

## 2 Conclusions

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## **The reference**

2.1. On 9 May 2002, the Secretary of State for Trade and Industry referred to us, under the merger provisions of the Fair Trading Act 1973 (the Act), the acquisition by G4F of TWC.

2.2. We were asked to investigate and report on the following questions:

- whether enterprises carried on by or under the control of G4F will cease to be distinct from enterprises carried on by or under the control of TWC (at least one of which is carried on in the UK) and whether the value of the assets to be taken over exceeds £70 million and, if so, whether a merger situation qualifying for investigation arises; and
- whether, if events so require, the actual results of those arrangements are the creation of a merger situation and, if so, whether a merger situation qualifying for investigation arises.

2.3. In either case, we were asked whether the creation of that situation may be expected to operate or (if events so require) operates against the public interest.

2.4. The full terms of reference are set out in Appendix 1.1.

2.5. The Press Release issued by the Department of Trade and Industry with the reference quoted the Secretary of State for Trade and Industry as stating:

The Director General of Fair Trading (DGFT) has advised me that this acquisition may raise competition concerns in the markets for the provision of transportation and custodial services. The transaction would bring together the leading suppliers of these services in the UK. The DGFT concludes that there is a clear possibility that the merger would substantially lessen competition for future contracts.

We were asked to report by 30 August 2002, subsequently extended to 27 September 2002.

## **The companies involved**

### **The G4F companies**

2.6. G4F is a Danish company, listed on the Copenhagen Stock Exchange. In 2001, G4F's worldwide turnover was £1.8 billion, and net assets were £229 million as at 31 December 2001. The company has three main business divisions: Global Solutions, Security Services and Safety Services.

2.7. Global Solutions are delivered through GSL, a UK company with subsidiaries in the UK and overseas. Its activities include the provision of prison and detention facilities and the transport of persons held in custody or detention, including remand prisoners, immigrant detainees and asylum seekers, and juveniles being moved to and from STCs (see paragraphs 4.35 to 4.41).

2.8. The Security Services division provides alarm services, electronic surveillance equipment, access control and closed circuit television systems (CCTV), guarding and airport security services (see paragraphs 4.23 and 4.31 to 4.34). The Safety Services division does not operate any of its activities (ambulance, fire-fighting and rescue services) in the UK (see paragraph 4.22).

## **The TWC companies**

2.9. TWC is a Florida-based corporation providing security and security-related services to both the public and private sectors. In 2001, TWC's worldwide turnover was £2.0 billion, and net assets were £119.6 million as at 31 December 2001. Gross assets were £426 million as at 31 December 2001.

2.10. TWC's worldwide security and security-related services include security officers and electronic security systems, cash-in-transit, airline and airport security, executive protection, satellite tracking of vehicles and cargo, secure storage of documents and postal services. TWC's international operations are conducted primarily through TWC and its wholly-owned subsidiary, Wackenhut International Inc, and other subsidiaries, affiliates and strategic partners. TWC's UK subsidiary, Wackenhut UK Ltd (WUK), provides security services and, for historical reasons, custody and facility management services for the Immigration and Nationality Directorate of the Home Office (IND). It provides nationwide transport for immigrant detainees between IDCs. WUK also provides certain airlines with manned guarding and other security-related services at both London Heathrow and Gatwick airports.

2.11. TWC owns 57 per cent of WCC, a company listed on the NYSE. The 43 per cent of shares which are in public hands is held by a range of institutional and private investors. In 2001, WCC's worldwide turnover was £390 million and net assets as at 31 December 2001 were £89.6 million.

2.12. WCC manages privatized correctional, detention and mental health services worldwide, and although it has no direct involvement itself in the UK, it is important to our inquiry because WCC is joint owner,<sup>1</sup> with Serco, of Premier and participates equally with Serco on the board of Premier. WCC and Serco each own 50 per cent of the shares of Premier. In 2001, Premier's turnover was £190 million, and net assets were some £21 million as at 31 December 2001. Premier holds contracts in the UK for prisons, STCs, IDCs, prisoner transport services and the electronic monitoring of offenders.

## **The acquisition**

2.13. On 8 March 2002, G4F announced the acquisition of TWC, including TWC's 57 per cent interest in WCC. The acquisition was completed on 8 May 2002.

2.14. The acquisition was notified to the Office of Fair Trading (OFT) on 15 March 2002 and referred to the CC on 9 May 2002. The transaction was not conditional on UK regulatory clearance.

## **The enlarged G4F group**

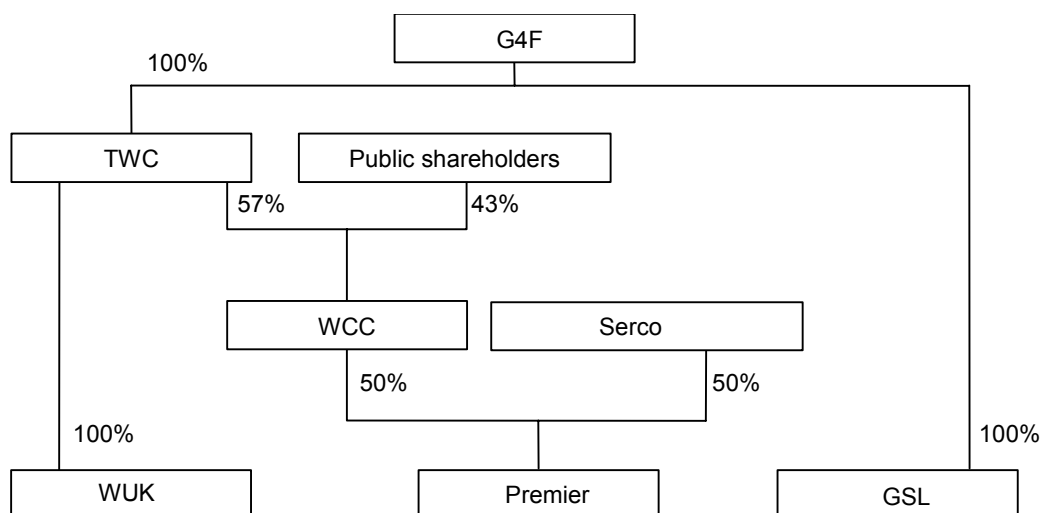
2.15. For the purposes of our inquiry, we defined the enlarged G4F group as consisting of G4F and its subsidiaries, TWC and its subsidiaries and Premier. A chart showing the simplified structure for the enlarged G4F group is shown in Figure 2.1. The chart shows only the companies and shareholdings relevant to our inquiry. Accordingly, it does not show intermediate holding companies and other companies which are not the focus of the inquiry.

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<sup>1</sup>The capital of Premier is jointly owned by Wackenhut Corrections (UK) Limited and Serco Investments Limited, which are in turn wholly owned by WCC and Serco respectively.

FIGURE 2.1

**Simplified structure chart of the enlarged G4F group**



Source: The parties.

**Jurisdiction**

2.16. As a result of the acquisition (see paragraph 2.13), we are satisfied that enterprises (as defined in the Act) which are carried on by or under the control of G4F ceased to be distinct from enterprises carried on by or under the control of TWC in the UK.

