November 2001

Mergers in the electricity distribution sector

Consultation document

Executive summary

This consultation paper sets out in general terms the issues raised by further consolidation among the regional electricity distribution companies operating within Great Britain and puts forward a possible approach for dealing with it. Since 1995, a number of corporate transactions including mergers have taken place in the electricity distribution sector which have resulted in some of the original fourteen companies being jointly owned and/or operated. At present the number of independent groupings of distribution companies is nine. Further corporate transactions including mergers are likely in the future. The aim of this consultation is to develop a clear and predictable framework for dealing with these transactions as a means of helping distribution companies plan for the future.

Ofgem's primary objective is to protect the interest of customers, where appropriate by promoting effective competition. In the case of distribution companies which are network monopolies, the promotion of effective competition means building on the rivalry which exists between them and making effective use of comparisons between these companies in setting RPI-X price controls. For example, the most recent price control review used a benchmarking process to forecast operating expenditure.

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, each merger also reduces the number of independent groups operating or owning distribution companies and hence limits the role, which comparisons between companies can play at or between price controls. The value of comparators is very difficult to quantify fully. Some attempts have been made in the water industry where the focus has been on quantifying the value attributed to using comparators in forecasting operating expenditure.

Given that competition in the distribution sector is comparative in nature, the regulatory regime is a very important mechanism for addressing concerns about further consolidation. As part of its ongoing regulation of the sector, Ofgem is seeking views on:

- whether there should be compensation for customers for the reduction in the role which comparisons can play in future at and between price controls by those companies undertaking mergers and, if so, the basis for calculating the amount; and

- the use of the price control process as a mechanism through which efficiency savings arising from the mergers are calculated and the timing of when those savings are passed back to customers.

Comments are invited by 4 January 2002.

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1. Introduction

Purpose of this document

1.1 There are fourteen regional electricity distribution companies operating within Great Britain. Since 1995, a number of corporate transactions including mergers have taken place in the electricity distribution sector which have resulted in some of these companies being jointly owned and/or operated. At present the number of independent groupings of distribution companies is nine. Further corporate transactions including mergers are likely in the future.

1.2 The electricity distribution companies are regional monopolies. The prices, which they charge customers, are determined by a price control review carried out periodically by Ofgem - at present once every five years. Customers can benefit from mergers in the sector if the combined grouping which results generates efficiency savings which are either greater than or are generated more quickly than those incurred by the separate entities. These benefits can be passed back to customers either at the time a merger takes place or at the time of the next price control review. Ofgem does not generally seek to prescribe the method through which these efficiency savings can be achieved unless the method adopted creates a detriment for customers in the future. This may be the case for mergers within the distribution sector, which reduce the number of independent groups, and hence limits the role, which comparisons between companies can play at or between price controls.

1.3 Ofgem supports the statutory functions of the Gas and Electricity Markets Authority ("the Authority"). The Authority's principal objective, set out in section 3A of the Electricity Act 1989, introduced by the Utilities Act 2000, is to protect the interests consumers in relation to electricity conveyed by distribution systems, wherever appropriate by promoting effective competition between persons engaged in, or in commercial activities connected with the generation, transmission, distribution or supply of electricity. Ofgem provides advice to the UK merger authorities on the impact of mergers in the electricity sector, although it has no formal merger control powers. The purpose of this document is to identify as part of the ongoing regulation of the sector:

- the issues raised by further consolidation in terms of its potential impact on customers (Chapter 2); and

- a possible approach to adopt for addressing those issues(Chapter 3).

Responding to this consultation

1.4 Ofgem would like to receive responses to the issues raised by this consultation paper and in particular to the proposed policy to be applied in considering future mergers as set out in Chapter 3. Any comments should be received by 4 January 2002. They should be sent to:

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1.5 Where paper copies of a consultation response have been sent, it would be helpful if responses could also be sent electronically. Unless marked clearly as confidential, all responses will be published, for example, by placing them in Ofgem's library or on Ofgem's website.

Next steps

1.6 Ofgem will use the consultation responses which it receives as an input to developing its policy to future mergers which take place within the sector. A further paper setting out Ofgem's policy towards distribution mergers is presently planned for the fourth quarter of 2001/02.

