

Anticipated acquisition by ESBNI Ltd of NIE plc, NIE Powerteam and PES

**ME/4628/10**

The OFT's decision on reference under section 33(1) given on 8 October 2010.  
Full text of decision published 8 November 2010

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**Please note that the square brackets indicate figures or text which have been deleted or replaced in ranges at the request of the parties or third parties for reasons of commercial confidentiality.**

## **PARTIES**

1. **ESBNI Ltd ('ESBNI')** is a wholly owned subsidiary of the Electricity Supply Board ('ESB') in the Republic of Ireland. ESB is a vertically-integrated business with operations at all levels of the electricity sector including generation, transmission, distribution, and the retail supply of electricity, mainly in the Republic of Ireland and Northern Ireland. ESB was established on 11 August 1927 as a statutory corporation in the Republic of Ireland (Ireland) under the Electricity (Supply) Act 1927 and it operates under the Electricity (Supply) Acts 1927 to 2006 of Ireland. ESB is majority owned by the Government of Ireland.
2. The ESB Group is organised into three principal operational divisions, namely ESN Networks, ESB Energy Solutions, ESB Energy International. ESBI, which is based in the ESB Energy International division, consists of a number of businesses, including the development and construction of thermal power plants and wind farms for internal clients outside the UK and Republic of Ireland. It also provides project management and engineering consultancy services related to the development and construction of such assets both to internal and external clients together with other engineering consultancy, facility management and strategic

consultancy services, both in Ireland and internationally. The UK turnover of the ESB Group amounted to approximately £[ ] million in 2009.

3. The target comprises several subsidiary businesses of Viridian Group Ltd and Viridian Capital Ltd ('Viridian'). Viridian is a privately-owned,<sup>1</sup> vertically-integrated energy group active at all levels of the energy sector in the Republic of Ireland and Northern Ireland. The Group's operating businesses and principal activities comprise:
- **Northern Ireland Electricity plc ('NIE')**, which owns the regulated electricity transmission and distribution network in Northern Ireland and is responsible for the planning, development, construction and maintenance of the entire network, as well as the operation of the distribution network.<sup>2</sup>
  - NIE Energy, which engages in regulated power procurement through the Power Procurement Business ('PPB')<sup>3</sup> and in regulated supply of electricity through NIE Energy Supply.
  - Viridian Power & Energy ('VP&E'), which is active in electricity generation and in unregulated supply of electricity and gas in both the Republic of Ireland and Northern Ireland through separate subsidiaries.
  - **NIE Powerteam Limited ('NIE Powerteam')**, which provides electrical infrastructure construction/installation and refurbishment services exclusively to Viridian's transmission and distribution network business (that is, NIE), and
  - **Powerteam Electrical Services UK Limited ('PES')**, which provides similar services to a range of third-party utility and industrial customers.<sup>4</sup>
4. NIE's turnover for the year ending 31 March 2010 was £242 million; the electrical installation business had external revenues of £[ ] million.

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<sup>1</sup> Viridian was acquired by Electric Invest Acquisitions Ltd, a company beneficially owned by the international investment bank Arcapita Bank B.S.C(c) in December 2006.

<sup>2</sup> SONI (sold by Viridian to EirGrid in March 2009) is the Transmission System Operator in Northern Ireland.

<sup>3</sup> Specifically, PPB manages a portfolio of power purchase agreements (PPAs), whereby it commits to purchase the output from specified generating units at three power stations in Northern Ireland (Ballylumford, Kilroot, and Coolkeeragh). These are legacy agreements to which NIE was a party and which were permitted to remain in force following the introduction of the Single Electricity Market (SEM) in Ireland in 2007. The output is then traded into the SEM pool by PPB. In June 2010 the Northern Ireland Authority for Utility Regulation decided to instruct the cancellation of the agreement in relation to two of the units at Kilroot station in November 2010.

<sup>4</sup> These customers include [ ] industrial customers with their own high-voltage networks and wind farm developers.

## **TRANSACTION**

5. ESB and ESBNI entered into the share purchase agreement with Viridian on 6 July 2010 and announced the proposed transaction on 7 July 2010. Under the terms of the proposed transaction, ESBNI will acquire NIE, NIE Powerteam and PES. ESBNI will also acquire Capital Pensions Management Limited<sup>5</sup> which is an internal service company which administers the group pension scheme.
6. ESB will not acquire VP&E and accordingly, this business is not considered further. ESB will also not acquire NIE Energy which includes PPB. [ ].<sup>6</sup>
7. The administrative deadline for the OFT to make a decision on this transaction is 8 October 2010.
8. The transaction was also notified to the Irish Competition Authority on 5 August 2010.

