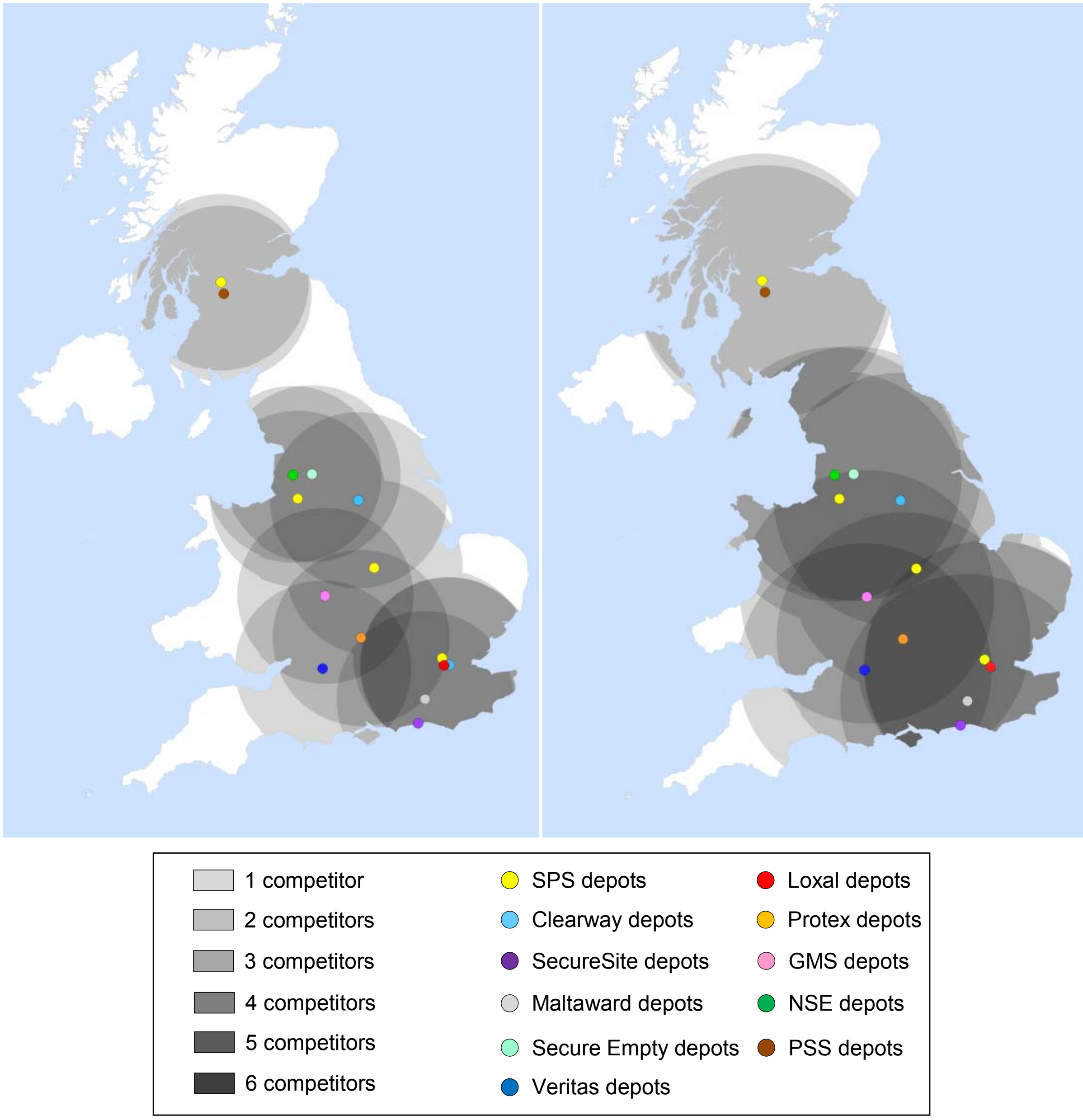
11.12 Our view was that suppliers were willing generally to travel relatively large distances of up to 70 miles to serve commercial customers on a regular basis. This was consistent with the distance suggested by CRA for commercial customers (see paragraph 7.30). We noted that suppliers were sometimes willing to travel further than this (for example, where the value of the work justified the travel cost and/or where road links were good) and so, as a sensitivity check, we also considered the implications of suppliers being prepared to travel up to 100 miles on a regular basis to secure vacant properties (we recognized that, for some jobs, suppliers may travel even further: our analysis was based on a reasonable range to serve commercial customers on a regular basis).[177] Therefore we considered that it was appropriate to assess the effects of the merger on the commercial sector using these distances of 70 and 100 miles (we referred to this as 'the regional level').

11.13 Figure 3 shows the areas of Great Britain covered by competing suppliers of SSVP based on 70-mile and 100-mile radii around their depots. It indicates the number of suppliers covering each point in the country, although it does not distinguish between the identity of those suppliers for presentational reasons. We noted that the identity of suppliers was likely to be more important than the number of suppliers due to the differences in size and other characteristics of SSVP suppliers and so, as we discuss below, we did not consider it was sufficient to rely only on a count of the number of potential suppliers without taking into account their identity. Figure 3 should be read in conjunction with Figure 4, which gives a clearer indication of each of the competitors with more than one depot (SPS and Clearway).

[177] We noted that using straight-line distances to determine an appropriate catchment area may not always reflect the time it may take to supply individual customers; for example, due to variations in drive-time in different parts of the country.

FIGURE 3

Geographic range covered by competing suppliers (70m radius, left, and 100m radius, right)



Source: CC analysis.

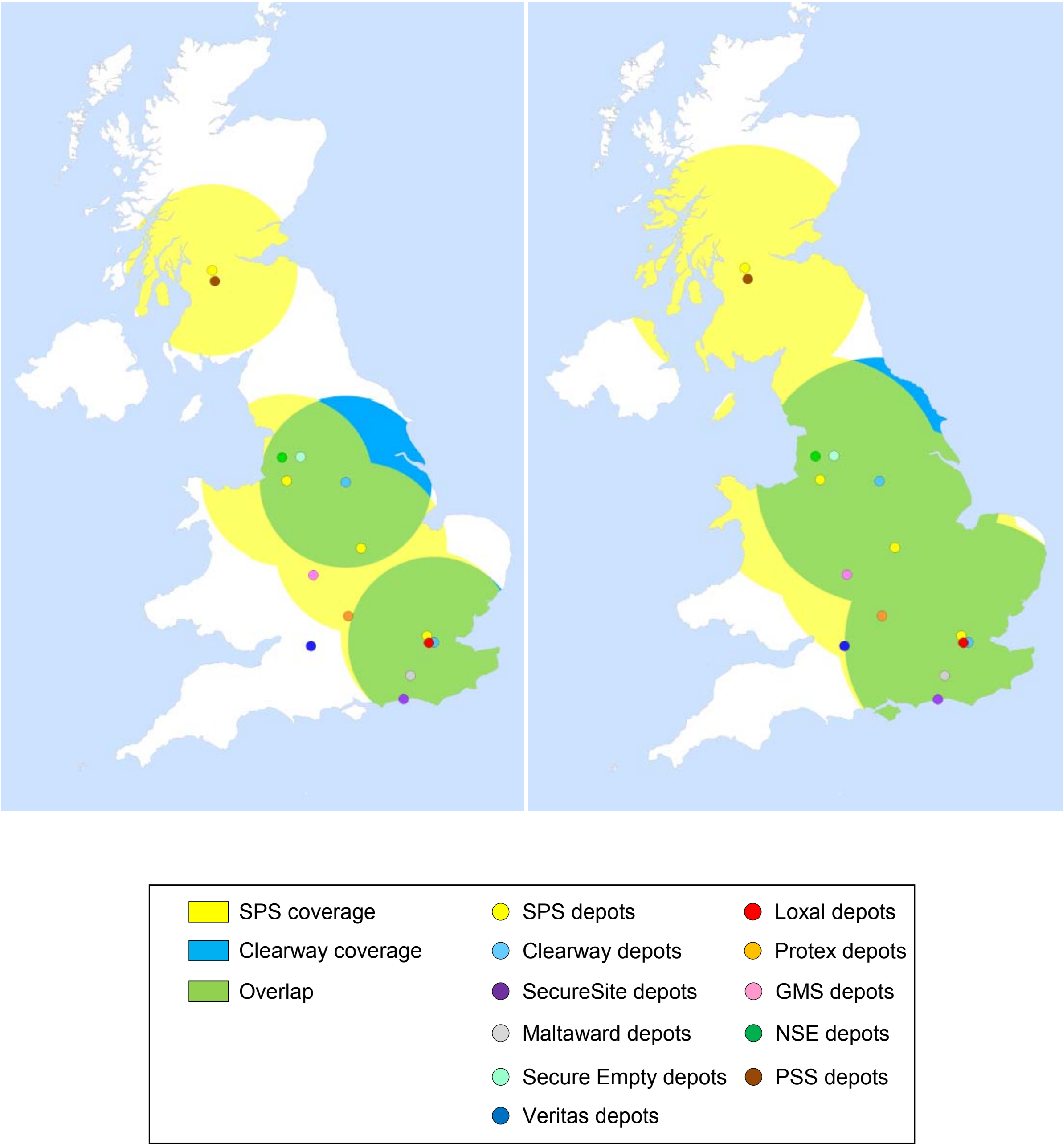
11.14 We also found that some customers had national requirements and would find it difficult or costly to fulfil those requirements using different suppliers in different regions. Therefore we also separately assessed the effect of the merger on those customers at a national (Great Britain) level and we assessed the level of geographic coverage required to be viewed as a suitable supplier by such customers, and the nature of competition between suppliers operating at this level. Our view was that suppliers would not generally be willing to cover all of Great Britain from a single depot at uniform prices (ie although they may be willing to travel long distances, they would have to price accordingly, and so for a customer in Scotland, a supplier in the South of England was unlikely to be competitive on price with a supplier with a depot in

Scotland). However, a relatively small number of well-located depots may have been sufficient to cover all or most of Great Britain.

11.15 Figure 4 shows the geographic area that each of SPS, Clearway and SecureSite might reasonably cover from their depot networks. Other suppliers' depots are marked on the map but (for simplicity of presentation) we do not show the areas that they cover.

FIGURE 4

Geographic range covered by multi-depot competitors (70m radius, left, and 100m radius, right)



Source: CC analysis.

11.16 CRA told us that, based on analysis by VPS, most of VPS's commercial customers had one or more specialist SSVP suppliers (other than the merging parties) located within [70–80] miles. It said that [✂] per cent of customers had one or more supplier; [✂] per cent of customers had two or more; and [✂] per cent of customers had three or more.

11.17 We made the same observations in relation to this analysis as we did in relation to the equivalent analysis for social housing (in particular, that CRA's analysis was based on a different set of information to the CC and may overstate the proportion of customers who would have a choice post-merger: see paragraphs 10.17 to 10.19).

Serving national customers

11.18 In order to compare the distances that each supplier might have to travel to service national customers from their current depots, we looked at SitexOrbis's base of commercial customers in Great Britain and considered how far each supplier would have to travel to service each property (assuming in every case that each property is serviced from the nearest depot of the supplier in question).

11.19 The results are shown in Table 5. The first column shows the average radius of the circular area around depots within which 50 per cent of the served properties are located. Similarly, the second column shows the average radius of the area around depots covering 80 per cent of the properties served. These measures provide an indication of the degree of concentration of customers around depots. The third column shows the average distance between a property and the closest depot, which gives an indication of the average distance travelled. Finally, the fourth column shows the maximum distance we typically observed between a property and the closest depot (that is, we have taken the average[178] across depots of the maximum distance travelled from each depot to serve its most distant property).

TABLE 5 **Straight-line distances to serve existing SitexOrbis commercial customers from existing depot networks**

miles

	50% customer radius	*80% customer radius*	*Mean distance*	*Maximum distance*
SitexOrbis	[✂]	[✂]	[✂]	[✂]
VPS	[✂]	[✂]	[✂]	[✂]
SPS	[✂]	[✂]	[✂]	[✂]
Clearway	[✂]	[✂]	[✂]	[✂]
SecureSite	[✂]	[✂]	[✂]	[✂]
North Star Estates	[✂]	[✂]	[✂]	[✂]
Pro-tex	[✂]	[✂]	[✂]	[✂]
GMS	[✂]	[✂]	[✂]	[✂]
Loxal	[✂]	[✂]	[✂]	[✂]
PSS	[✂]	[✂]	[✂]	[✂]
Secure Empty Property	[✂]	[✂]	[✂]	[✂]
Veritas	[✂]	[✂]	[✂]	[✂]

Source: Customer locations supplied by SitexOrbis, depot locations supplied by each party, CC calculations.

11.20 From this table we observed that:

(a) For SitexOrbis, 80 per cent of commercial customers were within [10–20] miles of the nearest depot.

[178] This has been weighted by the amount of work carried out by each depot so that atypical small depots do not skew the results.

(b) For VPS, 80 per cent of these customers were within [20–30] miles of its nearest depot.[179]

(c) For SPS and Clearway, 80 per cent of these customers were within [50–60] miles and [60–70] miles respectively—distances substantially greater than those of either merging party.

11.21 Consistent with our catchment area analysis of distances currently travelled (see paragraphs 7.29 to 7.36), these seemed to be realistic distances to travel and we could therefore say that on the basis of catchment areas VPS, SitexOrbis, Clearway and SPS might have been credible potential suppliers for national accounts. For the remaining competitors shown, reaching 80 per cent of customers (and even 50 per cent in some cases) would have required travelling longer distances than we would expect them to be willing to travel regularly based on their current infrastructure (70 to 100 miles). We considered that this analysis showed that other SSVP suppliers, based on their current depot infrastructures, were not as able to serve national customers as the merging parties, Clearway and SPS. This was because smaller suppliers currently had only one depot (although we noted that SecureSite was likely to open a depot in the Midlands and was considering opening an additional depot in northern England) and travelled distances to reach customers in many parts of Great Britain which were likely to be unrealistic, at least on a regular basis.

11.22 This was consistent with the maps shown in Figure 4, which suggested that SPS can cover the majority of Great Britain within 70 to 100 miles of its depots. Clearway had good coverage of England but would have to travel significantly further than typical maximum distances of 70 to 100 miles to supply properties in Scotland and Wales. The single depots of other suppliers were not well placed to cover even all of England and, again, this suggested that they were not as credible suppliers for most nationwide customers.

11.23 We acknowledged that some 'nationwide' customers may have had a concentration of properties in certain areas and that suppliers may have been willing to travel very long distances where economic to do so; for example, Clearway may have been willing to supply a customer with many properties in England and a small number of properties in Scotland and Wales. Despite this, a simple geographical analysis suggested that suppliers other than SPS and Clearway were unlikely to offer significant competitive constraint for customers with national needs and that Clearway would have been at a disadvantage for customers whose needs included Scotland or Wales.

Share of supply

11.24 Table 6 shows the revenues earned from SSVP from commercial customers as an indication of the relative size of the main suppliers. The table also includes the suppliers' total revenues and the total revenues they earned from all services provided to vacant commercial properties to illustrate other aspects of their scale.

[179] Post-merger we expect VPS to rationalize its combined network of VPS and SitexOrbis depots but we still expect the distances it needs to travel to be no higher than this.

TABLE 6 **Revenue and share of supply for SSVP suppliers (commercial sector)**

Supplier	*Total UK revenue £'000*	*Total revenue from vacant property services to commercial customers £'000*	*Revenue from SSVP to commercial customers £'000*	*Share of commercial SSVP market %*
VPS	[✂]	[✂]	[✂]	[60–70]
SitexOrbis	[✂]	[✂]	[✂]	[0–10]
SPS*	[✂]	[✂]	[✂]*	*[10–20]*
Clearway	[✂]	[✂]	[✂]	[0–10]
Veritas	[✂]	[✂]	[✂]	[0–5]
SecureSite	[✂]	[✂]	[✂]	[0–5]
North Star Estates	[✂]	[✂]	[✂]	[0–5]
Maltaward	[✂]	[✂]	[✂]	[0–5]
PSS	[✂]	[✂]	[✂]	[0–5]
Pro-tex	[✂]	[✂]	[✂]	[0–5]
GMS	[✂]	[✂]	[✂]	[0–5]
Total		[✂]	[✂]	100

Source: The parties.

*[✂] Hence this will overstate its SSVP revenue and share.
Notes:
1. Revenues for most recent financial year available.
2. Loxal and Secure Empty Property were recent entrants and have been excluded from this table. We also excluded Shieldcom, a supplier whose main focus was on other activities and who earned a very small amount of revenue from SSVP.

11.25 The first column of figures shows the suppliers' total revenues in the UK from their entire operations; the second column shows the revenues they earned from all services provided to vacant commercial properties; the third column shows the revenues they earned from providing SSVP to commercial customers. Finally, the fourth column shows each supplier's share of the revenues in the third column. Our focus is on the third and fourth columns, but the first two columns provide a useful illustration of the broader scale of these suppliers. From the data available we were not able to compile revenue or share information for national customers (where we considered that the merging parties' combined shares were high, based on the few national customers we were aware of who use other suppliers), or customers in particular regions. The table should be interpreted as one indicator of each supplier's competitive strength which was informative when combined with considering the geographic areas in which each supplier operated.

11.26 The table excluded companies (such as [✂]) that subcontract these services to specialist SSVP suppliers since to include them would result in some double counting. It may have excluded some small suppliers for which we do not have information, and excluded self-supply, since it was difficult to estimate the level of self-supply. Hence the table was likely to overstate the true shares of supply of SSVP for all the companies listed. We also did not rule out the possibility that other SSVP suppliers exerted some level of competitive constraint, as we discuss below, but we nevertheless thought that the table was a useful guide to the relative size of VPS and SitexOrbis and the other main suppliers of SSVP.

Closeness of competition

11.27 VPS was by a large margin the biggest supplier of SSVP to commercial customers, and combined the merging parties would have had a share of around [70–80] per cent of revenues (see Table 6 above). SPS was the next largest supplier with a share of no more than [10–20] per cent (which was likely to overstate its share [✂]) followed by SitexOrbis and Clearway. We noted that several parties told us that this was a growing sector and therefore we regarded these figures as informative but not the only indicator of each supplier's competitive strength.

