

# 9 Views of other parties

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## Introduction

9.1. We invited views on the bid from Government and regulatory bodies, consumer bodies, local government authorities, major users of services provided by both Northumbrian and NEW, trade associations, WoCs, WaSCs and other interested parties. This chapter summarizes the evidence we received.

## **Government departments**

### ***Department of the Environment***

9.2. The DoE explained that on the general question of mergers between water companies, the Government's policy was that these should be treated in the same manner as for any other industry and, subject to any MMC inquiry, allowed to take their course. For this reason, the Secretary of State had relinquished his 'golden share' in the water and sewerage companies on 1 January 1995. The DoE therefore had no further comments to make.

## **Regulatory bodies**

### ***National Rivers Authority***

9.3. The NRA said that it had recently agreed a five-year investment programme with Northumbrian for sewerage and sewage works improvements. Although the majority of the programme was driven by EC Directives, and these statutory responsibilities would continue to apply to the merged company, Northumbrian had nevertheless made a voluntary public commitment to spend some of the money gained from efficiency savings on additional schemes, which would lead to improved river and marine water quality. The NRA emphasized that it would wish to see this commitment honoured by Lyonnaise should it acquire Northumbrian.

9.4. In addition, the NRA explained that the operating agreement for Kielder reservoir was currently under review. The co-operation of Northumbrian and NEW, or any future owner of either, was essential in ensuring that consumers were served and the environment protected.

9.5. The NRA added that as it understood the merger would result in significant cost savings, it hoped that some of these would be returned to the customer, or reinvested in schemes to benefit the environment.

## **Consumer bodies**

### ***Northumbria Customer Service Committee***

9.6. NCSC explained that the ten regional CSCs were established by the DGWS in April 1990 under section 6 of the Water Act 1989 (now section 28 of the 1991 Act). The CSCs were independent of the water companies and had statutory duties to represent the interests of and to investigate complaints from domestic, business and other customers and potential customers. NCSC pointed out that at the time it was established it had four companies allocated to it-Northumbrian, Newcastle and Gateshead Water Company, Sunderland and South Shields Water Company and Hartlepool Water Company. Newcastle and Gateshead and Sunderland and South Shields were in the common ownership of Lyonnaise, and subsequently came together to form NEW.

9.7. NCSC said that since its inception it had regularly used comparative information both from the regional companies and from companies operating outside its area. In some instances this information had been used to inform internal debate and assist in the preparation of position papers. In other cases it had published the information to draw attention to the relative performance of the water companies, with the aim of committing those companies to improve their customer service.

9.8. NCSC pointed out that, unlike other CSC regions where there was only one water company, or where there were two companies of disparate size, it was originally allocated four companies of varying size from which to undertake comparative analysis. It added that when the two Lyonnaise companies merged, in some respects the scope for comparative work was reduced, but in other respects it was strengthened as Northumbrian and the merged NEW companies demonstrated a range of similarities, in terms of size, topography, demography and the economic and political issues facing them.

9.9. NCSC emphasized that, of the companies in the region, Hartlepool had invariably been at the forefront of customer service, often adopting and implementing OFWAT's initiatives before the other companies had set up working groups to look at the issues. It had led so often that both Northumbrian and NEW had come to

treat comparative competition more in terms of competition with each other than with their much smaller neighbour. Nevertheless, NCSC was keen to ensure that Hartlepool maintained its position as an independent comparator. It considered that the rivalry between the two large companies had led to improvements in customer service. NCSC cited a number of specific cases where comparative information had been used to obtain positive improvements in customer services.

9.10. NCSC complained that the proposed merger would lead to an immediate loss of comparators and would effectively place it in the same position as a number of other regional CSCs, where the dynamics of regional comparative competition was non-existent or virtually non-existent. It thought a newly-merged company was unlikely to regard Hartlepool as a relevant comparator; it would look further afield and compare itself against companies of a similar size outside the region. NCSC argued that without access to the base data of companies outside the region, it would have limited opportunity to make meaningful comparisons to persuade the merged company to make further improvements to its customer service.