## **JURISDICTION**

9. As a result of this transaction, NIE, NIE Powerteam, PES and ESBNI will cease to be distinct. The UK turnover of NIE is £235.5 million and therefore the turnover test contained in section 23(1)(b) of the Enterprise Act 2002 (the Act) is met. The OFT therefore believes that it is or may be the case that arrangements are in progress or in contemplation which, if carried into effect, will result in the creation of a relevant merger situation.

## **RATIONALE FOR THE MERGER**

10. ESB submits that the proposed transaction will provide it with a presence outside the Republic of Ireland in a core business area (that is, electricity networks). ESB also notes that the acquisition will strengthen the ESB Group as a whole, since it is an efficient and well-run business in a mature economic and regulatory environment.

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<sup>5</sup> Given the lack of overlap in this area between the merging parties, this business is not considered further.

<sup>6</sup> [ ]

11. ESB also submits that, among other things, the proposed transaction will [ ] facilitate the delivery of sustainability targets in both jurisdictions and better value for customers in the longer term.

## **MARKET DEFINITION**

### **Background**

12. The electricity markets in Northern Ireland and the Republic of Ireland have recently undergone a process of reform. In particular, a Single Electricity Market (SEM) - operated by the SEM Operator ('SEMO'), a joint venture between EirGrid and SONI - was created in 2007. The SEM is the all-island wholesale electricity market into which all electricity generated on or imported onto the island of Ireland must be sold, and from which all wholesale electricity for consumption on or export from the island of Ireland must be purchased.
13. The retail supply of electricity to end-users (that is, domestic and industrial customers) is also in the process of liberalisation, and a large portion of the market can now directly contract with suppliers, whereas smaller customers pay a published tariff for their consumption of electricity.
14. In both Northern Ireland and the Republic of Ireland the 'network' businesses, that is, the transmission and distribution of electricity, have been ring-fenced from the competitive businesses (that is, Viridian's and ESB's units active in generation and retail supply of electricity). In particular, licence conditions prohibit cross-subsidies and restrict the use of sensitive information. Furthermore, in the case of the transmission networks (but not of the distribution networks) ownership has been separated from operation. Indeed, the transmission network is owned by NIE and ESB in Northern Ireland and the Republic of Ireland, respectively, where the respective operators are SONI Limited (owned by EirGrid since March 2009) and EirGrid.
15. The sectoral regulators are the Northern Ireland Authority for Utility Regulation ('NIAUR') and the CER (Commission for Energy Regulation) in the Republic of Ireland. Responsibility for the overall energy policy is with the Department of Enterprise, Trade and Investment ('DETI') in Northern

Ireland and the Minister for Communications, Energy and Natural Resources in the Republic of Ireland.

### **Implementation of the Third Electricity Directive**

16. It is also important to mention that both jurisdictions are consulting the industry on how to implement Directive 2009/72/EC (concerning common rules for the internal market in electricity and repealing Directive 2003/54/EC).
17. In particular, in December 2009 DETI published a consultation paper in which initial views and comments were sought on the implementation of the Directive in Northern Ireland, and in particular on unbundling of the electricity transmission networks.<sup>7</sup> DETI intends to initiate a second consultation later this year.
18. One of the main issues under consultation is the effective separation of networks from the activities of generation and supply (unbundling). The Directive states that the transmission unbundling requirements must be effective by 3 March 2012 (although an extension to 3 March 2013 can be granted in certain cases).
19. In brief, three options are available under the new Directive:
  - Ownership unbundling, where the transmission asset owner is the same entity as the Transmission System Operator (TSO) and is independent in ownership from any electricity generation and supply businesses.
  - Independent System Operator (ISO), where the transmission asset owner is part of a vertically-integrated undertaking, but the system is operated by a TSO which is independent in ownership from the vertically-integrated undertaking, and
  - Independent Transmission Operator (ITO), where the transmission asset owner is the same entity as the TSO and remains part of a vertically-integrated undertaking, but it is ring-fenced within it, to make it independent in terms of branding, decision-making and management.
20. Of these three transmission unbundling options, DETI says that the current arrangements are closest to the ISO option. DETI, however, also notes that

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<sup>7</sup> See DETI, Consultation on implementation of the unbundling provisions of the 2009 electricity directive (2009/72/EC), December 2009. It is also important to note that the Directive is transposed separately in Great Britain and Northern Ireland by DECC and DETI, respectively.

the full requirements for the ISO option are not satisfied in Northern Ireland in relation to the maintenance and development of the transmission system. This is because under the Directive the ISO has responsibility for planning, construction and commissioning of further developments of the transmission system; and that the transmission owner does not have responsibility for investment planning.

21. DETI also says that an additional option would be not to apply the Directive to Northern Ireland if the conditions of Art. 9.9 are satisfied, that is:

'Where, on 3 September 2009, the transmission system belongs to a vertically integrated undertaking and there are arrangements in place which guarantee more effective independence of the transmission system operator than the provisions of Chapter V [that is, the ITO option listed above], a Member State may decide not to apply paragraph 1 [that is, ownership unbundling].'

