

**November 2001**

**London Electricity Group plc's  
proposed acquisition of TXU Europe  
Group plc's Eastern Electricity Limited  
and its 50 per cent shareholding in  
24Seven Utility Services Limited**

**A consultation paper**

# 1. Introduction

## *Purpose of this document*

1.1 This document:

- ◆ gives details of London Electricity Group plc's proposed acquisition of TXU Europe Group plc's Eastern Electricity Limited and its 50 per cent shareholding in 24Seven Utility Services Limited;
- ◆ explains the merger control process for this transaction; and
- ◆ requests comments on the regulatory issues arising from the proposed transaction.

1.2 Ofgem<sup>1</sup> will make recommendations to the Office of Fair Trading in relation to the merger. In order to allow comments to be considered, Ofgem needs to receive these not later than 5pm on 28 November 2001.

---

<sup>1</sup> With the commencement of the relevant provisions of the Utilities Act in December 2000, the duties and functions of the Director Generals of Electricity and Gas Supply were transferred to the new Gas and Electricity Markets Authority. However, this document refers to the Office of Gas and Electricity Markets (Ofgem) throughout.

## 2. Details of the proposed acquisition

- 2.1 London Electricity Group plc (LEG) proposes to acquire TXU Europe Group plc's electricity distribution business in eastern England, Eastern Electricity Limited (Eastern), and its 50 per cent interest in the 24Seven joint venture that operates and maintains the electricity distribution networks of both parties. As LEG already has a 50 per cent stake in 24Seven, it will own 24Seven outright if the transaction is completed.
- 2.2 The acquisition of Eastern includes the acquisition of meters belonging to the Eastern distribution business, but not the acquisition of any metering or meter reading business.
- 2.3 On 19 November 2001 LEG notified the proposed transaction to the Merger Task Force at the European Commission for a decision to clear the transaction or to refer it to Phase II of the European Community Merger Regulation.
- 2.4 On 19 November 2001 LEG separately notified the Merger Task Force at the European Commission of a proposal for it to acquire West Burton power station from TXU Europe Group plc. Ofgem has published a separate consultation paper on the issues raised by that transaction.

### 3. Merger Control Process

- 3.1 Under the European Community Merger Regulation (Council Regulation 4064/89 as amended by Council Regulation 1310/97) ("the Regulation"), a merger having a Community dimension should be appraised by the Commission of the European Union ("the Commission") with a view to establishing whether or not it is compatible with the common market. Because of the parties' combined world-wide and EC turnover, the proposed acquisition appears to meet the relevant criteria for a merger having a Community dimension. The Commission has one month from the date of receipt of a complete notification to decide whether the merger raises serious doubts as to the acquisition's compatibility with the common market and whether to initiate an in-depth investigation under Phase II of the Regulation.
- 3.2 Article 9 of the Regulation provides for the Commission to refer a merger to the competent authorities of a Member State where on application of that Member State:
- ◆ a concentration threatens to create or to strengthen a dominant position as a result of which effective competition would be significantly impeded in a market within that Member State, which presents all the characteristics of a distinct market; or
  - ◆ a concentration affects competition in a market within that Member State which presents all the characteristics of a distinct market and which does not constitute a substantial part of the common market.
- 3.3 If a merger is referred back to the Member State under Article 9, the Member State may only take measures strictly necessary to safeguard or restore effective competition in the market concerned. Unless the Commission decides to refer the merger to the UK, the UK will be precluded from applying its national legislation on competition to the merger. The EU Commission then has exclusive jurisdiction to determine whether the proposed acquisition, with or without conditions, does or does not create or strengthen a dominant position as a result of which effective competition would be significantly impeded in the

common market or a substantial part of it and accordingly whether it is, or is not compatible with the common market.

- 3.4 Article 21 of the Regulation provides for a Member State to take appropriate measures to protect legitimate interests other than those taken into consideration by the Regulation.

