Anticipated acquisition by Acergy SA of Subsea 7 Inc

ME/4689/10

The OFT's decision on reference under section 33 given on 21 December 2010. Full text of decision published 2 February 2011.

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 commercial confidentiality.

PARTIES

1. **Acergy S.A (Acergy)** is an offshore engineering, construction, and maintenance company, working for oil and gas companies worldwide. This involves engineering, project management, procurement, fabrication, installation, construction, commissioning and maintenance of fixed surface and subsea production facilities, offshore pipelines and associated infrastructure. Acergy's 2009 UK turnover was [ ]

2. **Subsea 7 Inc. (SubSea 7)** is a subsea engineering and construction contractor which operates worldwide. SubSea 7 provides project management, engineering, procurement, fabrication, installation and commissioning services for the development of oil and gas production facilities on the seabed and the tie-back of these facilities to fixed or floating production platforms or to shore facilities. SubSea 7 also provides integrity management, inspection, repair and maintenance services for these facilities throughout their lifetime. SubSea 7's 2009 UK turnover was [ ].

TRANSACTION

3. On 20 June 2010 the parties entered into a business combination agreement. The all-share agreement is intended to be effected by means of

a Cayman Islands scheme of arrangement of SubSea 7 with Acergy as the acquirer and SubSea 7 as the target. Under this scheme of arrangement, SubSea 7 shareholders will receive new shares from Acergy. Following completion, Acergy will hold 54 per cent ownership stake in the merged entity and SubSea 7 will hold 46 per cent stake. The parties notified the transaction to the Office of Fair Trading (OFT) on 23 September 2010. The OFT's extended administrative deadline for deciding whether to refer the merger to the Competition Commission (CC) was 6 December 2010.

JURISDICTION

4. As a result of this transaction, Acergy and SubSea 7 will cease to be distinct. The UK turnover of SubSea 7 (the target company) exceeds £70 million so the turnover test contained in section 23(1)(b) of the Enterprise Act 2002 (the Act) is satisfied. Therefore the OFT believes that it is or may be the case that arrangements are in progress or in contemplation which, if carried into effect, will result in the creation of a relevant merger situation.

BACKGROUND

5. The parties provide offshore oilfield services, in particular between the seabed and the surface of the water. They plan, design and deliver a number of project types by using a number of different vessels and capabilities on a customised basis.

6. Acergy operates 21 vessels (owned and long-term chartered) - 10 pipelay vessels, four diving support vessels (DSVs), four construction vessels, three survey vessels. In addition to these 21 vessels, Acergy also has remotely operated vehicle (ROVs) and support vessels (ROVSVs) and smaller vessels such as cargo barges.

7. SubSea 7 operates 20 vessels (owned and long-term chartered) - eight pipelay vessels, six diving support vessels, three ROVSVs, a number of ROVs and three construction vessels.

8. Each type of vessel is used for specific activities which are required for a given project. For example, pipelay vessels are used for the installation of pipelines. DSVs are used in order to perform certain tasks, for inspection, construction or repair purposes and frequently to support subsea

construction of pipelines and their components. In addition, for remote intervention work, ROVs and ROVSVs are used to perform inspections, construction and repairs. However, the parties made the point that, more recently, ship-owners were seeking to insulate themselves from the downturns in the oil and gas industry by building multi-purpose vessels that can operate across several activities.

MARKET DEFINITION

Product scope

Segmentation by project type

9. The parties argue that the relevant product market is the supply of all OECM (Offshore Engineering, Construction and Maintenance) services. The parties consider that projects for conventional/refurbishment,[1] trunklines, [2] LOF,[3] and SURF[4] all fall within a single overarching OECM market and do not constitute distinct product markets. In relation to other offshore oilfield services such as surveying, or drilling the parties state that these are not part of the overall OECM market.

10. In particular, the parties argue that the majority of the North Sea region's oil fields (in particular those in UK waters) are in shallow water (less than 300 metres depth) so customers are free to substitute between SURF and conventional transmission projects (for example, the use of tankers rather than pipeline). In addition, the parties argued that although each project is different, the facilities needed to establish and support an offshore field

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[1] 'Conventional' is the fabrication and installation of fixed platforms and pipelines and umbilicals, typically in shallower water. 'Conventional refurbishment' refers to maintenance and refurbishment of conventional facilities.

[2] 'Trunklines' (transporting gas or oil over long distance) involves the installation of large diameter export and transmission pipelines (either from offshore oil or gas field to the shore or from producing country to consumer country). Trunklines typically feature pipelines in excess of 24 inches diameter.

[3] 'Life of Field' (LOF) encompasses the integrity management of installed subsea infrastructure, including engineering studies and risk assessments, planned inspection, routine maintenance, repair, incremental development and, finally, abandonment. Such services are generally provided by DSVs (in shallow waters – typically, less than 300 metres) or ROVs in deeper waters.

[4] 'SubSea Umbilicals, Risers and Flowlines' (SURF) is focused on the development of subsea infrastructure for the purpose of connecting oil and gas wells on the seabed to surface oil and gas facilities. This involves the engineering, procurement, fabrication, installation and commissioning of subsea pipelines, risers, umbilicals and various other subsea structures.

require most, if not all, of the OECM capabilities mentioned above to be deployed at one time or another. Therefore, the parties submitted that OECM capabilities, as they are applied to the various project types, represent a single market.

11. However, evidence from the parties' internal documents (Acergy Feb 2010) tends to suggest that Acergy considers the market to be segmented between different types of projects (see paragraph 9 above). Specifically, in relation to SURF projects Acergy's internal documents show the segment as consisting of four SURF leaders (Technip, Acergy, SubSea 7 and Saipem), three challengers (AllSeas, Helix and Heerema) and a range of smaller firms, that is, as constituting a separate area of activity with certain competitive dynamics.

12. Moreover, the OFT's investigation did not support the parties' contentions that the market could be described as all OECM. Even in relation to narrower project types, such as SURF and LOF, third parties were more concerned from a demand-side perspective with the capability of the parties' operations for example, vessel capability, and did not consider it appropriate to view the market by project type. The OFT therefore considers segmentation by vessel type.