9.11. NCSC accepted that some benefits might result from the merger. Rationalization would provide cost savings which could be passed on to the consumer by lower prices. Also, some customers presently served by both Northumbrian and NEW might find it easier to have only one contact point and this would end confusion in the public's mind about which company provided each service.

9.12. NCSC concluded by saying that it accepted the DGWS's argument that the merger would be against the public interest because of its detriment to the regulatory arrangements set up by the Government. The loss of a regional comparator would be keenly felt. NCSC argued that unless enforceable remedies could be devised to compensate the region's customers, the merger should not proceed. It suggested that remedies should include large price reductions over the next five years, and corresponding improvements in customer service. Improvements should include a flexible approach to methods of payment, including the option of paying fortnightly, and recognition that a contract existed between the company and the customer to provide a reasonable level of service, with automatic compensation if the company failed to provide an adequate service.

9.13. NCSC added that remedies would also have to ensure that any time-scales could be met. Experience of the merging of Sunderland and South Shields and Newcastle and Gateshead had indicated that it took time to rationalize services to obtain increased efficiency and deliver a better deal for customers.

### ***Northumbrian Water Customer Liaison Panel***

9.14. Northumbrian Water Customer Liaison Panel (CLP) explained that it was established in September 1992 to provide a forum for Northumbrian and its customers to meet and exchange views. Northumbrian wanted to be accountable to the community it served and, for the first time, its customers were able to directly influence its policy decisions. The CLP met at least every two months and was free to discuss with Northumbrian anything that was of interest or was causing concern to customers. In particular, it emphasized that since the CLP was established, Northumbrian had made considerable progress in water quality, environmental issues (including the disposal of sewage), standards of customer service, and customer awareness. It had also responded to customers' concerns about water metering and fully recognized the importance of consumer choice in this matter.

9.15. The CLP saw Northumbrian as an integral part of the north-east region and had encouraged the company's commitment to the region through its sponsorship of both regional and local events. CLP explained that when it was first established some of its members perceived Northumbrian as a remote, 'money grabbing monopoly', 'unanswerable to the general consumer'. Now, nearly three years later, the company was actively listening and responding to its customers, who (through the CLP) had direct access to Northumbrian's Board of Directors. CLP now believed the company's approach was fairly summed up in its slogan 'Northumbrian Water-serving the North East'.

9.16. In conclusion, the CLP said that it was extremely concerned that some or all of the benefits referred to above might be lost if the merger went ahead. The open accountability and forum for discussion might be lost if there was a change in Northumbrian's management or ownership. Discussions with NEW in the past about establishing a similar forum had clearly indicated that they could not or did not consider consultation and dialogue with their customers a priority. The CLP also thought, as Northumbrian had demonstrated, that it was better to have decision-making at the point of delivery rather than from a Head Office outside the region.

9.17. It added that another concern was the effect of the proposed merger on the north-east region. Inevitable job losses resulting from the merger would not only have a detrimental effect on the quality and standards of service delivered to customers but would also adversely affect the economic climate of the region.

### **Local government authorities**

9.18. We wrote to 22 local government authorities representing areas which received their water supplies from either NEW or Northumbrian. Four replied with comments.

#### ***Berwick-upon-Tweed Borough Council***

9.19. Berwick-upon-Tweed Borough Council (Berwick) stressed that it was essential that a merged company, in whatever shape or form, had the ability to maintain and wherever possible enhance standards of water quality.

9.20. It pointed out that it was responsible for the enforcement of standards of water in respect of many private water supplies throughout the district. The current source of private water supply chemical analysis would, in the event of the merger, appear to be directly linked with the supplier of water distribution and sewerage services. Private water supply consumers might perceive that the analysis arrangements which they paid for would become less independent, particularly where the outcome of an investigation might be a recommendation to connect properties to the public mains water supply.

9.21. Berwick added that any enforcement action taken against the water/sewerage supplier might require independent analysis of water or other samples. If a degree of independence was to be maintained, such work would need to be carried out at laboratories outside the area.

#### ***Castle Morpeth Borough Council***

9.22. Castle Morpeth Borough Council said that the monopoly of water supply resulting from the proposed acquisition of Northumbrian Water Group by Lyonnaise would not be in the best interests of the residents of the borough.

