

Anticipated acquisition by Bottomline Technologies (DE), Inc of Albany Software Limited

ME/5475-12

The OFT's decision on reference under section 33(1) given on 3 September 2012. Full text of decision published 20 September 2012.

Please note that the square brackets indicate figures or text which have been deleted or replaced in ranges at the request of the parties or third parties for reasons of commerce.

PARTIES

1. **Bottomline Technologies (de), Inc (Bottomline)** is a NASDAQ listed company registered in Delaware, USA. It provides payment, invoice and banking solutions to companies and financial institutions. Bottomline's activities in the UK include the manufacture and supply of software and associated services relating to payments through the Bankers' Automated Clearance System (Bacs) and the Faster Payments System (FPS). Bottomline's global turnover for the year ended 30 June 2011 was US\$189.4 million. Its revenue earned from customers in the UK was £[] million.
2. **Albany Software Limited (Albany)** is a private limited company registered in England and Wales. It is owned by Adrian and Christina Stafford-Jones (each holding 50 per cent of the shares in Albany). Its principal activity is the manufacture and sale of software and associated services relating to payments through Bacs and FPS. Albany's turnover for the year ended 31 December 2011 was £[] million. All of that revenue was earned from customers in the UK.

TRANSACTION

3. On 13 March 2012, Bottomline and Albany signed a share purchase agreement under which Bottomline will acquire 100 per cent of the shares in Albany. The consideration is £20 million. The transaction is conditional upon UK merger clearance.
4. A satisfactory submission was received on 31 May 2012. The OFT's administrative deadline is 3 September 2012.

JURISDICTION

5. The OFT believes that the proposed transaction would result in two or more enterprises ceasing to be distinct under section 23(2) of the Enterprise Act 2002 (the Act).
6. The parties overlap in the supply of Bacs and FPS software and associated services in the UK. Bottomline estimated that the parties' share of the supply of software to businesses in the UK to make automated payments via the Bacs or FPS systems¹ (that is, software used to make Bacs and/or FPS payments, excluding payments made via bureaux or e-banking) would be [30-40] per cent and agreed that the parties overlap in this segment. The OFT considers that the parties' combined shares of supply in relevant markets may be higher (see further below). However, the OFT believes that, for jurisdictional purposes, the share of supply outlined above is sufficient to satisfy the test contained in section 23(2) of the Act.

MARKET DEFINITION

Introduction

7. Businesses need to interact with the Bacs or FPS payment networks in order to make automated payments, for example to pay staff or suppliers, and to receive payments from third parties, for example payments from customers. There are three main channels through which a business can use the Bacs or FPS payment networks. First, the business can buy software approved by Bacs or FPS that allows it to interact directly with

¹ The Bacs and FPS networks are each owned by consortia of banks.

the Bacs or FPS networks. Second, the business can instruct a bureau to make/receive payments from the networks on its behalf (the bureau will do so using approved software). Third, the business can use the e-banking platform offered by its bank to make payments to the networks. The parties overlap in the following activities:

- supply of software (and associated services)² to businesses to make direct payment submissions to the Bacs system (Bacs software to business)
 - supply of software to bureaux to make submissions to the Bacs system (Bacs software to bureaux)
 - supply of Bacs and FPS software to banks on a white-label basis (white-label software to banks) (Albany does not currently supply white-label software but has previously competed to supply this software)
 - supply of software to businesses to make direct submissions to the FPS system (FPS software to business)
 - supply of software to bureaux to make submissions to the FPS system (FPS software to bureaux) and
 - supply of bureau services to businesses to make indirect payments to the Bacs or FPS system (bureau services).
8. E-banking solutions are electronic platforms offered by banks to allow their business customers, inter alia, to make payments to the Bacs or FPS networks. The parties are not active in e-banking nor in the supply to banks of the technology underlying e-banking solutions.
9. The parties also overlap in the provision of Direct Debit management services, document process automation services and supply of account validation software. However the overlaps between the parties in these

² Suppliers of payments software generally also provide associated installation, support and maintenance services. Hereinafter in this decision assessment of the supply of each type of software also covers the supply of the services associated with that type of software – see further paragraphs 10 and 32 below.

activities are minimal and they are not discussed further in this decision.

Product Scope

10. The OFT has considered each of the overlaps between the parties outlined at paragraph 7 above and considered whether it constitutes a relevant market for the OFT's competitive assessment. The candidate markets considered are the supply of:

- Bacs software to business³
- Bacs software to bureaux
- white-label software to banks
- FPS software to business
- FPS software to bureaux, and
- bureau services.

11. As outlined in the OFT/CC Merger Assessment Guidelines, market definition is not an end in itself and the boundaries of the market do not determine the outcome of the analysis of the competitive effects of the merger in any mechanistic way.⁴ This is especially important in the present case as there is evidence of significant product differentiation within some of the markets discussed below and of competitive constraints from outside some of the markets. The OFT has regard to these matters in its competitive assessment.

³ Suppliers of payments software generally also provide associated installation, support and maintenance services. The evidence available to the OFT indicates that after-sales services are provided by the software supplier on terms agreed when the software is sold and that competitive conditions for initial sales and after-sales services are similar. Therefore in this decision after-sales services are considered as part of the market for the supply of software.

⁴ OFT/CC Merger Assessment Guidelines, paragraph 5.2.2.

