



Water Industry Act 1991 Section 13

Proposals by the Director General of Water Services for the Modification of the Conditions of Appointment of Southern Water Services Ltd

The process

Any representations about, or objections to, these proposals for the modification of the conditions of appointment of Southern Water Services Ltd (Southern Water) must be sent in writing to the Director General of Water Services, Centre City Tower, 7 Hill Street, Birmingham, B5 4UA (fax, 0121-625 3609 or e-mail keith.mason@ofwat.gsi.gov.uk) to be received no later than 5.00pm on 21 July 2003.

Background to the Proposed Modifications

In May 2002 Vivendi Water UK¹ (Vivendi) sought to acquire First Aqua (JVCo) Limited (First Aqua), Southern Water's holding company. Due to Vivendi's existing water interests in Three Valleys Water plc, Tendring Hundred Water Services Ltd and Folkestone and Dover Water Services Ltd, the proposed acquisition was referred to the Competition Commission (the Commission). Under the Water Industry Act 1991 all mergers between water companies above a certain size must automatically be referred to the Commission. The Commission must decide whether the proposed merger is against the public interest and in doing so must have particular regard to Ofwat's ability to make comparisons between water companies.

The Commission decided that the merger would be against the public interest and recommended it should only be able to go ahead subject to certain remedies. It recommended one such remedy. However, Ofwat and the Office of Fair Trading (OFT) were asked by the Competition Minister to further consider alternative remedies. During this period of further investigations Vivendi announced that it now intended to take only a minority stake in First Aqua, with the remaining shares being held by a third party.

Under these revised proposals Vivendi would not be able to control the policy of Southern Water, but it would be able to exercise a material degree of influence. Ofwat and the OFT therefore advised the Minister that a remedy was still required, albeit a less onerous one than under the original proposals.

The OFT and Ofwat recommended that, in addition to Vivendi divesting its stake in South Staffordshire Water, Southern Water should be required to provide an additional data set for the discrete Hampshire part (including the Isle of Wight) of its water supply area. This would require modification of Southern Water's conditions of appointment.

The Competition Minister accepted this advice and Vivendi was allowed to complete the acquisition subject to these conditions.

The Proposed Modifications and the reasons for them

The ability to make comparisons between water companies is a cornerstone of the regulatory regime for the water sector. Where companies are under common ownership or control their value as comparators is reduced. The provision of additional data from Southern Water will help offset the harm to the robustness of our comparative analysis caused by Vivendi being able to control, or influence the policy of, more than one water company.

We propose to modify Condition M of Southern Water's licence to require it to provide Ofwat with this additional data as part of its annual June data return. The modification will require Southern Water to provide the following information for the Hampshire part (including the Isle of Wight) of its water supply area.

1. Information about asset condition and serviceability in the Hampshire area.
2. Capital cost information necessary to identify cost drivers in the Hampshire area.
3. Operating cost information necessary to identify cost drivers in the Hampshire area.
4. Information on the reliability of water supplies and security of supply in the Hampshire area.

These data are in addition to the data we ordinarily collect for the whole company.

Office of Water Services
June 2003

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