#### ***Teesdale District Council***

9.23. Teesdale District Council said that, if the merger went ahead, it would want to see safeguards introduced, including indemnities, against the costs or consequences of failure in the quantity or quality of the water supply for all categories of users. Undertakings should also be given concerning the maintenance, repair, improvement and eventual replacement of the infrastructure of water supply delivery and disposal, including any future improvements in water quality.

9.24. The council was also concerned about the lack of information on future plans and proposals for the combined company and added that, in principle, it opposed the acquisition of British natural resources by non-British companies.

#### ***Wear Valley District Council***

9.25. Wear Valley District Council said that it strongly opposed the proposed merger, which it considered was against the public interest. The council was concerned about the level of future water charges and was particularly anxious that a water company needed to be locally-based to meet local needs.

## **Major customers**

9.26. We wrote to 44 major users of water supplied by either NEW and Northumbrian. Ten replied with comments.

### ***Cleveland Potash Ltd***

9.27. Cleveland Potash Ltd said that it had no objections to the proposed merger provided the merged company was subject to the same price controls as applied at present to Northumbrian. Furthermore, it expected that the merged company would offer a more commercial and customer-orientated approach.

### ***Formica Limited***

9.28. Formica Limited said that its main concerns regarding the merger were its possible impact on prices and costs, together with its effect on existing quality contracts. In addition, it wanted to ensure that existing controls over environmental areas of the business would continue to be met and monitored and that existing checks were maintained.

### ***ICI C&P Ltd***

9.29. ICI C&P Ltd (ICI) said that it had become increasingly concerned about the increase in charges for potable water after the privatization of the water industry. It pointed out that it was the first company to challenge the unified tariff system universally employed by water companies and, after two years of debate, a cost-reflective tariff was introduced by North West Water, which reduced charges by 25 per cent. Other companies, including Northumbrian, had followed suit and currently all but one of the ten water and sewerage operators had introduced a large users' tariff. However, it added that further progress still needed to be made in this area.

9.30. ICI stressed that it was essential that the water industry provided what the customer wanted, ie security of supply, at the specified quality and at the lowest possible price. It argued that the most efficient way of providing this was through competition between water companies for contracts in other regions. It suggested that the MMC obtained policy statements from Lyonnaise on such issues before reaching their final conclusions.

9.31. ICI emphasized that the availability of comparative information was crucial for the effective regulation of local monopolies and was concerned that the regulator's ability to apply effective price control to a monopoly water services business might be impaired, particularly in respect of cross-subsidization between businesses and the costs of corporate overheads. It trusted that the DGWS was satisfied with the effectiveness of his guidelines and would ensure that any efficiency gains were passed on to the customer; on balance, it thought a reduction by one in the number of independent water companies used by the regulator as comparators would not be detrimental to customers' interests.

9.32. ICI concluded by saying that its general view was that a properly regulated and controlled merger of the kind proposed could have advantages. The superimposition of a new management structure could bring a diversity of view, with accepted practices being challenged and cost containment given a new impetus. The pace of development could be further stimulated if the company adopted a more progressive attitude. However, it was concerned that NEW, a member of the Lyonnaise group which operated within the sewerage service area of Northumbrian, had not yet introduced a large users' tariff. Nine of the 21 WoCs, it noted, already had such tariffs.

### ***KP Foods Group***

9.33. KP Foods Group said that it was concerned about the proposed merger on two counts. First, the interpretation of, and reaction to, the dictates of OFWAT by the directors of the new company might not be the same as that of the existing company. Secondly, the accounts of the UK water and sewerage operation

could easily be hidden in the new group accounts, making it difficult to see the true costs of the services supplied.

### ***Nissan Motor Manufacturing (UK) Limited***

9.34. Nissan Motor Manufacturing (UK) Limited (Nissan) said that, given that NEW was a subsidiary of Lyonnaise, it saw little benefit if the merger went ahead. It pointed out that at present there were few competitive pressures on water supply companies supplying large-scale customers. The limited success of inset agreements had clearly been recognized by the DGWS when he recently put forward proposals to encourage 'Appointees' to supply large customers in other water companies' territories. Clearly any reduction in the number of such water suppliers within the north-east region reduced the scope for such new competitive measures to take effect.

