# Completed acquisition by DX Network Services Limited of the businesses and assets of The Legal Post (Scotland) Limited and First Post Limited

# Decision on relevant merger situation and substantial lessening of competition

**ME/6627/16**

The CMA's decision on reference under section 22(1) of the Enterprise Act 2002 given on 21 October 2016. Full text of the decision published on 17 November 2016.

**Please note that [✂] indicates figures or text which have been deleted or replaced in ranges at the request of the parties for reasons of commercial confidentiality.**

## SUMMARY

1. On 27 May 2016, DX Network Services Limited (**DX**) acquired the businesses and assets comprising each of The Legal Post (Scotland) Limited (**Legal Post**) and First Post Limited (**First Post**) (the **Merger**). DX, Legal Post and First Post are together referred to as the **Parties**.

2. The Competition and Markets Authority (**CMA**) believes that it is or may be the case that the Parties' enterprises have ceased to be distinct and that the share of supply test is met. The four-month period for a decision, as extended, has not yet expired. The CMA therefore believes that it is or may be the case that a relevant merger situation has been created.

3. DX and Legal Post overlap in the supply of document exchange services for mail sent and received within Scotland. Customers that responded during the CMA's merger investigation did not consider other mail services, such as those offered by Royal Mail Group Ltd (**Royal Mail**) or other point-to-point mail operators, to be substitutable with document exchange services. Further, Legal Post's document exchange network is confined to Scotland and Legal Post does not compete for document exchange mail volumes sent or received

outside of Scotland. The CMA has therefore assessed the impact of the Merger on the supply of document exchange services for mail sent and received within Scotland.

4. Based on the evidence available to it, the CMA believes that pre-Merger:

   *(a)* DX and Legal Post competed closely for some customers and mail volumes, and that this competition may have exerted some downward pressure on DX's pricing.

   *(b)* As a result of the closed nature of document exchange networks and the limited overlap between their members, DX and Legal Post were only competing for a small volume of document exchange mail and so the degree of competition between the two providers was less than would usually be expected in a market where only two providers are present.

   *(c)* Actual switching between DX and Legal Post was limited, although the threat of switching could be expected to drive prices down for some customers.

   *(d)* While the pricing practices of DX and Legal Post indicated some constraint from Royal Mail's standard services, that constraint is unlikely to prevent price rises for at least some customers.

5. In light of the evidence of competition between DX and Legal Post pre-Merger and the lack of alternative suppliers, the CMA believes on balance that the Merger gives rise to a realistic prospect of a substantial lessening of competition (**SLC**) as a result of horizontal unilateral effects in the supply of document exchange services for mail sent and received within Scotland.

6. However, on the facts of this case, the CMA believes that it is appropriate to exercise the CMA's discretion to apply the de minimis exception to its duty to refer the Merger. In reaching this conclusion, the CMA has taken into account the size of the affected market (approximately £[1-5] million), the fact that DX and Legal Post were only competing for small volumes of mail sent and received through document exchange services within Scotland prior to the Merger, and that the decline of document exchange services means that any Merger effect is likely to be limited in duration.

7. The Merger will therefore **not be referred** under section 22(1) of the Enterprise Act 2002 (the **Act**).

# ASSESSMENT

## Parties

8. DX is a wholly-owned subsidiary of DX (Group) plc, a company listed on the AIM market of the London Stock Exchange and active in the parcels, mail and logistics sectors. DX is the trading company for DX (Group) plc's freight, document exchange, courier and mail services in the UK. The turnover of DX (Group) plc in the financial year ended 30 June 2016 was approximately £287.9 million in the UK.[1]

9. Legal Post comprises the businesses and assets of The Legal Post (Scotland) Limited, a company active in the supply of document exchange services in Scotland. Legal Post's turnover in the financial year ended 31 May 2016 was approximately £[1-5] million,[2] all of which was generated in Scotland.

10. First Post comprises the businesses and assets of First Post Limited, a company active in the supply of downstream access (**DSA**) services[3] in Scotland. The turnover of First Post in the financial year ended 31 May 2016 was approximately £[1-5] million,[4] all of which was generated in Scotland.

## Transaction

11. DX acquired the businesses and assets of Legal Post and First Post under two business purchase agreements. These agreements were signed on 9 May 2016 and the acquisitions completed on 27 May 2016.