## 4. Details of the Parties

### *LEG*

- 4.1 LEG is wholly owned by London Electricity Holding Group, a subsidiary of EdF UK Limited<sup>2</sup>. EdF UK Limited is wholly owned by EdF International, which itself is a wholly owned subsidiary of EdF. EdF is wholly owned by the French state.
- 4.2 The principal business of EdF is the generation, transmission, distribution and supply of electricity in France. In 1999, its output was 469 TWh out of a total of 500 TWh in France. It exports electricity from France to neighbouring countries, including to England and Wales through the 1988 MW France/England interconnector. EdF and National Grid Company each hold a 50 per share of the physical assets of the interconnector, and EdF carries out the auctions of 100 per cent of the capacity. EdF generates, transmits, distributes and supplies electricity elsewhere in the world. It is active in electricity trading other than in France through a joint venture with Louis Dreyfus called EdF Trading Limited, which is based in England. EdF also designs, builds and acts as a technical consultant in relation to the construction, operation and maintenance of electrical plants and power networks and, through specialised subsidiaries, provides waste recycling and street lighting services.
- 4.3 LEG's principal business interests are:
- ◆ electricity generation – through its subsidiary London Power Company plc, LEG has interests in three UK businesses involved in power generation (Sutton Bridge Power Limited, Jade Power Generation Limited and a 13.475 per cent stake in Barking Power Limited). LEG currently has a 4.4 per cent share of capacity in the England and Wales generation market<sup>3</sup>. LEG's share of output in 2000/2001 was about 4.52 per cent<sup>4</sup>.

---

<sup>2</sup> EdF acquired control of EdF UK Limited following a decision of the European Commission in 1999 to grant merger clearance.

<sup>3</sup> The market share, capacity and output figures in this document and in Ofgem's consultation document on the proposed acquisition of West Burton exclude the French interconnector. However, in assessing whether that transaction is likely to raise any competition concerns, Ofgem intends to take into account capacity that may be available to EdF through the French interconnector.

<sup>4</sup> Or approximately a 3.9 per cent share of capacity and approximately a 3.8 per cent share of output in the Great Britain market.

However, LEG has recently agreed, subject to clearance by the European Commission, to acquire from TXU Europe Group plc, the TXU subsidiary that operates West Burton power station. In the event that this acquisition is completed, LEG's share of generation in England and Wales would increase to around 7.4 per cent of capacity and around 5.9 per cent of output<sup>5</sup>.

- ◆ electricity distribution - through its subsidiary London Power Networks plc (LPN), LEG owns the principal electricity distribution network in the London metropolitan area, to which 2.3 million customers are connected. With TXU Europe Group plc, LEG has a 50:50 joint venture, 24Seven Utility Services Limited (24Seven), which provides utility network asset management services to a number of distribution network owners, including LPN and Eastern, in the UK<sup>6</sup>. LEG also operates a number of private distribution networks;
- ◆ electricity and gas supply – LEG also owns London Electricity plc (LE), which is an electricity and gas supplier operating principally in England and Wales, and which owns SWEB Limited, the electricity supply business acquired from South Western Electricity plc in September 1999, following a decision of the European Commission in July 1999 to grant merger clearance. LEG also has a 75 per cent interest in Virgin Energy Limited, the other 25 per cent of which is owned by the Virgin Group. LE supplies energy to 3.3 million customers in Great Britain. LE has 3.0 million retail electricity customers in Great Britain, giving it a 10.4 per cent share of the market, and 0.3 million retail gas customers in Great Britain, giving it a 1.6 per cent market share.

---

<sup>5</sup> This would represent approximately a 6.6 per cent share of capacity and approximately a 5.3 per cent share of output in the Great Britain market.

<sup>6</sup> 24Seven is managed by a board comprising two directors from each parent company and an independent Chairman. 24Seven controls the assets previously employed by each distribution company in maintaining, managing and operating its distribution networks, including equipment, IT systems, staff and leases of property and vehicles. 24Seven provides the security and safety of supply enquiry service and new connections for both distribution companies. There are separate, different fixed term contracts between each distribution company and 24Seven.