9.35. Nissan added that the DGWS had set different K factors for NEW and Northumbrian. It was concerned to ensure that safeguards were in place, in the event of the merger proceeding, to prevent unjustified cost increases to former NEW customers. It considered that this could easily come about given the inevitable differences in cost efficiency between the two independent companies and the potential within a merged business for blurring the allocation of cost and capital expenditure charges between the different regulated activities and pricing mechanisms.

### ***Northern Rock Building Society***

9.36. Northern Rock Building Society (Northern Rock) pointed out that like Northumbrian it was one of all too few large firms whose headquarters and centre of control lay in the North-East. Regional economies not only benefited directly through head office jobs created by businesses headquartered in the region but also benefited indirectly in so far as those businesses looked to purchase the goods and services they needed locally. As such Northumbrian was not just a supplier of a vital service but it also played a leading role in the wider affairs of the region.

9.37. Northern Rock explained that it was a customer of both Northumbrian and NEW. Both companies currently provided a first class service—a state of affairs which it believed arose because of the rivalry between them. If the merger went ahead there would be no competition and a worrying monopoly supply situation would be created. Guarantees about service quality and customer protection were poor substitutes for straightforward choice. Northern Rock added that it would be most concerned if the acquisition adversely affected the price it paid for water services outside the region, nor would it want to see a merger which resulted in a 'quick fix' for customers but one which was eroded in subsequent years.

9.38. In conclusion, Northern Rock said that it endorsed the view of the regulator and others that Northumbrian's service was efficient and good value for money. In its experience, Northumbrian was a high-performing company with a clearly stated strategy to improve services and rewards for its customers, staff and the wider community. Benefits of efficiency leading to lower prices and better service from the merger were doubtful in the extreme, but the real harm of loss of local control and competitiveness were certain if Lyonnaise's unsought and unnecessary bid was allowed to proceed.

### ***Phillips Petroleum Company UK Limited***

9.39. Phillips Petroleum Company UK Limited (Phillips) said that its concern was that the DGWS had no apparent powers to monitor or control raw water prices to industry from monopoly suppliers. It noted that around 30 per cent of the water supplied by Northumbrian was raw water for industry.

9.40. Phillips explained that raw water was a key resource in its oil processing operations. It had already found it difficult to negotiate on equal terms with a monopoly supplier and had been without a formal contract for raw water since April 1992. Despite requests, no detailed proposals had been submitted. It was worried that the acquisition might exacerbate its already exposed position.

### ***Scottish & Newcastle Beer Production Ltd***

9.41. Scottish & Newcastle Beer Production Ltd expressed a number of concerns regarding the proposed merger. First, it thought a merger could disadvantage customers in respect of the cost of services. It argued that the customers' right to receive a competitively-priced and quality service should be maintained. Second, the merger might strengthen the power of the merged company in dealings with the DGWS which might disadvantage customers. It said that it would seek assurances in this respect. Finally, the merger might mean that any difficulties with water supply would take longer to resolve if decision-taking was through the parent company in France. Again, it would seek assurances to ensure that regional empathy was maintained.

### ***Sterling Organics Ltd***

9.42. Sterling Organics Ltd (Sterling) said that it would be concerned about any material change in the range of services and/or prevailing operating conditions presently offered by Northumbrian which might have an adverse impact on its operations.

9.43. It explained that essentially Northumbrian was the sole provider of trade effluent and special waste disposal within the region, and, because the provision of these services was not covered by the DGWS, it could be exposed to vagaries of management policy from a new owner of the business.

9.44. Regarding water supply services, it hoped that the DGWS would remain diligent in monitoring these services. However, as it believed customers' interests were best served by competition between suppliers in the industry, any reduction in the number of suppliers would be undesirable.

9.45. Sterling added that, despite the presence of the DGWS, the cost of the services provided since privatization had risen well in excess of general cost inflation. This escalation of cost had affected the company's profitability and had not been demonstrated as being supportable by the capital investment needs of the service providers. Against this background, it was concerned about a further diminution of cost/performance comparisons, as well as the loss of the present 'notional' competitor in the local supply of water services.