11.28 We also noted that SitexOrbis had refocused its efforts on the commercial sector only relatively recently[180] but had been able to use its depot network and reputation from the social housing field to grow. Although its share was estimated at only around [0–10] per cent, we expected it to have grown its revenues further, absent the transaction. SitexOrbis told us that it had a growth plan which had been delayed due to the merger but which it considered otherwise achievable. Clearway was also a relatively recent entrant to the supply of SSVP but had been increasing its revenues in the commercial sector.

11.29 VPS and SitexOrbis had the largest networks of depots (with 20 and 23 depots respectively[181]) while the next largest specialist suppliers of SSVP had four. This meant that we expected that, for many customers, the two nearest depots would have belonged to the merging parties and, while other suppliers may have been willing and able to meet their needs, some or all of those suppliers would have been at a cost disadvantage due to greater travelling times.

11.30 In assessing the closeness of competition between the merging companies, we evaluated a number of sources of evidence, including the parties' internal documents, information based on tenders and quote and order sales in which the parties had participated, views expressed in customer hearings, our customer survey, and possible sources of cost advantages. We summarize each of these in turn below.

Views expressed in internal documents

11.31 In its Budget Commentary 2009/10 written in January/February 2009, VPS identified [✂].[182]

11.32 In TDR's initial assessment of the investment opportunity that the acquisition of SitexOrbis represented, TDR included among the upsides of the acquisition [✂].[183]

11.33 [✂] prepared a report to guide SitexOrbis's commercial sector strategy in late 2010. It said '[✂]'. The other suppliers named in the [✂] report were [✂].

11.34 VPS said that this report stated that VPS and SitexOrbis's market share in the broader commercial vacant property security market was only [✂] per cent, and this market had traditionally been dominated by local suppliers providing a range of vacant property solutions.[184] It said that [✂] per cent of the 'narrow commercial market' was supplied by local suppliers.[185] This estimate was based on the [✂] Report, which covered a wider range of services including inspections, alarms, fencing and bollards, CCTV, guards and patrols, and steel screens. [✂] reported that only around 15 per cent of buildings in its survey were protected with steel, which [✂] described as a '100% specialist market due to required steel inventories and low usage levels of steel outside variants'. For these reasons, we did not consider that the market for which the [✂] Report estimated shares corresponded to the market we were investigating.

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[180] VPS/TDR told us that Orbis had previously attempted to enter [✂].
[181] Including one in Northern Ireland; see paragraph 5.30 above.
[182] [✂]
[183] [✂]
[184] VPS & TDR response to CC provisional findings, paragraph 3.3, referring to slide 5F of the [✂] report.
[185] VPS & TDR response to CC provisional findings, paragraph 1.7.

Tender information from the merging parties

11.35 We had some information on tenders in the commercial sector but, as noted above, tenders were relatively rare: quote-and-order customers made up [✂] per cent of VPS's commercial SSVP revenue and [✂] per cent of the commercial properties they served. VPS told us that the remainder came from non-exclusive contracts with [✂] and [✂], which received fixed prices regardless of the size of the property.

11.36 In the data that VPS submitted on commercial tenders in the last three years, there were [✂] commercial bids, of which VPS won [✂], SitexOrbis [✂] (although [✂] winner was unknown), Legion Security Services won [✂] (not involving SSVP), Clearway [✂], and GMS and SecureSite were appointed along with [✂] in the [✂]. VPS reported that it believed that SitexOrbis bid in [✂] of these [✂], Clearway in [✂], SPS in [✂], and a number of other suppliers in [✂].

11.37 SitexOrbis gave us information on [✂] commercial tenders, of which SitexOrbis was a winner in [✂] and VPS in at least [✂]. Other winners included [✂] others (whose identities were not revealed to SitexOrbis) alongside [✂] tender and an [✂] ([✂]). We did not know who else bid in the tenders in the SitexOrbis data, but the data was consistent with a view that VPS was the closest competitor to SitexOrbis.

11.38 Some switching did occur among quote and order customers. VPS provided some examples of customers switching from VPS to a range of other suppliers—both end-suppliers and contractors—in the last three years including SitexOrbis, SPS, Clearway, MITIE, Securitas/Reliance, Ward Security and G4S.

Customer views

11.39 Many customers that we spoke to seemed to consider that the two parties were each other's closest competitor, especially in terms of their geographical coverage.[186] However, some of the customers we spoke to believed that other suppliers—notably SPS and Clearway—were capable of meeting their needs.

11.40 We were aware that a number of commercial customers multisourced. Of these, we generally expected customers who used one of the merging parties and a third party supplier ([✂] was one such example) to be less affected or concerned by the merger than customers who used both of the merging parties (such as [a major grocery retailer]).

11.41 In its response to our provisional findings, VPS said that we had failed to take into account in our assessment the fact that the 'vast majority' of national commercial customers interviewed by the CC were unconcerned by the merger.[187] We summarize relevant information from our evidence-gathering process below.

(a) [A major grocery retailer] was concerned by the merger and said that only the parties could supply its security needs.

(b) Enterprise Inns told us that it was vital to have a supplier with a nationwide network and depots close to its vacant properties, since it required a supplier that could react on a national basis at often very short notice (same day).

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[186] See Appendix F.
[187] VPS & TDR response to CC provisional findings, paragraph 1.7. See also TDR Capital and VPS joint response to third party responses to the provisional findings report and Notice of possible remedies.

(c) AXA said that the merger would have no impact on it and limited impact on the market. But AXA made limited use of steel, and said that it required a supplier who could offer a single nationwide price schedule without subcontracting.

(d) Grant Thornton said that the merger would not have a huge impact on its business but that it viewed the alternative large-sized suppliers as being SPS Doorguard and SecuriGroup (which did not provide SSVP itself).

(e) If VPS tried to increase the prices it charged Spirit, Spirit would go back to market and would also look at its strategy again. Spirit said that there would remain some choice in suppliers. Spirit's specifications were very individual and stringent,[188] and it required a national network of depots (it would be unusual to supply national services from two depots).

(f) G4S said that the merger had the potential to drive up prices but a price rise may increase the chance of entry.

11.42 We agreed with VPS that national commercial customers (other than [a major grocery retailer]) with which we held hearings did not explicitly state that the merger raised concerns for them. We noted that the hearing evidence nevertheless indicated that they had quite specific requirements (such as single national pricing without subcontracting and/or a national network of depots) which in practice was likely to restrict the pool of potential SSVP suppliers. Moreover, two of the four alternative suppliers mentioned by these customers (SecuriGroup and Camelot) did not supply SSVP. Finally, one customer noted that post-merger price rises may have increased the chance of entry; however, our detailed assessment of the competitive effects of the merger did not support the view that this would defeat such a price rise.[189]

Customer survey

11.43 Our customer survey asked customers of each of the merging parties which supplier they would switch to if their supplier ceased to exist. The results are presented in more detail in Appendix F. Our two general conclusions were that the majority of respondents did not know to which supplier they would switch, and that those who did name an alternative generally picked the other merging party. In general, awareness of other suppliers was very low, with around 30 per cent of both social and commercial customers saying that they were not aware of any supplier other than the one(s) they currently used and, in addition, over 40 per cent answering 'Don't know'.

11.44 Among SitexOrbis's commercial customers, 64 per cent said 'Don't know', 3 per cent 'Depends' and 3 per cent said that they would undertake research or tender. 10 per cent said VPS and 3 per cent each named a range of suppliers (including Clearway, SecureSite and general contractors). As with social housing customers, we considered excluding those who could not answer and assuming that those who did name a particular customer were representative of where all customers would go. If we did this, we would say that 33 per cent would switch to VPS.[190]

11.45 Among VPS's commercial customers, there was greater uncertainty, perhaps reflecting VPS's strong position in the commercial sector. 68 per cent said 'Don't know' and 3 per cent said that they would undertake research or tender. 6 per cent

[188] In Spirit`s most recent tender exercise for SSVP, the response rate from tenderers who met the basic criteria was lower than expected and it was felt that one reason might be the already restricted size of the national market for suppliers of such services.
[189] See paragraphs 11.109–11.153 below.
[190] Survey Q21; note small sample size for last statistic.

said SitexOrbis and 3 to 6 per cent named each of a range of suppliers (including SecureSite with 6 per cent, Clearway, SPS, MITIE and general contractors). If we again excluded those who could not give an answer, the share of named answers giving SitexOrbis was 21 per cent.[191]

11.46 As described in paragraphs 10.37 to 10.40, we consider that diversion ratios can be instructive information about the effects of a merger. For commercial customers, we calculated a lower bound of 10 per cent (from SitexOrbis to VPS) or 6 per cent (from VPS to SitexOrbis), but allocating the answers of those who did not know gave 33 or 21 per cent respectively. Again, we did not place too much weight on particular numbers (the level of uncertainty may itself be more informative than any particular answer), but we did observe that diversion ratios were likely to be reasonably high (although lower than in the social housing sector).

Cost advantages—competition at the national level

11.47 We noted that the parties each operated from a large network of depots, which entailed a different cost structure from their competitors (which operated at most four, in contrast to VPS and SitexOrbis's 20 and 23 depots respectively[192]). This implied that competitors were likely to travel longer distances to serve properties, which would incur additional manpower and transport costs; on the other hand, they would have lower total overheads (the difference being mainly property rent). We considered whether this different business model might be significant if this allowed VPS and SitexOrbis to compete at lower marginal costs, as this would imply a cost advantage in competing for work, especially for customers with national requirements (where VPS and SitexOrbis were likely to have shorter travel times and lower costs—see paragraph 11.20). [✂][193]

11.48 VPS told us that a business with a national infrastructure and a large number of depots would have a cost advantage over smaller competitors due to shorter average journey times. It also told us that this advantage was small in the context of the overall cost to serve a customer. This was because a significant percentage of the total cost of servicing a commercial customer [✂] could arise from inspection costs which could be delivered through a network of inspectors working from home or could be subcontracted. Weekly inspections therefore did not need to be delivered from a regional depot, which reduced (but did not eliminate) the cost advantage of a national network.

11.49 VPS produced a comparative analysis of the total variable cost of serving a typical national commercial customer using its current network of depots and using only two depots ([✂][194]). We considered that such an analysis was likely to give a good insight into the cost advantage of a business with a national infrastructure, such as the main parties, over a business such as Clearway and SPS (with two and four depots respectively).

11.50 The VPS analysis showed that costs would be approximately [✂] per cent higher using just two depots rather than VPS's own network [✂]. This included the costs of a weekly inspection and alarm monitoring. If these were excluded (ie a customer did not want these options), then the competitive advantage was [✂] per cent [✂]. VPS told us that just over half ([✂] per cent) of its commercial customers required

[191] Survey Q21; note small sample size for last statistic.
[192] Including one in Northern Ireland; see paragraph 5.30 above.
[193] See paragraph 9.16.
[194] See paragraph 11.9 above.

inspections, of which [✂] per cent were less frequent than weekly,[195] and therefore we considered that the higher ([✂] per cent) figure would apply to a large proportion of customers. We considered that this [✂] per cent advantage was conservative because vehicle depreciation was not included in VPS's analysis and would be higher for a vehicle covering significantly longer distances; more vehicles would also be required as availability would be reduced by the longer journey times; and because VPS included the time of sales staff, which we regarded as largely a fixed cost.[196]

11.51 We note that VPS's analysis assumed that drive-time would be [✂] times longer for a small network (two depots) than for a large national network (VPS's current network). Our own analysis suggested that SPS's average distance travelled to reach SitexOrbis's customers would be three times that of SitexOrbis or VPS,[197] but we found that Clearway would have to travel even greater distances.[198]

11.52 This implied that SPS was likely to face at least a [✂] per cent direct cost disadvantage against either VPS or SitexOrbis when competing for national commercial customers, and Clearway would be at a greater cost disadvantage.

11.53 SitexOrbis told us that it could supply commercial customers at a lower cost and [✂] than suppliers with a smaller network because it did not have the same fuel costs or the same time costs of travelling.

11.54 VPS's due diligence in connection with the merger indicated that it intended [✂]. Nevertheless, the merged entity would still have had a larger depot network than either VPS or SitexOrbis individually which would tend to reduce the merged entity's average travel distances, increasing its cost advantage to serve national customers.

11.55 In response to our provisional findings, VPS said that this cost saving was at least partially offset by the increased investment in depots and potential management problems given that the social and commercial sectors operated in different ways and might use different equipment.[199] However, we would expect marginal cost savings (from reduced travel time) to lead to lower prices whereas higher fixed costs (depot costs) would not directly affect prices. Moreover we did not accept VPS's argument about the cost of serving both social and commercial customers from the same depots, since any disadvantage from this also applied to all their major competitors who also served both social and commercial customers from each of their depots.

11.56 We did not dispute that VPS operated a successful business in the commercial sector from two depots for several years or that SPS and Clearway were able to serve commercial customers including (at least to some extent) national customers.[200] These facts are consistent with VPS and SitexOrbis having cost advantages: it is not an industry with perfectly homogeneous products where only the cheapest supplier would ever win business; it features differentiated services and complex prices, and there are many transactions, so we would expect other suppliers to win business some of the time.

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[195] VPS told us that competitors like [✂] outsourced inspections. (Whilst we noted that the ability to outsource inspections meant that competitors were able to offer an inspections capability to customers, competitors would not be able to capture margin on outsourced inspections.) VPS also told us that inspections could be subcontracted at a cost which was [✂] per cent higher (£[✂] vs £[✂]) than its in-house cost of delivery.

[196] We would not expect the number of salespeople employed to change according to whether a supplier won a particular customer's business.

[197] See paragraph 11.20 above.

[198] See Table 5 above.

[199] VPS & TDR response to CC provisional findings, paragraphs 3.11–3.12.

[200] VPS & TDR response to CC provisional findings, paragraph 3.11.

11.57 We did not generally attempt to model cost advantages to serve sub-national customers since this would depend on the location(s) of each customer's properties (although the same analysis can be used to look at the effect on an individual customer as we did in one example below in the first footnote to paragraph 11.97). We did expect, based on Figure 1 and Table 5, that on average the merged company would have been nearer than its rivals to customers' properties and hence would have enjoyed some level of cost advantage, although the level would vary between customers and for some customers the reverse may have been true. In particular, when considering certain areas where the merging parties had local depots but competitors would have had to travel long distances, we expected the parties to enjoy a significant cost advantage.[201]

11.58 We also noted that the merging parties had far more operatives trained to fit steel and alarms. VPS had [✂] employees (or [✂] full-time equivalents) for steel and alarm fitting and SitexOrbis had [✂] steel-fitting teams (most teams are two people, occasionally three), [✂] full-time mobile alarm wardens and a number of other employees who could also fit alarms. By comparison, Clearway had [✂] alarm and steel fitters, and Veritas had about [✂] steel installers. We considered that this would give the merged company certain operational advantages over its competitors in its ability to respond efficiently to customer service requests and credibly to promise rapid response throughout the country.

Conclusion on closeness of competition

11.59 Whilst our analysis indicated that Clearway and SPS were important SSVP suppliers to commercial customers, we found that the merging parties appeared to be each other's closest competitor, particularly when considering the evidence of the parties' own internal documents and the similarity and size of their range of operations and depots. It was clear that for some customers there were other suppliers which would also be viewed as close competitors, although our survey generally found that there was low awareness of other suppliers and each of the merging parties was felt to be the other's closest (or equal closest) competitor. Generally, the greater the geographic range of the customer's operations, the fewer the suppliers that would be considered to be credible suppliers. For customers with national requirements, this list would have included SPS and, in most cases, Clearway (we noted also that SecureSite was expanding its geographic coverage). Depending on the region(s) in which the customer operated, the evidence we saw suggested that customers with regional requirements could also have been served by some of the smaller operators with single depots that we have discussed in this report.[202]

11.60 We also considered whether smaller local suppliers imposed a competitive constraint on the larger specialists we have considered. However, we saw very little indication in our survey or hearings that customers viewed local suppliers as a viable option or that larger SSVP suppliers (other than VPS) viewed local suppliers as a competitive constraint. Accordingly we did not expect local suppliers to impose a significant constraint either pre- or post-merger.

Self-supply

11.61 The nature of the commercial sector was that for most customers, their portfolios of properties were relatively small and vacant properties did not arise with regularity.

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[201] Again, see first footnote to paragraph 11.97 for one example.
[202] As we discuss in paragraphs 11.90–11.100.

For larger customers, their properties were often spread over a wide geographic area. Both of these factors reduced the attractiveness of self-supply, since it was best suited to companies responsible for a large number of vacant properties that were geographically concentrated: the key factors were having enough regular work for internal contractors to carry out and having it spread over a small area to enable efficient scheduling and travel.

11.62 Our customer survey suggested that very few (3 per cent) of commercial customers would consider self-supply of SSVP, and no customers of the merging parties said that it would be their first choice if their existing supplier did not exist.[203] None of the commercial customers with which we held hearings expressed an interest in or willingness to self-supply (although some contractors acknowledged the possibility, as we discuss in paragraph 11.138 below).

11.63 Therefore, although we acknowledged that some customers may have had the option to self-supply, we considered that self-supply was unlikely to be a strong competitive constraint on the main parties.

Profitability of a hypothetical price increase

11.64 As noted in paragraph 9.6, the incentives for merging parties to increase prices would depend partly on the extent to which customers would substitute away (to other suppliers of SSVP, or to alternative security services, or indeed ceasing to use any form of security services), and partly on the margins they earned. Below we assess in turn the importance of price, substitution and margins.

Importance of price

11.65 [✂] prepared a report to guide SitexOrbis's commercial sector strategy in late 2010. It said that [✂], although it noted that in many cases [✂]. It found that [✂] were the key purchase criteria, with [✂]. It noted that [✂]. It noted that VPS offered '[✂]'. It also noted that [✂].

11.66 Our customer survey found that price was among the most important elements in choosing a supplier, but other factors were of similar importance (including speed of response, minimizing the risk of damage, requirements of insurance cover, and customer service).[204]

Substitution to other products or suppliers

11.67 The evidence we received on the likelihood of commercial customers substituting away from the parties pointed in different directions. On the one hand, our hearings gave us a fairly consistent view that customers would find it difficult to reduce the level of protection on their properties.[205] Some said that it would be difficult to find alternative suitable suppliers who could offer prices at the current level; others said that they were not concerned by the merger, but still had stringent requirements for suppliers which, in our view, a very limited number of suppliers would be able to meet.[206]

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[203] Survey Q14c & 21 respectively.
[204] Survey Q32.
[205] See, for example, our hearing summaries with [a major grocery retailer] (paragraph 2), Spirit (paragraphs 2, 4 & 11) and Grant Thornton (paragraph 9).
[206] See paragraphs 11.39–11.40 above.