Bacs software to business

12. Bottomline submitted that Bacs software to business is part of a wider market including FPS software, e-banking and bureau services. It submitted that each of these represents a substitute for Bacs software, since each performs the same basic function of allowing businesses to make and receive automated payments. However, the third party evidence available to the OFT did not indicate clearly that the constraint from these alternatives was sufficient to warrant their inclusion in the relevant market.
13. As regards FPS software, customers told the OFT that FPS payments incur much higher bank charges than Bacs payments and that FPS tends to be used only for time-sensitive payments, whereas Bacs (which operates on a three day clearing cycle) is used for less urgent scheduled payments. Customers who can use FPS software⁵ indicated that it tends to be used as a complement to Bacs software rather than providing a substitute.
14. As regards e-banking, a number of third parties indicated that e-banking solutions can be a viable substitute to Bacs software, particularly for customers whose payment requirements are relatively basic. However, several customers and competitors told the OFT that e-banking solutions have limited functionality in comparison to software (for example, a lack of reporting to verify successful completion of payments). Some third parties indicated that these limits mean e-banking is not a viable alternative for many customers. In light of this evidence and the prospect that it may be possible for the merged entity to price discriminate against groups of customers for whom e-banking is a less viable option, the OFT has adopted a cautious approach and excluded e-banking from the relevant market. However, the OFT has considered the extent of the constraint from e-banking in its competitive assessment.
15. As regards bureau services, few customers indicated that they would switch to bureaux in the event of an increase in the price of Bacs software. The parties provided only a small number of examples of customers who had switched from Bacs software to bureau services. In light of this evidence the OFT does not consider it appropriate to include bureau

⁵ Currently only Barclays permits its customers to use FPS software to make direct submissions to the FPS network.

services in the relevant market but does consider the extent of any constraint in its competitive assessment.

16. The OFT has also considered whether it is appropriate to segment the supply of Bacs software (and the other candidate markets) based on customer requirements for different levels of functionality. However, the evidence indicates that, while software is differentiated, there is a spectrum of product functionality and there are no clearly demarcated segments based on customer requirements. Therefore, the OFT considers it appropriate not to segment the candidate markets further but to consider product differentiation within the markets as part of its competitive assessment.

Bacs software to bureaux

17. Bottomline submitted that it may be appropriate to consider the supply of Bacs software to bureaux as a separate market.
18. The Bacs network requires bureaux to use software containing additional code not included in the standard Bacs software for businesses. Accordingly, bureaux cannot use the Bacs software supplied to businesses.
19. The OFT considered whether suppliers of Bacs software to bureaux may be constrained by the options available to the bureaux customers (including Bacs software and e-banking). However, the OFT does not have sufficient evidence on the demand-side substitutability from bureau services to Bacs software or e-banking to conclude that these services should be included in the relevant market. Accordingly, the OFT considers it appropriate to consider the supply of Bacs software to bureaux as a separate market.

White-label software to banks

20. Bottomline submitted that white-label software⁶ may constitute a separate market. Third party evidence indicates that Bacs or FPS software sold through a white-label arrangement with a bank will generally have the same

⁶ Currently only the Barclays white-label software offers FPS functionality. Barclays procured the Bacs and FPS functionality as part of the same tender process. The OFT therefore considers the supply of white-label Bacs and FPS software together.

functionality as the equivalent supplier-branded software and that there is a high degree of demand-side substitutability between white-label and branded products on the downstream market for sale to business customers. Therefore, it is arguable that the indirect constraint from software to business should be considered when assessing the supply of white-label software to banks.

21. It is not necessary for the OFT to reach a conclusion on whether the relevant market should include software to business since competition concerns do not arise on either basis. However, taking a cautious approach, the OFT has treated the supply of white-label software to banks as a separate market.

FPS software to business

22. Bottomline submitted that the supply of FPS software is part of a wider market for payment software and services. The OFT has considered whether other types of software/services impose a sufficient constraint on FPS software to be included in the same market.
23. As regards Bacs software, as outlined above, third party evidence indicated that customers tend to use FPS and Bacs software as complements rather than substitutes. The evidence available to the OFT does not indicate that sufficient FPS customers would switch to Bacs software to justify widening the product scope. As regards bureau services and e-banking solutions, similarly, the OFT has not received sufficiently clear evidence of demand-side substitutability from FPS software to these services to justify including them in the relevant market. However, the extent of the constraint from e-banking and bureaux services is considered in the competitive assessment. Accordingly, the OFT considers it appropriate to treat the supply of FPS software to business as a separate market.

FPS software to bureaux

24. The FPS network requires bureaux to use software containing additional code not included in the standard FPS software used by businesses. Accordingly, bureaux cannot use the FPS software supplied to businesses.
25. The OFT considered whether suppliers of FPS software to bureaux may be constrained by the options available to the bureaux customers (including

FPS software and e-banking). However, the OFT does not have sufficient evidence on the demand-side substitutability from bureau services to FPS software or e-banking to conclude that these products should be included in the relevant market. Accordingly, the OFT considers it appropriate to consider the supply of FPS software to bureaux as a separate market.

Bureau services

26. Bottomline submitted that the supply of bureau services is part of a wider market for payment software and services. However, the OFT does not have sufficient evidence that bureau customers would switch to other payment methods (such as software or e-banking) in the event of a price rise to conclude other payment methods should be included in the relevant market. Accordingly, the OFT considers it appropriate to treat bureau services as a separate market.
27. The OFT has considered whether, given the differences between Bacs and FPS payments, the supply of Bacs bureau services should be assessed separately from the supply of FPS bureau services. However, it is not necessary to reach a conclusion on this matter since no competition concerns arise on either basis.

Geographic scope

28. Bottomline submitted that each of the relevant markets is national in scope (UK-wide). Bottomline submitted that the vast majority of software suppliers and bureaux operate nationally and that all e-banking solutions are available nationally. This is consistent with the OFT's investigation which found that suppliers compete nationally and did not uncover any material sub-national variation in competitive conditions. The OFT therefore considers the appropriate geographic scope for each market to be national.