### ***Vaux Group plc***

9.46. Vaux Group plc (Vaux) pointed out that Northumbrian was one of the largest independent water companies to have its headquarters situated within its region. Northumbrian was responsive to the needs of the region and the North-East had benefited from the presence of a major corporate entity based within the area. It added that, whilst it had no criticism about NEW's performance, as a subsidiary of a foreign company it inevitably had a lower profile within the local business community.

9.47. Vaux concluded by saying that it would be concerned if its water supply became monolithic, particularly if ultimate decision-making was divorced from the region. It argued that if the merger went ahead undertakings should be obtained to ensure that services would not suffer and that the needs and interests of customers were fully protected in the long term.

## **Trade associations**

### ***British Water***

9.48. British Water, representing over 200 companies in the UK involved in all aspects of the water cycle, said that it was aware of the policy imperative of promoting competition in the water utilities industry, which new participants in the market would theoretically tend to encourage. It believed the industry as a whole would endorse such trends, regardless of the nationality of new market entrants.

9.49. Nevertheless, it thought that in the present case there were important considerations which should be taken into account, namely:

- (a) French water companies enjoyed 'state patronage' on a scale wholly unfamiliar to UK companies. They had, moreover, established a formidable track record of so-called co-operation in international markets without the significantly augmented strength in the UK (and particularly waste water) business which the acquisition would produce.
- (b) The acquisition of Northumbrian Water Group by Lyonnaise would add materially to its competitive strength by providing it with access to the waste water business in the UK. Lyonnaise already had a significant presence in the UK commercial sphere through shares in several British companies.
- (c) The acquisition would tend to reduce the capacity of UK contractors to secure business in both the Northumbrian region and in international markets, because Lyonnaise would invariably strive to favour its own group of companies in all possible circumstances. Where French commercial and/or geo-political interests required it, Northumbrian could be excluded from international markets to satisfy those considerations.

### ***Society of British Water Industries***

9.50. The Society of British Water Industries (SBWI) thought a reduction in the number of water companies under independent control would prejudice the ability of the DGWS to make effective comparisons between water companies and could be considered contrary to the public interest. It felt strongly that the UK must have adequate controls to ensure that water met public health, safety and environmental requirements.

9.51. SBWI added that, as manufacturers and contractors to the UK water industry, some of its members were concerned that the merging of the water companies' core business (ie water supply and distribution and the subsequent treatment of sewage) could eventually result in a monopolistic situation in respect of the procurement of goods and services. It thought this would not be in the best interests of the UK, since it could lead to a reduction in the numbers of suppliers and hence limit innovation and development of new products and processes. This could have a detrimental effect on the UK industry and also on the export of such products and processes.

### ***Water Companies Association***

9.52. The Water Companies Association (WCA) explained that it represented all water supply companies within England and Wales, apart from Mid Kent. It pointed out that Lyonnaise's acquisition of NEW and Essex & Suffolk had not affected the participation of their senior staff in WCA's business. Lyonnaise had devolved control of its businesses to local managers who had considerable autonomy. Lyonnaise clearly attached importance to its companies retaining strong local connections and involvement, and to the maintenance of good relations with its staff.

9.53. The WCA thought it inappropriate to comment on how the balance between public interest benefits and possible detriments should be weighed up when considering the merger. However, it noted the conclusion the MMC had reached in their report on the 'Three Valleys' merger and endorsed the implication from that case that potential benefits should be shared between customers and shareholders.

9.54. The WCA indicated its support for robust comparative or yardstick competition in the water industry. However, in this case, it thought the loss of one water supply comparator would not prevent comparative competition and that, in respect of sewerage services, the proposed merger would not reduce the number of comparators available to the DGWS.

9.55. The WCA explained that inset Appointments were a further form of potential competition. It welcomed the DGWS's commitment to ensure that applications for inset Appointments reflected the true costs of supply, and attached importance to the principle that prices should reflect costs. In this connection, it had clear views on the use of the financial assistance which the Government had provided (in 1989) to the former WAs, now the WaSCs. It suggested that the best way of getting an equitable structure for tariffs would be to apply that financial assistance only to sewerage businesses. Such an allocation would enhance the fairness of comparative competition between existing WaSCs on the one hand and WCA member companies who did not

receive any financial assistance on the other. It would also enhance competition for inset Appointments and would ensure that all customers benefited equally from such assistance.