22. DETI told the OFT that Art. 9.9 is one of the options under review, alongside the other three, and that no formal decision has been taken at this stage. The OFT has taken the options available under the Directive into account in its competitive assessment.

## **Product scope**

### **Transmission & Distribution of Electricity**

#### Background

23. In previous decisions by the OFT and the European Commission the following four segments have been identified as constituting separate product markets within the electricity industry:

- generation and wholesale supply of electricity
- transmission of electricity
- distribution of electricity, and
- retail supply of electricity.

24. The markets which are directly affected by the proposed transaction are the transmission and distribution of electricity. These are in turn described below.
25. In respect of the transmission of electricity, the European Commission has consistently identified the operation and management of the high voltage grid (electricity transmission) as a separate product market and as a natural monopoly.<sup>8</sup> The geographic scope of the markets for electricity transmission has been defined by the European Commission as being regional within the limits of the area covered by the respective grid.<sup>9</sup>
26. In respect of the distribution of electricity, the European Commission has previously concluded that the distribution of electricity (that is, the operation and management of the lower-voltage grids) is a separate product market and a natural monopoly.<sup>10</sup> The European Commission has consistently considered the markets for distribution to constitute separate local markets.<sup>11</sup>

## Conclusion

27. The Parties note the existing precedents point to separate product markets for transmission and distribution of electricity within the electricity industry.
28. In this case the OFT has seen no evidence to suggest a departure from these precedents. Accordingly, the OFT considers that transmission of electricity in Northern Ireland and the Republic of Ireland are distinct markets. Similarly, distribution of electricity in Northern Ireland and the Republic of Ireland are also distinct markets.
29. In respect of generation and wholesale supply as well as retail supply of electricity, it is not necessary for the OFT to define the exact scope of the

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<sup>8</sup> Case COMP/M.3696 - E.ON/MOL (21/12/2005) at paragraph 212 and Case COMP/M.4922 - EMCC (22/08/2008) at paragraph 12.

<sup>9</sup> Case COMP/M.3696 - E.ON/MOL of 21 December 2005 at paragraph 253 and Case COMP/M.4922 - EMCC (22/08/2008) at paragraph 12.

<sup>10</sup> Case COMP/M.3696 - E.ON/MOL of 21 December 2005 at paragraph 215 and Case No COMP/M.5224 - EDF / British Energy of 22 December 2008 at paragraph 149.

<sup>11</sup> Case COMP/M.3696 - E.ON/MOL of 21 December 2005 at paragraph 254; Case COMP/M.5170 - E.ON / ENDESA EUROPA / VIESGO of 19 June 2008 at paragraph 11 and Case No COMP/M.5224 - EDF / British Energy of 22 December 2008 at paragraph 149.

markets because no vertical foreclosure concerns arise as a result of the proposed transaction irrespective of the market definition.

### **Electrical Installation and Engineering Consultancy**

30. The parties note that in the past the European Commission has suggested that 'electrical installation' of network infrastructure (such as electricity, data and telecommunications, water, sewage and ventilation) forms a distinct market which can possibly be further segmented into high (220kV to 380kV) and low (up to 48kV) voltage installations and possibly further subdivided by size of installation. However, the Commission did not find it necessary to conclude on the relevant product market definition.<sup>12</sup>
31. The parties also submit that in the past the Commission has distinguished a separate market for 'mechanical and electrical services' including 'the provision of both mechanical and electrical design and project management services and the provision of technical equipment for every type of industrial and commercial project'.<sup>13</sup>
32. On the other hand, the parties point out that the OFT has previously identified a fairly broad market for 'contracting services'.<sup>14</sup>
33. In this case the parties submit that two distinct markets should be identified:
  - **Electrical installation services in the electricity sector**<sup>15</sup> (as distinct from installations in other sectors, for example gas, telecommunications, etc). The parties consider that this includes the supply of labour (including project management), plant and civil engineering work with or without the supply of materials (and with the design provided by customers) in relation to the construction and refurbishment of electricity overhead lines and sub-stations, and

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<sup>12</sup> Case No COMP/M.2118 - Telenor / Procuritas / Isab / Newco of 25 September 2000.

<sup>13</sup> Case IV/M.874 - Amec / Financière Spie Batignolles / Spie Batignolles of 6 February 1997. This market definition approach was recently confirmed in Case COMP/M.5445 - Mytilineos / Motor Oil / Corinthos Power of 30 March 2009.

<sup>14</sup> Case ME/1204/03, SSE Power Distribution Ltd / Aquila Sterling Ltd of 24 July 2003.

<sup>15</sup> The Parties submit that it is not appropriate to segment further the electrical installation market based on voltage (low and high) or size of the installation (large and small).



