Completed acquisition by GXS of Inovis

The OFT's decision on reference under section 22(1) given on 25 June 2010. Full text of decision published 14 July 2010.

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. GXS and Inovis are global providers of business-to-business (B2B) e-commerce services and software solutions, which enable business documents, such as purchase orders, delivery information and invoices, to be processed and exchanged electronically between parties.

2. In the UK, GXS operates through GXS Limited (GXS UK) and Inovis through its wholly-owned subsidiary Inovis UK Limited (Inovis UK, formerly Harbinger Commerce Limited) and Freeway Commerce Limited (acquired in August 2007).

TRANSACTION

3. The parties entered into an Agreement and Merger Plan on 7 December 2009 (the Transaction). Pursuant to this agreement, a new holding company, incorporated in the US (NewCo), became the indirect 100 per cent parent of GXS and Inovis. The current GXS shareholders collectively hold 71.7 per cent of the equity in Newco, with the current Inovis shareholders collectively holding the remaining 28.3 per cent. The Transaction completed on 3 June 2010.

4. The Transaction is predominantly US-led, with the UK element of the Transaction comprising a relatively small part of the overall deal (less than 10 per cent of the total value of the deal). The OFT received a

satisfactory submission by the parties on 6 April 2010 and the administrative deadline was 24 June 2010.

JURISDICTION

5. As a result of the Transaction, GXS and Inovis will cease to be distinct enterprises within the meaning of section 26 of the Enterprise Act (the Act). Inovis's 2009 UK turnover was approximately [ ] so that the turnover threshold under section 23(1)(b) is not met.

6. The parties' share of supply of Electronic Data Interchange (EDI) messaging services in the UK exceeds 25 per cent, so that the Transaction qualifies for review under the Act.

BACKGROUND

7. The Competition Commission (CC) has previously considered EDI in *Francisco Partners/G international*, which was cleared in 2005.[1]

8. On that occasion the CC found that 'EDI is one of a number of electronic tools which were developed in the 1980s to provide a more efficient exchange of business information between trading partners using a specific means of formatting (a message content standard), and various ways of transmitting data.'[2] The business information exchanged between trading partners includes purchase orders, delivery/shipping information, invoices, and order status inquiries.

9. At its inception, EDI was carried out using direct point-to-point telecommunications lines. This method of exchanging data is suitable when the number of trading partners involved in the exchange is small. In the 1980s, however, as the number of businesses using EDI started growing intermediaries introduced private proprietary networks (called value-added networks, or VANs) to facilitate EDI messaging.

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[1] A report on the acquisition by Francisco Partners LP of G International, Inc, September 2005 ('CC report'). In particular, the section in the text above draws from section 2 of the CC report, and the parties' submission.
[2] paragraph 2.4 CC report

10. VANs allowed users to connect to a single access point for the VAN using an appropriate message content and communications protocol, rather than support independent direct connections to each of their trading partners.

11. In other words, VANs can be thought of as a form of 'electronic post office' which allows multiple trading partners that use different EDI standards to communicate with each other without the need for direct point-to-point connections. EDI VANs act as a post office, routing the documents and data to the recipient. EDI VANs also provide a number of additional services, for example, retransmitting documents, auditing and validating the information, acting as a gateway for different transmission methods, and handling telecommunications support.

12. An EDI VAN combines two elements: a) a physical communications and computing infrastructure, and b) data management processes that enable the handling and transmitting of messages that represent business transactions.

13. The role of 'traditional' EDI messaging (point-to-point EDI and EDI VANs) remained broadly unchanged until the late 1990s, when the emerging use of Internet technologies for the transmission of EDI messages started to transform this industry. In particular, the Internet made possible the introduction of several newer approaches, namely:

- traditional EDI VANs accessed via the Internet (rather than via leased lines or dial-up connections)
- internet EDI VANs (which rely on the Internet not only for the transmission of electronic documents to and from the VAN, but also for operating the VAN itself)
- web EDI, which allows smaller trading partners to exchange electronic documents through a web site (usually set up by a larger trading partner)
- point-to-point Internet EDI (including technologies such as AS2), where trading partners are connected directly to each other via

the Internet, and hence there is no need for direct leased lines and VAN infrastructure at all.[3]

14. As explained in detail below, the CC found that all these new Internet-based approaches were part of the same relevant market as 'traditional' EDI VANs.

15. In this case the parties also note the significant growth experienced by the provision of managed EDI services, whereby customers outsource their EDI messaging needs to service providers as opposed to the traditional approach of renting VAN infrastructure from intermediaries such as GXS. The OFT understands that EDI VANs usually remain an underlying component of managed EDI services (that is, unless direct, point-to-point solutions, such as AS2, are implemented). The main difference between managed and non-managed EDI services is that in the former case the service provider takes care of all aspects of the EDI service, for example, there is no need for the customer to retain dedicated staff in-house. In the case of non-managed EDI services, instead, the customer usually retains some dedicated staff in-house that are responsible for the day-to-day functioning of EDI. While it is possible that providers of managed EDI services to provide additional functionalities, for example, in terms of software customisation and usage data analysis, when referring to the term 'managed EDI services' the OFT is using it to describe the outsourcing of EDI messaging services. The parties note that [ ] estimates a compound annual growth rate of 17.9 per cent between 2007 and 2012 for managed services and that managed services are forecast to overtake traditional EDI messaging (in terms of revenues) by 2012. According to the parties, this growth has been driven by, amongst other factors, a desire by users for more functionality from their B2B provider than simply message transportation, as well as reducing the complexity of provisioning for hundreds or thousands of external business partner connections.

[3] It is often said that point-to-point Internet EDI (such as AS2) 'cuts the VAN out of EDI', to highlight that with these methods there is no need for an intermediary (that is, the VAN) to act as a post office and facilitate data interchange between trading partners.

PRODUCT MARKET

Introduction

16. In the UK, GXS and Inovis are both active at all different levels of the supply chain of EDI messaging services, namely:

- at the upstream level, they are active in the supply of the messaging infrastructure used in the provision of EDI messaging services (also known as the 'VAN')

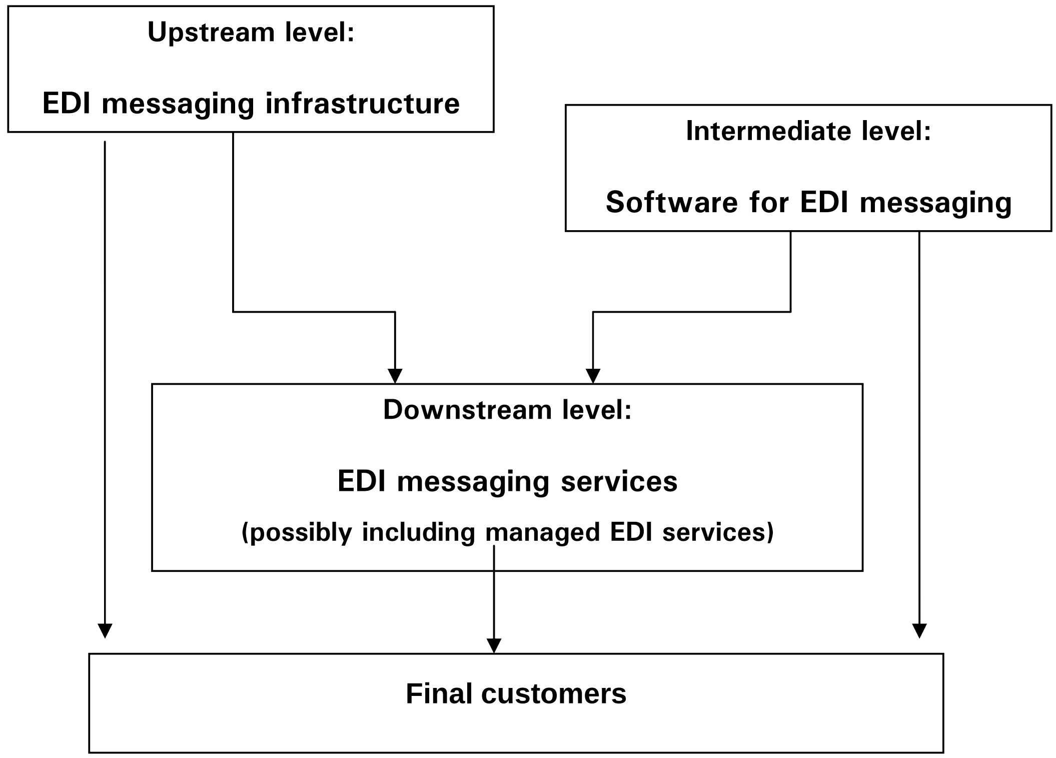
- at an intermediate level, GXS and Inovis supply software for EDI messaging

- at the downstream level, GXS and Inovis provide EDI messaging services and managed EDI services to final customers (for example, insurance brokers, large retailers, automotive industry, manufacturers and their trading partners).