### ***Water Services Association***

9.56. The Water Services Association (WSA) explained that it was the trade association for the regulated business of the ten WaSCs in England and Wales, which included Northumbrian. Its member companies provided drinking water to 75 per cent of the population, and sewerage services to virtually all the population.

9.57. The WSA thought it would be helpful if, in the course of the inquiry, the MMC were to set out a clear framework for the examination of take-over and merger proposals in the water industry in England and Wales. Whilst recognizing that the MMC were not bound by precedent, it stressed that the framework should be designed to be effective in terms of the eventual structure of the industry if subsequent cases arose, and said that establishing a clear framework would reduce uncertainty about the principles which would apply to future take-over and merger proposals, which would benefit all parties.

9.58. The WSA noted that the first issue which the MMC had to consider was whether or not arrangements were in progress which, if carried into effect, would result in the creation of a merger of two or more water enterprises. It believed principles should be established to test the seriousness of potential bidders to ensure that companies did not unnecessarily become involved in intensive, time-consuming MMC inquiries. It also believed it was particularly important that companies which were either 'fishing' for potential take-over targets, or were bidders in contested take-overs, should not have access to data which would assist them in deciding upon and pricing a bid.

9.59. The WSA pointed out that the existence of over 20 WoCs and 10 WaSCs had provided the DGWS with the opportunity of developing a framework for comparative competition between companies, even though each company was still a monopoly supplier in its own licensed area. It thought the DGWS's ability to make comparisons between the companies had been extremely useful to him in reviewing their performance and setting new price limits. The WSA argued that it would be helpful if the MMC could set out a framework against which this and any future take-over/merger proposals could be assessed indicating, for example, how the adequacy of the number of comparators would be assessed, whether or not these needed to be separate licensed Appointments, and how the loss of a comparator would be evaluated. Also, it would be useful to have clarification of the principles applied in balancing the interests of consumers directly affected by a merger with the generality of customers in England and Wales who might be disadvantaged by the loss of a comparator.

9.60. With regard to the distribution of any benefits from a take-over/merger, the WSA believed such a distribution should be balanced between customers and shareholders. The WSA stressed that, when considering any price reductions which might be offered to customers to try to secure approval of a merger, it was vital that the MMC separated potential benefits arising from the merger from ongoing efficiencies which would be generated by the target company regardless of the merger. Any price reductions should be sustainable from the benefits arising from the merger and should not be financed through cross-subsidies, and bidders should not be led to believe that if they failed to realize expected benefits, prices would be increased at the next Periodic Review to compensate.

9.61. It argued that any promises of cross-subsidies should be disregarded since they would distort the comparative process. In this context, the MMC should focus on the potential for sustainable cost savings.

9.62. Regarding the wider international market, it said that whilst it recognized that the European competition authorities were dealing with competition aspects of the merger, it nevertheless wanted to notify the MMC of some uncertainties and concerns it had in this area.

9.63. The WSA pointed out that although EC companies were in principle meant to have equal access to all EC markets, in reality it was not clear whether this situation prevailed. It appeared that the EU Procurement Directive did not apply to some categories of concessions for the provision of services, including many water and sewerage services concessions. Companies based in England and Wales could not therefore seek redress when concession arrangements were arrived at by procedures which did not meet the

Procurement Directive's requirements on, for example, advertisement of the proposed concession, tendering procedures or bid evaluation.

9.64. The WSA added that companies based in England and Wales might also seek to become involved in the provision of water and sewerage services in other countries by buying shares in, or taking over, companies already providing those services, which had stock market listings. This route was readily available to foreign companies which wished to become involved in companies quoted on the UK Stock Exchange. However, significant barriers to entry might exist in other countries which might discourage new entrants. Also, the system of economic regulation applying to WaSCs in other countries might be relatively opaque and informal, making the decision to take part in that market a risky one for a newcomer.