Conclusion on market definition

29. The OFT considers it appropriate to examine the transaction by reference to the following markets, supply of:
 - Bacs software to business

- Bacs software to bureaux
- white-label software to banks
- FPS software to business
- FPS software to bureaux and
- bureau services (as a whole and Bacs and FPS separately).

30. In each case, the market is national in scope.

THEORIES OF HARM

31. The OFT has examined the transaction by reference to the following theories of harm:

- horizontal unilateral effects arising from loss of competition in each of the markets identified in paragraph 29 above
- vertical unilateral effects arising from input foreclosure in the supply of white-label software to banks
- vertical unilateral effects arising from input foreclosure in the supply of Bacs and/or FPS software to bureaux, and
- coordinated effects in each of the markets identified in paragraph 29 above.

HORIZONTAL EFFECTS

32. As outlined above, suppliers of payments software generally also provide associated installation, support and maintenance services to customers using their software. The OFT considers that suppliers in the relevant markets compete on a range of parameters and a reduction in competition could result in consumer harm on one or more competitive parameters. For example, as regards price, a reduction in competition could result in higher upfront licence fees, higher maintenance fees and/or the withdrawal of support for existing software, so as to oblige customers to purchase new

software. A loss of competition could also result in deterioration in the quality of the competitive offering, for example, less innovation in the development of new software and/or poorer quality support/maintenance services.

Bacs software to business

Shares of supply

33. The OFT was made aware of 19 suppliers of Bacs software to business. Bottomline was unable to provide revenue shares for individual suppliers. Bottomline submitted that the best available proxy for shares of supply is the share of direct payment transactions (submissions) made to the Bacs network using each supplier's software. Table 1 below shows shares of submissions for the period June 2011 to May 2012 provided by Vocalink (the group that operates the Bacs system).⁷

⁷ Bottomline submits that the Vocalink data available to it suggest the parties have a smaller share of supply. However, the parties included both direct and indirect submissions to Bacs and thus included payments made by bureaux as well as direct submissions by businesses. The OFT considers that the data in Table 1 are a better proxy for the parties' share of software to business.

Table 1 Bacs Software to Businesses – Shares of Direct Bacs Submissions⁸

Supplier	Share of Submissions (per cent)
Bottomline	[20-30]
Albany	[10-20]
Combined	[40-50]
Experian	[30-40]
Fundtech	[0-10]
Microgen	[0-10]
Barron McCann	[0-10]
Others	[0-10]
Total	100

Source: Vocalink. Parties' shares do not sum due to rounding.

34. Pre-merger, Bottomline and Albany are the second and third largest suppliers of Bacs software to business measured by share of submissions. Experian is the largest supplier while Fundtech and Microgen are slightly smaller than Albany. Barron McCann accounts for [0-10] per cent of submissions and the remaining suppliers each have small shares.
35. The OFT considers that the share of supply data provide only a limited view of the competitive dynamics in this sector. First, the products are highly differentiated, such that share of supply data do not fully reflect the relative closeness of competition between different suppliers (see further below). Second, shares of supply based on total submissions made using each supplier's software are partly driven by the size of each supplier's installed base of users and do not provide a clear indication of the relative importance of each supplier more recently. Accordingly, the OFT has placed only limited evidential weight on the share of supply data.

⁸ The data attribute to each supplier submissions made through its own branded software and, in respect of Bottomline and Fundtech, submissions made through white-label software it supplies to banks. On a cautious basis, the OFT considers that it may be appropriate to exclude these white-label sales from the market total. Excluding white-label would reduce Fundtech's share of supply and would slightly increase Bottomline's share but does materially change the competitive assessment.

Closeness of competition

Customer requirements

36. The supply of Bacs software to business is highly differentiated. While all software facilitates the same basic function of making and receiving payments from the Bacs network, there is a wide variety of additional functionality relating to, inter alia, security features, the number of users who can access the software simultaneously, the volume of payments that the software process and the detail of reports generated by the software to verify that the payments have taken place correctly. These variations in functionality are reflected in a wide range of prices. For example, the list price of Bottomline's most sophisticated product (Webseries) is around [] times higher than its most basic product (Winbacs).
37. Third party evidence indicates that there is a spectrum of customer requirements based on the number and complexity of their payments but has not suggested any clear or consistent demarcation between different customer requirements. Each of the parties internally segments the sector into different customer requirements and has different products focussed on each segment. However, the parties' internal customer segmentations are different from one another. Bottomline aims its upper tier product (Webseries) at customers with revenue greater than £[] million, its mid-tier product (C-series) at customers with revenue between £[] million and £[] million and its lower tier product at customers with revenue lower than £[] million. Albany aims its upper tier product (AlbacsEnterprise) at customers with more than [] employees, its mid-tier product (Albacs cs) at customers with between [] and [] employees and its lower tier product (Albacs sbe) at customers with fewer than [] employees.
38. While there are no clearly demarcated customer segments, for the purposes of assessing potential closeness of competition within a differentiated market, the OFT considers it useful to assess competitive conditions within different segments of the market. Therefore, the OFT has considered competitive conditions in respect of notional upper tier, mid-tier and lower tier customer requirements, while recognising that, in reality, these segments are not consistently defined within the industry.

Parties' differentiated customer focus

39. Bottomline submitted that the parties focus on different customers, with Bottomline focussing on customers with more sophisticated requirements and Albany focussing on customers with more basic requirements. Bottomline submitted that the only customer segment where there is a substantial degree of competition between the parties is in the mid-tier. Bottomline submitted that, even within this mid-tier, the parties are differentiated, with Bottomline tending to offer more sophisticated products than Albany. This is consistent with a Bottomline internal transaction document which states that Albany's software set is 'relatively simple'⁹ (few of the other internal documents provided by the parties contained information on closeness of competition).
40. Table 2 below shows the proportion of each parties' Bacs revenue associated with their upper, mid and lower tier products.