Segmentation by vessel type/activity

13. Furthermore, the parties described many of their vessels and those of their competitors as multi-functional. In particular, the parties argued that pipelay vessels, DSVs and ROVSVs can be used in both SURF and wider OECM projects. In shallow water, such as the UK Continental Shelf (UKCS), DSVs and remotely operated vessels can sometimes be substituted. The parties contended that, on this basis, many suppliers can carry out many of the functions within the OECM market.

14. However, from its market investigation, the OFT understands that there are often specific projects that only vessels with specific capabilities can perform. In particular, customers mentioned diving services, where DSVs are usually used and pipelay projects where pipelay vessels are needed for the construction and installation of pipelines. Within pipelay projects, third parties mentioned that there are specific vessels capable of laying either

small or large diameter pipelines, as well as vessels with capabilities to lay rigid or flexible pipes.[5]

15. Furthermore, evidence provided by third parties shows that the execution of a project depends on the capability of a specific vessel, which cannot be easily substituted with another vessel with different capabilities. In this respect, the OFT did not receive any strong evidence from the parties indicating that vessels of different capabilities (DSVs, pipelay vessels, construction vessels and ROVSVs) could be substituted with each other to perform certain services.

16. Finally, even projects that require more than one vessel, such as installation of a pipeline where a pipelay and diving support vessels are often required, or a project that requires a DSV, a construction vessel and a ROVSV, the OFT understands that each vessel used will perform a specific activity according to its capabilities and no substitutability between these vessels exists.

17. Therefore, based on the evidence before it, the OFT notes that there is no or limited substitutability between different categories of vessels (DSVs, pipelay, ROVSVs) for the fulfilment of specific projects.

18. In summary, the OFT has assessed whether an overall OECM market is appropriate, segmentation by project type or vessel type/activity is a more appropriate framework for assessing this transaction. In light of the third party responses and in view of its investigation, it has therefore considered, on a cautious approach, appropriate to assess the transaction through the capabilities of the parties' vessels and in relation to the specific services that each category of vessel is often used for. In this case, based upon the concerns put to the OFT, the OFT believes that the appropriate frame of reference is to consider separately:

    - the provision of diving services/DSVs
    - the provision of pipelay services/vessels and within pipelay services, the provision of integrated small diameter rigid pipelay and diving services
    - the provision of construction services/vessels and
    - the provision of remote intervention services using ROVs/ROVSVs.

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[5] The OFT has considered the implications for its assessment of different types of pipelay services within its unilateral effects analysis (see below).

Geographic scope

19. The parties consider that the supply of OECM services, whether considered as a single market or a series of sub-markets, is global. In particular they argue that service providers are active globally, competition takes place on a world-wide basis, location of headquarters is not relevant in contract allocation, vessels are commonly moved from one region to another in response to contract wins, and engineering and project management teams manage projects in distant locations.

20. On the demand side, the parties argue that oil companies often manage their portfolios globally, setting up contracts with several large global customers. In addition, vessels are mobile on the supplier side, although there are some lost revenues while a vessel is in transit. The parties claimed that few vessels had remained in the same region for the most recent five-year period.

21. In particular, the parties provided evidence of vessels being systematically switched between regions and listed examples of competitors' vessels transiting into (and out of) the North Sea area.

22. Third parties had mixed views on the geographic scope of the market. Some stated that there was a global market for some types of vessels whereas others were less sure of this. Other third parties stated that any potential competition concerns were not affected by whether or not this was a global market since patents (for pipelay) or availability of sufficiently advanced DSVs limited competition however the market was defined geographically.

23. Other third parties have suggested that for some contracts, such as larger EPIC subsea construction, a number of vessels are required (up to five from a single operator) and that only firms with established shore side infrastructure can operate this many vessels in the North Sea. It may also be uneconomic, some third parties argued, logistically to arrange to move so many vessels at one time. Other customers have said that DSVs cannot move easily due to the lack of shore side infrastructure. That said, no third parties suggested that the UKCS should be considered on its own, but rather they considered it should be viewed as part of the wider North Sea area.

24. The parties claimed that, looking ahead, few of their vessels were planned to remain exclusively in the North Sea. They also argued that their vessels had moved between regions regularly and in the last year more of their vessels had moved in and out of the North Sea than had stayed in the North Sea. However, the OFT is not confident that the movements of vessels in and out the North Sea have been in response to changes that equate to no more than five or ten per cent price change. The parties have presented some data on competitors transiting vessels although the size of the demand shift required to induce this was unclear to the OFT.

25. Finally, the parties argued that they do not need their own port facilities to service their customers' requirements in the North Sea. To support projects in the North Sea, OECM contractors use a wide variety of commercial ports in all countries bordering the North Sea, where they use commercially available services from a range of specialist marine support and logistics companies.

26. Based on the evidence available to it, on a cautious approach, the OFT cannot rule out the possibility that the relevant geographic market may be no wider than the North Sea. In particular, the OFT understands that rates for similar projects in other areas of the world are different (generally lower) than the rates applicable in the North Sea. In addition, evidence available to the OFT, shows that trends of margins are different in various regions as well. Therefore, the OFT concludes that the relevant geographic frame of reference may be no wider than the North Sea. It is important to note, however, that in applying this geographic scope the OFT has still considered the constraint posed on North Sea operators by firms based outside the North Sea, such as bids made using vessels that are located outside the North Sea.

UNILATERAL EFFECTS

Introduction

27. As stated in the Mergers Assessment Guidelines, '[t]heories of harm are drawn by the Authorities to provide a framework for assessing the effects of a merger and whether it would lead to a substantial lessening of competition. They describe possible changes arising from the merger, any

impact on rivalry and expected harm to customers as compared with the situation likely to arise without the merger'.[6]

28. Before setting out its theories of harm in relation to this investigation, the OFT has summarised the share of supply information provided by the parties by reference to the following areas:

    i. share by project type
    ii. share by vessel type (based on number of days in North Sea).

Shares of Supply

Shares by project type

29. The parties provided market share data in relation to types of projects that they overlap in. In particular, the parties submitted that their combined share of the 2009 global OECM market based on revenues was [five-10] per cent with Technip having [five-10] per cent and Saipem [10-20] per cent. The parties listed another 15 principal competitors. However, given the bidding nature of the market, the parties commented that shares of supply in any one year were not especially illustrative of market structure or competition.