11.68 On the other hand, respondents in our survey gave the indication of being price sensitive. In response to an across-the-board price rise by both VPS and SitexOrbis, 42 per cent of commercial customers told us that they would consider use of a cheaper alternative, 40 per cent would consider a different supplier and reduce business with their current supplier, and 36 per cent would consider moving their business to a different supplier.[207] Each of these numbers was slightly higher than the equivalent for social housing customers.

11.69 These numbers were based on a price increase of an unspecified size. To gauge responsiveness to price increases of different sizes, and to attempt to allow for stated preference bias,[208] we asked each respondent a follow-up question as to how likely they would be actually to carry out the stated response at different levels of price increase. They could be very likely, quite likely, quite unlikely or very unlikely, or they could say 'Don't know'. We looked at those who said 'very likely', and the larger group who said either 'very likely' or 'quite likely' (which we group together under 'likely'). This approach led to the following results:[209]

(a) For a 5 per cent price increase, we found that:

(i) 9 per cent were *very likely* to reduce their business and 10 per cent to move it; and

(ii) 19 per cent were *likely* (ie either very likely or quite likely) to reduce their business and 21 per cent to move it.

(b) For a 10 per cent price increase, we found that:

(i) 21 per cent were *very likely* to reduce their business and 21 per cent to move it; and

(ii) 29 per cent were *likely* to reduce their business and 27 per cent to move it.[210]

(c) We did not prompt respondents for their likelihood of switching to a cheaper alternative, but we would expect[211] this to be in the order of:

(i) for a 5 per cent price increase, 10 to 12 per cent would be *very likely* to use a cheaper alternative and 20 to 24 per cent would be *likely* to do so; and

(ii) for a 10 per cent increase, 22 to 24 per cent would be *very likely* to use a cheaper alternative and 31 to 32 per cent would be *likely* to do so.

11.70 In addition, 72 per cent of commercial customers said that they did not think the merger would have any effect on them (and a slightly lower figure of 61 per cent of cus-

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[207] Multiple responses were allowed and so these figures include a small amount of double counting, but 94 per cent of respondents gave at least one of these answers. All of these figures were calculated excluding respondents who answered 'Don't Know' or refused to answer from the denominator, ie we effectively assumed that those respondents would give answers in the same proportions as those who did reply. Excluding them made little difference to the results.
[208] As described in paragraph 10.60.
[209] Again, these figures excluded those who answered 'Don't know' when asked what they would do from the denominator. However, for customers who answered 'Don't Know' to the follow-up question about how likely they were to carry out the action they considered, we assumed that they were not likely to carry it out in practice. Similarly anyone who did not say they would consider a particular response to the opening question was considered unlikely to actually carry out that response (as explained in the footnote to paragraph 10.60*(a)*).
[210] We also asked about 20 per cent and higher price increases and slightly more customers became likely to reduce or switch purchases.
[211] Based on the proportions of those who said they would consider reducing or moving their business that said they were likely to do so.

tomers of VPS or SitexOrbis, ie excluding prospective customers); and only 11 per cent thought it would have a negative effect.[212]

11.71 We viewed these responses to our survey as indicating a willingness to switch among some customers, but we had to reconcile it with other evidence. VPS said that 'the only explanation for these customers being unconcerned by the merger is because they [must be] confident that there are alternative security solutions and suppliers for their vacant properties'.[213] We agreed that if customers thought they could avoid a price increase, it was probably because they believed that they could find alternative suppliers willing to supply on equal terms to the merging parties. However, the evidence, including other questions in the survey, suggested that most customers had limited knowledge of alternative solutions and suppliers and that, moreover, such confidence was inconsistent with other evidence (including awareness of other suppliers in the survey) and was likely to be misplaced.

11.72 Around two-thirds of respondents who said that they would consider a different supplier did not know who they would move to, and the only SSVP specialists mentioned were Clearway (by 4 per cent) and SPS, SecureSite and Loxal (by 2 per cent each).[214] Indeed, some respondents mentioned companies which did not supply SSVP, eg security alarm companies. Customers with experience only of (one or both of) the merging parties might have expected to be able to elicit similar quality and prices from other suppliers. We had to consider whether in practice, if they tried to find a new supplier, customers would have been able to find one willing and able to supply under the same terms as VPS or SitexOrbis offered pre-merger.

11.73 In practice, if they tried to find a new supplier, and they were able to identify the suppliers we have identified, our analysis suggested that customers would have found a limited choice of suppliers willing and able to supply under similar terms as VPS or SitexOrbis offered pre-merger. As discussed above, we considered that national customers had a limited choice of alternative suppliers, currently consisting of SPS and Clearway; and we noted that the merging parties were likely to have cost advantages over both those companies. We also noted that Clearway currently did not compete for some of the larger commercial tenders (see paragraph 11.85). We did not rule out the possibility that smaller single-depot suppliers such as SecureSite may have been viewed as credible suppliers for some national commercial contracts too (perhaps depending on the exact geographic requirements of the customer).[215] However, we did not expect these suppliers to be as credible as VPS, SitexOrbis, SPS and Clearway for most customers with national requirements because *(a)* the distances they would have had to travel were large, making it harder for them to compete on price, and *(b)* we considered that customers would place weight on a depot network as evidence of being able to respond to a nationwide estate of properties in a timely basis.[216] Therefore we found that any constraint these suppliers would have imposed on the merged company would have been limited.

11.74 Commercial customers with regional SSVP requirements were likely to have a wider choice of suppliers, depending on their location, although in some parts of the UK we found that they would have a limited choice of suppliers which were able to compete as effectively as the merged entity (taking into account the distance of their operations from regions where we identified a limited number of suppliers and the cost

[212] Survey Q37.
[213] VPS and TDR response to CC provisional findings, paragraph 2.5(a).
[214] Survey Q40.
[215] We were aware that SecureSite was appointed to secure Little Chef's sites in 2007.
[216] For example, Spirit Pub Company (Spirit) told us that the extent of a supplier's depot network was not in itself a critical factor but added to the credibility of the supplier's claims on response times.

advantage the merged company was likely to have for customers who were not located close to a competing supplier).[217]

11.75 We also considered the nature of the transactions between customers and suppliers and the likelihood of price discrimination.[218] We have explained that we expected there to be some customers who had better alternatives than others (see paragraph 7.17)—for example, because their security needs could be met by different types of security—and that prices were generally set individually and can vary widely from customer to customer. Therefore we did not expect the merging parties uniformly to increase their prices across the board to all customers. We expected that the merged company would try to identify which customers would bear a price increase, and what size of price increase, and set prices accordingly post-merger. Taking this into account, a possible interpretation of the results of the simple uniform price rise question in our customer survey was that there would be substantial switching; but this interpretation was likely to be misleading because it would have overstated the amount of switching that would take place assuming a strategy of targeted price increases, which we considered to be more likely than equal price increases for all customers. As discussed in paragraph 7.17, we did not think that the existence of some customers who were willing to switch to alternative security products would constrain a price rise for other customers.

Margins

11.76 We had limited information on margins since the main parties did not record margins by business activity and in practice costs were shared between them. However, the evidence was that margins in the commercial sector were typically substantially higher than in the social housing sector.[219]

11.77 VPS told us that its gross margin (excluding depreciation) for rental services in the commercial sector was [✂] per cent, and its overall gross margin (excluding depreciation) for rental services across social and commercial was [✂] per cent. Including depreciation, its overall margin across all service lines and across both social and commercial was [✂] per cent.

11.78 SitexOrbis told us that for its self-delivered security work in the commercial sector, its gross margins were '[✂]'.

11.79 We regarded these [✂] gross margins as being supportive of a view that the parties would have an incentive to increase prices post-merger.[220]

Conclusions in the absence of countervailing factors

11.80 Below we present, in turn, our conclusions in relation to the markets for the supply of SSVP to: *(a)* customers in Great Britain with national needs; *(b)* customers in Great Britain with regional needs; and *(c)* customers in Northern Ireland.

National level

11.81 We considered the evidence from our hearings with commercial customers carefully. We noted that these hearings did not explicitly indicate significant concern on the part

[217] See Figure 3 above and paragraphs 11.93–11.98 below, and the specific example in the first footnote to paragraph 11.97.
[218] See paragraph 9.13 above.
[219] Paragraph 5.7 above.
[220] See footnote to paragraph 9.6 and Guidelines, paragraph 5.2.15.

of most of the customers we spoke to, but our assessment suggested that in reality the pool of alternative suppliers for these customers was likely to be smaller than they anticipated. We also noted that our customer survey indicated low levels of concern. The responses from the hearings and the results of the customer survey were two elements in our wider assessment of whether or not this merger would have given rise to an SLC.

11.82 We found that, at present, VPS, SitexOrbis, SPS and Clearway had the depot infrastructure sufficient to cover most of Great Britain, albeit that VPS and SitexOrbis had significantly larger depot networks and Clearway in particular would have faced long journeys to cover Wales and Scotland. We noted that the customers we spoke to appeared to have quite specific requirements which may have served to restrict the pool of potential SSVP suppliers. Therefore for most customers the merger represented, at best, a reduction from four to three suppliers, where one supplier was very large and the other three main suppliers pre-merger were much smaller (and of similar size to each other) in terms of relevant turnover. Although this was a relatively small increment to VPS's pre-merger size, VPS's strong position in the market, combined with the enhanced depot infrastructure VPS has acquired through the merger, meant that any significant increment was cause for potential concern.

11.83 As described above,[221] we did not expect that smaller single-depot suppliers such as SecureSite would be as credible as VPS, SitexOrbis, SPS and Clearway for most customers with national requirements because of the distances involved and the value for credibility of having a depot network. Therefore we found that any constraint that these suppliers would have imposed on the merged company would have been limited.

11.84 Tender data provided limited evidence on the relative strength of different suppliers. SitexOrbis [✂] of the commercial tenders for which VPS provided information, although it was the most commonly reported bidder and [✂] was the only specialist SSVP supplier to beat VPS. On the other hand, in SitexOrbis's tender data, VPS appeared to be the main competitive constraint.

11.85 Clearway told us that Scotland was a long way from the Clearway depots and this distance became problematic when securing a property, especially if there were security issues at the property and multiple trips needed to be made. Clearway also told us that it did not compete for some of the larger commercial tenders (at the 100 to 150 vacant property level) for strategic reasons; to do so it would need a different management system within the office, and would need additional staff and would have to open a bigger depot and/or two or three more depots. Operationally and financially, the challenges would be surmountable. However, both its limited depot network and its current internal structure suggested that Clearway was not pre-merger a strong competitor for at least some national contracts.

11.86 Evidence on costs suggested that VPS and SitexOrbis had a significant direct cost advantage over other suppliers due to their depot structure,[222] which may be increased by their greater volumes of total SSVP work enabling them to schedule work more efficiently.[223] This suggested that SPS and Clearway in their current form were likely to be less competitive on price than the merging parties.

11.87 Furthermore, we considered that the merger may remove a [✂] from the market. SitexOrbis told us that its efforts to enter the pub sector caused [✂], telling us, for

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[221] See paragraph 11.73 above.
[222] See paragraph 11.47ff.
[223] For example, VPS told us that [✂].

example, that it was able to go to [✄] and put a credible offer on the table that [✄] by [✄] per cent.[224]

11.88 Various aspects of service quality were also important to customers and the evidence indicated that, again, the merging parties were likely to have certain advantages over SPS and Clearway. For example, their larger depot networks should have allowed them to service properties faster and, importantly, give credible assurance to customers that they could do so.[225] The parties' larger depot networks may also have provided assurance that the parties were able to respond in emergency situations.[226]

11.89 In conclusion, in relation to customers with national SSVP requirements, in a situation where VPS and SitexOrbis had, at best, two competitors for most customers, and where VPS and SitexOrbis appeared to be each other's closest competitors (on the balance of the evidence we have reviewed above) and other suppliers were more distant competitors, we would expect a merger to lead to price increases absent countervailing factors.

Regional level

11.90 In regions where they had depots, we expected SPS and Clearway to be stronger competitors than they were for national contracts. Differences in average travel distances may be less pronounced at the regional level, rendering them more attractive to regional customers than to national customers and placing them at less of a cost disadvantage.

11.91 We also considered that smaller competitors (notably SecureSite but also other suppliers) were more likely, at the regional level, to provide a degree of competition and hence a degree of competitive constraint post-merger.

11.92 The evidence available suggested that SitexOrbis was still likely to be the closest competitor to VPS but it would be possible for a combination of competitors to provide sufficient competitive constraint to prevent an SLC in some regions. Figure 3 showed that customers in the South-East of England could be served by SPS, Clearway and SecureSite as well as smaller suppliers. Customers in the Midlands, Yorkshire and the North-West could be served by SPS, Clearway and at least one smaller supplier. Customers in North Wales could be served by companies including SPS, GMS, North Star Estates and possible Clearway (if we extended distances travelled to 100 miles). On balance, we considered that customers in these areas had sufficient choice of suppliers, in addition to the merged company, to prevent price rises post-merger.

11.93 However, other regions of Great Britain appeared to be much less well served. Using a 70-mile straight-line radius from depots, we had concerns about some regions including major urban areas (see Figure 4 above) where, other than the merging parties:

- Scotland was covered by only SPS and PSS.

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[224] VPS attributed this [✄]; but we note that pub companies' ability to negotiate lower prices is likely to have been affected by the willingness of SitexOrbis to enter and supply at those prices. [✄]
[225] For example, see footnote to paragraph 11.73.
[226] For example, AXA gave an example of how VPS had helped secure a £40 million commercial property which had been broken into by squatters over the Christmas period. VPS had mobilized very rapidly to help secure the premises (Source: Hearing summary, fn 1 (p3)).

- The North-East (Newcastle, Sunderland, Middlesbrough and Durham) was largely outside the area covered by any competitor.[227]

- No other suppliers had depots in South Wales and much of this region was unserved; Veritas was within range of Cardiff and Newport, and GMS may have been within range of Newport, but Swansea was outside the range of both. Therefore on this simple measure we had concerns about all of South Wales but especially the region west of Newport (including Cardiff and Swansea).

- South-west England (west of Bristol and Poole) was not covered by any large SSVP competitor,[228] and only Veritas may have been able to serve some (but not all) of this region.

11.94 The best case scenario in the latter three of these regions[229] is that, post-merger, there will be a single competitor to the merged company. We discussed in Appendix F VPS's argument that a single alternative bidder may be sufficient to constrain the merged company, and concluded that this was unlikely. We also noted that some commercial customers prefer to dual source and would have no choice of suppliers if left with only two. There may also be smaller local suppliers offering SSVP, but, as noted in paragraph 11.60, we saw very little indication in any of the evidence before us that local suppliers were viewed as credible alternatives by customers or as significant constraints by suppliers. In Scotland, we viewed SPS as a credible supplier but we saw no evidence to suggest that PSS added significantly to that competitive constraint: its commercial SSVP revenue was small (see Table 6) and it was not mentioned to us by any customer (including our survey respondents) or competitor. Therefore we considered that the competitive constraint was unlikely to be sufficient to replace SitexOrbis.

11.95 As a sensitivity check, we considered how the situation in each region would change if we extended radii to 100 miles on a straight-line basis. We suspected that, in practice, this may have been more feasible for some journeys (involving good road links) than others. We noted that some suppliers told us that they would be willing to travel longer distances to service a profitable commercial contract. However, they were likely to be at a considerable cost disadvantage compared with the merged company when travelling long distances, and so in order for the contract to be 'profitable' the price would have had to be relatively high. Therefore although they may have provided some level of constraint to the merged company, they were unlikely to be able to impose as effective a competitive constraint on the merged entity as VPS and SitexOrbis provided to one another pre-merger.

11.96 Even using 100-mile radii, our concerns about Scotland and the South-West were largely unchanged.

11.97 In South Wales, analysed using 100-mile radii, Veritas would have been able to reach as far as Swansea, but it would have been the only supplier that could reach points west of Cardiff. Cardiff and Newport may have been within reach of both Veritas and two additional small suppliers, GMS and Pro-tex, and so we considered whether the sum of these suppliers would have constituted a competitive constraint to the merged company here comparable to that imposed pre-merger by SitexOrbis.

[227] In response to our provisional findings, VPS said that Shieldcom, a SSVP supplier based near Liverpool, could supply the North-East. We spoke to Shieldcom, which does a very small amount of SSVP business and is largely focused on the North-West and, in any case, was well over 100 miles from the North-East by road (170 miles by Google Maps' suggested route).
[228] We spoke to a number of social housing providers in this region who were unable to name any SSVP supplier other than VPS and SitexOrbis.
[229] With the possible exception of the small part of South Wales that is east of Newport.

We considered it relevant that both GMS and Pro-tex were small suppliers in the SSVP sector (see Table 6); excepting GMS (which supplies Grant Thornton), none of these three suppliers were mentioned as a significant competitor by either suppliers (other than VPS, and they did not appear in its internal documents) or customers (in either our survey or hearings); and that they would all have had to travel long distances relative to the merged company to supply customers in South Wales (especially for GMS and Pro-Tex which were located 70 miles or more away) which would have placed them at a cost disadvantage.[230] For all these reasons, we thought Veritas and particularly GMS and Pro-Tex would have been significantly more distant competitors to the merged company than SitexOrbis was to VPS pre-merger.[231]

11.98 It was possible that Clearway might serve the North-East using a 100-mile straight-line radius (although it was more than 100 miles by road). North Star Estates, Secure Empty Property and, possibly, SPS might have been able to reach the North-East, but each would be a long journey by road and we have not seen evidence to indicate that either North Star Estates or Secure Empty Property was a strong competitive constraint[232] (ie even on a 100-mile basis, customers in the North-East were likely effectively to face a three to two merger where the third was at a cost disadvantage to the merging parties, with the possibility that there was a fringe of other competitors who would not be close competitors when taking into account both identity and cost disadvantages).[233] Therefore we did not consider that using a 100-mile radius significantly affected our conclusions.

