25 May 2016

ANTICIPATED ACQUISITION BY IRON MOUNTAIN INCORPORATED OF RECALL HOLDINGS LIMITED

RESPONSE TO PROVISIONAL FINDINGS

This submission is made on behalf of Iron Mountain Incorporated ("Iron Mountain") in response to the CMA's Provisional Findings Report dated 4 May 2016 (the "Provisional Findings").

Iron Mountain agrees with the CMA's provisional determination that the Transaction cannot reasonably be expected to result in a substantial lessening of competition ("SLC") in England, given the fragmentation of existing supply and ability of numerous rivals to compete effectively. For reasons discussed in Iron Mountain's Response to the CMA's Notice of Possible Remedies and at the subsequent remedies hearing, Iron Mountain considers that a divestment of C21 Data Services Ltd ("C21") would offer a comprehensive, reasonable and practicable remedy to the SLC identified in the Provisional Findings with respect to North-East Scotland and, given the relatively limited nature of that remedy, the company sees little value in continued debate about the competitive effects of the Transaction in that region alone. However, Iron Mountain sets out below a few observations about the Provisional Findings which the company believes would strengthen the assessment and further support the conclusions laid out there.

I. Product market definition

As a preliminary matter, whilst of somewhat secondary importance to the ultimate conclusions in this case, Iron Mountain believes that discussion of the relevant product markets in the Provisional Findings should be revised in two areas, namely, [i] recognition of supply-side substitution amongst RMS and OSDP, and [ii] treatment of in-house supply of RIMS.

A. Supply-side substitution

Whilst competition regulators normally place primary reliance on demand-side substitution in defining relevant markets, it also is generally recognised that there are some circumstances in which supply-side substitution alone may constitute reason to broaden the relevant market definition. As noted in a leading economics treatise, *"[a] hypothetical monopolist . . . would not find it profitable to increase prices relative to other products if either a sufficient number of consumers would switch to other products . . . or suppliers of other products could easily and quickly begin to supply the products of the hypothetical monopolist (i.e. supply-side substitution provides an effective competitive constraint)."*[1] The CMA's *Merger Guidelines*, likewise, recognise that supply-side substitution can be an important part of proper market definition.[2]

The Parties have provided clear evidence that a RIMS supplier can provide OSDP services with essentially the same assets and infrastructure as are used to provide RMS. No appreciable investments are required – RMS providers can (and do) supply OSDP services from document warehouses, with negligible investments in things like a fireproof safe or, potentially, through the use of *existing* rooms that are already used to store valuable documents and require no OSDP-related investment whatsoever.[3] The CMA's determination that supply-side substitution does not support a market encompassing both RMS and OSDP therefore is very difficult to reconcile with the facts, and essentially writes supply-side substitution out of the analysis entirely – it is difficult to envisage any case in which supply-

1 Simon Bishop & Mike Walker, *Economics of EC Competition Law* (3rd ed. 2010), paragraph 4-028.

2 CC2/OFT1254 – *Merger Assessment Guidelines* (Sept 2010 (revised)), paragraphs 5.2.17-5.2.19.

3 See Iron Mountain's White Paper on Entry and Expansion (14 April 2016), pages 3-4.

side substitution might warrant a broadening of the relevant product market if it does not do so here.[4]

In light of the foregoing, Iron Mountain respectfully submits that the CMA's assessment should be revised. At a minimum, the company believes that the CMA may provide a more solid assessment, if it chooses to assess RMS and OSDP separately, by reserving judgment as to any "market" definitions and simply finding it unnecessary (in light of its ultimate conclusions with respect to any SLC) to define the relevant markets in this regard.

B. In-house RIMS supply

The CMA has concluded that in-house provision of RIMS should not be included in the assessment of market structure.[5] Iron Mountain agrees with that, but respectfully submits that the CMA's current analysis appears to obscure the relevant considerations here. Iron Mountain recognises that the OFT, in 2003, addressed in-house provision of RIMS as a facet of "market" definition, but the company itself has not done so, and finds such an analysis rather puzzling. By way of analogy, one might also consider whether a merger of florists should include the "shares" of all flowers that were grown in consumers' own gardens – an analysis that would be difficult to defend. Iron Mountain respectfully submits that in-house supply can play an important role in the competitive assessment, but in some cases (including this one) that role is to be found in an assessment of competitive constraints, rather than in definition of the relevant markets.

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4 While the CMA has provisionally concluded that "Existing RMS suppliers would be no better placed to substitute into the supply of OSDP than suppliers in other sectors who might be involved in warehousing and transport" (Provisional Findings, paragraph 6.22), one would have thought that this is evidence of how easy it is for a warehouse operator to store computer tapes and therefore would *support* expansion of the relevant market to include both RMS and OSDP. Iron Mountain is not aware of any authority for the proposition that supply-side substitution is important only where it is easier for the parties in a market affected by a transaction than it is for companies operating in other types of businesses. Likewise, the fact that "[s]ome of the largest RMS providers offer OSDP services from some of their sites but were not able to separate out OSDP revenue" (*id.*, paragraph 7.152) would appear to provide compelling evidence that the costs of providing both services from a single facility are so small (too insignificant to justify separate accounting treatment) that the two services cannot be regarded as appreciably different from a supply perspective.