## Jurisdiction

12. As a result of the Merger, the enterprises of DX, Legal Post and First Post have ceased to be distinct.

13. DX and Legal Post overlap in the supply of document exchange services for mail sent and received within Scotland and have a combined share of supply by revenue of more than 25%.[5] The CMA therefore believes that the share of supply test in section 23 of the Act is met.

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[1] DX (Group) plc Annual Report and Accounts 2016.
[2] Draft Financial Statements for The Legal Post (Scotland) Limited for the year ended 31 May 2016.
[3] These services involve collecting, sorting and transporting mail from customers to Royal Mail's inward mail centres for onward delivery by Royal Mail.
[4] Draft Financial Statements for First Post Limited for the year ended 31 May 2016.
[5] See share of supply analysis at paragraph 34.

14. The Merger completed on 27 May 2016 and was first made public on 31 May 2016. The four month deadline for a decision under section 24 of the Act is 18 November 2016, following extensions under section 25(2) of the Act.

15. The CMA therefore believes that it is or may be the case that a relevant merger situation has been created.

16. The initial period for consideration of the Merger under section 34ZA(3) of the Act started on 8 September 2016 and the statutory 40 working day deadline for a decision is therefore 2 November 2016.

## Counterfactual

17. The CMA assesses a merger's impact relative to the situation that would prevail absent the merger (ie the counterfactual). For completed mergers the CMA generally adopts the pre-merger conditions of competition as the counterfactual against which to assess the impact of the merger. However, the CMA will assess the merger against an alternative counterfactual where, based on the evidence available to it, it believes that, in the absence of the merger, the prospect of these conditions continuing is not realistic, or there is a realistic prospect of a counterfactual that is more competitive than these conditions.[6]

18. Neither DX nor any third party who responded to the CMA's investigation has submitted that the Merger should be considered against an alternative counterfactual. Therefore, the CMA believes the pre-Merger conditions of competition to be the relevant counterfactual.

## Background

19. Document exchanges are closed business-to-business user-group networks providing overnight delivery for enveloped mail and parcels. In order to send mail via a particular document exchange network, both the sender and recipient must be a member of that network. Each network comprises a number of exchanges housing individual customer (or member) mail boxes. Members visit their local exchange to deposit mail for delivery to other members at any exchange on the network and to collect mail delivered to their member box.

[6] *Merger Assessment Guidelines* (OFT1254/CC2), September 2010, from paragraph 4.3.5. The *Merger Assessment Guidelines* have been adopted by the CMA (see *Mergers: Guidance on the CMA's jurisdiction and procedure* (CMA2), January 2014, Annex D).

20. DX submitted that typical customers of document exchange networks are legal and financial services firms and public bodies. Customer responses received during the CMA's merger investigation confirmed that most customers use document exchange networks for sending and receiving mail to and from third parties. However, some customers (principally public bodies and some larger law firms) also use document exchange services to transfer mail between their own offices (with each office being an independent member of the network).

## Frame of reference

21. Market definition provides a framework for assessing the competitive effects of a merger and involves an element of judgement. The boundaries of the market do not determine the outcome of the analysis of the competitive effects of the merger, as it is recognised that there can be constraints on merger parties from outside the relevant market, segmentation within the relevant market, or other ways in which some constraints are more important than others. The CMA will take these factors into account in its competitive assessment.[7]

22. DX and Legal Post overlap in the supply of document exchange services for mail sent and received within Scotland.

23. DX and First Post overlap in the supply of DSA services. However, their activities do not overlap geographically: First Post is only active in Scotland while DX is only active in the rest of the UK, excluding Scotland. For the supply of DSA services in the UK as a whole, DX and First Post estimated their combined share of supply to be less than [0-5]%. As this horizontal overlap is negligible and does not give rise to prima facie competition concerns, it is not discussed further in this decision.