Table 2 Parties' Bacs Revenue by Product

Segment	Supplier	Total Revenue (per cent)
Upper Tier	Bottomline	[20-40]
	Albany	[0-20]
Mid Tier	Bottomline	[20-40]
	Albany	[40-60]
Lower Tier ¹⁰	Bottomline	[20-40]
	Albany	[40-60]
All Tiers	Bottomline	100
	Albany	100

Source: parties.

41. Table 2 indicates that Albany's revenue from its upper tier product (Albacs Enterprise) is relatively small. []. This is consistent with the balance of third party evidence provided to the OFT. Most third party evidence indicates that Albany is not a major supplier of sophisticated, upper tier software. Third party evidence indicates that Experian is Bottomline's main

⁹ Albany Software Acquisition Opportunity Memorandum, 3 February 2012.

¹⁰ Bottomline submits that a substantial portion of its lower tier revenue is generated by sales of white-label software to Barclays and HSBC (which it is unable to exclude from the data).

competitor as regards customers with top tier requirements.

42. Bottomline submitted that both parties compete in the mid-tier segment but that, even within this segment, Bottomline tends to cater for more sophisticated requirements than Albany. As regards new sales of C-series and Albacs cs (the parties' mid-tier products) in the past two years, the average value of each Bottomline sale was £[], whereas the average value of each Albany sale was £[].
43. Bottomline submitted that a large number of suppliers are active in the mid-tier and that the parties do not exert an especially strong constraint on one another. The third party evidence provided to the OFT indicated that the parties compete against one another for customers with mid-tier requirements but that several other suppliers have strong offerings in this segment. Most third party evidence indicated that there is a range of strong suppliers other than the parties, including Fundtech and Barron McCann.
44. Bottomline submitted that it does not focus on the lower tier such that the merger would have little impact in respect of customers with lower tier requirements. Bottomline submitted that, even to the extent it is active in the lower tier, it tends to cater for more sophisticated requirements than Albany. As regards new sales of Winbacs and Albacs sbe (the parties' lower tier products) in the past two years, the average value of each Bottomline sale was £[], whereas the average value of each Albany sale was £[].
45. The balance of third party evidence provided to the OFT indicated parties compete against one another for customers with lower-tier requirements but that several other suppliers have strong offerings in this segment. Most third party evidence indicated that there were a range of strong suppliers other than the parties, including Fundtech, Barron McCann and Mosaic.
46. In general, only a few of the customers contacted by the OFT expressed any concerns in relation to the merger. The great majority of customers did not indicate that the merger would materially reduce their choice of software suppliers.

Diversion evidence

47. The OFT has considered evidence on diversion submitted by Bottomline to

assess the extent of customer switching between the parties. Bottomline provided two sets of data which it submitted indicate that diversion between the parties is likely to be low, such that the merger would have little impact on the parties' incentive to increase prices or otherwise deteriorate their competitive offerings.

Cancellation data

48. The first dataset is based on cancellations of Bacs software products by customers of Bottomline and Albany over the past two years. The parties cross-checked cancellations by Bottomline customers against Albany's new customers (and vice versa) to indicate the level of diversion between the parties.
49. Bottomline submitted that of [] relevant cancellations by its Bacs software customers, only [] diverted to Albany. The OFT has some reservations over the reliability of these data. In particular, it is not clear that all instances recorded as cancellations by Bottomline led to a customer switching to another payment solution (such that not all the cancellations necessarily relate to competition). Therefore, the OFT has taken a cautious approach and excluded from the denominator 35 per cent of cancellations that were not clearly lost to a competing supplier.¹¹ This gives an estimated customer diversion ratio¹² from Bottomline to Albany of [five-10] per cent.
50. Bottomline submitted that of [] cancellations by Albany customers that were lost to competition, only [] diverted to Bottomline, resulting in a diversion ratio of [0-five] per cent. Again, the OFT has concerns that diversion ratio may be biased downwards by the inclusion in the denominator of cancellations that were not genuinely lost to a competing supplier. However, even if the denominator was reduced very substantially to reflect this concern, the diversion ratio would be less than five per cent.

¹¹ Bottomline recorded the reason for cancellation for six months within the two-year period. The OFT extrapolated from these data to exclude the proportion of cancellations (35 per cent) which were not related to switching to a competing supplier (for example, where the cancellation was caused by the customer going out of business).

¹² The data source did not record the revenue associate with each cancellation, such that it is not possible to calculate revenue diversions.

51. In light of the uncertainties associated with the correct denominator, the OFT has placed only limited evidential weight on the diversion ratios generated from the cancellation data. However, the fact that the diversion ratios remain low, even following the OFT's adjustments to provide a more conservative approach, tends to support Bottomline's submission that the parties are not a key competitive constraint on one another.