11.99 VPS argued that it was likely that only a limited number of affected customers were located in regions where we had found an SLC.[234] We did not consider that it would be possible to estimate the number of affected customers in each region. Moreover, we were required to assess whether or not the merger would give rise to an SLC within any market or markets in the UK for goods or services; the number of customers within those markets is not relevant once we have found an SLC.

11.100 We therefore concluded that, absent countervailing factors, we expected an SLC throughout Scotland, in the North-East, in South Wales and in the South-West for the supply of SSVP to commercial customers.

[230] In paragraphs 11.47–11.57 we referred to VPS's cost model which, we found, showed that if a competitor had to travel three times as far as the merged company it would be at a direct cost disadvantage of at least 5–15 per cent (depending on whether weekly inspections were required). This can also be applied to trips from specific depots to an individual customer. So for example, to serve a customer near to Cardiff, if the merged company's round trip drive-time was 1 hour and GMS's round trip drive-time was 4 hours, GMS's cost disadvantage would have been at least 6–17 per cent.

[231] VPS disagreed with the conclusion that 'smaller competitors such as GMS and Pro-Tex would be unable to constrain the merger entity's prices in this region' (VPS & TDR response to CC provisional findings, paragraph 3.39), citing the fact that GMS has been appointed to the Grant Thornton framework on a national basis. We do not claim that they would have provided no constraint, but we did not consider they would have been able to replicate SitexOrbis's pre-merge constraint. With regard to VPS's specific example, GMS was one of three firms appointed to Grant Thornton's framework and so Grant Thornton was not reliant on it.

[232] Secure Empty Property was a recent start-up and did not have any meaningful amount of customers at the time of our report, and told us that it was primarily interested in potential customers around its office and depot in the North-West.

[233] Road networks made this journey considerably longer than 100 miles in practice. Google Maps' suggested driving route from SPS's north-west depot to Newcastle was 157 miles, from NSE's depot in Leyland to Newcastle was 149 miles, and from Secure Empty Properties to Newcastle was 150 miles.

[234] VPS & TDR response to CC provisional findings, paragraphs 3.55–3.56. VPS based this on the level of commercial respondents to our survey who would be 'likely' to move or reduce business if prices rose by 10 per cent, combined with figures on the proportion of VPS's commercial revenues that came from the North-East and Scotland. We have discussed in paragraph 11.71 the need to interpret figures from the survey with care, and noted that we would also be concerned about customers who would not respond to a 5 per cent price increase. The size of VPS's customer base in these regions may also be misleading since we were also concerned about effects of the merger on customers of SitexOrbis and prospective customers.

Northern Ireland

11.101 For the same reasons as given in paragraphs 10.74 to 10.77, our view was that the likelihood of the merger resulting in an SLC for commercial customers was remote.

Countervailing factors

11.102 The Guidelines suggest that an SLC may be prevented if there are countervailing factors such as buyer power, relevant efficiencies or entry or expansion. We consider each of these in turn below.

Buyer power

11.103 As we explained above,[235] in some circumstances, an individual customer may be able to use its negotiating strength to limit the ability of a merged company to raise prices. We were told that the commercial sector was characterized by short-term non-exclusive contracts and multi-sourcing. This may have reduced the importance of any particular job to suppliers (because the job would not have been large relative to the supplier's size) but it ensured that suppliers were competing for every job, giving them an incentive to keep prices low if that competition was effective (ie if there were credible alternative suppliers). VPS said that the countervailing buyer power of large customers created a broader constraint eliminating the merging parties' ability and incentives to raise prices and price discriminate in relation to commercial customers.

11.104 However, any buyer power ultimately depended on customers having strong credible alternatives to buying from the merging parties and, as we have discussed in relation to social housing,[236] their alternatives were limited, particularly when buying at the national level. Further, we expected large companies to be more likely to have buyer power if they offered exclusive contracts of guaranteed volumes or expenditure, but VPS told us that it did not have any such contracts in the commercial sector; and as far as we were aware nor did other suppliers. We also noted the example that SitexOrbis gave us of [✂], which would be an example of a large commercial customer that might have buyer power. Several years ago it had been able to get [✂] not because its buyer power increased but because SitexOrbis started competing for its business.[237] This suggested that for any customer who might plausibly have buyer power, competition between the merging parties can still have a significant effect on the price it pays.

11.105 The parties told us that in the commercial sector, [✂] subcontracted void security to Clearway and [✂] subcontracted void security to [✂].[238] This may have increased the set of competitive constraints on the parties, since they had to compete not only against direct competitors such as Clearway and SPS but also against larger intermediary companies such as MITIE or Morrison which could offer a wider range of services and subcontract SSVP.

11.106 However, these intermediaries were likely to be limited in their ability to provide additional competition since they outsourced their SSVP and so depended on being able to procure services at competitive rates. For example, Securitas told us that it generally passed through [✂]'s charges to its customers. It was unlikely that an end-

[235] See paragraph 10.79.
[236] See paragraph 10.80.
[237] As described in paragraph 11.87.
[238] Initial submission, paragraphs10.39–10.41, and Response to Issues Statement, paragraph 5.10.

supplier would compete with the intermediary that it supplied and so intermediaries did not expand the competitive set in any given transaction; at best they could add value to make the end-supplier a stronger competitive constraint.

11.107 We concluded that buyer power was unlikely to offset the SLCs we identified.

Efficiencies

11.108 As noted above,[239] we saw no evidence of significant merger-related efficiencies to offset any lessening of competition.

Entry/expansion

11.109 In this section, we consider whether new entry or expansion, at the regional and national levels, in the commercial sector would be timely, likely and sufficient to prevent any lessening of competition resulting from the merger.

11.110 We completed a similar analysis to that which we conducted for the social housing market. We assessed:

(a) whether there were barriers to entry and expansion in the availability or cost of SSVP products, labour and transport;

(b) the history of expansion, whether customer inertia might be an issue[240] and whether entry and expansion would have been constrained by the economics of depot expansion (paragraphs 11.115 to 11.120);

(c) whether a company with a large depot infrastructure (such as the merging parties) would have had advantages of economies of scale, density and scope and whether this constituted a barrier to entry (paragraphs 11.121 to 11.134); and

(d) finally, what the appetite for expansion was among both existing competitors and businesses in adjacent markets (paragraphs 11.134 to 11.139).

11.111 As discussed above (see paragraphs 11.9 to 11.12), the service requirements and market dynamics of the commercial and social housing markets differed in several important respects.

11.112 In addition, it was less important for a supplier of SSVP to commercial customers to have access to a depot near to customers' properties, as required response times were generally longer and, as a result of the relatively higher margins (compared with the social housing sector), higher travel costs could be sustained. This would allow a new entrant or expanding competitor to source new work and serve it profitably from further away than was possible in the social housing sector (although costs may have been higher and margins lower if the supplier was competing on price with a supplier located closer to the customer's properties).

11.113 As with the social housing sector,[241] we considered whether potential entry might be sufficient to constrain the merged company or whether actual entry would be required. We again thought that potential entry would be much less effective than actual entry in constraining prices. As with social housing, we thought there would be

[239] See paragraphs 10.86–10.89.
[240] See paragraph 10.99 above.
[241] See paragraph 10.93 above.

little incentive for the merged company to keep its prices low in case of entry, because it could lower them in response to entry instead.

11.114 As in the social housing sector, we found that acquiring SSVP stock (ie steel screens/doors and wireless alarms), a suitable workforce and transport in order to supply SSVP to commercial customers was straightforward and that access to these inputs did not constitute a barrier to entry.

11.115 The parties submitted evidence on the history of expansion in the sector. This included Camelot, Clearway, Loxal, MITIE and SitexOrbis. Camelot was not an SSVP supplier and Loxal was a new entrant aiming to expand in the commercial sector. We discuss MITIE in paragraph 11.137*(b)*. SitexOrbis had been successful in growing its commercial business from 2008 until the merger [✂] by leveraging its existing social housing infrastructure, and Clearway had been successful in growing its commercial business since 2004. Overall we assessed that there was more evidence of successful entry and expansion in the commercial sector than in the social housing sector.

11.116 We saw some evidence that customer inertia was a significant factor in the commercial market, but less than in the social housing sector. Our customer survey suggested that over half of commercial customers of VPS or SitexOrbis had used their current supplier for longer than three years.[242] The [✂] Report said that SitexOrbis's customer account churn rate was low, around 6 per cent a year. VPS provided us with some examples of commercial customers switching to rivals but did not provide evidence that this was widespread. We understood that few, if any, customers had contracts that tied them to a particular supplier and we were told that some customers used more than one supplier and were willing to try new suppliers by letting them handle one or two properties.

11.117 We repeated for the commercial market the analysis on depot expansion that we conducted for the social housing market. This is presented in Table 7.

TABLE 7 **Commercial depot expansion**

	Lower estimate	*Higher estimate*
Annual depot overhead (£'000)	[✂]	[✂]
% overhead covered by clean-and-clear services*	[✂]	[✂]
Overhead to cover from SSVP	[✂]	[✂]
Assumed gross margin (pre-labour, %)	[✂]	[✂]
Revenue required to cover overhead (£'000)	[✂]	[✂]
Average 2012 quartile 4 customer revenue (£'000)	[✂]	[✂]
Average 2012 quartile 3 customer revenue (£'000)	[✂]	[✂]
Average 2012 quartile 2 customer revenue (£'000)	[✂]	[✂]
Average 2012 quartile 1 customer revenue (£'000)	[✂]	[✂]
Number of quartile 4 customers to cover overhead	[✂]	[✂]
Number of quartile 3 customers to cover overhead	[✂]	[✂]
Number of quartile 2 customers to cover overhead	[✂]	[✂]
Number of quartile 1 customers to cover overhead	[✂]	[✂]

Source: VPS data, CC calculations.

*[✂]
Note: See the notes to Table 4 in paragraph 10.117. We thought these estimates were conservative since Clearway estimated that it would need £360,000 of revenue to cover the higher overhead estimate. The pre-labour margins of [✂] per cent reflected the [✂] in the commercial sector.

[242] DJS customer survey. 63 per cent of VPS customers and 64 per cent of SitexOrbis customers who responded had used their services for more than three years.

11.118 We considered that a number of differences between the social housing and commercial markets were relevant to our assessment of the likelihood of new depot expansion to serve the commercial market in that, compared with the social housing market, the commercial market had:

(a) less customer inertia;

(b) less tender activity (and entrants could win custom incrementally without the need to win large 'all-or-nothing' competitions);

(c) higher average revenues per job;

(d) higher margins;

(e) larger depot catchment areas within which to win new business; and

(f) more growth potential (so entrants could win new business rather than having to displace incumbents).

11.119 Taken together, we considered that these factors mean that it is more credible that a new entrant or expanding competitor in a particular region may be able to compete and win new customers, either through numerous smaller commercial jobs or a combination of some smaller and larger work within the operating radius of its depot.

11.120 Our view was that any expansion was most likely to occur first through the growth of commercial revenues within an existing depot catchment area with expansion into adjacent areas.

Economies of scale, density and scope

11.121 As in the social housing sector, we considered whether a company with a large network of depots would enjoy economies of scale, density and scope in the supply of SSVP which would hinder the likelihood of timely and sufficient entry or expansion. We considered potential advantages in economies of scale, density and scope at three levels for commercial customers:

(a) regional;

(b) national which will impact at a regional level; and

(c) national.

- *Regional*

11.122 We considered whether economies of scale, density and scope could provide an advantage at the regional level. As in social housing, a higher density of customers in a given area would reduce average costs of serving existing customers as well as the incremental cost of serving an additional customer in the area.

11.123 We considered that, for the same reasons as given in paragraphs 10.124 and 10.125, in regional areas where VPS and/or SitexOrbis were already present, their existing customer base provided them with some degree of economies of scale, density and scope.[243] As a consequence, the incremental cost of serving an additional customer in the area was likely to be relatively low for the main parties, and competitors not present in the area may have found it difficult to win sufficient business to match the economies of scale, density and scope enjoyed by the incumbents and therefore to expand profitably. We did not expect this to be a large advantage but it could affect suppliers' ability and incentives to serve customers in that area and the pricing that they were prepared to offer.

11.124 The ability of a new entrant into an area to match or compete with the merging parties' economies of scale, density and scope would be driven by the entrant's ability to win new business and effectively fill its network. For the reasons given in paragraph 11.145, we considered that it was likely to be easier for a new entrant or expanding competitor to supply regional commercial customers than it was for a new entrant or expanding competitor to supply social housing customers.

- *National which will impact at a regional level*

11.125 We considered whether national economies of scale, density and scope could provide an advantage at the regional level.

11.126 We found that, for the same reasons as given in paragraphs 10.128 to 10.130, in areas where VPS and/or SitexOrbis were not present, they may still have been able to benefit from depots in neighbouring areas. For example, by reassigning commercial and/or social housing customers from existing depots to new depots and adjusting the capacity of their depots, the main parties may have been able to take advantage of their larger network of depots and reduce the average costs of serving their customers. This option was not available to competitors who had a significantly smaller infrastructure than the merging parties. They would also be able to manage better their stocks of steel and other materials.

- *National*

11.127 We considered whether national economies of scale, density and scope could provide an advantage at the national level.

11.128 SitexOrbis told us that it had found that the competitive advantage was about having the infrastructure, where it could prove that it could deliver on a single pricing structure on a single invoice for customers, anywhere in the country. Clearway told us that having a network of depots was important to competition and this was where SitexOrbis and VPS had an advantage over it.

11.129 VPS said that '… you will find that a customer base will sometimes have sites all around the country, or they will have sites in multiple regions, in which case as we described, we will then service that particular property from a more local depot'. We inferred from this statement that VPS benefited from a network advantage in that it was able to service a customer's vacant properties in multiple regions from a network of local depots. Competitors with smaller networks of depots and with no depot in the local area would not have had this advantage.

[243] VPS said that the only significant barrier to entry and expansion that we had identified at the regional level was the parties' depot network and the consequent ability to reassign customer from existing depots to new depots (VPS & TDR response to CC provisional findings, paragraph 3.16). This was not the only barrier we identified. We also considered that even at a regional level the merged entity would benefit from economies of density and scope (between social housing and commercial customers), enabling them to serve new customers more efficiently than rivals who did not have the same volume of customers and who consequently had to make longer journeys on average.

11.130 As discussed in paragraphs 11.47 to 11.51 above, we considered that VPS and SitexOrbis's larger depot infrastructure was likely to mean that competitors with smaller networks were able to secure vacant properties spread across Great Britain at a higher cost than the merging parties. We considered that a company with a large number of depots around the country would have shorter average journey times than one with a few depots seeking to serve customers with a geographically spread estate (see Table 5). It would be able to serve more customers for a given level of fleet, labour and fuel or alternatively have lower costs per customer in these areas. Consequently, average costs would be lower and the incremental cost of serving an additional customer would also often be lower. We noted that at a depot level (ie excluding central overheads) for SitexOrbis just under [✄] per cent of total costs were labour and transport; so utilizing these costs efficiently was important (although a significant percentage of labour costs would relate to property inspection which VPS told us could be outsourced or delivered by workers from home who did not need to be attached to a depot).

- *Conclusion*

11.131 Taking the above into account, we considered that the merging parties had important advantages in relation to economies of scale, scope and density over other SSVP suppliers. We found that whilst there were no insurmountable obstacles to opening individual new depots, individual depots were unlikely to constitute a significant competitive constraint for customers with national requirements. We found that *(a)* the merging parties' customer base and large depot infrastructure constituted a barrier to expansion by other smaller SSVP suppliers and that *(b)* potential entrants from adjacent sectors would find it possible to overcome this barrier to entry if they could leverage off an existing depot network (eg as some large facilities management or security companies may have) but still would be at a disadvantage until they acquired an SSVP customer base of sufficient size.

Ability to enter or expand

11.132 We found various examples of entry into the supply of SSVP to the commercial sector. Clearway appeared to have had some success in expanding its business from primarily a property clearance business, and SitexOrbis had increased its revenues in the commercial sector in recent years since adopting a strategy that focused more on that sector. However, TDR submitted evidence from the annual reports of Orbis (ie the predecessor company to SitexOrbis) and submitted to us that [✄], and TDR stated that [✄]. This suggested that gaining scale in the commercial sector was not entirely straightforward even for a company with experience and reputation in the social housing sector, but could be achieved under some circumstances.

11.133 In its response to our provisional findings, VPS argued that this conclusion was inconsistent with the evidence that *(a)* Clearway had grown in the commercial sector and that *(b)* SitexOrbis had refocused its effort on the commercial sector only recently, and said that the key point was that a supplier could grow rapidly within the commercial sector with or without an extensive depot network if it had the appropriate strategy and management structure.[244] We did not perceive any inconsistency. On the first point, Clearway's own evidence was that the main challenge for it to expand and service larger commercial clients was that it would need a different management system. Therefore it had achieved some success but was not currently able to serve

[244] VPS & TDR response to CC provisional findings, paragraph 3.22.

the largest national customers. On the second point, the fact that SitexOrbis had in the past failed with its efforts to expand significantly in the commercial sector caused us to doubt the proposition that every supplier seeking to expand will be successful, but equally its more successful recent attempt indicated that it was possible.

Appetite for entry and expansion

11.134 We assessed appetite for expansion both from adjacent markets and by existing competitors.

11.135 We assessed that the appetite for expansion among existing competitors was notably higher in the commercial market than in the social housing market. A number of competitors told us that they aimed to grow and they thought there were higher margins and better prospects for growth in this sector.

11.136 We noted that there are a number of companies in adjacent markets which could potentially use their large UK infrastructure to enter and supply commercial customers with national SSVP requirements. A number of these companies also currently outsource the provision of SSVP within larger contracts to the main parties or one of their competitors. VPS/TDR told us that margins in SSVP [✄] to encourage entry and that these companies had deep pockets and customer relationships. These companies could potentially leverage their existing networks in order to compete with the merged parties. We spoke to a number of potential new entrants.[245]

11.137 VSG (part of the Compass Group), Morrison and Securitas told us that they currently outsourced SSVP services and were not considering self-supply. G4S and MITIE told us that they would consider entering the market:

(a) [✄] It said that it was reviewing the commercial market and not the social housing market.