### *Product scope*

24. As a starting point, the CMA adopted a frame of reference for the supply of document exchange services.

25. DX submitted that Royal Mail's single piece priority mail services (comprising stamped, metered and account services) should be included in the relevant frame of reference.[8] However, the majority of customers that responded

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[7] *Merger Assessment Guidelines*, paragraph 5.2.2.
[8] Metered services, also referred to as franked mail, involve the customer applying the postmark and paying for postage using a franking machine which is pre-paid with credit. Account mail, which includes services such as Printed Postage Impressions (PPI), involves the customer paying for postage through an account with the Post

during the CMA's merger investigation either did not consider Royal Mail's services to be directly substitutable, or stated that they were substitutable but significantly more expensive.[9]

26. DX also submitted that the frame of reference should include other point-to-point mail operators, such as couriers, Royal Mail's Relay service[10] and in-house public sector networks. However, no customers cited Relay as an alternative supplier for document exchange services and those customers that the CMA specifically questioned about this service had not heard of it. No customers (whether in the public or private sector) cited in-house networks or third party couriers as viable alternatives to document exchange services. One private sector respondent stated that it had considered an in-house courier option when faced by rising document exchange costs, but found it to be uneconomical.[11]

27. The CMA considered whether each of DX's and Legal Post's document exchange networks should be defined as separate frames of reference. This is because mail cannot be sent between different networks and therefore both the sender and recipient must be a member of the same network in order to send and receive mail between each other. The CMA considered whether there existed particular customer 'networks' in Scotland, that primarily exchanged documents between one another, and which would consequently be more likely to use one document service provider or the other. DX submitted that customers of a certain size or with particular business needs may be more inclined to use one or the other supplier as their primary supplier, although not necessarily as a sole supplier. Third parties who responded to the CMA's merger investigation indicated that both DX and Legal Post compete to attract broadly the same customers to their networks and that customers on both networks have a choice, at least for some of their mail volumes, as to which network to use.[12] The CMA found that these views did not support the existence of distinct customer networks in Scotland.

28. For the reasons set out above, and on a cautious basis, the CMA believes that the appropriate product frame of reference is the supply of document exchange services. However, the CMA has taken into account the constraint from other mail service providers, including Royal Mail and point-to-point

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Office. Both offer a discount against Royal Mail stamp prices. Royal Mail submitted that both metered and account services are typically used by medium-sized businesses of 30 people or more.

[9] See further paragraph 51.

[10] Royal Mail's Relay service offers a schedule collection and delivery service between different sites of a customer's business.

[11] See further paragraph 53.

[12] See further paragraph 41.

operators, as well as the closed nature of document exchange networks, in its competitive assessment.

### *Geographic scope*

29. DX offers a UK-wide document exchange network, whilst Legal Post's document exchange network operates in Scotland only.[13] None of the internal documents submitted by DX or Legal Post gave the CMA grounds to believe that Legal Post had any plans to expand its network outside of Scotland.

30. In light of the above, the CMA believes that the appropriate geographic frame of reference is mail sent and received within Scotland.

### *Conclusion on frame of reference*

31. For the reasons set out above, the CMA has considered the impact of the Merger in the supply of document exchange services for mail sent and received within Scotland.

## Competitive assessment

### *Horizontal unilateral effects*

32. Horizontal unilateral effects may arise when one firm merges with a competitor that previously provided a competitive constraint, allowing the merged firm profitably to raise prices or degrade quality on its own and without needing to coordinate with its rivals.[14] Horizontal unilateral effects are more likely when the merger parties are close competitors. The CMA assessed whether it is or may be the case that the Merger has resulted, or may be expected to result, in a substantial lessening of competition in the supply of document exchange services for mail sent and received within Scotland as a result of horizontal unilateral effects.

*Shares of supply*

33. DX submitted that DX and Legal Post are the only providers of document exchange services for mail sent and received within Scotland. Ofcom confirmed that there are no other document exchange providers in the UK.

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[13] Legal Post confirmed that it offers customers a very limited service outside of Scotland (a weekly, courier-based title deeds return service to some lenders in England). Legal Post confirmed that this service is significantly slower than regular document exchange services. Given the very limited scale of this service and its lack of suitability for time-sensitive mail, the CMA does not consider that this service competes with DX's services and it is therefore not discussed further in this decision.
[14] *Merger Assessment Guidelines*, from paragraph 5.4.1.

34. DX submitted evidence that its document exchange revenue in Scotland in the financial year ended June 2016 was £[1-5] million, of which [90-100]% (£[1-5] million) related to mail sent and received within Scotland. According to Legal Post's financial accounts, its revenue for the year ended May 2016 was £[1-5]m.[15] On this basis, the parties' respective shares of supply of document exchange services for mail sent and received within Scotland in the 2016 financial year were approximately [40-50]% (DX) and [50-60]% (Legal Post).