- 4.4 EdF Trading Limited, EdF's joint venture with Louis Dreyfus, is involved in the trading of electricity in Great Britain and is a participant in the electricity balancing mechanism.
- 4.5 LEG, through ECS Metering Services Limited, carries out the majority of metering and meter reading work in the London area. As stated above, the acquisition of Eastern includes the acquisition of meters belonging to the Eastern distribution business, but not the acquisition of any metering or meter reading business.
- 4.6 24Seven also carries out electricity connections work and has a market share of around 17 per cent in Great Britain. 24Seven carried out the vast majority of connections undertaken across the distribution areas of LPN and Eastern in 2000/2001.

***TXU Europe Group plc***

- 4.7 Eastern is wholly owned by TXU Europe Group plc (TXU Europe). Eastern owns the electricity distribution network in the eastern region of England. This network is managed and operated by 24Seven, which is at present a 50:50 joint venture between LEG and TXU Europe.
- 4.8 TXU Europe is a wholly owned subsidiary of TXU Corporation, an investor-owned holding company headquartered in Dallas, Texas. The principal activities of the TXU Corporation are the provision of services in the gas and electricity sectors, energy trading, energy marketing and telecommunications. These activities are carried by subsidiaries primarily in the United States, Europe and Australia.
- 4.9 TXU Europe, whose principal business is the generation and distribution of electricity, energy trading and gas marketing, carries out TXU Corporation's European activities. TXU Europe operates primarily in the UK, where it has interests in power stations and two electricity supply businesses, but is also active in continental Europe, where it has generation plant, holdings in energy supply and retail companies, energy trading licences and trading and retail joint ventures.
- 4.10 TXU Europe's principal businesses in Great Britain include



- ◆ electricity generation, through TXU Europe Power, which owns (either outright or in part) five<sup>7</sup> generation stations in the UK (not including Shotton, a 240MW CHP which provides power to a local paper mill, exporting any excess power onto the system). TXU Europe Power has a total capacity of 5,061 MW. Following the recent sale of King's Lynn and Peterborough power stations to Centrica, TXU Europe Power's share of the England and Wales generation market is approximately 7.5 per cent by capacity and 5.1 per cent by output for the financial year 2000/2001<sup>8</sup>. If the proposed sale of West Burton power station is completed, TXU Europe Power's market share will fall to 4.5 per cent of capacity, with an adjusted output share of 3.4 per cent for the financial year 2000/2001<sup>9</sup>;
- ◆ gas shipping, through its subsidiary TXU Europe Energy Ltd;
- ◆ electricity distribution - Eastern holds a licence to distribute electricity in Great Britain. Its distribution service area comprises Norfolk, Suffolk and Hertfordshire, most of Bedfordshire, Essex and Cambridgeshire, parts of Oxfordshire and Buckinghamshire and the northern suburbs of Greater London. 3.4 million customers are connected to this network. As stated above, TXU Europe also has a 50 per cent share in 24Seven;
- ◆ gas shipping, through its subsidiary TXU Europe Energy Ltd;
- ◆ electricity supply, through TXU UK Limited, Norweb Energi Limited and TXU Direct Sales, currently supplying about 4.4 million electricity customers in total (which represents 15.4 per cent of the market); and
- ◆ gas supply, through wholly owned subsidiaries including Norweb Gas and Eastern Natural Gas (Retail) Ltd, currently supplying 1.2 million gas customers (which represents 5.6 per cent of the market).

---

<sup>7</sup> A sixth station, the 1046 MW coal plant, Rugeley B, is currently in the final stages of divestment to International Power plc.

<sup>8</sup> Or approximately a 6.7 per cent share of capacity and approximately a 4.5 per cent share of output in the Great Britain market.

<sup>9</sup> This would represent approximately a 4.0 per cent share of capacity and approximately a 3.1 per cent share of output in the Great Britain market.