Lost prospect data

52. The second dataset is based on an internal Bottomline database recording 'lost prospects' (that is, opportunities recorded by Bottomline as a potential sale but not ultimately converted into an actual sale). This database included [] lost prospects over the last two years.
53. The database recorded the salesperson's best available information on what the prospect ultimately purchased. Bottomline used this information to estimate diversion to third parties and, for Albany, cross-checked against Albany's new customer list to estimate diversion to Albany. Bottomline did not record the destination of [] of the [] lost prospects. The OFT considers it appropriate, on a cautious basis, to exclude these from diversion calculations, leaving [] lost prospects. Bottomline submitted that only [] of the remaining [] prospects were lost to Albany, giving a customer diversion ratio of [10-15] per cent and revenue diversion of [five-10] per cent. This was lower than diversions to each of Experian, Microgen, Mosaic and RBS and was similar to diversion to Fundtech, Barron McCann and Data Interchange. Bottomline submitted that, even when focussing on prospects associated with Bottomline's mid-tier product (C-series) (where the diversion would potentially be expected to be higher than in relation to lower-tier or mid-tier products), the revenue diversion was only [five-10] per cent.
54. The OFT has some reservations on the use of these data. While lost prospects data can, in principle, provide information on closeness of competition, it is not clear to the OFT that they should be given the same weight as switching data (that is, observations of a supplier's existing customers switching to other suppliers). For example, a potential purchaser may be a prospect for many suppliers and it is not clear that the diversion behaviour of prospects will be similar to the diversion behaviour of existing customers. Therefore, it is not clear that diversion ratios based on lost prospects data will be as informative of the effect of the merger on the

parties' incentives as diversion ratios based on switching data.

55. Aside from this general reservation, the OFT has some additional concerns around the reliability of the data in this case. First, it was not clear to the OFT that all of the prospects recorded in the database were genuine potential sale opportunities for Bottomline (as opposed to purely speculative approaches). Second, given the small number of lost prospects, the OFT was mindful that it could place only limited confidence in any estimates of revenue diversion.
56. In light of its reservations, the OFT does not consider much weight can be placed on the precise level of the diversion ratios. However, data are not entirely without evidential value and the OFT notes that, in general terms, the data are consistent with a number of competitors offering viable alternatives to the parties' Bacs software products.

Innovation

57. The OFT also considered whether the parties were particularly close competitors as regards innovation and the development of new products. However, the evidence available to the OFT indicates that Albany has not been a particularly important innovator in recent years and that third party suppliers have been active in product innovation. For example, the OFT understands that Barron McCann and Fundtech were the first suppliers to develop cloud-based technology solutions. Therefore, the OFT considers that the parties are not particularly close competitors as regards innovation.

Conclusion on closeness of competition

58. In light of the above evidence, the OFT considers that the parties are not close competitors as regards upper tier customer requirements. The OFT does consider the parties are closer competitors in the mid-tier and, to a lesser extent, the lower tier. However they face vigorous competition from several suppliers in each of mid- and lower tiers. In particular, while Barron McCann, Fundtech and Microgen have smaller installed bases than Albany, the evidence available to the OFT suggests that they (and some smaller suppliers) compete strongly for new and existing customers, at least in the lower and mid-tiers. The OFT also notes that each of Fundtech, Barron McCann and Microgen are part of large organisations, with significantly greater resources than Albany.

59. The OFT also notes that there are few constraints on competitors' ability to increase volumes significantly in response to increased demand. In particular, the evidence indicates that the marginal cost of selling additional copies of existing software is low and that it is possible to outsource some installation and maintenance functions, such that increasing volumes does not require substantial investment. The OFT considers that the ability of third parties present in all tiers who are strong and credible rivals to the merged entity to increase volumes quickly in response to a deterioration in the merged entity's competitive offering constitutes a strong constraint.

Other constraints

60. As outlined above, the OFT does not include non-Bacs software products in the relevant market. Nonetheless, the OFT has considered the extent of the competitive constraint imposed on the parties' Bacs software activities by e-banking solutions and bureau services.

E-banking

61. As outlined above, third party evidence indicated that, e-banking is unlikely to provide a viable solution for many of those customers with complex Bacs requirements and, on a cautious basis, e-banking was excluded from the market. Bottomline submitted that e-banking is a large and growing constraint on Bacs software suppliers. Bottomline provided examples of customers who had switched away from the parties Bacs software products in favour of e-banking solutions and internal documents indicating that the parties consider e-banking to constitute a competitive threat.¹³ Albany marketing documents indicate that it is actively targeting its products at customers who might otherwise consider using e-banking solutions.

62. Third party evidence indicated that, while e-banking is unlikely to provide a viable solution for some of those customers with very complex Bacs requirements, it can provide a solution for those with more basic requirements. The balance of evidence suggested that e-banking provided a viable solution for the majority of lower tier requirements. Some of the

¹³ For example, Cornflower's Competitors presentation.

evidence suggests that e-banking also provides a viable solution for at least some customers with mid-tier requirements.

63. The parties' cancellation data suggest high levels of diversion to e-banking: [more than 50] per cent from Bottomline and [more than 50] per cent from Albany. Bottomline's lost prospects data suggest diversion of [more than 25] per cent to e-banking. As noted above, the OFT has placed only limited reliance on these data and does not consider the parties' lost prospects data can be used to infer precise diversion ratios. However, the OFT notes that, in general terms, the data are consistent with e-banking exerting some degree of constraint on Bacs software suppliers.
64. Taking the above evidence in the round, the OFT considers that e-banking provides an additional constraint on the parties' software activities, at least in respect of customers with lower tier requirements.

Bureau services

65. Bottomline submitted that bureau services are an additional constraint on Bacs software suppliers. Bottomline's lost prospects data suggested diversion of [0-10] per cent to bureaux. While the OFT does not consider the parties' lost prospects data can be used to infer precise diversion ratios, the data provide an indication that bureaux exert some constraint on Bacs software suppliers, albeit to a lesser extent than e-banking. However, third party evidence indicated that only a small number of existing software customers would be willing to switch to using bureaux in the event of a price increase. In light of the mixed evidence, the OFT considers that bureaux are, at most, a marginal constraint on the parties' Bacs software activities.