*Closeness of competition*

35. The CMA assessed the extent to which DX and Legal Post were close competitors by reference to two key factors: levels of customer switching between DX and Legal Post and the pricing practices of each party.

*Levels of customer switching*

36. The CMA investigated two kinds of customer switching:

*(a)* Switching of entire contracts between suppliers; and

*(b)* Switching of mail volumes between suppliers.

37. In doing so the CMA assessed evidence that customers had switched and also instances in which DX or Legal Post had sought to win particular business from the other.

- *Switching of contracts between suppliers*

38. The CMA found that only a small fraction of customers (less than 5%) had switched from one party to the other in the past three years.[16] Further, whilst half of the customers that responded to the CMA's Merger investigation considered the two parties to be substitutes, only one customer had in fact switched between the parties and one other stated that it had threatened to do so.[17]

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[15] See footnote 2.

[16] The CMA based its analysis on data submitted by DX and Legal Post regarding customer boxes opened and closed with each party in the past three years. The CMA has taken into account that the degree of customer switching may be higher than suggested by its analysis, on the basis that the data provided only represents instances where an account associated with sending from a document exchange box was closed, and not instances where a customer stopped using their account for sending mail but retained a box (eg for receiving mail).

[17] However the contemporaneous correspondence submitted by this customer does not mention this specific threat to switch but only a protest at the increase in price.

39. The CMA's investigation also found that the parties only occasionally tendered against one another for the same contracts. [✄].[18] However, two DX internal documents indicated that DX had fought hard to win [✄] from Legal Post [✄].[19] Another DX internal document[20] discussed a proposed marketing campaign [✄], although DX submitted that this did not take place.

- *Switching mail volumes between suppliers*

40. The CMA found that only a small proportion of a customer's mail volumes could immediately be switched between the parties' document exchange networks.

41. As described in paragraph 19, in order to send mail via a particular document exchange network, both the sender and recipient of the mail must be a member of that network. As a result, only mail volumes sent and received between customers common to both DX and Legal Post could immediately be switched between the two suppliers. Customer lists submitted by DX and Legal Post demonstrated that only about half of DX customers and less than one third of Legal Post customers were common to both suppliers. Third party responses to the CMA's Merger investigation indicated that some customers perceived the proportion of their mail that could immediately be switched to be even lower. The CMA asked five customers to estimate the proportion of mail currently sent with their preferred supplier that could be sent via the other supplier. Four of these customers responded with estimates of 5%, 5-10%, 30% and 50% respectively. The fifth customer was unable to provide an estimate, but stated that it had limited contact with firms who were members of the other supplier.

*Pricing practices*

42. The CMA then analysed the pricing practices of DX and Legal Post to assess whether there was evidence:

    *(a)* that the two suppliers had set their pricing by reference to one another; and/or

    *(b)* that DX's prices in Scotland were lower than in the rest of the UK (where DX is the only document exchange provider) and, if so, whether this was a result of competition from Legal Post in Scotland.

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[18] [✄].
[19] An internal DX email described the tendered contract as [✄]. A further internal email stated [✄].
[20] [✄].

43. DX's pricing is based on an annual subscription model. Each customer is assigned to a particular tariff, which sets a nominal per-item rate for different weights and formats of mail. However, [✂].[21] [✂], the CMA believes that there is scope for competition to lead to different outcomes, even for individual customers on the same tariff.[22]

44. The CMA found that, while the majority of DX's customers were charged by reference to tariffs that did not vary between Scotland and the rest of the UK, [✂] subscription tariffs for DX's Scottish customers (representing £[✂] revenue in the 2016 financial year)[23] were specifically designed to provide a competitive rate against Legal Post prices. The CMA also found that one payment model available to new customers of Legal Post offered a 20% discount against the fees of the customer's existing document exchange provider (ie DX). However, the CMA understands that this payment option is little used by customers today.[24] [i]

45. Notwithstanding that the majority of DX's customers are on UK-wide tariffs, the CMA identified one DX internal document[25] which stated that [✂]. The CMA understands this statement to mean that DX was forced to lower its prices in Scotland as a result of competition from Legal Post. DX submitted that this statement was speculative and unqualified. The CMA compared average prices paid by DX customers in Scotland (taking into account negotiation) relative to those paid by customers in the rest of the UK. Using data submitted by DX,[26] the CMA found that customers in Scotland paid prices that were approximately [✂]% lower than in the rest of the UK in 2015, and approximately [✂]% lower in 2016.