- **Engineering consultancy services for the electricity sector.**<sup>16</sup> The parties consider that these services include at least project management, surveying, electrical, mechanical and civil design and planning.
34. The parties consider that there is a separate market for 'electrical installation' as distinct from 'engineering consultancy' services because:
- these activities require different skills, expertise, certifications and tools.<sup>17</sup>
  - these services are generally contracted/procured separately (and should thus be considered complementary), and
  - while some of the larger players may have both capabilities, most companies specialise in either electrical installation or engineering consultancy.
35. In respect of the geographic scope, the parties firstly note that in the previous cases mentioned above the European Commission did not conclude on the relevant geographic market, whereas the OFT considered Great Britain to be the relevant geographic market for these services.
36. Furthermore, the parties consider that the relevant geographic market for electrical installation services is at least as wide as the UK and the Republic of Ireland together because:
- there are no material barriers to entry, and accordingly, an Irish company is not prevented from effectively competing for contracts for electrical installations in the UK and vice versa
  - PES as well as some of its main competitors are active on both the UK and the Irish market (such as Enterprise Power Systems and Integrated Utility Services), and
  - ESB currently has over [ ] contractors that have pre-qualified for its advertised electrical installation contracts, of which [ ] are based in Ireland, [ ] are based in the UK and [ ] are located outside the UK and Ireland.

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<sup>16</sup> The parties consider that the market is much wider and consists of infrastructure engineering consultancy because many of the skills are transferable and a number of ESBI's competitors are active across sectors.

<sup>17</sup> For example, installation involves manual labour and requires construction and other specialist equipment whereas consultancy work is confined to computational analysis, engineering design and on-site supervision.

37. Similarly, in respect of the geographic scope of the relevant market for engineering consultancy services, the parties consider that the relevant market is at least as wide as the UK and the Republic of Ireland together because there are no material barriers to entry and almost all the of the parties' competitors operate on an international basis.
38. The majority of respondents indicated that the proposed frame of reference put forward by the parties was appropriate in this case and no further segmentation (for example by voltage or size) is necessary.

#### Conclusion

39. While the frame of reference put forward by the parties appears to be appropriate in this case and account has been taken also of responses from third parties, the OFT does not find it necessary to conclude on the relevant market for electrical installation and engineering consultancy services, given the absence of competition concerns.

## **HORIZONTAL ISSUES**

40. The OFT considered the impact of any horizontal overlaps arising from the merger in the markets for the transmission and distribution of electricity and for electrical installation and engineering consultancy.

### **Transmission and Distribution of Electricity**

41. As noted above, NIE owns the electricity transmission and distribution networks in Northern Ireland. NIE also operates the distribution network, but not the transmission network (which is instead operated by SONI Limited, owned by EirGrid). Similarly, ESB - through its subsidiary ESB Networks - owns the electricity transmission and distribution networks in the Republic of Ireland. While ESB also operates the distribution network, the operation of the transmission network is entrusted to the licensed TSO in the Republic of Ireland, EirGrid.<sup>18</sup>

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<sup>18</sup> NIE and ESB also own and maintain the transmission circuits interconnecting Northern Ireland and the Republic of Ireland as far as their respective borders go. System operation of those circuits is the joint responsibility of SONI and EirGrid.

42. In respect of **actual competition** concerns, in line with precedents set by the European Commission,<sup>19</sup> there is no horizontal overlap between the merging parties because they own neighbouring networks that are located in separate jurisdictions, separately regulated and ring-fenced and are not substitutable on the demand or supply side. Accordingly, the proposed transaction does not give rise to competition concerns in this respect.
43. Furthermore, in respect of **potential competition** concerns in Northern Ireland (that is the possibility for ESB to develop and build new distribution networks and connections), the OFT notes that the Northern Irish regulatory regime is currently not designed for standalone distribution activities.<sup>20</sup> Even assuming that there is a contestable market for transmission and distribution of electricity (which might happen in the future), the OFT has not seen evidence that ESB is better prepared than possible rivals (for example distribution network operators in Great Britain) as a potential entrant in Northern Ireland.
44. Lastly, the OFT considered whether the proposed acquisition will reduce the ability of NIAUR to benchmark NIE's performance against comparable businesses and establish appropriate price controls in the future.<sup>21</sup> However, NIAUR told us that they have in the past benchmarked NIE's performance against network operators in Great Britain, and not against ESB Networks' performance. Accordingly, the OFT takes the view that the proposed transaction does not raise competition concerns in this respect either.

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<sup>19</sup> For example, distribution networks in different regions within Hungary in Case COMP/M.3696 - E.ON/MOL (21/12/2005) and transmission networks in different regions within Germany in Case COMP/M.4922 - EMCC (22/08/2008), and also transmission networks in different countries, in particular Germany and Denmark, in Case COMP/M.4922 - EMCC (22/08/2008). See also Case COMP/M.2890 - EDF/Seeboard (regarding distribution networks in England) paragraph 18 and 19 and Case COMP/M.3440 - ENI/EDP/GDP at paragraph 34.