2.17. For jurisdiction purposes, we have to consider whether the ‘share of supply test’ or the ‘assets test’ under section 64(1) of the Act is satisfied. If we find that either of these is satisfied, we are required by our terms of reference to exclude the other from our consideration. The assets test is satisfied if the value of the assets taken over exceeds £70 million. The value of the worldwide gross assets of TWC exceeds this figure (see paragraph 2.9). We therefore find that the assets test for conferring jurisdiction is satisfied and, in accordance with our terms of reference, we exclude the share of supply test for that purpose.

**The rationale for the acquisition**

2.18. G4F informed us that the principal rationale for the acquisition was to allow G4F to become a global provider of security and security-related services, and in particular to gain access to the US and Latin American markets where growth in the demand for security services was forecast. We were told that it was no part of G4F’s strategy in seeking to acquire TWC to expand G4F’s activities in the custodial services sector or to buy more businesses in the UK. G4F did not originally seek to acquire the WCC stake and only did so when it became clear that the sellers insisted on a complete exit from TWC as a whole.

2.19. With regard to UK markets, G4F told us that it intended to merge WUK’s immigration-related services with the operations of GSL and to merge WUK’s security-related services with the business of Group 4 Total Security Ltd.

## Disposal plans

2.20. In its announcement of the acquisition on 8 March 2002, G4F said that it did not regard itself as a long-term owner of its stake in WCC and that for financial reporting purposes it did not intend to consolidate the results of WCC. It also announced that it intended to divest Wackenhut Resources Inc (WRI), TWC's staffing services subsidiary, because it did not fit G4F's core business strategy.

2.21. On 28 June 2002, the President and Chief Executive Officer of G4F, Mr Lars Nørby Johansen, wrote to us describing the board's strategy relating to disposals.

2.22. His letter explained that the G4F board had now decided to initiate the sale of its shareholding in WCC as soon as possible, subject to an appropriate price being obtained. Financial and legal advisers were being appointed. The letter stated that the expected time frame for the sale was six to nine months. G4F explained that this decision had been taken in order to concentrate the focus of G4F on security services and not to allay any competition or public interest concerns on the OFT's or our part.

2.23. G4F's intention to sell TWC's shareholdings in WCC and WRI was further confirmed in a statement by Mr Johansen to the Reuters news agency on 9 July 2002 to the effect that he was hoping to sell both for approximately \$250 million. [

*Details omitted. See note on page iv.*

] The intention to sell its WCC shareholding was further confirmed by G4F when it announced to the Copenhagen Stock Exchange on 21 August its interim results for the six months to 30 June 2002.

2.24. We noted that WCC (which carries out its business in the UK through Premier) was disputing the action being taken by Serco to acquire WCC's 50 per cent share in Premier (see paragraph 4.64), and that this might have an effect on the value and price of WCC's shares. Our conclusions on the likelihood of the disposal of G4F's shareholding in WCC, the timing of this disposal and its impact on competition are set out in paragraphs 2.132, 2.134 and 2.135.

2.25. [

*Details omitted. See note on page iv.*

]

2.26. [

*Details omitted. See note on page iv.*

]

## The competitive positions of GSL and Premier

2.27. G4F put great emphasis on arrangements it had entered into which were designed to ensure that Premier would continue to be able to compete with other companies in the enlarged G4F group such as GSL, in the same way that it had done before the acquisition. These arrangements were formally documented in the Safeguards Agreement and associated agreements between G4F, TWC and WCC: they extended to the activities of the companies and their subsidiaries worldwide.

2.28. G4F told us that these arrangements had the effect of preserving the competitive integrity of Premier in the UK by ring-fencing the decision-taking process within Premier from any influence by the custodial arm of G4F and by ring-fencing confidential information arising within Premier or WCC from access by G4F custodial directors. We were told that these agreements indicated that while TWC and G4F had agreed not to compete with WCC ‘in the business of managing or operating prison, detention facility or mental health facility management business anywhere in the United States’, G4F was excluded from WCC’s information and decision processes in respect of prison management and related services to allow competition elsewhere in the world. WCC had given an assurance that it would support Premier bidding for any contract in the UK regardless of whether GSL or WUK proposed to bid for the same contract. G4F told us that this assurance had effectively ceded decisions on contracts to the management of Premier and Serco, and disbarred WCC from any influence in that regard.

2.29. Several interested parties, and in particular Serco, suggested to us that the efficacy of the arrangements in the Safeguards Agreement and the related agreements must be discounted, regardless of the ostensible formality of the Safeguards Agreement. They put to us three arguments. First, they argued that as the parties to the Agreement were companies within the enlarged G4F group, they would have no incentive to enforce their rights, as they would do if they were independent parties. Second, they argued that preservation of competitive freedom between group companies could only mimic the kind of competition which takes place between unconnected companies. Third, they argued that economic factors would nullify the effects of any agreement, however binding. This was because G4F, as the ultimate parent, would have an incentive to withhold parental financial support from Premier (which was only partly owned within the enlarged G4F group) and divert such support to GSL (which was wholly owned).

2.30. With the agreement of WCC, Serco provided us with a copy of two Shareholders’ Agreements relating to Premier, the first dated 3 July 1992 when the joint venture was established, and a later agreement dated 16 December 1999.

2.31. Our conclusions as to whether G4F can control or influence Premier, and whether competition is materially affected, are set out in paragraphs 2.116 to 2.129.

## **The markets affected**

### **The services provided by the parties**

#### ***Custodial services***

2.32. For the purposes of our inquiry we have defined custodial services as an operation in the course of which the supplier undertakes to provide secure accommodation, whether for prisons, STCs or IDCs. The definition includes specialist services (see paragraph 3.27) which are an integral part of custodial management.

2.33. The purchasers of all or some of these services are, in England and Wales, parts of the Home Office, namely the Prison Service, the IND, and the Youth Justice Board (YJB), and, in Scotland, the Scottish Prison Service which is an agency of the Scottish Executive. The authorities in Northern Ireland do not procure custodial services from private sector providers. Of 161 prison establishments in the UK, 13 are now managed by the private sector.

2.34. Private sector prison management in Great Britain started in the early 1990s, with the award by the Home Office of one contract each to G4F, Premier and UK Detention Services Limited (UKDS). These management-only contracts were awarded following a process of competitive tendering. Following the abolition in 1992 of Treasury rules which had previously restricted the use of the private capital market for the funding of public infrastructure projects,

the Private Finance Initiative (PFI) began to be used as a means of harnessing private sector finance and management expertise into public sector infrastructure projects, including prisons and other secure establishments (see paragraphs 3.6 to 3.13). The Prison Service told us that it had adopted PFI in the light of its successful experience of using competitive tendering to introduce private sector prison management and in response to the need to accommodate the growing prison population.

2.35. The private sector suppliers of custodial services in Great Britain other than companies in the enlarged G4F group are:

- (a) Securicor PLC (Securicor), a UK-based international business to business group specializing in the provision of security services worldwide; and
- (b) UKDS, a consortium originally formed as a joint venture between John Mowlem & Company PLC and Sir Robert McAlpine Ltd (two large construction companies) and Corrections Corporation of America, but since November 2000 solely owned by Sodexho Alliance SA (a French company).