46. The CMA believes that this evidence supports the proposition that DX was pricing lower in Scotland than in the rest of the UK prior to the Merger, which (in light of the DX internal documents reviewed by the CMA) may at least partly be as a result of competition with Legal Post. However, given the limitations of the data submitted by DX, and the possibility of other factors

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[21] [✂].

[22] Legal Post submitted that [✂] of its revenue is also from fixed fee contracts, negotiated between Legal Post and the customer. [✂] revenue is [✂] based on transactional pricing whereby customers are charged on a uniform basis according to the volume and type of mail sent. A small proportion of customers are charged on a headcount (per capita) basis, with no direct relationship between price and volume.

[23] Approximately [✂]% of DX's total Scottish revenues.

[24] Legal Post submitted that this option was principally used at Legal Post's inception in 2011 but is little used today. Legal Post estimated that only two customers (£2,600 revenue) were charged under this option in the past 12 months.

[25] [✂].

[26] DX provided a breakdown of revenues and annualised mail volumes (by weight category) for all member boxes which had been monitored in the past 24 months. DX submitted that monitored mail volumes represent only a relatively small proportion of total customer mail volumes and further that that this data is subject to several sources of error. The CMA used this data to compare the total revenues received from customers, against the amount which those customers would have paid on the basis of a strict application of one of DX's standard tariffs.

which could lead to this price differential (such as the cost of doing business in Scotland relative to the rest of the UK and, in particular, London) the CMA has not put weight on the size of the price differential implied by its calculations, nor on the changes in this differential between 2015 and 2016.[27]

*Conclusion on closeness of competition*

47. Based on the evidence above, the CMA believes that pre-Merger DX and Legal Post competed with one another to win particular customers, and that this competition may have exerted some downward pressure on DX's prices in Scotland for some customers.

48. However, as a result of the closed nature of the document exchange networks and the limited overlap between their members, DX and Legal Post only competed prior to the Merger for a small volume of document exchange mail and so the degree of competition between the two providers was less than would usually be expected in a market where only two providers are present. Furthermore, actual switching between the DX and Legal Post was limited, although the threat of switching could have been expected to drive prices down for at least some customers.

*Competitive constraints from outside the frame of reference*

49. The CMA assessed the extent to which Royal Mail and other point to point mail providers exercise some competitive constraint on document exchange providers in Scotland.

50. Specifically, DX submitted that:

    *(a)* Royal Mail's priority mail services offer very similar services to document exchange services and all document exchange customers use Royal Mail alongside document exchange services, making it easy for customers to switch;

    *(b)* services provided as part of Royal Mail's universal service obligations are VAT-exempt, allowing Royal Mail to offer a competitive advantage over document exchange providers, particularly for customers that cannot reclaim VAT;

[27] In addition to the limitations set out in footnote 26, the CMA has taken into account that the data was submitted at the member box, rather than the customer, level. In some cases, revenue may have been allocated to a single box, rather than distributed between a number of boxes held by a single customer. If affected customers have boxes in both Scotland and the rest of the UK, this may affect the CMA's estimate of the differential in prices between Scotland and the rest of the UK.

(c) both DX and Legal Post [✂], and Legal Post offers up to 50% discount against Royal Mail's first class stamp prices;[28] and

(d) Royal Mail's specialist service Relay[29] is also an alternative to document exchanges, particularly for large financial institutions. DX cited two recent examples of DX customers switching to Relay, each worth £[✂] of lost revenue, and one of which primarily related to Scottish mail volumes.

51. However, the majority of customers that responded to the CMA's merger investigation stated either that Royal Mail's services are not substitutable for mail volumes currently sent via document exchange or that they are substitutable but significantly more expensive.[30] This is the case notwithstanding that the majority of customers questioned use cheaper Royal Mail alternatives to first class stamps (such as sending mail second class or franked) if not using a document exchange. Some customers also stated that Royal Mail is not substitutable due to non-price factors, such as the fact that it does not provide guaranteed overnight delivery before opening of business, the security of a closed network system nor a simplified mail addressing system.

52. As set out in paragraph 26, no customer responses cited Royal Mail's Relay service as an alternative supplier for document exchange services and those customers that the CMA specifically questioned about this service had not heard of it. Further, [✂].