- 4.11 TXU Europe also has a subsidiary, TXU Europe Energy Trading, which is involved in the sale and purchase of electricity and gas in the wholesale and forward markets. TXU Europe Energy Trading is one of the largest energy traders in the UK. In 2000 it traded 308 TWh of electricity and 1,489 TWh of gas in the UK.

## 5. Issues arising from the proposed acquisition

5.1 Ofgem believes that this acquisition raises four issues for consideration:

- ◆ regulation of distribution businesses;
- ◆ efficiency savings
- ◆ the nature of undertakings to be requested from EdF International by Ofgem in relation to 24Seven; and
- ◆ metering competition.

The potential effect of this acquisition on each of these issues is discussed below.

### *Regulation of distribution businesses*

5.2 Ofgem has just published a consultation document seeking views on the issues raised by further consolidation among the electricity distribution companies operating within Great Britain<sup>10</sup>. In that document we noted that, since 1995, a number of corporate transactions including mergers had taken place in the electricity distribution sector which had resulted in some of the original fourteen companies being jointly owned and/or operated, and that there were now nine independent groupings of distribution companies.

5.3 Ofgem recognises that customers can benefit from mergers if the combined grouping generates efficiency savings or improvements in quality of service which are either greater than or are generated more quickly than those incurred by the separate entities. However, at the same time mergers reduce the quality and comparability of information available to the regulator. Moreover, mergers between distribution businesses reduce the comparators available for analysis when carrying out a review of the distribution price controls. This is because the number of different management approaches is reduced, the real number of observable data-points for an efficiency measure is reduced, and the scope for inappropriate cost allocation is increased.

---

<sup>10</sup> "Mergers in the electricity distribution sector – a consultation document", Ofgem, November 2001. The closing date for responses is 4 January 2002.

- 5.4 At present, LPN and Eastern, each of which is a licensed electricity distribution network operator (DNO), are respectively owned by LEG and TXU Europe but jointly operated by 24Seven under contracts entered into in 2000. Ofgem considers that these arrangements effectively brought LPN and Eastern under common management. As a result of the proposed transaction, LEG will own Eastern as well as LPN, and will acquire TXU Europe's 50 per cent share of 24 Seven. However, the transaction will not reduce the number of independent management teams operating within the electricity distribution sector. Accordingly, Ofgem considers that the transaction will not further diminish its ability effectively to set price controls and performance standards applicable to LPN and Eastern. Views are invited on this issue.

### ***Efficiency savings***

- 5.5 When 24Seven was created, Ofgem said that it regarded the joint venture to all intents and purposes as a merger. Therefore, Ofgem indicated that it expected a sustained annual saving of at least £12.5 million (reckoned to be half of the estimated fixed costs of a single distribution business) to be rebated to customers five years after the venture or merger to reflect efficiency savings. This remains our view.

### ***Undertakings to be requested from EdF International by Ofgem in relation to 24Seven***

- 5.6 In March 2000 Ofgem required that TXU Europe and EdF International each undertake, in respect of each their PES subsidiaries:
- ◆ to procure that legally enforceable agreements are entered into by both Eastern and London with the Joint Venture Company governing the provision of all services and supplies such that it is clear, both managerially and legally, where responsibility lies for the performance of each function;
  - ◆ to procure that its respective licensee subsidiary shall at all times have available to it sufficient resources to enable such licensee to:
    - a) to carry on its respective licensed activities;

- b) to secure compliance with the Agreement; and
  - c) to comply in all respects with its obligations under its licence and the Electricity Act 1989
- ◆ that it will not, and will procure that neither the Joint Venture Company nor any of its subsidiaries will, take any action if such action would then be likely to cause its respective licensee subsidiary to breach its obligations under its licence or the Act; and
  - ◆ that it will, and will procure that the Joint Venture Company and each of its subsidiaries will, provide promptly any information relating to any of them that its respective licensee subsidiary may from time to time require in order:
    - a) to comply with any requirement of Ofgem
    - b) to assess the performance and position of a service provider with respect to the provision of any service or supply, or
    - c) to monitor adherence to the terms of the Agreement; and
  - ◆ to procure that the Joint Venture Company explicitly discloses to the relevant licensee the bases of all charges for services provided and all other suppliers to that licensee, together with details of any mark-up over attributable cost included in any such charges and of the cost attribution methods utilised by such service provider in calculating such mark-up, and will not raise any objection to, nor seek to prevent the disclosure of, such information to Ofgem.