## **Water-only companies**

9.65. We wrote to the 21 WoCs operating in England and Wales, but only two wished to comment.

### ***Hartlepool Water PLC***

9.66. Hartlepool explained that it supplied water to some 92,000 people, as well as to a substantial number of industrial customers, in and around Hartlepool. Sewerage services were provided in the area by Northumbrian, for whom Hartlepool acted as an agent in collecting charges. Hartlepool pointed out that it was considerably smaller in size than either Northumbrian or NEW.

9.67. Hartlepool considered it inappropriate to comment directly on the proposed merger. It stressed that it would continue to work constructively and in customers' interests with whichever company provided sewerage services in the area. Nevertheless, it drew the MMC's attention to a number of points of principle which it thought were of particular relevance to the proposed merger. In particular, it suggested that a number of safeguards should be in place if the merger was to proceed.

9.68. Hartlepool emphasized the importance the DGWS attached to comparative competition; the DGWS had reiterated this view on many occasions. It pointed out that comparisons had consistently demonstrated that it provided an excellent service and good value for money to all its customers. It was therefore a valuable comparator despite its size. It was important that its role as an independent comparator should not be compromised by the proposed merger.

9.69. Hartlepool pointed out that if the merger went ahead its customers would be the only people in the region to receive their water supply and their sewerage services from different companies. It noted the DGWS's expectation that WaSCs should achieve an equitable balance in tariffs between their services and welcomed the attention the DGWS was giving to this matter.

9.70. Hartlepool added that any determination of whether a balance had been struck should also consider the financial assistance given by the Government to WaSCs at the time of privatization, but which was denied to WoCs. Apart from the potential for unfair competition that this created, if the merger were to proceed, and the enlarged company was, as Hartlepool expected and supported, to equalize its water tariffs, then all its customers would benefit equally from the financial assistance. Hartlepool stressed that in this situation its customers would be the only ones in the region discriminated against in this way. This would be a serious concern for customers and the company alike. It argued, therefore, that if the merger were to proceed, it should be conditional on the Government's financial assistance being used to benefit all the region equally.

9.71. Hartlepool considered that two other aspects of tariff balancing were of importance. The first was that charges to measured and unmeasured customers should be in balance. The company welcomed the DGWS's intention to pursue tariff balancing. In its view, the proposed merger, if it proceeded, would offer an ideal opportunity for a balance to be achieved. (NEW's water tariff was already nearly in balance, as were Northumbrian's sewerage charges.) The second concern was that discounts to industrial customers should be appropriate. It considered that Northumbrian's discount to large-volume industrial customers had potential competition implications. Although the basic principle that discounts should be cost-reflective had been generally accepted throughout the industry, it nevertheless thought it would be helpful, and in the interest of fair competition, for more detailed guidance to be given so that a consistent approach could be followed.

## ***Mid Kent Water PLC***

9.72. Whilst declining to comment specifically on the merger, Mid Kent said that it supported OFWAT's policy of the need for company comparators. It stressed that there had to be a minimum number of separate companies as comparators to make this method of evaluating company performance of any value.

## **Water and sewerage companies**

9.73. We wrote to the other nine WaSCs operating in England and Wales, but none wished to make representations on the bid.

## **Others**

### ***Institute of Directors***

9.74. The Institute of Directors (IoD) explained that at present competition in the water industry in England and Wales was largely simulated by decisions of the DGWS, based on comparisons between independent companies. There were few other stimuli to promote competition, such as access to alternative suppliers within the various regions. IoD thought it was important that those competitive pressures which did exist were fully applied to the water companies.

9.75. IoD considered that, in the absence of consumer choice, one way in which the performance of water companies could be improved was by foreign companies acquiring English and Welsh water companies, within the rules laid down by the DGWS. In the absence of genuine competition, the threat of a merger was an important competitive discipline on the water companies. For this reason, it thought it was in the public interest for the merger to go ahead.

D G GOYDER (*Chairman*)

A G ARMSTRONG

P BRENNAN

D J JENKINS

J D MONTGOMERY

A ROBINSON

A J NIEDUSZYNSKI (*Secretary*)

4 July 1995