2.36. Other companies have competed for contracts less regularly and their involvement is set out in Tables 5.2 and 5.3. A description of the types of contract of relevance to our inquiry is given in paragraph 2.42, and a summary of contracts awarded is set out in paragraph 2.44. A full list of contract holders is shown at Appendix 3.1.

2.37. The Prison Service has not announced a programme for future private sector prison contracts. Under the YJB's current programme, there are plans to expand two of the three existing STCs, and a further five new STCs are to be opened by 2005, bringing the total to eight.

### ***Prisoner and immigrant detainee transport***

2.38. In England and Wales nearly all court escort and transport services for the conveyance of prisoners and immigrant detainees are outsourced to private sector providers (see paragraphs 3.88 and 3.89). There are eight court escort area contracts, one contract for the national inter-prison transport of prisoners currently involving about 70,000 movements a year, and one national contract for the secure transport of immigrant detainees. Vehicles used vary according to circumstances, ranging from those specially constructed for secure holding to semi-secure coaches and vans. The vehicles are usually leased from specialist firms. In Scotland and Northern Ireland, transport of prisoners and immigrant detainees continues to be undertaken by the respective Prison Services.

2.39. In 1992, GSL won the first court escort area contract for the transport of prisoners. It won two more area contracts in 1994 and a further area contract in 1996. The other holders of court escort area contracts are Premier, Securicor and Reliance Security Group plc (Reliance). In 1998, GSL won the national inter-prison transport contract which runs until 31 March 2006.

2.40. WUK holds the only contract so far awarded for the national transport of immigrant detainees.

2.41. HM Prisons has recently completed a review of the eight court escort area contracts, all of which will have expired by 2004. The Prison Service has decided to reduce the number of areas to four with the consequence that there will be fewer contracts and competitions.

## ***Contract types***

2.42. The custodial and prisoner and immigrant detainee transport services currently provided by one or more companies in the enlarged G4F group include:

- (a) DCMF contracts<sup>1</sup> for ‘new-build’ prisons (often as part of joint ventures with others such as construction companies)—these contracts generally run over a 25-year term and involve all elements of design, construction, finance and operation of the prison over that period;
- (b) MO contracts to operate existing prisons and IDCs—these involve operators tendering to manage an existing facility and the persons detained within;
- (c) STCs—these are similar contracts to those for DCMF prisons, but they relate to custodial institutions for 12- to 17-year-olds;
- (d) Design, Construct and Maintain (DCM) contracts<sup>2</sup> for IDCs; and
- (e) transport contracts to move prisoners between prisons or between courts and prisons, or for the transport of immigrant detainees to and from IDCs, reception centres and elsewhere.

2.43. A full description of these services and the overlap between the companies is provided in Chapter 3, and summarized in paragraph 2.50.

2.44. The contracts relevant to our inquiry that have been awarded, each as a result of competitive tendering, including those awarded through PFI schemes, are:

- (a) eight DCMF prison contracts, which are of 25 years’ duration;
- (b) ten MO contracts for existing prisons (five of which were earlier contracts which expired and were retendered, so only five are current);<sup>3</sup>
- (c) three (15-year) DCMF contracts for STCs;
- (d) two (six-year) DCM contracts for IDCs; and
- (e) four (six-year) MO contracts for IDCs.

2.45. Two further DCMF contracts for prisons and one DCMF contract for an STC are at an advanced stage of negotiation. [

*Details omitted. See note on page iv.*

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## ***Manned guarding services provided by the G4F or TWC companies***

2.46. Manned guarding services provided by the enlarged G4F group include staffed guarding (provided by WUK and G4F’s subsidiary Group 4 Total Security Ltd), alarm and CCTV installation and monitoring (provided by WUK and G4F’s subsidiary, Group 4 Technology Limited), and aviation security services (provided by WUK and G4F’s subsidiary, Group 4 Total Security Ltd).

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<sup>1</sup>DCMF contracts require the contractor to be responsible for the lifetime maintenance of the premises as well as the management of the activities within them.

<sup>2</sup>DCM contracts require the contractor also to undertake the management of the functions within the facility.

<sup>3</sup>Typical duration of MO contracts for prisons is ten years; original contracts were for five years with an option to extend (see paragraph 3.54).

## The bidding process

2.47. The Home Office and the Scottish Prison Service operate a competitive tendering process when they seek to procure custodial services and prisoner and immigrant detainee transport services from the private sector. A bidding round might be for one or several contracts. Firms that meet the criteria set out in a pre-qualification phase are asked to submit sealed bids. At the next stage, a preferred bidder is named, with another firm sometimes held in reserve as a standby pending the conclusion of negotiations with the preferred bidder. The whole process can be completed in six to nine months but some recent contracts have taken over two years to progress from bid invitation to contract closure. The details of contracts that are finally awarded are not usually published but bidders are debriefed on the strengths and weaknesses of their bids. The bidding process is designed to ensure that firms submitting bids are not supplied with any information about the prices or specifications contained in other firms' proposals.

2.48. The contracting process is subject to EC rules on public procurement. These are designed to ensure that bids are invited on equal terms from all interested parties across the EC and that the assessment of those bids is fair and transparent. We noted that the Home Office has said that the Prison Service will select the tenders which it perceives to be the most advantageous to it and which represent the best combination of deliverability, quality, innovation and risk transfer on the one hand and cost on the other. This has not in every case meant that the lowest-cost bid has been accepted: the Home Office told us that the Prison Service considers the existing market share of the respective bidders as part of its overall strategy of building a strong supplier base to meet the needs of the developing custodial service market. We considered that the Prison Service had been particularly active in the early years of PFI in encouraging new entrants (see, for example, paragraph 3.74).

## Market definitions

2.49. We considered what market definition should apply in respect of each of the services in which there was an overlap in supply between the companies in the enlarged G4F group.

2.50. Companies in the enlarged G4F group overlap in the supply of the following custodial and transport services:

- (a) DCMF contracts for prisons;
- (b) MO contracts to operate prisons and IDCs;
- (c) DCMF contracts for STCs; and
- (d) transport contracts for prisoners and immigrant detainees.

The companies also overlap in the supply of other manned guarding services in the UK: staffed guarding; alarm and CCTV installation and monitoring; and aviation security.

2.51. We analysed each of the overlapping services in turn in order to define the product and geographic markets of which the services are part. We did not consider DCM IDC services or electronic monitoring services after this point in our inquiry, as the enlarged G4F group did not overlap in the supply of these particular services.

2.52. Markets are generally defined by examining whether there are close substitutes on either the demand or the supply side for the relevant products or service being examined and by applying the 'hypothetical monopolist' (or SSNIP<sup>1</sup>) test. This asks whether someone who

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<sup>1</sup>A small but significant non-transitory increase in price.

supplied 100 per cent of a particular product or service (or a collection of products or services) could raise prices by a small but significant amount, and for a reasonable time, without the price rise being rendered unprofitable because sufficient customers buy other products or services, or suppliers of similar products or services switch to supplying the service instead. If the hypothetical monopolist could not sustain such a price rise, then those other products or services should be included in the same markets as the ones under consideration. Our application of this test to the overlapping services supplied by companies in the enlarged G4F group is discussed in greater length in Chapter 5.