<sup>20</sup> Stand-alone electricity distribution activities are not licensable under the current regulatory regime in Northern Ireland. As a result, NIE's electricity distribution activities are regulated in the context of its transmission licence.

<sup>21</sup> For example, in May 2010 the British regulator, Ofgem, expressed the view that network mergers 'have a potential detrimental impact on our ability to regulate energy networks effectively and protect the interests of customers. In particular, a reduction in the number of independent companies in the energy networks sector could potentially impact on the regulator's ability to push for further efficiencies and improvements in quality of service for customers.' See the corresponding press release at:

[www.ofgem.gov.uk/Media/PressRel/Documents1/Network%20Mergers%20info%20note%20AW%20FINAL.pdf](http://www.ofgem.gov.uk/Media/PressRel/Documents1/Network%20Mergers%20info%20note%20AW%20FINAL.pdf)

## **Electrical installation and engineering consultancy**

45. As noted above, PES is active in the supply of physical electrical installation and refurbishment services to third-party utility and industrial customers throughout the UK and the Republic of Ireland. Neither ESBI Consultants nor any of the other ESB entities or business units provide any physical electrical installation services to any third parties.
46. Accordingly, there is no horizontal overlap between the parties in relation to the provision of electrical installation services.
47. In respect of engineering consultancy services, the ESB Group (in particular through ESBI Consultants) provides such services (including mechanical and electrical design and project management services) to third-party utility and private operators in the electricity sector around the world (including in the UK and the Republic of Ireland).
48. The parties note that PES typically provides design services as part of its 'turnkey' project approach with its focus being installation services, whereas ESBI Consultants offers only engineering consultancy services with no associated physical installation works.
49. Furthermore, the parties estimate that, although information on market shares is difficult to obtain, their combined market share would amount to [0-5] percent of the total engineering consultancy market in the UK and the Republic of Ireland.<sup>22</sup>
50. The OFT has received no evidence contradicting the parties' submission. Third parties did not express any concerns about the proposed transaction in respect of electrical installation and engineering consultancy services (or any sub-segments). Furthermore, the parties submitted internal evidence indicating that PES' presence in the UK is not significant and that PES faces competition from multiple players.
51. On this basis, therefore, the OFT takes the view that the proposed transaction does not raise competition concerns.

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<sup>22</sup> The parties also note that, even if electrical installation and engineering consultancy services should be considered to form one single market, there would be no SLC because ESBI Consultants and PES focus on very different segments of this overall market and are therefore not close competitors.

## **Conclusion**

52. Based on the evidence before it, the OFT does not believe the transaction raises competition concerns in either the Transmission and Distribution of Electricity or in the market for electrical installation and engineering consultancy as a result of the limited overlaps in the provision of services by the parties.

## **VERTICAL ISSUES**

### **Transmission and distribution of electricity**

53. The proposed transaction will result in a vertical overlap between:
- Viridian's electricity transmission and distribution businesses in Northern Ireland (that is, NIE), respectively, and ESB Group's electricity generation business in the SEM (including the ESB's CCGT plant in Northern Ireland located in Coolkeeragh), and
  - Viridian's electricity transmission and distribution businesses in Northern Ireland, respectively, and ESB Group's retail electricity supply business in Northern Ireland.
54. The parties noted that these vertical relationships do not give rise to competition concerns for a number of reasons, namely:
- NIE's statutory duties as the entity licensed to carry out electricity transmission activities in Northern Ireland.<sup>23</sup>
  - The existence of a detailed regulatory (ring-fencing) regime governing the operation of NIE's network businesses and their interaction with other businesses (including generation and supply).
  - The fact that NIE owns but does not operate its transmission networks.
55. Some third parties expressed concerns about these vertical relationships. In particular, SONI, the TSO in Northern Ireland pointed out that, under the terms of NIE's transmission licence, NIE is responsible for the maintenance, planning and development of the transmission network in Northern Ireland, whereas SONI's obligation is to operate the transmission system.

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<sup>23</sup> Specifically, the Electricity Order 1992 (as amended) imposes obligations on NIE as transmission and distribution network owner, in particular, to: i) develop and maintain an efficient, coordinated and economical system of electricity transmission and distribution; ii) contribute to security of supply through adequate transmission capacity and system reliability; and iii) facilitate competition in the supply and generation of electricity.

According to SONI, these arrangements are different from those in place in the Republic of Ireland (where EirGrid, the TSO, is responsible for operating the transmission network as well as for the maintenance, planning and development) and fall short of the requirements imposed by the Third Electricity Directive in respect of the ISO model.