30. In relation to SURF projects, internal documents pointed to a different view of the global market. These tended to indicate that Technip, Acergy, Subsea 7, and Saipem are the biggest global firms in this market and that the merged entity would become the largest global operator ([20-30] per cent combined share). Evidence from internal documents showed that concentration in SURF projects, with only four significant players, was perceived to effectively limit the scope for future consolidation.

31. In the North Sea the parties estimated that their 2009 OECM market share was [20-30] per cent with an increment of [five-15] per cent. However, they had no revenue for conventional refurbishment or trunklines for this year and only minimal revenue for conventional projects. In relation to SURF, the parties estimated their combined market share is [35-45] per cent with an increment of [10-20] per cent, and in relation to LOF [30-40] per cent with an increment of [five-15] per cent. The parties estimated that Technip had shares of [20-30] per cent for SURF and [15-25] per cent for

[6] OFT/CC Mergers Assessment Guidelines, paragraph 4.2 (OFT 1254).

LOF, whilst Allseas had [five-10] per cent for SURF and Saipem had [five-10] per cent.

32. Based on the market share data, it is clear that the parties are two of the three largest operators in SURF and LOF in the North Sea. However, as set out in paragraph 17 above, the OFT's investigation has not shown that a market based on types of project is appropriate for an assessment of this merger. It considered it more appropriate to examine the merger through the capabilities of the parties' vessels and in relation to the specific services that these vessels are often used for.

Shares by vessel type/activity (based on days in the North Sea)

33. The parties stated that it was more relevant to analyse the time their vessels spend in the North Sea.[7] Based on the data provided,[8] the OFT estimated that the parties have the largest number of vessel days in the North Sea in the last three years with a combined estimated share of 34.6 per cent (increment of 13.5 per cent), with DeepOcean following with [10-20] per cent, Technip with [five-15] per cent.

34. In relation to the share of days of each type of vessel for each operator, the parties' estimated combined share of vessels days in the North Sea for DSVs is 44 per cent, Technip with [20-30] per cent and Bibby with [10-20] per cent. For pipelay vessels the parties' combined estimated share is 32.7 per cent, followed by DeepOcean with [10-20] per cent, Technip with [10-20] per cent and Saipem with [five-15] per cent. Finally for ROVSVs the parties' combined share is 29.3 per cent followed by DeepOcean with [15-25] per cent, Fugro with [five-15] per cent and DOF with [five-15] per cent.

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35. As measured by the data on the number of vessels days in the North Sea:

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[7] The parties provided information on the number of vessels that they and some competitors owned or chartered globally. However, the OFT believes that the shares by vessels days in the North Sea were the most appropriate proxy for it to base its assessment of the merger.

[8] The data did not include trunkline pipelay vessels and other OECM support vessels such as Heavy Lift vessels.

- the merger gives rise, on a cautious approach, to a reduction in significant DSV providers from four to three.[9]

- The position is similar for pipelay vessels, although the combined share is more modest. In particular, the OFT received a number of third party views, where concerns were raised about the merger giving rise to a reduction in competition in small diameter pipelay projects from 'three to two' as a result of the merger.

- There were no third party concerns in relation to projects with ROVSVs and projects with construction vessels involved. Evidence available to the OFT indicated that there are a number of competitors bidding for each of these projects, as well as significant new entry planned. The OFT did not consider these projects any further in its assessment.

36. Therefore, the OFT has assessed whether the merger may create competition concerns in the following areas:

    i. unilateral effects in relation to the supply of DSV services in the North Sea
    ii. unilateral effects in relation to the supply of pipelay services in the North Sea
    iii. unilateral effects in relation to the supply of integrated services both pipelay and DSV for small diameter pipelay projects in the North Sea.

37. In relation to each of these theories of harm, the OFT has assessed the transaction by reference to the above share of supply information and conducted an analysis of the closeness of competition between the parties' vessels, capabilities and activities and the competitive constraints they are likely to face post-merger. The discussion of theories of harm is then followed by an assessment of countervailing factors such as, buyer power and barriers to entry.

[9] Based on third party views Well Ops was not considered by customers a competitor to the parties.

Diving/DSV services

38. The parties provided a list of 56 vessels that had been active in the last three years in the North Sea, including 16 DSVs. Based on this list Acergy has three of these DSVs, SubSea7 has four, Technip has five, Bibby has three, and Saipem has one. On the basis of these figures, the merger represents a 'five to four' in diving operators in the North Sea, or a 'four to three' in relation to diving operators with more than one DSV in the North Sea. The parties have a combined share of supply of 44 per cent of DSVs.

39. In a subsequent submission the parties stated that the list of 56 North Sea vessels was merely indicative, and updated the list to show 131 vessels. Based on this list, there were 20 DSVs that had operated in the North Sea in the last three years, and the parties have seven out of the 20 DSVs, resulting in a combined market share of 35 per cent in the North Sea. Technip has five DSVs, Bibby has three, Well Ops/Helix has two and Saipem, GB/Smith SubSea, and Noordhoek have one each.

40. They added that the 16 or 20 vessels, as identified by the OFT, were not the total supply side of the market, as these were only DSVs which happened to be available in the North Sea between 2008-2010. In particular, the parties argued that DSVs operated in a global market and could easily transit from one region to another. They provided a number of examples of vessels moving between different regions globally including the North Sea. In particular, the parties provided a list of international DSV transits (by the independent ship broker Kennedy Marr).

41. However, the OFT notes that the reasons for these DSV transits were unclear – many of the DSVs recorded in the Kennedy Marr list as entering or leaving the North Sea in recent years were not recorded in the SOR data[10] as having worked in the North Sea. Therefore, the OFT cannot exclude that they may not have been competing with (or intending to compete with) the parties.

42. In addition, the parties submitted a list (constructed by Kennedy Marr) of over 50 DSVs globally, of which it was believed that 41 had actually provided diving services in the North Sea. However, some third parties stated that many of the vessels in the Kennedy Marr global list would not

[10] Data from Strategic Offshore Research Ltd (SOR) provided by the parties.

meet the requirements of marine assurance providers and would need significant upgrades to work in the North Sea area.