(b) MITIE told us that it subcontracted SSVP to [✄], and to SPS in [✄]. It said that it did not have any plans to supply its own steel screens/doors for the next 12 to 18 months but it could potentially bring steel screens/doors in-house. We reviewed the MITIE Void Security Management business plan (the relevant division) which said that SSVP would be outsourced until April 2013 although it would also explore the potential of undertaking steeling services directly.

11.138 We assessed that G4S and MITIE would have a strong capability to compete with the merged parties in national commercial SSVP, if they chose to. They had adequate resources, large national networks (MITIE has [✄], G4S operates [✄]) and they already subcontracted these services. Since they were already customers of the merging parties, the possibility of self-supply, if considered credible by the merged company, may have helped to constrain post-merger pricing (since the merged company may not wish to increase prices to such intermediaries if it would encourage entry).

11.139 VPS submitted that, with respect to the regions where we had found an SLC, entry would become more attractive following the merger, even at current price levels,

[245] VPS/TDR told us that [✄], and in its response to our provisional findings, VPS referred to our hearing with MITIE and MITIE's statement that: 'MITIE's commercial void property security business said that it might now reassess its strategy with regards to self-supply in the commercial market as a result of the CC's provisional decision and the divestiture packages'. VPS said that this indicated that entry and expansion had already commenced. We disagreed with VPS that this was the correct conclusion to reach. MITIE told us that it had not changed its plans in this business and was still considering whether to self-supply SSVP.

because there would be less choice available to customers (since two suppliers had merged); and this would increase the opportunity for an entrant to pick up business without necessarily undercutting the incumbent's current prices, particularly from customers who valued choice or preferred to dual source (as a number of commercial customers did).[246]

11.140 We agreed that the merger may make entry more attractive. However, in the regions where we found an SLC, the choice of suppliers was already limited so these regions would already appear to be prime sites for entry or expansion, other things being equal. Yet recent and planned entry and expansion appeared to be focused in the regions of south-east and central England and the trans-Pennine area, all regions where a number of suppliers already existed. This suggested that when considering the likelihood of entry or expansion into a region, the reduction in the number of suppliers caused by the merger would be less important than other factors such as the volume of customers and the ability to build a network of depots in adjacent regions. Therefore we did not find this argument compelling for the regions where we found an SLC, in the absence of other corroborative evidence.

Our assessment of entry and expansion in the commercial sector

11.141 Based on the evidence above, and in line with the Guidelines, we considered entry and expansion under the following framework:

(a) whether entry or expansion was likely (whether firms had the ability and incentive to enter the market, or the intent to do so—see the Guidelines, paragraph 5.8.8);

(b) if it was likely, could it occur soon (usually within less than two years—see the Guidelines, paragraph 5.8.11); and

(c) if it did occur, would it be likely to occur on a sufficient scale to constrain the merged parties.

11.142 We assess entry/expansion first for commercial customers with regional SSVP requirements and then for commercial customers with national SSVP requirements.

Regional demand from commercial customers

11.143 We assessed whether expansion at a regional level would be likely, timely and sufficient to constrain the merged parties. Of specialist SSVP suppliers which we spoke to, SPS told us that it did not have any plans to open any new depots. However, some suppliers did say that they were considering possible expansion:

(a) Clearway indicated that it might possibly open new depots in the future (in the North-West and the Midlands);

(b) [✂] told us that it was looking at opening an additional depot in Yorkshire;

(c) SecureSite told us that it was planning to open a new depot in the Midlands and was also considering opening a new depot in the North of England at some point;

(d) Veritas told us that it was keen to expand and had begun pro-actively to market itself more.

[246] VPS & TDR response to CC provisional findings, paragraphs 3.29–3.34.

11.144 We assessed that the key to entry and expansion for a new entrant or existing business was building sufficient scale in a timely manner in order to match the advantages of scale, scope and density which the merging parties had.

11.145 We assessed that there were a number of reasons why an entrant into the regional commercial market may find it easier to expand and win new business than a new entrant into the social housing market. Notably, customers could be serviced from greater distances, meaning that there was an ability to win and profitably service work much further from a depot. Tenders were much less prevalent in the commercial market which should make entry easier and we were also told that there was less customer inertia.

11.146 Taking these factors together, our view was that a new entrant or expanding competitor in the regional commercial market had greater opportunities to win customers in a wider area and therefore become profitable more quickly and with less risk.

11.147 VPS submitted that an entrant could set up a single depot that would service more than one of the areas where we had found an SLC. For example, South Wales and the South-West could be covered from a single depot located near Bristol.[247] We considered that this was possible, but did not greatly affect our analysis since our concern was whether relevant entry in such a location was likely and we have seen no evidence that it was.

11.148 VPS said that removing our concerns in these areas would not require any new entry, but only that an existing competitor establish a base which covered these areas within one to two years. It said that 'Given the geography of the region, and the existence of a number of credible competitors today, this requirement will easily be met'.[248] VPS also said that if prices increased to commercial customers in the North-East and Scotland it 'does not seem plausible … that competitors will not rapidly expand into these areas'.[249] We noted that we were concerned by the identity of competitors and not just the number of them, and so expansion by a single competitor may not be sufficient to restore the competitive constraint provided by SitexOrbis if it was a less close competitor to VPS.

11.149 The evidence of possible expansion that we saw (see paragraph 11.143) suggested that expansion was most likely to be seen in areas adjacent to existing competitors' depots and/or in areas where there was a density of commercial opportunities. We therefore assessed that in some areas expansion would be likely, timely and sufficient to constrain the merged parties (if they were not already constrained). In the SLC areas,[250] however, whilst we did not rule out the possibility that entry or expansion may occur, we saw no evidence that new entry would be likely. Indeed, none of the competitors we spoke to indicated any plans to open new depots in any of the SLC areas. Further, the SLC areas were not adjacent to existing competitors' depots and it may be difficult for new entrants to secure a sufficient toehold to justify the investment required to open a new depot (even if a single depot were able to serve effectively two areas). Accordingly, we found that in the case of each of the SLCs we identified in these parts of the country, the balance of evidence was such that we could not form an expectation that either entry or expansion was likely to occur so as to defeat the SLCs in these parts of the country.

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[247] VPS & TDR response to CC provisional findings, paragraph 3.40.
[248] VPS & TDR response to CC provisional findings, paragraph 3.41.
[249] VPS & TDR response to CC provisional findings, paragraph 3.38.
[250] Namely south-west and north-east England, Scotland and South Wales—see paragraph 11.93.

National demand from commercial customers

11.150 We assessed that a company with a large number of depots, such as VPS and SitexOrbis, would enjoy economies of scale, density and scope that would result in a cost advantage compared with a competitor with only a small number of depots.

11.151 Consequently, a new entrant or an existing supplier of SSVP seeking to expand in the national commercial sector would find it difficult to compete effectively with the merged entity unless it acquired or already had access to a significant number of depots spread around the UK.

11.152 Entry at sufficient scale to serve nationwide customers was likely to be difficult. We consider that it would be necessary to have at least two, and possibly four, depots in order to be able to serve the majority of Great Britain, and we expected that new entry would initially take place at a regional level with the possibility of subsequent expansion. The existence of economies of scale suggested that some potential competitors may not be able to act as an effective constraint at a national level. Creating from scratch or expanding from a low base a national network of depots equivalent to that of the merged entity would expose a rival to very significant costs and risks, and for this reason we consider it unlikely that this would happen. We therefore assessed entry and expansion into the national commercial market by existing competitors or new entrants (not including businesses in adjacent sectors which are discussed in paragraph 11.153) as not likely to be timely or sufficient.

11.153 We considered it plausible that a company operating in an adjacent market area, for example property security or property repair and maintenance/facilities management, could leverage its existing branch/depot assets to enable it to compete effectively with the merged entity (including realizing similar economies of scale given time, if they chose to enter on a large scale). However, we found that the evidence we reviewed indicated that new entry was either not likely[251] or, if a company was considering entry,[252] its planning was insufficiently developed such that we could not reasonably form an expectation that entry would occur so as to defeat the SLCs we identified in the supply of SSVP to commercial customers at the regional and national levels. Even if such entry were to occur within a two-year period, we considered that entry would initially be at a sub-national level and that it would take time for any new entrant to attract customers and grow scale to a point where it could attain low costs and restore the level of pre-merger competition with the merged company.

Findings: commercial sector

National level

11.154 We found that the merging parties faced limited competition for customers with nationwide SSVP requirements pre-merger, and a number of factors suggested that they were likely to be each other’s closest competitors, with other existing competitors providing a weaker competitive constraint. This was reinforced by our finding that they were individually and jointly likely to have a significant cost advantage over other existing suppliers.

11.155 While we consider that new entry into the sector by large companies in adjacent sectors was possible, we expected that this would be on a regional or contract by contract basis initially and hence we found that it was more likely than not that there

[251] See for instance, VSG, Morrison and Securitas.
[252] See for instance G4S and MITIE.

would be no significant new entry into the supply of nationwide customers within the next two years such as to constrain effectively the merged parties.

11.156 We considered that, to the extent that there was buyer power pre-merger, much of it derived from the competition between the merging parties (which were large companies that could serve most customers, or from the existence of intermediaries which could be supplied by those two large companies), and so this buyer power would be diminished significantly post-merger; and buyer power for some customers was unlikely to protect all customers. We saw no evidence that there were likely to be significant relevant efficiencies arising from the merger.

11.157 Accordingly, we found that the merger may be expected to result in an SLC in the supply of SSVP to commercial customers with national SSVP requirements.

Regional level

11.158 We found that the supply of SSVP is highly concentrated, and the merged company would have a large share of supply. Absent entry, there would be relatively few other suppliers post-merger. However, there was some evidence to suggest that other suppliers may be credible competitors for commercial customers with regional requirements in areas relatively close to their depots (within 70 to 100 miles). Hence we found that there was likely to be sufficient competition in most of England and some of Wales to prevent an SLC and defeat a price rise for customers with regional requirements.

11.159 However, we considered that the merged company would have the incentive and ability to increase prices in some parts of Great Britain (namely in Scotland, South Wales, south-west and north-east England), areas in which the merged entity would face at most one competitor post-merger. In these areas, whilst we found that entry and/or expansion may occur, we saw no evidence that entry and/or expansion is likely to occur in these areas so as to prevent an SLC and defeat a price rise for customers with regional requirements.

11.160 Our analysis in paragraph 11.156 in relation to other possible countervailing factors (ie buyer power and any relevant efficiencies) applies equally to our assessment here.

11.161 Accordingly, we found that there was an SLC in relation to the supply of SSVP to commercial customers in the following parts of Great Britain: Scotland, South Wales, south-west England and north-east England.

Northern Ireland

11.162 For the reasons given in paragraph 11.101, we found that the merger may not be expected to result in an SLC for commercial customers in Northern Ireland.

12. Findings

12.1 For the reasons given above, we found that the merger may be expected to result in an SLC leading to prices for SSVP being higher than the pre-merger level:

(a) to social housing customers across Great Britain; and

(b) to commercial customers in some parts of Great Britain (namely, in Scotland, South Wales, south-west England and north-east England); and

(c) to commercial customers with national SSVP requirements.

12.2 For the reasons given above, we found that the merger may not be expected to result in an SLC in the supply of SSVP in Northern Ireland.

13. Remedies

Introduction

13.1 In this section, we consider remedies to the SLC and resultant adverse effects summarized in Section 12.

13.2 Under section 35 of the Act and having found an SLC, the CC needs to decide on the following questions regarding remedial action:

(a) Should the CC itself take action for the purpose of remedying, mitigating or preventing the SLC or any adverse effects resulting or expected to result from the SLC?

(b) Should the CC recommend the taking of action by others for the purpose of remedying, mitigating or preventing the SLC or adverse effects resulting or expected to result from the SLC?[253]

(c) In either case, if action should be taken, what action should be taken and what is to be remedied, mitigated or prevented?

13.3 The Act requires that the CC when considering possible remedial actions shall 'in particular, have regard to the need to achieve as comprehensive a solution as is reasonable and practicable to the substantial lessening of competition and any adverse effects resulting from it'.[254] To fulfil this requirement, the CC will seek remedies that are effective in addressing the SLC and its resulting adverse effects and will then select the least costly and intrusive remedy that it considers to be effective. The CC will also seek to ensure that no remedy is disproportionate to the SLC or its adverse effects. The CC may also have regard to any relevant customer benefits arising from the merger.[255]

13.4 Remedies are conventionally classified as either structural or behavioural. Structural remedies, such as divestiture or prohibition, are generally one-off measures that seek to restore or maintain the competitive structure of the market through a direct change in market structure. Behavioural remedies are measures that are designed to regulate or constrain the behaviour of merger parties with the aim of restoring the conditions of competition that would have been present absent the transaction. Behavioural remedies are generally subject to higher risks than structural remedies and are therefore less likely to be effective and/or proportionate solutions to an SLC in a merger inquiry.[256]

13.5 In our Notice of Possible Remedies (the Remedies Notice) published on 25 June 2012 we invited views on three different structural remedies, namely the divestiture of:

[253] In this inquiry, it has not been necessary to recommend the taking of action by others.
[254] Section 35(4).
[255] Section 35(5).
[256] *CC8—Merger Remedies: Competition Commission Guidelines* (the Merger Remedies Guidelines), November 2008, paragraphs 2.14 & 2.15.

(a) the UK business and assets of SitexOrbis (SitexOrbis UK);

(b) the Great Britain business and assets of SitexOrbis (SitexOrbis GB); and

(c) a package of assets less than SitexOrbis GB.

13.6 In response to the Remedies Notice and in response to a remedies working paper, TDR/VPS proposed three alternative divestiture options and a behavioural remedy in which VPS would provide access to its depots and steel stocks to third party suppliers. No other remedies were proposed.

13.7 We have considered all these remedy options. We tested our views about possible remedies with TDR/VPS and SitexOrbis, and with third parties.

13.8 The remainder of this section is structured as follows:

(a) in paragraphs 13.9 to 13.18, we outline the remedy options that we have considered;

(b) in paragraphs 13.21 to 13.113, we evaluate the effectiveness of these remedy options;

(c) in paragraphs 13.114 to 13.120, we set out our assessment of the proportionality of those remedies that we have found to be effective;

(d) in paragraphs 13.121 to 13.124, we set out our assessment in relation to relevant customer benefits;

(e) in paragraphs 13.125 to 13.143, we set out how we will implement our preferred remedy; and

(f) in paragraphs 13.144 to 13.146, we summarize our decision on remedies.

Outline of possible remedy options

13.9 In paragraphs 13.9 to 13.18, we outline the remedy options that we have considered:

(a) divestiture of SitexOrbis UK;

(b) divestiture of SitexOrbis GB;

(c) mix and match divestitures proposed by TDR/VPS; and

(d) a behavioural remedy proposed by TDR/VPS.

13.10 We considered whether each divestiture package (that is, those outlined in sub-paragraphs *(a)*, *(b)* and *(c)* above) should also include the SitexOrbis insurance business based in Guernsey, Sitex Insurance PCC Limited. SitexOrbis told us that this was not a subsidiary of SitexOrbis but was a subsidiary of Insite Facility Services Limited and was an important part of the UK operation. It said that it was used to write certain insurance products for its UK customers and that this business only had operational interaction with the UK and not with any of the Continental European businesses of SitexOrbis. [✂] We concluded that the Guernsey business should form part of any divestiture package (and we have therefore added the underwriting profit it generated to the profit figures for each divestiture package in Table 8 below).

Divestiture of SitexOrbis UK

13.11 This divestiture option is the SitexOrbis UK business and assets, which comprises the brand name of SitexOrbis and all the business and assets that currently reside in the SitexOrbis business that is being held separate under the terms of the initial undertakings adopted by the CC on 9 March 2012.

Divestiture of SitexOrbis GB

13.12 This divestiture option is SitexOrbis UK (see paragraph 13.11) excluding the business and assets of the SitexOrbis 'business unit' in Northern Ireland (which consists of one depot in Belfast) which would be transferred to VPS. TDR/VPS told us that this business unit would comprise: [✂].[257,258]

13.13 [✂][259]

Mix and match divestitures proposed by TDR/VPS

13.14 TDR/VPS proposed three 'mix and match' divestiture options each based on SitexOrbis UK (see paragraph 13.11) as the starting point with the Northern Ireland business unit excluded followed by some further 'business unit' 'swaps':

(a) 'Option 1', [✂].

(b) 'Option 2', [✂].

(c) An additional option proposed in response to the remedies working paper, [✂].

13.15 In each case the 'business units' being transferred in and out were to comprise the equivalent assets to the Northern Ireland business unit (see paragraph 13.12).

13.16 [✂][260]

Behavioural remedy proposed by TDR/VPS

13.17 TDR submitted a behavioural remedy in which VPS would undertake to offer one or more third party suppliers (the Competitor) active in SSVP services in the UK the opportunity to share the use of its depots and steel stocks. It said it would do so on the following terms: [✂].

13.18 [✂][261]

Our assessment of the effectiveness of remedy options

13.19 In paragraphs 13.21 to 13.108, we consider the structural remedy options before considering TDR/VPS's behavioural remedy proposal in paragraphs 13.109 to 13.112.

[257] These are SitexOrbis alarms. They are discussed further in paragraph 13.70.
[258] TDR response to the Remedies Notice, paragraph 4.81.
[259] TDR response to the Remedies Notice, paragraph 4.82.
[260] TDR response to the Remedies Notice, paragraph 4.82.
[261] TDR response to the Remedies Notice, paragraph 4.99.

13.20 Before we consider each of the structural remedies, we set out our framework for assessing the divestiture options, TDR/VPS's general views on the scope of a structural remedy and how we have assessed the effectiveness of each divestiture option.

Framework in the Merger Remedies Guidelines for assessing structural remedies

13.21 When assessing structural remedies, the CC takes a risk-based approach. The Merger Remedies Guidelines set out three categories of risk that the CC considers:[262]

(a) Composition risks: these are risks that the scope of the package may be too constrained or not appropriately configured to attract a suitable purchaser or may not allow a purchaser to operate as an effective competitor in the market.

(b) Purchaser risks: these are risks that a suitable purchaser is not available or that the merger parties will dispose to a weak or otherwise inappropriate purchaser.