Margins

66. The OFT notes that the parties both earn high variable profit margins on their payments software products. Bottomline's gross margin for the last financial year was [] per cent and Albany's was [] per cent.¹⁴ The OFT is mindful that high variable profit margins may make unilateral effects more likely because the value of sales recaptured by the merged entity,

¹⁴ These margin data relate to all payment products (not only Bacs software to business).

previously lost to the other merging firm, will be greater than would otherwise be the case. However, the OFT is also mindful, in respect of Bacs software to business and the other markets assessed, that high margins alone will not give rise to concerns in circumstances where diversion between the parties is likely to be low and/or where there is likely to be a significant supply-side response to any post-merger deterioration in the competitive offering of the merged entity.

67. In the supply of Bacs software to business, overall the evidence available to the OFT does indicate that diversion between the merging parties would be expected to be reasonably low and that competitors could be expected to increase volumes in response to a deterioration in the merged entity's competitive offering. In weighting this evidence, given the reservations in relation to the diversion data (see paragraphs 48 to 56 above), the OFT has placed more reliance on the supply-side responses of the numerous credible third party rivals that exist in this market.

Entry/Expansion

68. Bottomline submitted that there are no material barriers to entry in the supply of Bacs software. Bottomline notes that three new entrants have become Bacs approved software suppliers in the last year (Fidelity, AccessPay and Unified). Third party evidence indicated that the main barrier to entry is the low number of sales opportunities, given that the market is relatively mature and that customers purchase new products infrequently. Third parties also indicated that, given the importance of reliability, some customers can be reluctant to purchase from a supplier without a proven track record in payments software. However, there are also examples of small suppliers who have entered successfully and won large customers. For example, Bottomline submitted that BMW, BT, Centrica, Norwich Union and Toyota became customers of Eiger (now Experian) soon after it had entered the market and when it was a small organisation. Third party evidence confirms that Experian won a significant number of large customers when it entered the market. In light of the mixed evidence on entry, the OFT has found that, while new entry is possible, new entrants may not compete strongly, especially for mid- and upper tier requirements in the near term.
69. Bottomline submitted that existing suppliers can expand quickly and cheaply. As outlined above, third party evidence did not indicate significant

barriers to a supplier increasing volume within its existing market segment but some third parties suggested it is more difficult for a supplier focussed on the lower and mid-tiers to expand into the upper tier given customers' preference for suppliers with a proven track record of supplying large organisations. However, third party evidence indicated that a supplier focussed on the upper tier could more easily expand into lower tiers where customers' requirements are less sophisticated. Therefore, the OFT considers that any deterioration in the parties' competitive offering in the mid-tier could also result in Experian expanding further into that segment. Indeed, Experian confirmed to the OFT that it would [].

Conclusion

70. The OFT concludes that the merger will not give rise to any competition concerns in the supply of Bacs software to businesses. The OFT considers that, while Albany is an important competitor to Bottomline, the evidence indicates that the merged entity would continue to face strong competition from a number of other software suppliers and that several of these suppliers would be well-placed to compete for further business in response to a deterioration in the merged entity's competitive offering.
71. Therefore, notwithstanding high margins in the sector, the OFT considers that actual and potential competition from third parties will be sufficient to constrain the merged entity. The OFT also considers that, at least in respect of customers with less sophisticated requirements, the merged entity would also be constrained by e-banking solutions.
72. The OFT has considered narrower customer segments based around different levels of product functionality. Even when considering such narrower customer segments the OFT has not found that competition concerns arise.
73. As regards top-tier requirements, the OFT considers that Albany is, at most, a weak competitor to Bottomline in respect of supply of Bacs software to these customers, such that the merger will have little impact. Bottomline's key competitor in respect of these customers will continue to be Experian.
74. As regards mid-tier requirements, Albany is a more important competitor to Bottomline. However, the third party evidence indicates that there are a

number of other suppliers with the software and expertise necessary to supply mid-tier customers. These include, Microgen, Barron McCann and Fundtech. In the event of a post-merger deterioration of merged entity's competitive offering, these suppliers (together with Experian) would be well-placed to offer alternatives to customers.

75. As regards lower-tier requirements, both Albany and Bottomline compete in the supply to these customers. However, there are a large number of suppliers offering lower tier software. In the event of a post-merger deterioration of the merged entity's competitive offering, these suppliers would be well-placed to offer alternatives to customers. Furthermore, the evidence indicates that the existence and ongoing rapid development of e-banking solutions will continue to exert a constraint on the merged entity as regards lower-tier customer requirements.

Bacs software to bureaux

Shares of supply

76. The OFT was made aware of 13 suppliers of Bacs software to bureaux. Each of the largest suppliers of software to business also supplies software to bureaux.
77. Table 3 below contains Vocalink data for the period June 2011 to May 2012. The table shows the share of indirect submissions to Bacs (that is, submissions on behalf of bureau customers) made via a bureau using each supplier's software. The OFT is mindful that these data provide only a rough proxy for the parties' share of supply of software to bureaux.

Table 3 Bacs Submissions via Bureaux – Share of Submissions

Supplier	Share of Submissions (per cent)
Bottomline	[10-20]
Albany	[0-10]
Combined	[20-30]
Experian	[60-70]
Fundtech	[0-10]
Microgen	[0-10]
Barron McCann	[0-10]
Others	[0-10]
Total	100

Source: Vocalink. Parties' shares do not sum due to rounding.

78. Experian is the largest supplier in terms of number of submissions. As in the supply of software to business, Experian tends to focus on more sophisticated customer requirements and, in part, its high share of submissions is based on a relatively small number of very large bureau clients (albeit Experian also supplies software to some smaller bureaux). Fundtech, Microgen and Barron McCann are each slightly smaller than Albany in terms of share of submissions.
79. Bottomline submitted that, in terms of number of customers, the parties together supply software to around [35-45] per cent of Bacs bureaux but submitted that the parties' share of customer numbers would be lower since many bureaux source from more than one software supplier.