2.53. Once we have used the SSNIP test to identify the relevant product market, we then evaluate the competitive constraints acting on the market. A firm that enjoys a large share of the relevant product market may not have sufficient power to raise prices if rivals in the market—or potential entrants currently outside the market—will undercut it, or if buyers are sufficiently strong to resist price increases. Among other things, this means that competitive constraints can emerge from both outside and within the relevant market.

### *The markets for custodial services*

2.54. In order to define the relevant markets for the custodial services in which companies in the enlarged G4F group overlap in supply, we considered the whole range of demand and supply of custodial services, recognizing the particular characteristics of transactions made as a result of bids. We considered the extent to which competition in these markets in the future might be affected by the acquisition, including any changes in firms' bidding behaviour and the wider issue of changing techniques for private sector involvement in these markets and the related prisoner and immigrant detainee transport markets.

2.55. On the demand side all the purchasers have to operate within the constraints of government policy guidelines and legal requirements. In the context of our inquiry, for certain types of offence, there is no substitute for secure accommodation, either in prisons or STCs. The evolving policy on immigrant detainees (see paragraphs 3.63 to 3.72) requires the IND to make IDCs available for housing certain immigrant detainees subject to detention orders. We therefore considered that there was no scope for demand-side substitution of alternative services to prison, STC or immigrant detainee custodial services.

2.56. We also considered, for each of these services, whether the market was defined by each contract or whether there would be scope for other firms supplying very similar services to provide an immediate supply-side constraint. The SSNIP test has some limitations in markets such as these, where prices are agreed for the period of each contract. In the event of a government purchaser having to accept a small but significant price increase on one contract, we considered that other firms already involved in the supply of similar services (for example, other DCMF prison services) would be able to provide a supply-side constraint when the contract was relet or similar contracts were next tendered.

2.57. With regard to DCMF and MO prison services, we also considered that the similar services the Prison Service supplies 'in-house' (ie not through a competitive tender) would not form an immediate supply-side constraint because of the current policy whereby the Prison Service does not compete for DCMF prison contracts and the uncertainty as to whether it would continue to compete for MO prison contracts in the future.

2.58. As to whether supply-side substitution widens the relevant product markets further than the following groups of services—DCMF prisons, MO prisons, DCMF STCs and MO IDCs—there are some differences in the type of expertise needed to manage the different populations and a more marked difference in the level of financial commitment required for

DCMF contracts (see paragraphs 5.14 to 5.16 for more details). We therefore did not believe that a firm involved solely in supplying one of the group of services above would immediately be able to switch to supplying another of the groups of services above.

2.59. Taking all these supply- and demand-side considerations into account, we concluded that there are four relevant product markets for custodial services as we have defined them: DCMF prisons, MO prisons, DCMF STCs and MO IDCs.

2.60. In considering the geographic market we saw no reason to suppose that companies supplying one of the custodial services markets in one part of Great Britain would not be able or willing to bid for a contract in another area in such a way that it would provide an immediate supply-side constraint. We then considered whether companies operating from outside Great Britain might provide a supply-side constraint (see paragraph 5.23). Our conclusion was that, while overseas companies (and any based in Northern Ireland) might provide a competitive constraint as potential new entrants, the direct geographic market is Great Britain.

### *Market shares*

2.61. In the DCMF market for prisons in Great Britain, Table 5.1 shows that before the acquisition, GSL had 25 per cent of the market defined by number of contracts won. The most successful bidder was Premier which had 50 per cent. With Premier included, the enlarged G4F group has 75 per cent of the market defined by number of contracts won. UKDS and Securicor between them account for the remaining 25 per cent. In the contract bid rounds (summarized in Table 5.2), GSL competed regularly with Premier, Securicor and UKDS and, to a lesser extent, with Correctional Services Corporation (CSC) and, in the earlier rounds, with Secure Care Services.

2.62. Only a small proportion of prison management activity has been opened up to the private sector through competitive tendering. Of this, GSL's and Premier's pre-acquisition share by numbers of contracts in the MO prisons market was 20 per cent each: the enlarged G4F group therefore accounts for 40 per cent. The number of contracts that the Prison Service has won through competing in the tender process accounts for the remaining 60 per cent: it has achieved a 57 per cent bidding success rate<sup>1</sup> against GSL's 33 per cent, and Premier's 22 per cent. No other competitor has won a contract, although Securicor, UKDS and CSC have been regular competitors. Two other companies (both American) were also competitors for early DCMF prison contracts but neither firm has competed in recent times (see paragraph 5.57).

2.63. The YJB has awarded only three DCMF STC contracts to date so interpretation of market share data has to be treated with caution. Two of these were won by GSL, giving it a market share by number of contracts pre-acquisition of 67 per cent; and the third was awarded to Premier (33 per cent share) so that the enlarged G4F group has all existing contracts. The YJB told us that Securicor had been selected as the preferred bidder for a new DCMF STC contract. We noted that because the number of contracts in these markets is small, market shares could change significantly with the award of just one contract.

2.64. The same limitations on interpretation of data apply in the MO IDC market. Only four contracts have been awarded. G4F's market share by the number of contracts, prior to the acquisition, was 50 per cent (two contracts) and WUK's share was 25 per cent (one contract). Premier holds the remaining contract, accounting for the remaining 25 per cent share, giving the enlarged G4F entity 100 per cent of contracts awarded (see Table 5.6). G4F, WUK and Premier have competed for all four contracts, and Securicor and Reliance for three (see Table 5.7).

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<sup>1</sup>Any difference between a company's market share expressed as the percentage of number of contracts won and the percentage showing its bidding success rate is explained by the fact that not every company bid in every bidding round.

## ***The market for prisoner and immigrant detainee transport***

2.65. We used the same criteria as those applied to the custodial markets above, to define the relevant product market for prisoner and immigrant detainee transport. Our conclusion was that the service requirements in respect of transport contracts are similar enough to enable any firm with the capacity to supply secure transport to provide an immediate supply-side constraint, although we were of the view that there was no scope for demand-side substitution of other services (see paragraphs 5.25 to 5.36 for greater detail). We found, therefore, that the relevant product market was no wider than all prisoner and immigrant detainee transport supplied by private operators to the IND and Prison Service.

2.66. In considering the geographic market (described in paragraphs 5.37 and 5.38), we observed that bidding patterns for transport contracts show that many firms bid for all the contracts available and therefore we conclude that the market is England and Wales. (No private firms supply these services in Scotland or Northern Ireland—see paragraph 3.84.)

2.67. Before the acquisition, G4F's share of the market, in terms of contracts won, was 50 per cent. With the acquisition of WUK, this increased to 60 per cent. Premier accounts for a further 20 per cent and so the enlarged G4F group accounts for 80 per cent (see Table 5.8). Two other firms, Securicor and Reliance, account for the remaining 20 per cent. Of the ten contracts awarded, GSL has won five and Premier has won two, and Securicor, Reliance and WUK have won one each. UKDS competed for four and won none.

## ***The markets for manned guarding services***

2.68. As we discussed above, G4F and TWC also overlap in the supply of manned guarding services (namely staffed guarding, aviation security, alarm and CCTV installation and monitoring services) as a result of the acquisition (see paragraphs 3.107 to 3.130 for a fuller description).