17. The OFT's distinction above between upstream, intermediate and downstream levels is for convenience and ease of exposition only. The OFT understands that both infrastructure and software are complementary inputs into EDI messaging services, and therefore it would be incorrect to view infrastructure as an input into software (as the categorisation into upstream and intermediate levels above could imply). However, as EDI messaging infrastructure is also supplied on a merchant basis (that is, software providers or final customers can rent it), it makes sense in this case to consider theories of harm arising from market power in EDI messaging infrastructure (that is, at the 'upstream level' in the diagram below); hence, we consider the distinction above useful.

18. The chart below provides a graphical representation of this supply chain:

Figure 1: Supply chain for EDI messaging services



Source: OFT

19. Each of the parties is also a monopolistic provider of interconnection to its own EDI messaging infrastructure.[4]

20. The parties' sales in the different EDI messaging segments for 2009 are shown in the Table below.

[4] Furthermore, the parties also have some minimal overlap in data synchronisation and managed file transfer. Given the very small turnover of both parties in these two segments in the UK, the OFT does not consider them in any further detail.

Table 1: Parties' sales in the UK in 2009 – by segment

Company	EDI messaging[5]	Managed EDI services	EDI messaging + managed EDI services	EDI software	Other services	All services
	(a)	(b)	**(c) = (a) + (b)**	(d)	(e)	**(f) = (a) + (b) + (d) + (e)**
GXS	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]
Inovis	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]
GXS + Inovis	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]

Source: the parties

21. As the demand for infrastructure and software is largely derived from the demand for EDI messaging services, a sensible approach to market definition in this case is to look at the 'downstream' level first.

Product scope: EDI messaging services (the downstream market)

The CC's findings in 2005

22. In its report of 2005 the CC defined the relevant product market as 'the market for the transmission of EDI messages from one business to another' *(*paragraph 4.25). The CC described the market as 'EDI communication services' (paragraph 4.26).

23. According to the CC, this market included point-to-point EDI (also called direct-connect EDI) as well as 'traditional' EDI VANs. Both direct-connect EDI and traditional EDI VANs are accessed through telecommunications lines (that is, either leased lines or dial-up connections). In addition, the CC considered that the relevant market included the newer approaches that had been developed since the

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5 It was not possible for the OFT to separate revenues for EDI messaging services and EDI messaging infrastructure.

late 1990s exploiting Internet technology, referred to above in paragraph 13, namely traditional EDI VANS accessed via the Internet, Internet EDI VANs, web EDI and point-to-point Internet EDI (including technologies such as AS2). The CC found that these newer services were technically feasible and economically viable substitute for traditional EDI VANs.

24. As noted below (see the subsection on software for EDI messaging below), the CC included communication software (but not translation nor application interface software) in the same relevant market as EDI communication services. In addition, the CC did not consider managed EDI services, since this type of service had a marginal presence in 2005.

The parties' view

25. In this case the parties distinguish a market for EDI messaging and a market for managed EDI services. They agree with the CC's conclusion that the relevant product market for EDI messaging is wider than 'traditional' EDI VANs and should include all Internet-based solutions listed at paragraph 23 above. In fact, they argue that, given significant technological developments since 2005, the relevant product market should be even wider and also include managed EDI services on the basis that customers outsource their EDI messaging needs to external service providers (as opposed to the traditional approach of buying a complete EDI VAN solution from integrated players such as GXS and Inovis or from resellers).

26. Ultimately, however, the parties submit that it is not necessary for the OFT to conclude on product market definition because, even if managed EDI services are not included in the same market for EDI messaging, the proposed transaction will not give rise to a substantial lessening of competition.

The OFT's assessment in this case

27. The OFT is of the view that the appropriate market to consider at the downstream level is 'EDI messaging services'.

28. We have seen no evidence which would justify excluding Internet-based solutions for EDI messaging from the relevant market in this

case. These solutions appear to be well-established in the market and fully compete with 'traditional' EDI VANs.[6]

29. As to whether managed EDI services should also be included in the relevant market, the OFT notes the fact that revenues for managed EDI services are growing and are also forecast by industry sources to surpass the revenues associated with 'traditional' EDI messaging (which are reportedly stagnant) by 2012. However, this is not in itself evidence that managed services exert a competitive constraint on EDI messaging and therefore should be considered as part of the same market.

30. Similarly, the fact that managed EDI services fulfil the same basic function as the other types of EDI messaging included in the CC's market definition is not sufficient for the OFT to conclude that they are both in the same market (although it is, admittedly, consistent with them being in the same market).

31. On the other hand, the parties reported several examples of companies switching part or all of their EDI messaging traffic to providers of managed EDI services in recent years.[7] During its investigation the OFT also received a few responses from companies who had switched (or were considering switching) to managed EDI services. Third parties also told us that outsourcing of part or the whole of EDI messaging needs by firms is a growing trend. While it is therefore plausible that managed services do constrain EDI messaging services, the OFT does not have evidence that switching to managed EDI services from EDI messaging is related to changes in relative prices of EDI messaging, for example, so as to be able to definitively conclude that customers would switch to managed EDI services. The OFT cannot therefore draw definitive conclusions on market definition from this movement towards managed EDI services.

32. Ultimately, however, the OFT considers that in this case it is not necessary to conclude on whether managed EDI services are in the

[6] While point-to-point Internet EDI may not have grown rapidly over the last years (see below), it is still an alternative option to EDI messaging.
[7] The parties mention that [ ] are examples of GXS customers who recently switched from traditional EDI messaging to managed EDI services. Examples of customers who recently outsourced their EDI requirements to Inovis include [ ] and [ ].

same relevant market as the other EDI messaging solutions identified by the CC in 2005. This is because the competitive assessment is largely unaffected by this issue, since at the downstream level the same competitors who provide EDI messaging services are also able to provide managed EDI services (and indeed they do), and these include the merging parties as well as their main competitors (for example, Sterling Commerce, Easylink, Descartes, Crossgate, DiNet) and resellers (for example, [ ], [ ], [ ]). In addition, evidence provided by the parties does not suggest that there is stronger competition between the parties in respect of EDI managed services. In addition, other providers of managed EDI services (for example, B2B / e-commerce vendors) can be treated in a similar way as resellers (in that they also need to procure EDI messaging infrastructure from third parties), and any competitive constraint which they exert on the parties is appropriately considered in the competitive assessment below.

33. In addition, the inclusion of managed EDI services in the relevant market (which the OFT understands is smaller, although growing) does not significantly change the competitive assessment.

Product scope: Software for EDI messaging (the intermediate market)

The CC's findings in 2005

34. In its report of 2005 the CC said (at paragraph 4.21) that EDI software can be classified in three categories:

- communication software, which permits communication, including data transmission, with the VAN
- translation software, which converts data from the in-house format into the agreed EDI standard before transmission (or the reverse for incoming messages), and
- application interface software, which imports and exports data between customers' in-house applications and the translation software.