2. Issues raised by mergers in electricity distribution

Transactions in electricity distribution to date

2.1 Since privatisation in 1990 and 1991 a number of mergers and take-overs have taken place that have involved electricity distribution companies. More recently a transaction has taken place which resulted in the joint operation of two distribution companies but where the assets of each continue to be owned by separate companies. The table below summarises the present ownership of the distribution companies.

Table 1: The present ownership of electricity distribution companies

Distribution company	Owner(s)
Eastern Electricity Ltd*	Texas Utilities
East Midlands Distribution plc	Powergen
London Power Networks plc*	Electricité de France
Manweb plc	ScottishPower
GPU Power Networks (UK) plc	FirstEnergy
Northern Electric Distribution Ltd	Mid American Energy Holdings
NORWEB plc	United Utilities
SP Distribution Ltd	ScottishPower
Scottish Hydro-Electric Power Distribution Ltd	Scottish & Southern
SEEBOARD Power Networks plc	American Electric Power
Southern Electric Power Distribution plc	Scottish & Southern
Western Power Distribution (South Wales) plc	PP&L Resources and Mirant Corporation
Western Power Distribution (South West) plc	PP&L Resources and Mirant Corporation
Yorkshire Electricty Distribution plc	Mid American Energy Holdings

* Eastern and London have both contracted the management and operation of their distribution companies to 24Seven.

2.2 There are now four groups that each own and operate two distribution companies, two companies under separate ownership that are operated jointly and four remaining independent distribution companies. As companies seek to identify new ways of achieving efficiency savings, Ofgem expects to have to consider further transactions. To date all transactions have resulted in two distribution companies being operated jointly. In future transactions might result in groupings of three or more distribution companies.

2.3 While the nature of transactions may vary, they tend to have one factor in common - they will reduce the number of independent management teams operating within the electricity distribution sector. In terms of general competition policy, further concentration of ownership within the electricity distribution sector may not be a problem as these companies are themselves regional monopolies with no overlap between their activities. Further, regulation should not seek to inhibit companies from adopting corporate solutions, such as mergers, that promote greater efficiency.

2.4 Nevertheless consolidation does raise significant questions for the regulation of these companies and in particular in the use which can be made of comparative analysis between electricity distribution companies at and between price control reviews. In the light of these concerns and the prospect of further consolidation within the sector, now seems an appropriate time to consider the issues relating to the regulation of these companies.

2.5 The remainder of this chapter sets out :

- the role which comparisons have and could play in setting price controls;
- the potentially advantageous effects of further consolidation through, for example, the generation of additional efficiency savings; and
- a summary of the main advantages and disadvantages of further consolidation within electricity distribution.

The role of comparisons

2.6 In setting network price controls regulators typically consider four main issues. These are:

- the overall level of capital and operating costs that are likely to be incurred by an efficient business;
- how the recovery of these costs should be financed;
- what are the appropriate quality of supply targets and associated incentives; and

- whether the overall balance of incentives created by the price control regime is appropriate.

2.7 The ability to compare distribution companies can be particularly helpful in assessing operating and capital costs and quality of supply targets and incentives.

Operating costs

2.8 In setting a network price control it is usual to make a projection of efficient operating costs. Where there are no direct comparators these estimates are usually based on assessing the cost base and reviewing the company forecasts for reasonableness. Where possible, external and market based benchmarks are used to assist with this analysis. Nevertheless, it is difficult to develop robust benchmarks and this limits the effectiveness of the analysis. A typical figure for the assessment of a stand-alone business has been controllable operating costs falling at about 3 per cent per year. This is broadly consistent with the results of the 2000 NGC price control review and the final proposals for Transco published in September 2001. Where there are direct comparators operating within the same industry the scope for benchmarking is much more extensive. The 1999 distribution price control review made very extensive use of comparative analysis and provided for comparable reductions in controllable operating costs of 4.3 per cent per year.

2.9 In comparing the 4.3 per cent with the 3 per cent referred to above, a legitimate question is whether there is anything about the particular circumstances of distribution companies, other than the scope for comparative assessment, that would facilitate projections of cost reductions above other comparable price controls. There are a number of factors that may lead to above average cost reduction in a privatised utility. These include:

- in the years immediately after privatisation there may be greater scope for efficiency savings as obvious inefficiencies are removed;

- if a company has reduced its costs relatively slowly in the immediate past there may be increased scope for introducing new techniques and practices designed to increase efficiency;

- the cost base of a company may be inflated by one-off costs, accounting charges or costs relating to other activities;

- if the level of technical progress and innovation within the industry is high then there will be scope for above average efficiency gains; and

- where demand is increasing rapidly there may be more opportunity to take advantage of economies of scale.