2.69. We judged the relevant product market for staffed guarding to be no wider than the provision of static and mobile guarding services. We believed that switching costs would prevent significant demand-side substitution to the closest substitute of physical security in the event of a small but significant price rise on staffed guarding services. We also considered that there were sufficient entry barriers to prevent easy supply-side substitution by other firms operating in similar industries. The geographic market was considered to be UK-wide (for more details see paragraphs 5.39 to 5.41).

2.70. We found that the group of aviation services formed another separate relevant product market. We were of the view that there were few demand-side product substitutes available to customers if they were facing a small price rise on aviation security services such as guarding baggage and planes. We also considered that aviation security services were sufficiently differentiated from other manned security services (by, for example, higher levels of insurance and stricter personnel vetting) to prevent easy supply-side substitution. We considered the geographic market to be UK-wide (for more details see paragraphs 5.42 to 5.44).

2.71. Finally, we considered that alarm and CCTV installation and monitoring services formed another separate relevant product market. Again, we considered that the costs of establishing differing security systems would prevent sufficient demand-side substitution to similar services such as manned guarding services. We also thought that requirements such as a manufacturing operation would form a sufficient barrier to entry to prevent quick and easy supply-side substitution by other firms operating in similar industries. We judged the geographic market to be UK-wide (for more details see paragraphs 5.45 to 5.48).

2.72. When considering these three product markets, we found that G4F had gained very small incremental and combined market shares as a result of its acquisition of TWC. We also found that there were a large number of competitors in each market. Such evidence indicated that it was unlikely that G4F would acquire or increase its market power in any of these markets as a result of the acquisition.

## **The effects of the acquisition on competition**

2.73. In our Issues Statement published on 3 July 2002, we set out the issues we had put to G4F in a letter dated 2 July 2002 that we said we would need to consider in determining whether the acquisition of TWC by G4F operated, or might be expected to operate, against the public interest.

2.74. We considered all the responses to the Issues Statement from main and third parties and as a result we concluded that the areas we needed to examine to assess the effects of the acquisition on the public interest were:

- (a) the effects of the acquisition on competition, prices and quality in the markets for custodial services and secure transport;
- (b) the roles and nature of the Safeguards Agreement made between G4F, WCC and TWC, the related Confidentiality Agreement, the 1992 Shareholders' Agreement between WCC and Serco and the 1999 Shareholders' Agreement between WCC, Wackenhut Corrections (UK) Limited and Serco relating to Premier and related undertakings; and
- (c) G4F's intentions regarding the disposal of its interest in WCC; [ *Details omitted. See note on page iv.* ]

## **Competitive constraints**

2.75. Officials from the Prison Service expressed concern about the market power that the enlarged group would be able to exercise. They said that the specialized nature of the contracts and the high costs involved in preparing bids, particularly PFI bids, presented substantial barriers to entry to any new entrant to the market. They also believed it was possible that some companies might be deterred from bidding because of reputational risk. They told us that to the best of their knowledge, apart from the five companies currently fulfilling custodial and transport contracts in Great Britain, there were only two other major companies (both based in the USA) that they saw as credible bidders for Home Office contracts. One had already bid unsuccessfully on two separate occasions and was unlikely to return to the market in the near future, and the other had not yet shown any real interest in entering the British market. The Scottish Prison Service said that the specialized nature of the contracts and the high costs of bidding, particularly for PFI contracts, were substantial barriers to entry.

2.76. The YJB was concerned that following the acquisition G4F now effectively 'controlled' all three STCs, which reinforced G4F's market power and reduced competition. The STC market was small and specialized, with few credible bidders. The YJB wanted to widen the bidding market for future STC contracts.

2.77. The IND had similar concerns. Officials told us that it had not been particularly proactive in trying to broaden the market. They thought there were barriers to entry for those who did not understand the nature of the custody business, and that it was difficult and expensive for new entrants to bid in a market in which other players were well established.

2.78. G4F told us, however, that, as the markets had matured, many of the original uncertainties about entering the markets and some of the concerns about finding finance for contracts had diminished. They said that tender requirements had become more explicit and performance measures within contracts had become more specific. G4F believed that it was now easier for a new entrant to understand what the requirements were for a successful bid. Given this, G4F expressed some surprise that there were not more potential contractors currently interested in the custodial and transport markets.

2.79. We considered the extent to which wider competitive pressures on the enlarged G4F group would have the capacity to constrain or nullify effects that might otherwise be expected to operate against the public interest. We considered several factors that may serve to constrain market power. These included the potential for inter-firm rivalry, actual or potential new entrants (which might be adversely deterred by any advantages which incumbents have), and the extent to which countervailing monopsony buyer power would constrain any market power that the enlarged G4F group might be able to exercise and restrain it from raising prices or lowering the quality of service. Other factors considered were the way in which the bidding process operates, in particular the confidentiality of sealed bids and the possible incentive not to raise prices in markets where the ‘winner takes all’.

### ***Inter-firm rivalry***

2.80. We considered whether rivalry between market suppliers would be likely to act as a constraint on the enlarged G4F group from exercising any market power. We found that Premier and GSL have acted as strong rivals to each other in the custodial services and prisoner and immigrant detainee transport markets. This rivalry was likely to have been a significant constraint on either firm exercising market power in the past to increase prices or reduce the quality of service. We consider later in this chapter (in paragraphs 2.116 to 2.128) whether the Safeguards Agreement and related Confidentiality Agreement, together with the status of Premier as a jointly-owned company regulated by its Shareholders’ Agreements, will ensure that this rivalry is maintained.

2.81. Actions, or expectation of actions, on the part of other firms in the markets could also serve as an effective competitive constraint. We noted that there have been, on average, two or three other companies competing against TWC and G4F companies for custodial services and prisoner and immigrant detainee transport contracts. We considered that this limited number of competitors might increase the potential for firms to compete less vigorously in these markets, as potential bidders would have fewer firms’ actions to take into account when considering business strategies.

2.82. We considered, however, that the particular characteristics of the markets we examined might counteract this tendency and encourage competition between firms. First, the markets are characterized by infrequent sales opportunities. Bidding at any price but the lowest always carries the possibility of the contract being lost to a competitor—a high penalty. The bidding process is demanding on resources, providing an incentive to put in the keenest possible bid. This means that the presence of even one rival credible bidder is likely to act as some constraint on another.

2.83. We also judged, however, that other firms in the custodial services markets might be prevented from competing against the enlarged G4F group by constraints on their capacity. For example, Premier told us that it currently had insufficient resources to compete for all contracts that might be offered. On the other hand, we received no conclusive evidence that competitors have any less capacity to compete than companies in the enlarged G4F group. [

*Details omitted. See note on page iv.*

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2.84. We considered that the sealed-bid design of the bidding process was likely to prevent the transmission of price information between competitors during the bidding process. This would prevent firms following any price rises set by the enlarged G4F group, as could happen in other kinds of market.

### *New entry*

2.85. We considered whether new firms were likely to enter the custodial services and prisoner and immigrant transport markets, and the extent to which this would constrain the enlarged G4F group from exercising market power.