5.7 Ofgem considers that TXU Europe should, in the event that the transaction is completed, be released from the undertakings that it gave in March 2000. In the light of the separation of the former PES' distribution businesses from their supply businesses in accordance with the Utilities Act 2000, Ofgem will need to consider the extent to which these undertakings remain applicable to EdF International. In particular, Ofgem will consider what undertakings it may request EdF International to give in relation to 24Seven's contract with Eastern. We would welcome views on this issue.

- 5.8 As described in paragraph 5.6 above, the undertakings given by TXU Europe and EdF International each in respect of their PES subsidiaries (ie. Eastern in the case of TXU Europe and London Electricity plc in the case of EdF International) included provisions regarding the form of contract each had to enter into with 24Seven and performance of those contracts by 24Seven. On October 1 2001 Ofgem issued a general consent under standard condition 29 of the electricity distribution licence in relation to contracts entered into between a DNO and its affiliate(s), such as those that Eastern and London Electricity (now LPN) have with 24Seven. Subject to provisions as to notification and information requests, the general consent allows the licensee to dispose of or relinquish operational control over any relevant asset.
- 5.9 In the event that LEG completes the acquisition of Eastern and of TXU Europe Group's 50 per cent interest in 24Seven, 24Seven will be an affiliate of both LPN and Eastern, with the result that, provided the existing contracts between LPN and Eastern, respectively, and 24Seven comply with the requirements of such general consent, the present arrangements would be covered by it. In that case, LEG will be required to enter into new undertakings in favour of each of LPN and Eastern in the form stipulated by the general consent, in substitution for the existing undertakings described above, and each of LPN and Eastern must, within seven days of completion, produce to us evidence that such undertakings have been given. LEG would then need no further consent from Ofgem.

### ***Metering competition***

- 5.10 The acquisition by LEG of Eastern includes the electricity metering assets belonging to Eastern but does not include its operational metering and meter reading business. In order to avoid the possibility of action by Ofgem for failure to meet licence obligations, the distribution businesses owned by LEG will remain able to meet their licence obligations to provide electricity metering services to suppliers in the distribution services areas of LEG and Eastern.

### ***Competition in connections***

- 5.11 Ofgem is in the process of establishing an effective competitive connections market. The successful implementation of competition requires all participants to compete on equal terms. To this end, 24Seven must not unfairly benefit or be

shown undue favour by the regional distribution licence holder. It may be necessary to consider whether additional undertakings are required in respect of 24Seven and the successful introduction of connections competition.

## 6. Conclusion

- 6.1 Ofgem is seeking the views of interested parties on the acquisition by London Electricity Group plc of Eastern and TXU Europe Group plc's 50 per cent shareholding in 24Seven Utility Services Limited, so that we may make recommendations to the Office of Fair Trading.
- 6.2 Responses will normally be available in the Ofgem library unless there are good reasons why they must remain confidential. Consultees should mark the part of their response (or whole response) which is to remain confidential, if this is the case, and where possible should consign any confidential material to appendices.
- 6.3 In order to meet the timetable laid down in the Merger Regulations, Ofgem requires comments (preferably by email) from interested parties not later than 5pm on 28 November 2001. Comments should be sent to:

Andy MacFaul  
Head of Secretariat  
Ofgem  
9 Millbank  
London  
SW1P 3GE

Fax: 020 7901 7197

E-mail: [andrew.macfaul@ofgem.gov.uk](mailto:andrew.macfaul@ofgem.gov.uk)