43. Based on the above, the OFT could not rule out that the parties were close competitors in the provision of diving services in the North Sea and examined whether there are other firms capable of constraining the merged entity in the provision of diving services in the North Sea.

Alternative companies in the provision of DSV services

44. Apart from the list of over 50 DSVs mentioned above, 41 of which the parties believed had worked in the North Sea at some time, the parties also provided a representative list of projects using DSVs where they argued that a significant number of competitors bid against them. In particular, the parties stated that there were at least five recent projects where more than five firms bid for each of these. In addition, evidence provided to the OFT by the parties showed that Acergy, SubSea 7, Technip and Bibby bid for all 16 projects for which the parties provided information.

45. The OFT's market investigation confirmed that, apart from the parties, Technip, Bibby, ISS Mermaid, DOF Subsea and Saipem placed bids against the parties in a number of projects. In addition, customers confirmed that they received more than five bids for their projects and stated that these diving operators were considered equally and seriously in all tenders that they had bid for, and that new entrants such as Noordhoek and ISS Mermaid were effective competitors having recently won DSVs projects.

46. In relation to demand for DSVs in the North Sea, the parties argued that this was in decline – falling from 3,800 vessel days in 2008 to 2,600 in 2009 and 2,300 in 2010.

47. However, the parties argued that the supply of DSVs in the North Sea was increasing. In particular, they provided internal documents (SubSea 7 presentation dated 12 January 2010) which listed 40 global Class 1 DSVs, of which the parties had 10 (although this list missed some of those in the original list of 16 active in the North Sea). Several of the vessels in this list had not commenced operation at the time of the presentation but the OFT confirmed with several industry sources that new vessels entered (or were intended to enter) the global or North Sea fleet in 2010 ([ ]) and vessels

were due to commence operation in 2011 or 2012. This was confirmed by third parties.

48. The Subsea 7 internal documents showed that supply for North Sea DSVs would exceed demand during 2011-2014 and these projections were supported by comments from industry participants that stated that DSV day rates were predicted to remain lower in 2011-2013 than they had been in 2009. Some third parties withdrew initial concerns about the impact of the loss of competition in the supply of DSV services arising from the merger when they researched the industry projections on DSV rates.

Conclusion on the provision of DSV services

49. Therefore, based on the evidence available to it, and the lack of third party concerns in relation to the supply of DSV services, the OFT concludes that there are a number of competitors supplying such services in the North Sea and that these can be expected to continue to exercise a competitive constraint on the parties. In addition, the investigation has shown evidence of actual and planned/potential new entry. Therefore, the OFT does not expect the merger to give rise to a realistic prospect of a substantial lessening of competition in the supply of DSV services in the North Sea.

Pipelay services

Small diameter rigid pipes

50. The second theory of harm assessed by the OFT relates to unilateral effects in the supply of pipelay services for projects in the North Sea, specifically, the provision of small diameter rigid pipes. [11]

51. In relation to pipelay services, the concerns of third parties were limited to the provision of small diameter rigid pipes in the North Sea.[12] Third parties contended that there were only three companies that regularly bid for small diameter pipelay contracts in the North Sea, namely Acergy, SubSea 7 and Technip. Therefore, the merger would lead to a reduction from 'three to

[11] Small diameter pipes are generally considered those of around 16 inches or below.
[12] In relation to larger diameter rigid pipelay, the OFT did not receive any third party concerns and evidence presented by the parties showed that there were a number of operators and vessels imposing a competitive constraint to the parties.

two' in terms of major suppliers, with the potential to lead to increased prices or a reduction in service quality.

52. The parties provided the OFT with data[13] which indicated that the two main pipelay vessels of the parties (Acergy's *Falcon* and SubSea 7's Seven *Navica*) are currently competing against each other in relation to bidding for 10 forthcoming small diameter rigid pipelay projects in the North Sea.

53. However, the parties argued that this data was provided to demonstrate historic bidding and vessel movements, and that it was not suitable to seek to rely on it to show trends in relation to future bidding. The parties contended that these data were out of date, with many of these projects having already occurred or being delayed for several years. Some of the projects that were listed as requiring rigid pipe were due to be carried out with other techniques.

54. The parties stated that the merger had no or limited impact on the provision of rigid pipes in the North Sea as the parties do not overlap in this segment or their services are differentiated. This is because, according to the parties, the Acergy Falcon lays only a limited amount of rigid pipe and does not lay any pipe using the reel lay method (the Navica and Apache II are both reel-lay vessels).[14] In particular, the parties argued that Acergy opted to equip itself with vessels and equipment necessary to offer the S-lay technique and flexible solutions.

55. Whilst, the OFT is aware that in the last three years the Acergy *Falcon* has done only limited pipelay work in the North Sea (working only [ ] days in the North Sea since 2007), it has won a contract for 2011 in the North Sea to lay small diameter pipes. In addition, customers considered the Acergy Falcon as being both active in the North Sea and a competitor in this region to Subsea 7's Seven Navica and Technip's Apache II. Consequently, the OFT considers that Acergy Falcon's limited work undertaken in the North Sea may underestimate the competitive impact that the vessel when projects are put out to tender. More specifically, a number of customers told the OFT that they consider the Acergy Falcon

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[13] Data from US-based independent offshore industry publishing company Quest Offshore Resources Inc.

[14] The OFT understands that reel-lay technique is generally used for small diameter pipes and s-lay technique for larger diameter pipes.

(although not a reel lay vessel[15]) to compete closely with these vessels, and more closely than does any other pipelay vessel by virtue of it being (i) a smaller vessel with lower day rates and, as a consequence, (ii) more economical for laying small diameter pipes.

56. In addition, based on the SOR data available to the OFT, the Acergy Falcon, SubSea 7's Seven Navica and Technip's Apache II are the only vessels that have won small diameter pipelay work in the North Sea in the last three years.[16] However, the parties argued that this (SOR) data did not include other pipelay vessels that had been active in the North Sea because they were classified as concentrating on larger diameter pipes. Overall, the OFT could considers that the above evidence shows that the parties compete closely in relation to the provision of small diameter pipes alongside Technip's Apache II.