2.86. We found that bidding costs could represent a moderate barrier to entry, particularly in the DCMF prison and STC markets. Historically, some companies have had to tender several times before winning a contract. Bidding costs are lower for entry into MO markets for IDCs and prisons, which do not require the same level of financial backing. We noted, however, that the preferred bidder for the most recent DCMF STC contract was Securicor, which would be a new entrant (although it had been an established bidder since the market opened).

2.87. In the prisoner and immigrant detainee transport market, we considered that barriers to entry were low, even though there had been little successful competition from non-G4F group companies. This consideration led us to conclude that new entry was probable in the short term.

2.88. As for the custodial markets, we considered whether incumbent firms could accrue advantages that could be significant enough to deter entry by new firms, most importantly through their experience of providing the services. It was G4F's view, drawn from its own experience in rebidding for contracts, that incumbents obtain no advantage from their position. On the other hand, we believed that government purchasers could be expected to look for, and prefer, providers with a proven track record in managing high-risk groups where safety and security are paramount. Incumbents also have the advantage of knowing how to set out bids which, in substance and presentation, would give confidence to the purchaser. Incumbents are also able to draw on their experience of the cost outcomes of previous contracts when preparing new bids. This could reduce the risk of incorrectly pricing a bid.

2.89. Other advantages for incumbents might include the ability to attract skilled and experienced prison directors. Despite there appearing to be a reasonable number of suitable directors in the UK, new entrants might have difficulty recruiting for such posts because of the uncertainty as to whether or when they might win a contract. In addition, there is evidence that market incumbents would experience small economies of scale and scope that would enable them to submit more competitively-priced tenders for contracts. Finally, incumbents with a good insurance record are also likely to be able to obtain lower-cost insurance premiums than potential new entrants, although the size of this advantage is unclear as we were told that insurance premiums are rising substantially across the industry.

2.90. We also considered whether reputational risks might deter new entrants. The private operation of custodial services in the UK is sufficiently unusual in historic terms to receive a high level of press scrutiny and consequently firms need to be prepared to manage the risk of negative press coverage. New entrants may perceive this risk as being higher than those who are already in the industry managing these risks.

2.91. Further, it was plausible to believe that new entrants would perceive that managing the operational risks of containing people in prisons or in secure vans and, to a lesser degree, in

IDCs would be more difficult for themselves than for incumbents. This is because new entrants would lack the direct operational knowledge that incumbents have acquired through experience.

2.92. Private operators were divided on whether risks in these markets were high. The Prison Service told us that the private operation of prisons was a very politically sensitive area. They said that operators were concerned about this and that the accompanying public scrutiny could act as a deterrent to new firms considering entering these markets.

2.93. We noted that several firms have expressed an interest in entering these markets. Cornell Companies Inc (Cornell) told us that it was ‘prepared and eager to expand its quality services and skills to other countries, particularly the United Kingdom’. It said that it was primarily interested in expanding into prison, juvenile detention, STC and IDC construction and management services. Cornell also commented that perceived advantages to incumbents would not deter it from submitting a bid in the UK. It said that increasing the number of UK private custodial contracts would make entry into the UK market more attractive to the company.

2.94. CSC told us that it would be interested in providing transport services for immigrant detainees in the UK. Incumbency advantages would not deter it from bidding for projects it found attractive. On the other hand, Rentokil Initial plc and Securitas Security Services Limited told us that the prospect of entering the custodial markets in the UK was not attractive. Chubb plc, too, told us that it had not bid for custodial guarding or escort contracts as it felt that there were already established players in this field, and the substantial costs associated with submitting a credible bid as a new entrant were prohibitive.

### *Conclusions on the likelihood of new entrants*

2.95. There clearly has been some new entry into these markets in recent years, which we believed was encouraging. However, the majority,<sup>1</sup> that is three of us, concluded that it was unlikely to be widespread in the near future, based on the history of firms bidding in these markets and the entry barriers considered earlier in this chapter.

2.96. The majority was concerned, too, that if Premier’s share of the market was taken into consideration as part of the enlarged G4F entity, the concentration of contracts within certain markets (DCMF contracts for prisons, MO services for prisons, MO services for IDCs, DCMF contracts for STCs, and prisoner and immigrant transport) gave the enlarged G4F group some advantages over potential entrants, to the extent that new entrants would be deterred. G4F would enjoy some small cost advantages arising from economies of scale and scope. The minority,<sup>2</sup> namely two of us, considered that the purchasers were likely to act so as to encourage new entry into the markets and thereby to counter any perception of incumbency advantage. (This is considered further in paragraphs 2.105 to 2.111 in the section on the likely use of countervailing buyer power to encourage new entry.)

2.97. We noted that a recent report on the prison service by Mr Patrick Carter (the Carter report<sup>3</sup>) had recommended a more prescriptive approach to the specification of inputs in contracts, such as minimum staffing levels on the basis that this might help speed up the tendering process. We considered that greater specificity could bring more clarification to the bidding process, to the benefit of new entrants. On the other hand, we also thought that greater specificity could reduce the scope for innovation and the possibility of associated cost savings.

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<sup>1</sup>The majority’ referred to in this report are: Mr Jeremy Seddon, Professor John Baillie and Mr Alan Young.

<sup>2</sup>The minority’ referred to in this report are: Professor Catherine Waddams and Mr Robert Bertram.

<sup>3</sup>*The Carter Report*, published January 2001. The terms of reference for the Carter report were ‘to consider how best to develop the contribution of the private sector, particularly PFI, to achieving the objectives of the Prison Service; and to make recommendations’. This report was commissioned from Mr Patrick Carter following a previous report commissioned by the Home Office (*Modernising the Management of the Prison Service, An Independent Report by the Targeted Performance Initiative Working Group*, Home Office, 2000).

## ***Countervailing buyer power***

2.98. We considered the two different ways in which the purchasers could exert countervailing buyer power. First, we examined whether there was a credible threat of self-supply which could constrain any market power the enlarged G4F group might have obtained as a result of the acquisition. Second, we considered whether the purchasers could encourage entry into the relevant markets.

### *The threat of 'self-supply'*

2.99. There is a long history of self-supply by the prison authorities in Great Britain in the custodial and transport markets. This is a feature that distinguishes them from purchasers in many other markets.

2.100. The Prison Service has already shown that it can compete effectively for MO contracts for existing prisons. There is, however, no history of the public sector bidding for STC or IDC contracts although this does not rule out the public sector from providing these services in the future.

2.101. The threat of self-supply must be credible in order to act as a sufficient constraint on competitors. We judged that, in the markets where PFI is used (for example, DCMF prisons and DCMF STCs), the Public Sector Borrowing Requirement could be a restriction on implementing the threat of self-supply that could be recognized by private sector competitors in these markets.

2.102. We noted a further factor that might reduce the credibility of certain self-supply options. There is evidence that the Government has used private sector provision as a sanction for poor public sector performance. For example, the recent Government White Paper *Justice for All*<sup>1</sup> stated that 'failing prisons' would be contracted out to the private sector.

2.103. We also noted that the Home Office and the Scottish Executive are under pressure to improve the value for money and the quality of custodial services. Although there has been criticism of private sector provision, it was our view that more opportunity for private sector provision would be an effective method of achieving this goal.