35. The CC noted that communication software is usually provided as part of the EDI service, whereas application interface software and translation software are often provided by specialist software

providers. On this basis, the CC concluded that communication software is part of the same market as EDI messaging, but that translation and application interface software are in a separate (but related) market.

The parties' view

36. In this case the parties submit that the boundaries between these different types of software are blurring. They note that 'today, a more common classification of EDI software includes 'stand-alone EDI translators' (equivalent to translation software in the [CC] Report), which interprets incoming EDI information and converts it into the format used by the company's internal systems; and 'gateway software' (comprising both application interface software and communication software as defined in the [CC] Report), which is used to consolidate and centralise a company's data and to interoperate with external business partners.'

37. Accordingly, the parties submit that the distinction between communication software and other types of EDI software is no longer appropriate since most software packages have both translation and communications capabilities, and therefore all three types of software should be included in an EDI software market which is separate from EDI messaging services.

The OFT's assessment in this case

38. The OFT's market investigation confirms that the boundaries between these different types of software have blurred since 2005. This suggests that there is an EDI software market (possibly comprising communication, translation and application interface software) at the 'intermediate' level of the supply chain that is distinct from EDI messaging services.

39. In any event, the parties' overlap in this market is limited as confirmed by third parties (given the weak position of GXS in software). There are also several other software suppliers in this market. As such, the OFT does not need to conclude on the precise scope of the EDI software market. In addition, because of the lack of horizontal concerns, the OFT does not consider the EDI software market further in the competitive assessment described below.

Product scope: EDI messaging infrastructure (the upstream market)

40. The CC did not explicitly consider the market for EDI messaging infrastructure in its report of 2005. However, given the OFT's market investigation, that has revealed the market structure identified in paragraph 18 above, the OFT has considered it appropriate to define the upstream market which third parties typically refer to as 'infrastructure', 'the VAN', 'backbone services' or 'the network component of EDI messaging'. This includes Internet connections or telecommunications lines, servers, mainframes, data centres, and all the infrastructure components that are needed for the exchange of electronic data. Historically, 'traditional' EDI VANs were proprietary but the advent of newer Internet-based technologies (for example, AS2) has reduced their importance.

GEOGRAPHIC MARKET

41. In 2005 the CC found that there were significant price differences for EDI services across countries. It also noted that many European and US EDI VAN providers did not sell in the UK and the prominence of the UK-specific Tradacoms standard in the UK retail, food and beverage sectors. On this basis, the CC concluded that the relevant geographic market was the UK.

42. In this case, while the parties submit that the relevant geographic market is global, they acknowledge that the OFT will want to consider the impact of the transaction in the UK and therefore provide share of supply and revenue information on this basis.

43. The OFT considers that in this case it is possible that the geographic boundaries of the upstream market for EDI messaging infrastructure are wider than the geographic scope of the market for EDI messaging services. In particular, the OFT notes that neither GXS nor Inovis have data centres in the UK (nor indeed do some of their competitors such as Sterling Commerce). However, the OFT does not need to conclude as to the precise scope of the geographic market for EDI infrastructure as its competitive assessment does not change on any plausible candidate geographic market.

CONCLUSION ON FRAME OF REFERENCE

44. In summary, the OFT considers that EDI messaging infrastructure and EDI software represent two distinct product markets. Infrastructure and software are complementary to each other inasmuch as both are used to provide EDI messaging services. In turn, EDI messaging services forms a distinct market at the downstream level. This market may include managed EDI services, although the OFT does not need to conclude on this specific issue.

45. As to the geographic scope, the OFT considers that EDI messaging, managed EDI services and EDI software markets are UK-wide while the market for EDI messaging infrastructure could be wider than national. Ultimately, the OFT does not need to conclude on whether this is the case or not.

ASSESSMENT

46. The OFT has examined the following effects of the merger:

- **horizontal** unilateral effects in the downstream market for EDI messaging services
- **horizontal** unilateral effects in the upstream market for EDI messaging infrastructure
- **vertical** unilateral effects in the downstream market for EDI messaging services (which can result in foreclosure of resellers and other competitors), and
- **conglomerate** effects in the downstream market for EDI messaging services.

47. The OFT has received no evidence to cause concerns that the merger would increase the possibility of tacit or explicit coordination and this will not, therefore, be analysed further. The OFT's concerns on unilateral effects are discussed in detail below.

I. HORIZONTAL UNILATERAL EFFECTS

I.A The downstream market for the supply of EDI messaging services to final customers

48. The parties overlap in the supply of EDI messaging services. The OFT has therefore examined the possibility that after the merger the merged entity could unilaterally increase prices or otherwise worsen terms to customers in the downstream market for EDI messaging services.

49. The OFT's investigation has shown that competition in EDI messaging services does not only occur on price. Third parties have indicated that quality of service is important given the business-critical nature of EDI messaging. In addition, some third parties have indicated that they consider Inovis's EDI messaging to be of higher quality than the GXS's, and that GXS is generally perceived as a less innovative player in the market.

50. In respect of horizontal unilateral effects, the parties submit that the proposed acquisition does not result in a realistic prospect of a substantial lessening of competition because:

    - Inovis does not add significantly to GXS' market share and is largely complementary to GXS's EDI messaging business

    - GXS and Inovis exert only a very limited competitive constraint on each other in EDI messaging, and

    - there are additional competitive constraints.

51. The OFT's assessment of the parties' arguments is below.

Number of providers of EDI messaging services

52. In its 2005 report the CC noted that prior to the merger 'GXS was by far the largest provider of EDI communication services with over two-thirds of the market' and that GXS had a particularly strong position as a provider of EDI services to retailers and their trading partners, thanks to the Tradanet network it set up in 1985.[8]

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[8] See Section 2 of the CC report

53. The other major providers of EDI communication services to the UK market identified by the CC (other than IBM, the target) were Easylink and BT. The CC also identified Sterling Commerce (currently owned by AT&T, but in the process of being acquired by IBM[9]), Harbinger Commerce (now Inovis) and Internet Commerce Corporation (ICC, which traded as Freshlook in the UK) as providers of EDI services in the UK (albeit all with a very small market share).

54. The CC also noted that a number of EDI software providers resold third-party EDI VAN services combined with their own software. These resellers included Freeway Commerce, Kewill Systems, Perwill, Data Interchange, SAA Consultants, Atlas Products International, Cyclone Commerce, iSoft Corporation and Cleo Communications, as well as (in the personal lines insurance sector) Software Solutions Partners (SSP) and Misys Financial Systems.

55. Overall, the CC concluded that 'resellers have a small share of the market (five per cent) and generally provide services to smaller customers which often need individualised support'.

56. The OFT notes that since 2005 there have been some examples of consolidation, exit and expansion (in particular of EDI competitors that are being bought by or are partnering with large software companies moving into EDI VAN). In particular, BT exited the EDI messaging market in 2010 and is no longer offering EDI VAN services to new or existing customers. Among resellers, Freeway Commerce was acquired by Inovis in 2008 and Perwill was acquired by Kewill in 2005. In addition, ICC/Freshlook acquired Easylink (which retained the name) in 2007. Furthermore, as noted above, IBM has recently announced it will re-enter the EDI market by acquiring Sterling Commerce from AT&T.

57. The OFT's market investigation has also revealed that there are additional vertically integrated (albeit small) EDI providers in the UK such as Tradocs, netEDI, DiNet and nuBridges. In addition, the OFT is aware of a number of resellers who are active in the EDI segment but who were not explicitly mentioned in the CC's report such as Seeburger, Crossgate and Orbit.

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[9] IBM's acquisition of Sterling Commerce from AT&T was announced on 28 May 2010.