57. To assess the extent of constraints on the parties' post-merger in the supply of small diameter rigid pipelay services, the OFT considered whether other pipelay operators posed a constraint by reference to those laying (i) flexible pipes and (ii) large diameter rigid pipes before assessing more widely, alternative companies in the pipelay services area. Taking each of these in turn.

Flexible pipes

58. The OFT considered whether operators laying flexible pipes in the North Sea should also be viewed as imposing an effective competitive constraint to the parties in the provision of small diameter rigid pipelay. The parties argued that flexible pipes are a viable alternative to rigid pipes for some applications with flexible pipes comprising ten per cent of all pipes in field developments in the North Sea in the last three years and over 50 per cent of pipes in Brazil. Furthermore, they stated that there were a number of potential options which a customer could utilise and clients would present these to contractors at the tender stage and not make a definite choice until the tender was well advanced.

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[15] The OFT's investigation indicated that SubSea 7 (Seven Navica) and Technip (Apache II) are the only operators that can lay rigid pipe (using the reel lay method) in the North Sea (in particular specialising in delivering small diameter pipes on a single reel)

[16] The SOR data refers to flowline installation projects. However, the OFT believes that flowline installation projects are equivalent to small diameter rigid pipelay projects, as flowline projects in the SOR data refer to the installation of small diameter pipes.

59. However, third parties did not consider flexible pipes as imposing an effective constraint on the parties' post-merger. Specifically, they said that the durability of flexible pipes is much lower with guarantees often lasting only a couple of years. The OFT would expect to see evidence of switching between small diameter rigid pipes and flexible pipes in order to consider them as effective constraints upon each other but it is notable that customers did not provide or mention any examples of switching between the two. Therefore, on a cautious approach, the OFT did not consider that operators laying flexible pipes impose a strong competitive constraint on operators, such as the parties, laying small diameter rigid pipelines.

Large diameter rigid pipes

60. The OFT also considered whether operators laying larger diameter rigid pipes in the North Sea should be viewed as imposing an effective competitive constraint to the parties in the provision of small diameter rigid pipelay. In relation to larger diameter rigid pipelay, evidence available to the OFT showed that operators laying large diameter rigid pipes would not necessarily have the capability to lay small diameter rigid pipes (at a price that would be competitive with the parties). Hence when they have bid for such projects they have to bid with vessels that were too large or expensive to be viable for smaller pipes and have not been successful.

61. Based on the above, the OFT considers that the merger may raise competition concerns in relation to the provision of small diameter rigid pipelay in the North Sea. The OFT has therefore examined below whether there are other potential companies capable of constraining the merged entity in the provision of small diameter rigid pipelay in the North Sea.

Alternative companies

62. The parties submitted that nine firms could lay rigid pipes in the North Sea and that six had done so in the last five years. They listed 13 vessels that have laid rigid pipes in the North Sea region, only two of which were owned by the parties (the Seven Navica and the Acergy Falcon). The list included one vessel for Technip, four for Allseas, five for Saipem, and one for Helix.

63. However, as mentioned above paragraph 51, the SOR data indicate that the Acergy Falcon, Seven Navica and Technip's Apache II are the only

vessels that have worked on small diameter rigid pipelay projects, and this work is the majority of the work done by these vessels. Furthermore, the data on projects completed by these firms suggest that during the summer of each year two, if not all three, of these vessels are present in the North Sea and completing a string of projects consecutively, indicating that the parties and Technip compete closely. Other pipelay vessels are not typically in the North Sea and may be less competitive for smaller projects partly because they have the added cost of transit.

64. Furthermore, the OFT's investigation indicated that many of the vessels listed by the parties in the data referred to in paragraph 62 above had not won any contracts to lay small diameter rigid pipes in the North Sea (any infield pipelay work that they had done was for particular projects that required larger diameters). [ ] confirmed that [ ]. [ ] confirmed that [ ] but [ ]. Therefore, the OFT understands that neither [ ] nor [ ] are strong competitors to the parties for small diameter rigid pipelay projects in the North Sea.

65. In this respect, several customers that were in the process of tendering for construction work that involved small diameter pipelay, or who had recently tendered for such work, said that their choices for this work were effectively reduced from 'three to two' by the merger (some were concerned specifically about this service on its own, while others were more concerned about the provision of such pipelay services in combination with the required DSV services – see paragraphs 68ff below). In addition third parties stated that reputation and commercial experience of operator are key factors in winning contracts and providing a credible competitive constraint in this market.

Conclusion

66. Based on the evidence available to it, in particular evidence from third parties, the OFT believes that the parties were (with Technip) closest competitors in the supply of services for small diameter rigid pipelay projects in the North Sea area. Although there are at least three further companies bidding for some of these projects, the evidence from the OFT's investigation indicates that the bids of most of these companies have not been successful and that only one further company has had any minor success.

67. Therefore, the OFT concludes that there is a realistic prospect of a substantial lessening of competition in the provision of small diameter rigid pipelay in the North Sea resulting from the merger.

Combination of DSVs and small diameter rigid pipelay vessels – integrated projects

68. The third theory of harm assessed by the OFT relates to the overlap between the parties in the fulfilment of integrated projects combining small diameter rigid pipelay and diving capabilities.

69. According to evidence from the parties and third parties, the OFT understands that there are only three firms, namely Acergy, SubSea 7 and Technip, that have been used in the past for projects that require both small diameter rigid pipelay and diving capabilities in the North Sea in recent years. In addition, based on the information provided by the parties, only these three firms offer an integrated service for small diameter pipelay projects that also require DSVs.

70. In addition, customers expressed specific concerns about loss of choice for contracts that required both DSV **and** small diameter pipelay capabilities. Some customers have argued that it is not efficient for them to tender work to separate operators because of the additional project management required and the risk that some vessels could be delayed, therefore risking holding up the project. Some customers indicated that integrated firms, such as the parties, might be able to increase prices significantly before facing competition from consortia or bids being broken up. Some customers have said that this merger could result in significant price rises in the next few years from integrated firms.