2.104. The Prison Service told us that each time it ran a competition, it compared the bids received against the costs it would incur in supplying the service itself. It would be able to re-examine whether the competitive tendering was the best option if private sector bids exceeded the public sector comparator (see paragraph 5.158). However, it appeared to us that as the tendering exercises currently take months or even years to complete, failure to make an award to a private sector bidder could lead to unacceptable delays in markets where demand is difficult to predict.

### *Encouraging new entry*

2.105. The Home Office and Scottish Executive could also exercise their buyer power by encouraging entry by new firms into the markets concerned. Entry, or the threat of entry, might be sufficient to prevent the enlarged G4F group from exercising its market power. We noted, however, that the Prison Service thought that there was little it could do to encourage new entrants apart from what it was doing already through advertising contracts extensively.

2.106. We considered that there were political factors affecting to some degree the ability of the purchasers effectively to encourage new entry. The purchasers were limited to some

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<sup>1</sup>Cm 5563, presented to Parliament in July 2002.

extent in their ability to signal their future intentions for these markets because government policy, and the necessary funding, was not within their control.

2.107. We therefore considered whether we could form a reasonable expectation that the purchasers (including the Prison Service) would act in future to encourage new entry by reducing some of the barriers to entry (such as bidding costs and the strategic advantages of incumbents).

2.108. The majority of us were of the view that there was little evidence that the purchasers have taken positive steps of this kind to encourage new entrants, with the exception of the Prison Service which had on occasion sought to widen the market by selecting a range of suppliers for its contracts. The minority took the view that the record of the purchasers in creating the markets from scratch over the last decade, and particularly the recent behaviour of the purchasers in encouraging companies which had not previously been major players in the markets (see paragraph 2.45), showed that the purchasers were keenly aware of the potential problem posed by a concentration in these markets of a small number of established players and were willing and able to address that problem.

### *Conclusions on countervailing buyer power*

2.109. Having weighed up these different considerations, we are agreed, on balance, that there is, potentially, sufficient countervailing buyer power in each of the markets we have considered to prevent G4F from raising prices or reducing quality of service. Furthermore, the Home Office and Scottish Executive have it in their power to counteract any perception in the minds of potential bidders that incumbency carries any advantage and to negotiate tight contract terms even where there are only a small number of bidders for a contract.

2.110. The majority, however, consider that there is evidence in recent years of the purchasers not fully using their potential buyer power in the award of contracts. They conclude that the purchasers are less likely or willing to exercise their power rigorously on three grounds. First, the Home Office and the Scottish Executive may feel comfort using tried and tested operators in this high-risk industry rather than bringing in new entrants. Second, contracts increasingly specify inputs rather than outputs or outcomes which may deter some new entrants. Third, the irregular intervals at which contracts are offered make it difficult for new entrants to assemble the resources required to bid.

2.111. The minority, on the other hand, believe that the Home Office and the Scottish Executive not only possess countervailing buyer power but have demonstrated an ability to use it in developing the market, and in recent years have exercised it in the contracting process.

### **Conclusions on the competitive constraints**

2.112. We could not come to a unanimous conclusion as to whether the competitive pressures in all the relevant markets would provide sufficient constraints on any market power which the enlarged G4F group might have obtained as a result of the acquisition.

2.113. On balance, after considering the strength of these competitive constraints, the minority believed that the competitive forces in play in all the relevant markets were likely to be sufficient to constrain any market power available to the enlarged G4F group.

2.114. On the other hand, the majority were concerned that the competitive constraints would not be sufficient to constrain the enlarged G4F entity from exercising any market power acquired as a result of the acquisition in the markets for DCMF and MO prisons and DCMF STCs.

2.115. We did, however, unanimously agree that the competitive pressures operating in the MO IDC and prisoner and immigrant detainee transport markets are sufficiently strong so as to constrain any market power which the enlarged G4F group might be able to exert as a result of the acquisition.

## **Conclusions on the effectiveness of the agreements**

2.116. In our analysis of the effect of the acquisition of TWC by G4F on competition, we considered the possibility that the enlarged G4F group could exert market power to raise prices or reduce quality of service. In this context, G4F had argued that GSL and Premier, both companies within the enlarged G4F group, would still be in competition with each other. We therefore considered how effective the agreements, described more fully in paragraphs 4.11 to 4.19 and 4.61 to 4.63, would be in ensuring that competition between G4F and Premier would continue following the acquisition.

2.117. We took legal advice from a Florida law firm<sup>1</sup> on the interpretation and legal context in which the terms of these agreements would be enforced. The Shareholders' Agreements are subject to the law of England and Wales, and the Safeguards Agreement is subject to the laws of the State of Florida, USA. We considered associated agreements including a Confidentiality Agreement made in accordance with the Safeguards Agreement. We also took evidence from Premier, Serco and WCC on how the operations of Premier are actually managed.

2.118. We considered possible and actual criticism from competitors. We recognized that they would probably be unaware of the key provisions of some of the relevant agreements because, with the notable exception of the Safeguards Agreement, some were not in the public domain.

2.119. In particular, we considered the possibility that TWC (100 per cent owned and controlled by G4F), with its 57 per cent shareholding in WCC and thus a 28.5 per cent economic stake in Premier, would be less inclined to assist in providing the funds for bids being planned by Premier, as against bids being planned for the same contracts by G4F's 100 per cent owned subsidiary, GSL. Under this scenario, it would be plausible for G4F to refuse to provide support for bids by Premier for new business. In addition, we also considered the point put to us that G4F now had an incentive to use its corporate powers in relation to Premier to coordinate the commercial activities of GSL and Premier by, for example, adopting an agreed bidding strategy.

2.120. Our own analysis of the agreements led us to the conclusion that assessment of the efficacy of the ring-fencing arrangements could not depend on examination of the Safeguards Agreement in isolation. It was necessary, in our view, to take account of the wider situation of both WCC in the USA and Premier in the UK. The wider situation of WCC was relevant at two levels. First, the Safeguards Agreement was initiated by the independent directors on the WCC board and was a precondition of the merger between G4F and TWC, not a reaction to it. Second, the ultimate interest to enforce the competitive integrity objectives of the Agreement comes not from WCC itself but from the minority shareholders of WCC. Those shareholders, moreover, include sophisticated investors protecting an investment in a publicly-listed company. The object of our seeking legal advice on the applicable Florida law was to establish whether that law would provide mechanisms for individual investors in WCC to protect their interests if the Agreement was not observed. That advice confirmed that there are a variety of such mechanisms since, under Florida law, duties are owed by a company's directors not merely to the company but also to the individual shareholders in it.

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<sup>1</sup>Mr Andrew L McIntosh, Piper Rudnick LLP, Tampa, Florida, USA.

2.121. The wider situation of Premier is relevant in three ways. First, Premier is not controlled either by WCC or by Serco. As a 50:50 joint venture it is subject to their equal influence. Second, the influence of WCC to block a bid for a new contract by using its veto on the board of Premier has effectively been ceded by WCC to Serco. We were told that the reason for this was that exercise of its veto would, under the terms of the Shareholders' Agreements, impose a 'keep-out' covenant on the relevant party such that neither it nor its affiliates could thereafter engage in activities in the UK in competition with Premier. Since this sanction could impact on GSL (when it became an affiliate of WCC), WCC had agreed to protect GSL and G4F by undertaking to permit any opportunity which Premier wished to develop. Moreover, since WCC's undertaking to protect G4F was itself conditional upon G4F observing the Safeguards Agreement and its associated agreements such as the Confidentiality Agreement, the latter was thereby further underpinned.