58. The parties also submit that a significant and growing competitive constraint on providers of EDI messaging services is exerted by B2B/e-commerce vendors that deliver some combination of EDI messaging and managed services,[10] system integrators,[11] specialist IT providers[12] and ERP ('Enterprise Resource Planning') vendors.[13] More specifically, the parties submit that the real growth area in EDI services relates to the ability of service providers to conduct business analytics for their customers (which involves analysing customers' data that is transmitted through the EDI system the customer has in place) in order to provide customers with valuable strategic information. The parties considered that there were signs of new entry or re-entry by large B2B firms, such as IBM, Oracle and SAP through acquisition, strategic partnership or enhanced reseller arrangements with the parties' EDI messaging services competitors.

59. The OFT notes the recent trends in the B2B segment, as evidenced by the announcements of the acquisition of Sterling Commerce by IBM,[14] the SAP/Crossgate Global Reseller Agreement[15] and the partnership between Oracle and E2Open. Likewise, it also notes that [ ] recently chose an integrated product offering supplied by IBM/WeSupply and Inovis[16] for its EDI messaging and other business analysis requirements. These trends, however, are very recent and the OFT's market investigation did not wholly support the parties' view as to the extent that these system integrators currently constrain the parties. Furthermore, no convincing evidence has been supplied as to the likely level of future constraint these B2B firms may impose over and above the current constraints imposed by the EDI messaging firms they have acquired or partnered with, and in any event, the level of existing constraint from such EDI messaging firms is already taken into account in the competitive assessment as regards all areas of overlap where they currently impose a constraint. Therefore, on a cautious basis, only limited weight has been placed

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[10] According to the parties, the main vendors that provide these B2B integration / e-commerce solutions in the UK include: InflueGroup, Kleinschmidt, T-System, TIE Commerce, TrueCommerce and SWIFT.
[11] For example, Accenture, Atos Origin, HP (EDS) and IBM.
[12] For example, Oracle, SAP and Crossgate.
[13] For example, the partnership between SAP and Crossgate.
[14] 25 May 2010
[15] 23 February 2010
[16] In this case, Inovis was providing the EDI messaging infrastructure

in the OFT's analysis on the constraint from the purported entry of large systems integrators/B2B players.

Shares of supply

60. The market for the supply of EDI messaging services (at the downstream level) is characterised by an absence of publicly available data, which makes it difficult to calculate the size of the market and hence individual market shares.

61. In its 2005 report the CC estimated the total market size in 2004 to be between £25 million and £30 million but noted that it could shrink from 2005 onwards because ASDA and its trading partners were expected to move traffic away from 'traditional' EDI VANs to AS2-based point-to-point Internet EDI communication. The report noted that GXS had more than two-thirds of the market.

62. The parties estimated that in 2009 EDI messaging and managed EDI services in the UK were worth £[60-70] million and £[40-50] million, respectively. Given these figures and their sales, the parties calculated the market shares shown in the table below and in Annex I.

Table 2: Parties' sales (in £m) and market shares in the UK in 2009 – as calculated by the parties

Company	**EDI messaging (a)**		**Managed EDI services (b)**		**EDI services (c) = (a) + (b)**		**EDI software (d)**	
GXS	[ ]	[20-30]%	[ ]	[0-10]%	[ ]	[10-20]%	[ ]	[0-10]%
Inovis	[ ]	[0-10]%	[ ]	[0-10]%	[ ]	[0-10]%	[ ]	[0-10]%
GXS + Inovis	[ ]	[ ]%	[...]	[ ]%	[ ]	[ ]%	[ ]	[ ]%
TOTAL market size	£[60-70]m		£[40-50]m		£[ ]m		£[40-50]m	

Source: The parties

63. As can be seen from Table 2, the parties estimated that post-merger the merged entity would have a combined share of [ ] per cent (GXS: [20-30] per cent; Inovis: [0-10] per cent). This share does not take into account the fact that BT exited the market in 2009. Based on the assumption that BT's share would be distributed amongst the remaining suppliers in proportion to their relative size (as estimated by the parties), the parties calculate that their combined market share would increase to [ ] per cent (with an increment of [0-10] per cent) in the market for EDI messaging.

64. In view of this, the parties submit that there can be no credible horizontal concerns that the merged entity would have the ability to raise prices as a result of the merger as the increase in share of supply is negligible (an increment of [0-10] percent if managed services are excluded and [0-10] percent if they are included).

65. While the OFT acknowledges the significant difficulties in calculating the market size and shares in this case, it has the following concerns in relation to both the methodology used by the parties to calculate the market size and the results:

- In order to calculate the market size for EDI messaging, the parties used [ ] estimate of the global spending on B2B Integration as a Service (IaaS) for 2009.[17] In order to calculate the size of the UK market, the parties used the UK share (8.3 per cent) of global spending on IT services. The OFT notes that it may not be appropriate to use [ ] IaaS market segmentation as a proxy for the relevant product market in this case as this appears to include other products (for example, e-marketplaces) which were explicitly excluded from the CC's definition of the relevant market in 2005, and in any event do not appear to be substitutes for EDI messaging services. In addition, the assumption that the UK share of global spending on IT services is the same as the UK share of EDI messaging appears contradicted by other evidence.[18]

[17] [ ]

[18] In particular in arriving at their market share figures the parties assume that Internet EDI, web EDI, and point-to-point solutions accounted in 2009 for a quarter of the total market. However, data from GXS show that its sales of EDI VAN and EDI VAN accessed via the Internet in 2009 accounted for £[10-20] million out of a total of £[10-20] million, that is, [90-100] per cent, which greatly exceeds one quarter.

- The OFT notes that the parties' estimate of the size of the market (£[60-70] million) is more than twice the size of the CC's estimate of the market in 2004. The market for EDI messaging services in the UK, however, appears to have been declining in value terms since then (or at best to have been stagnant)—notwithstanding an apparent increase in volumes—because prices are falling as the cost of transmitting data declines. Even if, as the parties claim, the CC significantly underestimated the value of the market in 2004,[19] a value of £[60-70] million for EDI messaging **only** does not appear supported by the OFT's understanding of market trends since then.

- Evidence provided to the OFT by some competitors in respect of their EDI messaging services turnover also indicates that the market size calculated by the parties is too large.

66. On the basis of the evidence available to the OFT the market for EDI messaging services (including managed EDI services) is between approximately £40 and £50 million in value.

67. Based on the total market size estimates arising from the OFT's market investigation, the Table below summarises the parties' market shares (and the implied diversion ratio from GXS to Inovis) in the supply of EDI messaging services only and EDI messaging services including EDI managed services.

Table 3: Parties' market shares and implied diversion ratios from GXS to Inovis under different assumptions about market size

UK market size, excluding managed services	£40m	£50m
GXS	[40-50]%	[30-40]%
Inovis	[0-10]%	[0-10]%
GXS + Inovis	[ ]%	[ ]%
Implied diversion ratio from GXS to Inovis*	**4%**	**3%**

[19] The parties argue that the CC figures might only include providers of traditional EDI VANs (that is, exclude Internet EDI, web EDI and point-to-point EDI), and therefore underestimate the total market size.

UK market size, including managed services	**£40m**	**£50m**
GXS	[40-50]%	[40-50]%
Inovis	[0-10]%	[0-10]%
GXS + Inovis	[ ]%	[ ]%
Implied diversion ratio from GXS to Inovis*	**10%**	**6%**

Source: OFT analysis.

Note:*the diversion ratio from GXS to Inovis is calculated as (Share of Inovis)/(100 per cent - Share of GXS).

68. Under these alternative (and in the OFT's view more realistic) estimates of the market size, the proposed transaction could give rise to prima facie competition concerns on the basis of high combined market shares.

69. Furthermore, the OFT's concerns in this case are not allayed by the parties' submission that the increment attributed to the proposed transaction is small. Firstly, the increment may be as large as [0-10] per cent. Secondly, a small increment may well be problematic in a market where the other merging party has a large presence since the merger removes a significant part of the small competitive constraint left in that market. Thirdly, even a small increment in market shares could be considered problematic in markets characterised by high switching costs. Fourthly, small players can sometimes have disproportionate competitive impact beyond that implied by their market shares. For example, if GXS and Inovis were particularly close competitors pre-merger, the OFT could have cause for concern.