56. According to SONI, given these arrangements and the highly concentrated structure of the electricity market in Ireland, the proposed transaction might strengthen ESB's existing position and raise barriers to market entry in generation, as a result of ESB's new and expanded role in relation to certain operational aspects on the transmission system in Northern Ireland.<sup>24</sup>
57. SONI's concerns are broadly the same as those which led the European Commission to adopt the Third Directive, namely that the lack of effective separation between network businesses and competitive activities (that is, generation and retail supply) might lead vertically-integrated undertakings to discriminate against competitors and not to invest adequately in the networks.
58. Given these concerns, the OFT examined ESB's ability to engage in such foreclosure strategy post-merger, bearing in mind the existing regulatory arrangements. It also examined whether ESB has the incentive to foreclose rivals (including new entrants) and the effects (if any) resulting from such conduct.

#### Ability to foreclose

59. In respect of ability, the OFT note that the existing licence conditions appear adequate to prevent ESB from foreclosing rivals. In particular, in its consultation document of December 2009<sup>25</sup> DETI summarised the licensing arrangements for electricity transmission as follows:

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<sup>24</sup> Of note that SONI is not opposed in principle to the proposed transaction, provided the negative impacts on competition are mitigated by an accompanying requirement for effective (that is ownership) unbundling of transmission.

<sup>25</sup> See page 9 of the DETI's 'Consultation on Implementation of the Unbundling Provisions of The 2009 Electricity Directive (2009/72/EC)'

- There are existing conditions of both NIE and SONI's transmission licences relating to:
  - preparation of separate accounts for their transmission businesses from their other businesses
  - restrictions on use of certain information
  - independence of their licensed businesses
  - transmission interface arrangements
  - prohibited activities
  - ring-fencing.
- The relationship between NIE and SONI is governed by transmission interface arrangements including the Transmission Infrastructure Agreement ('TIA') which address the efficient discharge of their respective obligations (including in relation to the single electricity market), technical and operational issues, and other matters.

60. Specifically, the TIA provides for the following steps:

- the agreement of an annual planning programme
- the production of an annual transmission network report
- the production of a transmission development programme, and
- the production of a transmission investment plan.

61. In addition, it is important to note that, where agreement cannot be reached on a particular step, SONI has the power to refer the dispute to the regulator for determination. The parties noted that there have been no such disputes since the introduction of these arrangements, and this has been confirmed by the regulator and third parties.

62. The parties also noted that, in order to ensure the implementation of the steps described above in practice, NIE and SONI have established a 'Planning Panel' as well as a 'Wind Connections Panel' (to specifically discuss and review the implications of wind connections on planning). Both panels meet monthly. The output of these meetings is fed into a 'TIA Steering Committee' which also has monthly meetings and performs an overview role.

63. The parties also noted that licence conditions provide for third-party access rights under fair and equitable conditions. In particular, they submitted that:

- SONI is required to offer terms for connection to and use of the transmission system on a non-discriminatory basis and secure NIAUR's approval for the basis of charges, and
- NIE is required to offer terms for connection to and use of the distribution system on a non-discriminatory basis and secure NIAUR's approval for the basis of charges.

64. Moreover, the parties submitted that there are detailed ring-fencing arrangements in place in relation to NIE's transmission and distribution businesses. Pursuant to these arrangements, NIE must comply with restrictions on the use of sensitive information and be managerially and operationally independent from other businesses within the group, in particular those with generation and supply interests. In addition, according to the parties, NIE must submit for approval by NIAUR, keep up to date and report to NIAUR on a compliance plan that sets out the practices, procedures, systems and rules of conduct which NIE has adopted to ensure compliance with this requirement of independence. Lastly, they submitted that NIE will continue to operate as a standalone entity in accordance with these ring-fencing arrangements post-transaction.

65. The OFT note NIAUR's intention to soon propose changes to NIE's existing licence conditions, in advance of and separately from the implementation of the Third Directive. Notwithstanding the fact that these proposed changes are not specifically directed to address ESB's ability to foreclose rivals post-merger and also our view that the existing licence conditions are overall adequate to prevent such behaviour, we have taken the cautious approach of inferring from NIAUR's intention that ESB might have some ability (albeit small) to foreclose. Therefore, on a cautious basis, the OFT also consider incentives and effects in turn below.

#### Incentives to foreclose

66. In respect of incentives, the OFT note that the proposed transaction does not change the market structure significantly, because NIE was already part of a vertically-integrated utility and this will not change after ESB acquires it. It is difficult, therefore, to see how ESB's incentives to foreclose rivals are affected by the proposed transaction, given the existing regulatory framework.