53. With respect to other point-to-point operators, none of the public sector respondents cited in-house networks as an alternative for the mail that is currently sent via DX or Legal Post. One public sector respondent stated that a courier company had participated alongside DX and Legal Post in a tender for its inter-office mailing requirements and had been a distant third choice due to price. One private sector respondent stated that it has considered an in-house courier option when faced by rising document exchange costs, but has found it to be uneconomical.

*Conclusion on competitive constraints from outside the frame of reference*

54. In light of its investigation, the CMA believes that, while the pricing practices of DX and Legal Post indicate some constraint from Royal Mail's standard

[28] Equivalent Royal Mail stamp prices for each of Legal Post's mail formats are listed explicitly on Legal Post's pay-as-you-go pricing sheets.
[29] See footnote 10.
[30] Only one customer considered Royal Mail's standard services to be price competitive against document exchanges services. This customer compared document exchange prices to Royal Mail's second class franked mail pricing.

services, that constraint is unlikely to prevent price rises for at least some customers. Further, the CMA believes that DX and Legal Post will not face any significant constraint following the Merger from Royal Mail's Relay service or other point-to-point operators, such as couriers or in-house mail networks.

*Conclusion on horizontal unilateral effects*

55. As set out above, the CMA believes that pre-Merger:

*(a)* DX and Legal Post competed closely for some customers and mail volumes, and that this competition may have exerted some downward pressure on DX's pricing;

*(b)* as a result of the closed nature of document exchange networks and the limited overlap between their members, DX and Legal Post were only competing for a small volume of document exchange mail and so the degree of competition between the two providers was less than would usually be expected in a market where only two providers are present;

*(c)* actual switching between DX and Legal Post was limited, although the threat of switching could be expected to drive prices down for some customers; and

*(d)* while the pricing practices of DX and Legal Post indicated some constraint from Royal Mail's standard services, that constraint is unlikely to prevent price rises for at least some customers.

56. Accordingly, the CMA believes that the Merger raises competition concerns as a result of horizontal unilateral effects in relation to the supply of document exchange services for mail sent and received within Scotland.

***Barriers to entry and expansion***

57. Entry, or expansion of existing firms, can mitigate the initial effect of a merger on competition, and in some cases may mean that there is no substantial lessening of competition. In assessing whether entry or expansion might prevent a substantial lessening of competition, the CMA considers whether such entry or expansion would be timely, likely and sufficient.[31]

58. DX submitted that document exchange services form part of the priority mail sector and that, in principle, entry into the priority mail sector is simple in so

[31] *Merger Assessment Guidelines*, from paragraph 5.8.1.

far as regulatory hurdles to entry are low. It stated that many entrepreneurial businesses have entered the market and established local delivery networks.

59. However, no firms other than Legal Post have replicated a document exchange model in the UK and [✂]. Further, document exchange services are in decline (see further paragraphs 81 to 83), which the CMA believes would make the sector unattractive for new entrants.

60. For the reasons set out above, the CMA believes that entry or expansion would not be timely, likely or sufficient so as to prevent a realistic prospect of a substantial lessening of competition as a result of the Merger.

## Third party views

61. The CMA contacted customers of DX and Legal Post, as well as Royal Mail. The CMA also sought input from Ofcom. Some customers raised concerns regarding the Merger, primarily that prices would rise as a result of loss of competition (notwithstanding that four of these customers did not consider DX and Legal Post to be substitutable). No other third parties raised concerns about the Merger.

62. Third party comments have been taken into account where appropriate in the competitive assessment above.

## Conclusion on substantial lessening of competition

63. Based on the evidence set out above, the CMA believes that the Merger has resulted, or may be expected to result, in a substantial lessening of competition as a result of horizontal unilateral effects in the supply of document exchange services for mail sent and received within Scotland.

## Exceptions to the duty to refer

64. Where the CMA's duty to refer is engaged, the CMA may, pursuant to section 22(2)(a) of the Act, decide not to refer the merger under investigation for a Phase 2 investigation on the basis that the market(s) concerned is/are not of sufficient importance to justify the making of a reference (the **de minimis exception**). The CMA has considered below whether it is appropriate to apply the de minimis exception to the present case.