70. To assess these prima facie concerns, the OFT has therefore proceeded to examine (i) further evidence on the competitive interaction between GXS and Inovis in the UK, that is, whether pre-merger, they are close competitors; (ii) the position of other participants in the market; (iii) whether switching costs are significant; and (iv) barriers to entry/expansion in this market.

(i) Evidence on the competitive interaction between GXS and Inovis in the UK

Evidence on closeness of competition between the parties from GXS' cancellation data

71. GXS provided the OFT with data relating to contract cancellations for the period 2005 – 2009. In most instances these data record the general reason why a contract with GXS was cancelled (for example, breach of contract, customer request, switching to a competitor, no longer using the system, etc.) and, for each of these general reasons, a more detailed comment (for example, 'moved to Inovis' within 'moved to a competitor').[20]

72. The parties submitted that these data show that the competitive interaction between GXS and Inovis is very limited, since the percentage of GXS's customers by revenue which cancelled to switch to Inovis in each of the last three years is [less than one] per cent.

73. The OFT, however, has analysed separately those instances which record customers cancelling their contract with GXS because they move to a competitor. The results of this analysis in terms of revenue and number of customer diversion from GXS to Inovis are shown in Table 4 below.

Table 4: Diversion ratios from GXS to Inovis calculated from GXS' cancellation data

Variable of interest	2006	2007	2008	2009	All years
Number of customers	[30-40]%	[20-30]%	[30-40]%	[40-50]%	[30-40]%
Revenues	[20-30]%	[10-20]%	[40-50]%	[30-40]%	[20-30]%

Source: OFT analysis of parties' data.

[20] The cancellation data provided by Inovis did not allow for the type of analysis described in the text above.

74. Analysis of the cancellation data shows that more customers leaving GXS in 2009 went to Inovis and Freeway than to any other competitor, and that Inovis was the second most popular destination for customers leaving GXS (after [ ]) in 2007 and 2008. This is consistent with third party views that Inovis became a stronger competitor in the UK after acquiring Freeway Commerce in 2007. In addition, the data shows that GXS lost most revenues to [ ], followed by Inovis. The data also shows diversion to [ ], [ ] and [ ].

75. The parties submitted that the cancellation data analysed by the OFT are not robust enough to provide an indication of diversion ratios on the basis that:

- in the cancellation data, information on which competitor customers were moving to is extremely limited, since a competitor is explicitly recorded only in [50-60] cases out of a total [2000-3000] cancellations, a statistically insignificant sample

- because it records only 'total substitution' (that is, complete switching) by a customer, the cancellation data over-represents smaller customers as these customers are most likely to switch all their business. As smaller customers are more likely to switch to Inovis/Freeway than GXS's customers as a whole, the OFT's diversion ratios to Inovis and Freeway are biased upwards

- the information recorded in the cancellation data is at times erroneous and it is reasonable to expect that a customer would eventually move to a competitor even in most of the instances where the stated reason for cancelling was different from 'moving to a competitor', and

- the competitive picture emerging from GXS' cancellation data appears inconsistent with other market information, since [ ].

76. We did not accept the parties' arguments for the following reasons:

- statistically speaking, the [50-60] observations available to the OFT provides sufficient degrees of freedom to accurately estimate the handful of diversion ratios that are relevant to the OFT's analysis. Further, on a revenue basis, the [50-60] instances of cancellation represent almost [10-20] per cent of the total revenue lost by GXS over the last five years, which is a sizeable sample

- the sample does not appear to over-represent smaller customers. For example, the average revenue per customer of GXS customers lost to Inovis is [ ] and to Freeway is [ ] both of which greatly exceed the average value of Inovis and Freeway customers generally ([ ] and [ ], notwithstanding that the cancellation data is in US dollars). Neither does the data supplied by the parties on the size distribution of all GXS customers and of customers in the cancellation data show that the cancellation data over-represents smaller customers to an extent sufficient to explain the OFT's diversion ratios

- the parties identified [0-10] instances (out of [20-30]) where a customer that was recorded in the cancellation data as having moved to Inovis or Freeway did not appear in either company's sales data. However, the parties also identified at least [0-10] customers who were recorded as not having switched to Inovis or Freeway but who actually did so,[21] and

- the picture that emerges from the cancellation data is not obviously inconsistent with other market information. In particular, the parties' observation that Sterling and Easylink are the second and third largest players in the market is premised upon their shares of the installed base of EDI messaging customers. In a market with potentially high switching costs (see further below), smaller competitors (with a smaller installed base) may be more likely to target customers who are likely to switch than are larger competitors (with a larger installed base).[22]

77. The parties also note that many of the customers recorded as moving to Inovis are in fact moving to Freeway. The parties consider this to be relevant since according to their later submissions, Freeway offers markedly different solutions to Inovis and, as a consequence, they argue, may be active in a different segment of the overall EDI messaging services market. In particular, the parties argue that Freeway would not be a direct competitor of GXS as it

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[21] Footnote 3 in CRA's paper of 3 June 2010 'Validating GXS's Cancellation Data'.
[22] See paragraph 115 *Anticipated acquisition by Lloyds TSB plc of HBOS plc*, Report to the Secretary of State for Business Enterprise and Regulatory Reform, 24 October 2008

offers what they describe as 'a midmarket integrated solution' to customers (with a different profile to GXS or Inovis customers) that is not a substitute for the GXS product. Thus, the parties consider that the distinction between Freeway (vertical issue) and Inovis (horizontal issue) may be relevant to the weight that can be attached to the OFT's analysis of their cancellation data.

78. The OFT considers that this representation is not consistent with the results of the market investigation in this case for the following reasons:

- the OFT's understanding is that before its acquisition by Inovis in 2007, Freeway rented EDI messaging infrastructure from GXS and combined this infrastructure with its own software to offer a fully integrated EDI messaging service to its customers. In this respect, Freeway competed in the downstream market (that is, the supply of EDI messaging services to final customers, for example, retailers and their trading partners) not only with other resellers (Kewill, Orbit, etc.) but also with 'vertically integrated' players such as GXS and BT. In particular, while GXS' Tradanet and Freeway's Spectrum EDI solutions[23] may be heavily differentiated, on the basis of the evidence gathered so far we consider that they are substitute products for (at least a significant portion of) final customers

- following its acquisition by Inovis, Freeway ceased to rent the VAN from GXS and migrated all its customers onto Inovis's VAN (that is, Inovisworks). Freeway, however, has maintained its brand and its range of software solutions. We also understand that these solutions are particularly suitable for small and mid-size customers, so that the combined Inovis/Freeway entity can now offer a **fuller** range of solutions (that is, Inovisworks plus Freeway's Spectrum solutions). Freeway products are, however, also used by larger customers, such as [ ] so (while its product may be differentiated) the OFT does not see the Freeway solution as belonging to a different market than the GXS product, and

- in any event, it is clear that there is some switching (that is not insignificant) from GXS to Freeway, and that the corresponding

[23] These are the EDI messaging products marketed by GXS and Freeway respectively.

diversion ratios are higher than those implied by market shares, contradicting the argument that Freeway and GXS do not compete at all.

79. The diversion ratios calculated from the OFT's analysis of the GXS cancellation data are therefore high enough to give rise to a rebuttable presumption of horizontal unilateral effects. The following sections therefore discuss other evidence that, taken together, successfully rebuts this presumption.

Evidence on closeness of competition between the parties from win/loss and pipeline data

80. In order to assess the extent to which Inovis provides a competitive constraint on GXS, the parties matched Inovis and GXS UK pipeline and sales datasets and therefore made the following observations:

- **The match between GXS' opportunities list and Inovis' two datasets:** in seeking to assess the extent to which GXS and Inovis compete for the same opportunities, and the extent to which Inovis is successful in winning opportunities that were also targeted by GXS, the parties examined the extent of the overlap between Inovis' pipeline database in 2008/09 (consisting of [50-60] unique customer names) and GXS' opportunities data. On the basis that that the overlap between the parties' respective pipeline data is limited to [0-10] instances, the parties submit that GXS and Inovis UK target different opportunities.