67. More importantly, in respect of effects, we note that that any harm resulting from any potential foreclosure strategy by ESB will be of limited duration, namely until the third Electricity Directive is implemented in March 2012 (or in March 2013, if an extension is granted). In particular, even if the default option of ownership unbundling is not implemented, the other arrangements will contain effective unbundling provisions and will be certified by the Northern Irish regulator (NIAUR) as well as by the European Commission. Considering the lead times typically involved in building new connections (18 months or more), the OFT is of the view that the duration of any potential foreclosure strategy implemented by ESB is likely to be very limited.
68. Furthermore, the effects of any foreclosure strategy that ESB might implement could also be limited by the NIAUR's proposed changes to NIE's existing licence conditions.
69. Lastly, the OFT consulted several wind farm developers<sup>26</sup> active in Ireland (as well as other conventional generators competing with ESB and Viridian) and none of them raised issues related to foreclosure, which might indicate ESB's limited ability to foreclose as well as the absence of any significant effects from such strategy.

## Conclusion

70. Accordingly, taking into consideration the evidence described above, together with the lack of complaints from recent or likely entrants (particularly, wind farm developers), the OFT concludes that the proposed transaction does not raise concerns in respect of ESB foreclosing competitors on the market for electricity generation or for retail supply of electricity. On this basis, the transaction does not give rise to a substantial lessening of competition.<sup>27</sup>

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<sup>26</sup> There is a significant push by the authorities in both the Republic of Ireland and Northern Ireland to invest in renewable sources, also given the favourable climatic conditions. Hence, in the text above we have focused on what it was put to us as the most likely entrants, that is, wind farm developers, without limiting the analysis to such type of generators.

<sup>27</sup> The parties note that this conclusion is consistent with the European Commission's approach in Case COMP/M.5224 - EDF / British Energy (22/12/2008), where the Commission found that the concentration did not raise serious doubts in relation to the vertical relations between British Energy's activities on the market for generation and wholesale of electricity and for retail supply of electricity and EDF, as the owner and operator of three distribution networks in Britain, in particular given that EDF's distribution network activities were regulated under licence conditions monitored by OFGEM.

## **Electrical installation and engineering consultancy services**

71. The parties note that the ESB Group - namely, through ESB Networks, ESB Wind Development and possibly ESB Energy International also - purchases electrical installation services from PES. Moreover, they note that ESB Networks could (at least in theory) purchase engineering consultancy services from PES, although the ESB Group is not a significant purchaser of such services from third parties, given its own in-house capabilities. In turn, ESBI has provided engineering consultancy services to NIE. Accordingly, the parties point out that there are some vertical relationships between these activities.
72. In general, the OFT is less worried substantively about partial foreclosure as a theory of harm than total foreclosure. Having considered both partial input foreclosure and customer foreclosure, the OFT does not believe that these vertical relationships between the ESB Group and PES and NIE give rise to competition concerns in respect of either electrical installation or engineering consultancy services.
73. In particular, in respect of input foreclosure, the OFT note that neither PES (for electrical installation services) nor ESBI (for engineering consultancy services) have a significant overall position on their respective relevant markets in the UK and the Republic of Ireland. In addition, there are other established providers of these types of services, for example Enterprise Power Systems (active in both the UK and the Republic of Ireland), Balfour Beatty Utility Solutions and AMEC (both operating on an international basis), Babcock Networks and Freedom Network Services (both operating in the UK), as well as several smaller and independent competitors (including Norpower, Powermann, CIET, Transmission Links Ireland, Kirby Power, O'Hara Engineering, Laing O'Rourke, Gaeltec Utilities and Suir Engineering). Moreover, the parties note that in most cases these services are procured through a competitive tender under EU public procurement rules, which ensures visibility and effective competition.
74. In respect of customer foreclosure, the parties note that neither the ESB Group (for electrical installation services) nor NIE (for engineering consultancy services) are significant purchasers of these services in the UK and the Republic of Ireland, and that there are a range of other potential purchasers. In addition, the parties note that PES received [five-10] per

cent of the total amount spent by the ESB Group on electrical installation services, and that ESBI [ ] business from NIE in 2009.

75. On this basis, the OFT take the view that no competition concerns arise in respect of vertical relationships related to electrical installation and engineering consultancy services.

## **NON-UNILATERAL EFFECTS**

### **CO-ORDINATED EFFECTS**

76. As noted above, the impact of the proposed transaction on the structure of any relevant market is negligible. Accordingly, there is no realistic prospect that the proposed transaction will increase the likelihood of tacit (or explicit) collusion aimed at raising prices, reducing quality or innovation, or curtailing output. On this basis, the proposed transaction does not give rise to competition concerns in terms of co-ordinated effects.
77. Given the finding that the transaction does not give rise to competition concerns, it has not been necessary to consider barriers to entry and buyer power.