71. In response to these arguments the parties argued that consortium bids tend to be of more importance in other regions than the North Sea, given the relative size and scope of projects in the North Sea. However, the parties provided evidence indicating that a pipelay project will always require services other than pure pipelay and may require other vessels (DSVs, survey vessel, trenching). In addition, the parties provided evidence showing that for a rigid pipelay project, engineering, project management, diving and subsea construction capabilities may be required. In this respect, the parties argued that few, if any, contractors can provide all of the

services required to perform full EPIC[17] projects and parts of the projects generally need to be subcontracted. In relation to diving, the parties argued that the company winning the pipelay work can provide the diving service itself or subcontract it to another company with DSV capabilities, based on the customer's choice. In addition, the parties argued that a company that has diving capability will sometimes still choose to subcontract (some of) the diving scope of the work to a third party for commercial reasons. Furthermore, the parties argued that there are several capable rigid pipelay contractors, which compete to take on pipelay projects, even though they have no diving capability to support the tie in.

72. However, evidence provided by the parties showed that, although consortia are able to bid for the projects globally, only three per cent of bids won in the North Sea in 2007 to 2010 were won by consortia. According to the data the parties have presented competing consortia have not won bids for projects. There was no evidence available to the OFT showing that other operators have been successful in their bids as consortia against the parties for the fulfilment of integrated projects combining small diameter rigid pipelay and diving capabilities.

73. Based on the evidence before it, the OFT understands that there might be a number of companies bidding for large EPIC projects which require pipelay and diving capabilities. In addition, the OFT understands that there might be the possibility for different companies providing separately the diving and the pipelay parts of these projects.

74. In addition, the OFT understands from third parties that some of the North Sea projects combining diving and small diameter pipelay may be capable of being bid for by vessels currently located outside the North Sea. According to third parties, the OFT understands that when more vessels are required (say, pipelay and supporting DSV(s)) the cost and logistics of transiting the two or three vessels needed will be greater than when one additional vessel is needed. So, the barriers to entry for a contractor with

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[17] 'Engineering, Procurement, Installation, Commissioning' (EPIC) is a term used to encompass major construction projects and project management, or delivery of these projects. The parties' work may involve pipelay, umbilical lay, diving (using DSVs), remote intervention (using ROVs and/or ROVSVs), subsea construction (supported by DSVs or ROVs), heavy lift (more than 500T), fabrication (shore based), other services including positioning and tooling services.

no local presence, knowledge, safety clearance, or shore support in the North Sea will be higher.

75. Furthermore, the evidence available to the OFT indicates that the parties (with Technip) are close competitors. Evidence provided by the parties showed that from the 22 largest projects (by value), nine appeared to centre around the small diameter pipelay offering of the Acergy Falcon, Seven Navica or Technip Apache II.

76. In addition, evidence from third parties and example of projects provided by the parties showed that for a company to be successful as an integrated contractor for projects combining small diameter pipelay and related diving capability services in the North Sea area, it often had at least two DSVs available in its fleet. Several small diameter pipelay projects have required two DSVs to be present at the same time as a pipelay vessel to complete a project. Acergy has often had the Acergy Falcon and two DSVs present in the North Sea for most of the summer season.

77. Finally, the OFT's investigation and evidence from third parties revealed that, although there are a number of companies with DSVs active in the North Sea, and a few of these (such as, [ ] and [ ]) bid for small diameter pipelay projects, these companies do not impose a strong competitive constraint on the merged entity, as shown by the lack of, or limited, success in bidding for such contracts. This is because they are not capable of bidding for an integrated service as required by a number of customers. Specifically, [ ] [ ] has [ ] that is often outside the North Sea and [ ].

78. In this respect, the OFT believes that the parties and Technip are the only companies who have pipelay vessels suitable for small diameter rigid pipes and at least two DSVs active in the North Sea. Therefore, the OFT concludes that the merger would result in the reduction from 'three to two' of companies providing an integrated service for small diameter pipelay and related diving capability projects. The OFT concludes that there is a realistic prospect of a substantial lessening of competition in the provision of integrated small diameter rigid pipelay and related diving capability projects in the North Sea.

Barriers to entry

79. The parties argued that there are low barriers to enter the supply of OECM projects in the North Sea. In particular, the parties argued that there were low barriers for operators accessing vessels. Vessels can be chartered or bought, they are movable, can be deployed elsewhere and can be converted for various functions. The parties stated that some vessels such as those used for flexible pipelay can easily be constructed by the adaptation of an existing vessel.

80. In addition, the parties mentioned that 14 firms entered the OECM projects area In the North Sea in the last five years including Bibby, Aker, DOF, ISS, McDermott, Helix, and Global. The parties further referred to six firms that are adding new vessels including three for Technip.

81. The threshold for the OFT to consider that entry or expansion can remove its competition concerns is that entry must be timely, likely and sufficient.[18] Third parties stated that reputation and commercial experience of the operator are key factors in winning contracts and providing a credible competitive constraint in this market. Furthermore, in relation to small diameter pipelay services, the OFT did not receive any third party confirmation of entry occurring. In relation to integrated projects where vessels with different capabilities are often used, the market investigation revealed that in order for a new entrant to be a credible competitive constraint to the merged entity, it should be able to offer an integrated service with a number of different types of vessels in its fleet.

82. The OFT understands that there have been examples of entry in previous years in the North Sea and that entry or expansion might occur for certain projects, in particular in diving services with DSVs. However, the OFT has not been able to verify that these will be sufficient to provide a competitive constraint to the merged entity in all three types of projects discussed above. In addition, the OFT did not receive any evidence in relation to new vessels being built or vessels entering the North Sea for the provision of small diameter rigid pipelay services. The lack of significant evidence submitted by the parties on the effect that previous entries had on the parties' ability to win contracts for small diameter rigid pipelay projects has obliged the OFT to be particularly cautious about accepting entry or

[18] OFT/CC Mergers Assessment Guidelines, paragraph 5.8

expansion as countervailing factors which outweigh its competition concerns in that area.

Buyer power

83. As mentioned in the Merger Assessment Guidelines,[19] the existence of countervailing buyer power will be a factor in making a substantial lessening of competition less likely. In particular, the OFT will assess whether a customer may be able to use its negotiating strength to limit the ability of the merged entity to raise prices.