### *Markets of insufficient importance*

65. In considering whether to apply the de minimis exception, the CMA is required to weigh up, in broad terms, whether the costs involved in a reference would

be disproportionate to the size of the market(s) concerned, also taking into account the likelihood that harm will arise, the magnitude of competition potentially lost and the duration of such effects.[32]

66. For the purposes of applying the de minimis exception, the market concerned is the affected market. In the analysis below the CMA has taken the frame of reference, namely the supply of document exchange services for mail sent and received within Scotland to be the affected market.

*'In principle' availability of undertakings in lieu*

67. The CMA's general policy, regardless of the size of the affected market, is not to apply the de minimis exception where clear-cut undertakings in lieu of a reference could, in principle, be offered by the parties to resolve the concerns identified.[33]

68. Clear-cut undertakings in lieu will not in principle be available if the competition concerns arising from the merger relate to such an integral part of the transaction that to remedy them via structural divestment would be tantamount to prohibition of the merger.[34]

69. The CMA's competition concerns relate to the supply of document exchange services for mail sent and received within Scotland. These concerns could be addressed by the divestment of Legal Post.

70. However, DX's internal documents indicate that the purchase of Legal Post was of fundamental importance to DX's decision to enter into the Merger. In particular, one DX management presentation[35] listed under 'rationale' the benefits arising from the acquisition of Legal Post but did not address any benefits arising from the acquisition of First Post. Discussion of the benefits of the transaction in contemporaneous emails between DX and First Scottish Group (the parent of Legal Post and First Post) also focus principally on the combination of their document exchange businesses and significantly less on their DSA businesses.

71. Accordingly, the CMA believes that the acquisition of Legal Post relates to such an integral part of the Merger that to require its divestment would be

[32] *Mergers: Exceptions to the duty to refer and undertakings in lieu of reference guidance* (OFT1122), December 2010, chapter 2. The *Mergers: Exceptions to the duty to refer and undertakings in lieu of reference guidance* were adopted by the CMA (see *Mergers: Guidance on the CMA's jurisdiction and procedure*, Annex D).
[33] *Mergers: Exceptions to the duty to refer and undertakings in lieu of reference guidance*, paragraphs 2.2 and 2.18 to 27.
[34] *Mergers: Exceptions to the duty to refer and undertakings in lieu of reference guidance*, paragraph 2.25.
[35] Presentation *'Project Laurel: Proposed acquisition of Legal Post and First Post from First Scottish Group'*.

tantamount to prohibition. The CMA therefore does not believe that an 'in principle' clear-cut undertaking in lieu is available in this case.

*Relevant factors*

72. The CMA will assess the likely level of consumer harm by reference to a number of factors when deciding whether or not to apply the de minimis exception: the size of the market, the strength of the CMA's concerns that harm will occur as a result of the merger, the magnitude of competition that would be lost by the merger, and the likely durability of the merger's impact.[36] The CMA will also assess the wider implications of a de minimis decision, such as the replicability of the merger.[37] Each is explained in turn below.

*Market size*

73. The combined revenue of DX and Legal Post in the supply of document exchange services for mail sent and received within Scotland in the 2016 financial year was approximately £[1-5] million (comprised of Legal Post revenues of approximately £[1-5] million and DX revenues of approximately £[1-5] million).[38] This is at the lower end of the £3 million to £10 million range within which the CMA typically undertakes a broad cost/benefit analysis in considering whether to exercise its discretion to apply the de minimis exception.[39]

*Strength of the CMA's concerns*

74. The CMA may attach weight to the strength of its belief that the merger will have an anti-competitive effect (ie whether its level of belief is on the 'is the case' (more likely than not) standard rather than the 'may be the case' standard).[40]

75. As set out in paragraph 63, the CMA believes that it is the case that the Merger has resulted, or may be expected to result, in a substantial lessening of competition. The CMA's level of belief is therefore higher than the minimum required to make a reference.

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[36] *Mergers: Exceptions to the duty to refer and undertakings in lieu of reference guidance*, paragraph 2.28.
[37] *Mergers: Exceptions to the duty to refer and undertakings in lieu of reference guidance*, paragraph 2.40 to 43.
[38] See paragraph 34.
[39] *Mergers: Exceptions to the duty to refer and undertakings in lieu of reference guidance*, paragraph 2.16. Below this range the CMA would generally not consider a reference justified, provided that there is in principle not a clear-cut undertaking in lieu of reference available: paragraph 2.2.
[40] *Mergers: Exceptions to the duty to refer and undertakings in lieu of reference guidance*, paragraph 2.33.