## **THIRD PARTY COMMENTS**

78. A few third parties expressed some concerns about ESB's current (allegedly dominant) position in the generation and retail supply of electricity in the Single Electricity Market (SEM) in Ireland. Although generation and retail supply of electricity are not affected by the proposed transaction, these submissions were taken into account in the analysis of vertical concerns.
79. In particular, one third party - SONI, the TSO in Northern Ireland - suggested that ESB - by acquiring the networks assets in Northern Ireland and the corresponding responsibilities for maintenance, planning and development - might have the ability and incentives to foreclose new entrants or manipulate the functioning of the SEM, for example by delaying investment in new transmission lines (or not investing altogether). These concerns have been discussed above.

80. The majority of third parties consulted by the OFT, however, were not concerned about this merger since in their view the proposed acquisition did not give rise to a material change of circumstances.
81. The Northern Irish regulator, NIAUR, while it intends to propose changes to certain licence conditions for transmission asset owners, was also of the view that the merger would not lead to a substantial lessening of competition in any affected market.

## **ASSESSMENT**

82. ESB and Viridian are both vertically-integrated businesses with operations at all levels of the electricity sector including generation, transmission, distribution, and the retail supply of electricity, mainly active in the Republic of Ireland and Northern Ireland, respectively.
83. The core of the proposed transaction is that ESB - through its wholly-owned subsidiary ESBNI Limited - will acquire the entire share capital of NIE and subsidiaries, that is, the transmission and distribution network business of Viridian.
84. As part of the proposed transaction, ESBNI will also acquire:
- NIE Powerteam
  - Powerteam Electrical Services (UK) Limited, including its wholly owned subsidiary Powerteam Electrical Services Limited (together, 'PES'), and
  - Capital Pensions Management Limited.
85. In respect of the transmission and distribution of electricity, there is no horizontal overlap between the parties because they are active in different (although neighbouring) geographic markets (Northern Ireland and the Republic of Ireland, respectively) in each of the relevant product markets.
86. The OFT considered whether the proposed transaction might affect potential competition in Northern Ireland or reduce the Northern Irish Regulator's ability to benchmark NIE's performance against comparable businesses and establish appropriate price controls in the future. However, the OFT found no evidence that the proposed transaction would raise any competition concerns in this respect.

87. With regard to electrical installation services, the OFT found no horizontal overlap between the parties in relation to the provision of such services. And, with regard to engineering consultancy services, the parties have a different focus (that is, PES typically provides design services as part of its 'turnkey' project approach with its focus being installation services, whereas ESBI Consultants offers engineering consultancy services only with no associated physical installation works). Furthermore, their combined share of the market for engineering consultancy in the UK and the Republic of Ireland is negligible. Accordingly, the OFT takes the view that the proposed transaction does not raise competition concerns in respect of engineering consultancy services.
88. The OFT also considered vertical relationships between the parties. Having considered both input foreclosure and customer foreclosure, the OFT believes that the vertical relationships between the ESB Group on the one hand and PES and NIE on the other hand do not give rise to competition concerns in respect of either electrical installation or engineering consultancy services.
89. Finally, the OFT examined in detail whether post-merger ESB might foreclose rivals in the generation or retail supply markets. On the information available, it appears that ESB may have limited scope to implement a foreclosure strategy. However, after taking ESB's incentives and the possible effects of such foreclosure strategy into account, the OFT is of the view that no competition concerns arise in this respect.
90. Consequently, the OFT does not believe that is or may be the case that the merger has resulted or may be expected to result in a substantial lessening of competition within a market or markets in the United Kingdom.

## **DECISION**

91. This merger will therefore **not be referred** to the Competition Commission under section 33(1) of the Act.

## ENDNOTES

1. With reference to paragraph 3, the parties clarified that Viridian is a privately-owned, vertically-integrated energy group active in the energy sector in the Republic of Ireland and Northern Ireland.
2. With reference to paragraph 13, the parties clarified that the liberalisation process has formally completed in both jurisdictions.
3. With reference to paragraphs 20-22, DETI clarified that the views expressed in these paragraphs refer to their Consultation on the implementation of the unbundling provisions of the 2009 electricity directive (2009/72/EC), December 2009.
4. With reference to paragraph 55, SONI clarified that EirGrid does not have total responsibility for the 'maintenance, planning and development' of the transmission system in the Republic of Ireland, as ESB retains a substantial role in the execution of development activity.
5. With reference to paragraphs 65, 68, 81, the NIAUR has advised that in accordance with the Electricity (Single Wholesale Market) (Northern Ireland) Order 2007, the Single Electricity Market (SEM) Committee has deemed the exercise of relevant regulatory functions in connection with the transaction to be a SEM matter. Consequently, it will be the SEM Committee that will consult on any proposed changes to NIE's and ESB's licence conditions.
6. With reference to paragraph 81, NIAUR clarified that their view of the merger was that it was unlikely to lead to a substantial lessening of competition in any affected market, and this was especially so should the proposed changes to the licence conditions be made. This clarification does not impact on the OFT's conclusions in this case.