- **The match between GXS' list of existing customers and Inovis' two datasets**: the parties also sought to measure the extent to which Inovis actively targets GXS' customers (as opposed to seeking de novo implementations or 'poaching' from other competitors). They therefore matched GXS' EDI messaging sales data for 2008/09 (containing [4000-5000] unique customer names corresponding to [3000-4000] unique existing customers) against the [50-60] unique customer names appearing in the Inovis' pipeline database. Since only [30-40] GXS customers appear in Inovis' pipeline data, the parties concluded that Inovis targets a very small portion of GXS's customer base.

- **The match between GXS' list of lost customers and Inovis' two datasets:** the parties also sought to estimate how many customers (a) considered switching, and (b) ultimately switched away from GXS to Inovis UK, which they submit is the most accurate proxy for the diversion from GXS to Inovis, in the event of a price increase by GXS. The parties defined a GXS customer as a 'loss' if GXS's EDI messaging revenue for that customer falls by 80 percent or more between 2008 and 2009.[24] Using this method, the parties identified [500-600] GXS losses, representing [ ] of revenue in 2008. Subsequently, they checked how many of these [500-600] instances could be found in Inovis' pipeline sales opportunities data and list of new customers for 2008/09 and identified [0-10] instances. Since at most [0-10] out of a total of [500-600] customers lost by GXS during 2008/09 switched to Inovis[25] the parties submitted that Inovis UK does not represent a material competitive constraint on GXS in EDI messaging.

81. The OFT also notes, in respect of the parties' win/loss analysis, that the majority of Inovis' targeting activity (that is, [30-40] out of [50-60] opportunities) is focussed on GXS customers. This appears to be in line with the OFT's best estimate of GXS' share of supply. In addition, out of Inovis' new customers, only [0-10] matched GXS' lost customers. This would point to a relative competitive interaction between GXS and Inovis that is in line with their market shares and does not paint a competitive picture showing Inovis to be a particularly aggressive competitor to GXS.

Internal documents and analyst reports

82. The OFT has reviewed some internal documents relating to the parties' ordinary course of business, only some of which were prepared prior to the merger being announced, as well as some [ ] and [ ] reports submitted by the parties.

83. As a preliminary point, the OFT notes that most documents focus on the US (where both GXS and Inovis make most of their sales and

[24] In the parties' view, this captured switching customers even if they do not cancel – for example, customers switching only part of their messaging traffic away from GXS; or customers ceasing to use the GXS service, but not cancelling their mailbox.
[25] In fact only [0-10] appear in Inovis' pipelines data

which forms the centre of the transaction). Some internal documents, however, also monitor the parties' activities in the UK.

84. In general, GXS does appear to be monitoring Inovis' activities in the UK and does refer to Inovis' growing credibility in Europe (especially following the IBM/WeSupply/Inovis win for the [ ] contract). However, internal documents also show GXS monitoring a number of other competitors (including both integrated suppliers and resellers) such as [ ], [ ], [ ], [ ], [ ], [ ], [ ], [ ] and [ ].

85. In addition, [ ] and [ ] analyst reports provided by the parties, albeit in a worldwide context, confirm the multiplicity of competitors active in this market in addition to the merging parties.

86. On this basis, while the OFT considers that internal documents provided do show that GXS and Inovis compete against each other, they also indicate that GXS faces significant competition from a number of other firms. There also appears to be nothing in these internal documents that would 'single out' Inovis as GXS' closest (or most aggressive) competitor in the UK.

Inovis' competitive position in the UK market for EDI messaging services

87. The parties submit that, given the relatively small amount of sales realised by Inovis in the UK (that is, [ ] and [ ] for EDI messaging and managed EDI services, respectively), regardless of the UK market size, Inovis does not exert a significant competitive constraint on GXS and therefore any lessening of competition caused by the merger would be negligible.

88. The OFT notes that the figures quoted by the parties refer to 2009, that is, when BT was still active on the market. While it is possible that revenues for 2010 for Inovis will be higher as a result of BT's exit, the OFT's market investigation did not necessarily support this. For example, Inovis did not appear to have a surge in customer numbers following BT's exit. In addition, the letter that BT sent to its customers prior to terminating its service includes a long list of alternative suppliers of EDI services, among which Inovis is not particularly prominent. In addition, [ ].

89. Some third parties consulted by the OFT in this case said that Inovis and GXS offer similar products and are direct competitors in the UK.

Furthermore, Inovis' acquisition of Freeway Commerce in 2007 – combined with its investment in new infrastructure – seems to have strengthened its competitive position in the UK since 2007. However, while the acquisition of Freeway has increased Inovis' customer base, it is not clear that Inovis has been particularly growing its EDI messaging services since 2008. Inovis has also confirmed that (excluding the Freeway customers that were migrated onto its VAN following its acquisition of Freeway) it has only [40-50] EDI messaging customers and, despite efforts by management and the advertised quality of its network, it has not been particularly successful in growing its UK business through attracting customers from its competitors. This is confirmed by the analysis of Inovis' win/loss data provided by the parties, that show that out of the [500-600] customers that GXS lost in 2008/2009, only [0-10] of these switched to Inovis.

(ii) Position of other competitors in the market

90. The cancellation data discussed above, show that there is significant diversion from GXS customers to other competitors such as [ ], [ ] and [ ]. This was also supported by the OFT's market investigation: customers named a range of other competitors to the parties (including Sterling Commerce, Easylink, Kewill, Seeburger and DiNet) that could provide EDI messaging services in addition to the parties.

(iii) Customer inertia and switching costs

91. The parties also submit that the number of new customers seeking *de novo* implementation of EDI messaging solutions is extremely limited, as most new customers prefer to invest in more modern B2B integration solutions such as managed services. In addition, they claim that existing customers (the 'installed base') are reluctant to switch provider and refer to the CC's finding in 2005 that the market was characterised by 'customer inertia'. Accordingly, they claim that any competitive interaction between GXS and Inovis is minimal.

92. As discussed above, and as a related point, the OFT would tend to be more concerned about relatively small increments in market shares where customers face high switching costs.[26]

93. The OFT's market investigation has revealed that the parties' claims regarding customer inertia are not necessarily consistent with customer views, nor with the evidence obtained from the GXS' cancellation data or the win/loss data discussed in the previous subsection. In addition, while there are some switching costs the OFT notes that the advent of newer Internet-based technologies for EDI messaging may have made it easier and cheaper for customers to switch providers, compared to the situation examined by the CC in 2005. Indeed, some of the parties' competitors are marketing the ease with which firms can switch providers.[27] While some customers indicated that there are some switching costs involved in changing EDI provider, they did consider switching to be possible (and, in fact, some customers had recently switched).

94. Moreover, internal documents from GXS state that loss of customers to competitors is the largest driver of cancellation by far, accounting for [ ] per cent of all cancellations.[28] This would indicate that competition is not muted and that switching costs are not preventing customers from changing their EDI service provider.

95. Accordingly, the OFT considers that the evidence available at present does not support the parties' claim that there is limited competition in EDI. However, as a corollary to that, the evidence also does not indicate that switching costs are such that moving to a different EDI provider is excessively difficult: the evidence shows that customers can and do indeed switch (or consider switching) to a different provider of EDI VAN services. In light of this, the OFT does not consider that there are such high switching costs that would warrant particular concern for a relatively small increase in market share, as is the case here.