*Magnitude of competition lost*

76. As set out in the competitive assessment, the Merger will reduce the number of competitors in the affected market from 2 to 1. This would usually suggest that a substantial amount of competition will be lost as a result of the Merger.

77. However, as discussed in paragraphs 41 and 48, the CMA believes that, as a result of the closed nature of the document exchange network, DX and Legal Post only competed prior to the Merger for a minority of document exchange mail volumes. This is on the basis that only mail volumes sent and received between customers that are common to both parties (approximately half of DX customers and less than one third of Legal Post customers) could immediately be switched between the two. The customer responses discussed in paragraph 41 demonstrate that some customers perceive that as little as 5 to 10% of their mail volumes could immediately be switched for this reason.

78. Further, as set out in paragraph 38, the degree of actual customer switching between DX and Legal Post was limited and DX and Legal Post infrequently tendered against one another for customer business pre-merger. The CMA has also taken into account that, of those customers that considered Legal Post and DX to compete (just over half of customers that responded to the CMA's merger investigation), only a small number had concerns regarding the Merger.

79. As a result of these factors, the CMA believes that the magnitude of competition lost as a result of the Merger is significantly lower than would usually be expected in a 2 to 1 merger.

*Durability*

80. The CMA may consider whether the merger's impact will be limited because technological or market transformation will render the merger effect relatively short-lived.[41]

81. DX submitted that demand for document exchange services is in severe decline. DX estimated that, [✄]. Data submitted by DX demonstrated that, [✄]. Further data submitted by DX demonstrated that, [✄]. While the CMA has taken into account that the above data sets present certain limitations which may affect the accuracy of the trends shown, the CMA believes that the data supports an overall picture of decline.

[41] *Mergers: Exceptions to the duty to refer and undertakings in lieu of reference guidance*, paragraph 2.39.

82. DX submitted that a key cause of this decline is the rise of e-substitution, with customers increasingly using electronic methods of document transfer. This view was shared by Ofcom, as well as a number of customers that responded to the CMA's merger investigation (two of which stated that they would look to move away from physical mailing entirely if faced with a price rise from their document exchange provider).

83. DX submitted further that both the Land Registry and the criminal justice sector have announced initiatives to launch digital platforms for filing of documents, which could materially reduce document exchange volumes further. Public sources confirm that the Land Registry is undergoing a digital transformation, with 73% of registration applications now being received electronically, and has recently consulted on rules relating to the creation of a single, digital local land charges register.[42] The Scottish Courts and Tribunal Service (SCTS) separately confirmed to the CMA that an electronic case management system is due to roll out gradually across Scottish courts from 31 October 2016,[43] which is likely to reduce reliance by the Courts and court-users on document exchange services over time.

84. Based on the evidence above, the CMA believes that there are strong indications that demand for document exchange services is in decline and that, as a result, any adverse effect of the Merger may be relatively short-lived.

*Replicability*

85. The CMA will be less likely to apply this discretion where it believes that the merger in question is one of a potentially large number of similar mergers that could be replicated across the sector in question.[44] Given that there are no other suppliers in the sector in a comparable position to DX and Legal Post, the CMA believes that the likelihood of issues of replicability arising in this case is remote.

*Conclusion on the application of the de minimis exception*

86. Taking all the above factors into consideration, the CMA believes that the market concerned in this case is not of sufficient importance to justify the making of a reference. As such, the CMA believes that it is appropriate for it to exercise its discretion to apply the de minimis exception.

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[42] Land Registry Consultation on Draft Local Land Charges Rules 2017: Summary of Responses, October 2016 (Land Registry Summary of Consultation responses).
[43] As further shown in an announcement on the SCTS website: The journey to online processing.
[44] *Mergers: Exceptions to the duty to refer and undertakings in lieu of reference guidance*, paragraphs 2.40.

## Decision

87. Consequently, the CMA believes that the Merger has resulted, or may be expected to result, in a substantial lessening of competition within a market or markets in the United Kingdom. However, pursuant to section 22(2)(a) of the Act, the CMA believes that the market concerned is not of sufficient importance to justify the making of a reference.

88. The Merger will therefore **not be referred** under section 22 of the Act.

**Stephanie Canet**
**Director, Mergers**
**Competition and Markets Authority**
**21 October 2016**

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[i] With respect to footnote 24, DX clarified that Legal Post was formed in January 2001.