Closeness of competition

80. Similar to software to business, there is a high degree of product differentiation in the supply of software to bureaux, with bureaux requirements varying depending, inter alia, on the size of their business and the sophistication of the service they offer to their customers. In practice, bureau software is usually based on standard business software product, together with an additional 'bolt-on' bureau module. The evidence available to the OFT indicates that the relative positioning of the suppliers to bureaux is similar to supply to business.

81. As regards upper tier customer requirements, third party evidence suggests that Albany is, at most, a weak constraint on Bottomline. []. Third party evidence indicates that Experian is Bottomline's main competitor as regards sophisticated software.
82. As regards mid-tier customer requirements, third party evidence suggests that Bottomline and Albany are competitors to one another. Two mid-tier customers told the OFT that the parties are close competitors. However, in general the evidence from customers indicated that a range of other suppliers compete strongly in this segment, including Fundtech, Microgen, Barron McCann and Mosaic. Evidence from competitors also indicated that a large number of suppliers compete for mid-tier customer requirements.
83. As regards lower-tier customer requirements, third party evidence suggests that Bottomline and Albany both compete but that a range of other suppliers compete strongly in this segment, including Barron McCann, Fundtech and smaller suppliers. Evidence from competitors also indicated that a large number of suppliers compete for lower-tier customer requirements.
84. As with Bacs to business, there are few constraints on competitors' ability to increase volumes significantly in response to increased demand. The OFT considers that the ability of third parties to increase volumes quickly in response to any a deterioration in the merged entity's competitive offering constitutes a strong constraint.
85. Furthermore, since payment software forms a central part of the business of many bureaux (whereas it is often a peripheral back-office matter for many businesses), bureaux are likely to be relatively sophisticated purchasers of software. Accordingly, it is likely that bureaux would be sensitive to any post-merger deterioration in competitive offering and would consider switching to one of the alternative suppliers.
86. In general, only a small number of the customers contacted by the OFT expressed any concerns in relation to the merger. The great majority of customers did not indicate that the merger would materially reduce their choice of software suppliers.

Entry/Expansion

87. The evidence available to the OFT has found that scope for entry and expansion in the supply of software to bureaux similar to the supply of software to business.

Conclusion

88. The OFT concludes that the merger will not give rise to any competition concerns in the supply of Bacs software to bureaux. The OFT considers that, while Albany is a significant competitor to Bottomline, the evidence indicates that the merged entity would continue to face strong competition from a number of other software suppliers and that several of these suppliers would be well-placed to compete for further business in response to a post-merger price increase or other deterioration in the merged entity's competitive offering. Therefore, notwithstanding high margins in the sector (see paragraph 66 above), the OFT considers that actual and potential competition from third parties will be sufficient to constrain the merged entity.
89. Even when considering narrower customer segments, no competition concerns arise. As regards upper tier requirements, the OFT considers that Albany is, at most, a weak competitor to Bottomline. As regards mid-tier and lower tier customer requirements, there are a number of other strong competitors, including Microgen, Barron McCann and Fundtech. Furthermore, each of the competitors could increase volumes with relative ease in the event of a post-merger deterioration in competitive offering by the merged entity.

White-label software to banks

90. Three high street banks (Barclays, HSBC and RBS) offer white-label payments software to their business customers. Barclays and HSBC are supplied by Bottomline and RBS is supplied by Fundtech.
91. Bottomline submitted that no competition concerns arise in respect of the supply of white-label software to banks given the wide range of viable suppliers and the buyer power of banks. Albany has only previously bid in one white-label tender process. Bottomline also bid in that tender, along with Fundtech. Other tender processes have attracted several third party

software suppliers.

92. Two banks expressed some concern that the merger could reduce the choice of white-label software suppliers. However, one of these banks noted that there were other viable suppliers. The other bank had previously excluded a third party supplier from its tender process on the basis that they lacked a specific functionality that that supplier has now added to its product portfolio.
93. The balance of third party evidence suggested that there are a range of viable suppliers of white-label software. Third parties noted that, since white-label software is aimed at small and medium sized businesses, it is generally only required to have lower tier or mid-tier functionality that can be provided by a range of suppliers. Furthermore, RBS's selected Intersoftware (now Fundtech) to supply its white-label software at a time when it was a very small software supplier. This indicates that it is not only the largest suppliers that are viable bidders for bank white-label contracts.
94. The OFT also considers that banks have a substantial degree of buyer power when procuring white-label software, arising from the fact that it is the banks that have the ongoing relationships with business customers. In this capacity, the banks are an important source of referrals for software suppliers and a competitor to software suppliers as regards their e-banking offering. The banks could retaliate against any post-merger deterioration in the merged entity's white-label competitive offering either by seeking to persuade more customers to use e-banking rather than Bacs software and, in respect of upper tier customers, by referring them to a different software supplier.
95. Accordingly, given the wide range of viable alternative suppliers and the buyer power of the banks, the OFT does not consider that any competition concerns will arise in respect of the supply of white-label software to banks.

FPS software to business

96. Bottomline was unable to provide share of supply data in respect of FPS software to business. Bottomline submitted that no competition concerns arise given that there are several third party suppliers and that more

suppliers could be expected to enter in the event that the market grows from its current small base.