84. The parties argued that their customers are global, powerful and sophisticated, including large majors and national oil companies. The parties also argued that even their smaller customers have market capitalisation much larger than that of the parties. In particular, the parties argued that customers tend to include 'termination for convenience' clauses to contracts, allowing them to terminate agreements and push for negotiation at any time. In addition, the parties provided examples of customers forcing renegotiation of contracts. Furthermore, the parties argued that they are dependent on their large customers' demand in several regions and customers would react to any price increase in the North Sea by limiting their business with the parties in other regions.

85. In relation to buyer power being exercised through purchasing in other markets, however, the OFT is aware that the North Sea has more independent oil firms than other regions and that these firms may purchase relatively little from the parties in these other markets. This factor is likely to limit the ability to discourage any potential attempt to use market power in the markets where concerns have been identified.

86. The OFT is aware that some customers are sophisticated and pre-merger may have some ability to negotiate prices. However, it is unclear to what degree these customers can negotiate or to what extent this ability may be harmed by the merger. The negotiating position of a customer will be stronger if it can easily switch its demand away from the supplier. Typically the ability to switch away from a supplier will be stronger if there are several alternative suppliers to which the customer can credibly switch. In

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[19] Merger Assessment Guidelines – a joint publication of the Competition Commission and the Office of Fair Trading, September 2010, paragraphs 5.9.1-5.9.8.

this respect, the merger will reduce from 'three to two' the choice of companies in the provision of small diameter rigid pipelay projects with or without diving requirements.

87. An additional factor that may limit customers' ability to exercise buyer power is that the OFT also understands that the market is relatively transparent, in that the parties will be aware of those contracts won by Technip and so the periods for which the Apache II is already 'booked'. This might be expected to influence the price at which the merged entity might bid for other contracts running at the same time. Therefore, the OFT believes that the existence of Technip as the only alternative to the parties post-merger may reduce customers' ability credibly to switch away and any buyer power will not be sufficient (or at least not for all customers) to be a countervailing factor.

THIRD PARTY VIEWS

88. The OFT received a number of comments and concerns from third parties, including competitors and customers. These have been dealt with above where relevant.

89. There were six customers who expressed significant competition concerns about the effect of the merger in the North Sea. Some of these later scaled back their level of concern to varying degrees, in particular in relation to diving services, having examined the merger in more detail or through discussions with other industry participants. However, in relation to small diameter rigid pipelay and the provision integrated services some firms that had significant annual spending on these services in the North Sea remained concerned about the reduction in competition as a result of the merger. One customer stated that they would be adversely affected by the merger but they would accept the cost incurred. Finally, information from third parties indicated that other firms that may tender for small diameter rigid pipelay projects in the future (but had not necessarily done so recently) could also be adversely affected.

ASSESSMENT

90. The parties overlap in the provision of certain offshore oilfield services. The OFT, on a cautious approach, assessed the transaction in relation to the specific services that each type of the parties' vessel is often used for in

the North Sea. In relation to ROVSVs and construction vessels, the OFT did not receive any third party concerns and considered that there were a number of operators able to impose a competitive constraint to the merged entity.

91. In relation to diving services the OFT had prima facie concerns that the merger represents a four to three in significant diving operators (more than one DSVs) in the North Sea with the parties having a combined market share between 35 and 44 per cent of DSVs. However, the market investigation confirmed that, apart from the parties, Technip, Bibby, ISS Mermaid, DOF Subsea and Saipem placed bids against the parties in a number of current projects and customers confirmed that they were all considered seriously. Therefore, the OFT concluded that there are a number of competitors in the provision of diving/DSVs services in the North Sea exercising a competitive constraint to the parties and therefore the merger did not give rise to a realistic prospect of a substantial lessening of competition in this market in the North Sea.

92. In relation to pipelay services in the North Sea, the OFT examined whether the merged entity may have the incentive and ability to increase prices and/or reduce service levels. In its assessment the OFT concluded that operators laying larger diameter rigid pipes and flexible pipes in the North Sea were not imposing a competitive constraint to the parties in the provision of small diameter rigid pipelay. In addition, evidence indicated that Acergy Falcon, Seven Navica and Technip's Apache II were the only vessels that have worked on small diameter rigid pipelay projects and that many of the vessels listed by the parties had not won any contracts to lay small diameter rigid pipes in the North Sea and only one operator had minimal success in the bids they made. The OFT concluded that the parties (with Technip) are closest competitors for small diameter rigid pipelay projects in the North Sea. Therefore, the OFT concluded that there is a realistic prospect of a substantial lessening of competition in the provision of small diameter rigid pipelay in the North Sea resulting from the merger.

93. Finally in relation to integrated projects combining small diameter rigid pipelay and related diving capability services, concerns have been put to the OFT that the merger may lead to increased prices and/or reduced service levels. Based on the evidence before it, the OFT understands that there might be possibilities of different companies providing separately the diving and the pipelay parts of these projects. However, further evidence

showed that the parties are close competitors and Technip is the only other effective competitor for these integrated projects. Therefore, the OFT concludes that the merger results in the reduction from 'three to two' of companies providing an integrated service for small diameter pipelay and diving projects. The OFT concludes that there is a realistic prospect of a substantial lessening of competition in the provision of projects in the North Sea combining small diameter rigid pipelay and two DSVs.

94. The OFT does not believe that entry or expansion would be sufficient to deter or defeat any attempt by the merged entity to exploit any lessening of competition resulting from the merger. In addition, the OFT does not believe that any buyer power will be sufficient to countervail the loss of competition given that there is only one remaining supplier in the market (Technip).

95. Consequently, the OFT believes 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.

UNDERTAKINGS IN LIEU

Introduction

96. Where the duty to make a reference under section 33(1) of the Act applies, pursuant to section 73(2) of the Act the OFT may, instead of making such a reference, and for the purpose of remedying, mitigating or preventing the substantial lessening of competition concerned or any adverse effect which may be expected to result from it, accept from such of the parties concerned undertakings as it considers appropriate.