5 See, e.g. Provisional Findings, paragraphs 10 ("we were not persuaded that in-house provision of these services should be counted as part of the market"), 6.24-6.29 ("we provisionally conclude that in-house RMS is not in the same product market as outsourced RMS").

No party has suggested that RIMS users might divert their in-house services to the supply of potential customers (i.e. that consumers would choose to become vendors) if market conditions made new entry desirable. Likewise, in its Provisional Findings, the CMA has based its estimates of market shares on company turnovers (and not, e.g. on some measure of production/capacity where in-house operations might bear consideration).[6] Consistent with its prior submissions, Iron Mountain respectfully submits that the role of in-house services should be assessed as a potential competitive constraint on market supply, rather than as a part of the market structure itself.

II. Entry and expansion

Given the fact that RIMS supply is already very fragmented and competitive, the prospects for new and continuing entry/expansion should not be required for a finding that the Transaction cannot reasonably be expected to result in an SLC. However, if the CMA addresses entry/expansion in its final decision, Iron Mountain believes it would be inexplicable to continue resting on repeated expressions of scepticism that future entry/expansion will occur. The record demonstrates conclusively that entry/expansion has occurred with great frequency in recent years, and a number of competitors have told the CMA in this review that they have plans to continue to enter and expand.[7]

It appears to be common ground, in the submissions of the Parties and results of the CMA's market testing, that barriers to entry into the supply of RIMS are low. RIMS providers can enter and/or expand very rapidly, as competitive conditions warrant, both because barriers to entry are low, and because rivals can compete effectively for new business before they must establish the facilities required to service business that they win. Likewise, it now appears to be common ground that the transportation and warehousing of customer records is a "commodity" service in which possible competitive differentiators (e.g. the quality of service/security or resulting reputational benefits) are extremely limited or non-existent, at

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6 For reasons noted previously, Iron Mountain considers that any estimates of market shares in this industry are broad approximations at best, and do not contribute meaningfully to the competitive assessment. The point here is not to endorse such estimates, but simply to point out that the use of revenues in this regard would appear to make consideration of in-house operations (as a matter of market definition) inappropriate.

7 See, e.g., CMA Working Paper on Entry and Expansion, paragraph 35.

least with respect to such a large number of rivals that they cannot make an appreciable difference to the competitive assessment.

Despite the foregoing, in its assessment of entry/expansion, the CMA has made several provisional findings that Iron Mountain believes cannot be sustained on a reasonable evaluation of the evidence. Each of these is noted briefly below.

A. Price declines

The CMA has suggested that new entry/expansion is less likely given the fact that prices are currently declining in the RIMS industry.[8] However, entry/expansion is normally viewed as important facets of a merger assessment because they may constrain the parties' efforts to raise prices to non-competitive levels post-merger.

The CMA's focus on current price declines appears to be misguided, because it focuses on current (or past) conditions, rather than on potential rivals' likely responses to any future price rises. It is the ability and incentive to respond *if competitive conditions warrant* (i.e. if prices rise above the competitive level) that should be important. In treating evidence that the market is operating very competitively (i.e. that prices are falling) as evidence that potential competitive constraints (i.e. new entry/expansion) may be ineffective, the CMA seems to have missed this fundamental point.

B. Pre-investment bidding

It is a common feature of the RIMS industry that competitors may bid on contracts before they have the storage capacity that they will need if they win the business. Such capacity is then added following an award. This ability to expand following a contract award is important for two principal reasons. First, it is clear that the ability to compete for new business is not limited by any current ability to service that business. Second, the views of the Parties and their customers and competitors, as expressed in the CMA's market testing,

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8 See, e.g. Provisional Findings, paragraphs 27, 7.108 ("We also note that there are currently declining charges for storage, reducing the attractiveness of entry").

make clear that a *single* contract may be sufficient to ensure that it is commercially feasible and attractive to open a new warehouse.

The CMA appears to have discounted the importance of entry/expansion that is predicated on vendors' winning new business.[9] However, that potential vendors can compete for new business without having to invest first in new assets/infrastructure makes new entry/ expansion a *particularly significant* competitive constraint on existing suppliers. Small customers that have insufficient volumes of business to attract bids requiring post-award investments doubtless have recourse to a large number of relatively small RIMS providers, and cannot be of concern here. What might be of concern is procurements by relatively large customers, who may be served by somewhat fewer RIMS vendors – but those are the customers that, almost by definition, have sufficient volumes of business that new rivals are motivated to bid even without the existing assets/infrastructure to service the business post-award.

In dismissing the fact that RIMS vendors can – and, the record shows, regularly do – bid on business before investing in the capacity that is needed to perform on an award, the CMA erroneously discounted strong evidence that the RIMS market is open to intense competition, and will continue to be post-merger.