2.10 These factors do not appear to apply to electricity distribution companies over the period of the new price controls. Privatisation was in 1990, ten years before the present price controls were introduced. Over the period 1995/96 to 1999/00 many companies had already reduced costs very significantly. Before setting the targets for cost reduction over the new price control period very significant adjustments were made to the base data to take account of one-off costs, accounting charges and the costs relating to activities such as metering, supply and corporate costs. The rate of technical progress and demand growth in electricity distribution is broadly in line with the economy as a whole. Therefore, the evidence suggests that the dominant factor in determining the rate of projections of cost reduction underlying the 1999 distribution price control review was the scope for comparative assessment.

Capital costs

2.11 Similar considerations apply to the assessment of capital costs as to the assessment of operating costs. In theory it should be possible to apply comparative competition to capital as well as operating costs. During the last distribution price control review much of the analysis of capital costs was based on common assumptions across all companies. Nevertheless, the reductions in the companies total capital expenditure forecasts of around 15 per cent are broadly consistent with the reductions proposed in the 2000 NGC review and the 2001 Transco review.

Quality of supply targets and incentives

2.12 Increasingly regulators are starting to specify the outputs which companies are required to deliver for a given level of regulated revenue. As part of the last distribution review, quality of supply targets for the number and duration of customer interruptions were set for each of the companies. Since the last review Ofgem has - as part of the Information and Incentives Project - specified a common set of definitions, accuracy requirements and reporting and auditing arrangements. Work is also going on with the companies to develop a model to normalise the data for differences in the areas they serve so that meaningful comparisons of quality of supply and changes in quality can be made. This should enable more robust analysis to be carried out at future reviews.

2.13 Companies also need to be given incentives to meet these targets. The initial proposals arising from the Information and Incentives Project seek to address this in several ways for the period 2002/05. These approaches for incentivising quality depend on being able to compare performance between companies and involve:

- establishing an auditable set of quality of supply targets which could be reset at future price control reviews by reference to an industry quality frontier;
- introducing an incentive scheme which includes the publication of annual tables comparing companies network performance. Annual performance tables will encourage a sense of rivalry between distribution companies so that they will retain a focus on quality even when they are not directly financially incentivised to do so; and
- developing an incentive scheme on companies with respect to the quality of their telephone service in which no targets are set but companies will be incentivised on the basis of their performance relative to their peers.

The benefits of further consolidation

Efficiency savings

2.14 Consumers benefit from mergers if the efficiency savings or improvements in quality which the merged company is able to generate are greater (or achieved more quickly) than those of the unmerged companies. At the time of the last price control review of distribution companies, a broad brush adjustment was made to pass back the benefit of mergers which had already taken place to consumers. It was assumed that a sustained reduction of half the fixed costs, such as corporate costs, would arise as a result of distribution companies merging. These fixed costs were estimated at between £20 and £25 million. Companies were allowed to retain the benefit of merger savings during the five years following the merger. There was also a view that there may be additional savings and benefits from mergers which were not captured by the £12.5 million. (Ofgem's approach towards previous distribution mergers is set out in more detail in paragraphs 3.2 to 3.5 of this document.)

2.15 Analysis of costs at the last price control review was not able to demonstrate greater efficiencies being achieved by the first merger, which took place in 1995/96 between Scottish Power and Manweb. The analysis was based primarily on costs in 1997/98, although information from 1994/95 to 1996/97 and 1998/99 was also considered. The majority of the efficiency savings arising from a merger could be expected to occur in the two or three years following the take-over as the new organisation takes advantage of the synergies and other cost reducing initiatives. It may be that the timing of the analysis meant that it was not possible to identify explicitly the efficiency savings arising from the merger. The second take-over was in 1998/99 and so any effects would be outside the scope of this analysis. Cost analysis undertaken as part of the next price control review will provide an opportunity to review the benefits of mergers which have occurred in the present price control period and enable a more robust assessment to be carried out of the early mergers.

Other benefits

2.16 In addition to the efficiency savings which mergers themselves are expected to generate, the threat of take-overs can also have a positive effect on the management of the remaining distribution companies. However, it is not possible to quantify the benefit associated with the threat of take-over.