97. The OFT has therefore considered whether there might be undertakings in lieu of reference which would address the competition concerns outlined above. The OFT's *Exceptions and Undertakings Guidance* states that, undertakings in lieu of reference are appropriate only where the remedies proposed to address any competition concerns raised by the merger are clear cut, and furthermore those remedies must be capable of ready implementation.[20]

[20] See OFT Mergers – *Exceptions to the duty to refer and undertakings in lieu of reference guidance* OFT1122, paragraph 5.7.

98. The parties indicated that in order to remedy any competition concerns identified by the OFT, and to avoid a reference to the CC, they would be prepared to offer undertakings in lieu. Specifically the parties offered to divest:

- (to address any concerns relating to the supply of pipelay services) the Acergy *Falcon* with its existing pipelay spread and

- (to address any further concerns regarding an integrated pipelay/DSV capability) [ ].

99. The OFT considers below the extent to which the parties' proposed divestment package is capable of addressing the competition concerns identified above in a clear cut manner, in accordance with the scheme of the Act as well as the OFT's guidance and decisional practice.

Divestments

100. The OFT considers that the structural undertakings offered to divest certain of the parties' vessels (as identified above) are in principle capable of clearly addressing the competition concerns identified in the decision in relation both to the provision of small diameter rigid pipelay in the North Sea and the provision of integrated service for small diameter rigid pipelay and diving projects in the North Sea.

101. However, the OFT believes that such a divestment will remedy the substantial lessening of competition only if the effect of implementation of the remedy is to recreate the competitive constraint which is lost by the merger – that is, a third player (alongside Technip and Subsea 7) with at least one pipelay vessel and at least two DSVs operating in the North Sea.[21]

102. Therefore, the OFT considers it necessary that either:

- the Acergy Falcon is divested to an existing diving operator in the North Sea with at least two DSVs in the North Sea, or

[21] The OFT understands that Acergy generally has two DSVs active in the North Sea.

- the Acergy Falcon and one of the DSVs identified in paragraph 98 above is divested to an existing diving operator in the North Sea with one DSV in the North Sea area.

103. In this way, the OFT considers that the undertakings in lieu will remedy the competition concerns identified above by allowing the potential purchaser to impose the same competitive constraint on the merged entity that the parties did on each other, and on Technip, pre-merger.

Need for an up-front buyer

104. The OFT considered whether it was appropriate in the circumstances of this case to require that the relevant divestment(s) be made to an up-front buyer.[22]

105. The OFT will seek an up-front buyer where the risk profile of the remedy requires it, for example, where the OFT has reasonable doubts with regard to the ongoing viability of the divestment package and/or there exists only a small number of candidate suitable purchasers.[23]

106. The parties submitted that an up-front buyer requirement would not be appropriate in this case, since they believe there are more than five identified suitable potential purchasers, the parties have clearly expressed their commitment and ability to deliver the stated undertakings in lieu, and there are no questions about the commercial attractiveness of the assets to be divested. However, if the OFT considered it necessary, the parties stated that they would be willing to accept that the relevant divestments be made to an up-front buyer.

107. In this case, the OFT considered that an up-front buyer requirement was required for the following reasons.

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[22] An up-front buyer requirement means both that the proposed purchaser will be contractually committed by the time the OFT accepts the undertakings in lieu such that the OFT can be confident before relinquishing its duty to refer that there is actually a suitable buyer, and the OFT is then able to consult publicly on the suitability of the actual proposed divestment purchaser, as well as any other aspects of the draft undertakings, during the public consultation period.

[23] See OFT Mergers – *Exceptions to the duty to refer and undertakings in lieu of reference guidance* OFT1122, paragraph 5.33.

- The OFT believes that there are a reasonably small number of potential purchasers that, even after acquisition of the vessel(s), would be capable of providing small diameter rigid pipelay and diving services in the North Sea in such a way as to restore pre-merger competitive levels. This reflects the fact that reputation and commercial experience of operators are important factors in winning contracts and providing a credible competitive constraint in this market. Use of the upfront buyer mechanism has the advantage of enabling the OFT to market test the proposed purchaser at the time it consults on the text of any undertakings in lieu.

- The parties' offer involves divestment of the Acergy *Falcon* as the pipelaying vessel. [ ]. Given that the undertakings in lieu offer considered by the OFT did not extend alternatively to sale of the Subsea 7 Navica, [ ], the OFT considers that the most appropriate way of handling potential divestment risk in relation to the saleability of the *Falcon* is through the upfront buyer mechanism. [24] If it becomes evident within a specified period that [ ], then the OFT would reactive its duty to refer the merger to the CC.

108. Therefore, the OFT concludes that it is appropriate to suspend its duty to refer only on the basis that it will seek an up-front buyer for the divestment remedy in this case.

109. As a result of the above considerations, the OFT will accept undertakings in lieu of reference only when the parties have agreed either:

- a provisional sale of the Acergy Falcon to a buyer that already has at least two DSVs operating in the North Sea or

- a provisional sale of the Acergy Falcon and any one of the [ ] DSVs identified by the parties in paragraph 98 to a buyer that already has at least one DSV operating in the North Sea

[24] See the *Exceptions and undertakings* guidance, ibid, paragraph 5.3.4, in which the OFT states: 'the certainty provided for by the upfront buyer mechanism may provide latitude for exploration of a remedy option that the OFT would not feel confident accepting in a non-upfront context. For example, certainty around saleability becomes less important where the OFT retains the ability to refer should a suitable purchaser not be found within a limited, specified period.'

such that a divestment in either case will allow the divestment purchaser to provide a sufficient competitive constraint to remedy the substantial lessening of competition created by the merger.

Conclusion on undertakings in lieu

110. As the parties have offered undertakings in lieu of reference that the OFT considers are in principle clear-cut and capable of restoring pre-merger levels of competition, the OFT considers it appropriate to suspend its duty to refer this case while it considers further whether to accept these in lieu of reference under section 73 of the Act.

DECISION

The OFT's duty to refer the anticipated acquisition by Acergy of SubSea 7 to the Competition Commission pursuant to section 33 of the Act is therefore suspended because the OFT is considering whether to accept undertakings in lieu of reference under section 73 of the Act.