2.122. Following the advice we have received on the applicable Florida Law, we concluded that the Safeguards Agreement contains all the necessary elements to be a binding agreement and could be enforced in the Florida Courts against the parties to it. In addition, the business context in which the Safeguards Agreement operates suggests that it is in the interests of the parties to the Agreement to secure compliance with it.

2.123. In considering the provisions of the Shareholders' Agreements we noted the undertaking given by WCC that it will vote its interest in the Premier joint venture in favour of all proposed new projects for custodial or related facilities in the UK for so long as G4F may be subject to the consequential restrictions under the Shareholders' Agreements.

2.124. We concluded that the effect of all these agreements, taken together, means that measures are in place which should effectively maintain Premier as a separate business from G4F and ensure continuing competition between the two concerns.

2.125. These conclusions relate to the structures which operate to ensure that Premier and GSL can continue to compete with each other. We thought it right, however, to consider the position if two of the parties to the Safeguards Agreement (G4F and WCC) concluded that their best interests did not lie in competing against each other for contracts in the UK but rather in cooperating. We asked ourselves what deterrent there would be to their acting in this way, which is the opposite of what is envisaged by the Safeguards Agreement.

2.126. We believe that the provisions of the Competition Act 1998 would provide the necessary deterrent to any such activities. These would be effective because for the purposes of the Act, GSL and the Premier joint venture would be considered not to be within a group and hence would not enjoy the group company exemptions from the Act's sanctions against anti-competitive behaviour.

2.127. It follows that, in addition to our conclusions on the overall effect of the agreements described above, we consider that the prohibitions in the Competition Act 1998 on agreements preventing, restricting or distorting competition and abuses of dominant position, taken with the provisions of Articles 81 and 82 of the EC Treaty, are sufficient to deter any actions which could be taken which might adversely affect continuing competition between the two concerns.

2.128. We also considered the possibility (given that G4F had put in hand plans to sell [ ✂ ] its shareholding in WCC) that GSL and Premier might each independently decide to raise the prices in future bids for contracts in the expectation that this would in the long term enhance the value of their respective companies. We judged, however, that this was a less likely scenario than both companies continuing, at least in the short to medium term, to seek to win contracts at competitive prices.

2.129. Our findings on the legal framework and on the commercial factors which determine the ability of Premier to compete with G4F therefore led us to conclude that Premier was an

independent competitor in the relevant markets and would have the necessary resources to compete effectively.

2.130. We therefore unanimously concluded that there were no competition concerns arising from G4F's acquisition of TWC in respect of the markets for DCMF prison contracts, MO contracts for prison services and DCMF contracts for STCs.

## Conclusion on the public interest

2.131. We are unanimous in finding that the acquisition may be expected not to lead to a significant reduction in competition in the markets for the services affected by the acquisition. We identified no other factors which would cause the acquisition to have a significant impact on the public interest. We conclude that the acquisition of TWC by G4F may be expected not to operate against the public interest.

## Conclusions on possible disposals

2.132. During our inquiry, we considered G4F's plans to sell its shareholding in WCC, recognizing that this would have the effect of removing all ties between G4F and Premier. G4F's intentions on this disposal had been confirmed in public on several occasions. When the announcement was first made, and on subsequent occasions, G4F said that it would be looking to secure an acceptable price. G4F told us that it had engaged advisers to handle the sale with the aim of completing it by Christmas 2002. This is consistent with its long-term plans to focus its business on security services rather than custodial and correctional services and to release funds to lower its indebtedness and provide scope for further security acquisitions. Our concern was about timing, against the background of volatility in financial markets and the litigation initiated by Serco over its pre-emption rights in respect of Premier. Nonetheless, we have a reasonable expectation that the disposal of the shareholding in WCC will go ahead, even if there might be some delay in the timetable originally envisaged by G4F.

2.133. [

*Details omitted. See note on page iv.*

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2.134. On the current evidence before us, we have no reason to doubt G4F's intentions over [ ✂ ] WCC [ ✂ ]. We further consider [ ✂ ] may be expected to take place within the next year.

2.135. We also considered the possibility that WCC would be required under the terms of the Shareholders' Agreements to sell its holding in Premier to Serco. In that event, WCC would no longer be asked to help finance Premier's bids. The evidence given to us by Premier on the financing of bid proposals indicated that, in practice, the special purpose vehicles (SPVs) established when bidding for certain contracts (and described in more detail in paragraph 3.12) would not normally be asked to arrange ultimate group parental guarantees. If injections of additional equity into the SPVs were required, a gap might arise, but Premier told us that it would look to its parent companies for any additional finance it needed, particularly in respect of DCMF contracts. We believe any financing gap would be one which could be expected to be filled by Premier, WCC or Serco, or through capital market intermediaries if the need arose.

2.136. Serco's claim that it now had the right to purchase WCC's holding in Premier is subject to litigation. But we have concluded that, whether the outcome is in favour of WCC's continuing ownership of 50 per cent of Premier or in favour of Serco being able to take 100 per cent ownership, it will in neither event be likely to operate against the public interest.

## **Concluding remarks on the possible development of the markets**

2.137. We have already noted (in paragraphs 2.98 to 2.111) the importance of counter-vailing buyer power as a possible constraint on any market power gained by G4F as a result of its acquisition of TWC. We consider that the Home Office and the Scottish Executive, in consultation with other government departments and agencies such as the Treasury and the Office of Government Commerce, could find ways to exercise buyer power more effectively to make a much more significant contribution to competition.

2.138. Based on our analysis we believe that, in conjunction with other departments and agencies, the Home Office and Scottish Executive should consider taking the following actions to enhance competition:

- publish a response to the relevant recommendations made in the Carter report and announce an action plan in order to give greater certainty to both private sector and public sector providers on likely future trends in the market;
- clarify how the Government will actively promote best value through the encouragement of new entrants, making it clear that there is no predisposition to favour incumbent contractors;
- clarify the policy of contracting out 'failing prisons' and consider whether a similar competitive process should also be established for the management of a number of prisons that are not in this category;
- publish an indicative timetable for likely future contracts, to the extent that the information is available, to enable new entrants, encouraged by the prospect of a reasonable flow of future tendering opportunities, to marshal the necessary resources;
- explore ways of reducing the costs of bidding and consider reimbursing some or all of the costs of the standby bidder;
- review whether the specification of inputs in contracts either encourages or inhibits entry or innovation, and whether reducing the specification of inputs would be preferable; and
- explore alternative methods of contracting and balancing the contributions of the public and private sectors in order to gain the best value for money, for example by separating Design and Management responsibilities from Construction and Finance responsibilities.

2.139. We believe that competition in the public sector markets affected by the acquisition could be further enhanced if the purchasers of the relevant services were to exercise their buyer power more effectively, and we put forward these suggestions for that purpose.