Mergers with specific characteristics

2.17 It has been suggested that certain mergers are likely to have a greater impact on the quality of comparators than others and that they should be treated differently as a result. These include transactions resulting in a single group owning or operating the assets of three or more licensed areas, where it has been argued that the relative size of the resulting companies would cover a greater range than before, reducing the robustness of comparisons. To date those transactions that have taken place have resulted in one entity covering two licensed areas. In practice all distribution companies are already part of larger groups with significantly different corporate structures. At an operational level, the companies retain separate licences for each licensed area and are required to provide the regulator with information on an area specific basis. It may be appropriate to review the individual licence conditions to ensure that this ring fence continues to be robust as further consolidation takes place within the sector, but in general mergers covering three licensed areas or more would not appear to raise any special issues.

2.18 It is sometimes said that mergers of contiguous licensed areas should be treated differently. Two transactions have already taken place covering contiguous franchises. Subject to these mergers not compromising the quality and hence comparability of information used by the regulator, contiguous franchises merging do not seem to raise any special issues.

A summary of the advantages and disadvantages of further consolidation

2.19 The use of comparators is an important tool in establishing a robust regulatory framework. This chapter has highlighted its importance with respect to setting future levels of price control revenue (where an estimate of the actual benefits of comparison can be made) and increasingly with respect to quality of supply. Although data comparisons can continue to be made following a merger, especially if licence conditions are put in place to allow effective information gathering, the scope to make comparisons between independent management teams is reduced. If further consolidation within the sector continues, this may require changes in the method used to set price controls and to incentivise improvements in quality of supply.

2.20 Mergers can deliver benefits to consumers in the form of greater efficiency savings or through the delivery of higher quality. An allowance was made at the last price control review to take account of some of those savings in companies that had been merged for more than five years. The limited analysis which has been carried out subsequently has not yet been able to demonstrate that the costs of merged companies are lower than those of other distribution companies. Companies that have undertaken mergers subsequently have indicated that these efficiency savings do exist and by their actions have demonstrated that they are in excess of £12.5 million – the amount by which their revenue was reduced as a result of the mergers taking place.

2.21 This suggests that in developing a framework for dealing with the issues raised by further consolidation, the key is to understand the nature and scale of costs associated with a diminished role for comparative competition versus the possible efficiency benefit which is likely to accrue from mergers.

Issues for consultation

2.22 Views are sought on the issues set out in this chapter and in particular on:

- how the benefit associated with being able to make comparisons between distribution companies can be quantified;
- how the efficiency savings associated with mergers in the electricity distribution sector can be quantified; and
- whether mergers with specific characteristics for example covering more than two licensed areas, warrant special consideration.

3. A framework for consideration of further mergers

3.1 The previous chapter set out in broad terms the trade-off between greater efficiency and a diminution in the role of comparators, which arises from further consolidation in the distribution sector. This chapter sets out:

- Ofgem's approach to date for the treatment of mergers within distribution;
- the approach adopted in the water industry; and
- a possible framework for the treatment of distribution mergers in the future.

Ofgem's policy to date

3.2 Ofgem has no formal powers under the merger control rules operated by either the UK merger authorities or the European Commission. So far as UK merger control is concerned the Director General of Fair Trading (DGFT) has a statutory duty to advise the Secretary of State in respect of mergers. The advice of the DGFT and the decision of the Secretary of State to refer the merger to the Competition Commission for consideration are, other than in exceptional and narrowly defined circumstances, based on competition grounds.

3.3 When a merger involves a regulated gas or electricity company, the DGFT consults Ofgem. Before providing the DGFT with advice Ofgem consults publicly on the issues which it considers the merger raises. When a merger falls within the exclusive jurisdiction of the European Commission the Commission has a duty to consult the EU Member States' competition authorities. In the UK, the Department of Trade and Industry and the Office for Fair Trading are joint Competition Authorities for this purpose. In formulating advice on a merger which is in the European Commission's jurisdiction, the DGFT consults Ofgem who publishes a consultation document before providing advice.