(c) Asset risks: these are risks that the competitive capability of a divestiture package will deteriorate before completion of the divestiture, for example through loss of customers or key members of staff.

13.22 The Merger Remedies Guidelines state that 'in identifying a divestiture package, the CC will take, as its starting point, divestiture of all or part of the acquired business. This is because restoration of the pre-merger situation in the markets subject to an SLC will generally represent a straightforward remedy'.[263]

13.23 When considering a divestiture package the Merger Remedies Guidelines state:

> The CC will generally prefer divestiture of an existing business that can compete effectively on a stand-alone basis independently of the merger parties, to divestiture of part of a business or a collection of assets. This is because divestiture of a complete business is less likely to be subject to purchaser and composition risk and can generally be achieved with greater speed.[264, 265]

13.24 In general the CC has a preference for avoiding 'mix and match' divestitures as they may create additional composition risks such that the divestiture package will not function effectively.[266] The Merger Remedies Guidelines state that 'it will normally be preferable for all the assets to be provided by one of the merger parties unless it can be demonstrated ... that there is no significant increase in risk from a mix and match alternative'.[267]

[262] *CC8*, paragraph 3.3.
[263] *CC8*, paragraph 3.6.
[264] *CC8*, paragraph 3.9.
[265] In *SRCL v Competition Commission* [2012] CAT 14, the CAT observed (paragraph 32) that 'the CC was entitled to examine any proposed package falling short of full divestment with great care'. The Tribunal also noted that it was for the CC to decide whether factors in that case were important enough to justify the more intrusive remedy and that the CC's decision as to the preferred remedy was a decision which could only be disturbed on judicial review grounds if there was clear evidence of irrationality or unreasonableness on the part of the CC (paragraph 33).
[266] *CC8*, paragraph 3.12.
[267] *CC8*, paragraph 3.12.

General views of VPS and TDR on scope of a structural remedy

13.25 VPS and TDR told us that they believed there were divestiture options of less than SitexOrbis GB that would be effective in addressing the SLCs and which would not entail the composition, purchaser and asset risks identified in the Remedies Notice. Specifically TDR/VPS put to us the ‘mix and match’ options described in paragraph 13.14.

13.26 TDR and VPS told us that the CC/OFT had on a number of occasions approved ‘mix and match’ remedies in industries with similar characteristics to SSVP. It specifically cited the examples of Morrisons/Safeway, The Co-operative/Morrisons and Jewson/Build Centre.

13.27 TDR and VPS told us that any of the divestment options would result in a more attractive, financially stable and competitive business than the SitexOrbis business pre-merger. The reasons for this were that SitexOrbis would no longer be required to service a significant debt burden, there was an opportunity for a purchaser to make significant central overhead cost savings and cash flow would be improved.[268] [✂]

13.28 [✂]

How we have assessed the effectiveness of each divestiture option

13.29 We used as our starting point divestiture of the acquired business, SitexOrbis UK, as this represents the restoration of the *status quo ante* and is the most straightforward remedy.[269] Consistent with the Merger Remedies Guidelines, we have assessed the effectiveness of each divestiture option both relative to this divestiture (in terms of whether it leads to a significant increase in risk) and on its own merits by considering first whether it is capable of addressing the SLCs in principle (ie on the assumption that the divested business would be viable), and second what composition, purchaser and asset risks it creates (to determine whether it would in fact be likely to be viable).[270] The assessment is structured as follows:

(a) We first explain what we mean by composition risk and then set out a quantitative summary of the divestiture packages as well as an assessment of capital expenditure and central overheads. We refer back to this assessment when we consider each divestiture package separately.

(b) We then explain what we mean by purchaser risk and asset risk.

(c) Finally we set out, for each divestiture package, whether we consider that it is effective, considering (i) whether it addresses the SLCs in principle; (ii) composition risk (referring back to the quantitative assessment); (iii) purchaser risk; and (iv) asset risk.

Composition risks

13.30 In considering composition risks we have examined whether each divestiture option is capable of being operated as an effective competitor in the areas where we have found SLCs. This requires the divested business to be able to compete effectively both immediately upon acquisition by a purchaser and over time. In assessing the

[268] TDR/VPS response to the Remedies Notice, paragraphs 3.3–3.8.
[269] *CC8*, paragraph 3.6.
[270] *CC8*, paragraph 3.12.

effectiveness of the competitive constraint imposed by the proposed divestment packages, we have considered the nature of the constraint imposed by SitexOrbis on VPS pre-merger. The divested business needs to be an effective competitor to address both static and dynamic aspects of the loss of competition that we have identified. Underpinning this assessment are both qualitative and quantitative considerations. Qualitative assessments relate to whether the scope of the divestiture package 'works' in practice. Quantitative assessments consider whether each divestiture package would leave sufficient financial headroom in the divested business for it to be effective.

- *Quantitative assessment of divestiture options*

13.31 Our quantitative assessment focuses on EBITDA as a starting point. EBITDA will need to be at a level to provide sufficient headroom to cover the cash requirements of the business, which may include: (i) relevant ongoing capital expenditure and working capital requirements, (ii) any interest payments (to the extent these are relevant, if the business is to be financed through debt),[271] (iii) taxation, (iv) working capital requirements and (v) any one-off exceptional items such as restructuring. As performance of the business will vary over time we would expect the divestiture package to have reasonable financial headroom to avoid significantly increasing the risk that it would not be effective.

13.32 In Table 8 we set out the summary EBITDA of each package for FY11, FY12 and the last 12 months' trading to June 2012 (LTM). This gives a measure of profitability before potential central overhead cost savings and capital expenditure requirements are taken into account (see paragraphs 13.40 to 13.46 below).

TABLE 8 **EBITDA of the four divestiture options**

			£ million
	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	
[✂]	[✂]	[✂]	
[✂]	[✂]	[✂]	
[✂]	[✂]	[✂]	
[✂]	[✂]	[✂]	
[✂]	[✂]	[✂]	
[✂]	[✂]	[✂]	[✂]†
[✂]	[✂]	[✂]	
[✂]	[✂]	[✂]	
[✂]	[✂]	[✂]	[✂]†
[✂]	[✂]	[✂]	
[✂]	[✂]	[✂]	
[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]†

Source: SitexOrbis/VPS

*Central overhead includes all central overhead relating to SitexOrbis. This includes some elements which are applicable to the European business which will remain under the ownership of VPS (see paragraph 13.43).
†Clearwater (TDR's advisers) estimate.
Note: Figures may not sum due to rounding.

13.33 TDR told us it believed that the CC's assessment of SitexOrbis's viability in the remedies working paper was based on historical and misleading financial information and was unnecessarily conservative. TDR told us that a purchaser would be likely to rely upon LTM figures and also on run-rate profitability (by 'run-rate', that is: assuming the most recent 3-month period is replicated for the next 9 months to give a full

[271] [✂]

year trading result). TDR said that this was particularly important given the recent improvement in profitability of the SitexOrbis UK business.

13.34 Throughout our analysis of divestiture packages we have used FY11 and FY12 financial figures and we have placed more emphasis on the more recent of these two financial years. By using FY12 figures we have followed a conservative approach. We also considered that there was merit in using LTM figures because they show the most recent 12-month trading performance and we have considered these figures along with FY12 in our assessment. The figures are shown in Table 8.

13.35 However, we were sceptical about the use of annualized trading performance based on three months trading. Our concern is not whether a purchaser would use three-month annualized figures as part of any investment appraisal, but rather whether the divested business will be a viable and effective competitor. Using the most recent three-month period may not be representative of the trading performance which could be expected in the medium term and it is more appropriate for the purposes of assessing viability of the divestiture package to consider a period of 12 months, which captures likely variability in profitability within a year. We observed that there was significant variability in monthly trading performances—a range of at least £[✂] a month (excluding exceptional months—see Appendix H). If this variation is annualized over a year, this could lead to a margin of error in excess of £[✂]. Furthermore, [✂]. For these reasons, we considered that using three-month annualized figures to assess the divested business's financial headroom would carry significant risk of overestimating the profitability of the divestiture packages.

13.36 We also noted that TDR and Clearwater (sell-side advisers to TDR) referred us to forecast figures for SitexOrbis for FY13. We have not relied on FY13 figures in reaching our judgement as there are only three months of actual trading data available and any forecasts are too uncertain to reach a judgement on likely viability of a divestiture package.

13.37 We have considered carefully TDR's and VPS's argument in paragraph 13.27 that any of the divestment options would result in a more attractive, financially stable and competitive business than SitexOrbis UK pre-merger.

- *Elimination of debt*

13.38 First, we considered the elimination of debt following VPS's acquisition of SitexOrbis and the effect this has had on cash flow. The SitexOrbis group (ie including the Continental European operations) carried a reasonably high amount of leverage pre-merger which has subsequently been repaid by VPS as part of the acquisition process. However, the business was also larger (in sales and profits) than all of the divestiture options we are considering. Prior to acquisition SitexOrbis group was making around £4 million of EBITDA at group level, its cash flow was positive in aggregate over FY09–FY11 and the financial structure of the business prior to acquisition did not prevent SitexOrbis from being an effective competitor (see Section 6).

13.39 Our assessment of whether the divestiture package is an effective remedy focuses on whether the proposed divestiture package creates a viable and effective competitor capable of addressing the SLCs. Although we recognize that the SitexOrbis UK business is now likely to be free from any material third party debt (assuming it is purchased without debt financing), we are primarily interested in whether the cash flows the divested business (however comprised) is able to generate from its EBITDA are sufficient to enable it to be an effective competitor. It is important to have sufficient headroom to allow a margin for error and reduce the risk that the business will not be self funding. The financial structure of the business affects the extent to which these cash flows are needed to cover interest payments. The focus of our quantitative assessment at this stage is primarily on what range of EBITDA the packages are likely to generate in order to cover ongoing capital expenditure and other cash requirements (see paragraph 13.31). We note that the cash-flows of the business would need to be greater if the business were funded at least in part by debt.

- *Capital expenditure requirements*

13.40 Second, we considered the likely capital expenditure requirements of the divestiture packages. TDR said that the CC's estimated capital expenditures were too high. It told us that once infrastructure was set up, which SitexOrbis already had, vast levels of capital expenditure were not required to compete. It said that capital expenditures as part of daily business were not significant. It told us that capital expenditure could run at a level significantly below depreciation because many of the capital items lasted significantly longer than the time they were depreciated over. For example, steel screens lasted up to 20 years and were depreciated over a much shorter period. TDR also told us that it believed capital expenditure was fully variable with sales in the long term and therefore any estimate for the proposed packages needed to adjust for the reduced level of sales. Clearwater also prepared an estimate of how capital expenditure could be varied with sales in the short term. [✂]

13.41 The SitexOrbis UK business made capital expenditures of between £[✂] million and £[✂] million a year over the period FY08–FY12 and the original budget for FY13 was £[✂] million (which was subsequently revised down to £[✂] million). SitexOrbis told us that a good estimate for capital expenditure in a normal year was £[✂] million. It said that a drop in sales would not reduce the capital expenditure budget much as a significant amount of the budget related to replacing outdated alarm stocks. We were told that the larger expenditures over the period FY08 to FY12 included a number of one-off items related to building the SitexOrbis commercial business and the Alarm Response Centre.

13.42 Using the downward revised SitexOrbis budget for FY13 and fully adjusting any sales reduction of proposed packages gives an estimate of capital expenditure of £[✂] million. This is the lowest estimate for capital expenditure in all scenarios. Using SitexOrbis's own estimates of its ongoing capital expenditure requirements provided to us (which it said would not vary without a significant reduction in sales) would give an estimate of £[✂] million. Given this variation in views and accepting that capital expenditure on alarms might be capable of being reduced to some extent due to a lower revenue base, we judge that a range of £[✂] million to £[✂] million is a reasonable estimate of the capital expenditure requirements of the packages, with a central estimate of £[✂] million, between the TDR and SitexOrbis figures. The top end of our range allows for some small additional projects (up to £[✂] over SitexOrbis's own estimates) which, based on the capital expenditure profile over the past few years, one might expect to occur as SitexOrbis continues to compete with VPS.

- *Potential reductions in central overheads*

13.43 Third, we considered TDR's and VPS's statement that there was an opportunity to reduce central overheads in the SitexOrbis business. TDR said that cost savings were always analysed by potential buyers. Part of the central overhead for SitexOrbis UK relates to supporting a pan-European rather than a UK business. In total for FY12 the total central overhead was £[✂] million (FY11: £[✂] million). £[✂] million of this overhead related to the UK only and £[✂] million related to operating companies in both Continental Europe and the UK. We were told by TDR and SitexOrbis that central overhead cost savings were achievable:

(a) SitexOrbis told us that significant cost savings ([✂]) might be achievable if SitexOrbis were to focus just on social housing. It said that a full strategic review would be necessary before it was possible to quantify these savings. It also said that it was not easy to identify savings from the overhead costs of FY12. [✂]

(b) TDR told us that substantial cost savings of £[✂] were possible. This would represent approximately [✂] per cent of the current central overhead. Clearwater prepared two 'teaser' documents designed to promote interest in two of the divestiture options. [✂]

(c) TDR told us that it believed the Clearwater approach of varying central costs [✂] per cent with sales (ie a [✂] per cent fall in sales leads to a [✂] per cent fall in central costs) was correct as these costs were variable in the medium term and this would be the approach a buyer would take (in addition to a detailed analysis of branch and group overheads). However, it also prepared an alternative approach based on which central costs could be varied in the short term, which it told us was over a two to three month period ('partial cost savings'). This analysis showed that for a 10 per cent fall in sales central costs alone (ie excluding branch overheads and group overheads) could be reduced by approximately [✂] per cent.

13.44 We considered TDR's areas of proposed cost savings in detail. We did not accept TDR's view that central overhead costs would vary in a [✂] ratio with any reduction in revenue. As TDR itself noted, many of these costs have elements that are fixed, at least in the medium term (for example, buildings and utilities costs, IT costs). Therefore we did not consider it appropriate to assume that such costs would be capable of being reduced as a result of a reduced revenue base—any such reduction would be highly uncertain.

13.45 We therefore considered TDR's partial cost savings approach (see paragraph 13.43*(c)*) which took into account that some costs would not be variable in the short term. We considered this was a more realistic approach than the [✂] cost savings approach (see paragraph 13.44) and examined the specific cost savings proposed by TDR. We noted that around [✂] per cent of the proposed central cost savings were from [✂] with a further [✂] per cent from [✂] and we considered the likelihood of these cost savings being realized:[272]

(a) [✂] We were concerned that reducing [✂] may make SitexOrbis a less effective competitor.

(b) The largest single cost line within [✂]. We were concerned that this area may already be under-resourced (see paragraph 13.43) as [✂] and SitexOrbis has been [✂].[273] We were concerned that further reducing [✂] in an area in which SitexOrbis may be currently under-resourced could reduce the effectiveness of a divestiture. The evidence suggests that this may be an area which requires investment rather than cost savings. Further, the fall in revenue for the proposed packages occurs mainly from the smaller scale of provision of services to social housing customers under those packages; so it is unclear why a reduction in social housing revenue would lead to a reduction in the size of [✂]. Any reduc-

[272] The remaining cost savings included Office Admin and Cars & Travel.
[273] We note that several of the ten account managers would be allocated at a branch level. Of the required new hires none were employed in the three-month period to June 2012.

tion in [✂] resources also suggests a change to the existing SitexOrbis approach of trying to expand in this area.

(c) Other significant areas in which central costs were proposed to be reduced in line with sales included [✂]. We agree some savings may be possible in these areas but considered it uncertain whether or to what extent demand for areas such as [✂] would vary with sales. We viewed any relationship between sales and these central overhead functions as uncertain and unlikely to be as easily realizable as TDR suggested.

13.46 We viewed any potential central overhead savings as highly uncertain. They would be purchaser-dependent and may not necessarily be realizable in the short to medium term. Assessing these cost savings would require a strategic review of the business. In any case the sort of cost reductions proposed by TDR would be likely to lead to the divested business being a smaller competitor which, in particular, was scaled back in its commercial market expansion plans and therefore a less effective competitor to VPS than SitexOrbis is currently. Trying to achieve such cost savings would also absorb significant management time, which would detract from running the business. If cost savings involved redundancies or changes to IT systems, for example, there would also be one-off costs (although we acknowledged that these could become part of the purchase price negotiations). As a result, when considering each divestiture package we have not assigned a specific central overhead cost saving amount. However, we recognize that some cost savings are likely to be possible (especially given some of the central overheads relate to the European business which will remain under the ownership of VPS) and we considered how the partial central cost saving assumptions made by TDR (described in paragraphs 13.43 and 13.44) may affect our assessment of the proposed packages.

Purchaser risks

13.47 In considering purchaser risks we have examined the likely interest in an effective divestiture package and the likelihood of a suitable purchaser being found.

Asset risks

13.48 In considering asset risks we have assessed whether any carve-outs of SitexOrbis ‘business units’ would create risks as compared with the competitiveness of the SitexOrbis UK business before completion of divestiture.

13.49 We now consider the effectiveness of each of the divestiture packages, described in paragraph 13.5, in line with this framework.

Divestiture of SitexOrbis UK

13.50 In this section we consider the effectiveness of a divestiture of the UK business and assets of SitexOrbis UK.

Addressing the SLCs

13.51 A successful divestiture of SitexOrbis UK would address the SLCs by reinstating the rivalry that existed prior to the merger in all areas in which an SLC has been identified.

Composition risk

13.52 Under the terms of the initial undertakings adopted by the CC, the UK business and assets of SitexOrbis have been held separate. As this divestiture involves no change in the structure of the UK business, in our view this business is able to operate as a stand-alone business.

13.53 We considered the viability of this divestiture package. Based on the EBITDA of £[✂] million in FY12 from Table 8 and the likely capital expenditure requirements of the business (paragraphs 13.40 to 13.42), we found that:

(a) SitexOrbis UK is profitable at an EBITDA level.

(b) There is sufficient EBITDA to cover likely ongoing capital expenditure requirements [✂] with reasonable financial headroom which should allow the business to be an effective competitor.

(c) We would expect it to generate cash for an owner, provided that the financing structure was not excessively leveraged.

(d) SitexOrbis UK is likely to be viable as a stand-alone business.