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[26] See paragraph 115, *Anticipated acquisition by Lloyds TSB plc of HBOS plc*, Report to the Secretary of State for Business Enterprise and Regulatory Reform, 24 October 2008
[27] See, for example, www.easylink.com/easylink-services/edi/edi-van.php, www.nubridges.com/managed-services/edi_van , www.netedi.co.uk/news.aspx
[28] GXS' 2010 Strategy Review and Planning Meeting (dated 16-17 September 2009)

(iv) Entry and expansion

96. Third parties told us that there has not been any significant entry in EDI messaging in recent years. In fact, it appears that the preferred way for firms to expand is by acquisition (recall the acquisitions by Inovis, ICC/Freshlook and GXS of Freeway Commerce, Easylink and G International, respectively), rather than by organic growth. In addition, BT exited the market in 2009/10.

97. However, the OFT also notes the dynamic aspects of this market and the recent announcement of IBM's acquisition of Sterling, SAP's recent reseller agreement with Crossgate and the relationship between Oracle and E2Open. While it is not necessary for the OFT, given its findings above, to conclude on whether these instances of expansion into EDI would avert any finding of substantial lessening of competition, it is mindful of their occurrence and the possibility that competition in EDI services could be more intense going forward.

Conclusion

98. The parties' combined market share in EDI messaging services is high enough to give rise to prima facie competition concerns and these are confirmed by the OFT's analysis of the closeness of competition between the parties from GXS's cancellation data. In contrast, however, the parties' matching analysis of their various sales datasets indicates that the competitive interaction between them is in line with estimated market shares (so that Inovis does not appear to be exerting a particularly significant constraint on GXS).

99. Further, additional qualitative evidence indicates that while Inovis is a direct competitor to GXS in the UK market (and there is consequently some competitive interaction between them) the merged entity will still face significant competition from a range of other EDI messaging service providers such as Sterling Commerce, Easylink, Kewill, Descartes, DiNet, Atlas, Crossgate and Orbit, that could replicate the constraint that Inovis was exerting on GXS prior to the merger. The OFT in particular notes the position of Crossgate (that has recently entered into a deeper co-operation agreement with SAP) and [ ]. The OFT also notes the recent entry by other significant software players through partnering with or acquiring

existing EDI competitors (such as IBM and Oracle), that could further strengthen the position of these EDI competitors, although it has not needed to rely on these recent events in order to reach its conclusions. The OFT's investigation has not revealed significant customer concerns regarding the merger.

100. In light of the above, the OFT considers that the merger does not lead to a realistic prospect of a substantial lessening of competition in the downstream EDI messaging market.

I.B The upstream market for the supply of EDI messaging infrastructure

101. The merger combines the largest provider of EDI messaging infrastructure in the UK (GXS) with another infrastructure provider (Inovis), although the latter appears to have a smaller presence. This therefore gives rise to horizontal concerns in the upstream market for the supply of EDI messaging infrastructure. While any foreclosure concerns are examined in more detail below, the OFT has examined the horizontal concerns separately given that there is a merchant market for EDI messaging infrastructure (that is, some customers purchase EDI messaging infrastructure separately and combine it with EDI software themselves).

102. There is a lack of information on market shares at the upstream level. Apart from GXS and Inovis, the two other significant providers of EDI messaging infrastructure in the UK are Easylink and Sterling Commerce. In addition, there are a number of other smaller competitors such as Descartes, DiNet and nuBridges.

103. The OFT's market investigation has shown that EDI messaging infrastructure is a commoditised product and that its providers face no capacity constraints.

104. Moreover, the OFT notes that there does not appear to be a requirement for EDI messaging infrastructure (which, as discussed in paragraph 40 above, relates to the 'backbone' required in order to transmit data) to physically be present in the UK: indeed neither GXS or Inovis have their infrastructure in the UK. Third parties have also confirmed that EDI messaging infrastructure does not need to be in the UK.

105. In light of the above, the OFT does not consider that the merger gives rise to a realistic prospect of a substantial lessening of competition in the supply of EDI messaging infrastructure.

II. VERTICAL UNILATERAL EFFECTS

106. In general, the OFT acknowledges that most vertical mergers do not raise competition concerns, and can in fact be pro-competitive. In this case, however, the OFT has considered two vertical theories of harm on the basis of third party complaints.

II.A Foreclosure by making access to EDI messaging infrastructure more expensive or difficult

107. Typically, resellers are software providers who combine EDI VANs (or other types of infrastructure) rented from a third party (for example, GXS, Inovis and others) with their own software. In addition, resellers provide managed EDI services (in a similar way to EDI messaging services providers that have their own messaging infrastructure such as GXS, Inovis, Easylink and Sterling Commerce).

108. Some third parties have expressed concerns that post-merger the parties might make access to their EDI messaging infrastructure more expensive or difficult for competitors who do not own such infrastructure. So as to assess these third-party concerns, the OFT has considered whether the parties will have the ability and incentive to foreclose competitors, and whether this foreclosure may give rise to anticompetitive effects.[29] In doing so, the OFT notes that—given the ability and incentive to do so—it generally regards total foreclosure as more likely to give rise to anticompetitive effects than partial foreclosure.

[29] In its 2005 report the CC noted that prior to the merger GXS had not generally made use of resellers in the UK market and that GXS planned to continue to operate the reseller contracts transferred with the merger with IBM. The CC also noted that any attempt by GXS to displace a reseller by raising prices or by approaching its customers directly could result in the reseller moving some or all of its existing or future business to another EDI VAN provider (paragraph 5.75). As a result, the CC concluded that it was not in GXS's interest to try and displace resellers (paragraph 5.87).

Ability to foreclose competitors in downstream EDI messaging services market

109. In respect of ability to foreclose, the OFT makes the following points:

- Further to its conclusion as to the absence of unilateral effects in the upstream market, the merged firm would not appear to have sufficient ability to make access to EDI infrastructure more difficult.

- The OFT has no evidence that the merged firm could credibly commit to refusing access to EDI infrastructure, because resellers could turn to other suppliers of EDI infrastructure. Indeed, the OFT notes that resellers [ ] multisource their infrastructure from a number of providers.

- In addition, the OFT notes that resellers using GXS and Inovis have multi-year contracts with them so that there is no short-term ability to foreclose.

Incentive to foreclose competitors in downstream EDI messaging services market

110. In respect of the incentive to foreclose, the parties submit that GXS intends to continue to supply resellers post-merger and that there is every incentive for it to do so. In particular, the parties note that GXS currently achieves significant revenues through sales of EDI VAN to [ ], [ ] and [ ] for resale with their EDI software products (approximately [ ] for FY09) which would be lost in the event that a foreclosure strategy was adopted post-merger.

111. Moreover, the parties note that, given the presence of alternative VANs and of alternatives to EDI VANs for EDI messaging (for example, AS2), it is highly unlikely that any potential foreclosure strategy would be profitable for the parties, as resellers could easily switch to using another VAN or another form of message transmission and so prevent customer loss.

112. However, given the OFT's conclusion that the merged entity would have no ability to foreclose resellers, it does not need to conclude on

the parties' incentives or on whether any foreclosure strategy would have detrimental effects on competition in this market.

113. In light of the above, therefore, the OFT does not consider that the merger gives rise to a realistic prospect of substantial lessening of competition through foreclosure of resellers by making access to EDI messaging infrastructure more expensive or difficult.

II.B Foreclosure by increasing interconnection costs or denying interconnection altogether

114. In 2005 the CC found that the historic practice in the UK had been not to impose any charges to customers for interconnection between networks (paragraph 5.36). Moreover, GXS had submitted to the CC that it had an open policy on interconnection and considered all requests from other networks to interconnect according to a defined set of rules, taking account of various factors such as the expected volumes of traffic in each direction. GXS also told the CC that whilst it reserved the right to charge for interconnecting with EDI VANs, to reflect the relative value realised by the providers from the interconnection, such charges have only exceptionally been levied by GXS, and never in the UK (paragraph 5.41). In conclusion, the CC considered that the market for EDI messaging exhibited some network effects because of the preferences of some customers to be on the same network as their trading partners and because of some perceived potential problems with interconnection, but did not consider these effects to be sizeable (paragraph 5.43).