3.4 Ofgem does, in meeting its Electricity Act 1989 objectives and obligations, have a direct role in the ongoing regulation of the electricity distribution sector. Following previous mergers or comparable transactions, assurances have been sought by Ofgem to address regulatory issues relating to the conduct of the merged company. These assurances are distinct from formal undertakings which may be sought in the UK by the Secretary of State in lieu of a reference to the Competition Commission. In addition, Ofgem has also said that it will review the efficiency savings which have been delivered on the fifth anniversary of the venture or merger and will apply a minimum rebate from these gains to customers of £12.5 million. The clear expectation was that the actual rebate will be greater than this as the incentives to maximise efficiencies will have operated freely. At the time of the next price control review distribution companies involved in mergers will be expected to be at the frontier both in terms of costs and quality of service. Ofgem has not sought to compensate customers directly for the diminished role and value of comparison between distributions companies as a result of the mergers taking place.

3.5 In previous consultation papers, Ofgem has raised the possibility of advising referral of the next distribution merger to the Competition Commission as a way of considering in more detail the public interest issues set out in the previous chapter.

Mergers in the water industry

3.6 The concept of comparative competition is also at the heart of water regulation, although the legislative framework within which it operates is different. In that sector, mergers above a certain size between appointed undertakings are automatically referred to the Competition Commission. The Commission is required to make an explicit finding on the detriment to the public interest of the loss of a comparator. On the basis of the Commission's report, the Secretary of State then decides whether to block the proposed merger.

3.7 There are currently 24 appointed undertakings in the water sector of which 14 are water only companies. The remaining 10 undertakings are the larger water and sewerage companies. No mergers have been allowed between these water and sewerage companies. Some mergers have taken place between water only companies and water only and water and sewerage companies. In some of these cases prices to customers have been reduced at the time the merger took place to compensate customers for the detriment associated with loosing a comparator. The size of reduction was calculated by treating the merged company as if it had been a frontier company i.e. a leading comparator at the price control review.

3.8 Three mergers in the water sector have been blocked[1]. In each case the Commission found that there would be a loss of comparator for which there was no plausible off-setting consumer benefit. In spite of finding that there was an irremediable loss associated with the proposed mergers, the Commission was unable to quantify the loss represented by the removal of one water and sewerage company from the comparative process. The methods which tended to have been put forward for calculating the loss did so for one important aspect of the comparative system, that of operating costs. However, comparators are used in many dimensions and the methods used were likely to underestimate the value of comparisons. Moreover, the Commission noted that there were many different techniques for approaching this question.

Framework for consideration of future mergers

The interface of regulation and merger control

3.9 It is legitimate to ask whether the concerns set out in the preceding chapter about further consolidation in the distribution sector can only be dealt with through the merger control rules operated by the European Commission and the OFT or whether they could be adequately dealt with through the regulatory process. Questions of market structure arising from a proposed merger can only be dealt with through merger control. As each distribution company already operates as a monopoly, concentration of ownership in distribution does not raise market structure issues. Even if consolidation resulted in a single distribution company being formed, the regulatory framework means that Ofgem would continue to be able to protect customer interests by setting prices, specifying quality of supply and so on. However further consolidation could potentially make this task more difficult, making it appropriate for Ofgem to seek remedies in the form of licence modifications. Ofgem has adopted this approach in the past to a limited extent, to put in place for example, licence conditions on

[1] They were two bids for South West Water by Wessex and Severn Trent respectively and a joint bid by Saur and Vivendi for Mid-Kent.

financial ringfencing between the licensed activity and the rest of the group. Were a licensee to refuse to agree to licence modifications, a reference under the Electricity Act 1989, could then be made to the Competition Commission to consider the proposed modification.

3.10 Even if for the purposes of UK or European merger control transactions are not considered to be mergers, the regulatory regime, as set out in the Electricity Act 1989, can allow those transactions, which result in companies being jointly operated but where assets remain separately owned, to be treated in the same way as a merged company.

Compensating for a reduction in the number of comparators

3.11 The analysis in Chapter 2 demonstrated the potential detriment to consumers if it was not possible to carry out any comparative analysis between distribution companies at future price control reviews. Each merger, or comparable transaction which takes place, gradually erodes the scope for this analysis. This suggests that it may be appropriate, in addition to passing back the efficiency savings which mergers will deliver, to compensate customers for the detriment which reducing the number of comparators will have on future price controls.