Purchaser risk

13.54 In relation to the original sales process run by E&Y, SitexOrbis told us that:

(a) private equity buyers were more interested than trade buyers;

(b) many buyers were put off by the pan-European nature of the business; and

(c) UK private equity firms were only really interested in SitexOrbis UK.

13.55 We could therefore expect a similar level of interest in the SitexOrbis UK business from private equity firms given it would not be complicated by the Continental European business. TDR told us it had received a significant amount of interest in the assets of the SitexOrbis business. This was primarily from [✂] it said it would expect the interest to be significant and not significantly less than the interest in the other divestiture packages it had market tested.

13.56 Based on the views of third parties we would expect interest from private equity firms and some trade buyers: [✂].

13.57 On the basis of the evidence from the previous sales process, third party views and TDR's feedback on its market testing, we believe that it is likely that a suitable purchaser would be available for the SitexOrbis UK business.

Asset risk

13.58 Under the terms of the initial undertakings adopted by the CC, the UK business and assets of SitexOrbis have been held separate with a monitoring trustee in place. This means that there is limited asset risk from this divestiture as the assets would continue as they are currently configured. Although there remains a risk with regard to retention of customers and key staff throughout the divestiture process, this risk applies to all the divestiture packages we are considering. This risk can be mitigated by setting an appropriate divestiture period, which we consider in paragraphs 13.136 to 13.142.

Conclusion on effectiveness

13.59 Based on the analysis in paragraphs 13.51 to 13.58, we conclude that this divestiture option would be effective in addressing the SLCs which we have identified. We judge that it carries low composition, purchaser and asset risk. It is also likely to be practicable to implement.

Divestiture of SitexOrbis GB

13.60 In this section we consider the effectiveness of a divestiture of the GB business and assets of SitexOrbis (ie SitexOrbis UK excluding the business and assets of SitexOrbis in Northern Ireland).

Addressing the SLCs

13.61 Provided that the divested business is viable, a successful divestiture of SitexOrbis GB would address the SLCs by reinstating the rivalry that existed prior to the merger in all areas in which SLCs have been identified. As we did not identify a competition problem in relation to Northern Ireland, the exclusion of these business and assets from the divestiture package does not affect its ability in principle to address the SLCs.

Composition risk

13.62 Table 9 sets out the key data relating to SitexOrbis's Northern Ireland branch.

TABLE 9 **SitexOrbis Northern Ireland**

	SitexOrbis
Number of depots	[✄]
Number of social housing customers	[✄]
Number of properties	[✄]
Number of alarms	[✄]
Number of staff	[✄]
Turnover FY12	[✄]
EBITDA FY12 pre-central overhead	[✄]

Source: SitexOrbis.

13.63 From Table 9 and the information in Appendix H, it can be seen that the Northern Ireland branch was profitable for SitexOrbis, generating £[✄] million EBITDA from £[✄] million revenues in FY12.

13.64 TDR submitted that the financial performance of the SitexOrbis Northern Ireland business unit was not such that its exclusion from a divestment package would affect the financial viability of the rest of the SitexOrbis business in comparison to the pre-merger scenario. It also told us that it would not affect SitexOrbis' ability to offer a national commercial service as it (VPS) ran a much larger national commercial business with no Northern Ireland presence. We considered that excluding Northern Ireland was unlikely to significantly affect SitexOrbis ability to offer a national commercial service as the Northern Ireland depot is mainly a social housing business and has commercial revenues of [✄].

13.65 It can be seen in Table 8 that EBITDA for this divestiture package [✄] for FY2012 and [✄] for LTM (to June 2012). Whilst this creates some risks for the divestiture package, in our view it is an adequate level of profitability to finance capital expenditure of £[✄] million (see paragraphs 13.40 to 13.42) and any other cash requirements assuming that the purchase is funded with an appropriate capital structure. There would be approximately £[✄] million of financial headroom after capital expenditure. This range of financial headroom is sufficient that it does not create significant additional risk. Although less profitable than SitexOrbis UK we concluded that this business would still be a viable stand-alone competitive entity and an effective competitor if it were divested to a suitable purchaser within an appropriately limited period.

Purchaser risk

13.66 Based on views from TDR/VPS and third parties, we would not expect divestiture of SitexOrbis GB to be significantly less attractive to potential purchasers than the divestiture of SitexOrbis UK:

(a) [✄]

(b) Clearway told us that it was not sure how significant Northern Ireland was for SitexOrbis but thought it should be regarded as largely irrelevant to the divestiture package.[274]

(c) MITIE's commercial void property security business said that SitexOrbis UK divestiture package [✄] and that it did not see much of a difference between the GB and UK divestiture packages.[275]

13.67 Based on this evidence our view is that the exclusion of Northern Ireland from the divestiture package is unlikely to materially affect purchaser risk.

Asset risk

13.68 [✄][276,277]

13.69 We noted that the transfer of the Republic of Ireland and Dutch businesses from SitexOrbis to VPS had been conducted relatively smoothly and we were not aware of any significant issues during this process. This process had commenced in mid-April 2012 and was completed by mid-July. At the time of this report, [✄]. The businesses transferred comprised both social housing and commercial properties: [✄] customers with [✄] properties in the Republic of Ireland and [✄] customers with [✄] properties in the Netherlands.

13.70 We considered whether there were any differences between the Republic of Ireland transfer and a potential Northern Ireland carve out. We found that:

(a) The Northern Irish business is significantly larger than the Republic of Ireland business in terms of revenues, profits and number of installed alarms. In particular, the Northern Ireland business has approximately [✄] the number of properties compared with the completed Republic of Ireland/Netherlands transfers. [✄]

(b) The SitexOrbis Republic of Ireland business used alarms purchased from a third party whereas the Northern Ireland business uses SitexOrbis's own alarms which are monitored by the SitexOrbis Alarm Response Centre in England. As these

[274] Clearway Remedies Call, 2 July 2012, paragraph 11.
[275] MITIE Remedies Call, 3 & 4 July 2012, paragraph 3.
[276] TDR response to the Remedies Notice, paragraph 4.94.
[277] TDR response to the Remedies Notice, paragraphs 2.24–2.26.

are SitexOrbis's own, rather than being from a third party manufacturer, a transfer of the depot could expose SitexOrbis to IP risk as well as potentially posing a small security risk to those buildings. [✂]

(c) The Republic of Ireland business is a separate legal entity whereas the Northern Ireland business is an integrated part of SitexOrbis UK. Whilst the Republic of Ireland business was sold as a share sale, the Northern Ireland business is a part of SitexOrbis UK. [✂]

(d) Staff in Northern Ireland (and in particular the branch manager) have knowledge of the SitexOrbis GB business which increases the risk of information leakage post-merger. Further, there is a risk that confidential information may be transferred. TDR said that it saw the risk at three levels—paper documents in the depot; IT data; and knowledge retained by staff. It said that the first two of these risks could be addressed by destroying relevant confidential information. It said that the last risk was present when any employee left a business.

(e) SitexOrbis told us that it had [✂] customers in Great Britain that also asked for commercial work to be done in Northern Ireland. SitexOrbis told us that customers did want the ability to be able to deliver commercial services in Northern Ireland. However, it is not clear that this is a particularly significant requirement or that loss of this capability would affect SitexOrbis's ability to compete for those customers in the rest of Great Britain (see paragraph 13.64).

13.71 These asset risks would need to be considered carefully when managing the carve-out of the Northern Ireland business unit, but we did not find that they would be so great as to reduce significantly the future competitiveness of SitexOrbis GB. The risks of integration would primarily fall on VPS and not the SitexOrbis business being divested, because any carve-out is one-way (from SitexOrbis to VPS).

Conclusion on effectiveness

13.72 Based on the analysis in paragraphs 13.61 to 13.71, we concluded that the divestiture of SitexOrbis GB would be effective in addressing the SLCs which we have identified if it were divested to a suitable purchaser within an appropriately limited period. It carries higher asset and composition risk than the divestiture of SitexOrbis UK because of the need to carve out the Northern Ireland business unit and the lower level of profitability. However, overall this risk is not significant and we therefore concluded that this divestiture would be effective.

Mix and match divestitures proposed by TDR/VPS

13.73 In this section, we consider the three mix and match divestitures proposed by TDR/VPS: [✂].

Addressing the SLCs in principle

13.74 TDR/VPS said that each of these divestiture options resulted in substantially the same package as the SitexOrbis GB divestiture package. They said that this would remedy the SLCs in any of the relevant markets because the conditions of competition in the regions of Northern Ireland, [✂] would not change and SitexOrbis would be able to compete effectively for commercial customers with national requirements.[278]

13.75 TDR/VPS also told us that it believed these divestitures would enhance competition in both the commercial and social housing markets. It said that this was because these remedy options would lead to each of VPS and SitexOrbis [✄].[279] In our view this may be the case but would only apply if the packages are firstly viable and secondly acquired by a suitable purchaser. If the packages are either not viable, and/or not acquired by a suitable purchaser then the competitive threat represented by SitexOrbis would be significantly reduced.

13.76 We have already considered the impact of excluding the Northern Ireland business from the divestiture package, in paragraph 13.61, so here we consider whether in addition the [✄] alters the effectiveness of the divestiture options in addressing the SLCs.

13.77 We are required to remedy the SLCs and their adverse effects that are expected to result from the merger and this requirement determines which divestiture package(s) is/are effective. We have therefore to consider whether any of the mix and match divestitures would lead to a package that in principle would be effective in addressing the SLCs we have identified, provided that the divested business is viable.

- *[✄]*

13.78 TDR said that as a result of this remedy, [✄][280] as well as competition from local suppliers. In relation to potential competition in the region, it said that SitexOrbis would have the same ability and incentive to open new business units in areas that it could not currently service in [✄] as VPS had pre-merger.[281]

13.79 In relation to the commercial SLCs we identified, we assessed what difference the depot swap would make to the customer coverage of the two parties. We used a 70-mile straight-line radius, the same as that used in our assessment of the competitive impact of the merger in our provisional findings and final report. The pre-merger overlap in the relevant area is shown in Figure 2 of Appendix H. The overlap under this package is shown in Figure 3 of Appendix H. Whilst the overlaps are not identical, the [✄] would still provide a competitive constraint to the 'new VPS' [✄] depots. We therefore judge that subject to our assessment of whether the divested business is viable, this divestiture package would in principle appear to address both the regional SLC and the national SLC we have identified.

13.80 In relation to the social housing SLC we identified, we assessed that there were few if any local areas where it would not be attractive to the merging parties to compete for social housing contracts, across Great Britain, either serving them from their existing depots or by opening new depots (see paragraph 10.13). As long as the [✄] is sold to a suitable purchaser and is an effective package (which we assess below) we do not see any reason why this should change for either party. Subject to our assessment of whether the divested business is viable, the [✄] is unlikely to impact on the level of competition in social housing offered by SitexOrbis.

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[278] TDR response to the Remedies Notice, paragraphs 4.25 & 4.60.
[279] TDR response to the Remedies Notice, paragraph 4.64.
[280] Business unit is TDR's and VPS's terminology.
[281] TDR response to the Remedies Notice, paragraph 4.61.

- *[✂]*

13.81 In relation to the commercial SLC we identified we note that the current SitexOrbis depot in [✂] is only [✂] from VPS in [✂]. Figure 2 in Appendix H shows the pre-merger overlap using a 70-mile straight-line radius whilst Figure 4 shows this adjusted for [✂]. It can be seen that the overlap area is slightly reduced [✂] but the reduction in overlap is quite small. In addition the ‘new SitexOrbis’ depot still imposes a constraint on the VPS depots using a 70-mile radius. We therefore judge that, subject to our assessment of whether the divested business is viable, in principle this divestiture package would appear to be capable of addressing both the regional SLC and the national SLC we have identified.

13.82 In relation to the social housing SLC we identified, our conclusion is identical to that for the [✂] (paragraph 13.80).

- *[✂]*

13.83 TDR said that as a result of this remedy, both SitexOrbis and VPS [✂].[282]

13.84 We did not identify any reason for our views in paragraphs 13.78 to 13.82 to change when considering the [✂].

- *Overall view on addressing the SLCs in principle*

13.85 Given our assessment of the effect on competition in the commercial and social housing markets we concluded that each of these divestiture packages would appear in principle to address the SLCs we have identified (subject to our assessment of whether the divested business is viable). However, under each proposal we note the lack of symmetry between the VPS business(es) and the SitexOrbis business(es) in terms of customer mix, size and financial contribution (see Tables 10 and 11 below). Whilst not seeming to affect the ability of the divestiture package to address the SLCs in principle, we consider that this may affect SitexOrbis’s ability to compete if the [✂] were to reduce its viability significantly (composition risk). We consider these issues in further detail in the following sections.

Composition risk

13.86 In this section we consider the composition risk of the proposed mix and match divestitures [✂].

13.87 TDR presented information which it said showed that under its proposed packages SitexOrbis would be a viable business capable of acting as an effective competitor against VPS for the foreseeable future. It said that [✂].

13.88 Tables 10 and 11 show a high-level comparison of the relevant [✂] business units.

[282] TDR response to the Remedies Notice, paragraph 4.27.

TABLE 10 [✂] **business unit comparison**

	VPS	*SitexOrbis*
Number of depots	[✂]	[✂]
Number of customers	[✂]	[✂]
Of which: social	[✂]	[✂]
Commercial	[✂]	[✂]
Number of properties	[✂]	[✂]
Number of alarms		[✂]
Number of staff	[✂]	[✂]
Turnover FY12	[✂]	[✂]
EBITDA FY12 pre-central overheads	[✂]	[✂]

Source: SitexOrbis, VPS.

13.89 [✂]

13.90 VPS told us that [✂] per cent of its [✂] was for [✂]; the [✂] appears to be heavily dependent on this relationship. VPS told us this contract was signed [✂] and was a [✂]-year contract with the option for a [✂]-year extension. Therefore whilst there appears to be no imminent risk associated with this contract nevertheless the depot does have a high reliance on this customer. In addition, the [✂] of its revenue accounted for by quote and order contracts, which is higher than normal for VPS. Quote and order contracts have less certainty than work carried out under a long-term contract.

TABLE 11 [✂] **business unit comparison**

	VPS	*SitexOrbis*
Number of depots	[✂]	[✂]
Number of customers	[✂]	[✂]
Of which: social	[✂]	[✂]
Commercial	[✂]	[✂]
Number of properties	[✂]	[✂]
Number of alarms		[✂]
Number of staff	[✂]	[✂]
Turnover FY12	[✂]	[✂]
EBITDA FY12 pre central overheads	[✂]	[✂]

Source: SitexOrbis; VPS.

13.91 [✂] We had a number of general composition risk concerns about these options:

(a) [✂]

(b) There is no certainty that the VPS businesses swapped into SitexOrbis will 'fit' with the business in the medium term. We were told that VPS has a much more centralized operating structure compared with SitexOrbis, which could reduce the effectiveness of the business units being transferred in as they are not used to operating in the this type of operational structure. This will increase composition risk for the divestiture package.[283]

(c) The business units being transferred in from VPS are very different to the ones being transferred out from SitexOrbis. [✂], which means the SitexOrbis business strategy in [✂] (and how that fits with the wider business strategy) would need to be reconfigured and potentially scaled down.

[283] VPS told us that several employees in the relevant businesses had previously worked for SitexOrbis but we did not consider this sufficient to overcome the larger risks to the divested business of having to integrate the new business unit(s).

(d) [✄]

(e) In each case the proposed package loses a significant amount of EBITDA which increases composition risk (we discuss this in further detail below).

13.92 We have set out in Table 8 how SitexOrbis's FY12 and LTM EBITDA would change as a result of each of the proposed packages and using the full current central overhead (see paragraphs 13.43 to 13.46): [✄].[284]

13.93 For these reasons we concluded that each of the packages would lack adequate financial headroom which would significantly increase composition risk.

13.94 For the reasons discussed earlier (see paragraphs 13.33 to 13.35) we assessed what the EBITDA performance of the packages would have been using both FY12 and LTM financials, and also including the partial central cost savings (which we have significant concerns about, see paragraphs 13.43 to 13.46). The results are set out in Table 12.

TABLE 12 **Modelled EBITDA including partial cost savings**

	[✄]	[✄]
[✄]	[✄]*	[✄]*
[✄]	[✄]	[✄]
[✄]	[✄]	[✄]

Source: Clearwater estimates. We have reconciled the Clearwater estimates to our estimates of the proposed packages and have not found any material differences.

*CC estimate.

13.95 Using Table 12 we note: [✄].

13.96 Each of the [✄] would therefore significantly increase the composition risk.

13.97 We have significant doubts about whether the partial central cost savings would be fully achievable in practice (see paragraphs 13.43 to 13.46), whether they would weaken the competitive position of SitexOrbis and hence whether it is appropriate to take them into account. Nevertheless, we concluded that based on paragraphs 13.94 to 13.95 that even if we were to accept them as fully achievable the packages still have little financial headroom and create significant composition risk and there is therefore uncertainty as to whether they would be viable in the medium term.

Purchaser risk

13.98 TDR told us that the level of interest in both [✄] was high and it had received [✄] expressions of interest in the mix and match packages. It said that [✄] package had received more interest from turnaround buyers.[285] It also told us that it was [✄].

13.99 Whilst we have little doubt that purchasers are interested in the business we have to consider our duty to address the SLCs and their adverse effects. The reduced viability (see paragraph 13.92 above) of these divestiture packages make it less likely that a buyer can be found who is able to satisfy the CC's criteria for a suitable purchaser because any business plan is unlikely to be viable without making

[284] [✄]
[285] TDR/VPS did not market the [✄] swap.

assumptions that there would be significant central overhead savings. As these savings are uncertain this adds to the purchaser risk.

13.100 We are also concerned about divesting a business which, due to composition risk, [✂]. There is more risk that such a business is not sustainable and is therefore less likely to be an effective competitor.

Asset risk

13.101 We considered whether there were additional risks with these swaps than in the carve-out of the Northern Ireland business unit. In the case of alarms, locks, staff knowledge and the size of the business we judged that the risks are similar to the Northern Ireland carve-out. Whilst the addition of [✂] increases the risk profile associated with any carve-out this additional risk is not significant. TDR presented us with a plan to carve-out the businesses within [✂] weeks followed by an [✂].