115. During its current investigation, the OFT received the following third party concerns:

- some third parties expressed concerns that post-merger GXS could levy an interconnection fee or increase its level to allow interconnection to the combined GXS/Inovis network and hence access to the parties' customer base. More specifically, if GXS charges for interconnection, competitors could be driven out of the market. This is because their customers will inevitably need to be interconnected to a GXS network (in order to exchange data with trading partners on the GXS network) and the imposition of an interconnection fee would increase competitors' costs and make their offer uncompetitive.

- Some third parties also expressed concerns that post-merger GXS could deny interconnection to the combined GXS/Inovis altogether.

- Third parties noted that GXS had changed (or had attempted to change) its administrative practices in relation to letting its customers switch to competitors. In particular, it appears that while in the past GXS only required notification from the new EDI provider, it has recently started to require notification of the cancellation from all trading partners involved in the switch.

116. Given these concerns, the OFT has further investigated whether the merger could result in foreclosure of competitors through the raising of interconnection costs or through altogether denying interconnection.

Ability to foreclose competitors in downstream EDI messaging services market

117. In respect of imposing interconnection fees, post-merger the merged entity will be the monopoly provider of interconnection to the combined GXS/Inovis network. Accordingly, the merged entity's ability to foreclose access to the GXS/Inovis network is not in dispute.

118. Regarding third party concerns that administrative practices were increasing switching costs for customers, GXS submitted information to the OFT regarding the migration of its systems to a new platform whereby customers would be able to set up their own interconnects going forward thereby obviating the burdensome requirement of notifying GXS in this respect. The OFT understands that this was done for administrability reasons and was not related to the merger.

Incentive to foreclose competitors in downstream EDI messaging services market

119. In respect of incentives, some third parties told us that in the past GXS has made repeated (although reportedly mostly unsuccessful) attempts to charge an interconnection fee for access to its network. In addition, [ ]. The parties make the following points in this respect:

- the GXS interconnect policy was in place prior to the merger and the merger does not result in a change in incentives to grant interconnection given the small increment to the GXS customer base

- the interconnection charge is in place to cover the costs that GXS incurs for interconnecting these smaller EDI service providers to its own VAN where the volume of data flowing through these small providers (and consequent cost) does not justify the cost for GXS of interconnecting them for free

- customers expect to be able to interconnect so that any attempt to make interconnection with trading partners more difficult will impact customers' business and, by implication, GXS' business

- transactions flowing through interconnects are a source of revenue for GXS: smaller EDI VAN players often grow the market by offering EDI VAN services to customers/industries that did not traditionally use it so there is no incentive for GXS to foreclose them. and

- terminating interconnects entails costs for GXS so that it would not be incentivised to do so.

120. From the information provided to the OFT by GXS, it is clear that GXS' interconnection policy was in place prior to the merger and that, given the small increment to GXS following the merger, it does not appear to the OFT that the merger has resulted in any change in incentives to GXS. In addition, the rationale for imposing interconnection costs pre-merger does not appear to have been exclusionary and the merger does not appear to change this.

Effects on competition in EDI messaging services

121. Given its conclusions on ability and incentives, the OFT does not need to conclude as to the effect on competition in EDI messaging services of any increase in interconnection costs.

122. In light of the above, the OFT does not consider that the merger gives rise to a realistic prospect of substantial lessening of competition through foreclosure of interconnection to the parties' EDI messaging infrastructure.

III. CONGLOMERATE EFFECTS

123. As shown in Table 1 above, in terms of sales GXS is focused on EDI messaging services, whereas Inovis is focused on EDI software. Several third parties also told us that that unlike Inovis, GXS is not a strong player in the EDI software market.

124. Some third parties have expressed concerns that the proposed acquisition would create a dominant player with a strong position in both EDI messaging infrastructure and software which will be able to offer a 'one-stop shop' for all customers' EDI needs. The same third parties have expressed concerns that [ ] post-merger GXS will leverage its strong position in the market for EDI messaging infrastructure to increase sales of EDI software, and vice versa. In this respect, these third parties told us that GXS already has a 'preferred partner' relationship with Inovis as a provider of EDI software, and expressed the view that the merger will further consolidate this relationship. In addition, they submitted that the foreclosure effects described in this section might be exacerbated by the existence of 'network effects' in view of the fact that GXS is currently the largest provider of EDI messaging services in the UK.

125. Final customers may have a preference for purchasing an integrated EDI messaging service from a single provider (such as a reseller), for example, because they enjoy economies of scale in purchasing ('one stop shopping'). The OFT considers that bundled selling arising from a merger in the presence of such economies of scale are generally competitively benign. However, given the complementary nature of EDI infrastructure and software, if there is a large pool of common customers for an integrated EDI messaging service then bundled selling arising from the merger could nonetheless result in conglomerate effects leading to foreclosure of competitors in the downstream market.

126. However, as discussed in section IB above, EDI messaging infrastructure is a commodity product; the OFT has received no evidence that GXS' VAN is a 'must have' product. Similarly, although Inovis has been put forward as a strong player in software, the OFT has not received any evidence that its software product is 'must have'.

127. In light of this, the OFT does not consider that this case gives rise to a realistic prospect of a substantial lessening of competition through competitor foreclosure from conglomerate effects.

THIRD PARTY VIEWS

128. Third parties' views were discussed above where appropriate.

129. In general, there were some limited concerns [ ]. The concerns related to any reduction of quality of service post-merger.

130. There were mixed responses from competitors [ ].

ASSESSMENT

131. The parties overlap in the supply of EDI messaging infrastructure services, in the supply of EDI software and in the supply of EDI services. The OFT had no initial concerns in relation to EDI software given that there are numerous players and the parties' combined position did not give rise to any preliminary concerns.

132. The OFT had preliminary concerns in relation to the provision of EDI messaging services where it estimated that the parties' combined market share would be approximately [30-60] per cent with an increment of [0-10] per cent. Such an increment could, prima facie, give rise to concerns (in particular where switching costs are high). In addition, analysis of cancellation data provided by the parties led to some further concerns regarding the competitive interaction between the parties and specifically, that they might be stronger competitors than their market shares suggested. However, additional analysis of the parties' customer datasets (provided by the parties) showed less significant interaction between the parties. The OFT further examined additional evidence to ascertain whether GXS and Inovis competed particularly closely and whether a competitor would be able to replicate any loss of constraint by Inovis on GXS post merger. The OFT's investigation (including third party comments and GXS pre-merger internal documents) showed that there are a number of competitors active in the UK that could replicate any competitive constraint exerted by Inovis. In addition, the OFT's market investigation showed that switching was possible and that costs of switching were not particularly high.

133. The OFT also examined unilateral effects in the upstream EDI messaging infrastructure and (related to this) the possibility of foreclosure of resellers of EDI services by refusing access to EDI messaging infrastructure or raising their costs. The OFT found that this upstream market is of a commodity product that and that there are no capacity constraints in providing EDI messaging infrastructure.

134. The OFT also considered whether, following the merger, the merged entity would foreclose competitors by refusing interconnection to its EDI VAN or imposing a charge in respect of this. While the OFT considered that the merged entity would have the ability to do so, this was a policy formulated by GXS prior to the merger and, given the small increment to GXS following the merger in the UK, it did not consider that the merger significantly altered its incentives to charge an interconnection fee.

135. Finally, the OFT considered whether there would be any conglomerate effects arising out of the merger given the parties' strong position in each of EDI messaging infrastructure and EDI software. However, the OFT's market investigation did not show that either of the parties' 'inputs' are 'must have' so that the OFT did not consider that there would be any such conglomerate effects arising out of the merger.

136. In light of the above, the OFT does not believe that it is or may be the case that the merger may be expected to result in a substantial lessening of competition within a market or markets in the United Kingdom.

DECISION

137. This merger will therefore **not be referred** to the Competition Commission under section 22(1) of the Act.

ENDNOTE

1. In relation to paragraph 3, the parties informed the OFT that the Transaction in fact closed on 2 June 2010, but was publicly announced the next morning on 3 June 2010.