3.12 If such an approach is to be adopted, it raises immediately the question of how such a loss is to be valued. Chapter 2 sought views on how this type of analysis might be carried out. Experience in the water industry and consideration of this analysis by the Competition Commission suggests that there is no universally accepted method and indeed that the approaches considered to date tend to focus only on one aspect of comparison. The analysis set out in Chapter 2, identified the differences in operating cost savings between the distribution price control and those price controls where there were no industry comparators. It is possible that this could be used to estimate some of the value associated with comparison. An outline of a calculation along these lines is set out in Appendix 1.

3.13 The problems of valuing the detriment of reducing the number of comparators are well documented. However, such an approach does have the advantage of providing companies with clarity and certainty in advance about the treatment of future mergers. It is for consideration whether there are alternative approaches, not based on valuing the detriment, which could be used as a means of determining the level of compensation to be paid to customers.

3.14 The detriment, which occurs as a result of further mergers taking place, arguably applies to all customers and not just those of the merged company. In an ideal world, this would suggest that compensation should be paid from the merging companies to all customers and not just the customers of the merged companies. In practice this is likely to be difficult to achieve and compensation will only be received by the customers of the merged companies.

3.15 It is suggested that the timing of any payments should take place when the merger completes as this is when the reduction in the number of comparators takes place.

Treatment of efficiency savings

3.16 The main benefit to consumers of further mergers will be the greater efficiency savings that merged companies are likely to be able to achieve. The most appropriate mechanism for identifying these efficiency savings is as part of the price control process. Merger savings can then be passed back as part of the price control settlement. In dealing with mergers previously, Ofgem has allowed companies to keep the benefits of savings achieved through mergers for five years before passing them back to customers. By identifying a fixed period of time rather than a fixed point in time when savings will be passed back to customers, the incentive on companies to undertake corporate transactions is consistent through out the price control period.

Other issues

3.17 The value of comparing licensed areas is diminished if they are jointly owned or operated. However some use can continue to be made of data at this level in reviewing costs, quality of supply, medium terms performance of assets etc. It may be appropriate to review the licence conditions relating to information provision etc to make sure that the regulator will continue to be able to collect data on the same basis as before so that some comparisons can continue to be made.

3.18 The Utilities Act 2000 introduced a standard distribution licence. The licence is divided into three parts. Licence conditions in section C apply to distribution companies who were formerly Public Electricity Suppliers. The normal method of modification to these licence conditions for all such licences will only be possible if a proportion of distribution companies weighted according to their market share do not object. The manner in which this is to be applied has yet to be determined by the Secretary of State. Mergers within the distribution sector will have the effect of increasing the market share of the resulting groupings. It may be the case therefore that as a result of a merger a single grouping will be able to block a modification where previously that was not the case. In future consideration of mergers market share may be an important regulatory consideration.

3.19 The initial proposals being considered as part of the Information and Incentives Project envisage an incentive scheme for the quality of telephone services based on companies' relative performance. Significant consolidation in the distribution sector may require changes to the way in which the scheme operates. It may also require changes to be made to the way in which quality of supply targets are set and the role which performance tables can play.

Issues for consultation

3.20 Views of consultees are sought on the issues set out in this chapter and in particular on:

- seeking to compensate customers for the reduction in the number of comparators associated with further mergers and if so, the method for determining the compensation and the timing for making any payments;
- the treatment of efficiency savings incurred by merged companies and the timing for passing back any savings; and
- other issues which further consolidation in the distribution sector is likely to raise.

Appendix 1 Compensating for a reduction in the number of comparators

1.1 As part of the last price control review Ofgem estimated the controllable operating costs for distribution as a whole as being £1027 million in 1997/98. The price control settlement included an annual reduction of 4.3 percent. For Transco and NGC the comparable reduction was 3 per cent. For this analysis it is assumed that the difference of 1.3 per cent represents the benefit which can be derived from use comparisons in setting price controls. In net present value terms this represents a cumulative benefit of £231 million for the current price control period. Replicating this analysis for the next three price control periods results in a total benefit of approximately £350 million, which could arguably be attributed to the role of comparators in regulation.

1.2 The policy outlined in Chapter 3 suggests that for each merger which takes place customers should be compensated, so that if no comparison was possible (i.e. there was only one distribution business) all the benefit of comparisons had been passed back to customers in the form of price reductions. At the time of the last price control review, there were twelve independent groups of distribution companies. This suggests that for each future merger it may be appropriate for approximately £30 million of compensation to be passed back to customers.