13.102 [✂] TDR told us that this was mainly a labour issue and would require a larger project team in order to be successfully completed on time.

Conclusion on effectiveness

13.103 Based on the analysis in paragraphs 13.74 to 13.102 we viewed all these mix and match divestitures as significantly more risky than the divestiture of SitexOrbis UK or SitexOrbis GB. Absent substantial central overhead cost savings they are unlikely to be sufficiently profitable to be self-funding which leads us to have significant concerns about their effectiveness. Even including the 'partial' cost savings suggested by TDR (about which we had significant doubts) a purchaser would have little financial headroom. The significant uncertainty regarding the achievability of these cost savings coupled with viability concerns create significant composition risk for each of the proposed mix and match divestitures.[286]

13.104 The mix and match divestitures also generate other additional risks relative to the divestiture of SitexOrbis UK and SitexOrbis GB because they introduce new risks to the business—principally related to operating a reconfigured business. In [✂] there would also be a reliance on one social housing customer.

13.105 We considered whether protective measures such as an upfront buyer or allowing TDR to attempt to divest these packages before SitexOrbis GB or SitexOrbis UK would be sufficient to overcome the composition risks we have identified. These composition risks are, in our view, inherent in the specification of the mix and match divestitures and therefore in each case not capable of being addressed through a purchaser scrutiny process.

13.106 We concluded that TDR's proposals would significantly increase the risk that SitexOrbis would not be an effective competitor and that, under TDR's proposals, this risk would be borne by *(a)* SitexOrbis (which would have to operate as an independent competitor after the reconfiguration of its depots, whilst at the same time implementing uncertain and significant cost savings, with little financial headroom); and *(b)* customers who would bear the risk that the SLCs were not remedied effectively.

13.107 We considered whether to canvass further opinions from potential purchasers about the composition risks associated with the mix-and-match packages put forward by

[286] See also second footnote to paragraph 13.23.

TDR, including issues such as the extent of possible cost savings, whether they would put capital into the business, and whether they were concerned about the lack of financial headroom. We considered that we would be unlikely to get significant additional insight from potential purchasers on these issues, given their lack of business information on SitexOrbis's and VPS's businesses, and that any views on these issues would be qualified and involve a degree of speculation and would be unlikely to able to inform our judgement as to the longer-term viability of the business such as to be effective in remedying the SLCs we had identified.

13.108 For these reasons we concluded that the proposed mix and match divestitures posed significant risks and would not be effective in addressing the SLCs.

Behavioural remedy proposed by TDR

13.109 We have summarized TDR's proposed remedy in paragraphs 13.17 and 13.18. The Merger Remedies Guidelines state that in general one or more of the following conditions will normally apply in the unusual circumstances where the CC selects behavioural remedies as the primary source of remedial action:[287]

(a) divestiture is not feasible or the relevant costs of any feasible structural remedy far exceed the scale of the adverse effects of the SLC;

(b) The SLC is expected to have a relatively short duration; and

(c) relevant customer benefits are not substantial (see paragraphs 13.121 to 13.124 below).

13.110 In this case none of the above are applicable—divestiture is feasible and the costs do not outweigh the adverse effects of the SLCs (see paragraphs 13.119 to 13.120 below); the SLCs are not time-limited; and we have not identified any relevant customer benefits (see paragraphs 13.12113.123 and 13.124).

13.111 Nevertheless we have considered the specification, circumvention, distortion and monitoring risks associated with TDR's proposed behavioural remedy.

(a) *Specification risks.* [✂]

(b) *Circumvention risks.* [✂]

(c) *Distortion risks.* [✂]

(d) *Monitoring risks.* [✂]

13.112 In conclusion and for the reasons given above, this case does not meet the conditions where such a behavioural remedy would be effective and the remedy proposed contains additional specification, circumvention, distortion and monitoring risks. We therefore concluded that the proposed behavioural remedy would not be effective in addressing the SLCs.

Overall conclusion on effectiveness of remedies

13.113 Based on paragraphs 13.21 to 13.112, we conclude that the divestiture of either SitexOrbis UK or SitexOrbis GB would be effective remedies to the SLCs and their

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[287] *CC8*, paragraph 2.16.

adverse effects that we identified. We consider implementation of our preferred divestiture package in paragraphs 13.125 to 13.143, after consideration of proportionality.

Proportionality

13.114 Having considered the effectiveness of remedy options, the Merger Remedies Guidelines state that the CC will then consider the costs of those remedies that it expects would be effective in addressing the SLC and resulting adverse effects. In order to be reasonable and proportionate the CC will seek to select the least costly remedy, or package of remedies, that it considers will be effective. If the CC is choosing between two remedies which it considers will be equally effective, it will select the remedy that imposes the least cost or that is least restrictive. The CC will seek to ensure that no remedy is disproportionate in relation to the SLC and its adverse effects.[288,289]

TDR's views

13.115 TDR submitted that any requirement by the CC for VPS to divest the SitexOrbis Northern Ireland business unit (ie divesting SitexOrbis UK) would be 'disproportionate, inequitable and consequently unlawful'. [✂][290]

Our assessment

13.116 In this case we have found that the following divestiture remedies are effective:

(a) SitexOrbis UK; and

(b) SitexOrbis GB.

13.117 We judge that the divestiture of SitexOrbis GB represents a less intrusive solution to the SLCs that we have found than divestiture of SitexOrbis UK. This is because it allows VPS to retain the Northern Ireland business unit of SitexOrbis and thus achieve some of its acquisition objectives, while effectively addressing our competition concerns. We conclude that provided the divestiture could be made to a suitable purchaser within an appropriately limited period that this would be a less intrusive solution than divestiture of SitexOrbis UK. The divestiture of SitexOrbis GB is therefore our preferred remedy, prior to the consideration of any relevant costs and customer benefits.

13.118 [✂] The Merger Remedies Guidelines state that for completed mergers, as is the case here, 'the CC will not normally take into account costs or losses that will be incurred by the merger parties as a result of a divestiture remedy ... Since the cost of divestiture is, in essence, avoidable, the CC will not, in the absence of exceptional circumstances, accept that the cost of divestiture should be considered in selecting remedies'.[291] No such exceptional circumstances are present in this case.

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[288] *CC8*, paragraph 1.9.
[289] We consider that the framework for assessing the proportionality of remedies that is set out in our Merger Remedies Guidelines is in line with the proportionality principles in European law as outlined, for example, in Case C-331/88 *R v Ministry of Agriculture, Fisheries and Food and Secretary of State for Health, ex parte Fedesa* [1990] ECR I-4023 and referred to in cases such as *Tesco v Commission* [2009] CAT 6.
[290] TDR response to the Remedies Notice, paragraph 1.4.
[291] *CC8*, paragraph 1.10.

13.119 We also considered any costs that could fall on third parties. We identified the following potential costs in relation to the divestiture of SitexOrbis GB:

(a) The cost to customers in Northern Ireland from any change of supplier. We considered whether existing SitexOrbis customers would be inconvenienced by having to change supplier to VPS. We judged that, although there are some potential costs, [✂]. In addition, we noted that ongoing relationships between the customer and its SSVP provider would be little changed because the existing SitexOrbis staff team in the Northern Ireland business unit would transfer over to VPS and would continue to deliver the same services to Northern Irish customers.

(b) The cost to SitexOrbis from the carve-out of the Northern Ireland business. We have considered above that the ongoing viability of the SitexOrbis business is not significantly affected by removal of the Northern Ireland business unit (see paragraphs 13.60 to 13.72). We also found that, although there are some risks with a carve-out of the Northern Ireland business unit, these risks were not insurmountable and would largely fall on VPS when trying to integrate the business unit. To the extent that the carve out creates any one-off costs for SitexOrbis (for example, from changing alarms), [✂].

13.120 On balance, we do not find there to be any significant third party costs with the divestiture of SitexOrbis GB. We also considered that a divestiture of SitexOrbis UK would not entail material third party costs. Therefore neither remedy is disproportionate in relation to the SLCs and the adverse effects.

Relevant customer benefits

13.121 In deciding the question of remedies, the CC is permitted to have:

> regard to the effects of any action on any relevant customer benefits (RCBs) in relation to the creation of the relevant merger situation concerned.[292] RCBs[293] are limited by the Act to benefits to relevant customers in the form of:
>
> (a) lower prices, higher quality or greater choice of goods or services in any market in the United Kingdom … or
>
> (b) greater innovation in relation to such goods or services

13.122 The Act provides that a benefit is only an RCB if it accrues from or is expected to accrue to relevant customers within the UK within a reasonable period from the merger and would be unlikely to accrue 'without the creation of that situation or a similar lessening of competition'.[294]

13.123 TDR told us that for the divestiture options involving depot swaps each business (VPS and SitexOrbis) [✂]. It said this should benefit customers.

13.124 The benefits described by TDR apply to the potential divestiture packages and not to the merged entity and are therefore not applicable as RCBs within the meaning of the Act. We therefore have not adjusted our preferred remedy (see paragraph 13.117) to

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[292] Section 35(5).
[293] Section 30.
[294] Sections 30(2) & 30(3).

take account of RCBs and are of the view that it is not necessary to do so in relation to a possible divestiture of SitexOrbis.

Implementation of divestiture remedies

13.125 In this section we consider issues relating to the implementation of a divestiture of SitexOrbis GB:

(a) we set out our views on the approach to be taken to ensure the suitability of any purchaser of the divested operations;

(b) we set out our views on an upfront buyer requirement; and

(c) we set out our views on other aspects of the divestiture process.

Suitable purchaser

13.126 The identity and capability of a purchaser is of major importance in ensuring the success of any divestiture remedy. The risk that no suitable purchaser would be found for the divestiture package is a significant risk to the effectiveness of a divestiture remedy. We set out below the criteria that the CC applies in assessing the suitability of potential purchasers for a divestiture.

Criteria for suitable purchasers

13.127 The CC will wish to satisfy itself that a prospective purchaser is independent of the merger parties, has the necessary capability to compete, is committed to competing in the relevant market(s) and that divestiture to the purchaser will not create further competition concerns.[295] These criteria are set out in more detail below:

(a) Independence—the purchaser should have no significant connection to VPS that may compromise the purchaser's incentives to compete with VPS; for example, an equity interest, shared directors, reciprocal trading relationships or continuing financial assistance.

(b) Capability—the purchaser must have access to appropriate financial resources, expertise and assets to enable the divested business to be an effective competitor in the market. This access should be sufficient to enable the divestiture package to continue to develop as an effective competitor.[296]

(c) Commitment to relevant market—the CC will wish to satisfy itself that the purchaser has an appropriate business plan and objectives for competing in the relevant markets.

(d) Absence of competitive or regulatory concerns—divestiture to the purchaser should not create a realistic prospect of further competition or regulatory concerns. Moreover, the CC's approval of a purchaser may be subject to clearance by the OFT or other regulatory authority. In considering whether a divestiture is likely to give rise to competitive concerns the CC applies the same framework to the competitive assessment as we have used in our competition analysis in this investigation.

[295] *CC8*, paragraph 3.15.
[296] For example, a highly leveraged acquisition of the divestiture package that left little scope for competitive levels of capital expenditure or product development is unlikely to satisfy this criterion.

13.128 The CC will consider the suitability of each potential purchaser on its own merits. The CC will wish to satisfy itself about each of the above criteria before approving any potential purchaser.

Upfront buyer

13.129 We considered whether it would be appropriate in relation to the SitexOrbis GB divestiture to require TDR/VPS to identify a suitable purchaser that was contractually committed to the transaction (an upfront buyer) before allowing it to carve out the Northern Ireland business unit.

13.130 The Merger Remedies Guidelines state that:

> Where the CC is in doubt as to the viability or attractiveness to purchasers of a proposed divestiture package (ie composition risk) or believes there may be only a limited pool of suitable purchasers (ie purchaser risk), it may require the merger parties to obtain a suitable purchaser that is contractually committed (for example through exchange of contracts subject to limited conditions) to the transaction before permitting a proposed merger to proceed or a completed merger to progress with integration. Where the CC considers that the competitive capability of the divestiture package may deteriorate pending the divestiture (ie asset risk) or completion of the divestiture may be prolonged, it may also require that the up-front buyer completes the acquisition before the merger may proceed or, in the case of a completed merger, before the merger parties may progress with integration.[297]

13.131 Our consideration of composition, purchaser and asset risks of the SitexOrbis GB divestiture is set out in paragraphs 13.62 to 13.72 above.

13.132 TDR told us that, [✂], it was also willing to do so during the divestiture process or immediately following completion.

13.133 We considered that, whilst it was likely that a suitable purchaser of SitexOrbis GB could be found, there would be significant asset risks if the Northern Ireland business unit had been carved out of the business and any divestiture of SitexOrbis GB then subsequently failed or were to be significantly delayed, such that we would need to consider reintegrating the Northern Ireland business in order to divest the whole of SitexOrbis UK. Whilst we consider this unlikely we note the original sales process took 18 months to complete (paragraph 13.137). We have therefore decided that we will require an upfront buyer to assist with a prompt disposal of SitexOrbis GB and to protect the CC's ability to implement an effective remedy. In the context of this transaction, we will only require the purchaser to be contractually committed to the transaction before permitting VPS to proceed with the carve-out of the Northern Ireland business unit.

Divestiture process

13.134 An effective divestiture process will protect the competitive potential of the divestiture package before disposal and will enable a suitable purchaser to be secured in an

[297] *CC8*, paragraph 3.19.

acceptable timescale. The process should also allow prospective purchasers to make an appropriately informed acquisition decision.[298]

13.135 We have considered the timescale for divestiture and other relevant measures.

Timescale for divestiture

13.136 We considered what the appropriate timescale for a divestiture sale would be. The Merger Remedies Guidelines state that:[299]

> The length of this period will depend on the circumstances of the merger but will normally have a maximum duration of six months. The CC, when determining the initial divestiture period, will seek to balance factors which favour a shorter duration, such as minimizing asset risk and giving rapid effect to the remedy, with factors that favour a longer duration such as canvassing sufficient selection of suitable purchasers and facilitating adequate due diligence.

13.137 The process of VPS acquiring SitexOrbis took from March 2010, when E&Y were appointed as advisers to run the sales process, to September 2011, although agreement with VPS was reached in February 2011. This is a total period of 18 months and was complicated in part by four different shareholders, each with a different perspective and none with a control position; the management's attempt to buy the business in cooperation with LDC; the separation of the transaction into two sale and purchase agreements (one for UK and one for the rest of Europe); and French workers council consent.

13.138 TDR told us that it would require [✄] months to complete a divestiture of [✄]. TDR's response to the remedies working paper stated that [✄] months was a reasonable timeframe to achieve a comprehensive divestment.

13.139 SitexOrbis told us that it would take four to six months to complete a divestiture process.

13.140 A number of parties told us that an extended divestiture process would increase risk:

(a) G4S told us that the divestiture could potentially be completed within three months of the release of the Information Memorandum, subject to due diligence. It said that if the process were to take more than six months it envisaged that there would be gradual leakage of both existing customers and SitexOrbis employees.[300]

(b) MITIE said that the appropriate length of time for the sale of SitexOrbis depended on SitexOrbis's current contract lengths. It said that contracts needed to be analysed so that there was no natural wastage of contracts. It said that six to nine months would be an appropriate divestiture timescale.[301]

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[298] *CC8*, paragraph 3.20.
[299] *CC8*, paragraph 3.24.
[300] G4S response hearing, 10 July 2012, paragraph 10.
[301] MITIE response hearing, 3 July 2012, paragraph 10.

(c) Clearway told us that a longer timescale would increase risk as good employees may leave and key customers start looking elsewhere. It said three to six months would be the best timescale.[302]

(d) SecureSite told us that a longer divestiture process would increase the risks for the SitexOrbis business.[303]

(e) Ealing Council told us that protracted negotiations were possible in the current economic situation and would increase the danger of financial instability and could, as a worst case, jeopardize the firm's viability.[304]

13.141 Having considered the evidence above, in particular the views of TDR, and in order to achieve a swift and effective disposal, we will require TDR/VPS to complete the disposal of SitexOrbis GB within an initial period of [✂] from the date of acceptance of final undertakings or within such appropriate timescale as is provided in any order. This initial [✂] period will be extendable by a further [✂] if the CC is satisfied that sufficient progress is being made towards completion of an effective disposal.

13.142 Provision will be included in final undertakings for a divestiture trustee to be nominated at the end of the initial divestiture period and to be appointed if, at the end of either the initial divestiture period or the extended divestiture period, the CC is of the view that insufficient progress is being made towards completion of disposal. [✂][305]

Other relevant measures

13.143 Following the reference to the CC, a monitoring trustee was appointed to oversee the hold separate arrangements. Consistent with our undertakings, we will require the monitoring trustee to continue in place until the divestiture has been completed so as to ensure that the competitive capabilities of the divested operations are not harmed during the divestiture period.[306]

Our decision on remedies

13.144 We have decided to require TDR/VPS to divest the SitexOrbis GB business, as described in paragraph 13.113.

13.145 The implementation of the sale of SitexOrbis GB will be subject to the safeguards set out in paragraphs 13.125 to 13.143. In particular:

(a) the CC will wish to satisfy itself as to the suitability of potential purchasers (see paragraphs 13.126 to 13.128;

(b) TDR/VPS will be required to be contractually committed to a divestiture to a suitable purchaser prior to carving out the Northern Ireland business unit from SitexOrbis UK (see paragraph 13.133);

(c) the monitoring trustee will continue in place until the divestiture has been completed so as to ensure that the competitive capabilities of the divested operations are not harmed during the divestiture period (see paragraph 13.143); and

[302] Clearway response hearing, 2 July 2012, paragraph 7.
[303] SecureSite hearing summary, paragraph 7.
[304] Ealing Council response by email to the Remedies Notice.
[305] *CC8*, paragraph 3.13.
[306] *CC8*, paragraph 3.23.

(d) provision will be included in final undertakings for a divestiture trustee to be nominated at the end of the initial divestiture period of [✂] and to be appointed if, at the end of either the initial divestiture period or the extended divestiture period of a further [✂], the CC is of the view that insufficient progress is being made towards completion of disposal. [✂]

13.146 In our judgement, this package of measures represents as comprehensive a solution to the SLCs and their adverse effects as is reasonable and practicable.