3. Likelihood of entry

As noted above, Iron Mountain has submitted evidence of new entry/expansion (on a product-market or geographic-market basis) in just the past three years by Box-It, EDM, Hill Company, HW Coates, Kelly's Storage, Oasis, Recall, Restore, and Stor-A-File, to name a few.[10] Some of these initiatives have been entry into new geographic markets (whether *de novo* or by acquisition) and others have been from adjacent kinds of businesses. In any event, it is incontrovertible that entry/expansion is endemic in this industry.

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9 See, e.g. Provisional Findings, paragraph 27 ("While we have seen examples of investments in new facilities by established providers, this is usually based on securing a major customer in advance, and so it is very uncertain that this will be a generally applicable constraint").

10 See Iron Mountain White Paper on Entry and Expansion, at pages 8-9 and the Appendix thereto.

In the circumstances, questions about whether new entry/expansion is *likely* appear to be wholly misplaced – such questions more logically relate to a potentiality that has not yet been realised, or to the possibility that circumstances may change so materially that what was previously observed will not continue. Neither predicate can be supported in the record in this case.

The CMA itself has found that *"[t]here is a trend for customers to move from in-house, 'unvended', storage to outsourced, 'vended' storage for RMS"*.[11] While the CMA has observed that the Parties have [*confidential information redacted*], one would expect (given the existence of switching costs, on which the CMA has placed significant emphasis elsewhere) that customers newly entering the market are most likely to award their business to newer/smaller rivals – not to a long-established provider, with [*confidential information redacted*] legacy business, like Iron Mountain. Likewise, the evidence clearly shows that existing customers continue to generate significant volumes of records that must be sent to off-site storage, and that customers do switch providers.[12]

As noted in the Provisional Findings, a number of RIMS vendors have confirmed to the CMA that they plan continued entry/expansion initiatives. This (coupled with the frequent instances of entry/expansion in recent years) demonstrates that the RIMS industry offers substantial commercial opportunities to new and expanding operators. Accordingly, whilst the CMA may question rivals' willingness to pursue a growth strategy, the evidence on record clearly shows that the threat of rivals' expansion is a strong and credible constraint on the Parties.

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11 CMA Working Paper on Industry Background and Transaction, paragraph 20 (emphasis added). Moreover, while the CMA has suggested that such growth is "slow" because "more than half" of new storage volumes reflect organic growth of existing customers' business (Working Paper on Entry and Expansion, paragraphs 9(a), 82(b)), one must question whether the agency isn't confusing the importance of a glass-half-full with a glass-half-empty; it is certainly Iron Mountain's view, and appears to be the views of many whom the CMA consulted in market testing, that potential customers who do not yet outsource their RIMS requirements offer substantial business opportunities.

12 See, e.g. CMA Working Paper on Entry and Expansion, paragraphs 82(b)(i) (acknowledging that "customers do switch") and 58 (noting that "most" suppliers pay perm-out fees or offer other incentives to win business away from rivals).

III. Switching costs

The CMA has also questioned whether switching costs within the RMS sector (including so-called "perm-out" fees) may restrict competition.[13] Iron Mountain has submitted a White Paper on Switching Costs (April 14) in which it has reviewed past studies by the OFT and findings by the Competition Commission on this topic. These indicate, *inter alia*, that:

- Switching costs may make competition more vigorous (rather than less) in markets, like this one, where a new award is likely to entail a significant, long-term income stream for which opportunities to compete are unlikely to recur for some time (i.e. switching costs may create competitive dynamics much like those that exist in formal bidding markets).

- Switching costs may facilitate new entry/expansion in markets by smaller operators, who have some assurance that their investments will be covered and are likely to capture inordinately high volumes of business from larger incumbents.

Many of Iron Mountain's views in this regard reflect points from an economic study that was commissioned by the OFT roughly 10 years ago.[14] Surprisingly, the CMA appears to have wholly disregarded this study in its Provisional Findings. Iron Mountain respectfully submits that the agency's final decision may be made more analytically robust, and public confidence in the economic rigour of its assessments may be enhanced, by more considered development of those points, which provide strong evidence that switching costs are likely to enhance (rather than impede) effective competition in this sector.

Conclusion

As noted above, Iron Mountain considers that the CMA's Provisional Findings set out a sound conclusion, that the Transaction cannot reasonably be expected to result in a substantial lessening of competition ("SLC") in England, given the fragmentation of existing

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[13] See, e.g. Provisional Findings, paragraphs 16, 7.21.

[14] OFT665 – *Economic Discussion Paper 5: Switching costs* (April 2003).

supply and ability of numerous rivals to compete effectively. Moreover, given the relative ease with which the potential SLC in North-East Scotland may be remedied, through a divestment of C21 Data Services Ltd ("C21"), Iron Mountain sees little value in continued debate about the competitive effects of the Transaction in that region alone. However, Iron Mountain offers the observations above in the hope that they may assist the CMA in finalising a statement of findings that is both analytically sound and consistent with the evidence in this case.