97. The number of FPS submissions is less than one per cent of the number of Bacs submissions. As outlined above, currently only Barclays customers are able to use software to make direct submissions to the FPS network. However, other banks have told the OFT that they are considering enabling their customers to make direct FPS submissions.
98. Each of the main suppliers of Bacs software to business (Experian, Fundtech, Microgen and Barron McCann) offers FPS software to business. Furthermore, the balance of third party evidence indicates that it would be relatively easy for other Bacs software suppliers to expand into FPS software in response to increased demand. In addition, most e-banking solutions offer the facility to make FPS payments. Several customers told the OFT that they use e-banking to make FPS payments. Accordingly, as with Bacs, the OFT considers that, at least in respect of customers with less sophisticated requirements, the merged entity would also be constrained by e-banking solutions. The OFT did not receive evidence indicating that bureau services are a strong constraint on suppliers to FPS software to businesses.
99. No customers expressed any concerns in respect of the effect of the merger on the supply of FPS software.
100. Given the strength of actual and potential competition from third party suppliers and the lack of customer concerns, the OFT does not consider that the merger gives rise to concerns in respect of the supply of FPS software to businesses.

FPS software to bureaux

101. Bottomline was unable to provide share of supply data in respect of FPS software to business. However, the parties' activities in this sector are minimal with each earning less than £10,000 revenue in the last year. Indeed, none of Albany's bureau customers are actively making FPS submissions. Third party evidence suggests that there are a number of viable alternatives to the parties' software. Each of Experian, Fundtech, Microgen and Barron McCann is able to supply FPS software to bureaux. No customers expressed any concerns in respect of the effect of the

merger on the supply of FPS software to bureaux.

102. Given the limited scope of the parties' activities, the availability of several alternative suppliers and the lack of customer concerns, the OFT does not consider that the merger gives rise to concerns in respect of the supply of FPS software to businesses.

Bureau services

103. Both Bottomline and Albany are active in the supply of bureau services. Bottomline submitted that there are around 750 bureaux, including very large suppliers such as ADP, Capita, Centrefile, Ceridian, Liberata and Logica. Bottomline submitted that the parties' presence in bureau services is limited. In particular, Albany has only recently started offering stand-alone bureau services and achieved bureau revenue of [] in the last year.
104. Third parties confirmed that the parties are very small players in bureau services and that merger would not be expected to have any impact on competition. The evidence was the same both in respect of Bacs and FPS bureau services. Accordingly, the OFT considers that the merger will not give rise to any competition concerns in respect of bureau services.

OTHER THEORIES OF HARM

Vertical input foreclosure

105. The OFT found that the merged entity would have neither the ability nor the incentive to engage in vertical input foreclosure to banks. There are a range of alternative suppliers of software to banks. Banks are important business partners for the software suppliers and would be able to retaliate effectively against any attempted foreclosure strategy.
106. The OFT found that the merged entity would have neither the ability nor the incentive to engage in vertical input foreclosure to bureaux. There are a range of alternative suppliers of software to bureaux. The merged entity will have only a small presence in bureau services such that it could not be expected to capture a significant number of customers who switched away from a foreclosed bureau.

Coordinated effects

107. The OFT considered whether the merger could result in coordination between the merged entity and Experian. However, the OFT considers that there are a number of strong third party suppliers in each area of overlap where there is strong competition between the parties pre-merger. Furthermore, even in those areas where Experian and the merged entity would be the largest suppliers, the third party suppliers could increase sales quickly in response to any deterioration in competitive offering. Accordingly, the OFT does not consider that the merger could be expected to give rise to competition concerns based on coordinated effects.

108. No third parties expressed any concerns related to vertical foreclosure or coordinated effects.

THIRD PARTY VIEWS

109. Specific third party views have been discussed above where relevant. The OFT contacted a very large number of customers in this case and only a few of these customers expressed any concerns in respect of the merger. Three competitors expressed concerns but, in general, the competitors' responses indicated that the merger could be expected to increase the intensity of competition in payment software.

ASSESSMENT

110. The parties overlap in the supply of payment software and bureau services. The merger qualifies on the basis of the share of supply test. The OFT has assessed the transaction based on the national supply of:

- Bacs software to businesses
- Bacs software to bureaux
- white-label software to banks
- FPS software to businesses
- FPS software to bureaux, and

- bureau services (as a whole and Bacs and FPS separately).

111. As regards Bacs software to businesses and bureaux, the OFT considered both the market as a whole and customer segments based on upper, mid- and lower tier functionality requirements. The OFT found that Albany was not a strong competitor to Bottomline in respect of upper tier customer requirements. In respect of lower and mid-tier customer requirements, the OFT found that a number of third party suppliers are strong competitors and would be able to supply additional customers in response to any post-merger deterioration in the merged entity's offering. As regards supply to businesses, the OFT also found that e-banking would exert an additional constraint on the merged entity, at least in respect of lower tier customer requirements.
112. As regards white-label software to banks, the OFT found that there will be several viable third party bidders for white-label contracts and that the banks have substantial buyer power.
113. As regards FPS software to businesses and bureaux, the OFT found that a number of third party suppliers are strong competitors and would be able to compete to supply additional customers in response to any post-merger deterioration in the merged entity's offering. As regards supply to businesses, the OFT also found that e-banking would exert an additional constraint on the merged entity, at least in respect of lower tier customer requirements.
114. As regards the supply of bureau services (as a whole and separately based on Bacs and FPS), the OFT found that the parties are small suppliers and that the merged entity will continue to face competition from several much larger bureaux.
115. The OFT found that the merged entity would have neither the ability nor the incentive to engage in input foreclosure in the supply of software to banks or bureaux. The OFT also found that coordination between the merged entity and Experian would not be sustainable.
116. Accordingly, the OFT does not believe that it is or may be the case that the merger may be expected to result in a substantial lessening of competition

within a market or markets in the United Kingdom.

DECISION

117. The transaction will not be referred to the Competition Commission pursuant to section 33(1) of the Act.